PAINTED PONY ENERGY LTD.

2019 Annual Report

"Character is not made in a crisis, it is only exhibited"
- Robert Freeman

Message to Shareholders,

To say that these are challenging times in the Canadian energy industry would be a gross understatement. We seem to face opposition from many sides, including, at times, our federal government. This is something I find profoundly disappointing. Despite the challenges presented to Painted Pony during 2019, I remain optimistic for the future of the natural gas industry in Canada specifically, and the world more broadly. Natural gas remains one of the cleanest, most reliable and most affordable forms of energy on the planet. As countries around the globe continue to modernize and their need for energy continues to increase, I believe the demand for clean-burning natural gas will only continue to grow. While the long-term future for natural gas is positive, short-term challenges for the ongoing development of natural gas resources in Canada remain. Challenges such as low pricing caused by an abundance of natural gas supply and an LNG export industry which was delayed for almost five years, have negatively impacted the natural gas industry in Canada. There are however, some bright spots on the horizon. I expect LNG Canada to begin exporting Canadian LNG to countries around the world in late 2023 and I believe that will have a positive impact on the Canadian natural gas industry.

The past three years have been challenging for natural gas producers. At Painted Pony specifically, it has meant constrained capital spending, with net capital budgets being limited to our forecasted adjusted funds flow from operations. We felt that any cash above our forecast net capital expenditures should be directed to debt reduction so that we could maintain or enhance our balance sheet. Debt repayment in 2019 was due to a combination of higher than budgeted adjusted funds flow from operations during 2019 and the proceeds of an asset sale during the fourth quarter. I am pleased to report that at year-end 2019 Painted Pony reduced total bank debt by more than $43 million, a reduction of total bank debt of more than 26% compared to year-end 2018.

Asset Sale

After several months of negotiation, we were pleased to release the details of an asset sale. We sold a 75% working interest on 11,280 gross acres (8,460 net acres sold) on the liquids-rich South Townsend block to Tourmaline Oil Corp. ("**Tourmaline**") for $45 million, or approximately $5,300/acre. This land did not contain any proved developed producing ("**PDP**") reserves or production volumes and we did not have any capital allocated to this area in the near-term. We look forward to working with our new partner Tourmaline as we jointly develop this land block. Work is already underway as Tourmaline commenced an eight-well (2.0 net to Painted Pony) drilling program in March 2020.

We continue to assess our assets for opportunities to leverage our acreage into both opportunities for joint venture partnerships and for cash sales. Despite the headwinds in the energy market, the high quality of our assets provides us with opportunities. We are busy working on initiatives to proactively leverage our asset base. We have several highly economic development projects worth pursuing, however we are currently capital starved like many other producers.

Production
Production volumes were impacted by low prices during the summer and into the fall of 2019 so we opted to shut-in some uncontracted production volumes on those days when prices were below acceptable levels. While average daily production volumes during 2019 of 294 MMcfe/d (48,979 boe/d) were lower than average daily production volumes of 347 MMcfe/d (57,879 boe/d) during 2018, almost 70% or 37 MMcfe/d (6,100 boe/d) of the annual production volume difference was due to our voluntary, pricing-related shut ins. Our productive capacity remains strong as shown by our most recent three-month daily production volumes. During December 2019, January and February 2020 daily production volumes averaged more than 315 MMcfe/d (53,000 boe/d), based on actuals and field estimates. This is up more than 17% compared to average daily production volumes during Q4 2019 of approximately of 271 MMcfe/d (45,200 boe/d).

Future prices for natural gas in western Canada started to show improvement at the end of 2019, in part due to increasing demand in North America and the slowing of natural gas targeted drilling. These factors resulted in stagnating natural gas production growth over the last nine months in the United States and shrinking Canadian natural gas production. Additionally, we expect the recent collapse in crude oil prices to result in shrinking oil production and associated gas, which we believe is likely to result in higher natural gas prices in the latter half of 2020 and into 2021.

2019 Capital Program
As I stated earlier, net cash capital spending was constrained during 2019 as we grappled with low natural gas prices. We invested capital of $42 million for the year, net of asset sale proceeds, compared to our adjusted funds flow of $76 million. Our 2019 capital investment program included drilling 13 (13.0 net) wells, the completion of 14 (14.0 net) wells and investments into associated facilities and infrastructure.

Reserves
We finished 2019 with our Total Proved ("**1P**") and our Proved Plus Probable ("**2P**") reserves effectively flat year-over-year, despite the disposition of some 1P and 2P reserves in the asset sale to Tourmaline. Our team lowered the cost of bringing on future production by reducing the amount of capital necessary in the future to realize those reserves. This was accomplished through the drilling of longer lateral wells, which we further tested and verified in 2019 and which is now our preferred development plan going forward. The impact of longer lateral well capital efficiency was notable in the 1P category where we reduced our future development costs by $171 million. We are pleased that our PDP recycle ratio was 1.3 times in 2019 as our recycle ratio is a measure of our ability to invest capital efficiently. This is noteworthy when I consider that 2019 saw the lowest natural gas prices in more than 20 years in western Canada.

Environmental, Social, Governance
The role of environmental, social and governance ("**ESG**") metrics in our business is one which we have always taken seriously. Long before this moniker was placed on these areas of our business, we viewed these issues as crucial to the long-term success of our business.

Environmental – There are several kinds of emissions categorized as Greenhouse Gases ("**GHG**"). Of primary concern is the amount of CO_2 produced by operations which we track through measuring the amount of CO_2 our operations produce per boe of production. We have instituted several initiatives and programs in recent years to proactively reduce our CO_2 intensity. These programs include substituting natural gas as a fuel during some completion operations to reduce the amount of diesel fuel consumed. Additionally, we are not flaring any natural gas during the testing of new wells. These are just two examples of our efforts to reduce the CO_2 intensity of our operations. We are pleased to report that for the years 2014 through to 2018 we have reduced our tonnes of CO_2 per boe by 62%.

Reducing methane emissions, another GHG, is also a focus for us. We have become an industry leader in the use of the 'EPOD Solar Hybrid Power Generation and Instrument Air Systems' on well sites which eliminates vented emissions from individual well sites. We have recently implemented a 'zero venting protocol' on all new well sites which we believe long-term will further reduce our methane emissions, further lowering our total GHG emissions.

Reducing fresh water use whenever possible has always been a priority for us. We participate in a local 'Water Co-operative' with other producers in our operating areas. Through this program we share completion water to further reduce freshwater use. Not only does this reduce the amount of freshwater extracted from natural sources, this also helps us save on water trucking and disposal costs. This is good for the environment and our bottom line.

In addition to the sharing of completion water with other producers, we have been steadily increasing the amount of recycled water in our operations. We have not sourced any fresh water from streams or rivers in the past five years, instead sourcing any fresh water from dug outs. I am proud to say that in 2019 we used approximately 90% recycled water and in 2020 we anticipate using 100% recycled water for all completion operations. This is a significant milestone in our water conservation efforts, one of which we are proud, and which further reduces water costs.

Social – We continue to have constructive relationships with neighbouring Indigenous communities. We speak and meet with these communities frequently as I believe our open lines of communication and mutual respect are a large part of why these relationships are positive. They are our 'neighbours' and we strive to have a very good relationship with them.

In addition to our positive Indigenous relationships, we actively engage with many charitable and community initiatives. We continue to help groups who are supportive of youth mental health, various local social support programs, homelessness, and other worthy causes to support families and individuals.

Governance – We believe that good governance is the foundation of any great company. As such we note with pride that Institutional Shareholder Services Inc. ("**ISS**"), who is the world's leading provider of corporate governance and responsible investment solutions, provided Painted Pony with an aggregate score of '1' in 2019. The scale for this rating is a 1-10 scale where 1 is the highest level of governance quality and lowest level of governance risk. Our score of '1' in 2019 was the best aggregate score attainable and the best in our peer group of companies.

Health and Safety

We stress the importance of safety in absolutely everything we do at Painted Pony. In 2019 we saw no material incidents and we recorded zero lost time incidents.

2020 and Beyond

We have forecasted a modest first half 2020 capital budget of $25 to $30 million considering current commodity prices. We feel a cautious approach is warranted and we will review the near-term forward price curve to determine appropriate second half 2020 spending levels. As well, we will continue to pursue long-term contracts for the delivery of natural gas to large end-users while diversifying our sales into different markets.

I remain optimistic for the future of natural gas both in Canada and around the world. While it may seem difficult to see a path through given the headwinds of the COVID-19 pandemic and the resulting impact it is having on the capital markets, ultimately Canada and the world will need our energy to recover and to prosper in the future.

During this time of the COVID-19 crisis, I would especially like to thank our staff who continue to work as an essential service through this crisis, the Board of Directors for their commitment to Painted Pony and the hard work we are doing everyday. I would also like to thank our Indigenous neighbours, the people of BC, service providers and shareholders for their continued support of Painted Pony.

My wish is for all of us to get through these difficult times by working smartly and safely together.

'signed'

Patrick R. Ward

President & Chief Executive Office

April 6, 2020

DEFINITIONS AND ADVISORIES

Currency: All amounts referred to in this letter are stated in Canadian dollars unless otherwise specified.

Boe Conversions: Barrel of oil equivalent ("**boe**") amounts have been calculated by using the conversion ratio of six thousand cubic feet (6 Mcf) of natural gas to one barrel of oil (1 bbl). Boe amounts may be misleading, particularly if used in isolation. A boe conversion ratio of 6 Mcf to 1 bbl is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. Given that the value ratio based on the current price of oil as compared to natural gas is significantly different from the energy equivalent of 6:1, utilizing a conversion on a 6:1 basis may be misleading as an indication of value.

Mcfe Conversions: Thousands of cubic feet of gas equivalent ("**Mcfe**") have been calculated by using the conversion ratio of one barrel of oil (1 bbl) to six thousand cubic feet (6 Mcf) of natural gas. Mcfe amounts may be misleading, particularly if used in isolation. A conversion ratio of 1 bbl to 6 Mcf is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

Independent Reserves Evaluation

GLJ Petroleum Consultants ("**GLJ**"), independent qualified reserves evaluators of Calgary, Alberta, prepared a reserves estimation and economic evaluation of the Corporation's oil and natural gas properties effective December 31, 2019, which is contained in a report dated March 11, 2020 (the "**2019 Reserves Report**"). GLJ prepared reserves estimations and economic evaluations of the Corporation's reserves effective December 31, 2019. Reserves estimates stated herein as at December 31 of a year are extracted from the relevant evaluation.

The 2019 Reserves Report and the prior reserves evaluation were prepared in accordance with the standards contained in the Canadian Oil & Gas Evaluation Handbook ("**COGE Handbook**") and National Instrument 51-101 – Standards of Disclosure for Oil and Gas Activities ("**NI 51-101**"), which were in effect at the time of the evaluation.

The reserves data provided in this letter contains only excerpts of the disclosure required under NI 51-101. All of the required information is contained in the Corporation's Statement of Reserves Data and Other Oil and Gas Information incorporated by reference into the Corporation’s Annual Information Form for the year ended December 31, 2019.

Company Gross Reserves: In this letter, unless otherwise stated, references to "reserves" are to the Corporation's gross reserves, defined as the Corporation's working interest (operated or non- operated) share before deduction of royalties and without including any royalty interests of the Corporation.

Reserves Categories: Reserves are estimated remaining quantities of oil and natural gas and related substances anticipated to be recoverable from known accumulations, as of a given date, based on (i) analysis of drilling, geological, geophysical and engineering data; (ii) the use of established technology; and (iii) specified economic conditions, which are generally accepted as being reasonable, and shall be disclosed. Reserves are classified according to the degree of certainty associated with the estimates.

"Proved reserves" are those reserves that can be estimated with a high degree of certainty to be recoverable. It is likely that the actual remaining quantities recovered will exceed the estimated proved reserves. Proved reserves should have at least a 90 percent probability that the quantities actually recovered will equal or exceed the estimated proved reserves.

"Probable reserves" reserves, are those additional reserves that are less certain to be recovered than proved reserves. It is equally likely that the actual remaining quantities recovered will be greater or less than the sum of the estimated proved plus probable reserves. Probable reserves should have at least a 50 percent probability that the quantities actually recovered will equal or exceed the sum of the estimated proved plus probable reserves.

Forward-Looking Information: This letter contains certain forward-looking information within the meaning of Canadian securities laws. Forward-looking information relates to future events or future performance and is based upon the Corporation's current internal expectations, estimates, projections, assumptions and beliefs. All information other than historical fact is forward-looking information. Words such as "plan", "expect", "intend", "believe", "anticipate", "estimate", "may", "will", "potential", "proposed" and other similar words that indicate events or conditions may occur are intended to identify forward-looking information. In particular, this letter contains forward looking information relating to the date of anticipated Canadian LNG exports, capital expenditures, including drilling eight (2.0 net) wells as part of the Corporation’s joint venture with Tourmaline on the South Townsend block; future opportunities for joint venture partnership and for cash sales, anticipated higher nature gas prices in the latter half of 2020 and into 2021, future initiatives to reduce CO2 intensity, future reduction of methane emissions, future reductions of fresh water usage and increased recycled water usage, future cost savings resulting from water trucking and disposal, constructive relationships with neighboring Indigenous communities and future support of charitable and community initiatives, forecasted 2020 capital spending, continued pursuit of long-term projects for the delivery of natural gas to large end-users and diversification of sales into different markets.

Forward-looking information is based on certain expectations and assumptions including but not limited to future commodity prices, currency exchange rates interest rates, royalty rates and tax rates; the state of the economy and the exploration and production business; the economic and political environment in which the Corporation operates; the regulatory framework; anticipated timing and results of capital expenditures; the sufficiency of budgeted capital expenditures to carry out planned operations; operating, transportation, marketing and general and administrative costs; drilling success, production rates, future capital expenditures and the availability of labor and services.

Undue reliance should not be placed on forward-looking information, as there can be no assurance that the plans, intentions or expectations on which they are based will occur. Although the Corporation's management believes that the expectations in the forward-looking statements are reasonable, there can be no assurance that such expectations will prove to be correct. As a consequence, actual results may differ materially from those anticipated.

Forward-looking information necessarily involves both known and unknown risks associated with oil and gas exploration, production, transportation and marketing. There are risks associated with the uncertainty of geological and technical data, operational risks, risks associated with drilling and completions, environmental risks, risks of the change in government regulation of the oil and gas industry, risks associated with competition from others for scarce resources and risks associated with general economic conditions affecting the Corporation's ability to access sufficient capital. Additional information on these and other risk factors that could affect operational or financial results are included in the Corporation's most recent Annual Information Form and in other reports filed with Canadian securities regulatory authorities.

Forward-looking information is based on estimates and opinions of management at the time the information is presented. The Corporation is not under any duty to update the forward-looking information after the date of this letter to revise such information to actual results or to changes in the Corporation's plans or expectations, except as required by applicable securities laws.

Non-GAAP Measures: This letter uses the term "adjusted funds flow from operations", which does not have a standardized meaning prescribed by IFRS and therefore may not be comparable with the calculation of similar measure presented by other issuers. Management uses "adjusted funds flow from operations" to analyze operating performance and considers "adjusted funds flow from operations" to be a key measure as it demonstrates the Corporation's ability to generate the cash necessary to fund future capital investment and to repay debt. "Adjusted funds flow from operations" denotes cash flow from operating activities before the effects of changes in non-cash working capital and decommissioning expenditures. This measure should not be construed as an alternative to, or more meaningful than, cash flows from (used in) operating activities as determined in accordance with IFRS as a measure of the Corporation's performance. The Corporation's method of calculating this non-GAAP measures may differ from other companies, and accordingly, may not be comparable to a similar measure used by other entities. Please see the "Non-GAAP Measures" section of the Corporation's management's discussion and analysis of the financial results of the Corporation for the year ended December 31, 2019 for further information regarding this "Non-GAAP Measure", including a reconciliation to the most directly comparable measure calculated in accordance with IFRS.

ABOUT PAINTED PONY

Painted Pony is a publicly-traded natural gas company based in Western Canada. The Corporation is primarily focused on the development of natural gas and natural gas liquids from the Montney formation in northeast British Columbia. Painted Pony's common shares trade on the TSX under the symbol "PONY".

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PAINTED PONY ENERGY LTD.
FINANCIAL AND OPERATING HIGHLIGHTS

	Years ended December 31,		
($ millions, except per share and shares outstanding)	**2019**	2018	Change
Financial			
Natural gas and natural gas liquids revenue[(1)]	**302.8**	404.4	(25)%
Cash flows from operating activities	**88.6**	169.0	(48)%
Per share - basic[(3)(8)]	**0.55**	1.05	(48)%
Per share - diluted[(4)(8)]	**0.52**	0.99	(48)%
Adjusted funds flow from operations[(2)]	**76.4**	174.6	(56)%
Per share - basic[(3)]	**0.47**	1.08	(56)%
Per share - diluted[(4)]	**0.45**	1.03	(56)%
Net income (loss) and comprehensive income (loss) - basic and diluted	**(232.9)**	7.1	— %
Per share - basic and diluted[(3)(4)]	**(1.45)**	0.04	— %
Cash capital expenditures (net)	**42.3**	154.4	(73)%
Working capital (deficiency)[(5)]	**(31.9)**	32.9	— %
Bank debt	**119.9**	163.1	(26)%
Senior notes	**144.8**	143.1	1 %
Convertible debentures - liability	**47.5**	46.1	3 %
Net debt[(6)]	**320.2**	348.5	(8)%
Total assets	**1,803.4**	2,055.4	(12)%
Shares outstanding *(millions)*	**161.0**	161.0	—
Basic weighted-average shares *(millions)*	**161.0**	161.0	—
Fully diluted weighted-average shares *(millions)*	**169.9**	169.9	—
Operational			
Daily production volumes			
Natural gas *(MMcf/d)*	**268.7**	316.5	(15)%
Natural gas liquids *(bbls/d)*	**4,198**	5,128	(18)%
Total *(MMcfe/d)*	**293.9**	347.3	(15)%
Total *(boe/d)*	**48,979**	57,879	(15)%
Realized commodity prices before financial risk management contracts			
Natural gas *($/Mcf)*	**2.40**	2.54	(6)%
Natural gas liquids *($/bbl)*	**44.05**	59.43	(26)%
Total *($/Mcfe)*	**2.82**	3.19	(12)%
Operating netbacks *($/Mcfe)*[(7)]	**1.66**	2.16	(23)%
Corporate netbacks *($/Mcfe)*[(7)]	**1.12**	1.71	(35)%

1. *Before royalties.*
2. *Adjusted funds flow from operations and adjusted funds flow from operations per share (basic and diluted) are non-GAAP measures used to represent cash flow from operating activities before the effects of changes in non-cash working capital and decommissioning expenditures. Adjusted funds flow from operations per share is calculated by dividing adjusted funds flow from operations by the weighted average number of basic or diluted shares outstanding in the period. See "Non-GAAP Measures".*
3. *Basic per share information is calculated on the basis of the weighted average number of shares outstanding in the period.*
4. *Diluted per share information reflects the potential dilutive effect of stock options and convertible debentures.*
5. *Working capital (deficiency) is a non-GAAP measure calculated as current assets less current liabilities. See "Non-GAAP Measures".*
6. *Net debt is a non-GAAP measure calculated as bank debt, senior notes, liability portion of convertible debentures, and working capital deficiency, adjusted for the net current portion of fair value of risk management contracts and current portion of finance lease obligation. See "Non-GAAP Measures".*
7. *Operating netbacks and corporate netbacks are non-GAAP measures. Operating netbacks are calculated on a per unit basis as natural gas and natural gas liquids revenues, adjusted for realized gains or losses on risk management contracts, less royalties, operating expenses and transportation expenses. Corporate netbacks are calculated as operating netback less finance lease expense per unit. See "Non-GAAP Measures" and "Operating and Corporate Netbacks".*
8. *Cash flows from operating activities per share, basic and diluted, are non-GAAP measures calculated by dividing cash flows from operating activities by the weighted average of basic or diluted shares outstanding in the period. See "Non-GAAP Measures".*

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following Management's Discussion and Analysis ("MD&A") of the financial results of Painted Pony Energy Ltd. ("Painted Pony" or the "Corporation") should be read in conjunction with the audited financial statements and related notes thereto for the years ended December 31, 2019 and December 31, 2018 (the "Annual Financial Statements"). Certain prior year amounts have been reclassified for consistency with the current year presentation. These reclassifications had no effect on the reported results of operations. This commentary is dated March 11, 2020.

The Annual Financial Statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"). The financial data presented is in accordance with IFRS in Canadian dollars, except where indicated otherwise. These documents and additional information about Painted Pony, including its Annual Information Form for the year ended December 31, 2018 ("AIF"), are available under the Corporation's profile on SEDAR at www.sedar.com and on the Corporation's website at www.paintedpony.ca.

BUSINESS OF THE CORPORATION

Painted Pony is a publicly traded corporation focused on the production of natural gas and natural gas liquids ("NGLs") from the Montney formation in northeast British Columbia. The common shares of Painted Pony ("Common Shares") trade on the Toronto Stock Exchange ("TSX") under the symbol "PONY". The Corporation's head office is located at Suite 1200, 520 - 3 Avenue SW, Calgary, Alberta.

NON-GAAP MEASURES

This MD&A contains the terms "adjusted funds flow from operations", "adjusted funds flow from operations per share", "cash flows from (used in) operating activities per share", "working capital (deficiency)", "net debt", "operating netbacks" and "corporate netbacks", which do not have standardized meanings prescribed by IFRS and therefore may not be comparable with the calculation of similar measures presented by other issuers.

