SEVEN GENERATIONS

E N E R G Y

# Consolidated Financial Statements

For the years ended December 31, 2017 and 2016

March 13, 2018

# Independent Auditor's Report

**To the Shareholders of**
**Seven Generations Energy Ltd.**

We have audited the accompanying consolidated financial statements of Seven Generations Energy Ltd. and its subsidiaries, which comprise the consolidated balance sheets as at December 31, 2017 and December 31, 2016 and the consolidated statements of comprehensive income (loss), changes in equity and cash flows for the years then ended, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

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

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

**Opinion**
In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Seven Generations Energy Ltd. and its subsidiaries as at December 31, 2017 and December 31, 2016 and their financial performance and their cash flows for the years then ended in accordance with International Financial Reporting Standards.

PricewaterhouseCoopers LLP

**Chartered Professional Accountants**

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"PwC" refers to PricewaterhouseCoopers LLP, an Ontario limited liability partnership.

**SEVEN GENERATIONS ENERGY LTD.**

**Consolidated Balance Sheets**

(millions of Canadian dollars)

| As at December 31, | Notes | 2017 | 2016 |
|---|---|---|---|
| **Assets** | | | |
| **Current assets** | | | |
| Cash and cash equivalents | 6 | **$ 165.3** | $ 630.8 |
| Accounts receivable | 7 | **302.7** | 181.9 |
| Risk management contracts | 10 | **36.2** | — |
| Deposits and prepaid expenses | | **18.8** | 17.7 |
| | | **523.0** | 830.4 |
| Risk management contracts | 10 | **36.1** | — |
| Oil and natural gas assets | 8 | **6,733.0** | 5,750.1 |
| Investment in associate | 9 | **2.4** | 21.9 |
| | | **7,294.5** | 6,602.4 |
| **Liabilities** | | | |
| **Current liabilities** | | | |
| Accounts payable and accrued liabilities | | **377.3** | 244.5 |
| Risk management contracts | 10 | **17.5** | 71.7 |
| | | **394.8** | 316.2 |
| Risk management contracts | 10 | **16.5** | 77.7 |
| Senior notes | 12 | **1,956.4** | 2,111.9 |
| Other long-term liabilities | 13 | **198.0** | 165.0 |
| Deferred income taxes | 14 | **278.4** | 108.8 |
| | | **2,844.1** | 2,779.6 |
| **Equity** | | | |
| Share capital | 15 | **3,864.4** | 3,830.5 |
| Contributed surplus | | **100.6** | 69.4 |
| Retained earnings (Deficit) | | **485.4** | (77.1) |
| | | **4,450.4** | 3,822.8 |
| | | **$ 7,294.5** | $ 6,602.4 |

Commitments and contingencies (Note 23)

See accompanying notes to the consolidated financial statements.

Approved on behalf of the Board of Directors:

*signed "Dale Hohm"*
Dale Hohm
Director

*signed "Kent Jespersen"*
Kent Jespersen
Director

**SEVEN GENERATIONS ENERGY LTD.**

**Consolidated Statements of Comprehensive Income (Loss)**

(millions of Canadian dollars)

| For the year ended December 31, | Notes | 2017 | 2016 |
|---|---|---|---|
| **Revenues** | | | |
| Liquids and natural gas sales | 18 | **$ 2,207.3** | $ 1,246.9 |
| Royalties expense | | **(62.1)** | (6.7) |
| | | **2,145.2** | 1,240.2 |
| **Risk management contracts** | | | |
| Realized gain | 10 | **15.7** | 90.8 |
| Unrealized gain (loss) | 10 | **186.7** | (271.6) |
| **Other income** | | **5.9** | 4.7 |
| | | **2,353.5** | 1,064.1 |
| **Expenses** | | | |
| Operating expenses | 19 | **357.8** | 181.9 |
| Transportation, processing and other | 20 | **371.4** | 238.6 |
| General and administrative | | **46.0** | 47.1 |
| Depletion and depreciation | 8 | **730.2** | 483.6 |
| Stock-based compensation | 22 | **28.5** | 18.0 |
| Finance expense | 21 | **193.2** | 138.7 |
| Foreign exchange gain | | **(129.6)** | (18.2) |
| Loss on associate | 9 | **21.0** | 8.0 |
| | | **1,618.5** | 1,097.7 |
| **Income (loss) before taxes** | | **735.0** | (33.6) |
| **Income Taxes** | | | |
| Current income tax expense | 14 | **2.9** | 1.4 |
| Deferred income tax expense (recovery) | 14 | **169.6** | (8.8) |
| | | **172.5** | (7.4) |
| **Net income (loss) and comprehensive income (loss)** | | **$ 562.5** | $ (26.2) |
| **Net income (loss) per share** | | | |
| Basic | 17 | **$ 1.59** | $ (0.09) |
| Diluted | 17 | **$ 1.54** | $ (0.09) |

See accompanying notes to the consolidated financial statements.

**SEVEN GENERATIONS ENERGY LTD.**

**Consolidated Statements of Cash Flows**

(millions of Canadian dollars)

| For the year ended December 31, | Notes | 2017 | 2016 |
|---|---|---|---|
| **Operating activities** | | | |
| Net income (loss) for the period | | **562.5** | (26.2) |
| Items not affecting cash: | | | |
| Deferred income tax expense (recovery) | 14 | **169.6** | (8.8) |
| Depletion and depreciation | 8 | **730.2** | 483.6 |
| Unrealized loss (gain) on risk management contracts | 10 | **(186.7)** | 271.6 |
| Stock-based compensation | 22 | **28.5** | 18.0 |
| Non-cash finance expenses and other | 21 | **2.4** | 7.2 |
| Premium on redemption of senior notes | 21 | **37.2** | — |
| Loss on associate | 9 | **19.5** | 3.9 |
| Foreign exchange gain on senior notes and other | 12 | **(134.9)** | (16.7) |
| Prepaid processing fees on third-party facilities | 8 | **(21.0)** | — |
| Changes in non-cash working capital | 25 | **(53.0)** | (88.0) |
| Cash provided by operating activities | | **1,154.3** | 644.6 |
| **Financing activities** | | | |
| Redemption of US$700 million 8.25% senior notes | 12 | **(912.7)** | — |
| Issuance of US$700 million 5.375% senior notes | 12 | **859.7** | — |
| Issuance of common shares for cash | 15 | **—** | 1,047.7 |
| Share issuance costs | 15 | **—** | (43.7) |
| Exercise of equity compensation units | 15 | **25.0** | 55.7 |
| Changes in non-cash working capital | 25 | **—** | — |
| Cash provided by (used in) financing activities | | **(28.0)** | 1,059.7 |
| **Investing activities** | | | |
| Investments in oil and natural gas assets | 8 | **(1,651.4)** | (978.0) |
| Acquisitions | 8 | **—** | (505.1) |
| Investments in associates | 9 | **—** | (25.8) |
| Changes in non-cash working capital | 25 | **61.9** | 30.9 |
| Cash used in investing activities | | **(1,589.5)** | (1,478.0) |
| Foreign exchange loss on cash in foreign currencies | | **(2.3)** | (0.5) |
| Increase (decrease) in cash and cash equivalents | | **(465.5)** | 225.8 |
| Cash and cash equivalents, beginning of period | | **630.8** | 405.0 |
| Cash and cash equivalents, end of period | | **165.3** | 630.8 |

Supplementary disclosure of cash flow information (Note 25)

See accompanying notes to the consolidated financial statements.

**SEVEN GENERATIONS ENERGY LTD.**

**Consolidated Statements of Changes in Equity**

(millions of Canadian dollars)

| Year ended December 31, | Notes | 2017 | 2016 |
|---|---|---|---|
| **Share capital** | | | |
| Balance, beginning of period | | **$ 3,830.5** | $ 1,775.7 |
| Issuance of common shares | 15 | **—** | 1,047.7 |
| Issuance of common shares for Acquisition | 8 | **—** | 965.1 |
| Share issuance costs, net of deferred tax | 15 | **—** | (31.8) |
| Exercise of equity compensation units | 22 | **33.9** | 73.8 |
| Balance, end of period | | **3,864.4** | 3,830.5 |
| | | | |
| **Contributed surplus** | | | |
| Balance, beginning of period | | **69.4** | 61.8 |
| Stock-based compensation | 22 | **40.1** | 25.7 |
| Exercise of equity compensation units | 22 | **(8.9)** | (18.1) |
| Balance, end of period | | **100.6** | 69.4 |
| | | | |
| **Retained earnings (deficit)** | | | |
| Balance, beginning of period | | **(77.1)** | (50.9) |
| Net income for the period | | **562.5** | (26.2) |
| Balance, end of period | | **485.4** | (77.1) |
| | | | |
| **Total shareholders equity, beginning of period** | | **$ 3,822.8** | $ 1,786.6 |
| **Total shareholders equity, end of period** | | **$ 4,450.4** | $ 3,822.8 |

See accompanying notes to the consolidated financial statements.

