yangarra resources ltd.

Yangarra Resources Ltd.

Condensed Consolidated Interim Financial Statements

September 30, 2016 and 2015

		September 30, 2016 (unaudited)		December 31, 2015 (audited)
Assets				
Current				
Accounts receivable *(note 12)*	$	**7,932,361**	$	10,281,917
Prepaid expenses and deposits		**3,984,887**		3,285,317
Commodity contracts *(note 12c iii)*		**525,003**		2,506,072
Total current assets		**12,442,251**		16,073,306
Non-current				
Property and equipment *(note 2)*		**270,291,202**		243,709,385
Exploration and evaluation assets *(note 4)*		**6,762,465**		6,762,465
Total assets	$	**289,495,918**	$	266,545,156
Liabilities				
Current				
Bank debt *(note 5)*	$	**60,586,018**	$	62,131,258
Accounts payable and accrued liabilities *(note 12)*		**9,718,971**		12,322,532
Commodity contracts *(note 12c iii)*		**83,558**		194,162
Interest rate contracts *(note 12c i)*		**275,252**		273,448
Total current liabilities		**70,663,799**		74,921,400
Non-current				
Other long-term liabilities *(note 11)*		**222,052**		252,228
Interest rate contract *(note 12c i)*		**195,800**		399,574
Flow-through share premium obligation		–		631,636
Decommissioning liability *(note 6)*		**11,190,835**		9,191,316
Deferred tax liability		**23,596,398**		20,015,861
Total liabilities		**105,868,884**		105,412,015
Shareholders' Equity				
Share capital *(note 7b)*		**162,301,055**		151,345,752
Contributed surplus		**13,505,256**		12,474,614
Retained Earnings (Deficit)		**7,820,723**		(2,687,225)
Total shareholders' equity		**183,627,034**		161,133,141
Total liabilities and shareholders' equity	$	**289,495,918**	$	266,545,156

Contingency (note 15), Commitments (note 16)

	Three months ended September 30,		Nine months ended September 30,	
	2016	2015	**2016**	2015
Revenue				
Petroleum and natural gas sales	$ **5,939,598**	$ 5,363,673	$ **17,950,262**	$ 18,527,820
Royalty income	**48,712**	66,770	**113,919**	181,048
Royalties	**(272,840)**	(120,664)	**(622,978)**	(744,867)
	5,715,470	5,309,779	**17,441,203**	17,964,001
Commodity price risk contracts *(note 12c iii)*				
Realized gain on commodity contract settlement	**468,105**	1,352,383	**1,877,098**	7,634,614
Change in fair value of commodity contracts	**(106,568)**	2,371,579	**(1,870,465)**	(5,077,550)
	6,077,007	9,033,741	**17,447,836**	20,521,065
Expenses				
Production	**1,672,896**	1,467,314	**5,590,821**	4,585,713
Transportation	**280,238**	274,708	**1,112,098**	915,134
General and administrative	**379,884**	258,205	**1,346,205**	1,216,517
Finance *(note 14)*	**488,725**	559,530	**1,726,639**	2,127,736
Share-based compensation *(note 8)*	**191,828**	295,585	**792,007**	541,092
Depletion and depreciation *(note 2)*	**3,208,061**	2,550,258	**10,386,589**	8,529,821
Exploration and evaluation asset impairment *(note 4)*	**–**	5,410,547	**756,845**	5,410,547
	6,221,632	10,816,147	**21,711,204**	23,326,560
Other Income				
Gain on settlement of lawsuit (note 3)	**–**	–	**13,082,687**	–
Income (loss) before tax	**(144,625)**	(1,782,406)	**8,819,319**	(2,805,495)
Deferred tax (recovery) expense	**326,158**	571,230	**(1,688,629)**	1,805,616
Net income (loss) and total comprehensive income (loss)	$ **(470,783)**	$ (2,353,636)	$ **10,507,948**	$ (4,611,111)
Earnings (loss) per share *(note 9)*				
Basic	$ **(0.01)**	$ (0.03)	**0.14**	$ (0.07)
Diluted	$ **(0.01)**	$ (0.03)	**0.14**	$ (0.07)
Weighted average number of shares *(note 9)*				
Basic	**79,181,804**	67,681,804	**73,054,066**	62,555,188
Diluted	**79,181,804**	67,681,804	**73,433,974**	62,555,188

The accompanying notes are an integral part of these condensed consolidated interim financial statements