Adjusted Funds Flow from Operations, Adjusted Funds Flow from Operations Per Share and Cash Flows from (Used in) Operating Activities Per Share

Management uses "adjusted funds flow from operations" to analyze operating performance and considers adjusted funds flow from operations to be a key measure as it demonstrates the Corporation's ability to generate the cash necessary to fund future capital investment and to repay debt. Adjusted funds flow from operations denotes cash flow from operating activities before the effects of changes in non-cash working capital and decommissioning expenditures. "Adjusted funds flow from operations per share" and "cash flows from (used in) operating activities per share" are calculated using the basic and diluted weighted average number of shares for the period. These terms should not be considered alternatives to, or more meaningful than, cash flows from (used in) operating activities as determined in accordance with IFRS as an indicator of the Corporation's performance. The Corporation reconciles each of adjusted funds flow from operations, adjusted funds flow from operations per share and cash flows from (used in) operating activities per share to cash flows from (used in) operating activities, which is the most directly comparable measure calculated in accordance with IFRS, as follows:

	Three months ended December 31,		**Years ended December 31,**	
($000s, except per share)	**2019**	**2018**	**2019**	**2018**
Cash flows from operating activities	**9,024**	48,475	**88,554**	169,035
Changes in non-cash working capital	**8,856**	10,228	**(12,149)**	5,604
Adjusted funds flow from operations	**17,880**	58,703	**76,405**	174,639
Cash flows from operating activities per share *($/share)*:				
Basic	**0.06**	0.30	**0.55**	1.05
Diluted	**0.05**	0.29	**0.52**	0.99
Adjusted funds flow from operations per share *($/share):*				
Basic	**0.11**	0.36	**0.47**	1.08
Diluted	**0.11**	0.35	**0.45**	1.03

Working Capital (Deficiency) and Net Debt

Management uses "working capital (deficiency)" and "net debt" as useful supplemental measures of the liquidity of the Corporation. Working capital (deficiency) is calculated as current assets less current liabilities. Net debt is calculated as bank debt, senior notes, the liability portion of convertible debentures and working capital (deficiency), adjusted for the net current portion of the fair value of risk management contracts and current portion of the finance lease obligation. These terms should not be considered alternatives to, or more meaningful than, current and long-term debt as determined in accordance with IFRS. The following table summarizes the Corporation's calculations of working capital (deficiency) and net debt:

($000s)	**December 31, 2019**	**December 31, 2018**
Current assets	**41,996**	92,976
Current liabilities	**(73,905)**	(60,086)
Working capital (deficiency)	**(31,909)**	32,890
Current portion of fair value of risk management contracts (net)	**15,626**	(34,685)
Current portion of finance lease obligation	**8,203**	5,680
Bank debt	**(119,901)**	(163,140)
Senior notes	**(144,754)**	(143,105)
Convertible debentures - liability	**(47,466)**	(46,113)
Net debt	**(320,201)**	(348,473)

Operating Netbacks and Corporate Netbacks
Management uses "operating netbacks" as a supplemental measure of the Corporation's profitability relative to commodity prices. Operating netbacks are calculated on a per unit basis as natural gas and natural gas liquids revenue, adjusted for realized gains or losses on risk management contracts, less royalties, operating expenses and transportation expenses. "Corporate netbacks" is used as a supplemental measure of the Corporation's profitability after taking into consideration the costs associated with finance leases. These terms should not be considered an alternative to, or more meaningful than net income (loss) and comprehensive income (loss) as determined in accordance with IFRS. Please refer to "Operating Netbacks" and "Corporate Netbacks" for a reconciliation of these measures.

RESULTS OF OPERATIONS - OVERVIEW

Subsequent to December 31, 2019, the Corporation announced facility cost structure improvements. The take-or-pay commitment at the Townsend Facility was reduced by 15 MMcf/d effective October 1, 2019, and will be reduced by an additional 16 MMcf/d on August 1, 2020 with an additional 9 MMcf/d reduction to the take-or-pay commitment on August 1, 2021, for a total reduction of take-or-pay obligation of 15% or 40 MMcf/d. In addition, Painted Pony will realize a reduced capital lease fee at the Townsend Facility, which is expected to lower the per unit cost by approximately 10%. Also, the annual fixed-cost liquids transportation expense has been reduced by approximately 40% from the Townsend Facility to the North Pine Fractionator.

Total shut-ins of 9,300 boe/d and 6,100 boe/d, respectively, experienced in the three months and year ended December 31, 2019 resulted from pricing related shut-ins and pipeline restriction shut-ins. This has been the primary factor in reduced production volumes and adjusted funds flow from operations for the three months and year ended December 31, 2019 compared to the same periods in 2018.

Painted Pony's realized commodity prices for the three months ended December 31, 2019 benefited from an average natural gas price representing a 17% premium to the AECO daily (5A) benchmark price. The Corporation's operating netback for the three months ended December 31, 2019 was $1.75/Mcfe, a decrease of 39% from the operating netback of $2.88/Mcfe for the three months ended December 31, 2018.

Painted Pony's realized commodity prices for the year ended December 31, 2019 benefited from an average natural gas price representing a 36% premium to the AECO daily (5A) benchmark price. Painted Pony's operating netback for the year ended December 31, 2019 was $1.66/Mcfe, a decrease of 23% from the operating netback of $2.16/Mcfe for the year ended December 31, 2018. As at December 31, 2019, the Corporation has executed fixed price risk management contracts on 48 MMcf/d of natural gas and 1,000 bbl/d of natural gas liquid production for 2020. The Corporation has access to multiple sales hubs as part of its long term sales point diversification strategy, including the Dawn and Sumas markets, and as a result, receives a premium over the AECO (5A) benchmark price.

During the fourth quarter of 2019, the Corporation sold a 75% working interest in 11,280 gross acres (8,460 net acres) of land in the northeast British Columbia Montney play for cash consideration of $45.0 million. The proceeds were applied against bank debt.

The Corporation's capital program for the fourth quarter of 2019 was $12.5 million, including $5.7 million for completion costs. During the three months ended December 31, 2019 the Corporation completed 2 (2.0 net) Montney natural gas wells. For the year ended December 31, 2019, the capital program was $87.3 million prior to dispositions, including $63.4 million for drilling and completion costs. The Corporation drilled 13 (13.0 net) and completed 14 (14.0 net) Montney natural gas wells during the year ended December 31, 2019 .

The Corporation's planned cash capital program for the first half of 2020 is currently estimated to be between $25 and $30 million, which is reviewed and updated on a periodic basis.

At December 31, 2019, the Corporation had syndicated credit facilities of $375 million. In addition, the Corporation has a $22 million unsecured letter of credit facility backstopped by Export Development Canada ("EDC").

CASH FLOWS FROM OPERATING ACTIVITIES, ADJUSTED FUNDS FLOW FROM OPERATIONS AND NET INCOME (LOSS)

For the fourth quarter of 2019, cash flows from operating activities decreased to $9.0 million, compared to cash flows from operations of $48.5 million in the fourth quarter of 2018. Adjusted funds flow from operations was $17.9 million in the fourth quarter of 2019, compared to $58.7 million in the fourth quarter of 2018. The decrease in cash flows from operating activities is a result of a 25% decrease in realized commodity prices (including the impact of physical contracts) and 14% lower production volumes.

For the year ended December 31, 2019, cash flows from operating activities decreased to $88.6 million, compared to $169.0 million in the year ended December 31, 2018. Adjusted funds flow from operations was $76.4 million in the year ended December 31, 2019, a decrease from $174.6 million in the year ended December 31, 2018. The respective decreases are a result of lower production volumes and a decrease in realized commodity prices (including the impact of physical contracts).

For the fourth quarter of 2019, the Corporation had a net loss and comprehensive loss of $178.5 million impacted by an impairment of property, plant and equipment ("PP&E") of $150.0 million, an unrealized loss on risk management contracts of $20.4 million and an unrealized foreign exchange gain of $1.7 million. This compares to net income and comprehensive income of $62.5 million for the fourth quarter of 2018. The decrease in net income (loss) is a result of the impairment, decrease in realized commodity prices (including the impact of physical contracts) and lower production volumes that impacted cash flows from operating activities.

For the year ended December 31, 2019, the Corporation had a net loss and comprehensive loss of $232.9 million impacted by an impairment of PP&E of $150.0 million, an unrealized loss on risk management contracts of $83.1 million and an unrealized foreign exchange gain of $2.9 million. This compares to a net income and comprehensive income of $7.1 million for the year ended December 31, 2018. The decrease in net income (loss) is a result of the impairment, decrease in realized commodity prices (including the impact of physical contracts) and lower production volumes that impacted cash flows from operating activities.

AVERAGE DAILY PRODUCTION

	Three months ended December 31,				**Years ended December 31,**			
	2019	**% of total**	**2018**	**% of total**	**2019**	**% of total**	**2018**	**% of total**
Natural Gas *(Mcf/d)*	**248,046**	**92**	289,820	92	**268,687**	**91**	316,507	91
NGLs *(bbls/d)*	**3,832**	**8**	4,150	8	**4,198**	**9**	5,128	9
Total *(Mcfe/d)*	**271,038**	**100**	314,718	100	**293,874**	**100**	347,274	100
Total *(boe/d)*	**45,173**	**100**	52,453	100	**48,979**	**100**	57,879	100

Production volumes for the three months ended December 31, 2019 decreased by 7,280 boe/d, or 14%, compared to the three months ended December 31, 2018. Temporary shut-ins of approximately 9,300 boe/d were experienced in the fourth quarter of 2019, comprised of pricing related shut-ins and pipeline restriction shut-ins.

Production volumes for the year ended December 31, 2019 decreased by 8,900 boe/d or 15%, compared to the year ended December 31, 2018. Temporary shut-ins of approximately 6,100 boe/d were experienced in 2019 due to pricing related shut-ins and pipeline restriction shut-ins. Production from successful new drills in the Townsend, Kobes and Diaber areas partially offset these temporary shut-ins. The Corporation saw strong production performance at the end of 2019, driven by a rebound in natural gas prices. This allowed the Corporation to maintain production, as well as see continued performance from recently completed long laterals at the 74-F pad. The Corporation continues to extend the limits of the lateral sections of wells, with the last three wells averaging over 3,000 meters in lateral length. Strong production rates and improved capital efficiencies from this approach allows the Corporation to continue to optimize this well design and cost structure as more experience and success is achieved.

NATURAL GAS AND NATURAL GAS LIQUIDS REVENUE

	Three months ended December 31,		Years ended December 31,	
($000s)	**2019**	**2018**	**2019**	**2018**
Natural Gas	**65,892**	104,014	**235,247**	293,145
Natural Gas Liquids	**15,111**	21,655	**67,503**	111,227
Total	**81,003**	125,669	**302,750**	404,372

For the three months ended December 31, 2019, natural gas and natural gas liquids revenue decreased by 36% compared to the fourth quarter of 2018. The change in quarterly revenue was driven by a 25% decrease in realized prices and 14% lower production volumes when compared to the three months ended December 31, 2018.

During the year ended December 31, 2019, natural gas and natural gas liquids revenue decreased by 25% to $302.8 million compared to the year ended December 31, 2018, as a result of a 15% decrease in average production volumes, and a 12% decrease in realized prices.

Commodity Prices

		Three months ended December 31,		Years ended December 31,	
Average Benchmark Prices:		**2019**	**2018**	**2019**	**2018**
Natural Gas	NYMEX *(U.S.$/mmbtu)*	**2.50**	3.64	**2.63**	3.09
	AECO, daily (5A) *($/Mcf)*	**2.48**	1.56	**1.76**	1.50
	Sumas *(U.S.$/mmbtu)*	**4.20**	11.06	**3.80**	4.30
	Dawn *($/Mcf)*	**2.95**	5.01	**3.19**	4.05
Crude Oil	WTI *(U.S. $/bbl)*	**56.96**	58.92	**57.03**	64.79
Exchange rate *(U.S. $/ CAD$)*		**0.76**	0.76	**0.75**	0.77
Realized Commodity Prices Before Financial Risk Management Contracts:					
Natural Gas *($/Mcf)*		**2.89**	3.90	**2.40**	2.54
NGLs *($/bbl)*		**42.87**	56.72	**44.05**	59.43
Total *($/Mcfe)*		**3.25**	4.34	**2.82**	3.19

The Corporation addresses volatility in commodity prices through an active risk management strategy which uses fixed price and location differentials (including Sumas and Nymex) to effectively reduce the Corporation’s exposure to the volatile pricing experienced at the AECO daily (5A) and Station 2 sales hubs. This strategy is further supported with physical transportation capacity to other sales hubs.

During the three months and year ended December 31, 2019, the Corporation's realized natural gas price of $2.89/Mcf and $2.40/Mcf, respectively, represented 17% and 36% premiums, respectively, to the AECO daily (5A) benchmark price, due to market diversification.

Financial Risk Management

The Corporation uses financial derivatives and physical delivery sales contracts to mitigate a portion of its exposure to commodity price risk, and provide a level of stability to operating cash flows, which assists the Corporation in funding its capital development program. The use of these transactions is governed by and is subject to risk management policies established by the Board of Directors of the Corporation (the “Board”). The Corporation’s risk management policies are discussed in note 15 to the Annual Financial Statements. These instruments are not used for trading or speculative purposes. The Corporation has not designated its financial derivative contracts as effective accounting hedges, even though the Corporation considers all commodity contracts to be effective economic hedges. As a result, all such commodity contracts are recorded at fair value on the statement of financial position, with changes in the fair value being recognized as an unrealized gain or loss in the statement of operations.

Realized (Loss) Gain On Risk Management Contracts

	Three months ended December 31,		Years ended December 31,	
	2019	**2018**	**2019**	**2018**
Realized (loss) gain on risk management contracts *($000s)*	**(1,657)**	474	**17,338**	38,650
Per unit *($/Mcfe)*	**(0.07)**	0.02	**0.16**	0.30

The Corporation's method of determining the fair values of derivative financial instruments is disclosed in note 16 to the Annual Financial Statements. At December 31, 2019, the Corporation held commodity risk management contracts summarized as follows:

Financial AECO Natural Gas Contracts

Options traded	Term	Volume (GJ/d)	Weighted average price (CAD$/GJ)
AECO Fixed Price Swap	January 2020 - March 2020	20,000	2.06
AECO Fixed Price Swap	April 2020 - October 2020	48,000	1.53
AECO Fixed Price Swap	April 2021 - October 2021	8,000	1.62
AECO Fixed Price Swap	April 2022 - October 2022	8,000	1.62

Financial NYMEX Natural Gas Contracts

Options traded	Term	Volume (Mmbtu/d)	Weighted average price (US$/Mmbtu)
USD Nymex Fixed Price	April 2020 - October 2020	10,000	2.53

Financial Sumas Natural Gas Contracts

Options traded	Term	Volume (MMBtu/d)	Weighted average price (US$/MMBtu)
USD Sumas Fixed Price Swap	January 2020	20,000	3.98

Financial AECO Differential Contracts

Options traded	Term	Volume (GJ/d)	Weighted average price (AECO 7A less CAD$/GJ)
AECO-Station 2 Differential Swap	January 2020 - October 2020	40,000	(0.32)
AECO-Station 2 Differential Swap	January 2020 - August 2021	20,000	(0.29)

Financial NYMEX Basis Contracts

Options traded	Term	Volume (MMBtu/d)	Weighted average price (NYMEX less US$/MMBtu)
NYMEX-AECO Basis Swap	January 2020 - September 2021	10,000	(1.14)
NYMEX-AECO Basis Swap	January 2020 - December 2023	40,000	(1.28)
NYMEX-AECO Basis Swap	April 2020 - October 2020	10,000	(1.45)
NYMEX-AECO Basis Swap	April 2020 - December 2023	10,000	(1.18)
NYMEX-AECO Basis Swap	October 2021 - March 2023	10,000	(1.05)
NYMEX-Dawn Basis Swap	January 2020 - December 2020	20,000	(0.09)
NYMEX-Dawn Basis Swap	January 2020 - December 2021	20,000	(0.09)

Financial WTI Crude Oil Contracts			
Options traded	**Term**	**Volume (Bbl/d)**	**Weighted average price (CAD$/Bbl)**
WTI Call Option Sell *	January 2020 - December 2020	250	82.50
WTI Call Option Buy *	January 2020 - December 2020	250	70.00
WTI Fixed Price Swap	January 2020 - December 2020	750	77.14

* WTI costless collar with a floor price of $70.00 and ceiling price of $82.50.

In addition to the commodity risk management contracts discussed above, the Corporation has entered into physical delivery sales contracts to manage commodity risk.

The Corporation has the following foreign exchange risk management contracts in place as at December 31, 2019:

Financial Foreign Exchange Contracts **			
Reference Currency	**Term**	**Notional Amount (USD $000s/month)**	**Strike Rate (CAD/USD)**
USD	January 2020 - September 2020	1,000	1.335
USD	January 2020 - March 2021	1,000	1.340
USD	January 2020 - December 2021	1,000	1.360

** Foreign exchange risk management contracts are fade-in forwards with an average fade-in level of 1.26.

The Corporation periodically enters into USD cross currency interest rate swaps related to LIBOR borrowings, which result in a reduction to interest expense paid on borrowings on the credit facility. As at December 31, 2019 the following cross currency swap was outstanding:

Contract Quantity	Type of Contract	Term / Expiry	Contract Price
$130 Million	Cross currency swap	January 21, 2020	$1.318 CAD/USD

ROYALTIES

	Three months ended December 31,		Years ended December 31,	
	2019	**2018**	**2019**	**2018**
Royalty expense *($000s)*	**1,052**	1,639	**4,645**	6,345
Per unit *($/Mcfe)*	**0.04**	0.06	**0.04**	0.05
Royalties as a % of Revenue	**1.3**	1.3	**1.5**	1.6

For the three months and year ended December 31, 2019, royalty rates of 1.3% and 1.5% respectively, are comparable to royalty rates of 1.3% and 1.6% respectively, for the three months and year ended December 31, 2018. The majority of the Corporation's properties are on the west side of the British Columbia royalty line and are eligible to receive an average royalty credit of approximately $2.2 million per well. The remainder of the Corporation's properties, on the east side of the British Columbia royalty line, are eligible to receive an average royalty credit of approximately $0.8 million per well.

For the first half of 2020, the Corporation anticipates overall royalty rates to be approximately 1.5% to 2.0% of total revenue. This estimate considers the combined impact of incremental sales volumes from newly drilled wells that will qualify for royalty holidays, net of royalties paid on wells that have obtained the full benefit of provincial royalty incentives.

OPERATING EXPENSES

	Three months ended December 31,		Years ended December 31,	
	2019	**2018**	**2019**	**2018**
Operating expenses *($000s)*	**13,418**	17,521	**57,251**	72,830
Per unit *($/Mcfe)*	**0.54**	0.61	**0.53**	0.57

Operating expenses decreased by 23% and 21% respectively, for the three months and year ended December 31, 2019 compared to the same periods in 2018, due to reduced facility costs and water management initiatives. Per unit operating expenses were lower in the three months and year ended December 31, 2019 and 2018 due to reduced facility costs and water management initiatives, the impact of which was partially offset by lower produced volumes. Carbon Tax contributed approximately $0.05/Mcfe to per unit operating expenses for the three months and year ended December 31, 2019.

For the first half of 2020, the Corporation anticipates that average per unit operating expenses will be between $0.60/Mcfe and $0.65/Mcfe.

TRANSPORTATION EXPENSES

	Three months ended December 31,		Years ended December 31,	
	2019	**2018**	**2019**	**2018**
Transportation expenses *($000s)*	**21,114**	23,468	**80,731**	89,876
Per unit *($/Mcfe)*	**0.85**	0.81	**0.75**	0.71

Transportation expenses decreased 10% for the three months and year ended December 31, 2019 compared to the same periods in 2018. Per unit transportation expenses for the three months and year ended December 31, 2019 increased by 5% and 6% respectively, compared to the three months and year ended December 31, 2018, due to lower production volumes. The Corporation has realized incremental revenues, net of transportation expenses, of approximately $80 million in 2019 as a result of its market diversification strategy.

For the first half of 2020, the Corporation expects average per unit transportation expenses to be between $0.85/Mcfe and $0.90/Mcfe.

OPERATING AND CORPORATE NETBACKS

	Three months ended December 31,		Years ended December 31,	
($/Mcfe)	**2019**	**2018**	**2019**	**2018**
Realized commodity price	**3.25**	4.34	**2.82**	3.19
Realized gain (loss) on risk management contracts	**(0.07)**	0.02	**0.16**	0.30
Royalties	**(0.04)**	(0.06)	**(0.04)**	(0.05)
Operating expenses	**(0.54)**	(0.61)	**(0.53)**	(0.57)
Transportation expenses	**(0.85)**	(0.81)	**(0.75)**	(0.71)
Operating netbacks	**1.75**	2.88	**1.66**	2.16
Finance lease expense	**(0.59)**	(0.49)	**(0.54)**	(0.45)
Corporate netbacks	**1.16**	2.39	**1.12**	1.71

For the three months and year ended December 31, 2019, per unit operating netbacks decreased by 39% and 23% respectively compared to the same periods in 2018, and per unit corporate netbacks decreased by 51% and 35% respectively. The decrease in operating netbacks was the result of lower realized commodity prices (including risk management contracts) and higher per unit transportation expenses, impacted by lower production volumes. This was partially offset by lower operating expenses. The decrease in per unit corporate netbacks was also impacted by reduced production volumes.

GENERAL AND ADMINISTRATIVE EXPENSES

	Three months ended December 31,		Years ended December 31,	
($000s)	**2019**	**2018**	**2019**	**2018**
Gross expenses	**6,922**	6,957	**24,455**	25,825
Capitalized	**(1,804)**	(644)	**(5,068)**	(6,399)
Capital recoveries	**(209)**	(334)	**(925)**	(1,735)
Operating recoveries	**(188)**	(194)	**(774)**	(733)
Net expenses	**4,721**	5,785	**17,688**	16,958
Per unit *($/Mcfe)*	**0.19**	0.20	**0.16**	0.13

Gross general and administrative ("G&A") expenses for the three months and year ended December 31, 2019 decreased by 1% and 5% respectively, compared to the same periods ended December 31, 2018 due to staff composition. Net G&A expenses per unit for the year ended December 31, 2019 increased by 23% compared to the year ended December 31, 2018, impacted by reduced gross expenses and lower production volumes.

The Corporation's policy of allocating and capitalizing costs associated with new capital projects remained unchanged for the year ended December 31, 2019. Capitalized G&A and operating recoveries are in accordance with industry practice.

The Corporation anticipates that per unit G&A expenses will average in the range of $0.14/Mcfe to $0.16/Mcfe for the first half of 2020.

FINANCE EXPENSE

	Three months ended December 31,		Years ended December 31,	
($000s)	**2019**	**2018**	**2019**	**2018**
Finance lease expense	**14,593**	14,119	**58,153**	56,927
Interest expense	**6,510**	6,241	**25,403**	25,427
Accretion	**836**	1,000	**3,876**	3,849
Total	**21,939**	21,360	**87,432**	86,203
Per unit *($/Mcfe)*	**0.88**	0.74	**0.82**	0.68

Finance expense per unit for the three months and year ended December 31, 2019 increased by 19% and 21% respectively, reflecting reduced production volumes.