**SEVEN GENERATIONS ENERGY LTD.**
**Notes to the Consolidated Financial Statements**
**As at and for the years ended December 31, 2017 and 2016**
(all tabular amounts in millions of Canadian dollars, except share and price information)


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## 1. NATURE OF BUSINESS

Seven Generations Energy Ltd. ("Seven Generations" or the "Company") is incorporated under the *Canada Business Corporations Act* and commenced operations in 2008. Seven Generations is a Canadian company focused on the exploration, development and production of condensate and natural gas properties in Western Canada. Seven Generations' principal place of business is located at 4400, 525 – 8 Avenue SW Calgary, AB T2P 1G1. The Company's class A voting common shares ("common shares") are publicly traded on the Toronto Stock Exchange under the symbol "VII". These consolidated financial statements were approved and authorized for issuance by the Board of Directors on March 13, 2018.

## 2. BASIS OF PREPARATION

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). They have been prepared on a historical cost basis, except for financial instruments which are measured at their estimated fair value. The Company's presentation currency is Canadian dollars and all amounts are reported in Canadian dollars unless noted otherwise. References to "US$" are to United States dollars. These consolidated financial statements include the accounts of Seven Generations and its wholly owned subsidiary, Seven Generations Energy (US) Corp. All inter-company transactions have been eliminated.

## 3. SIGNIFICANT ACCOUNTING POLICIES

### Financial instruments

All financial instruments are initially recognized at fair value on the consolidated balance sheet, with the exception of the senior notes which are recognized at amortized cost. The Company classifies each financial instrument into one of the following categories: "held for trading", "loans & receivables", "held to maturity", "equity investment" or "other financial liabilities".

The fair value measurement of the Company's financial instruments are classified according to the following hierarchy based on the amount of observable inputs used to value the instrument:

- Level 1 - Quoted prices are available in active markets for identical assets or liabilities at the reporting date.
- Level 2 - Values are based on inputs, including quoted forward prices for commodities, time value and volatility factors, which can be substantially observed in the marketplace but are not readily observable in an actively traded market.
- Level 3 - Valuation inputs that are not based on observable market data.

| Financial Instrument | Classification | Level Valuation | Measurement |
|---|---|---|---|
| **Assets** | | | |
| Cash and cash equivalents | Held for trading | Level 1 | **Fair value** |
| Accounts receivable | Loans & receivables | Level 3 | **Fair value** |
| Risk management contracts | Held for trading | Level 2 | **Fair value** |
| Investment in associate | Equity investment | Level 3 | **Equity method** |
| **Liabilities** | | | |
| Accounts payable and accrued liabilities | Other financial liabilities | Level 3 | **Fair value** |
| Risk management contracts | Held for trading | Level 2 | **Fair value** |
| Senior notes | Other financial liabilities | Level 2 | **Amortized cost** |

Transaction costs related to fair value through profit or loss instruments are immediately recognized in earnings. Transaction costs related to other financial liabilities are included in earnings or netted with the fair value of the financial instrument.

At each reporting date, the Company assesses whether there are any indicators that its financial assets are impaired. An impairment loss is only recognized if there is objective evidence that one or more events have had a negative impact on the estimated future cash flows of that asset. All impairment losses are recognized in the consolidated statement of comprehensive income (loss).

**Oil and natural gas assets**

Oil and natural gas assets are measured at cost less accumulated depletion, depreciation and accumulated impairment losses. Property, plant and equipment ("PP&E") represents all costs directly attributable to the development of oil and natural gas reserves after technical feasibility and commercial viability have been established. Exploration and evaluation assets ("E&E") are those investments for which technical feasibility and commercial viability have not yet been determined. The Company capitalizes these costs after the right to explore has been obtained, including geological and geophysical costs, land acquisition costs, drilling costs, and costs incurred for the completion and testing of exploration wells. Once technical feasibility and commercial viability have been established, E&E assets are tested for impairment and reclassified to PP&E. Technical feasibility and commercial viability are established when proved reserves are determined to exist and the Company has sanctioned the E&E assets for commercial development.

The majority of the Company's PP&E is depleted using the unit-of-production method based on estimated recoverable proved plus probable reserves. Natural gas reserves and production are converted to barrels of oil equivalent based upon the relative energy content (6:1). The depletion base includes capitalized costs, plus the estimated future costs required to develop the Company's estimated recoverable proved plus probable reserves, and excludes the cost of assets not yet available for use in the manner intended by management. Significant components, such as natural gas plants, are depreciated separately on a straight-line basis over their estimated useful lives. Corporate assets are depreciated over their estimated useful lives using the declining-balance method.

**Impairment**

Seven Generations reviews its oil and natural gas assets for indicators of impairment at each reporting date. For the purposes of the review, the Company's PP&E and E&E assets are grouped into cash-generating units ("CGUs") which are defined as the smallest group of assets that generates cash inflows that are largely independent of the cash inflows of other assets or group of assets. PP&E and E&E assets that are in the same CGU are combined. If impairment indicators exist, the CGU is tested for impairment and a loss is recognized if the carrying amount of the CGU exceeds its estimated recoverable amount.

The recoverable amount of the CGU is determined as the greater of its fair value less costs to sell ("FVLCTS") and value in use ("VIU"). FVLCTS is based on the amount obtainable from the sale of an asset or CGU in an arm's length transaction between knowledgeable parties, less the cost of disposal. In assessing VIU, the estimated future cash flows of the CGU are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and risks specific to the asset. The recoverable amounts of the Company's CGUs are generally estimated using discounted cash flows from the Company's proved plus probable reserves (Level 3 valuation) and/or imputed from relevant sales transactions on assets with similar geological and geographic characteristics (Level 3 valuation).

**Provisions**

Provisions are recognized when the Company has a present legal or constructive obligation as a result of a past event 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 rate that reflects current market assessments of the time value of money and the risks specific to the liability. The Company's provisions primarily consist of decommissioning obligations associated with the dismantling, decommissioning and site disturbance remediation activities for its oil and natural gas assets.

Decommissioning liabilities are measured at the present value of the expected cash outflow using the relevant risk-free rate. The liability is accreted in the consolidated statement of comprehensive income (loss) at each reporting date to reflect the passage of time. Actual expenditures incurred upon settlement of the obligations reduce the provision.

**Investment in associate**

The Company accounts for its investment in associate using the equity method of accounting as Seven Generations is considered to have significant influence. Significant influence is generally regarded as the ability to participate in the financial and operational decisions of the associate without having control or joint-control over the associate.

The carrying value of the investment in associate is increased or decreased for the Company's share of equity contributions and withdrawals, as well as the Company's share of income and losses, respectively. The carrying value of the Company's investment in associate is also reviewed for indicators of impairment at each reporting date. If indicators of impairment exist, the investment is tested for impairment and a loss is recognized if the carrying amount of the investment in associate exceeds its estimated recoverable amount. The estimated recoverable amount is primarily based on observable equity issuances made by the associate.

**Stock-based compensation**

The Company's stock-based compensation expense relates to stock options, performance warrants, performance share units ("PSUs"), restricted share units ("RSUs") and deferred share units ("DSUs") granted to employees, officers and directors of Seven Generations. Awards are measured at fair value on the date of grant and are expensed over the vesting periods.

The fair value of stock options and warrant grants are primarily determined using the Black-Scholes option pricing model.The fair value of DSUs, PSUs and RSUs are primarily based on the Company's share price on the date of grant. A forfeiture rate is estimated on the grant date and is adjusted to reflect the actual number of stock options, performance warrants, PSUs and RSUs that vest. DSUs are fully expensed at grant date because they vest immediately.

PSUs may be granted with certain market conditions that are determined by the Company's Board of Directors. If the Company satisfies the market conditions, a pre-determined adjustment factor is applied to the vested PSUs at the end of the performance period, based upon the relative share price performance of the Company compared to a peer group. The expense recognized over the PSU vesting period is the fair value of the PSUs with an estimated adjustment factor. If the actual adjustment factor is higher than estimated, an additional expense is recognized on vesting for the incremental fair value.