		2016		2015
Share Capital				
Balance, beginning of period	$	**151,345,752**	$	134,406,725
Issued *(note 7)*		**11,500,000**		20,002,390
Share issue costs *(note 7)*		**(745,969)**		(1,266,937)
Tax effect of share issue costs *(note 7)*		**201,272**		342,073
Flow-through share premium obligation		–		(2,135,590)
Balance, end of period		**162,301,055**		151,348,661
Contributed Surplus				
Balance, beginning of period		**12,474,614**		11,337,527
Share-based compensation		**1,030,642**		744,032
Balance, end of period		**13,505,256**		12,081,559
Retained Earnings (Deficit)				
Balance, beginning of period		**(2,687,225)**		2,093,945
Net income (loss)		**10,507,948**		(4,611,111)
Balance, end of period		**7,820,723**		(2,517,166)
Total Shareholder' Equity	$	**183,627,034**	$	160,913,054

The accompanying notes are an integral part of these condensed consolidated interim financial statements

	Three months ended September 30,		Nine months ended September 30,	
	2016	2015	**2016**	2015
Operating				
Net income (loss) for the period	$ **(470,783)**	$ (2,353,636)	$ **10,507,948**	$ (4,611,111)
Add back non-cash items:				
Change in fair value of commodity contracts	**106,568**	(2,371,579)	**1,870,465**	5,077,550
Change in fair value of interest rate contracts	**(73,719)**	19,013	**(201,970)**	305,047
Share-based compensation *(note 8)*	**191,828**	295,585	**792,007**	541,092
Depletion and depreciation *(note 2)*	**3,208,061**	2,550,258	**10,386,589**	8,529,821
Exploration and evaluation asset impairment *(note 4)*	–	5,410,547	**756,845**	5,410,547
Accretion *(note 6)*	**43,853**	45,112	**141,858**	127,307
Gain on settlement of lawsuit *(note 3)*	–	–	**(13,082,687)**	–
Deferred tax (recovery) expense	**326,158**	571,230	**(1,688,629)**	1,805,616
Change in non-cash working capital *(note 10)*	**1,534,201**	433,052	**(199,810)**	(2,091,226)
Net cash flow from operating activities	**4,866,167**	4,599,582	**9,282,616**	15,094,643
Financing				
Issue of equity instruments, net of costs *(note 3)*	**(518)**	(1,276)	**10,754,031**	18,735,453
Bank debt advance (repayment) *(note 5)*	**1,280,143**	2,050,000	**(1,545,240)**	887,354
Other long-term liabilities repayment	**(10,093)**	(9,786)	**(30,175)**	(29,058)
Change in non-cash working capital *(note 10)*	–	–	–	69,859
Net cash from financing activities	**1,269,532**	2,038,938	**9,178,616**	19,663,608
Investing				
Additions to property and equipment *(note 2)*	**(10,436,072)**	(7,000,448)	**(13,999,774)**	(24,501,614)
Property acquisitions *(note 3)*	–	(4,706,547)	**(3,707,693)**	(4,706,547)
Change in non-cash working capital *(note 10)*	**4,300,373**	5,068,475	**(753,765)**	(5,550,090)
Net cash flow used in investing activities	**(6,135,699)**	(6,638,520)	**(18,461,232)**	(34,758,251)
Change in cash and cash equivalents	–	–	–	–
Cash, beginning of the period	–	–	–	–
Cash, end of the period	$ –	$ –	$ –	$ –

The accompanying notes are an integral part of these condensed consolidated interim financial statements

1. Basis of preparation, adoption of IFRS and statement of compliance

Yangarra Resources Ltd. (the "Company") is a publicly traded company involved in the production, exploration and development of resource properties in Western Canada. The address of the registered office is 1530, 715 – 5 Avenue SW, Calgary Alberta, T2P 2X6.

These condensed consolidated interim financial statements include the accounts of the Company and its wholly owned subsidiary, Yangarra Resources Corp. ("YRC"), after the elimination of intercompany transactions and balances.

Statement of compliance and authorization

These interim consolidated financial statements have been prepared in accordance with International Accounting Standard 34 – *Interim Financial Reporting* on a basis consistent with the accounting, estimation and valuation policies described in the Company's audited Annual Consolidated Financial Statements as at and for the year ended December 31, 2015 (the "Annual Financial Statements"). These condensed consolidated interim financial statements have been prepared on a historical cost basis, except for certain financial instruments. Certain information and disclosures normally required to be included in the notes to the Annual Financial Statements prepared in accordance with International Financial Reported Standards have been condensed or omitted These condensed consolidated interim financial statements should be read in conjunction with the Annual Financial Statements. All financial information is reported in Canadian dollars.

The condensed consolidated interim financial statements were authorized for issue by the Company's Board of Directors on November 10, 2016.

Changes in accounting standards

There were no new accounting standards adopted by the Company for the three months ended September 30, 2016. A description of accounting standards that will be effective in the future is included in the notes to the Company's Annual Financial Statements.