Finance lease expense is related to the right-of-use assets included in PP&E. Interest expense includes interest on bank debt, standby charges on the Corporation's syndicated credit facilities, and letter of credit fees, as well as interest on the senior notes and convertible debentures.

Accretion expense consists of accretion on the decommissioning obligation, senior notes and convertible debentures. The Corporation has estimated the net present value of the decommissioning obligations based on an undiscounted total future liability of $96.3 million at December 31, 2019, compared to $116.3 million at December 31, 2018.

ADJUSTED FUNDS FLOW FROM OPERATIONS

	Three months ended December 31,		Years ended December 31,	
($000s)	**2019**	**2018**	**2019**	**2018**
Natural gas and natural gas liquids revenue	**81,003**	125,669	**302,750**	404,372
Royalties	**(1,052)**	(1,639)	**(4,645)**	(6,345)
Realized gain (loss) on risk management contracts	**(1,657)**	474	**17,338**	38,650
Operating expenses	**(13,418)**	(17,521)	**(57,251)**	(72,830)
Transportation expenses	**(21,114)**	(23,468)	**(80,731)**	(89,876)
General and administrative expenses	**(4,721)**	(5,785)	**(17,688)**	(16,958)
Share unit (expense) recovery	**(58)**	1,333	**188**	(20)
Finance lease expense	**(14,593)**	(14,119)	**(58,153)**	(56,927)
Interest expense	**(6,510)**	(6,241)	**(25,403)**	(25,427)
Adjusted funds flow from operations	**17,880**	58,703	**76,405**	174,639
Per unit *($/Mcfe)*	**0.72**	2.03	**0.71**	1.38

SHARE-BASED COMPENSATION AND SHARE UNIT EXPENSE (RECOVERY)

	Three months ended December 31,		Years ended December 31,	
($000s)	**2019**	**2018**	**2019**	**2018**
Share-based compensation	**323**	797	**1,781**	2,757
Share unit expense (recovery)	**58**	(1,333)	**(188)**	20
Total	**381**	(536)	**1,593**	2,777

As at December 31, 2019, there were 9,212,075 options outstanding under the Corporation's stock option plan (the "Stock Option Plan"), at a weighted average exercise price of $3.69.

Share-based Compensation
Gross share-based compensation expense is a non-cash estimate of the cost of granting stock options to purchase shares, calculated using the Black-Scholes model. The expense does not represent actual cash compensation realized by the recipients of the stock options upon the exercise of these stock options. A portion of share-based compensation costs are capitalized on the same basis as G&A costs.

Share Unit Plans
The Corporation has a deferred share unit ("DSU") plan, whereby DSUs may be issued to members of the Board and eligible executive officers. Each DSU is a notional unit equal in value to one Common Share, which entitles the holder to a cash payment upon redemption. DSUs vest at the end of the financial quarter in which they are granted, but can only be converted to cash upon the holder ceasing to be a director and/or executive officer of the Corporation. The expense associated with the DSU plan is determined based on the 20-day volume weighted average price ("VWAP") of Common Shares at the grant date. The expense is recognized in the statement of operations in the quarter in which the units are granted, with a corresponding DSU liability recorded as a current liability in the statement of financial position. At reporting dates, the DSU liability is adjusted based on the 20-day VWAP of Common Shares. As at December 31, 2019, there were 1,932,979 DSUs outstanding under the plan.

The Corporation has a restricted share unit ("RSU") plan, whereby RSUs may be issued to eligible employees and executive officers. Each RSU is a notional unit equal in value to one Common Share, which entitles the holder to a cash payment upon redemption. RSUs vest in three equal installments on the first, second, and third anniversaries of the grant date, at which time the holder is eligible to receive a cash payment equal to the number of vested awards multiplied by the fair market value. The expense associated with the RSU plan is determined based on the 20-day VWAP of Common Shares at the grant date. The expense is recognized in the statement of operations over the vesting period, with a corresponding RSU liability recorded as a current liability in the statement of financial position. At reporting dates, the RSU liability is adjusted based on the 20-day VWAP of Common Shares. As at December 31, 2019, there were 1,084,400 RSUs outstanding under the plan.

The Corporation has a performance share unit ("PSU") plan, whereby PSUs may be issued to eligible executive officers. Each PSU is a notional unit equal in value to one Common Share, which entitles the holder to a cash payment upon redemption. PSUs vest upon the third anniversary of the grant date, at which time the holder is eligible to receive a cash payment equal to the number of vested awards multiplied by the fair market value. The unit value is adjusted for a performance multiplier which can range from 0 to 2 and is dependent on the performance of the Corporation for a predefined period. The expense associated with the PSU plan is determined based on the 20-day VWAP of Common Shares at the grant date. The expense is recognized in the statement of operations over the vesting period, with a corresponding PSU liability recorded as a current liability in the statement of financial position. At reporting dates, the PSU liability is adjusted based on the 20-day VWAP of Common Shares. As at December 31, 2019, there were 1,403,900 PSUs outstanding under the plan.

DEPLETION AND DEPRECIATION EXPENSE AND IMPAIRMENT

	Three months ended December 31,		Years ended December 31,	
($000s)	**2019**	**2018**	**2019**	**2018**
Depletion and depreciation	**19,208**	23,204	**84,072**	107,513
Impairment of PP&E	**150,000**	—	**150,000**	—
Depletion and depreciation and impairment	**169,208**	23,204	**234,072**	107,513
Per unit *($/Mcfe)*	**6.79**	0.80	**2.18**	0.85

Depletion and depreciation expense for the three months and year ended December 31, 2019 decreased by 17% and 22% respectively, compared to the three months and year ended December 31, 2018. The depletion calculation for the three months ended December 31, 2019 included future development costs associated with the development of the Corporation's proved plus probable reserves of $3.3 billion, compared to $3.5 billion as at December 31, 2018.

During the fourth quarter of 2019, the Corporation identified indicators of impairment on its sole CGU with respect to its PP&E assets, as a result of declines in the forecasted commodity prices utilized in the 2019 reserve report, compared to the prior year, and a market capitalization deficiency relative to the book value of the Corporation's shareholders equity. As a result, the Corporation completed an impairment test. The recoverable value was estimated using the value in use based on before tax discounted cash flows from natural gas and natural gas liquids proved plus probable reserves estimated by the Corporation's third-party reserve evaluators. It was determined that the carrying value of the CGU exceeded the recoverable amount and an impairment of $150.0 million was recognized. The before tax discount rates applied in the value in use calculation as at December 31, 2019 ranged between 10% - 30% depending on reserve category.

The following table outlines forecasted commodity prices and exchange rates used in the Corporation's impairment test at December 31, 2019. These future prices were based on the forecasted commodity prices used by the external reserve evaluators, adjusted for commodity price differentials and transportation specific to the Corporation's production. The reserve evaluators also include financial assumptions regarding royalty rates, operating costs, and future development capital that can significantly impact the recoverable amount which are assigned based on historic rates and future anticipated activities of the Corporation.

Year	**Exchange Rate**	**Natural Gas**	**Condensate**	**NGLs**
	(U.S.$/CAD$)	(CAD$/Mcf)	(CAD$/bbl)	(CAD$/bbl)
2020	0.76	2.38	78.92	33.61
2021	0.77	2.65	80.39	34.30
2022	0.78	2.77	84.51	35.58
2023	0.78	2.88	87.73	36.76
2024	0.78	2.95	90.32	37.89
2025	0.78	3.15	92.89	39.26
2026	0.78	3.22	95.48	40.49
2027	0.78	3.27	97.83	41.52
2028	0.78	3.34	99.80	42.33
2029	0.78	3.40	101.82	43.14
Remaining	0.78	4.37	130.76	53.33

As at December 31, 2018, indicators of impairment were determined to exist in the Corporation's CGU, as a result of a sustained decline in forward commodity benchmark prices for natural gas and natural gas liquids. An impairment test was carried out and the recoverable amounts were determined to exceed the carrying value. No impairment charge was recorded at December 31, 2018.

EXPLORATION AND EVALUATION ASSETS

The Corporation's exploration and evaluation ("E&E") assets totaled $69.3 million as at December 31, 2019, compared to $130.3 million as at December 31, 2018, and were not subject to depletion. During the year ended December 31, 2019, the Corporation disposed of a 75% working interest in undeveloped lands for cash proceeds of $45.0 million, and transferred $15.8 million to PP&E from E&E assets. At December 31, 2019, management expensed $0.2 million (December 31, 2018 - $1.7 million) related to land that is expiring. Substantially all of the E&E assets relate to undeveloped land.

As at December 31, 2019, the Corporation determined that indicators of impairment existed with respect to its E&E assets largely as a result of changes in future development plans as a result of the decline in forward commodity benchmark prices and as such an impairment test was performed. It was determined that the recoverable amount of the Corporation's E&E assets exceeded the carrying value and, as such, no impairment was recorded. Further, there was no impairment recorded as a result of the mandatory impairment assessment on the transfer of exploration and evaluation assets to property, plant and equipment.

CAPITAL EXPENDITURES

($000s)	Three months ended December 31, 2019	2018	Years ended December 31, 2019	2018
Drilling and completions	**5,710**	17,148	**63,419**	127,636
Facilities and equipment	**4,408**	765	**17,046**	17,935
Lease acquisitions and retention	**218**	144	**682**	692
Seismic	**38**	61	**75**	102
Capitalized G&A and unit awards	**1,923**	716	**5,621**	6,923
Exploration and development	**12,297**	18,834	**86,843**	153,288
Head office expenditures	**182**	362	**419**	1,072
Cash capital expenditures	**12,479**	19,196	**87,262**	154,360
Proceeds on sale of exploration and evaluation assets	**(45,000)**	—	**(45,000)**	—
Cash capital expenditures (net)	**(32,521)**	19,196	**42,262**	**154,360**
Share-based compensation	**209**	13	**412**	978
Decommissioning costs	**(20,821)**	4,780	**(3,430)**	5,623
Total	**(53,133)**	23,989	**39,244**	160,961

During the year ended December 31, 2019, the Corporation drilled 13 (13.0 net) Montney natural gas wells, and completed 14 (14.0 net) Montney natural gas wells.

Capital expenditures for the three months and year ended December 31, 2019 included $5.7 million and $63.4 million respectively, on drilling and completions activity. Facilities and equipment capital consists of equipping costs, pipeline construction costs and spending on processing facilities.

Non-cash decommissioning costs are impacted by drilling activity and a change in the estimated net present value of the decommissioning obligations, based on an undiscounted total future liability of $96.3 million at December 31, 2019, compared to $116.3 million at December 31, 2018. A change in estimate of the decommissioning obligation resulted from using a discount factor, being the nominal interest rate related to the liability at December 31, 2019, of 1.76%, and a market inflation rate of 1.35% at December 31, 2019. The discount factor, being the risk-free rate related to the liability at December 31, 2018, was 2.2%, and the consumer price index inflation rate was 2.0% at December 31, 2018. The impact of this change in estimate on future periods is impractical to determine.

The planned cash capital program for the first half of 2020 is currently estimated between $25 million and $30 million.

LIQUIDITY AND CAPITAL RESOURCES

Liquidity risk is the risk that the Corporation will not be able to meet its financial obligations as they become due. The Corporation's approach to managing liquidity is to ensure, to the extent possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Corporation's reputation.

Management closely monitors cash flow requirements to ensure that it has sufficient borrowing capacity to meet operational and financial obligations currently and in the foreseeable future; this excludes the potential impact of extreme circumstances that cannot reasonably be predicted, such as natural disasters. To achieve this objective, the Corporation prepares capital expenditure budgets, which are regularly monitored and updated as considered necessary. Further, the Corporation utilizes authority for expenditures on both operated and non-operated projects to further manage capital expenditures. The Corporation also typically collects its natural gas and natural gas liquids revenues from most properties on the 25th of each month.

As at December 31, 2019, the Corporation had net debt of $320.2 million, which included a working capital deficiency of $31.9 million. Management anticipates that the Corporation will continue to have adequate liquidity to fund working capital requirements and capital expenditures, in the short and long term, through a combination of cash flows, available credit facilities, senior notes and convertible debentures. As a result of the current commodity pricing environment, uncertainty exists in the commodity, credit and capital markets, which the Corporation continues to monitor in conjunction with its financing alternatives.

The Corporation's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The Corporation manages its capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying natural gas and natural gas liquids assets. The

Corporation considers its capital structure to include shareholders' equity, loans and borrowings and working capital. In order to maintain or adjust the capital structure, the Corporation may issue shares or debt, dispose of assets, and adjust its capital spending to manage current and projected debt levels.

The Corporation monitors capital based on the net debt to EBITDA ratio, calculated on a trailing four fiscal quarter basis. This ratio is calculated as net debt, which is defined as bank debt, senior notes, the liability portion of convertible debentures, and working capital, adjusted for the net current portion of the fair value of risk management contracts and current portion of the finance lease obligation, divided by trailing four fiscal quarter EBITDA, calculated as net income plus finance expense excluding the costs associated with the finance lease obligation, plus income taxes and adjustments for earnings or losses attributable to extraordinary and non-recurring gains or losses, as well as adjustments for any non-cash items including depreciation, depletion, amortization, deferred income taxes and non-cash gains or losses resulting from marking-to-market the outstanding risk management contracts. In order to facilitate the management of this ratio, the Corporation prepares annual capital expenditure budgets, which are updated as necessary depending on varying factors including current and forecast prices, successful capital deployment and general industry conditions. The annual and updated budgets are approved by the Board.

The Corporation is not subject to externally imposed capital requirements. The syndicated credit facilities are subject to a semi-annual review of the borrowing base which is directly impacted by the value of the natural gas and natural gas liquids reserves.

SENIOR NOTES

On August 23, 2017, the Corporation issued $150.0 million of 8.5% senior unsecured notes (the "Notes") with a five-year term by way of a private placement. Interest is payable in equal quarterly installments in arrears. The Notes are fully and unconditionally guaranteed as to the payment of principal and interest, on a senior unsecured basis, by the Corporation. There are no maintenance financial covenants.

The Notes are non-callable by the Corporation prior to the three-year anniversary. If the Corporation chooses to redeem the Notes prior to August 23, 2020, they will be subject to a make-whole premium equal to the Canada Yield Price, plus accrued and unpaid interest. At any time on or after August 23, 2020, the Corporation can redeem all or part of the Notes at the redemption prices set forth in the table below plus any accrued and unpaid interest.

Redemption Schedule	Percentage
August 23, 2020 - August 22, 2021	104.250 %
August 23, 2021 - February 22, 2022	102.125 %
February 23, 2022 - August 23, 2022	100.000 %

If a change of control event, as described in the investment agreement governing the Notes, occurs at any time before maturity, the Corporation must offer to repurchase the Notes at a price according to the redemption schedule above.

CONVERTIBLE DEBENTURES

On August 23, 2017, the Corporation issued $50.0 million of convertible unsecured subordinated debentures (the "Debentures"). The Debentures mature on August 23, 2021 and bear interest at 6.5% per annum payable quarterly. At the holder's option, the Debentures may be converted into Common Shares at any time prior to the close of business on the date of maturity at a conversion price of $5.60 per share (the "conversion price").

The Debentures were non-redeemable by the Corporation before February 22, 2020 other than pursuant to the 90% redemption right (see change of control event below). The Debentures are redeemable by the Corporation until August 23, 2021 at a redemption price equal to principal amount plus interest. Redemption may be satisfied in Common Shares if the 30-day VWAP on the notice date and the closing price immediately prior to the notice date are both greater than 140% of the conversion price.

On maturity, the Corporation may satisfy its obligation to holders of Debentures by issuing Common Shares if the Corporation's market capitalization exceeds $750 million. The number of Common Shares issuable is calculated based on 95% of the lesser of the 30-day VWAP and the two-day VWAP on the date of maturity.

Upon the occurrence of a change of control event, the Corporation must offer to repurchase the Debentures at a price according to the schedule below. If holders of 90% or more of the principal amount of Debentures outstanding accept the offer, the Corporation shall have the right to repurchase 100% of the Debentures outstanding.

Redemption Schedule	Percentage of Principal
January 1, 2020 - February 22, 2020	105.000 %
February 23, 2020 - August 23, 2021	100.000 %

BANK DEBT

As at December 31, 2019, the Corporation's syndicated credit facilities consisted of available credit facilities of $375 million. The available facilities are provided by a syndicate of financial institutions, and include a $325 million extendable revolving facility and a $50 million operating facility. The facilities revolve for a two-year period, which is extendable annually, subject to syndicate approval. The current maturity date is May 11, 2021. The facilities are subject to semi-annual review and re-determination of borrowing base by April 30 and October 31 of each year, or in the circumstance of a material adverse change. Any re-determination of the borrowing base is effective immediately, and if the borrowing base is reduced, the Corporation has 60 days to repay any shortfall. In addition, the Corporation has a $22 million unsecured letter of credit facility backstopped by EDC.

The credit facilities bear interest on a matrix system that ranges from the bank's prime rate plus 0.5% to the bank's prime rate plus 2.5% per annum depending on the Corporation's senior debt to EBITDA ratio, calculated on a trailing four fiscal quarter basis as defined by the lenders, ranging from less than 0.50:1 to greater than 3.00:1. This ratio is calculated as senior debt, defined as outstanding loans and borrowings plus or minus working capital, excluding the fair value of risk management contracts, less the principal amount of the Corporation's unsecured notes and convertible debentures; divided by the trailing four fiscal quarter EBITDA, defined as net income plus finance expense excluding the costs associated with the finance lease obligation, plus income taxes and adjustments for earnings or losses attributable to extraordinary and non-recurring gains or losses, as well as adjustments for any non-cash items including depreciation, depletion, amortization, deferred income taxes and non-cash gains or losses resulting from marking-to-market the outstanding risk management contracts.

The credit facilities provide that advances may be made by way of prime rate loans, U.S. Base Rate loans, LIBOR loans, bankers' acceptances, letters of credit or letters of guarantee. A standby fee of 0.3375% to 0.7875% per annum is charged on the undrawn portion of the credit facilities, also calculated depending on the Corporation's senior debt to EBITDA ratio, calculated on a four fiscal quarter basis, which was 2.00:1.00 at December 31, 2019.

As at December 31, 2019, Painted Pony had USD $98.6 million (CAD $128.1 million) in LIBOR loans outstanding, with an effective interest rate of 3.785% per annum. In addition, as at December 31, 2019, the Corporation had outstanding letters of credit totaling CAD $34.6 million and USD $15.0 million (CAD $19.5 million), which reduce the credit available on the syndicated facilities, as well as outstanding letters of credit totaling CAD $21.5 million, which are backstopped by EDC.

Security over all of the Corporation's assets is provided by a floating charge demand debenture in the aggregate amount of $1.0 billion. The Corporation has provided a negative pledge and an undertaking to provide fixed charges over its natural gas and natural gas liquids reserves in certain circumstances. The syndicated facilities are not subject to financial covenants.

STRATEGIC ALLIANCE AND FINANCE LEASE OBLIGATION

The Corporation is party to a series of agreements (collectively, the "Strategic Alliance") with a Canadian midstream company (the "Midstream Company"), relating to the development of processing infrastructure and marketing services for natural gas and natural gas liquids.

Under the Strategic Alliance, the Midstream Company committed to building gas processing facilities including a 198 MMcf/d shallow cut gas processing facility at the Townsend property and related pipeline infrastructure, which commenced commercial operations in 2016 (the "Townsend Facility"). During 2017, Painted Pony entered into an agreement with the Midstream Company in respect of a Townsend Phase 2 expansion ("Townsend Phase 2") which consisted of a 99 MMcf/d gas processing train located on the existing Townsend site adjacent to, and sharing joint equipment with the original Townsend Facility. Painted Pony did not acquire any legal right, title, or interest in the Townsend Facility, Townsend Phase 2 or related pipeline infrastructure. The Corporation is not responsible for future pipeline or facility restoration liabilities. All construction costs were borne by the Midstream Company. The Corporation has the right to a minimum of 198 MMcf/d of firm capacity, in respect of which there is a take or pay obligation on production volumes delivered to the facility of 180 MMcf/d. The Corporation also has the right to the full 99 MMcf/d of firm capacity at Townsend Phase 2, in respect of which there is a take or pay obligation on production volumes delivered to the facility of 90 MMcf/d, which commenced in the first quarter of 2018.

The Townsend Facility, related pipeline infrastructure and Townsend Phase 2 have been recorded as a finance lease. Painted Pony has recorded the right-to-use asset, representing the total construction cost of the Townsend Facility of approximately $490 million, with a corresponding lease liability on the statement of financial position. Over the course of the 20-year term, there is a capital fee paid to the Midstream Company, which includes finance costs and the amortization of the obligation. The associated processing fee is recorded in operating expenses.

On transition to IFRS 16 - *Leases* ("IFRS 16"), the Corporation recognized an additional $1.4 million of right-of-use assets and lease liabilities related to office space. When measuring office lease liabilities, the Corporation discounted lease payments using an incremental borrowing rate at January 1, 2019 of 4.9%.

Total expected payments, not included in "Commitments" below, for the Corporation's facilities and related infrastructure, and office space recorded as finance lease obligations are reflected in the table below.

($000s)	**Within 1 year**	**After 1 year but not more than five years**	**More than five years**	**Total**
Processing	54,921	291,529	514,614	861,064
Transportation	10,144	54,559	157,836	222,539
Office space	480	848	—	1,328
Total	65,545	346,936	672,450	1,084,931
Principal	8,203	83,248	393,924	485,375

Subsequent to December 31, 2019, the Corporation announced cost structure improvements at the Townsend Facility, Townsend Phase 2, and the related pipeline infrastructure, which, amongst other savings, will decrease the capital fees associated with the facilities and related pipeline infrastructure. These costs are currently recorded as a finance lease on the statement of financial position. In addition to reduced facility costs, the Corporation will reduce firm transportation obligations on two associated pipelines, and reduce take or pay volume commitments at the facilities over time. In accordance with IFRS 16*,* when a finance lease is modified, the modified lease is evaluated to determine whether it is, or contains, a lease. The Corporation is currently assessing the contract modifications to determine whether or not the new contract contains a lease, and the effect that these changes have on the financial statements. If any right of use assets are derecognized, any gain or loss resulting from the derecognition of the right of use asset and lease liability will be recorded to the statement of operations from the effective date of the modification.

COMMITMENTS

The following is a summary of the estimated costs required to fulfill Painted Pony's remaining contractual commitments as at December 31, 2019.