When equity compensation units are exercised or released, the consideration received, together with the expense previously recognized in contributed surplus, is recorded as an increase to share capital. The Company's stock-based compensation plans allow the holder of the award to receive cash or common shares at the Company's discretion, equal to the fair market value of the Company's common shares calculated at the date of such payment. Because the Company does not intend to settle in cash, the plans are accounted for as equity-settled share-based compensation arrangements.

**Cash and cash equivalents**

Cash and cash equivalents consist of cash on hand and other short-term highly liquid investments with a maturity of three months or less and are presented as a current asset on the balance sheet. GIC Collateral accounts are primarily used to secure letters of credit issued as security in respect of long-term transportation commitments.

**Income taxes**

Income tax is comprised of current and deferred taxes which are recognized in the statement of comprehensive income (loss), except when it relates to share capital, in which case, it is recognized directly in equity. Current income tax expense is the expected cash tax payable on the taxable income for the period, using tax rates that have been enacted or substantively enacted.

Deferred tax is recognized on temporary differences between the carrying value of assets and liabilities for financial reporting purposes and the tax values. Deferred income tax is determined on an undiscounted basis using tax rates that have been enacted or substantively enacted and that are expected to apply in future periods when the temporary differences are anticipated to reverse. A deferred tax asset is only recognized to the extent that it is probable that future taxable profits will be available against which the temporary differences can be utilized.

### Revenue

Revenue from the sale of condensate, natural gas, and natural gas liquids ("NGLs") is recognized when the risks and rewards of ownership of the products are transferred to the buyer.

### Foreign currency translation

Monetary assets and liabilities denominated in a foreign currency are translated at the rate of exchange in effect at the balance sheet date. Revenues and expenses are translated at the average exchange rates for the period. Gains and losses from foreign currency translations are recognized in the consolidated statement of comprehensive income (loss).

### Jointly operated assets

The Company's oil and natural gas activities include jointly operated oil and natural gas assets and liabilities. These consolidated financial statements include the Company's share of these jointly operated assets and liabilities and a proportionate share of the related revenue and expenses.

### Per share information

Basic per share information is calculated using the weighted average number of common shares outstanding during the period. Diluted per share information is calculated using the basic weighted average number of common shares outstanding during the period, adjusted for the potential number of shares which could have had a dilutive effect on net income (loss) during the period.

### Business combinations

Business combinations are accounted for using the acquisition method. Identifiable assets, liabilities and contingent liabilities assumed in a business combination are measured at their fair values at the acquisition date. The cost of an acquisition is measured as the fair value of the consideration paid, equity instruments issued and liabilities incurred or assumed at the acquisition date. The excess of the cost of the acquisition over the fair value of the identifiable assets, liabilities and contingent liabilities acquired is recorded as goodwill. If the cost of the acquisition is less than the fair value of the net assets acquired, the difference is recognized immediately as a gain in net income. Transaction costs associated with business combinations are expensed as incurred.

## 4. SIGNIFICANT ACCOUNTING JUDGMENTS, ESTIMATES AND ASSUMPTIONS

### Judgments

The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amount of assets, liabilities, revenues and expenses. Actual results may differ from these estimates.

Oil and natural gas assets are grouped into CGUs based on their ability to generate largely independent cash flows. The determination of the Company's CGUs is subject to management's judgment. The Company's oil and natural gas assets are currently held in one CGU. In addition, the Company applies judgment when determining the classification of oil and natural gas assets as PP&E or E&E assets. In making this determination, management considers various factors, including the existence of reserves, and whether the appropriate approvals have been received from regulatory bodies and the Company's Board of Directors.

The Company applies judgment in determining when the transfer of risks and rewards of ownership from the sale of condensate, natural gas and NGLs occurs. Revenues are generally recognized upon the transfer of asset title.

The determination of the Company's income tax and royalty liabilities requires interpretation of complex laws and regulations and are subject to measurement uncertainty. All tax filings are subject to audit and potential reassessment. In addition, the recoverability of loss carryforwards and investment tax credits are uncertain. The Company records deferred income tax assets and liabilities using income tax rates that are substantively enacted at the balance sheet date, which is subject to change.

### Estimates and assumptions

The amounts recorded for depletion of oil and natural gas assets are based on estimated reserves and future development costs. The estimated recoverable reserves and associated future cash flows are also key in determining if the Company's natural gas assets have been impaired. These estimates are subject to measurement uncertainty. The determination of reserves involves estimates for oil and natural gas volumes in place, recovery factors, production rates, future commodity prices and future royalty, operating, and capital costs. The Company's reserve estimates have been determined in accordance with the standards contained in the Canadian Oil and Gas Evaluation Handbook.

Impairment test calculations require the use of estimates and judgments including estimates relating to future commodity prices, quantity of reserves, expected production volumes, land values, discount rates, recovery factors and future development and operating costs.

The Company's provision for decommissioning liabilities are based on assumptions regarding the interpretation of current legal and constructive requirements as well as estimates of future costs and expected timing of remediation.

The Company's stock-based compensation expense is subject to measurement uncertainty as a result of estimates related to forfeiture rates, expected life and underlying volatility of the Company's common shares.

The estimated fair value of financial instruments are subject to measurement uncertainty. The fair value of financial instruments without an actively traded market are estimated using the Company's assessment of available market inputs and other assumptions. These estimates may vary from the actual prices that will be achieved upon settlement of the financial instruments.

## 5. NEW ACCOUNTING POLICIES

These consolidated financial statements follow the same accounting policies as the consolidated financial statements for the year ended December 31, 2016. The accounting pronouncements listed below will be adopted in future accounting periods:

- **IFRS 15 Revenue from Contracts with Customers** was issued in May 2014 and replaces IAS 18 Revenue, IAS 11 Construction Contracts, and related interpretations. IFRS 15 provides a single, five-step model to be applied to all contracts with customers. The standard requires an entity to recognize revenue to reflect the transfer of goods and services for the amount it expects to receive when control is transferred to the purchaser. 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 early adoption permitted.

  Seven Generations will retrospectively adopt IFRS 15 on January 1, 2018. The Company has determined that there will not be any material changes in the measurement or timing of revenue recognition as a result of IFRS 15. However, the Company will expand disclosures to its consolidated financial statements as prescribed by IFRS 15.

- **IFRS 9 Financial Instruments** was issued in July 2014 and replaces IAS 39 Financial Instruments: Recognition and Measurement and uses a single approach to determine whether a financial asset is measured at amortized cost or fair value, and replaces multiple rules in IAS 39. The standard will come into effect for annual periods beginning on or after January 1, 2018, with earlier adoption permitted.

  Seven Generations will retrospectively adopt IFRS 9 on January 1, 2018. The Company has determined that there will not be any material changes in the disclosure, measurement or carrying value of the Company's financial instruments as a result of the adoption of IFRS 9.

- **IFRS 16 Leases** was issued in January 2016 and replaces IAS 17 Leases. For lessees applying IFRS 16, a single recognition and measurement model for leases would apply, with required recognition by lessees of assets and liabilities for most leases, including subleases. The standard will come into effect for annual periods beginning on or after January 1, 2019, with earlier adoption permitted if the entity is also applying IFRS 15 Revenue from Contracts with Customers. The standard is required to be adopted either retrospectively or using a modified retrospective approach.

  Seven Generations will adopt IFRS 16 on January 1, 2019. The Company is currently evaluating the impact of the standard on the consolidated financial statements. The Company has commenced its project planning and scoping phase and is in the process of identifying leases which fall within the scope of IFRS 16.

## 6. CASH AND CASH EQUIVALENTS

| As at December 31, | | 2017 | | 2016 |
|---|---|---|---|---|
| Cash | $ | **164.5** | $ | 325.5 |
| GIC Collateral accounts | | **—** | | 59.2 |
| Short-term investments[1] | | **0.8** | | 246.1 |
| Cash and cash equivalents | $ | **165.3** | $ | 630.8 |

(1) As at December 31, 2017, the short term investments bore interest at a weighted average rate of 1.35% (December 31, 2016 - 0.8%)

As at December 31, 2017, the credit risk associated with the Company's cash and cash equivalents balances was considered low as the balances were held with two large Canadian chartered banks.