Accounting standards issued but not yet applied

IFRS 16 Leases issued on January 13, 2016 by the IASB replaces IAS 17 Leases. The new standard introduces a single recognition and measurement model for leases, which would require the recognition of assets and liabilities for most leases with a term of more than twelve months. The new standard is effective for annual periods beginning on or after January 1, 2019. Early adoption is permitted for entities that apply IFRS 15 "Revenue from Contracts with Customers" at or before the initial adoption date of January 1, 2018. Management is currently assessing any potential impact of the adoption of IFRS 16.

On January 19, 2016, the IASB issued amendments to IAS 12, Income Taxes, relating to the recognition of deferred tax assets for unrealized losses. The amendments are effective for annual periods beginning on or after January 1, 2017, with early adoption permitted. The Company is currently assessing the impact of the adoption of these amendments on the Company's consolidated financial statements.

On January 29, 2016, the IASB issued amendments to IAS 7, Statement of Cash Flows, as part of its disclosure initiative. The amendments require an entity to disclose changes in liabilities arising from financing activities. The amendments are effective for annual periods beginning on or after January 1, 2017, with early adoption permitted. The Company is currently assessing the impact of the adoption of these amendments on the Company's consolidated financial statements.

In April 2016, the IASB issued its final amendments to IFRS 15 Revenue from Contracts with Customers, which replaces IAS 18 Revenue, IAS 11 Construction Contracts, and related interpretations. The standard is required to be adopted either retrospectively or using a modified retrospective approach for annual periods beginning on or after January 1, 2018, with earlier adoption permitted. IFRS 15 will be applied by Yangarra on January 1, 2018 and the Company is currently evaluating the impact of the standard on Yangarra's consolidated financial statements.

1. Basis of preparation, adoption of IFRS and statement of compliance (continued)

On June 20, 2016, the IASB issued amendments to IFRS 2, relating to classification and measurement of particular share-based payment transactions. The amendments are effective for periods beginning on or after January 1, 2018. The Company is currently assessing the impact of the adoption of these amendments on the Company's consolidated financial statements.

In July 2014, the IASB completed the final elements of IFRS 9 "Financial Instruments." The Standard supersedes earlier versions of IFRS 9 and completes the IASB's project to replace IAS 39 "Financial Instruments: Recognition and Measurement." IFRS 9, as amended, includes a principle-based approach for classification and measurement of financial assets, a single 'expected loss' impairment model and a substantially-reformed approach to hedge accounting. The Standard will come into effect for annual periods beginning on or after January 1, 2018, with earlier adoption permitted. IFRS 9 will be applied by the Company on January 1, 2018 and the Company is currently evaluating the impact of the standard on the Company's financial statements.

2. Property and equipment

	Oil and Natural Gas Interests	*Well and Plant Equipment*	*Other Assets*	*Total*
Cost				
Balance at December 31, 2014	$ 236,642,194	$ 43,632,623	$ 1,619,169	$ 281,893,986
Cash additions	27,512,533	8,307,293	205,295	36,025,121
Capitalized share based compensation	312,328	–	–	312,328
Decommissioning liability	834,014	–	–	834,014
Balance at December 31, 2015	265,301,069	51,939,916	1,824,464	319,065,449
Cash additions	**12,184,068**	**1,726,000**	**89,706**	**13,999,774**
Property acquisition *(note 3)*	**22,495,329**	–	–	**22,495,329**
Capitalized share-based compensation	**238,634**	–	–	**238,634**
Decommissioning liability *(note 6)*	**991,514**	–	–	**991,514**
Balance at September 30, 2016	**$ 301,210,614**	**$ 53,665,916**	**$ 1,914,170**	**$ 356,790,700**

Depletion, depreciation and impairment

	Oil and Natural Gas Interests	*Well and Plant Equipment*	*Other Assets*	*Total*
Balance at December 31, 2014	$ 56,317,971	$ 6,596,800	$ 824,872	$ 63,739,643
Depletion and depreciation	10,660,400	770,500	185,521	11,616,421
Balance at December 31, 2015	66,978,371	7,367,300	1,010,393	75,356,064
Depletion and depreciation	**9,583,600**	**564,900**	**238,089**	**10,386,589**
Asset impairment	**756,845**	–	–	**756,845**
Balance at September 30, 2016	**$ 77,318,816**	**$ 7,932,200**	**$ 1,248,482**	**$ 86,499,498**
At December 31, 2015	$ 198,322,698	$ 44,572,616	$ 814,071	$ 243,709,385
At September 30, 2016	**$ 223,891,798**	**$ 45,733,716**	**$ 665,688**	**$ 270,291,202**

2. Property and equipment (continued)

The depletion, depreciation and impairment of property and equipment, and any eventual reversal thereof, are recognized in the condensed consolidated interim statement of income and comprehensive income. At September 30, 2016 all of the Company's properties are pledged as security for the bank debt (see note 5).During the nine months ended September 30, 2016, the Company capitalized $991,514 (2015 – $618,267) related to the decommissioning liability of property and equipment and $238,634 (2015 – $202,943) of share-based compensation. The Company also capitalized $296,312 (2015 - $563,702) of recoveries related to the Company's working interest in operated capital expenditure programs on which overhead has been charged in accordance with standard industry operating agreements. During the nine months ended September 30, 2016, the Company capitalized $364,895 (2015 – $566,787) of salaries and consulting expenses directly to geological, drilling and completions projects as the individuals worked in the field directly on the operations.