($000s)	**2020**	**2021**	**2022**	**2023**	**2024**	**Thereafter**	**Total**
Transportation and processing	113,721	118,440	134,558	112,961	108,905	1,345,972	1,934,557
Interest on senior notes to maturity	12,750	12,750	9,563	—	—	—	35,063
Interest on convertible debentures to maturity	3,250	2,438	—	—	—	—	5,688
Other	1,115	1,098	989	—	—	—	3,202
Total commitments	130,836	134,726	145,110	112,961	108,905	1,345,972	1,978,510

Transportation commitments include contracts to transport natural gas and natural gas liquids through third-party owned pipeline systems in North America. Processing commitments include contracts to process natural gas and natural gas liquids through third-party owned gas processing facilities in British Columbia. Interest on senior notes includes quarterly interest on senior notes. Interest on convertible debentures includes quarterly interest on convertible debentures. Other commitments include variable lease payments not included in lease liabilities.

RELATED PARTY TRANSACTIONS AND OFF BALANCE SHEET ARRANGEMENTS

The Corporation was not involved in any related party transactions or off balance sheet arrangements for the year ended December 31, 2019 or the year ended December 31, 2018, except the off balance sheet arrangements discussed above under "Commitments".

SHARE CAPITAL

The Corporation has an unlimited number of Common Shares and an unlimited number of preferred shares ("Preferred Shares") authorized for issuance. As at December 31, 2019 and March 11, 2020, there were 160,995,692 Common Shares issued and outstanding, and there were no Preferred Shares issued and outstanding.

Pursuant to the Stock Option Plan, options to purchase Common Shares are granted to executive officers and employees of the Corporation. Non-employee directors are not eligible for grants of stock options. Stock options are granted at the VWAP of the Common Shares for the five trading days immediately preceding the date of grant, and have a five-year term. Stock options granted vest as to one-third on each of the first, second and third anniversaries of the grant date. As at December 31, 2019, an aggregate of 9,212,075 stock options were issued and outstanding at a weighted-average price of $3.69 per stock option. As at March 11, 2020, an aggregate of 11,581,036 stock options were issued and outstanding at a weighted-average price of $3.05 per stock option, of which 6,190,065 were exercisable.

INCOME TAXES

During May 2019, the Government of Alberta tabled legislation to decrease the general corporate tax rate from 12% to 8% which will be phased-in between July 1, 2019, and January 1, 2022. As these corporate income tax measures were included in Alberta Bill 3 they were considered substantively enacted under IFRS in the calculation of the Corporation's deferred tax liabilities in the second quarter of 2019. As a result of the reduction in the corporate provincial tax rate, the Corporation analyzed the expected timing of settlement of the taxable temporary differences which give rise to deferred income tax assets and liabilities and re-measured these amounts using the appropriate, newly enacted corporate provincial income tax rates.

As at December 31, 2019, the Corporation did not recognize a deferred tax asset in respect of $200.1 million of non-capital losses. A deferred tax asset is recognized to the extent that it is likely that future taxable income will be available against which the temporary difference can be utilized. The Corporation had a $10.9 million liability as at December 31, 2018. The deferred tax recovery was $10.9 million during the year ended December 31, 2019, compared to an expense of $3.1 million during the year ended December 31, 2018. The Corporation has non-capital losses of $382.2 million which expire in the years 2026 through 2035. Total tax pools available for deduction against future income at December 31, 2019 and 2018 were $1.4 billion.

DIVIDENDS

The Corporation has not declared or paid any dividends and does not have a current intention to do so.

PERFORMANCE COMPARED TO EXPECTATIONS

Readers are reminded that forward-looking statements in this MD&A are subject to significant risks and uncertainties, many of which are beyond Painted Pony's control and are based on a number of material factors and assumptions, some or all of which may prove to be incorrect. See "Advisories - Forward-looking Statements" in the MD&A for further discussion of forward looking statements, risks and uncertainties. A comparison of actual performance to the previously announced expectations of the Corporation is as follows:

- For 2019, the Corporation expected to receive a realized natural gas price at a premium to the AECO (5A) benchmark price. The actual weighted average price received during 2019 represented a 36% premium to the AECO (5A) daily spot price, influenced by the Corporation's market diversification efforts.
- Painted Pony's royalty rate for 2019 was expected to be approximately 1.5% to 2.0% of total revenues. The actual royalty rate for 2019 was 1.5% of total revenues.
- Operating expenses for 2019 were expected to be between $0.55/Mcfe and $0.60/Mcfe. Actual operating expenses for 2019 were $0.53/Mcfe, as a result of facility cost structure improvements and water management initiatives.
- Transportation expenses for 2019 were expected to be between $0.75/Mcfe and $0.80/Mcfe. Actual transportation expenses for 2019 were $0.75/Mcfe.
- Net G&A expenses for 2019 were expected to be between $0.14/Mcfe to $0.17/Mcfe. Actual net G&A expenses for 2019 were $0.16/Mcfe.

CRITICAL ACCOUNTING JUDGMENTS AND ESTIMATES

The preparation of financial statements requires management to make judgments, estimates and assumptions that affect the application of IFRS accounting policies, reported amounts of assets and liabilities, and income and expenses. Accordingly, actual results may differ from these estimates. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

Critical Accounting Judgments

The following are critical judgments that management has made in the process of applying accounting policies and that have the most significant effect on the amounts recognized in the financial statements.

Cash-Generating Units

The Corporation's assets are aggregated into cash-generating units ("CGU" or "CGUs") for the purpose of assessing impairment. CGUs are based on an assessment of the units ability to generate independent cash inflows. The determination of these CGUs was based on management's judgment in regard to shared infrastructure, geographical proximity, petroleum type and exposure to market risk and materiality. By their nature, these assumptions are subject to management's judgment and may impact the carrying value of the Corporation's net assets in future periods.

Impairment Indicators

Judgments are required to assess when impairment indicators exist and impairment testing is required. The Corporation is required to consider information from both external sources (such as negative downturn in commodity prices, significant adverse changes in the technological, market, economic or legal environment in which the entity operates) and internal sources (such as downward revisions in reserves, significant adverse effects on the financial and operational performance of a CGU, evidence of obsolescence or physical damage to the asset). In determining the recoverable amount of assets, in the absence of quoted market prices, impairment tests are based on estimates of reserves, production rates, future natural gas and natural gas liquids prices, future costs, discount rates, market value of land and other relevant assumptions.

The application of the Corporation’s accounting policy for E&E assets requires management to make certain judgments as to future events and circumstances as to whether economic quantities of reserves have been found.

Deferred Taxes

In determining its deferred tax provisions, the Corporation must apply judgment when interpreting and applying tax laws and regulations. The determination of the appropriate rules may be uncertain for many periods. The final outcome could result in amounts different from those initially recorded and could impact tax expense in the periods where a determination is made. Judgments are also made by management to determine the likelihood of whether deferred tax assets at the end of the reporting period will be realized from future taxable income.

Critical Accounting Estimates

The following are key estimates made by management affecting the measurement of balances and transactions in these financial statements.

Impact of Reserves

Estimation of recoverable quantities of proved and probable reserves includes estimates regarding future commodity prices, exchange rates, discount rates and production and transportation expenses for future cash flows as well as the interpretation of complex geological and geophysical models and data. Changes in expected future cash flows in reported reserves can affect the impairment of assets, the decommissioning obligation, the economic feasibility of E&E assets and the amounts reported for depletion and depreciation of PP&E, and the recognition of deferred tax assets. These reserve estimates are prepared in accordance with the Canadian Oil and Gas Evaluation Handbook and are verified by independent qualified reserve evaluators, who work with information provided by the Corporation to establish reserve determinations in accordance with National Instrument 51-101 - *Standards of Disclosure for Oil and Gas Activities* (“NI 51-101”).

In a business combination, management makes estimates of the fair value of assets acquired and liabilities assumed which includes assessing the value of natural gas and natural gas liquids properties based upon the estimation of recoverable quantities of proved and probable reserves being acquired.

Share-Based Compensation

All equity-settled, share-based awards issued by the Corporation are fair valued using the Black-Scholes option-pricing model. In assessing the fair value of equity-based compensation, estimates have to be made regarding the expected volatility in share price, option life, dividend yield, risk-free rate and estimated forfeitures at the initial grant date.

Derivative Financial Instruments

Painted Pony records risk management contracts at fair value with changes in fair value recognized in the statements of operations. The Corporation’s estimate of the fair value is determined using observable market data and external counterparty information, including estimated forward prices and volatility in those prices.

Decommissioning Obligation

The Corporation estimates future remediation costs of production facilities, wells and pipelines at different stages of development and construction of assets or facilities. In most instances, removal of assets occurs many years into the future. This requires estimates regarding abandonment date, future environmental and regulatory legislation, the extent of reclamation activities, the engineering methodology for estimating cost, future removal technologies in determining the removal cost and liability-specific discount rates to determine the present value of these cash flows.

Deferred Taxes

Tax provisions are based on enacted or substantively enacted laws. Changes in those laws could affect amounts recognized in the statement of operations both in the period of change, which would include any impact on cumulative provisions, and in future periods.

Deferred tax assets are recognized only to the extent it is considered probable that those assets will be recoverable. This involves an assessment of when those deferred tax assets are likely to reverse and a judgment as to whether or not there will be sufficient taxable income available to offset the tax assets when they do reverse. This requires assumptions regarding future profitability and is therefore inherently uncertain. Estimates of future taxable income are based on forecasted cash flows from operations.

Leased Assets

The incremental borrowing rates are based on judgments including economic environment, term, currency, and the underlying risk inherent to the asset. The carrying balance of the right-of-use assets, lease obligations, and the resulting interest and depletion and depreciation expense, may differ due to changes in the market conditions and lease term. Lease terms are based on assumptions regarding extension terms that allow for operational flexibility and future market conditions.

NEW ACCOUNTING PRONOUNCEMENTS

New accounting standards, amendments to accounting standards and interpretations are effective for annual periods beginning on or after January 1, 2019 and have been applied in preparing the financial statements year ended December 31, 2019. The standards applicable to the Corporation are as follows:

Leases

Effective January 1, 2019, the Corporation has applied IFRS 16, using the modified retrospective approach, and therefore the comparative information has not been restated and continues to be reported under IAS 17 and IFRIC 4. The impact of changes is disclosed in notes 3 and 17 of the Annual Financial Statements.

FUTURE ACCOUNTING PRONOUNCEMENTS

Business Combinations

On October 22, 2018, the IASB issued amendments to the guidance in IFRS 3 - *Business Combinations* ("IFRS 3"), revising the definition of a business and providing for the addition of an optional 'concentration test' to determine if the acquisition is a business. To be considered a business under the amendments to IFRS 3, an acquisition would have to include an input and a substantive process that together significantly contribute to the ability to create outputs. The three elements of a business are defined as follows:

- Input - Any economic resource that creates outputs, or has the ability to contribute to the creation of outputs, when one or more processes are applied to it.
- Process - Any system, standard, protocol, convention or rule that, when applied to an input or inputs, creates outputs or has the ability to contribute to the creation of outputs.
- Output - The result of inputs and processes applied to those inputs that provide goods or services to customers, generate investment income or generate other income from ordinary activities.

The optional 'concentration test' permits a simplified assessment that results in an asset acquisition if substantially all of the fair value of the gross assets is concentrated in a single identifiable asset or a group of similar identifiable assets. An entity may elect to apply, or not apply, the test. An entity may make such an election separately for each transaction or other event. If the concentration test is met, the sets of activities and assets is determined not to be a business and no further assessment is needed.

The amendments to IFRS 3 apply to businesses acquired in annual reporting periods beginning on or after January 1, 2020, with early adoption permitted. The Corporation has chosen to adopt the amendments to IFRS 3 effective January 1, 2020.

BUSINESS RISKS

Painted Pony's production and development activities are concentrated in western Canada, where activity is highly competitive and includes a variety of companies ranging from smaller junior producers to the much larger integrated producers. Painted Pony is subject to various types of business risks and uncertainties, including but not limited to:

- volatility of natural gas and crude oil prices;
- availability of qualified personnel and drilling and completion equipment;
- finding and developing natural gas and natural gas liquids reserves at economic costs;
- production of natural gas and natural gas liquids in commercial quantities;
- marketability of natural gas and natural gas liquids production, including transportation access;
- environmental risk associated with well operations and production facilities;
- political uncertainty in Canada and the impact on liquefied natural gas and other infrastructure projects; and
- changing government regulations relating to royalty legislation, income tax laws, incentive programs, operating practices, fracturing regulations and environmental protection relating to the oil and natural gas industry.

In order to reduce exploration risk, the Corporation strives to employ highly qualified and motivated professional employees with a demonstrated ability to generate quality proprietary geological and geophysical prospects. To help maximize drilling success, Painted Pony combines exploration in areas that afford multi-zone prospect potential, targeting a range of low to moderate risk prospects with minimal exposure to select high-risk plays with high-reward opportunities. Painted Pony also explores in areas where the Corporation's employees and consultants have significant experience.

The Corporation mitigates its risks related to producing hydrocarbons through the utilization of the most appropriate technology and information systems. Painted Pony seeks operational control of its projects, where feasible.

Natural gas and natural gas liquids development and production can involve environmental risks such as pollution of the environment and destruction of natural habitat, as well as safety risks such as personal injury. In order to mitigate such risks, Painted Pony conducts its operations with high standards and follows safety procedures intended to reduce the potential for personal injury to employees, contractors and the public at large. The Corporation maintains insurance coverage to address significant business risks, at market rates and within defined limits and deductibles.

The amount and terms of this insurance are reviewed on an ongoing basis and adjusted as necessary to reflect changing corporate requirements, as well as industry standards and government regulations. Painted Pony may periodically use financial or physical delivery hedges to reduce its exposure against the potential adverse impact of commodity price volatility, as governed by formal policies approved by senior management, subject to controls established by the Board.

The Corporation uses financial derivatives and physical delivery sales contracts to mitigate some of the exposure to commodity price, foreign exchange, and interest rate risk, and provide a level of stability to operating cash flows which enables the Corporation to fund its capital development program.

Additional information about the Corporation's business risks is outlined in the advisories section of this MD&A and is available in Painted Pony's AIF for the year ended December 31, 2018 that is filed on SEDAR at www.sedar.com under the Corporation's profile.

LEGAL, ENVIRONMENTAL, REMEDIATION AND OTHER CONTINGENT MATTERS

The Corporation reviews legal, environmental, remediation and other contingent matters to determine whether a loss is probable based on judgment and interpretation of laws and regulations, and to determine whether the loss can reasonably be estimated. When the loss is determined, it is charged to income. The Corporation's management monitors known and potential contingent matters and makes appropriate provisions by charges to income when warranted by the circumstances.

The Corporation may from time to time be involved in legal claims or litigation arising in the normal course of business. The outcome of legal claims or litigation is uncertain and there can be no assurance that such legal claims or litigation will be resolved in the Corporation's favour. Other than disclosed herein, the Corporation does not currently believe that the outcome of adverse decisions in any pending or threatened legal claims or litigation, or any amount which it may be required to pay, would have a material adverse impact on its financial position or results of operations.

There is ongoing litigation involving the Blueberry River First Nation ("BRFN") and the British Columbia Government regarding the obligations of natural resource companies and the Crown relative to the adequacy of consultation and cumulative effects in respect of upstream oil and gas development in northeast British Columbia, where a substantial portion of the Corporation's land and assets are situated. The Corporation is not a party to the litigation. While a successful claim by BRFN may be adversely material to the Corporation, at this point, the success of the claim and any corresponding impact is indeterminable. If the claim is decided in BRFN's favour, it would have an adverse impact on the Corporation, its operations and production, particularly for those operations that may be considered to impact Aboriginal traditional lands or rights. The Corporation is therefore, actively monitoring the status of the BRFN claim.

DISCLOSURE CONTROLS & PROCEDURES AND INTERNAL CONTROL OVER FINANCIAL REPORTING

The Corporation's Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") have designed, or caused to be designed under their supervision, disclosure controls and procedures ("DC&P"), as defined in National Instrument 52-109 - *Certification of Disclosure in Issuers' Annual and Interim Filings* ("NI 52-109") to provide reasonable assurance that: (i) material information relating to the Corporation is made known to the CEO and CFO by others, particularly during the period in which the annual and interim filings are being prepared; and (ii) information required to be disclosed by the Corporation in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time period specified in securities legislation. As at December 31, 2019, the CEO and CFO evaluated the design and operation of the Corporation's DC&P. Based on that evaluation, the CEO and CFO concluded that the Corporation's DC&P was effective as at December 31, 2019.

The CEO and CFO have designed, or caused to be designed under their supervision, internal controls over financial reporting ("ICFR"), as defined in NI 52-109, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS. The Corporation has established and maintains ICFR using the criteria that were set forth by the Committee of Sponsoring Organizations of the Treadway Commission in Internal Control - Integrated Framework (2013). As at December 31, 2019, the CEO and CFO evaluated the design and operating effectiveness of the Corporation's ICFR. Based on that evaluation, the CEO and CFO concluded that the Corporation's ICFR was effective as at December 31, 2019.

No material changes in the Corporation's ICFR were identified during the period beginning on October 1, 2019 and ended on December 31, 2019 that have materially affected, or are reasonably likely to materially affect, the Corporation's ICFR. It should be noted that a control system, including the Corporation's disclosure and internal controls and procedures, no matter how well conceived, can provide only reasonable, but not absolute assurance that the objectives of the control system will be met and it should not be expected that the disclosure and internal controls will prevent all errors or fraud.

SELECTED QUARTERLY INFORMATION

The following tables set forth selected financial information of the Corporation for the eight most recently completed quarters ending at the fourth quarter of 2019.

Quarter ended (*$000s*, except where noted)	**Dec 31, 2019**	**Sep 30, 2019**	**Jun 30, 2019**	**Mar 31, 2019**
Natural gas and natural gas liquids revenue	81,003	54,940	59,124	107,683
Cash flows from (used in) operating activities	9,024	(1,562)	22,250	53,757
Per share - basic	0.06	(0.01)	0.14	0.33
Per share - diluted	0.05	(0.01)	0.13	0.32
Adjusted funds flow from operations	17,880	2,888	9,141	46,696
Per share - basic	0.11	0.02	0.06	0.29
Per share - diluted	0.11	0.02	0.05	0.27
Net loss and comprehensive loss - basic and diluted	(178,466)	(37,055)	(14,715)	(2,622)
Per share	(1.11)	(0.23)	(0.09)	(0.02)
Cash capital expenditures (net)	(32,521)	22,951	15,286	36,906
Working capital (deficiency)	(31,909)	(32,523)	(20,461)	(6,222)
Bank debt	119,901	156,397	134,842	138,226
Senior notes	144,754	144,324	143,903	143,497
Convertible debentures - liability	47,466	47,112	46,767	46,435
Net debt	320,201	369,938	344,165	341,355
Total assets	1,803,447	2,018,194	2,013,380	2,043,719
Decommissioning obligation	51,009	71,778	68,488	60,567
Average daily production volumes *(boe/d)*	45,173	47,495	48,978	54,389
Average daily production volumes *(MMcfe/d)*	271.0	285.0	293.9	326.3
Realized commodity prices before financial risk management contracts				
Natural gas *($/Mcf)*	2.89	1.72	1.66	3.24
NGLs *($/bbl)*	42.87	36.14	45.57	51.17
Total *($/Mcfe)*	3.25	2.10	2.21	3.67
Operating netbacks *($/Mcfe)*	1.75	1.07	1.26	2.45
Corporate netbacks *($/Mcfe)*	1.16	0.51	0.72	1.96

Quarter ended (*$000s*, except where noted)	**Dec 31, 2018**	**Sept 30, 2018**	**Jun 30, 2018**	**Mar 31, 2018**
Natural gas and natural gas liquids revenue	125,669	90,238	87,656	100,809
Cash flows from operating activities	48,475	33,269	35,734	51,557
Per share - basic	0.30	0.21	0.22	0.32
Per share - diluted	0.29	0.20	0.21	0.30
Adjusted funds flow from operations	58,703	30,319	39,056	46,561
Per share - basic	0.36	0.19	0.24	0.29
Per share - diluted	0.35	0.18	0.23	0.27
Net income (loss) and comprehensive income - basic	62,473	(13,847)	(33,169)	(8,394)
Per share - basic	0.39	(0.09)	(0.21)	(0.05)
Net income (loss) and comprehensive income (loss) - diluted	63,071	(13,847)	(33,169)	(8,394)
Per share - diluted	0.37	(0.09)	(0.21)	(0.05)
Cash capital expenditures (net)	19,196	39,433	17,638	78,093
Working capital (deficiency)	32,890	(37,664)	(1,142)	(5,089)
Bank debt	163,140	172,909	184,271	163,533
Senior notes	143,105	142,715	142,335	141,968
Convertible debentures - liability	46,113	45,792	45,480	45,178
Net debt	348,473	385,119	375,313	396,062
Total assets	2,055,354	2,011,154	2,010,612	2,057,878
Decommissioning obligation	53,565	48,496	50,885	49,613
Average daily production volumes *(boe/d)*	52,453	58,330	60,116	60,703
Average daily production volumes *(MMcfe/d)*	314.7	350.0	360.7	364.2
Realized commodity prices before financial risk management contracts				
Natural gas *($/Mcf)*	3.90	2.10	1.90	2.38
NGLs *($/bbl)*	56.72	59.21	61.75	59.39
Total *($/Mcfe)*	4.34	2.80	2.67	3.08
Operating netbacks *($/Mcfe)*	2.88	1.72	1.95	2.18
Corporate netbacks *($/Mcfe)*	2.39	1.27	1.51	1.76

SELECTED ANNUAL INFORMATION

The following tables set forth selected annual financial information of the Corporation for the three most recently completed years ending December 31, 2019.