## 7. ACCOUNTS RECEIVABLE

| As at December 31, | 2017 | 2016 |
|---|---|---|
| Oil and natural gas sales | **$ 243.2** | $ 137.8 |
| GST, royalty recoveries and other | **46.5** | 42.5 |
| Joint venture billings | **13.0** | 1.6 |
| Accounts receivable | **$ 302.7** | $ 181.9 |

As at December 31, 2017, management believes collection risk on the outstanding accounts receivable balances was low given the high credit quality of the Company's material counterparties and history of collections. There were no material amounts past due as at December 31, 2017.

## 8. OIL AND NATURAL GAS ASSETS

| | Exploration and evaluation | Developed and producing | Other assets | Total |
|---|---|---|---|---|
| **Cost** | | | | |
| Balance at December 31, 2015 | $ 222.6 | $ 3,423.0 | $ 12.2 | **$ 3,657.8** |
| Acquisition | 300.0 | 1,772.3 | — | **2,072.3** |
| Additions | — | 976.1 | 1.9 | **978.0** |
| Dispositions | — | (6.0) | — | **(6.0)** |
| Transfers from E&E to PP&E | (11.0) | 11.0 | — | **—** |
| Non-cash capitalized costs[(1)] | — | 75.9 | — | **75.9** |
| Balance at December 31, 2016 | 511.6 | 6,252.3 | 14.1 | **6,778.0** |
| Additions | 19.6 | 1,628.3 | 3.5 | **1,651.4** |
| Transfers from E&E to PP&E | (200.0) | 200.0 | — | **—** |
| Prepaid processing fees on third-party facilities | — | — | 21.0 | **21.0** |
| Non-cash capitalized costs[(1)] | — | 41.3 | — | **41.3** |
| Balance at December 31, 2017 | 331.2 | 8,121.9 | 38.6 | **8,491.7** |
| **Accumulated depletion and depreciation** | | | | |
| Balance at December 31, 2015 | — | 541.0 | 3.3 | **544.3** |
| Depletion and depreciation | — | 481.5 | 2.1 | **483.6** |
| Balance at December 31, 2016 | — | 1,022.5 | 5.4 | **1,027.9** |
| Amortization of prepaid processing expenses | — | — | 0.6 | **0.6** |
| Depletion and depreciation | 4.5 | 724.1 | 1.6 | **730.2** |
| Balance at December 31, 2017 | $ 4.5 | $ 1,746.6 | $ 7.6 | **$ 1,758.7** |
| **Net book value** | | | | |
| Balance at December 31, 2016 | $ 511.6 | $ 5,229.8 | $ 8.7 | **$ 5,750.1** |
| Balance at December 31, 2017 | $ 326.7 | $ 6,375.3 | $ 31.0 | **$ 6,733.0** |

(1) For the year ended December 31, 2017, non-cash capitalized costs consisted of $29.7 million of decommissioning obligation assets and $11.6 million of stock-based compensation (year ended December 31, 2016 - $68.0 million and $7.7 million).

On August 18, 2016, the Company acquired assets for consideration valued at $1.9 billion at the time of announcement (the "Acquisition"). In connection with the Acquisition, the Company acquired $2.1 billion of oil and natural gas assets, assumed US $450.0 million of senior unsecured notes (Note 12) and assumed $10.7 million of decommissioning liabilities (Note 13). Consideration for the net assets acquired included the issuance of 33.5 million common shares (Note 15), $505.1 million of cash and $6.0 million of undeveloped acreage. The Acquisition also included approximately $2.4 billion of take or pay commitments assumed by Seven Generations.

During the year ended December 31, 2017, the Company invested $21.0 million to upgrade a third-party processing facility under the terms of a long-term processing agreement assumed by Seven Generations as part of the Acquisition. The prepaid expenditures were capitalized and will be amortized to processing expenses over the 20 year term of the agreement.

As at December 31, 2017, $339.7 million in oil and natural gas assets were not subject to depletion and depreciation as they were not ready for use in the manner intended by management (December 31, 2016 - $503.7 million).

In the fourth quarter of 2017, Seven Generations sanctioned the development of the Nest 3 exploration area within the Kakwa River Project ("Nest 3"). With technical feasibility and commercial viability having been established through delineation drilling and other exploration activities, the $200.0 million carrying value of Nest 3 was transferred into the Company's developing and producing assets.

In the fourth quarter of 2017, Seven Generations identified indicators of impairment as a result of declines in the forecasted commodity prices utilized in the Company's 2017 reserve report, compared to the prior year. Seven Generations performed an impairment test on the Kakwa River Project using after-tax discounted future cash flows with a two percent inflation rate and a discount rate of 10%. As at December 31, 2017, the recoverable value of the Kakwa River Project exceeded its carrying value, and no impairment was identified. The following table summarizes the price forecast used in the Company's discounted cash flow estimates:

| | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | 2025 | 2026 | 2027 | Thereafter |
|---|---|---|---|---|---|---|---|---|---|---|---|
| WTI (US$/bbl) | 58.50 | 58.70 | 62.40 | 69.00 | 73.10 | 74.50 | 76.00 | 77.50 | 79.10 | 80.70 | **+2% per year** |
| Henry Hub (US$/MMBtu) | 3.00 | 3.05 | 3.25 | 3.55 | 3.80 | 3.85 | 3.95 | 4.00 | 4.10 | 4.15 | **+2% per year** |
| AECO Spot Price ($/MMBtu) | 2.25 | 2.65 | 3.05 | 3.40 | 3.60 | 3.65 | 3.75 | 3.80 | 3.90 | 3.95 | **+2% per year** |
| US$ to C$ | 0.790 | 0.790 | 0.800 | 0.825 | 0.850 | 0.850 | 0.850 | 0.850 | 0.850 | 0.850 | **0.850** |

## 9. INVESTMENT IN ASSOCIATE

In 2016, Seven Generations invested $25.8 million for a 34.0% equity interest in Steelhead LNG Limited Partnership ("Steelhead LNG"), a Vancouver-based energy company focused on the development of LNG projects in British Columbia. Concurrent with the investment, the Company also entered into a development arrangement with Steelhead LNG, whereby the Company agreed to contribute $3.0 million in cash upfront and committed to invest up to an additional $9.0 million to participate in the pre-development of transportation alternatives to the west coast of British Columbia. As at December 31, 2017, the Company held a 24.4% equity interest in Steelhead LNG as a result of subsequent equity issuances to other parties.

The following table summarizes the change in the carrying value of the Company's investment in Steelhead LNG:

| For the year ending December 31, | 2017 | 2016 |
|---|---|---|
| Balance, beginning of year | **$ 21.9** | $ — |
| Investment in Steelhead LNG equity units | **—** | 25.8 |
| Recovery from additional equity units issued to Seven Generations | **4.2** | — |
| Share of Steelhead LNG's net loss | **(9.3)** | (3.9) |
| Impairment loss | **(14.4)** | — |
| Balance, end of year | **$ 2.4** | $ 21.9 |

The following table summarizes the Company's net loss on the investment in associate:

| For the year ending December 31, | 2017 | 2016 |
|---|---|---|
| Share of Steelhead LNG's net loss | **$ 9.3** | $ 3.9 |
| Midstream expenses incurred by Seven Generations | **1.5** | 4.1 |
| Recovery from additional equity units issued to Seven Generations | **(4.2)** | — |
| Impairment loss | **14.4** | — |
| Loss on associate | **$ 21.0** | $ 8.0 |

In 2017, Seven Generations agreed to provide a portion of the guarantee for Steelhead LNG's $14.9 million credit facility which is currently being used to fund its operations (Seven Generation's portion of the total guarantee is $5.4 million). The credit facility matures on April 11, 2018 and may be further extended.

In 2017, Seven Generations identified indicators of impairment for its investment in Steelhead LNG primarily due to the value of consideration received by Steelhead LNG in exchange for equity units that were issued by the entity during the fourth quarter of 2017. The Company tested the asset for impairment and determined that its Steelhead LNG investment may not be fully recoverable. The Company recognized an impairment loss of $14.4 million. The recoverable value of the investment was primarily based on the price of the equity units issued.