The Company impaired the Jaslan CGU to zero during the first quarter in 2016, management determined that as a result lower natural gas pricing in the quarter the area was no longer economic and therefore disassembled and transported the facility to another CGU.

3. Property acquisition

On January 1, 2016, Yangarra closed the acquisition of certain strategic light oil assets in Yangarra's Central Alberta core area. The property acquisition was accounted for as a business combination under IFRS 3. The acquisition included a cash component, forgiveness of accounts receivable balances and the settlement of a lawsuit between the two parties. The fair value of the petroleum and natural gas properties acquired was determined using the total proved ("1P") value as at January 1, 2016, discounted at 10%, prepared by an independent reserve evaluator. The amounts in the table below are preliminary and subject to adjustments.

Net Assets Acquired		
Petroleum and natural gas properties	$	**22,323,000**
Decommissioning liability		**(693,818)**
Deferred tax liability		**(4,838,802)**
	$	**16,790,380**
Consideration		
Cash	$	**1,400,000**
Working capital		**2,307,693**
Gain on settlement of lawsuit		**13,082,687**
	$	**16,790,380**

4. Exploration and evaluation assets

Cost		
Balance at December 31, 2014	$	11,831,752
Additions		4,706,547
Balance at December 31, 2015 and September 30, 2016	$	**16,538,299**
Impairment losses		
Balance at December 31, 2014	$	4,365,287
Impairment		5,410,547
Balance at December 31, 2015 and September 30, 2016	$	9,775,834
Net book value		
At December 31, 2014	$	7,466,465
At December 31, 2015 and September 30, 2016	$	**6,762,465**

Exploration and evaluation ("E&E") assets consist of the Company's undeveloped land which is pending the determination of proven or probable reserves. Additions represent the Company's share of costs incurred on E&E assets during the period.

5. Bank debt

As at September 30, 2016, the $60,586,018 (December 31, 2015 – $62,131,258) reported amount of bank debt with Alberta Treasury Branches ("ATB") was comprised of $10,800,000 (December 31, 2015 – $12,250,000) drawn on the revolving operating demand loan and $49,786,018 (December 31, 2015 – $49,881,258) of guaranteed notes. The Company is subject to a financial covenant requiring an adjusted working capital ratio above 1:1 (current assets plus the undrawn availability under the revolving facility, divided by the current liabilities less the drawn portion of the revolving facility, excluding unrealized commodity contracts and flow-through share premium obligation). The Company was in compliance with this covenant as at September 30, 2016 and December 31, 2015. The facility is secured by a general security agreement.

As at September 30, 2016, the maximum amount available under the revolving operating demand loan was $80,000,000 (December 31, 2015 – $80,000,000) at an interest rate of bank prime plus 1.00% per annum on the operating demand loan, payable monthly, or a credit spread of 2.25% on guaranteed notes. A decrease in the borrowing base could result in a reduction to the credit facility, which may require repayment to the lenders. During the nine months ended September 30, 2016, the weighted average effective interest rate for the bank debt was approximately 3.43% (2015 – 3.1%).

6. Decommissioning liability

The following table presents the reconciliation of the carrying amount of the liability associated with the decommissioning of the Company's property and equipment:

		September 30, 2016		*December 31, 2015*
Balance, beginning of period	$	**9,191,316**	$	8,250,475
Liabilities incurred		**172,329**		598,210
Property acquisition *(note 3)*		**693,818**		–
Decommissioning costs incurred		–		(64,178)
Effect of change in estimate		**991,514**		235,804
Accretion		**141,858**		171,005
Balance, end of period	$	**11,190,835**	$	9,191,316

The following significant assumptions were used to estimate the decommissioning liability:

		September 30, 2016		*December 31, 2015*
Undiscounted cash flows	$	**14,590,603**	$	13,193,357
Discount rate		**0.76% - 1.66%**		1.04% - 2.31%
Inflation rate		**2%**		2%
Weighted average expected timing of cash flows		**10 years**		10 years