Year ended *($000s*, except where noted*)*	**Dec 31, 2019**	**Dec 31, 2018**	**Dec 31, 2017**
Natural gas and natural gas liquids revenue	302,750	404,372	249,186
Cash flows from operating activities	88,554	169,035	106,917
Per share - basic	0.55	1.05	0.76
Per share - diluted	0.52	0.99	0.74
Adjusted funds flow from operations	76,405	174,639	109,204
Per share - basic	0.47	1.08	0.78
Per share - diluted	0.45	1.03	0.76
Net income (loss) and comprehensive income (loss)	(232,858)	7,064	122,376
Per share - basic	(1.45)	0.04	0.87
Net income (loss) and comprehensive income (loss) - diluted	(232,858)	7,064	123,226
Per share - diluted	(1.45)	0.04	0.85
Cash capital expenditures (net)	42,262	154,360	302,614
Working capital (deficiency)	(31,909)	32,890	33,025
Bank debt	119,901	163,140	149,228
Senior notes	144,754	143,105	141,613
Convertible debentures - liability	47,466	46,113	44,887
Net debt	320,201	348,473	363,884
Total assets	1,803,447	2,055,354	2,031,643
Decommissioning obligation	51,009	53,565	46,811
Average daily production volumes *(boe/d)*	48,979	57,879	42,882
Average daily production volumes *(MMcfe/d)*	293.9	347.3	257.3

Significant factors and trends that have affected the Corporation's results during the above annual and quarterly periods include:

- Natural gas and natural gas liquids revenues are impacted by both fluctuating commodity prices and production volumes. The Corporation's successful capital program and commencement of commercial operations at the Townsend Facility and Townsend Phase 2 have generated incremental production volumes, offset by shut-in production volumes during low pricing environments and pipeline disruptions. There has been significant volatility and fluctuation in commodity prices over the last three years.
- Seasonality of the Company's activities and the Canadian oil and gas industry.
- Royalties vary due to commodity prices, production levels and the status of provincial royalty incentive programs. As the production base matures, incremental royalties occur on wells as the maximum volumes provided for under provincial incentive programs are attained.
- Net income (loss) and comprehensive income (loss) throughout the periods was significantly influenced by unrealized and realized gains or losses on risk management contracts.
- Fluctuations in capital expenditures have reflected both available capital resources and capital spending restraints during weaker commodity price cycles.
- The Corporation's focus is now on development and production, with the Corporation utilizing bank debt, convertible debentures, senior notes and cash flow to assist with the capital program. As the Corporation proceeds with its prudent capital program, bank debt amounted to $119.9 million as at December 31, 2019.
- Total assets and non-current liabilities have generally increased as the Corporation's capital program has been executed.

ADVISORIES

Forward-looking Statements

Certain statements in this MD&A constitute forward-looking information (collectively, the "forward-looking statements") within the meaning of applicable Canadian securities laws. Such forward-looking statements relate to future events, including expectations of future production, components of cash flow and net income, expected future events, including with respect to the Corporation's well program, contractual commitments, capital expenditures, dividend policy and credit facility, and/or financial results that are forward-looking in nature and subject to substantial risks and uncertainties. All statements other than statements of historical fact contained in this MD&A may be forward-looking statements. Such statements and information may be identified by words such as "anticipate", "will", "intend", "could", "should", "may", "expect", "forecast", "plan", "potential", "project", "budget", "estimate", "assume", "believe", "shall", "continue", "target", "working to", "forward looking to", and similar terms or the negatives thereof or other comparable terminology. The forward-looking statements contained in this MD&A involve known and unknown risks, uncertainties and other factors that are beyond the Corporation's control, which may cause actual results or events to differ materially from those anticipated in such forward-looking statements.

The forward-looking statements contained in this MD&A represent management's reasonable projections, expectations and estimates as of the date of this document; however, undue reliance should not be placed upon them as they are derived from numerous assumptions, certain or all of which may prove to be incorrect. These assumptions are subject to known and unknown risks and uncertainties, including the business risks discussed in this MD&A and the risks discussed in the Corporation's AIF for the year ended December 31, 2018*, many of which are beyond Painted Pony's control and which may cause actual performance and financial results to differ materially from any projections of future performance or results expressed or implied by such forward-looking statements. In addition, forward-looking statements may include statements or information attributable to third-party industry sources. Additionally, there can be no assurance that the plans, intentions or expectations upon which such forward-looking statements are based will occur.*

In particular, and without limitation, this MD&A contains forward-looking statements pertaining to the following:

- *the expectation that fees at the Townsend facility will be reduced by approximately 10%;*
- *the expectation that fixed cost liquids transportation expense from the Townsend facility to the North Pine Fractionator will be reduced by approximately 40%;*
- *the Corporation receiving a natural gas price that exceeds the AECO (5A) benchmark price;*
- *expectations with respect to average price estimates for 2020;*
- *the expectation that overall royalties for 2020 will be approximately 1.5% to 2.0% of total revenues;*
- *the expectation that average per unit operating expenses will be between $0.60/Mcfe and $0.65/Mcfe for 2020;*
- *the expectation that the planned cash capital program for 2020 will be between $25 and $30 million;*
- *the expectation that average per unit transportation expenses will be between $0.85/Mcfe and $0.90/Mcfe for 2020;*
- *expectations regarding sales in the Dawn and Sumas market;*
- *the expectation that per unit G&A expenses will average between $0.14/Mcfe to $0.16/Mcfe for 2020;*
- *the Corporation having adequate liquidity to fund working capital requirements and capital expenditures through a combination of cash flows, available credit facilities, senior notes and convertible debentures;*
- *the Corporation's plans to monitor the commodity, credit and capital markets;*
- *the possibility that the Corporation may issue shares or debt, dispose of assets, and adjust its capital spending to manage current and expected debt levels;*
- *expectations as to payments in relation to the Townsend Facility and Townsend Phase 2;*
- *expectations as to timing and outcome of the next review of the Corporation's credit facilities;*
- *expectations as to the estimated costs required to fulfill the Corporation's remaining contractual commitments as at December 31, 2019;*
- *expectations with respect to the declaration or payment of dividends;*
- *expectations that future taxable income will be available to utilize accumulated tax pools;*
- *expectations as to the impact of critical accounting judgments and estimates;*
- *expectations regarding future accounting pronouncements and their impact on the Corporation;*
- *expectations regarding the consequences of the outstanding claim involving a potential settlement between the BRFN and the Province of British Columbia; and*
- *expectations as to potential future impacts of adverse decisions in any pending or threatened legal actions.*

With respect to the forward-looking statements contained in this MD&A, assumptions have been made regarding:

- *the continued suitability of the Corporation's planned capital program;*
- *the utilization of available credit facilities for 2020;*
- *the validity of data used by GLJ Petroleum Consultants Ltd.("GLJ") in their independent reserves evaluation;*
- *the continued adherence to contractual commitments;*
- *the financial position of the applicable entities mitigating the risk of accounts receivable becoming uncollectible;*
- *the cost structure of the Corporation;*
- *the potential impact of legal claims on the Corporation's financial position; and*
- *the ability to exercise rights or satisfy obligations under bank debt and debt securities.*

Certain or all of the forward-looking statements may prove to be incorrect. These forward-looking statements represent the Corporation's views as of the date of this MD&A and such information should not be relied upon as representing the Corporation's views as of any date subsequent to the date of this MD&A. The Corporation has attempted to identify important factors that could cause actual results, performance or achievements to vary from the current expectations or estimates expressed or implied by the forward-looking statements contained herein. However, there may be other factors that cause results, performance or achievements not to be as expected or estimated and that could cause actual results, performance or achievements to differ materially from current expectations. Other risks and uncertainties include, but are not limited to, the following:

- *normal risks common to the oil and gas industry, including exploration, development and production operations risks;*
- *volatility of commodity prices;*
- *risks and uncertainty associated with commodity, credit and capital markets;*
- *changes in interest and foreign exchange rates;*
- *risks and uncertainty of natural gas and natural gas liquids geological deposits and reserves estimates;*
- *health, safety and environmental risks;*

- *revisions, amendments or changes to capital expenditure plans including exploration, development and exploitation projects;*
- *uncertainty of estimates and projections of production and costs;*
- *unforeseen title defects;*
- *risks arising from future acquisition activities;*
- *restrictions contained in the Corporation's credit facility;*
- *future threatened litigation against the Corporation;*
- *uncertainty of the outcome of the underlying claim against the Province of British Columbia filed by the BRFN and the risk of delays resulting from the need to change the location of planned activities and a potential reduction in future volumes of natural gas and natural gas liquids available for production by the Corporation;*
- *risks as to the availability and pricing of appropriate financing alternatives on acceptable terms;*
- *potential changes in income tax regulations, governmental policies, rules, practices or approval process changes, or delays, or enhancements;*
- *delays resulting from adverse weather conditions;*
- *delays resulting from an inability to obtain required regulatory approvals and ability to access sufficient debt or equity capital from internal and external sources;*
- *public health crises, such as the recent outbreak of the novel coronavirus (COVID-19) and the related economic disruption that can result in volatility in financial markets, disruption to global supply chains, and the ability to directly and indirectly staff the Corporation's day to day operations;*
- *cyber security risks, loss of information and computer systems; and*
- *the Corporation's ability to attract and retain qualified professional employees and consultants.*

Statements relating to "reserves" or "resources" are by their nature deemed to be forward-looking statements, as they involve the implied assessment based on certain estimates and assumptions that the resources and reserves described can be profitably produced in the future.

There can be no assurance that the forward-looking statements contained herein will prove to be accurate, as results and future events could differ materially from those expected or estimated in such statements. Accordingly, readers should not place undue reliance on forward-looking statements. From time to time, Painted Pony's management makes estimates and forms opinions on which the forward-looking statements are based. The Corporation assumes no obligation to update forward-looking statements if circumstances, management's estimates, or opinions change, unless prescribed by securities laws. Furthermore, readers should be aware that historical results are not necessarily indicative of future performance.

Forecast Prices and Costs

Reserves estimates are calculated using the forecast price and cost assumptions by the reserves evaluator which were in effect at the time of the applicable reserves evaluation. The complete GLJ January 1, 2020 price forecast is available on its website at gljpc.com.

Gross Reserves

Unless otherwise stated, references to "reserves" are to the Corporation's gross reserves, defined as the Corporation's working interest (operating or non-operating) share before deduction of royalties and without including any royalty interests of the Corporation.

Estimated Future Net Revenues

Estimated future net revenues are stated before deducting income taxes and are reduced for estimated future abandonment and reclamation costs and estimated capital for future development associated with the reserves. The undiscounted and discounted net present values disclosed do not represent the fair market value of the reserves.

Potential Transactions

Within its focus area, the Corporation regularly reviews potential property acquisitions, dispositions, corporate merger and acquisition opportunities and long term natural gas sales transactions for the purpose of determining whether any such potential transaction would benefit the Corporation, as well as the terms on which such a potential transaction would be available. As a result, the Corporation may from time to time be involved in discussions or negotiations with other parties or their agents in respect of potential property acquisitions, dispositions, corporate merger and acquisition opportunities, and long term natural gas sales transactions. The Corporation is not committed to any such potential transaction and cannot be reasonably confident that it can complete any such potential transaction until appropriate legal documentation has been signed by the relevant parties.

BOE Conversions

Barrel of oil equivalent amounts have been calculated by using the conversion ratio of six thousand cubic feet (6 Mcf) of natural gas to one barrel of oil (1 bbl). Boe amounts may be misleading, particularly if used in isolation. A boe conversion ratio of 6 Mcf to 1 bbl is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

MCFE Conversions

Thousands of cubic feet of gas equivalent amounts have been calculated by using the conversion ratio of one barrel of oil (1 bbl) to six thousand cubic feet (6 Mcf) of natural gas. Mcfe amounts may be misleading, particularly if used in isolation. A conversion ratio of 1 bbl to 6 Mcf is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

Abbreviations

Mcf	*thousand cubic feet*	*bbls/d*	*barrels per day*
Mcf/d	*thousand cubic feet per day*	*NGLs*	*natural gas liquids*
MMcf/d	*million cubic feet per day*	*Mcfe*	*thousand cubic feet equivalent*
boe	*barrels of oil equivalent*	*Mcfe/d*	*thousand cubic feet equivalent per day*
boe/d	*barrels of oil equivalent per day*	*MMcfe/d*	*million cubic feet equivalent per day*
Mboe	*thousand barrels of oil equivalent*	*MMBtu*	*million British thermal units*
bbls	*barrels*	*MMBtu/d*	*million British thermal units per day*

ADDITIONAL INFORMATION

Additional information regarding the Corporation and its business and operations, including its AIF for the year ended December 31, 2018 is available on the Corporation's SEDAR profile at www.sedar.com. Copies of the Corporation's disclosure can also be obtained by contacting the Corporation at Painted Pony Energy Ltd., Suite 1200, 520 – 3 Avenue SW., Calgary, Alberta T2P 0R3 (Phone (403) 475-0440), by email at info@paintedpony.ca or on the Corporation's website at www.paintedpony.ca.

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL STATEMENTS

Management of Painted Pony Energy Ltd. (the "Corporation") is responsible for the preparation and integrity of the accompanying financial statements and all other information contained in this report. The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") and include amounts that are based on management's informed judgments and estimates where necessary.

The Corporation has established internal accounting control systems which are designed to provide reasonable assurance regarding the reliability of the Corporation's financial reporting and the preparation of the financial statements together with the other financial information for external purposes in accordance with IFRS.

The Board of Directors, through its Audit & Risk Committee, monitors management's financial and accounting policies and practices and the preparation of these financial statements. The Audit & Risk Committee meets periodically with the external auditors and management to review the work of each and the propriety of the discharge of their responsibilities.

The Audit & Risk Committee reviews the financial statements of the Corporation with management and the external auditors prior to submission to the Board of Directors for final approval. The Board of Directors also reviews the financial statements before they are finalized. The Board of Directors has approved the financial statements for the years ended December 31, 2019 and 2018.

The external auditors have full and free access to the Audit & Risk Committee to discuss auditing and financial reporting matters. The Audit & Risk Committee reviews the independence of the external auditors and pre-approves audit and permitted non-audit services and fees. The Shareholders have appointed KPMG LLP as the external auditors of the Corporation, and in that capacity, they have audited the financial statements for the years ended December 31, 2019 and 2018.

"signed"
Patrick R. Ward
President and CEO

"signed"
Stuart W. Jaggard
CFO

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INDEPENDENT AUDITORS' REPORT

To the Shareholders of Painted Pony Energy Ltd.

Opinion

We have audited the financial statements of Painted Pony Energy Ltd. (the "Company"), which comprise:

- the statement of financial position as at December 31, 2019 and December 31, 2018
- the statement of operations for the years then ended
- the statement of changes in equity for the years then ended
- the statement of cash flows for the years then ended
- and notes to the financial statements, including a summary of significant accounting policies

(Hereinafter referred to as the "financial statements").

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2019 and December 31, 2018, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards ("IFRS").

Basis for Opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the "*Auditors' Responsibilities for the Audit of the Financial Statements*" section of our auditors' report.

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

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

Other Information

Management is responsible for the other information. Other information comprises:

- the information included in Management's Discussion and Analysis filed with the relevant Canadian Securities Commissions.
- the information, other than the financial statements and the auditors' report thereon, included in a document likely to be entitled "2019 Annual Report".

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

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

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

We have nothing to report in this regard.

The information, other than the financial statements and the auditors' report thereon, included in a document likely to be entitled "2019 Annual Report" is expected to be made available to us after the date of this auditors' report. If, based on the work we will perform on this other information, we conclude that there is a material misstatement of this other information, we are required to report that fact to those charged with governance.

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

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

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

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

Auditors' Responsibilities for the Audit of the Financial Statements

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

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

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

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

We also:

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

  The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the

related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.
- Provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

The engagement partner on the audit resulting in this auditors' report is Jason Stuart Brown.

KPMG LLP

Chartered Professional Accountants

Calgary, Canada
March 11, 2020

PAINTED PONY ENERGY LTD.
STATEMENT OF FINANCIAL POSITION
($000s)

As at	December 31, 2019	December 31, 2018
ASSETS		
Current assets		
Accounts receivable *(note 15)*	38,687	55,532
Prepaid expenses and deposits	1,995	2,229
Fair value of risk management contracts *(note 15)*	1,314	35,215
	41,996	92,976
Non-current assets		
Fair value of risk management contracts *(note 15)*	142	7,350
Exploration and evaluation *(note 4)*	69,269	130,348
Property, plant and equipment *(note 5)*	1,692,040	1,824,680
	1,803,447	2,055,354
LIABILITIES		
Current liabilities		
Accounts payable and accrued liabilities	46,611	51,813
Share unit liability *(note 14)*	2,151	2,063
Fair value of risk management contracts *(note 15)*	16,940	530
Current portion of finance lease obligation *(note 17)*	8,203	5,680
	73,905	60,086
Non-current liabilities		
Fair value of risk management contracts *(note 15)*	28,416	2,834
Bank debt *(note 6)*	119,901	163,140
Senior notes *(note 7)*	144,754	143,105
Convertible debentures *(note 8)*	47,466	46,113
Deferred tax *(note 11)*	—	10,904
Decommissioning obligation *(note 12)*	51,009	53,565
Finance lease obligation *(note 17)*	477,172	484,118
	942,623	963,865
EQUITY		
Share capital *(note 13)*	1,015,235	1,015,235
Equity portion of convertible debentures *(note 8)*	2,382	2,382
Contributed surplus	61,131	58,938
Retained earnings (deficit)	(217,924)	14,934
	860,824	1,091,489
	1,803,447	2,055,354

Subsequent event *(note 17)*
Commitments *(notes 17 & 18)*
Contingency *(note 21)*

See accompanying notes to the financial statements.

Approved on behalf of the Board:

"signed" Joan E. Dunne
Director

"signed" Patrick R. Ward
Director

PAINTED PONY ENERGY LTD.
STATEMENT OF OPERATIONS
($000s, except per share amounts)

	Years ended December 31,	
	2019	**2018**
Revenue		
Natural gas and natural gas liquids *(note 19)*	302,750	404,372
Royalties	(4,645)	(6,345)
	298,105	398,027
Realized gain on risk management contracts *(note 15)*	17,338	38,650
Unrealized loss on risk management contracts *(note 15)*	(83,101)	(48,608)
	232,342	388,069
Expenses (recoveries)		
Operating	57,251	72,830
Transportation	80,731	89,876
General and administrative	17,688	16,958
Share-based compensation *(notes 13 and 14)*	1,593	2,777
Exploration and evaluation *(note 4)*	242	1,716
Depletion and depreciation *(note 5)*	84,072	107,513
Impairment of property, plant and equipment *(note 5)*	150,000	—
Unrealized foreign exchange gain *(note 2)*	(2,905)	—
	388,672	291,670
(Loss) income from operations	(156,330)	96,399
Finance expense *(note 10)*	87,432	86,203
(Loss) income before income taxes	(243,762)	10,196
Deferred income tax recovery (expense) *(note 11)*	10,904	(3,132)
Net (loss) income and comprehensive (loss) income	**(232,858)**	**7,064**
Net (loss) income and comprehensive (loss) income per share:		
Basic and diluted *(note 9)*	$(1.45)	$0.04

See accompanying notes to the financial statements.

PAINTED PONY ENERGY LTD.
STATEMENT OF CHANGES IN EQUITY
($000s, except shares)

Yeas ended December 31, 2019 and 2018	Number of Common Shares	Share capital	Equity portion of convertible debentures	Contributed surplus	Retained earnings / (deficit)	Total equity
Balance at December 31, 2017	160,995,692	1,015,235	2,382	55,203	7,870	1,080,690
Share-based compensation	—	—	—	3,735	—	3,735
Net income and comprehensive income	—	—	—	—	7,064	7,064
Balance at December 31, 2018	160,995,692	1,015,235	2,382	58,938	14,934	1,091,489
Share-based compensation	—	—	—	2,193	—	2,193
Net loss and comprehensive loss	—	—	—	—	(232,858)	(232,858)
Balance at December 31, 2019	160,995,692	1,015,235	2,382	61,131	(217,924)	860,824

See accompanying notes to the financial statements.

PAINTED PONY ENERGY LTD.
STATEMENT OF CASH FLOWS
($000s)

	Years ended December 31,	
	2019	**2018**
Cash flows from (used in) operating activities:		
Net (loss) income and comprehensive (loss) income	(232,858)	7,064
Adjustments for:		
Depletion and depreciation	84,072	107,513
Impairment of property, plant and equipment	150,000	—
Exploration and evaluation	242	1,716
Share-based compensation	1,781	2,757
Accretion expense	3,876	3,849
Unrealized foreign exchange (gain) loss	(2,905)	—
Deferred income tax (recovery) expense	(10,904)	3,132
Unrealized loss on risk management contracts	83,101	48,608
Changes in non-cash working capital *(note 20)*	12,149	(5,604)
	88,554	169,035
Cash flows from (used in) investing activities:		
Proceeds on sale of exploration and evaluation assets	45,000	—
Property, plant and equipment additions	(87,262)	(154,360)
Changes in non-cash working capital *(note 20)*	2,380	(22,513)
	(39,882)	(176,873)
Cash flows from (used in) financing activities:		
Increase in (repayment of) bank debt	(43,239)	12,824
Repayment of finance lease obligation	(5,774)	(1,062)
Changes in non-cash working capital *(note 20)*	341	(3,924)
	(48,672)	7,838
Change in cash and cash equivalents	—	—
Cash and cash equivalents, beginning of year	—	—
Cash and cash equivalents, end of year	—	—

See accompanying notes to the financial statements.

1. REPORTING ENTITY

Painted Pony Energy Ltd.'s ("Painted Pony" or the "Corporation") principal business activity is the development and production of natural gas and natural gas liquids resources in western Canada. The financial statements of the Corporation as at and for the years ended December 31, 2019 and 2018 include the accounts of the Corporation. The Corporation's head office is located at 1200, 520 - 3 Avenue S.W., Calgary, Alberta.

2. BASIS OF PRESENTATION

The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). The financial statements were authorized for issuance by the Board of Directors of the Corporation (the "Board") on March 11, 2020.

The financial statements have been prepared on the historical cost basis except for risk management contracts and share and cash settled awards, which are measured at fair value. The methods used to measure fair value are discussed in note 16. Certain prior year amounts have been reclassified for consistency with the current year presentation. These reclassifications had no effect on the reported results of operations.

These financial statements are presented in Canadian dollars, which is the Corporation's functional currency.

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 of assets, liabilities, revenue and expenses. Actual results may differ materially from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis, with revisions to accounting estimates recognized in the period in which the estimates are revised and in any applicable future periods.

(a) Critical Accounting Judgments

The following are critical judgments that management has made in the process of applying accounting policies and that have the most significant effect on the amounts recognized in the financial statements.

Cash-Generating Units

The Corporation's assets are aggregated into cash-generating units ("CGU" or "CGUs") for the purpose of assessing impairment. CGUs are based on an assessment of the units ability to generate independent cash inflows. The determination of these CGUs was based on management's judgment in regard to shared infrastructure, geographical proximity, petroleum type and exposure to market risk and materiality. By their nature, these assumptions are subject to management's judgment and may impact the carrying value of the Corporation's net assets in future periods.