## 10. RISK MANAGEMENT CONTRACTS

The Company periodically enters into risk management contracts to manage its commodity price, foreign currency and interest rate exposure. The Company had the following risk management contracts in place as at December 31, 2017:

| | Crude Oil | | | | | | Natural Gas | | | | Foreign Exchange | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | C$ WTI Collars | | C$ WTI 3 Way Collars | | US$ WTI Collars | | Chicago Citygate Swaps | | AECO 7A Collars/ Swaps | | C$/US$ Swaps | |
| Period | bbl/d | C$/bbl | bbl/d | C$/bbl | bbl/d | US$/bbl | MMbtu/d | US$/ MMbtu | GJ/d | C$/GJ | US $MM | US$/C$ |
| **2018** | 17,250 | $61.20 - $77.32 | 12,000 | $40.83/$56.25/$75.54 | 2,000 | $52.25 - $57.30 | 205,000 | $2.88 | 60,000 | $2.44 - $2.85 | 215.1 | 1.3100 |
| **2019** | 16,000 | $58.91 - $75.94 | 7,500 | $41.00/$56.33/$75.92 | 2,000 | $52.25 - $57.30 | 120,000 | $2.85 | 60,000 | $2.44 - $2.85 | 124.8 | 1.2907 |
| **2020** | 7,000 | $57.50 - $71.61 | 1,500 | $40.00/$55.00/$70.98 | 2,000 | $52.25 - $57.30 | 32,500 | $2.74 | 10,000 | $2.13 - $2.13 | 32.5 | 1.2683 |

(1) The volumes and prices reported are the weighted average volumes and prices for the period.

The following is a summary of the carrying value of risk management contracts in place by contract type:

| As at December 31, | 2017 | 2016 |
|---|---|---|
| Natural gas | **$ 70.2** | $ (70.0) |
| Oil | **(50.5)** | (71.0) |
| Foreign exchange swap | **18.6** | (8.4) |
| Net position asset (liability) | **$ 38.3** | $ (149.4) |

The Company's risk management contracts are subject to master netting agreements that create the legal right to settle on a net basis. The following is a summary of financial instruments that are subject to offsetting:

| | 2017 | | | 2016 | | |
|---|---|---|---|---|---|---|
| As at December 31, | Derivative Asset | Derivative Liability | Net | Derivative Asset | Derivative Liability | Net |
| **Balance sheet classification** | | | | | | |
| Current asset | **$ 44.1** | **$ (7.9)** | **$ 36.2** | $ — | $ — | $ — |
| Long-term asset | **37.5** | **(1.4)** | **36.1** | — | — | — |
| Current liability | **3.3** | **(20.8)** | **(17.5)** | 1.5 | (73.2) | (71.7) |
| Long-term liability | **3.4** | **(19.9)** | **(16.5)** | 3.6 | (81.3) | (77.7) |
| Net position asset (liability) | **$ 88.3** | **$ (50.0)** | **$ 38.3** | $ 5.1 | $ (154.5) | $ (149.4) |

As the Company operates in Canada and the United States, fluctuations in foreign exchange rates can have a significant effect on the Company's liquids and natural gas sales. An increase in the value of the Canadian dollar, compared to the US dollar, will generally reduce the prices received by the Company for its liquids and natural gas sales. The Company manages foreign currency exchange risk relating to its oil and natural gas sales by entering into a variety of foreign exchange risk management contracts.

The following table demonstrates the impact of changes in commodity pricing and changes in the foreign exchange rate on net income before tax, based on risk management contracts in place as at December 31, 2017:

| As at December 31, 2017 | Gain (Loss) |
|---|---|
| 10% increase in C$ WTI/bbl | **$ (119.8)** |
| 10% decrease in C$ WTI/bbl | **96.9** |
| 10% increase in US$ Chicago Citygate/MMbtu | **(46.3)** |
| 10% decrease in US$ Chicago Citygate/MMbtu | **46.3** |
| 10% increase in C$ AECO/GJ | **(7.0)** |
| 10% decrease in C$ AECO/GJ | **7.2** |
| 10% increase in US$ to C$ | **(49.1)** |
| 10% decrease in US$ to C$ | **$ 49.1** |

Refer to Note 12 for information on the Company's exposure to foreign exchange rate fluctuations related to the senior notes.

## 11. BANK DEBT

During the second quarter of 2017, Seven Generations expanded its existing undrawn senior secured credit facility from $1.1 billion to $1.4 billion (the "Credit Facility"). As part of the amendments, the Credit Facility was transitioned from a reserve-based structure to a covenant-based structure that matures on June 9, 2021.

The Credit Facility is secured by a floating charge over the Company's assets and contains certain covenants that limit the Company's ability to, among other things: incur additional indebtedness; create or permit liens to exist; and make certain dispositions and transfers of assets. The following two financial covenants are associated with the Credit Facility:

- Senior Secured Net Debt to Adjusted EBITDA Ratio - cannot exceed 2.50:1
- Adjusted EBITDA to Interest Expense Ratio - cannot be less than 2.50:1

For the purposes of the covenant calculation, Adjusted EBITDA is calculated as net income (loss) before interest, income taxes, depletion, depreciation and amortization, adjusted for certain non-cash, extraordinary and non-recurring items. Senior Secured Net Debt consists of amounts drawn under the Credit Facility (excluding the balance of the unsecured senior notes), less cash and cash equivalents.

As at December 31, 2017, the Company was in compliance with the covenants under the Credit Facility. The Senior Secured Net Debt to Adjusted EBITDA Ratio and Adjusted EBITDA to Interest Expense Ratio were (0.09):1 and 7.81:1, respectively.

As at December 31, 2017, $42.1 million in letters of credit were issued and outstanding under the Credit Facility (December 31, 2016 – nil). During the fourth quarter of 2017, the Company also entered into a unsecured demand letter of credit facility of $76.4 million. As at December 31, 2017, $60.5 million in letters of credit were issued and outstanding under the facility.

## 12. SENIOR NOTES

| As at December 31, | | 2017 | | 2016 |
|---|---|---|---|---|
| US$700 million 8.25% senior notes, due May 15, 2020 | **$** | **—** | $ | 939.9 |
| US$425 million 6.75% senior notes, due May 1, 2023 | | **533.2** | | 570.6 |
| US$450 million 6.875% senior notes, due June 30, 2023 | | **564.5** | | 604.2 |
| US$700 million 5.375% senior notes, due September 30, 2025 | **$** | **878.2** | $ | — |
| | | **1,975.9** | | 2,114.7 |
| Less unamortized debt issue costs | | **(24.3)** | | (25.5) |
| Plus unamortized premium | | **4.8** | | 22.7 |
| Balance, end of year | **$** | **1,956.4** | $ | 2,111.9 |

(1) The US dollar senior notes were translated into Canadian dollars at the period end exchange rate of US$1=C$1.25 (December 31, 2016 – US$1=C$1.34).

The senior notes are carried at amortized cost, net of premiums and transaction costs, and are accreted to their principal balance at maturity using the effective interest rate method. As at December 31, 2017, the fair value of senior notes was $2,059.2 million (December 31, 2016 - $2,254.0 million).

During the fourth quarter of 2017, Seven Generations completed refinancing transactions, repurchasing and redeeming all of the Company's outstanding US$700 million 8.25% senior unsecured notes due in 2020 (the "8.25% Notes") and completing a new debt offering of US$700 million 5.375% senior unsecured notes due in 2025 (the "5.375% Notes"). The refinancing transactions extended the Company's debt maturities and reduced the Company's combined effective interest rate on all of its senior unsecured notes to 6.3%. As part of the refinancing, the Company recognized financing expenses of C$37.1 million in respect of the tender and call premiums on the 8.25% Notes.

The following table summarizes the changes in senior notes arising from financing activities:

| For the year ending December 31, | | 2017 | | 2016 |
|---|---|---|---|---|
| Balance, beginning of year | **$** | **2,111.9** | $ | 1,546.8 |
| Redemption of US$700 million 8.25% senior notes[1] | | **(875.6)** | | — |
| Issuance of US$700 million 5.375% senior notes | | **859.7** | | — |
| Assumption of US$450 million 6.875% senior notes | | **—** | | 580.3 |
| Impact of foreign exchange gains on senior notes and other | | **(139.6)** | | (15.2) |
| Balance, end of year | **$** | **1,956.4** | $ | 2,111.9 |

(1) Excludes redemption premium of C$37.1 million.