7. Share capital

a. Authorized

Unlimited number of common shares, without nominal or par value
Unlimited number of preferred shares, without nominal or par value

b. Common shares issued

	Number of shares		*Amount ($)*
Balance, December 31, 2014	57,755,804	$	134,406,725
Equity financing	3,333,500		6,000,300
CDE flow-through financing	1,010,500		2,000,790
CDE flow-through premium liability	–		(181,890)
CEE flow-through financing	5,582,000		12,001,300
CEE flow-through premium liability	–		(1,953,700)
Share issue costs (net of $342,149 in tax)	–		(927,773)
Balance, December 31, 2015	67,681,804	$	151,345,752
Equity financing *(i)*	**11,500,000**		**11,500,000**
Share issue costs (net of $201,272 in tax)	**–**		**(544,697)**
Balance, September 30, 2016	**79,181,804**	**$**	**162,301,055**

i) On May 25, 2016 the Company closed a "bought deal" financing, completed by way of a short form prospectus. 11,500,000 common shares were issued at a price of $1.00 per common share for gross proceeds of $11,500,000.

8. Share-based compensation

The Company has an equity settled stock option plan under which the Board of Directors may grant options to directors, officers, other employees and key consultants. The purpose of the plan is to advance the interests of the Company by encouraging these individuals to acquire shares in the Company and thereby remain associated with, and seek to maximize the value of, the Company. Under the plan, the number of shares reserved for issuance pursuant to the exercise of all options under the plan may not exceed 10% of the issued and outstanding common shares on a non-diluted basis at any time. The options expire not more than five years from the date of grant, or earlier if the individual ceases to be associated with the Company, and vest over terms determined at the time of grant.

During the nine months ended September 30, 2016, the Company granted options to purchase 753,337 common shares, the options will vest equally over three years with the first tranche vesting one year after the grant date. The fair value of the options was estimated at $360,811 ($0.48 per option) using the Black-Scholes pricing model.

8. Share-based compensation (continued)

The following tables summarize information about stock options outstanding as at:

	September 30, 2016		*December 31, 2015*	
	Options	***Weighted – average exercise price***	*Options*	*Weighted – average exercise price*
Opening	**6,749,700**	**$1.59**	4,113,370	$1.90
Granted	**753,337**	**0.75**	3,646,173	1.35
Exercised	**–**	**–**	–	–
Expired	**(533,337)**	**2.20**	(728,388)	2.08
Forfeited	**(68,334)**	**0.86**	(281,455)	2.22
Closing	**6,901,366**	**$1.48**	6,749,700	$1.59

The following provides a summary of the stock option plan as at September 30, 2016:

Range of exercise price	*Number outstanding*	*Weighted-average remaining contractual life (years)*	*Weighted-average exercise price*	*Number exercisable*
$ 0.50 – $ 1.00	**2,335,008**	**3.56**	**$ 0.75**	**601,672**
$ 1.01 – $ 1.50	**908,344**	**1.95**	**1.19**	**680,010**
$ 1.51 – $ 2.00	**2,676,340**	**3.20**	**1.81**	**1,151,002**
$ 2.01 – $ 2.50	**333,334**	**2.41**	**2.28**	**333,334**
$ 2.51 – $ 3.00	**648,340**	**2.50**	**2.70**	**432,227**
	6,901,366	**3.05**	**$ 1.49**	**3,198,245**

The following provides a summary of the stock option plan as at December 31, 2015:

Range of exercise price	*Number outstanding*	*Weighted-average remaining contractual life (years)*	*Weighted-average exercise price*	*Number exercisable*
$ 0.50 – $ 1.00	1,865,005	4.07	$ 0.75	520,005
$ 1.01 – $ 1.50	680,010	1.68	1.18	680,010
$ 1.51 – $ 2.00	2,711,340	3.84	1.81	380,556
$ 2.01 – $ 2.50	841,671	1.37	2.24	841,671
$ 2.51 – $ 3.00	651,674	3.25	2.70	217,225
	6,749,700	3.32	$ 1.59	2,639,467

8. Share-based compensation (continued)

The Black-Scholes pricing model was used to estimate the fair value of options granted based on the following significant assumptions:

	2016	*2015*
Weighted average exercise per option	**$0.90**	$1.35
Risk-free interest rate	**0.57% - 0.71%**	0.61% - 0.96%
Expected volatility	**68%**	64% - 66%
Expected life	**5 years**	5 years
Forfeiture rate	**5%**	5%
Weighted average fair value per option	**$0.48**	$0.63

9. Earnings (loss) per common share

Basic earnings (loss) per share was calculated as follows:	Three months ended September 30,		Nine months ended September 30,	
	2016	2015	**2016**	2015
Net income (loss) for the period	$ **(470,783)**	$ (2,353,636)	$ **10,507,948**	$ (4,611,111)
Weighted average number of shares (basic)				
Issued common shares at beginning of period	**67,681,804**	67,681,804	**67,681,804**	57,755,804
Effect of shares issued	**11,500,000**	–	**5,372,262**	4,799,384
Weighted average number of common shares - basic	**79,181,804**	67,681,804	**73,054,066**	62,555,188
Diluted earnings (loss) per share was calculated as follows:				
Weighted average number of shares (diluted)				
Weighted average number of shares (basic)	**79,181,804**	67,681,804	**73,054,066**	62,555,188
Effect of outstanding options	–	–	**379,908**	–
Weighted average number of common shares - diluted	**79,181,804**	67,681,804	**73,433,974**	62,555,188

The average market value of the Company's shares for purposes of calculating the dilutive effect of share options was based on quoted market prices for the period that the options were outstanding. Excluded from diluted earnings per share is the effect of 6,901,366 options as the Company is in a loss position for the three months ended September 30, 2016. For the nine months ended September 30, 2016, 4,111,351 options are excluded as they are out of the money.