Impairment Indicators

Judgments are required to assess when impairment indicators exist and impairment testing is required. The Corporation is required to consider information from both external sources (such as negative downturn in commodity prices, significant adverse changes in the technological, market, economic or legal environment in which the entity operates) and internal sources (such as downward revisions in reserves, significant adverse effect on the financial and operational performance of a CGU, evidence of obsolescence or physical damage to the asset). In determining the recoverable amount of assets, in the absence of quoted market prices, impairment tests are based on estimates of reserves, production rates, future natural gas and natural gas liquids prices, future costs, discount rates, market value of land and other relevant assumptions.

The application of the Corporation's accounting policy for exploration and evaluation ("E&E") assets requires management to make certain judgments as to future events and circumstances as to whether economic quantities of reserves have been found.

Deferred Taxes

In determining its deferred tax provisions, the Corporation must apply judgment when interpreting and applying tax laws and regulations. The determination of the appropriate rules may be uncertain for many periods. The final outcome could result in amounts different from those initially recorded and could impact tax expense in the periods where a determination is made. Judgments are also made by management to determine the likelihood of whether deferred tax assets at the end of the reporting period will be realized from future taxable income.

(b) Critical Accounting Estimates

The following are key estimates made by management affecting the measurement of balances and transactions in these financial statements.

Impact of Reserves

Estimation of recoverable quantities of proved and probable reserves includes estimates regarding future commodity prices, exchange rates, discount rates and production and transportation expenses for future cash flows as well as the interpretation of complex geological and geophysical models and data. Changes in expected future cash flows in reported reserves can affect the impairment of assets, the decommissioning obligation, the economic feasibility of E&E assets and the amounts reported for depletion and depreciation of property, plant and equipment ("PP&E"), and the recognition of deferred tax assets. These reserve estimates are prepared in accordance with the Canadian Oil and Gas Evaluation Handbook and are verified by independent qualified reserve evaluators, who work with information provided by the Corporation to establish reserve determinations in accordance with National Instrument 51-101 - *Standards of Disclosure for Oil and Gas Activities* ("NI 51-101").

In a business combination, management makes estimates of the fair value of assets acquired and liabilities assumed which includes assessing the value of natural gas and natural gas liquids properties based upon the estimation of recoverable quantities of proved and probable reserves being acquired.

Share-Based Compensation

All equity-settled, share-based awards issued by the Corporation are fair valued using the Black-Scholes option-pricing model. In assessing the fair value of equity-based compensation, estimates are made regarding the expected volatility in share price, option life, dividend yield, risk-free rate and estimated forfeitures at the initial grant date.

Derivative Financial Instruments

Painted Pony records risk management contracts at fair value with changes in fair value recognized in the statements of operations. The Corporation's estimate of the fair value is determined using observable market data and external counterparty information, including estimated forward prices and volatility in those prices.

Decommissioning Obligation

The Corporation estimates future remediation costs of production facilities, wells and pipelines at different stages of development and construction of assets or facilities. In most instances, removal of assets occurs many years into the future. This requires estimates regarding abandonment date, future environmental and regulatory legislation, the extent of reclamation activities, the engineering methodology for estimating cost, future removal technologies in determining the removal cost and liability-specific discount rates to determine the present value of these cash flows.

Deferred Taxes

Tax provisions are based on enacted or substantively enacted laws. Changes in those laws could affect amounts recognized in the statement of operations both in the period of change, which would include any impact on cumulative provisions, and in future periods.

Deferred tax assets are recognized only to the extent it is considered probable that those assets will be recoverable. This involves an assessment of when those deferred tax assets are likely to reverse and a judgment as to whether or not there will be sufficient taxable income available to offset the tax assets when they do reverse. This requires assumptions regarding future profitability and is therefore inherently uncertain. Estimates of future taxable income are based on forecasted cash flows from operations.

Leased Assets

The incremental borrowing rates are based on judgments including economic environment, term, currency, and the underlying risk inherent to the asset. The carrying balance of the right-of-use assets, lease obligations, and the resulting interest and depletion and depreciation expense, may differ due to changes in the market conditions and lease term. Lease terms are based on assumptions regarding extension terms that allow for operational flexibility and future market conditions.

3. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to all years presented in these financial statements by the Corporation.

(a) Basis of Consolidation

Subsidiaries
Subsidiaries are entities controlled by the Corporation. Control exists when the Corporation 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.

Business Combinations
The purchase 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. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The excess of the cost of acquisition over the fair value of the identifiable assets, liabilities and contingent liabilities acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized immediately in the consolidated statement of operations.

Jointly Controlled Operations and Jointly Controlled Assets

A portion of the Corporation’s natural gas and natural gas liquids activities involve jointly controlled assets. The financial statements include the Corporation’s share of these jointly controlled assets and a proportionate share of the relevant revenue and related costs.

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) Financial Instruments

Classification and Measurement of Financial Instruments

Financial assets and financial liabilities are classified into three categories: Amortized Cost, Fair Value through Other Comprehensive Income (“FVTOCI”) and Fair Value through Profit and Loss (“FVTPL”). The classification of financial assets is determined by their context in the Corporation’s business model and by the characteristics of the financial asset’s contractual cash flows.

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

(i) Amortized Cost
Accounts receivable, prepaid expenses and deposits, accounts payable and accrued liabilities, bank debt, senior notes and debt portion of convertible debentures are measured at amortized cost. The contractual cash flows received from the financial assets are solely payments of principal and interest and are held within a business model whose objective is to collect the contractual cash flows. The financial assets and financial liabilities are subsequently measured at amortized cost using the effective interest method.

(ii) Fair Value Through Income and Loss
Risk management contracts, deferred share units (“DSUs”), preferred share units (“PSUs”) and restricted share units (“RSUs”), all of which are derivatives, are measured initially at FVTPL and are subsequently measured at fair value with changes in fair value immediately charged to the statements of operations.

(iii) Fair Value Through Other Comprehensive Income
As at December 31, 2019, the Corporation does not have any financial instruments measured at FVTOCI.

Compound Financial Instruments
The Corporation’s compound financial instruments are comprised of its convertible debentures that can be converted into common shares in the capital of the Corporation (“Common Share” or “Common Shares”) at the option of the

holder. The liability component of the convertible debentures is recognized initially at fair value of a similar liability that does not have an equity conversion option. The equity component is recognized initially as the difference between the fair value of the convertible debenture and the fair value of the liability component. Any directly attributable transaction costs are allocated to the liability and equity components in proportion to their initial carrying values. Subsequent to initial recognition the liability component of the convertible debentures is measured at amortized cost using the effective interest rate method. The equity component of the convertible debentures is not re-measured subsequent to initial recognition.

Derivative Financial Instruments
The Corporation has entered into certain financial risk management contracts in order to manage the exposure to market risks from fluctuations in commodity prices and foreign currency. These instruments are not used for trading or speculative purposes. The Corporation has not designated its financial risk management contracts as effective accounting hedges and, therefore, has not applied hedge accounting, even though the Corporation considers all risk management contracts to be economic hedges. As a result, all financial risk management contracts are classified as FVTPL and are recorded on the statement of financial position at fair value. Transaction costs are recognized in the statement of operations when incurred.

Impairment of Financial Assets
Impairment of financial assets is determined by measuring the assets' expected credit loss ("ECL"). Accounts receivable are due within one year or less; therefore, these financial assets are not considered to have a significant financing component and a lifetime ECL is measured at the date of initial recognition of the accounts receivable. ECL allowances have not been recognized for cash and cash equivalents due to the virtual certainty associated with their collection.

The ECL pertaining to accounts receivable is assessed at initial recognition and this provision is re-assessed at each reporting date. ECLs are a probability-weighted estimate of all possible default events related to the financial asset (over the lifetime or within 12 months after the reporting period, as applicable) and are measured as the difference between the present value of the cash flows due to the Corporation and the cash flows the Corporation expects to receive, including cash flows expected from collateral and other credit enhancements that are a part of contractual terms. In making an assessment as to whether financial assets are credit-impaired, the Corporation considers historically realized bad debts, evidence of a debtor's present financial condition and whether a debtor has breached certain contracts, the probability that a debtor will enter bankruptcy or other financial reorganization, changes in economic conditions that correlate to increased levels of default, the number of days a debtor is past due in making a contractual payment, and the term to maturity of the specified receivable. The carrying amounts of financial assets are reduced by the amount of the ECL through an allowance account and losses are recognized within general and administrative ("G&A") expense in the statement of operations.

(c) Exploration and Evaluation Assets and Property, Plant and Equipment

Recognition and Measurement

(i) *Exploration and evaluation assets*

Pre-license costs are expensed as incurred. E&E costs, including the costs of acquiring licenses, seismic, exploration drilling and directly attributable general and administrative costs initially are capitalized as E&E assets according to the nature of the assets acquired. The costs are accumulated in cost centers pending determination of technical feasibility and commercial viability.

The technical feasibility and commercial viability of extracting a mineral resource is considered to be determinable when proved or probable reserves are determined to exist. A review is carried out, on a quarterly basis, to ascertain whether proved or probable reserves have been discovered. Upon determination of proved or probable reserves, E&E assets attributable to those reserves are first tested for impairment and then reclassified from E&E assets to PP&E.

Exploration and evaluation asset dispositions are recorded based on transaction proceeds. For exchanges or parts of exchanges that involve only exploration and evaluation assets, the exchange is accounted for at carrying value of the asset given up, and no gain or loss is recognized.

(ii) *Property, plant and equipment*

Items of PP&E, which include natural gas and natural gas liquids development and production assets, and finance lease assets, are measured at cost less accumulated depletion, depreciation and accumulated impairment losses. Development and production assets are grouped into CGUs for impairment testing. When significant parts of an item of PP&E, including natural gas and natural gas liquids interests, have different useful lives, they are accounted for as separate items.

Gains and losses on disposal of PP&E, are determined by comparing the proceeds from disposal, or fair value of properties received, with the carrying amount of the asset and are recognized in the statement of operations.

Costs incurred subsequent to the determination of technical feasibility and commercial viability and the costs of replacing parts of PP&E are recognized as natural gas and natural gas liquids interests only when they increase the future economic benefits embodied in the specific assets to which they relate. All other expenditures are recognized in the statement of operations as incurred. Such capitalized natural gas and natural gas liquids interests generally represent costs incurred in developing proved and/or probable reserves and bringing on or enhancing production from such reserves. The carrying amount of any replaced or sold component is derecognized. The costs of periodic servicing of PP&E are recognized in the statement of operations.

Depletion and Depreciation

The net carrying value of development or production assets and finance lease assets are 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 costs necessary to bring those reserves into production. Future development costs are estimated taking into account the level of development required to produce the reserves. These estimates are reviewed by independent reserve engineers on an annual basis, at a minimum.

Proved and probable reserves are estimated using independent reserve engineer reports in accordance with NI 51-101 and represent the estimated quantities of 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. There should be a 50 percent statistical probability that the actual quantity of recoverable reserves will be more than the amount estimated as proved and probable and a 50 percent statistical probability that it will be less. The equivalent statistical probabilities for proved reserve components are 90 percent and 10 percent, respectively.

Such reserves may be considered commercially producible if management has the intention of developing and producing them and such intention is based upon:

- a reasonable assessment of the future economics of such production;
- a reasonable expectation that there is a market for all or substantially all the expected natural gas and natural gas liquids production; and
- evidence that the necessary production, transmission and transportation facilities are available or can be made available.

In determining reserves for use in the depletion and impairment calculations, a barrel of oil equivalent (“boe”) conversion ratio of six thousand cubic feet of gas (“Mcf”) to one barrel of oil (“bbl”) (6 Mcf:1 bbl) is used as an energy equivalency conversion method.

For other assets, depreciation is recognized in the statement of operations on a declining-balance rate of 20% based on their estimated useful lives. E&E assets are not depreciated.

Impairment

Non-financial Assets

The carrying amounts of the Corporation’s non-financial assets, other than E&E assets and deferred tax assets, are reviewed whenever there is an indication of impairment. If any such indication exists, the asset’s recoverable amount is estimated.

For the purpose of impairment testing, assets are grouped together into CGUs, being the smallest group of assets that generate cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets. The recoverable amount of an asset or a CGU is the greater of its value in use and its fair value less costs of disposal.

Fair value less costs of disposal is derived by estimating the discounted after-tax future net cash flows from proved plus probable oil and gas reserves, adjusted for the discounted abandonment and reclamation costs on proved plus probable undeveloped oil and gas reserves. Discounted future net cash flows are based on forecasted commodity prices and costs over the expected economic life of the reserves and discounted using market-based rates to reflect a market participant’s view of the risks associated with the assets. Value in use is assessed using the expected future cash flows from proved plus probable oil and gas reserves discounted at a pre-tax rate, adjusted for the discounted abandonment and reclamation costs associated with wells without reserves and facilities that relate to the CGUs.

E&E assets are assessed for impairment if: (i) sufficient data exists to determine technical feasibility and commercial viability, or (ii) facts and circumstances suggest that the carrying amount exceeds the recoverable amount.

An impairment loss is recognized if the carrying amount of an asset or its CGU exceeds its estimated recoverable amount. Impairment losses are recognized in the statement of operations. For purposes of impairment testing, E&E assets are combined with cash-generating units.

Impairment losses 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, if no impairment loss had been recognized.

(d) Leased Assets

The Corporation recognizes a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of costs to dismantle and remove the underlying asset or to restore the underlying asset or the site on which it is located, less any lease incentives received.

The right-of-use asset is subsequently depleted from the commencement date to the earlier of the end of useful life of the right-of-use assets or the end of the lease term. The estimated useful lives of right-of-use assets are determined on the same basis as those of PP&E. In addition, the right-of-use asset is reduced by impairment losses, if any, and adjusted for certain re-measurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease, or if that rate cannot be readily determined, the Corporation's incremental borrowing rate. Generally, the Corporation uses its incremental borrowing rate as the discount rate.

The lease liability is subsequently measured at amortized cost using the effective interest method. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, if there are any contract modifications, if there is a change in the Corporation's estimate of the amount expected to be payable under a residual value guarantee, or if the Corporation changes its assessment of whether it will exercise a purchase, extension or termination option. When the lease liability is remeasured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use assets, or is recorded in the statement of operations if the carrying amounts of the right-of-use asset has been reduced to nil.

The Corporation presents right-of-use assets in "property, plant and equipment" and lease liabilities in "finance lease obligation" in the statement of financial position.

Short-term leases and leases of low value assets

The Corporation has elected not to recognize right-of-use assets and lease liabilities for short term leases that have a term of twelve months or less and leases of low value assets. The Corporation recognizes the lease payments associated with these leases as an expense when incurred, over the lease term.

(e) Share Capital

Common Shares are classified as equity. Incremental costs directly attributable to the issue of shares and stock options are recognized as a deduction from equity, net of tax.

(f) Share-Based Compensation

The Corporation has issued stock options to acquire Common Shares to executive officers and employees. Non-employee directors are not eligible for grants of stock options. The fair value of stock options on the date they are granted is recognized as share-based compensation expense with a corresponding increase in contributed surplus over the vesting period. A forfeiture rate is estimated on the grant date, and the expense is adjusted to reflect actual forfeitures throughout the vesting period. The Corporation uses the Black-Scholes model to estimate fair value.

The Corporation has issued DSUs to members of the Board and eligible executive officers. Each DSU is a notional unit equal in value to a Common Share, which entitles the holder to a cash payment upon redemption. DSUs are measured at fair value upon grant and each reporting date, using the 20-day volume weighted average price ("VWAP") average price of Common Shares. DSUs are classified as fair value through income or loss and are recorded on the statement of financial position at fair value.

The Corporation has issued PSUs to eligible executive officers. Each PSU is a notional unit equal in value to a Common Share, which entitles the holder to a cash payment upon redemption. PSUs are measured at fair value through income or loss and are recorded on the statement of financial position at fair value.

The Corporation has issued RSUs to eligible employees and executive officers. Each RSU is a notional unit equal in value to a Common Share, which entitles the holder to a cash payment on redemption. RSUs are measured at fair value through income or loss and are recorded on the statement of financial position at fair value.

A portion of share-based compensation directly attributable to the exploitation and development of the Corporation's assets is capitalized.

(g) Provisions

A provision is recognized if, as a result of a past event, the Corporation has a present legal or constructive obligation that can be estimated reliably and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax risk free rate.

Decommissioning Obligation

The Corporation's activities give rise to dismantling, decommissioning and site disturbance remediation activities. Provision is made for the estimated cost of site restoration and is capitalized in the relevant asset category.

The decommissioning obligation is measured at the present value of management's best estimate of the expenditure required to settle the present obligation at the reporting 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 underlying the obligation. The increase in the provision due to the passage of time is recognized as a finance expense whereas increases/decreases due to changes in the estimated future cash flows are capitalized. Actual costs incurred upon settlement of the decommissioning obligation are charged against the provision to the extent the provision had been established.

(h) Revenue Recognition

Revenue associated with the sale of natural gas and natural gas liquids is measured based on the consideration specified in the contract with a customer and excludes amounts collected on behalf of third parties. The Corporation recognizes revenue when it transfers control of the product or service to a customer, which is generally when the title transfers from the Corporation to the customer.

The Corporation satisfies its performance obligations in contracts with customers upon delivery of natural gas and natural gas liquids at a point in time, when title transfers to the customer.

(i) Finance Expense

Finance expense consists of interest expense and standby fees on credit facilities, costs related to the implementation of the credit facilities, accretion on the decommissioning obligation, senior notes and convertible debentures, and costs associated with the finance lease obligation.

(j) Income Tax

Income tax expense comprises current and deferred tax expense and is recognized in the statement of operations except to the extent that it relates to items recognized directly in equity.

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 likely that future taxable income 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 likely that the related tax benefit will be realized.

(k) Foreign Currency Translation

The principal currency of the economic environment in which the Corporation operates is the Canadian dollar. Monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at exchange rates in effect at the reporting period, and revenues and expenses are translated into Canadian dollars at average exchange rates. All translation gains and losses are recorded in the statement of operations.

(l) Per Share Information

Basic per share information is calculated on the basis of the weighted average number of Common Shares outstanding during the period. Diluted per share information reflects the potential dilutive effect of stock options and convertible debentures. Anti-dilutive instruments are not included in the determination of diluted income (loss) per share.

(m) Changes to Accounting Policies

Leases

Effective January 1, 2019, the Corporation adopted IFRS 16 *Leases* (“IFRS 16”) using the modified retrospective approach, and therefore the comparative information has not been restated and continues to be reported under IAS 17 and IFRIC 4. The impact of changes is disclosed in note 17. IFRS 16, which replaces IAS 17 “Leases”, provides a single recognition and measurement model for leases, with required recognition of assets and liabilities for most leases. For lessees, IFRS 16 removes the classification of leases as either operating or finance leases, effectively treating all leases as finance leases. Certain short-term leases (less than 12 months) and leases of low value assets are exempt from the requirements, and may continue to be treated as operating leases.

On transition to IFRS 16, the Corporation elected to apply the practical expedient to retain the assessment of which transactions are leases. IFRS 16 was applied only to contracts that were previously identified as leases. Contracts that were not identified as leases under IAS 17 and IFRIC 4 were not reassessed for whether there is a lease. Therefore, the definition of a lease under IFRS 16 was applied only to contracts entered into or changed after January 1, 2019.

(n) Future Accounting Pronouncements

Business Combinations

On October 22, 2018, the IASB issued amendments to the guidance in IFRS 3 - *Business Combinations* (“IFRS 3”), revising the definition of a business and providing for the addition of an optional 'concentration test' to determine if the acquisition is a business. To be considered a business under the amendments to IFRS 3, an acquisition would have to include an input and a substantive process that together significantly contribute to the ability to create outputs. The three elements of a business are defined as follows:

- Input - Any economic resource that creates outputs, or has the ability to contribute to the creation of outputs, when one or more processes are applied to it.
- Process - Any system, standard, protocol, convention or rule that, when applied to an input or inputs, creates outputs or has the ability to contribute to the creation of outputs.
- Output - The result of inputs and processes applied to those inputs that provide goods or services to customers, generate investment income or generate other income from ordinary activities.

The optional 'concentration test' permits a simplified assessment that results in an asset acquisition if substantially all of the fair value of the gross assets is concentrated in a single identifiable asset or a group of similar identifiable assets. An entity may elect to apply, or not apply, the test. An entity may make such an election separately for each transaction or other event. If the concentration test is met, the sets of activities and assets is determined not to be a business and no further assessment is needed.

The amendments to IFRS 3 apply to businesses acquired in annual reporting periods beginning on or after January 1, 2020, with early adoption permitted. The Corporation has chosen to adopt the amendments to IFRS 3 effective January 1, 2020.

4. EXPLORATION AND EVALUATION ASSETS

($000s)	
As at December 31, 2017	159,004
Transfer to property, plant and equipment	(26,940)
Expensed	(1,716)
As at December 31, 2018	130,348
Transfer to property, plant and equipment	(15,837)
Disposition proceeds	(45,000)
Expensed	(242)
As at December 31, 2019	69,269

E&E assets consist of undeveloped lands and unevaluated seismic data on the Corporation's exploration projects which are pending the determination of proved or probable reserves. Additions represent the Corporation's share of costs incurred on E&E assets during the period. Transfers are made to PP&E as proved or probable reserves are determined and as ongoing wells are drilled within the Corporation's CGU. The Corporation assesses the recoverability of E&E assets on the transfer to PP&E.

E&E assets were expensed in 2019 and 2018 due to lease expires. During the year ended December 31, 2019, the Corporation disposed of a 75% working interest in undeveloped lands for cash proceeds of $45 million.

As at December 31, 2019, the Corporation determined that indicators of impairment existed with respect to its E&E assets largely as a result of changes in future development plans as a result of the decline in forward commodity benchmark prices and as such an impairment test was performed. It was determined that the recoverable amount of the Corporation's E&E assets exceeded the carrying value and, as such, no impairment was recorded. Further, there was no impairment recorded as a result of the mandatory impairment assessment on the transfer of exploration and evaluation assets to property, plant and equipment.