Following the repayment of the 8.25% Notes, the Company recognized a realized foreign exchange gain of $65.3 million for the year ended December 31, 2017. Since the dates of issuance for the $8.25% Notes in 2013 and 2014, the Company has recognized a cumulative net realized foreign exchange loss of $136.6 million. The Company has the option to redeem the senior notes at the following specified redemption prices:

| | US$700 5.375% million senior notes[1] | US$425 6.75% million senior notes[2] | US$450 6.875% million senior notes[3] |
|---|---|---|---|
| 2017 | **105.4%** | **106.8%** | **106.9%** |
| 2018 | **105.4%** | **105.1%** | **105.2%** |
| 2019 | **105.4%** | **103.4%** | **103.4%** |
| 2020 | **104.0%** | **101.7%** | **101.7%** |
| 2021 | **102.7%** | **100.0%** | **100.0%** |
| 2022 | **101.3%** | **100.0%** | **100.0%** |
| 2023 and thereafter | **100.0%** | **100.0%** | **100.0%** |

(1) The change in redemption price for the US$700 million 5.375% senior notes takes effect on September 30th of each year. Prior to September 30, 2020, the redemption option is only available if the 5.375% Notes are repaid using the proceeds of one or more equity offerings or by paying a make-whole premium represented by the present value of interest that would otherwise be payable over the remaining term of the debt in excess of the applicable redemption premium.
(2) The change in redemption price for the US$425 million 6.75% senior notes takes effect on May 1st of each year. Prior to May 1st, 2018, the redemption option is only available if the 6.75% Notes are repaid using the proceeds of one or more equity offerings or by paying a make-whole premium represented by the present value of interest that would otherwise be payable over the remaining term of the debt in excess of the applicable redemption premium.
(3) The change in redemption price for the US$450 million 6.875% senior notes takes effect on June 30th of each year. Prior to June 30th, 2018, the redemption option is only available if the 6.875% Notes are repaid using the proceeds of one or more equity offerings or by paying a make-whole premium represented by the present value of interest that would otherwise be payable over the remaining term of the debt in excess of the applicable redemption premium.

Subject to certain exceptions and qualifications, the senior unsecured notes have no financial covenants but limit the Company's ability to, among other things: make certain payments and distributions; incur additional indebtedness; issue disqualified or preferred stock; create or permit liens to exist; make certain dispositions; transfer assets; and engage in amalgamations, mergers or consolidations.

The Company is exposed to foreign exchange rate fluctuations on the principal and interest related to senior notes. As at December 31, 2017, a 10% increase to the value of the Canadian dollar relative to the US dollar would result in a gain of approximately $197.6 million (10% decline - loss of $197.6 million) to the amortized cost of the notes.

## 13. OTHER LONG-TERM LIABILITIES

| As at December 31, | | 2017 | | 2016 |
|---|---|---|---|---|
| Decommissioning liabilities | **$** | **194.2** | $ | 160.7 |
| Onerous lease | | **3.2** | | 3.6 |
| Deferred credits | | **0.6** | | 0.7 |
| Other long-term liabilities | **$** | **198.0** | $ | 165.0 |

### Decommissioning liabilities

| For the year ended December 31, | | 2017 | | 2016 |
|---|---|---|---|---|
| Balance, beginning of year | **$** | **160.7** | $ | 79.1 |
| Liabilities incurred | | **23.9** | | 21.3 |
| Liabilities acquired (Note 8) | | **—** | | 10.7 |
| Change in estimates | | **5.4** | | 27.9 |
| Change in discount rates[1] | | **0.4** | | 18.9 |
| Accretion (Note 21) | | **3.8** | | 2.8 |
| Balance, end of year | **$** | **194.2** | $ | 160.7 |

(1) Change in discount rates for the year ended December 31, 2016 includes a $20.5 million increase to acquired liabilities for the decrease from the 6.3% credit adjusted risk free rate at acquisition to a risk free rate of 2.3% at period end.

As at December 31, 2017, the total undiscounted, uninflated estimated cash flows required to settle the Company's decommissioning liabilities was approximately $205.8 million (December 31, 2016 – $164.8 million). These liabilities are anticipated to be incurred over the next 35 years with the majority of costs incurred between 2041 and 2052. As at December 31, 2017, the Company utilized a risk free rate of 2.2% (December 31, 2016 – 2.3%) and an inflation rate of 2.0% (December 31, 2016 – 2.0%).

## 14. INCOME TAXES

The following table reconciles the Company's expected income tax expense (recovery) calculated at the Canadian statutory rate of 27% (2016 - 27%) for the year ended December 31, 2017 and 2016:

| For the year ended December 31, | | 2017 | | 2016 |
|---|---|---|---|---|
| Net income (loss) before income taxes | **$** | **735.0** | $ | (33.6) |
| Statutory income tax rate | | **27%** | | 27% |
| Expected income tax expense (recovery) | | **198.5** | | (9.1) |
| Adjustments related to the following: | | | | |
| Non-taxable portion of foreign exchange gains | | **(18.9)** | | (2.2) |
| Change in unrecognized deferred tax asset | | **(13.3)** | | (1.3) |
| Stock-based compensation | | **8.2** | | 4.9 |
| Change in tax rates and other | | **(2.0)** | | 0.3 |
| Income tax expense (recovery) | **$** | **172.5** | $ | (7.4) |

For the year ended December 31, 2017, $2.9 million was recorded in current income tax expense relating to foreign sourced income from the Company's wholly owned US subsidiary (December 31, 2016 - $1.4 million). As at December 31, 2017, the Company had $5.5 billion tax pools available for future deduction, including $0.9 billion available for immediate deduction against taxable income (December 31, 2016 - $5.0 billion and $0.9 billion, respectively). The non-capital losses begin to expire after 2033.

Changes in the deferred tax balances are as follows:

| As at December 31, | | 2015 | | Movement | | 2016 | | Movement | | 2017 |
|---|---|---|---|---|---|---|---|---|---|---|
| Property, plant and equipment | $ | 193.0 | $ | 142.3 | $ | 335.3 | $ | 129.8 | **$** | **465.1** |
| Risk management contracts | | 33.3 | | (73.6) | | (40.3) | | 50.6 | | **10.3** |
| Non-capital losses | | (63.1) | | (61.6) | | (124.7) | | 2.8 | | **(121.9)** |
| Decommissioning liabilities | | (21.4) | | (22.0) | | (43.4) | | (9.0) | | **(52.4)** |
| Financing costs | | (10.9) | | (4.9) | | (15.8) | | (5.1) | | **(20.9)** |
| Unrealized foreign exchange losses | | (40.0) | | 2.1 | | (37.9) | | 17.9 | | **(20.0)** |
| Other | | (1.3) | | (1.6) | | (2.9) | | (4.1) | | **(7.0)** |
| | | 89.6 | | (19.3) | | 70.3 | | 182.9 | | **253.2** |
| Unrecognized deferred tax asset | | 39.8 | | (1.3) | | 38.5 | | (13.3) | | **25.2** |
| | $ | 129.4 | $ | (20.6) | $ | 108.8 | $ | 169.6 | **$** | **278.4** |

As at December 31, 2017, the unrecognized deferred tax asset consisted of foreign exchange capital losses of $19.0 million and $6.2 million related to investments in associates.

The changes in the deferred tax liability were allocated to:

| Year ended December 31, | | 2017 | | 2016 |
|---|---|---|---|---|
| Income statement | **$** | **169.6** | $ | (8.8) |
| Share capital | | **—** | | (11.8) |
| | **$** | **169.6** | $ | (20.6) |

## 15. SHARE CAPITAL

The Company’s authorized share capital consists of an unlimited number of common shares, class B common non-voting shares, preferred A, B, C and D shares and special voting shares. There are no class B common non-voting shares, preferred shares or special voting shares issued and outstanding.

| | 2017 | | | 2016 | | |
|---|---|---|---|---|---|---|
| **For the year ended December 31,** | **Number (millions)** | | **Amount ($)** | **Number (millions)** | | **Amount ($)** |
| Balance, beginning of year | **350.3** | **$** | **3,830.5** | 254.4 | $ | 1,775.7 |
| Issued for cash | **—** | | **—** | 52.1 | | 1,047.7 |
| Issued for Acquisition (Note 8) | **—** | | **—** | 33.5 | | 965.1 |
| Share issue costs, net of deferred income taxes | **—** | | **—** | — | | (31.8) |
| Exercise of stock options and performance warrants | **4.4** | | **25.0** | 10.3 | | 55.7 |
| Transfer from contributed surplus on exercise of equity compensation | **—** | | **8.9** | — | | 18.1 |
| Balance, end of year | **354.7** | **$** | **3,864.4** | 350.3 | $ | 3,830.5 |

On February 24, 2016, the Company completed a private placement of 21.4 million common shares at a price of $14.00 per share for gross proceeds of $300.0 million. Net proceeds after commissions and expenses were approximately $287.0 million.