10. Change in non-cash working capital

	Three months ended September 30,		Nine months ended September 30,	
	2016	2015	**2016**	2015
Accounts receivable	$ **(469,812)**	$ (1,107,453)	$ **2,349,556**	$ 926,365
Prepaid expenses and deposits	**239,714**	(309,974)	**(699,570)**	(528,574)
Accounts payable and accrued liabilities	**6,064,672**	6,918,954	**(2,603,561)**	(7,969,248)
	$ **5,834,574**	$ 5,501,527	$ **(953,575)**	$ (7,571,457)

The changes in non-cash working capital has been allocated to the following activities:

Operating	$ **1,534,201**	$ 433,052	$ **(199,810)**	$ (2,091,226)
Financing	–	–	–	69,859
Investing	**4,300,373**	5,068,475	**(753,765)**	(5,550,090)
	$ **5,834,574**	$ 5,501,527	$ **(953,575)**	$ (7,571,457)

11. Related party disclosure

The condensed consolidated interim financial statements include the financial statements of the Company and the subsidiary listed below:

Name	*Country of Incorporation*	*% equity interest* *2016*	*2015*
Yangarra Resources Corp.	Canada	100%	100%

Balances between the Company and its subsidiary have been eliminated on consolidation and are not disclosed in this note. Details of transactions between the Company and other related parties are disclosed below.

During the nine months ended September 30, 2016 and 2015, the Company was charged or invoiced the following amounts by certain of its officers and directors and by companies controlled by certain of the Company's officers and directors:

	Three months ended September 30,		Nine months ended September 30,	
	2016	2015	**2016**	2015
Administration and consulting fees	$ **64,136**	$ 107,502	$ **234,083**	$ 260,806
Production and capital expenditures	**85,683**	19,556	**219,863**	74,651
	$ **149,819**	$ 127,058	$ **453,946**	$ 335,457

Included in accounts payable and accrued liabilities at September 30, 2016 is $14,184 (December 31, 2015 - $6,207) relating to the above transactions. These transactions were in the normal course of operations and were measured at fair value.

Other long-term liabilities include a mortgage for $222,052 (December 31, 2015 - $252,228) held in the name of an officer of the Company for a property that is used as a field office. The Company is the beneficial owner through a trust agreement of the property against which the mortgage is secured. All mortgage payments are made by the Company.

12. Financial instruments and financial risk management

The Company's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to market conditions and the Company's activities. The Company has exposure to credit risk, liquidity risk and market risk as a result of its use of financial instruments. This note presents information about the Company's exposure to each of the above risks and the Company's objectives, policies and processes for measuring and managing these risks. Further quantitative disclosures are included throughout these financial statements. The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. The Board of Directors has implemented and monitors compliance with the risk management policies as set out herein:

a. Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations. A substantial portion of the Company's accounts receivable are with natural gas and liquids marketers and partners on joint operations in the oil and gas industry and are subject to normal industry credit risks.

Purchasers of the Company's natural gas and liquids are subject to credit review to minimize the risk of non-payment. As at September 30, 2016, the maximum credit exposure is the carrying amount of the accounts receivable of $7,932,361 (December 31, 2015 – $10,281,917) and $441,445 of commodity contracts (December 31, 2015 – $2,311,910). The maximum exposure to credit risk for accounts receivable as at September 30, 2016 and December 31, 2015 by type of customer was:

		September 30, 2016		December 31, 2015
Natural gas and liquids marketers	$	**2,368,525**	$	1,978,912
Partners on joint operations		**4,349,244**		5,861,464
Realized commodity contracts		**150,504**		684,955
Other		**1,064,088**		1,756,586
	$	**7,932,361**	$	10,281,917

Receivables from natural gas and liquids marketers are typically collected on the 25th day of the month following production. The Company has mitigated the credit risk associated with the natural gas and liquids marketer through a security arrangement with Computershare. The Company historically has not experienced any significant collection issues with its natural gas and liquids marketers. All of the revenue accruals and receivables from natural gas and liquids marketers were received in October 2016.