5. PROPERTY, PLANT & EQUIPMENT

($000s)	
Cost:	
As at December 31, 2017	2,048,067
Capital expenditures	154,360
Non-cash additions	6,601
Write off of office assets and leasehold improvements	(2,313)
Transfer from exploration and evaluation	26,940
As at December 31, 2018	2,233,655
Adoption of IFRS 16 *(note 17)*	1,351
Capital expenditures	87,262
Non-cash changes	(3,018)
Transfer from exploration and evaluation	15,837
As at December 31, 2019	2,335,087

Accumulated depletion and depreciation:	
As at December 31, 2017	303,775
Write off of office assets and leasehold improvements	(2,313)
Depletion and depreciation	107,513
As at December 31, 2018	408,975
Depletion and depreciation	84,072
Impairment	150,000
As at December 31, 2019	643,047

Carrying amounts:	
December 31, 2018	1,824,680
December 31, 2019	1,692,040

Estimated future development costs associated with the development of the Corporation's proved plus probable reserves were $3.3 billion at December 31, 2019 (December 31, 2018 - $3.5 billion).

Impairment

During the fourth quarter of 2019, the Corporation identified indicators of impairment on its sole CGU, as a result of declines in the forecasted commodity prices utilized in the 2019 reserve report, compared to the prior year, and a market capitalization deficiency relative to the book value of the Corporation's shareholders equity. As a result, the Corporation completed an impairment test. The recoverable value was estimated using the value in use based on before tax discounted cash flows from natural gas and natural gas liquids proved plus probable reserves estimated by the Corporation's third-party reserve evaluators. It was determined that the carrying value of the CGU exceeded the recoverable amount and an impairment of $150.0 million was recognized. The before tax discount rates applied in the value in use calculation as at December 31, 2019 ranged between 10% - 30% depending on reserve category.

The following table outlines forecasted commodity prices and exchange rates used in the Corporation's impairment test at December 31, 2019. These future prices were based on the forecasted commodity prices used by the external reserve evaluators, adjusted for commodity price differentials and transportation specific to the Corporation's production. The reserve evaluators also include financial assumptions regarding royalty rates, operating costs, and future development capital that can significantly impact the recoverable amount which are assigned based on historic rates and future anticipated activities of the Corporation.

Year	Exchange Rate	Natural Gas	Condensate	NGLs
	(U.S.$/CAD$)	(CAD$/Mcf)	(CAD$/bbl)	(CAD$/bbl)
2020	0.76	2.38	78.92	33.61
2021	0.77	2.65	80.39	34.30
2022	0.78	2.77	84.51	35.58
2023	0.78	2.88	87.73	36.76
2024	0.78	2.95	90.32	37.89
2025	0.78	3.15	92.89	39.26
2026	0.78	3.22	95.48	40.49
2027	0.78	3.27	97.83	41.52
2028	0.78	3.34	99.80	42.33
2029	0.78	3.40	101.82	43.14
Remaining	0.78	4.37	130.76	53.33

As at December 31, 2018, indicators of impairment were determined to exist in the Corporation's CGU, as a result of a sustained decline in forward commodity benchmark prices for natural gas and natural gas liquids. An impairment test was carried out and the recoverable amounts were determined to exceed the carrying value. No impairment charge was recorded at December 31, 2018.

Certain facilities and related pipeline infrastructure, and the Corporation's office leases are included in PP&E as right-of-use assets.

($000s)	**Processing facility and pipeline infrastructure**	**Office leases**	**Total**
As at December 31, 2018	471,942	—	471,942
Adoption of IFRS 16 *(note 17)*	—	1,351	1,351
Depletion / depreciation	(7,372)	(313)	(7,685)
As at December 31, 2019	464,570	1,038	465,608

Capitalized General and Administrative Expense, Recoveries and Share-Based Compensation

($000s)	**Years ended December 31,**	
	2019	**2018**
General and administrative and unit awards	5,621	6,923
Capital recoveries	925	1,735
Share-based compensation	412	978
Total	6,958	9,636

6. BANK DEBT

As at December 31, 2019, the Corporation's syndicated credit facilities consisted of available credit facilities of $375 million. The available facilities are provided by a syndicate of financial institutions, and include a $325 million extendable revolving facility and a $50 million operating facility. The facilities revolve for a two-year period, which is extendable annually, subject to syndicate approval. The current maturity date is May 11, 2021. The facilities are subject to semi-annual review and re-determination of borrowing base by April 30 and October 31 of each year, or in the circumstance of a material adverse change. Any re-determination of the borrowing base is effective immediately, and if the borrowing base is reduced, the Corporation has 60 days to repay any shortfall. In addition, the Corporation has a $22 million unsecured letter of credit facility backstopped by Export Development Canada ("EDC").

The credit facilities bear interest on a matrix system that ranges from the bank's prime rate plus 0.5% to the bank's prime rate plus 2.5% per annum depending on the Corporation's senior debt to EBITDA ratio, calculated on a trailing four fiscal quarter basis as defined by the lenders, ranging from less than 0.50:1 to greater than 3.00:1. This ratio is calculated as senior debt, defined as outstanding loans and borrowings plus or minus working capital, excluding the fair value of risk management contracts, less the principal amount of the Corporation's unsecured notes and convertible debentures; divided by the trailing four fiscal quarter EBITDA, defined as net income (loss) plus finance expense excluding the costs associated with the finance lease obligation, plus income taxes and adjustments for earnings or losses attributable to extraordinary and non-recurring gains or losses, as well as adjustments for any non-cash items including depreciation, depletion, amortization, deferred income taxes and non-cash gains or losses resulting from marking-to-market the outstanding risk management contracts.

The credit facilities provide that advances may be made by way of prime rate loans, U.S. Base Rate loans, LIBOR loans, bankers' acceptances, letters of credit or letters of guarantee. A standby fee of 0.3375% to 0.7875% per annum is charged on the undrawn portion of the credit facilities, also calculated depending on the Corporation's senior debt to EBITDA ratio, calculated on a four fiscal quarter basis, which was 2.00:1.00 at December 31, 2019.

As at December 31, 2019, Painted Pony had USD $98.6 million (CAD $128.1 million) in LIBOR loans outstanding, with an effective interest rate of 3.785% per annum. In addition, as at December 31, 2019, the Corporation had outstanding letters of credit totaling CAD $34.6 million and USD $15.0 million (CAD $19.5 million), which reduce the credit available on the syndicated facilities, as well as outstanding letters of credit totaling CAD $21.5 million, which are backstopped by EDC.

Security over all of the Corporation's assets is provided by a floating charge demand debenture in the aggregate amount of $1.0 billion. The Corporation has provided a negative pledge and an undertaking to provide fixed charges over its natural gas and natural gas liquids reserves in certain circumstances. The syndicated facilities are not subject to financial covenants.

7. SENIOR NOTES

On August 23, 2017, the Corporation issued $150.0 million of 8.5% senior unsecured notes (the "Notes") with a five year term by way of private placement. Proceeds net of discount and transaction costs of $8.9 million amounted to $141.1 million. Interest is payable in equal quarterly installments in arrears. The Notes are fully and unconditionally guaranteed as to the payment of principal and interest, on a senior unsecured basis by the Corporation. There are no maintenance financial covenants.

The Notes are non-callable by the Corporation prior to the three year anniversary. If the Corporation chooses to redeem the Notes prior to August 23, 2020, they will be subject to a make-whole premium equal to the Canada Yield Price, plus accrued and unpaid interest. At any time on or after August 23, 2020, the Corporation can redeem all or part of the Notes at the redemption prices set forth in the table below plus any accrued and unpaid interest.

Redemption Schedule	Percentage
August 23, 2020 - August 22, 2021	104.250 %
August 23, 2021 - February 22, 2022	102.125 %
February 23, 2022 - August 23, 2022	100.000 %

If a change of control event occurs at any time before maturity, the Corporation must offer to repurchase the Notes at a price according to the redemption schedule above.

The Notes were recorded at their fair value on the date of issuance of $141.1 million. Accretion of the liability is included in finance expense in the statement of operations. At December 31, 2019 the carrying value of the Notes was $144.8 million (December 31, 2018 - $143.1 million). Accretion expense of $1.6 million was recorded in the statement of operations for the year ended December 31, 2019 (for the year ended December 31, 2018 - $1.5 million).

8. CONVERTIBLE DEBENTURES

($000s)	Liability component	Equity component
As at December 31, 2017	44,887	2,382
Accretion of discount	1,226	—
As at December 31, 2018	46,113	2,382
Accretion of discount	1,353	—
As at December 31, 2019	47,466	2,382

On August 23, 2017, the Corporation issued $50.0 million of convertible unsecured subordinated debentures (the "Debentures") for net proceeds of $47.7 million. The Debentures mature on August 23, 2021 and bear interest at 6.5% per annum payable quarterly. At the holder's option, the Debentures may be converted into Common Shares of the Corporation at any time prior to the close of business on the date of maturity at a conversion price of $5.60 per share (the "conversion price").

The Debentures were non-redeemable by the Corporation until February 22, 2020 other than pursuant to the 90% redemption right (see change of control below). The Debentures are redeemable by the Corporation between February 23, 2020 and August 23, 2021 at a redemption price equal to the principal amount plus interest. Redemption may be satisfied in Common Shares if the 30-day VWAP on notice date and the closing price immediately prior to notice date are both greater than 140% of the conversion price.

On maturity, the Corporation may satisfy its obligation to Debenture holders by issuing Common Shares if the Corporation's market capitalization exceeds $750 million. The number of Common Shares issued is calculated based on 95% of the lesser of the 30-day VWAP and the 2-day VWAP on the date of maturity.

Upon occurrence of a change of control event, the Corporation must offer to repurchase the Debentures at a price according to the schedule below. If 90% or more of the principal amount accept the offer, the Corporation shall have the right to repurchase 100% of the Debentures outstanding.

Redemption Schedule	Percentage of Principal
January 1, 2020 - February 22, 2020	105.000 %
February 23, 2020 - August 23, 2021	100.000 %

The liability component of the Debentures was recognized initially at the fair value of a similar liability that does not have an equity conversion option, which was calculated based on a market interest rate of 8.5%. The difference between the $50.0 million principal amount of the Debentures and the fair value of the liability component was recognized in shareholder's equity, net of deferred taxes. Total transaction costs directly attributable to the offering of $2.3 million were allocated to the liability and equity components of the Debentures proportionately.

Accretion of the liability component and accrued interest payable on the Debentures are included in accretion and financing expense respectively, in the statement of operations.

9. NET (LOSS) INCOME AND COMPREHENSIVE (LOSS) INCOME PER SHARE

	Years ended December 31,	
	2019	**2018**
Net (loss) income and comprehensive (loss) income - basic and diluted *($000's)*	(232,858)	7,064
Weighted average Common Shares - basic and diluted	160,995,692	160,995,692
Net (loss) income and comprehensive (loss) income per share - basic and diluted ($/share)	(1.45)	0.04

The average market value of the Common Shares of the Corporation for purposes of determining the dilutive effect of outstanding stock options was based on quoted market prices for the period. For the year ended December 31, 2019, there were 9,212,075 stock options excluded from the weighted-average diluted share calculation of Common Shares as they were anti-dilutive (December 31, 2018 - 8,925,075).

For the years ended December 31, 2019 and 2018, there were 8,928,571 potential Common Shares related to the conversion of the convertible debentures that were excluded from the weighted-average diluted share calculation, as they were anti-dilutive.

10. FINANCE EXPENSE

($000s)	Years ended December 31,	
	2019	**2018**
Finance lease expense *(note 17)*	58,153	56,927
Interest expense	25,403	25,427
Accretion	3,876	3,849
Total	87,432	86,203

Finance lease expense is related to the right-of-use assets included in PP&E under IFRS 16. Interest expense includes interest on bank debt, standby charges on the Corporation’s syndicated credit facilities and letter of credit fees, as well as interest on the senior notes and convertible debentures. Accretion expense consists of accretion on the decommissioning obligation, senior notes and convertible debentures.

11. DEFERRED TAX

Reconciliation of effective tax rate:

($000s)	Years ended December 31,	
	2019	**2018**
(Loss) income before income taxes	(243,762)	10,196
Combined corporate tax rate	26.61 %	27.00 %
Expected tax reduction	(64,865)	2,753
Unrecognized deferred tax asset	47,535	—
Non-deductible expenses	140	139
Non-deductible share-based compensation	474	613
Change in statutory rates	5,323	(354)
Other	489	(19)
Deferred income tax (recovery) expense	(10,904)	3,132

During May 2019, the Government of Alberta tabled legislation to decrease the general corporate tax rate from 12% to 8% which will be phased in between July 1, 2019, and January 1, 2022. As these corporate income tax measures were included in Alberta Bill 3 they were considered substantively enacted under IFRS in the calculation of the Corporation's deferred tax liabilities starting in the second quarter of 2019. As a result of the reduction in the corporate provincial tax rate, the Corporation analyzed the expected timing of settlement of the taxable temporary differences which give rise to deferred income tax assets and liabilities and re-measured these amounts using the appropriate, newly enacted corporate provincial income tax rates.

Deferred tax assets and liabilities are attributable to the following:

($000s)	December 31, 2019	December 31, 2018
Deferred tax liabilities:		
PP&E and E&E assets	(67,315)	(119,783)
Fair value of risk management contracts	—	(10,584)
Senior notes	(178)	(646)
Convertible debentures	—	(134)
Other	(259)	—
	(67,752)	(131,147)
Deferred tax assets:		
Non-capital losses	43,667	103,312
Fair value of risk management contracts	10,475	—
Decommissioning obligation	12,171	14,462
Finance costs	1,234	2,241
Convertible debentures	205	—
Other	—	228
Net deferred tax liability	—	(10,904)

As at December 31, 2019, the Corporation did not recognize a deferred tax asset in respect of $200.1 million of non-capital losses. The Corporation has non-capital losses of $382.2 million which expire in the years 2026 through 2035. Total tax pools available for deduction against future income at December 31, 2019 and 2018 were $1.4 billion.

12. DECOMMISSIONING OBLIGATION

($000s)	December 31, 2019	December 31, 2018
Balance, beginning of year	53,565	46,811
Provisions	2,212	4,451
Revisions and other	(5,642)	1,172
Accretion	874	1,131
Balance, end of year	51,009	53,565

The Corporation's decommissioning obligation results from its ownership interest in natural gas and natural gas liquids assets including well sites and facilities. The total decommissioning obligation is estimated based on the Corporation's net ownership interest in all wells and facilities, estimated costs to reclaim and abandon these wells and facilities and the estimated timing of the costs to be incurred in future years.

A change in estimate of the decommissioning obligation of $5.6 million resulted from using a discount factor, being the nominal interest rate related to the liability of 1.76%, and a market inflation rate of 1.35% at December 31, 2019. The discount factor, being the risk-free rate related to the liability was 2.2%, and the consumer price index inflation rate was 2% at December 31, 2018. Due to this change in the risk-free rate and inflation rate, the Corporation has estimated the net present value of the decommissioning obligation based on an undiscounted total future liability of $96.3 million at December 31, 2019, compared to $116.3 million at December 31, 2018, with payments expected to be made over the next 10 to 47 years. The impact of this change in estimate on future periods is impractical to determine.

13. SHARE CAPITAL

(a) Authorized

The Corporation has an unlimited number of common shares ("Common Shares") and an unlimited number of preferred shares ("Preferred Shares") authorized for issuance. At December 31, 2019 and December 31, 2018 there were 160,995,692 Common Shares outstanding. At December 31, 2019 and December 31, 2018 there were no Preferred Shares outstanding.

The Common Shares entitle the holder thereof to one vote for every share held. There are no fixed dividends payable on the Common Shares. In the event of the liquidation or dissolution of the Corporation, the Common Shares are entitled to receive, on a pro rata basis, all assets of the Corporation as are distributable to the holders of shares.

(b) Stock options

The Corporation has a stock option plan (the "Stock Option Plan") pursuant to which options to purchase Common Shares are granted to executive officers and employees of the Corporation. Stock options are granted at the volume weighted average price of the Common Shares for the five trading days immediately preceding the date of grant, and have a five-year term. Stock options granted vest as to one-third on each of the first, second and third anniversaries of the grant date.

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

	Weighted Average Exercise Price ($)	Number
As at December 31, 2017	6.01	10,298,367
Granted	2.65	2,042,200
Forfeited	5.02	(1,872,992)
Expired	8.10	(1,542,500)
As at December 31, 2018	5.09	8,925,075
Granted	1.25	2,182,300
Forfeited	5.04	(980,800)
Expired	10.08	(914,500)
As at December 31, 2019	3.69	9,212,075

The following table summarizes information about stock options outstanding and exercisable at December 31, 2019:

Stock Options Outstanding			Stock Options Exercisable	
Number of Stock Options	Exercise Price Range ($)	Weighted Average Remaining Life (Years)	Number of Stock Options	Weighted Average Exercise Price ($)
2,168,400	0.67 - 1.65	4.1	—	—
1,763,800	1.66 - 3.50	3.0	590,733	2.66
1,350,225	3.51 - 4.20	1.9	1,119,225	3.91
2,305,050	4.21 - 4.82	1.6	1,967,016	4.27
1,624,600	4.83 - 8.78	1.3	1,377,566	7.39
9,212,075	3.69	2.5	5,054,540	4.85

The Corporation accounts for its stock options using the fair value method. In accordance with the Stock Option Plan, stock options have an exercise price equal to the fair value of the Common Shares at the date of grant.

The weighted-average fair value of the stock options granted and the assumptions used in the Black-Scholes option pricing model were as follows:

	Years ended December 31,	
	2019	2018
Fair value per stock option ($)	0.63	1.26
Volatility (%)	58	53
Life (years)	5	5
Risk-free interest rate (%)	1.71	1.90

A forfeiture rate of 10% was used when measuring share-based compensation during the year ended December 31, 2019, compared to 9% during the year ended December 31, 2018.

The components of share-based compensation expense are presented in the table below:

($000s)	Years ended December 31,	
	2019	2018
Share-based compensation	1,781	2,757
Share unit expense (recovery) *(note 14)*	(188)	20
Total	1,593	2,777

14. SHARE UNIT LIABILITY

Deferred Share Units

The Corporation has a deferred share unit plan, whereby DSUs may be issued to members of the Board and eligible executive officers. Each DSU is a notional unit equal in value to one Common Share, which entitles the holder to a cash payment upon redemption. DSUs vest at the end of the financial quarter in which they are granted, but can only be converted to cash upon the holder ceasing to be a director and/or executive officer of the Corporation. The expense associated with the DSU plan is determined based on the 20-day VWAP of Common Shares at the grant date. The expense is recognized in the statement of operations in the quarter in which the units are granted, with a corresponding DSU liability recorded as a current liability in the statement of financial position. At reporting dates, the DSU liability is adjusted based on the 20-day VWAP of Common Shares.

Restricted Share Units

The Corporation has a restricted share unit plan, whereby RSUs may be issued to executive officers and eligible employees. Each RSU is a notional unit equal in value to one Common Share, which entitles the holder to a cash payment upon redemption. RSUs vest in three equal installments on the first, second, and third anniversaries of the grant date, at which time the holder is eligible to receive a cash payment equal to the number of vested awards multiplied by the fair market value. The expense associated with the RSU plan is determined based on the 20-day VWAP of Common

Shares at the grant date. The expense is recognized in the statement of operations over the vesting period, with a corresponding RSU liability recorded as a current liability in the statement of financial position. At reporting dates, the RSU liability is adjusted based on the 20-day VWAP of Common Shares.

Preferred Share Units
The Corporation has a performance share unit plan, whereby PSUs may be issued to eligible executive officers. Each PSU is a notional unit equal in value to one Common Share, which entitles the holder to a cash payment upon redemption. PSUs vest upon the third anniversary of the grant date, at which time the holder is eligible to receive a cash payment equal to the number of vested awards multiplied by the fair market value. The unit value is adjusted for a performance multiplier which can range from 0 to 2 and is dependent on the performance of the Corporation for a predefined period. The expense associated with the PSU plan is determined based on the 20-day VWAP of Common Shares at the grant date. The expense is recognized in the statement of operations over the vesting period, with a corresponding PSU liability recorded as a current liability in the statement of financial position. At reporting dates, the PSU liability is adjusted based on the 20-day VWAP of Common Shares.

The following tables summarize information related to the Corporation’s deferred share unit plan, restricted share unit plan, and performance share unit plan (collectively the “share unit plans”):

	Deferred Share Units	Restricted Share Units	Preferred Share Units	Total
As at December 31, 2017	690,104	222,630	303,900	1,216,634
Granted	400,703	413,100	482,000	1,295,803
Exercised	(141,331)	(85,070)	—	(226,401)
Forfeited	—	(64,160)	(126,000)	(190,160)
As at December 31, 2018	949,476	486,500	659,900	2,095,876
Granted	1,019,871	832,900	744,000	2,596,771
Exercised	(36,368)	(197,100)	—	(233,468)
Forfeited	—	(37,900)	—	(37,900)
As at December 31, 2019	1,932,979	1,084,400	1,403,900	4,421,279

	Deferred Share Units	Restricted Share Units	Preferred Share Units	Total
($000s)				
Value of share unit liability as at December 31, 2019	1,339	489	323	2,151
Value of share unit liability as at December 31, 2018	1,448	410	205	2,063

During the year ended December 31, 2019, the Corporation capitalized $0.6 million (year ended December 31, 2018 - $0.5 million) related to the share unit plans.

15. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

The Corporation’s activities expose it to a variety of financial risks that arise as a result of its development, production and financing activities. These include market risk, credit risk and liquidity risk.

The Board oversees the establishment and execution of the Corporation’s risk management framework. Management has implemented and monitors compliance with risk management policies. The Corporation’s risk management policies are established to identify and analyze the risks faced by the Corporation, to set appropriate risk limits and controls and to monitor risks and adherence to market conditions and the Corporation’s activities.

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

Natural gas prices obtained by the Corporation are influenced by both U.S. and Canadian supply and demand. The exchange rate effect cannot be quantified but generally an increase in the value of the Canadian dollar as compared to the U.S. dollar will reduce the prices received by the Corporation for its natural gas and natural gas liquids. Commodity price risk is the risk that the fair value of future cash flows will fluctuate as a result of changes in commodity prices. Commodity prices for natural gas and natural gas liquids are impacted by not only the relationship between the Canadian and United States dollars, but also upon world political and economic events that dictate the levels of supply and demand.

The Corporation's production is usually sold through near term sales contracts with prices fixed at the time of transfer of custody or on the basis of a monthly average market price. The Corporation, however, may give consideration in certain circumstances to the appropriateness of entering into long term fixed price marketing contracts.

The Corporation uses financial derivatives and physical delivery sales contracts to mitigate some of the exposure to commodity price risk, and provide a level of stability to operating cash flows which enables the Corporation to fund its capital development program. The use of these transactions is governed by and is subject to risk management policies established by the Board.