On July 26, 2016, the Company closed a bought-deal financing arrangement, issuing 30.7 million subscription receipts at $24.35 per subscription receipt for gross proceeds of $747.7 million. Each holder of the subscription receipts received one common share for each subscription receipt held upon the closing of the Acquisition (Note 8). Net proceeds after commissions and expenses were approximately $717.7 million.

On August 18, 2016, the Company closed the Acquisition and as part of the consideration, issued 33.5 million common shares. The closing price of the common shares on August 18, 2016 was $28.81 per share.

## 16. CAPITAL MANAGEMENT

The Company's objective for managing capital continues to be to maintain a strong balance sheet and capital base to provide financial flexibility to position the Company for growth and development. The Company strives to grow and maximize long-term shareholder value by ensuring it has the financial capacity to fund projects that are expected to add value to shareholders. Near-term major acquisitions and capital development are anticipated to be funded by funds from operations, cash and cash equivalents and draws on its Credit Facility (Note 11). The Company endeavors to balance the proportion of debt and equity in its capital structure to take into account the level of risk being incurred in its capital investments.

| **As at December 31,** | | **2017** | | **2016** |
|---|---|---|---|---|
| Senior notes | **$** | **1,956.4** | $ | 2,111.9 |
| Shareholders' equity | | **4,450.4** | | 3,822.8 |
| Capital managed | **$** | **6,406.8** | $ | 5,934.7 |

The Company manages its liquidity risk through its capital structure, forecasting cash flows and available credit. As at December 31, 2017, the Company had $165.3 of cash and cash equivalents, and its undrawn Credit Facility of $1.4 billion (Note 11). Management believes it has sufficient funding to meet the Company's foreseeable liquidity requirements.

## 17. PER SHARE AMOUNTS

| **For the year ended December 31,** | **2017** | **2016** |
|---|---|---|
| Weighted average number of common shares - basic | **353.3** | 299.8 |
| Dilutive effect of outstanding equity compensation units(1) | **11.1** | — |
| Weighted average number of common shares - diluted | **364.4** | 299.8 |

(1) For the year ended December 31, 2016, 18.6 million units have been excluded from the diluted earnings per share calculation since these are anti-dilutive as the Company was in a net loss position.

## 18. LIQUIDS AND NATURAL GAS SALES

| For the year ended December 31, | | 2017 | | 2016 |
|---|---|---|---|---|
| Condensate | **$** | **1,248.9** | $ | 726.8 |
| Natural gas | | **617.4** | | 376.2 |
| NGLs | | **341.0** | | 143.9 |
| Liquids and natural gas sales | **$** | **2,207.3** | $ | 1,246.9 |
| **Sales by country** | | | | |
| Canada | **$** | **1,588.3** | $ | 835.2 |
| United States | **$** | **619.0** | $ | 411.7 |

The Company enters into physical delivery contracts on the Alliance Pipeline to Chicago, Illinois, the NGPL pipeline to the Gulf of Mexico, the TCPL Canadian Mainline to Dawn, Ontario and the NGTL pipeline in Alberta on a month-to-month and term contract basis. Pricing of the physical delivery contracts is primarily based on published North American natural gas indices and fixed prices. The following table summarizes the average daily volumes the Company has committed to deliver on a term contract basis as at December 31, 2017:

| Daily average volumes committed for the year ended December 31, | Chicago Citygate MMBtu/d | Gulf of Mexico MMBtu/d | Dawn MMBtu/d | AECO GJ/d |
|---|---|---|---|---|
| 2018 | **199,537** | **36,000** | **40,000** | **38,470** |
| 2019 | **—** | **—** | **—** | **19,808** |

From time to time, the Company purchases oil and natural gas for resale on a monthly basis in order to optimize the Company's transportation and take or pay commitment capacities. For the year ended December 31, 2017, $101.2 million of product purchased was netted against liquids and natural gas sales (December 31, 2016 - nil). Any gain on liquids and natural gas sales in excess of purchases are presented as marketing gains under transportation, processing and other expenses (Note 20).

## 19. OPERATING EXPENSES

| For the year ended December 31, | | 2017 | | 2016 |
|---|---|---|---|---|
| Trucking and disposal | **$** | **159.9** | $ | 62.0 |
| Equipment rental and maintenance | | **98.5** | | 56.6 |
| Chemicals and fuel | | **38.8** | | 25.4 |
| Staff and contractor costs | | **39.4** | | 25.7 |
| Other | | **21.2** | | 12.2 |
| Operating expenses | **$** | **357.8** | $ | 181.9 |

## 20. TRANSPORTATION, PROCESSING AND OTHER EXPENSES

| For the year ended December 31, | | 2017 | | 2016 |
|---|---|---|---|---|
| Pipeline tariffs | **$** | **263.9** | $ | 164.2 |
| Processing | | **80.7** | | 21.2 |
| Trucking and other | | **49.8** | | 66.9 |
| Third party marketing gains | | **(23.0)** | | (13.7) |
| Transportation, processing and other | **$** | **371.4** | $ | 238.6 |

## 21. FINANCE EXPENSE

| For the year ended December 31, | 2017 | 2016 |
|---|---|---|
| Interest on senior notes | **$ 149.3** | $ 131.3 |
| Premium on redemption of senior notes (Note 12) | **37.2** | — |
| Revolving credit facility fees and bank fees | **5.4** | 7.5 |
| Accretion (Note 13) | **3.8** | 2.8 |
| Amortization of premiums and debt issuance costs | **(0.6)** | 0.8 |
| Finance costs | **195.1** | 142.4 |
| Capitalized borrowing costs | **(1.9)** | (3.7) |
| Finance expense | **$ 193.2** | $ 138.7 |

## 22. STOCK-BASED COMPENSATION

The Company's current stock-based compensation plans consist of stock options, performance warrants, performance share units ("PSUs"), restricted share units ("RSUs") and deferred share units ("DSUs").

The following table summarizes the Company's outstanding equity compensation units as at December 31, 2017 and 2016:

| | December 31, 2017 | | | December 31, 2016 | | |
|---|---|---|---|---|---|---|
| | Units (millions) | Weighted Average Exercise Price ($) | Weighted Average Remaining Life (years) | Units (millions) | Weighted Average Exercise Price ($) | Weighted Average Remaining Life (years) |
| Stock options (a) | **12.4** | **$ 16.63** | **5.4** | 11.2 | $ 13.95 | 5.4 |
| Performance warrants (b) | **8.3** | **6.91** | **1.3** | 11.4 | 6.62 | 1.9 |
| PSUs and RSUs (c) | **1.1** | **—** | **8.7** | 0.6 | — | 8.9 |
| DSUs[1] (d) | **0.2** | **—** | **—** | 0.1 | — | — |
| Units outstanding | **22.0** | **$ 12.00** | **4.0** | 23.3 | $ 9.96 | 3.6 |

(1) DSUs fully vest on grant date and expire within one year of the Director's departure from Seven Generations' Board.

### (a) Stock Options

The Company's stock option plan allows for the granting of options to officers, employees and service providers of the Company. Options granted are generally fully exercisable for common shares after three years and expire ten years after the grant date.

| For the year ended December 31, | 2017 | 2016 |
|---|---|---|
| Balance, beginning of year | **11.2** | 12.0 |
| Granted | **2.6** | 2.6 |
| Exercised | **(1.2)** | (3.2) |
| Forfeited | **(0.2)** | (0.2) |
| Balance, end of year | **12.4** | 11.2 |

The fair value of stock options granted during the year was estimated using the Black-Scholes pricing model. The following weighted-average assumptions were used during the year ended December 31, 2017 and 2016:

| For the year ended December 31, | 2017 | 2016 |
|---|---|---|
| Fair value of options granted ($) | **7.54** | 12.92 |
| Risk-free interest rate (%) | **1.1** | 0.8 |
| Expected life (years) | **5.0** | 6.0 |
| Expected forfeiture rate (%) | **5.0** | 4.4 |
| Expected volatility (%) | **33.0** | 45.2 |
| Expected dividend yield (%) | **—** | — |