12. Financial instruments and financial risk management (continued)

Receivables from partners on joint operations are typically collected within one to three months of the bill being issued to the partner. The Company mitigates the risk from receivables from partners on joint operations by obtaining partner approval of capital expenditures prior to starting a project. However, the receivables are from participants in the petroleum and natural gas sector, and collection is dependent on typical industry factors such as commodity price fluctuations, escalating costs and the risk of unsuccessful drilling. Further risk exists with partners on joint operations as disagreements occasionally arise which increases the potential for non-collection. For properties that are operated by the Company, production can be withheld from partners on joint operations who are in default of amounts owing. In addition, the Company often has offsetting amounts payable to partners on joint operations from which it can net receivable balances.

As at September 30, 2016 and December 31, 2015, the Company considers its receivables to be aged as follows:

		September 30, 2016		December 31, 2015
Under 30 days	$	**3,591,350**	$	3,918,880
30 to 60 days		**195,622**		30,585
60 to 90 days		**68,955**		100,085
Over 90 days		**4,076,434**		6,232,367
	$	**7,932,361**	$	10,281,917

90% of the over 90 day receivables are made up of two industry partners. The Company has performed an analysis of each partner's financial situation and have determined they have the ability to pay. Included in the over 90 day receivables are balances that are currently in dispute with one of the industry partners (see note 15). The Company did not provide for any doubtful accounts nor was it required to write-off any accounts receivable during the nine months ended September 30, 2016.

b. Liquidity risk

Liquidity risk is the risk that the Company will incur difficulties meeting its financial obligations as they are due. The Company's approach to managing liquidity is to ensure, as far as possible, that it will have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions without incurring unacceptable losses or risking harm to the Company's reputation. The Company prepares annual capital expenditure budgets, which are regularly monitored and updated as considered necessary. The Company uses authorizations for expenditures on both operated and non-operated projects to further manage capital expenditures.

To facilitate the capital expenditure program, the Company has a credit facility agreement which is regularly reviewed by the lender. The Company monitors its total debt position monthly. The Company also attempts to match its payment cycle with collection of petroleum and natural gas revenues on the 25th of each month. The Company anticipates it will have adequate liquidity to fund its financial liabilities through its future cash flows and availability on bank facilities. The Company's financial liabilities are comprised of accounts payable and accrued liabilities, interest rate contracts, commodity contracts, other long-term liabilities and bank debt, which are classified as current or non-current on the condensed consolidated interim statement of financial position based on their maturity dates.

The Company intends to fund the 2016 budget with cash flow from operations and the availability on the revolving operating demand loan (see note 5).

12. Financial instruments and financial risk management (continued)

As at September 30, 2016, the contractual maturities of the Company's obligations are as follows:

	Carrying Amount	Contractual Cash Flows	Less than 1 year	1-2 Years	2-5 Years	More than 5 years
Accounts payable and accrued liabilities	9,718,971	9,718,971	9,718,971	–	–	–
Bank debt [(1)]	60,586,018	60,586,018	60,586,018	–	–	–
Other long-term liabilities	222,052	222,052	41,852	43,611	136,589	–
Commodity contracts	83,558	83,558	83,558	–	–	–
Interest rate contract	471,052	471,052	275,252	195,800	–	–
	71,081,651	71,081,651	70,705,651	239,411	136,589	–

c. Market risk

Market risk consists of interest rate risk, currency risk and commodity price risk. The objective of market risk management is to manage and control market risk exposures within acceptable limits, while maximizing returns. The Company may use both financial derivatives and physical delivery sales contracts to manage market risks. All such transactions are conducted in accordance with a risk management policy as set out herein:

i. Interest rate risk

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. The Company is exposed to interest rate fluctuations on its bank debt which bears interest at a floating rate and to mitigate this risk, the Company has entered into interest rate contracts. For the nine months ended September 30, 2016, if interest rates (including the effect of the interest rate contract) had been 1% lower with all other variables held constant, income for the period would have been $160,090 (September 30, 2015 - $129,715) higher, due to lower interest expense. An equal and opposite impact would have occurred had interest rates been higher by the same amount.

12. Financial instruments and financial risk management (continued)

The Company had the following interest rate contracts in place at September 30, 2016:

Contracts		Fair Value
Pay a 2.35% fixed rate (plus a 2.25% credit spread) on $10 million (October 2016 - June 2018)	$	(258,263)
Pay a 2.15% fixed rate (plus a 2.25% credit spread) on $10 million (October 2016 - May 2018)	$	(212,789)
	$	(471,052)

ii. Currency risk

Foreign currency exchange rate risk is the risk that the fair value or future cash flows will fluctuate as a result of changes in foreign exchange rates. All of the Company's petroleum and natural gas sales are denominated in Canadian dollars, however, the underlying market prices in Canada for petroleum and natural gas are impacted by changes in the exchange rate between the Canadian and United States dollar. The Company had no outstanding forward exchange rate contracts in place at September 30, 2016.

iii. Commodity price risk

Commodity price risk is the risk that the fair value or future cash flows will fluctuate as a result of changes in commodity prices. Commodity prices for petroleum and natural gas are impacted by world economic events that dictate the levels of supply and demand as well as the relationship between the Canadian and United States dollar, as outlined above.