These instruments are not used for trading or speculative purposes. The Corporation has not designated its financial derivative contracts as effective accounting hedges, even though the Corporation considers all commodity contracts to be effective economic hedges. As a result, all such commodity contracts are recorded at fair value on the statement of financial position, with changes in the fair value being recognized as an unrealized gain or loss in the statement of operations.

Financial assets and liabilities carried at fair value are required to be classified into a hierarchy that prioritizes the inputs used to measure the fair value. The Corporation's risk management contracts are valued using Level 2 inputs. Assets and liabilities in Level 2 are based on valuation models and techniques where the significant inputs are derived from quoted indices.

The following is a summary of all commodity and other risk management contracts in place as at December 31, 2019:

Financial AECO Natural Gas Contracts

Options traded	Term	Volume (GJ/d)	Weighted average price (CAD$/GJ)
AECO Fixed Price Swap	January 2020 - March 2020	20,000	2.06
AECO Fixed Price Swap	April 2020 - October 2020	48,000	1.53
AECO Fixed Price Swap	April 2021 - October 2021	8,000	1.62
AECO Fixed Price Swap	April 2022 - October 2022	8,000	1.62

Financial NYMEX Natural Gas Contracts

Options traded	Term	Volume (Mmbtu/d)	Weighted average price (US$/Mmbtu)
USD Nymex Fixed Price	April 2020 - October 2020	10,000	2.53

Financial Sumas Natural Gas Contracts

Options traded	Term	Volume (MMBtu/d)	Weighted average price (US$/MMBtu)
USD Sumas Fixed Price Swap	January 2020	20,000	3.98

Financial AECO Differential Contracts

Options traded	Term	Volume (GJ/d)	Weighted average price (AECO 7A less CAD$/GJ)
AECO-Station 2 Differential Swap	January 2020 - October 2020	40,000	(0.32)
AECO-Station 2 Differential Swap	January 2020 - August 2021	20,000	(0.29)

Financial NYMEX Basis Contracts			
Options traded	Term	Volume (MMBtu/d)	Weighted average price (NYMEX less US$/MMBtu)
NYMEX-AECO Basis Swap	January 2020 - September 2021	10,000	(1.14)
NYMEX-AECO Basis Swap	January 2020 - December 2023	40,000	(1.28)
NYMEX-AECO Basis Swap	April 2020 - October 2020	10,000	(1.45)
NYMEX-AECO Basis Swap	April 2020 - December 2023	10,000	(1.18)
NYMEX-AECO Basis Swap	October 2021 - March 2023	10,000	(1.05)
NYMEX-Dawn Basis Swap	January 2020 - December 2020	20,000	(0.09)
NYMEX-Dawn Basis Swap	January 2020 - December 2021	20,000	(0.09)

Financial WTI Crude Oil Contracts			
Options traded	Term	Volume (Bbl/d)	Weighted average price (CAD$/Bbl)
WTI Call Option Sell *	January 2020 - December 2020	250	82.50
WTI Call Option Buy *	January 2020 - December 2020	250	70.00
WTI Fixed Price Swap	January 2020 - December 2020	750	77.14

* WTI costless collar with a floor price of $70.00 and ceiling price of $82.50.

In addition to the commodity risk management contracts discussed above, the Corporation has entered into physical delivery sales contracts to manage commodity risk. These contracts are considered normal sales contracts and are not recorded at fair value in the financial statements.

The Corporation has the following foreign exchange risk management contracts in place as at December 31, 2019:

Financial Foreign Exchange Contracts **			
Reference Currency	Term	Notional Amount (USD $000s/month)	Strike Rate (CAD/USD)
USD	January 2020 - September 2020	1,000	1.335
USD	January 2020 - March 2021	1,000	1.340
USD	January 2020 - December 2021	1,000	1.360

** Foreign exchange risk management contracts are fade-in forwards with an average fade-in level of 1.26.

The Corporation periodically enters into USD cross currency interest rate swaps related to LIBOR borrowings, which result in a reduction to interest expense paid on borrowings on the credit facility. As at December 31, 2019 the following cross currency swap was outstanding:

Contract Quantity	Type of Contract	Term / Expiry	Contract Price
$130 Million	Cross currency swap	January 21, 2020	$1.318 CAD/USD

Changes in the price assumptions can have a significant effect on the fair value of the derivative assets and liabilities and thereby impact income. For financial instruments in place at December 31, 2019, it is estimated that a $0.10 per mcf change in forward natural gas prices used to calculate the fair value of natural gas derivatives at December 31, 2019 would result in a $1.3 million change in net income (loss) and comprehensive income (loss) for the year ended December 31, 2019. It is estimated that a $1.00 per bbl change in the forward crude oil prices used to calculate the fair value of crude oil derivatives at December 31, 2019 would result in a $0.2 million change in net income (loss) and comprehensive income (loss) for the year ended December 31, 2019.

Foreign currency exchange risk is the risk that the fair value of future cash flows will fluctuate as a result of changes in foreign exchange rates. The change in the fair value of risk management contracts in place at December 31, 2019, based on a $0.01 change in CAD - U.S. foreign exchange rates, is estimated to be $0.3 million. Increases and decreases in foreign exchange rates applicable to U.S. denominated accounts receivable and payable would have a nominal impact on the Corporations net income (loss) for the year ended December 31, 2019. Fluctuations in U.S. foreign exchange rates have no impact on the Corporation's U.S. LIBOR loans, as the rates are set on the date of the transaction.

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. The Corporation is exposed to interest rate fluctuations on its bank debt which bears a floating rate of interest. For the year ended December 31, 2019, it is estimated that a 1.0% change in interest rates would result in a change to net income (loss) and comprehensive income (loss) of $1.0 million.

Financial assets and liabilities are presented on a net basis if the Corporation has a legal right to offset and intends to either settle on a net basis or to realize the asset and settle the liability simultaneously. The Corporation offsets financial assets and liabilities when the counterparty, currency and timing of settlement are the same. The following tables provide a summary of the Corporation’s offsetting financial derivative positions, and how risk management contracts are classified on the statement of financial position, respectively.

($000s)	**December 31, 2019**	**December 31, 2018**
Gross in-the-money risk management contracts	3,221	48,325
Gross out-of-the-money risk management contracts	(47,121)	(9,124)
Net fair value of risk management contracts	(43,900)	39,201

($000s)	**December 31, 2019**	**December 31, 2018**
Current assets	1,314	35,215
Non-current assets	142	7,350
Current liabilities	(16,940)	(530)
Non-current liabilities	(28,416)	(2,834)
Net fair value of risk management contracts	(43,900)	39,201

(b) Credit risk

Credit risk is the risk of financial loss to the Corporation if a customer or counterparty to a financial instrument fails to meet its contractual obligations and arises principally from the Corporation’s receivables from joint venture partners and natural gas and natural gas liquids purchasers. The Corporation’s maximum exposure to credit risk at December 31, 2019 and 2018 is as follows:

($000s)	**December 31, 2019**	**December 31, 2018**
Accounts receivable	38,687	55,532
Fair value of risk management contracts	1,456	42,565
Total	40,143	98,097

Accounts receivable

All of the Corporation’s operations are conducted in Canada. The Corporation’s exposure to credit risk is influenced mainly by the individual characteristics of each customer.

Receivables from natural gas and natural gas liquids purchasers are normally collected on the 25th day of the month following production. The Corporation’s policy to mitigate credit risk associated with these balances is to establish marketing relationships with large purchasers. The Corporation historically has not experienced any collection issues with its natural gas and natural gas liquids purchasers. Receivables from joint venture partners are typically collected within one to three months of the joint venture bill being issued.

The Corporation does not anticipate any default as it transacts with creditworthy customers and management does not expect any losses from non-performance by these customers. The lifetime ECL allowances related to the Corporation's accounts receivable were nominal as at and for the years ended December 31, 2019 and 2018.

The breakdown of accounts receivable at the reporting date by type of customer was:

($000s)	**December 31, 2019**	**December 31, 2018**
Natural gas and natural gas liquids revenue	36,082	50,779
Financial risk management contracts	480	4,390
Joint interest	134	281
Other	1,991	82
Total	38,687	55,532

The Corporation has three primary purchasers of natural gas and natural gas liquids; these purchasers accounted for $26.9 million of accounts receivable at December 31, 2019, compared to $49.9 million at December 31, 2018. As at December 31, 2019 and 2018, the Corporation's accounts receivable is aged as follows:

($000s)	**December 31, 2019**	**December 31, 2018**
Less than 30 days	37,963	55,364
From 31 - 90 days	516	106
More than 90 days	208	62
Total	38,687	55,532

Derivative Financial Instruments

The use of financial swap agreements involves a degree of credit risk that the Corporation manages through its risk management policies which are designed to limit eligible counterparties to those with investment grade credit ratings or better.

(c) Liquidity risk

Liquidity risk is the risk that the Corporation will not be able to meet its financial obligations as they become due. The Corporation's approach to managing liquidity is to ensure, to the extent possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Corporation's reputation.

Management closely monitors cash flow requirements to ensure that it has sufficient borrowing capacity to meet operational and financial obligations currently and in the foreseeable future; this excludes the potential impact of extreme circumstances that cannot reasonably be predicted, such as natural disasters. To achieve this objective, the Corporation prepares annual capital expenditure budgets, which are regularly monitored and updated as considered necessary. Further, the Corporation utilizes authority for expenditures on both operated and non-operated projects to further manage capital expenditures. The Corporation also typically collects its natural gas and natural gas liquids revenues from most properties on the 25th of each month.

To facilitate the capital expenditure program, the Corporation has an aggregate of $375 million in syndicated credit facilities at December 31, 2019, as well as a CAD $22.0 million letter of credit facility backstopped by EDC, compared to $400 million in syndicated credit facilities at December 31, 2018, which are reviewed semi-annually by its lenders.

(d) Capital management

The Corporation maintains a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The Corporation manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying natural gas and natural gas liquids assets. The Corporation considers its capital structure to include shareholders' equity, loans and borrowings and working capital. In order to maintain or adjust the capital structure, the Corporation may issue shares or debt and adjust its capital spending to manage current and projected debt levels.

The Corporation monitors capital based on the net debt to EBITDA ratio, calculated on a trailing four fiscal quarter basis. This ratio is calculated as net debt, which is defined as bank debt, senior notes, the liability portion of convertible debentures, and working capital, adjusted for the net current portion of the fair value of risk management contracts and current portion of the finance lease obligation, divided by trailing four fiscal quarter EBITDA, calculated as net income plus finance expense excluding the costs associated with the finance lease obligation, plus income taxes and adjustments for earnings or losses attributable to extraordinary and non-recurring gains or losses, as well as adjustments for any non-cash items including depreciation, depletion, amortization, deferred income taxes and non-cash gains or losses resulting from marking-to-market the outstanding risk management contracts. In order to facilitate the management of this ratio, the Corporation prepares annual capital expenditure budgets, which are updated as necessary depending on varying factors including current and forecast prices, successful capital deployment and general industry conditions. The annual and updated budgets are approved by the Board of Directors of the Corporation.

The Corporation is not subject to externally imposed capital requirements. The syndicated credit facilities are subject to a semi-annual review of the borrowing base which is directly impacted by the value of the natural gas and natural gas liquids reserves.

16. DETERMINATION OF FAIR VALUES

A number of the Corporation'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.

(a) Property, Plant and Equipment and Exploration and Evaluation Assets

The fair values of PP&E and E&E assets recognized in an acquisition are based on market values. The fair values of PP&E and E&E are the estimated amounts for which they 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 natural gas and natural gas liquids interests (included in PP&E) and E&E assets is estimated with reference to the discounted cash flows expected to be derived from natural gas and natural gas liquids production, based on externally prepared reserve reports. The risk-adjusted discount rate is specific to the asset with reference to general market conditions.

(b) Accounts Receivable, Accounts Payable and Accrued Liabilities, Bank Debt, Senior Notes and Convertible Debentures

The fair value of accounts receivable, accounts payable and accrued liabilities, and bank debt are estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. At December 31, 2019 and December 31, 2018, the fair value of these balances approximated their carrying value. Bank debt has a floating rate of interest and therefore the carrying value approximates the fair value. The fair value of the senior notes fluctuates in response to changes in the market rates of interest payable on similar instruments.

(c) Stock Options

The fair value of employee stock options is measured using a Black-Scholes option pricing model. Measurement inputs include share price on measurement date, exercise price of the instrument, expected volatility, weighted average expected life of the instruments (based on historical experience and general stock option holder behavior), expected dividends and the risk-free interest rate.

(d) Derivatives

Measurement

The Corporation classifies the fair value of derivative transactions according to the following hierarchy based on the amount of observable inputs used to value the instrument.

(i) 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 pricing information on an ongoing basis.

(ii) 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.

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

The fair value of commodity price risk management contracts is determined by discounting the difference between the contracted prices and published forward price curves as at the date of the statement of financial position, using the remaining contracted natural gas and natural gas liquids volumes and risk-free interest rate (based on published government rates). The fair value of foreign exchange contracts is determined based on the difference between the contracted forward rate and current forward rates, using the remaining settlement amount. The Corporation's commodity price contracts, foreign exchange contracts, senior notes and convertible debentures are valued using Level 2 of the hierarchy.

The fair value of DSUs, PSUs and RSUs is measured upon grant and at each period end date, using the 20-day VWAP of Common Shares. The Corporation's DSUs, PSUs and RSUs are valued using Level 1 of the hierarchy.

17. FINANCE LEASE OBLIGATION

The Corporation is party to a series of agreements (collectively the "Strategic Alliance") with a Canadian midstream company (the "Midstream Company"), relating to the development of processing infrastructure and marketing services for natural gas and natural gas liquids. Under the Strategic Alliance, the Midstream Company committed to building gas processing facilities including a 198 MMcf/d shallow cut gas processing facility at the Townsend property and related pipeline infrastructure, which commenced commercial operations in 2016 (the "Townsend Facility"). During 2017, Painted Pony entered into an agreement with the Midstream Company in respect of a Townsend Phase 2 expansion ("Townsend Phase 2") which consisted of a 99 MMcf/d gas processing train located on the existing Townsend site adjacent to, and sharing joint equipment with the original Townsend Facility. The facilities and related pipeline infrastructure included in these agreements have been recorded as a finance lease obligation. The Corporation has recorded the asset, with a corresponding obligation on the statement of financial position. Over the course of the 20-year term there is a capital fee, which includes the finance expense and amortization of the obligation. The original cost of the facilities and related pipeline infrastructure capitalized was approximately $490 million.

On transition to IFRS 16, the Corporation recognized an additional $1.4 million of right-of-use assets and lease liabilities related to office space. When measuring office lease liabilities, the Corporation discounted lease payments using an incremental borrowing rate at January 1, 2019 of 4.9%.

Total expected payments, not included in note 18, for the Corporation's facilities and related infrastructure, and office space recorded as finance lease obligations are reflected in the table below.

($000s)	**Within 1 year**	**After 1 year but not more than five years**	**More than five years**	**Total**
Processing	54,921	291,529	514,614	861,064
Transportation	10,144	54,559	157,836	222,539
Office space	480	848	—	1,328
Total	65,545	346,936	672,450	1,084,931
Principal	8,203	83,248	393,924	485,375

Expenses relating to short-term and low value leases for which the recognition exemption is applied were $1.1 million for the year ended December 31, 2019.

On February 27, 2020, the Corporation entered into agreements with respect to the Townsend Facility, Townsend Phase 2, and the related pipeline infrastructure, which, change the take-or-pay volumes and capital fees associated with the facilities and related pipeline infrastructure. These costs are currently recorded as a finance lease on the statement of financial position. In accordance with IFRS 16*,* when a finance lease is modified, the modified lease is evaluated to determine whether it is, or contains, a lease. The Corporation is currently assessing the contract modifications to determine whether or not the new contract contains a lease, and the effect that these changes have on the financial statements. If any right of use assets are derecognized, any gain or loss resulting from the derecognition of the right of use asset and lease liability will be recorded to the statement of operations from the effective date of the modification.

18. COMMITMENTS

($000s)	**2020**	**2021**	**2022**	**2023**	**2024**	**Thereafter**	**Total**
Transportation and processing	113,721	118,440	134,558	112,961	108,905	1,345,972	1,934,557
Interest on senior notes to maturity	12,750	12,750	9,563	—	—	—	35,063
Interest on convertible debentures to maturity	3,250	2,438	—	—	—	—	5,688
Other	1,115	1,098	989	—	—	—	3,202
Total commitments	130,836	134,726	145,110	112,961	108,905	1,345,972	1,978,510

Transportation commitments include contracts to transport natural gas and natural gas liquids through third-party owned pipeline systems in North America. Processing commitments include contracts to process natural gas and natural gas liquids through third-party owned gas processing facilities in British Columbia. Interest on senior notes includes quarterly interest on senior notes. Interest on convertible debentures includes quarterly interest on convertible debentures. Other commitments include variable lease payments not included in the finance lease obligation.

19. REVENUE

Painted Pony produces natural gas and natural gas liquids from its assets in western Canada (specifically in northeast British Columbia). The Corporation sells its production pursuant to fixed and variable price physical delivery contracts. Under the contracts, the Corporation is required to deliver a fixed or variable volume of natural gas or natural gas liquids to the contract counterparty. The transaction price for variable priced contracts is based on a benchmark commodity price, adjusted for quality, location and other factors, whereby each component of the pricing formula can be fixed or variable depending on the contract terms.

Production revenue is recognized when the Corporation gives up control of a unit of production at the delivery point in accordance with the terms of the contract. Revenue recognized is based on the agreed transaction price and the volumes delivered. Any variability in the transaction price relates specifically to the Corporation's efforts to transfer production, and is therefore recognized in the period in which the variability relates. The Corporation does not have any factors considered to be constraining in the recognition of revenue for variable pricing factors.

Contract terms have lengths varying from one to 14 years, with delivery taking place throughout the term of the contracts. Production revenues are normally collected on the 25th day of the month following production.

The Corporation's revenue was generated entirely in British Columbia, and the production was sold in British Columbia, Alberta, and Ontario, primarily to three major purchasers. The three purchasers individually accounted for more than 10% of, and together represented 91% of sales for the year ended December 31, 2019 (year ended December 31, 2018 - 97%).

These three purchasers individually represented more than 10% of, and together represented 70% of accounts receivable at December 31, 2019 (December 31, 2018 - 89%). The following table represents the Corporation's natural gas and natural gas liquids sales disaggregated by product:

($000s)	**Years ended December 31,**	
	2019	**2018**
Natural gas	235,247	293,145
Natural gas liquids	67,503	111,227
Total	302,750	404,372

Under certain marketing arrangements, the Corporation transfers title of its natural gas production to a third party marketing company who subsequently redelivers the natural gas production by utilizing the Corporation's transportation pipeline capacity. Under the terms of these contracts, the Corporation has assigned a portion of their pipeline capacity to the marketing company for the specified contract term. The revenue related to these assigned transportation contracts for the year ended December 31, 2019 represents 17% of total natural gas revenue (year ended December 31, 2018 - 23%).

At times, the Corporation purchases commodity products from third parties to fulfill sales commitments and subsequently sells these products to its purchasers. During the year ended December 31, 2019, the net revenue related to these activities was $1.2 million (2018 - $0.8 million).

20. SUPPLEMENTAL DISCLOSURES

(a) Key Management Personnel Compensation

Key management personnel are persons who have the authority and responsibility for planning, directing and controlling the activities of the Corporation, directly or indirectly. This includes all directors and executives of the Corporation. Short-term compensation includes salaries, bonuses and short-term benefits paid to executives and fees paid to directors. Share-based compensation represents amortization of the expense associated with stock options, RSUs, PSUs and DSUs granted to executives and directors.

($000s)	**December 31, 2019**	**December 31, 2018**
Short-term compensation	5,000	5,829
Share-based compensation	1,724	2,505
Total	6,724	8,334

(b) Presentation in Statements of Cash Flows

Changes in non-cash working capital are comprised of:

($000s)	**December 31, 2019**	**December 31, 2018**
Source/(use) of cash:		
Accounts receivable	16,845	(16,417)
Prepaid expenses and deposits	234	(565)
Accounts payable and accrued liabilities	(5,202)	(15,118)
Unrealized foreign exchange translation	2,905	—
Share unit liability	88	59
	14,870	(32,041)
Operating activities	12,149	(5,604)
Investing activities	2,380	(22,513)
Financing activities	341	(3,924)
	14,870	(32,041)

21. CONTINGENCY

There is ongoing litigation involving the Blueberry River First Nation ("BRFN") and the British Columbia Government regarding the obligations of natural resource companies and the Crown relative to the adequacy of consultation and cumulative effects in respect of upstream oil and gas development in northeast British Columbia, where a substantial portion of the Corporation's land and assets are situated. The Corporation is not a party to the litigation. While a successful claim by BRFN may be adversely material to the Corporation, at this point, the success of the claim and any corresponding impact is indeterminable. If the claim is decided in BRFN's favour, it would have an adverse impact on the Corporation, its operations and production, particularly for those operations that may be considered to impact Aboriginal traditional lands or rights. The Corporation is therefore, actively monitoring the status of the BRFN claim.

CORPORATE INFORMATION

BOARD OF DIRECTORS
Glenn R. Carley (Chairman)
Calgary, Alberta

Kevin D. Angus
Calgary, Alberta

Joan E. Dunne
Calgary, Alberta

Nereus L. Joubert
Calgary, Alberta

Lynn Kis
Calgary, Alberta

Elizabeth G. Spomer
Houston, Texas

George W. Voneiff
Bryan, Texas

Patrick R. Ward
Calgary, Alberta

OFFICERS
Patrick R. Ward
President and Chief Executive Officer

Mike Backus
Vice President, Development and Operations

Tonya L. Fleming
Vice President, General Counsel and
Corporate Secretary

Edwin S. (Ted) Hanbury
Senior Vice President, Strategic Projects

Stuart W. Jaggard
Chief Financial Officer

L. Barry McNamara
Vice President, Development and Marketing

AUDITORS
KPMG LLP

BANKERS
The Toronto-Dominion Bank
Canadian Imperial Bank of Commerce
The Bank of Nova Scotia
Alberta Treasury Branches
HSBC Bank Canada
Royal Bank of Canada

EVALUATION ENGINEERS
GLJ Petroleum Consultants Ltd.

REGISTRAR AND TRANSFER AGENT
TSX Trust Company

EXCHANGE LISTING
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