A summary of stock options outstanding and exercisable into common shares at December 31, 2017 is as follows:

| | Outstanding | | Exercisable | |
|---|---|---|---|---|
| **Exercise Price ($)** | **Number of Options (Millions)** | **Weighted Average Remaining Life (Years)** | **Number of Options (Millions)** | **Weighted Average Remaining Life (Years)** |
| 2.50 - 7.49 | **3.7** | **1.4** | 3.6 | 1.4 |
| 7.50 - 17.49 | **1.8** | **6.9** | 1.1 | 6.6 |
| 17.50 - 19.99 | **2.2** | **3.9** | 2.1 | 3.5 |
| 20.00 - 24.99 | **2.3** | **9.3** | — | 7.3 |
| 25.00 - 30.90 | **2.4** | **8.4** | 0.8 | 8.4 |
| 16.63 | **12.4** | **5.4** | 7.6 | 3.4 |

**(b) Performance warrants**

Prior to the Company's Initial Public Offering ("IPO") that was completed on November 5, 2014, Seven Generations issued performance warrants to its directors, officers, and employees. These performance warrants were granted pursuant to the Amended and Restated Shareholder Agreement effective while Seven Generations was a private company. Subsequent to the IPO, no additional performance warrants may be granted.

| For the year ended December 31, | 2017 | 2016 |
|---|---|---|
| Balance, beginning of year | **11.4** | 18.5 |
| Exercised | **(3.1)** | (7.1) |
| Balance, end of year | **8.3** | 11.4 |

A summary of performance warrants outstanding and exercisable into common shares at December 31, 2017 is as follows:

| | Outstanding | | Exercisable | |
|---|---|---|---|---|
| **Exercise Price ($)** | **Number of Options (Millions)** | **Weighted Average Remaining Life (Years)** | **Number of Options (Millions)** | **Weighted Average Remaining Life (Years)** |
| 3.75 - 5.00 | **1.6** | **0.5** | 1.6 | 0.5 |
| 5.00 - 5.49 | **0.9** | **0.5** | 0.9 | 0.5 |
| 5.50 - 5.74 | **1.7** | **1.9** | 1.5 | 1.9 |
| 5.75 - 6.49 | **1.6** | **1.0** | 1.5 | 1.0 |
| 6.50 - 17.50 | **2.5** | **1.8** | 2.0 | 1.5 |
| 6.91 | **8.3** | **1.3** | 7.5 | 1.1 |

**(c) Performance share units and restricted share units**

The Company's Performance and Restricted Share Unit Plan ("PRSU Plan") allows for the granting of PSUs and RSUs to officers and employees of the Company. PSUs and RSUs represent the right for the holder to receive common voting shares or, at the election of holder and the Company, a cash payment equal to the fair market value of the common shares calculated at the date of such payment. PSUs and RSUs granted to date under the PRSU Plan generally vest annually over a three year period.

| For the year ended December 31, | 2017 | 2016 |
|---|---|---|
| Balance, beginning of year | **0.6** | 0.4 |
| Granted | **0.6** | 0.2 |
| Exercised | **(0.1)** | — |
| Balance, end of year | **1.1** | 0.6 |

The weighted average fair value of PRSUs granted during the year ended December 31, 2017 was $24.32. The vesting of PSUs is conditional on the satisfaction of certain performance criteria as determined by the Company's Board of Directors. If the Company satisfies the performance criteria, PSUs become eligible to vest and a pre-determined multiplier is applied to eligible PSUs. In calculating stock-based compensation for the PSUs, the Company used an adjustment factor of 1.0, which assumes that the Company will be within the $50^{th}$ percentile of its relative peer group, based on total shareholder return at the respective vesting dates. During the year ended December 31, 2017, PSU multipliers achieved on vested units ranged from 1.69 - 2.00 (December 31, 2016 - 2.0).

**(d) Deferred share units**

The Deferred Share Unit Plan ("DSU Plan") allows for granting of DSUs to directors of the Company. DSUs represent the right for the holder to receive common shares, or, at the election of the holder and the Company, a cash payment equal to fair market value of the common share calculated at the date of such payment. DSUs granted under the DSU Plan vest immediately upon grant. As at December 31, 2017, there were 0.2 million DSUs outstanding (December 31, 2016 - 0.1 million).

## 23. COMMITMENTS AND CONTINGENCIES

The following table lists the Company's estimated material contractual commitments as at December 31, 2017:

| | 2018 | 2019 | 2020 | 2021 | 2022 | Thereafter | Total |
|---|---|---|---|---|---|---|---|
| Senior notes[1] | $ — | $ — | $ — | $ — | $ — | $ 1,975.9 | **$ 1,975.9** |
| Interest on senior notes | 122.0 | 122.0 | 122.0 | 122.0 | 122.0 | 78.6 | **688.6** |
| Firm transportation and processing agreements | 434.2 | 452.3 | 490.4 | 517.0 | 481.6 | 2,553.5 | **4,929.0** |
| Office leases | 4.2 | 3.4 | 3.2 | 3.2 | 3.3 | 2.6 | **19.9** |
| Estimated contractual obligations | $ 560.4 | $ 577.7 | $ 615.6 | $ 642.2 | $ 606.9 | $ 4,610.6 | **$ 7,613.4** |

(1) Balance represents the US$1.575 billion principal converted to Canadian dollars at the exchange rate of US$1=C$1.25 at period end.

The Company is involved in legal claims arising in the normal course of business. The final outcome of such claims cannot be predicted with certainty and management believes that it has appropriately assessed any impact to the consolidated financial statements.

## 24. RELATED PARTY TRANSACTIONS

Seven Generations' related parties primarily consist of the Company's directors and officers. Amounts paid to directors and officers for the year ended December 31, 2017 were as follows:

| For the year ended December 31, | 2017 | 2016 |
|---|---|---|
| Stock-based compensation | **$ 18.7** | $ 10.7 |
| Salaries, benefits and other short-term compensation | **9.6** | 7.9 |
| Retention expense | **—** | 1.1 |
| | **$ 28.3** | $ 19.7 |

Steelhead LNG is also considered a related party due to common directorships and certain significant shareholders (Note 9), including Azimuth Capital Management who has a majority ownership in Steelhead LNG and has professional ties with four of Seven Generation's directors. All related party transactions have been measured at the exchange value.

## 25. SUPPLEMENTAL CASH FLOW INFORMATION

**Change in non-cash working capital**

| For the year ended December 31, | 2017 | 2016 |
|---|---|---|
| Accounts receivable | **$ (120.9)** | $ (105.5) |
| Deposits and prepaid expenses | **(0.8)** | (5.3) |
| Accounts payable and accrued liabilities | **132.8** | 53.7 |
| | **11.1** | (57.1) |
| Realized foreign exchange loss on non-cash working capital | **(2.7)** | — |
| Change in current portion of prepaid processing fees | **0.5** | — |
| | **8.9** | (57.1) |
| Relating to: | | |
| Operating activities | **(53.0)** | (88.0) |
| Financing activities | **—** | — |
| Investing activities | **$ 61.9** | $ 30.9 |
| **Other cash flow information** | | |
| Cash interest paid | **$ 189.2** | $ 139.9 |
| Cash taxes paid | **$ 2.8** | $ 1.5 |

## CORPORATE INFORMATION

**Management**
Marty Proctor
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Christopher Law
CFO

Glen Nevokshonoff
COO

Kyle Brunner
Vice President & General Counsel

Chris Feltin
Vice President, Corporate Planning

Randall Hnatuik
Vice President, Business Development

Barry Hucik
Vice President, Drilling

Kevin Johnston
Vice President, Accounting & Controller

Jordan Johnsen
Vice President, Operations & Engineering

Brian Newmarch
Vice President, Capital Markets

Charlotte Raggett
Vice President, Midstream Business Development

**Directors**
Kent Jespersen
Chairman

Marty Proctor
President & CEO

Kevin Brown

Pat Carlson

Avik Dey

Harvey Doerr

Paul Hand

Dale Hohm

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Canadian Imperial Bank of Commerce
Credit Suisse AG, Toronto Branch
Export Development Canada
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National Bank of Canada
The Bank of Nova Scotia
The Toronto-Dominion Bank
Alberta Treasury Branches
Barclays Bank PLC
Fédération des Caisses Desjardins Du Québec
Wells Fargo Bank, N.A., Canadian Branch

**Auditors**
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**Legal Counsel**
Stikeman Elliott LLP

**Independent Evaluators**
McDaniel & Associates Consultants Ltd.

**Stock Symbol**
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Toronto Stock Exchange