As at September 30, 2016, the Company was committed to the following commodity price risk contracts:

Contracts		Fair Value
Oil		
400 bbl/d January to December 2016 in a collar with a $73.45 CDN/bbl floor and a $85.00 CDN/bbl ceiling	$	525,003
200 bbl/d October 2016 to March 2017 at C$64.45 WTI/bbl		(28,983)
400 bbl/d January to December 2016 Edmonton par differential swap at $3.95 US/bbl		(54,575)
Total	$	441,445

12. Financial instruments and financial risk management (continued)

The following table summarizes the sensitivity of the fair value of the Company's derivative positions as at September 30, 2016 to fluctuations in commodity prices, with all other variables held constant. When assessing the potential impact of these commodity price changes, the Company believes 10 percent volatility in commodity prices is a reasonable measure ($4.71/bbl for oil). Fluctuations in commodity prices potentially could have resulted in unrealized gains (losses) impacting income before tax as follows:

	Impact on Income Before Tax	
	Increase 10%	Decrease 10%
Crude oil	(455,099)	455,099

13. Capital disclosures

The Company's objective when managing capital is to maintain a flexible capital structure which will allow it to execute its capital expenditure program, which includes expenditures in oil and gas activities which may or may not be successful. Therefore, the Company monitors the level of risk incurred in its capital expenditures to balance the proportion of debt and equity in its capital structure.

The Company considers its capital structure to include shareholders equity and debt:

		September 30, 2016		*December 31, 2015*
Shareholders' equity	$	**183,627,034**	$	161,133,141
Bank debt	$	**60,586,018**	$	62,131,258

The Company monitors capital based on annual cash from operations before changes in non-cash working capital and capital expenditure budgets, which are updated as necessary and are reviewed and periodically approved by the Board of Directors.

The Company manages its capital structure and makes adjustments by continually monitoring its business conditions including the current economic conditions, the risk characteristics of the Company's petroleum and natural gas assets, the depth of its investment opportunities, current and forecasted net debt levels, current and forecasted commodity prices and other facts that influence commodity prices and funds from operations such as quality and basis differentials, royalties, operating costs and transportation costs.

In order to maintain or adjust the capital structure, the Company considers its forecasted cash from operations before changes in non-cash working capital while attempting to finance an acceptable capital expenditure program including acquisition opportunities, the current level of bank debt available from the Company's lender, the level of bank debt that may be attainable from its lender as a result of petroleum and natural gas reserve growth, the availability of other sources of debt with different characteristics than existing debt, the sale of assets, limiting the size of the capital expenditure program and the issue of new equity if available on favorable terms. At September 30, 2016, the Company's capital structure was subject to the banking covenants disclosed in note 5. No changes were made to the capital policy in 2016.

14. Finance expenses

During the three and nine months ended September 30, 2016 and 2015, the following items were included in the finance expense on the condensed consolidated interim statements of income and comprehensive income:

	Three months ended September 30,		Nine months ended September 30,	
	2016	2015	**2016**	2015
Interest & finance costs	$ **449,936**	$ 426,516	$ **1,580,145**	$ 1,511,301
Realized loss on interest rate contracts	**68,655**	68,889	**206,606**	184,081
Change in fair value of interest rate contracts	**(73,719)**	19,013	**(201,970)**	305,047
Accretion *(note 6)*	**43,853**	45,112	**141,858**	127,307
	$ **488,725**	$ 559,530	$ **1,726,639**	$ 2,127,736

15. Contingency

In 2016, the Company served an industry partner with a Statement of Claim issued from The Court of Queen's Bench of Alberta, by which the Company claims production was misallocated on a number of wells the industry partner was operating. The industry partner has filed a Statement of Defense. The potential outcome of the lawsuit and claims are uncertain, however, they could be material.

In the normal conduct of operations, there are other pending claims by and against the Company. Litigation is subject to many uncertainties, and the outcome of individual matters is not predictable with assurance. In the opinion of management, based on the advice and information provided by its legal counsel, the final determination of these other litigations will not materially affect the Company's financial position or results of operations.

16. Commitments

The Company has entered into lease agreements for office premises and Company vehicles with estimated minimum annual payments as follows:

2016	$	92,357
2017	$	370,505
2018	$	374,175
2019	$	323,138
2020	$	332,439
Thereafter	$	126,198

As at September 30, 2016 the Company has satisfied the entire 12,001,300 CEE flow-through commitment.