

PERPETUAL ENERGY INC.
Condensed Interim Consolidated Statements of Financial Position

As at	March 31, 2017	December 31, 2016
<i>(Cdn\$ thousands unaudited)</i>		
Assets		
Current assets		
Cash and cash equivalents	\$ 38,231	\$ 2,877
Restricted cash	–	2,000
Accounts receivable	12,066	11,473
Tourmaline Oil Corp. (“TOU”) share investment (note 3)	49,440	66,343
Prepaid expenses and deposits	818	990
Fair value of derivatives (note 14)	5,123	8,326
	105,678	92,009
Fair value of derivatives (note 14)	–	2,351
Property, plant and equipment (note 4)	237,911	219,886
Exploration and evaluation (note 5)	46,150	47,159
Total assets	\$ 389,739	\$ 361,405
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	\$ 34,401	\$ 21,257
Fair value of derivatives (note 14)	3,769	9,221
TOU share margin loans (note 9)	35,039	39,953
Senior notes (note 10)	27,531	–
Gas over bitumen royalty financing	2,682	3,390
Provisions (note 11)	4,265	7,656
	107,687	81,477
Fair value of derivatives (note 14)	903	2,023
Term loan (note 8)	32,988	–
Senior notes (note 10)	32,310	60,120
Gas over bitumen royalty financing	3,607	4,954
Provisions (note 11)	32,457	30,118
Total liabilities	209,952	178,692
Equity		
Share capital (note 12)	1,336,908	1,327,016
Shares held in trust	(1,311)	(1,311)
Warrants (note 12)	923	–
Contributed surplus	43,430	42,999
Deficit	(1,200,163)	(1,185,991)
Total equity	179,787	182,713
Total liabilities and equity	\$ 389,739	\$ 361,405

Subsequent event (note 10).

See accompanying notes to the condensed interim consolidated financial statements.

/s/ Robert A. Maitland

/s/ Geoffrey C. Merritt

Robert A. Maitland

Geoffrey C. Merritt

Director

Director

PERPETUAL ENERGY INC.**Condensed Interim Consolidated Statements of Income (Loss) and Comprehensive Income (Loss)**

Three months ended March 31,
2017 2016

(Cdn\$ thousands, except per share amounts unaudited)

Revenue			
Oil and natural gas	\$	18,158	\$ 24,694
Royalties		(3,102)	(2,277)
		15,056	22,417
Change in fair value of derivatives (note 14)		3,993	19,016
Gas over bitumen royalty credit and other		925	530
		19,974	41,963
Expenses			
Production and operating		4,601	14,369
Transportation		1,015	2,499
Exploration and evaluation (note 5)		1,501	1,365
General and administrative		4,633	6,343
Loss (gain) on dispositions (note 4a)		2,191	(7,073)
Depletion and depreciation (note 4)		7,125	17,547
Income (loss) from operating activities		(1,092)	6,913
Finance expenses (note 13)		(1,864)	(8,576)
Change in fair value of TOU share investment (note 3)		(11,216)	33,954
Share of net income of gas storage facility investment		-	473
Net income (loss) and comprehensive income (loss)		(14,172)	32,764
Income (loss) per share (note 12)			
Basic	\$	(0.26)	\$ 0.72
Diluted	\$	(0.26)	\$ 0.70

See accompanying notes to the condensed interim consolidated financial statements.

PERPETUAL ENERGY INC.
Condensed Interim Consolidated Statements of Changes in Equity

	Share capital		Shares held	Warrants	Contributed	Deficit	Total equity
	(thousands)	(\$thousands)	in trust		surplus		
<i>(Cdn\$ thousands unaudited)</i>							
Balance at December 31, 2016	53,681	\$ 1,327,016	\$ (1,311)	\$ –	\$ 42,999	\$ (1,185,991)	\$ 182,713
Net loss	–	–	–	–	–	(14,172)	(14,172)
Common shares and warrants issued (note 12)	5,569	9,892	–	923	(1,101)	–	9,714
Share based payments	–	–	–	–	1,532	–	1,532
Balance at March 31, 2017	59,250	\$ 1,336,908	\$ (1,311)	\$ 923	\$ 43,430	\$ (1,200,163)	\$ 179,787

	Share capital		Shares held	Share purchase	Contributed	Deficit	Total equity
	(thousands)	(\$thousands)	in trust	rights	surplus		
<i>(Cdn\$ thousands unaudited)</i>							
Balance at December 31, 2015	19,115	\$ 1,297,911	\$ (1,177)	\$ 5,290	\$ 38,300	\$ (1,293,140)	\$ 47,184
Net income	–	–	–	–	–	32,764	32,764
Common shares issued (note 12)	33,268	27,407	(162)	(5,290)	–	–	21,955
Share based payments	–	–	–	–	400	–	400
Balance at March 31, 2016	52,383	\$ 1,325,318	\$ (1,339)	\$ –	\$ 38,700	\$ (1,260,376)	\$ 102,303

See accompanying notes to the condensed interim consolidated financial statements.

PERPETUAL ENERGY INC.
Condensed Interim Consolidated Statements of Cash Flows

Three months ended March 31,
2017 2016

(Cdn\$ thousands unaudited)

Cash flows from (used in) operating activities

Net income (loss)	\$	(14,172)	\$	32,764
Adjustments to add (deduct) non-cash items:				
Depletion and depreciation (note 4)		7,125		17,547
Exploration and evaluation (note 5)		1,313		842
Share based compensation expense		1,532		400
Change in fair value of derivatives (note 14)		(3,246)		(11,013)
Change in fair value of TOU share investment (note 3)		11,216		(33,954)
Loss (gain) on dispositions (note 4a)		2,191		(7,073)
Finance expenses (note 13)		(33)		1,643
Share of net income from gas storage facility investment		–		(473)
Expenditures on decommissioning obligations (note 11)		(563)		(1,094)
Payments of restructuring costs (note 11b)		(1,344)		–
Change in non-cash working capital		(6,308)		(6,359)
Net cash flows from (used in) operating activities		(2,289)		(6,770)

Cash flows from (used in) financing activities

Change in Term Loan (note 8)		33,728		–
Change in TOU share margin loans (note 9)		(5,835)		–
Change in gas over bitumen royalty financing		(816)		(650)
Issue costs on senior note exchange		(344)		–
Common shares and warrants issued (note 12)		8,945		22,117
Shares purchased and held in trust		–		(162)
Change in non-cash working capital		(216)		–
Net cash flows from financing activities		35,462		21,305

Cash flows from (used in) investing activities

Capital expenditures		(24,590)		(4,814)
Acquisitions		(208)		–
Net proceeds on dispositions (note 4a)		45		6,466
Proceeds on sale of TOU share investment (note 3)		5,687		7,354
Restricted cash		2,000		–
Change in non-cash working capital		19,247		374
Net cash flows from investing activities		2,181		9,380
Change in cash and cash equivalents		35,354		23,915
Cash and cash equivalents, beginning of period		2,877		2,116
Cash and cash equivalents, end of period	\$	38,231	\$	26,031

See accompanying notes to the condensed interim consolidated financial statements.

PERPETUAL ENERGY INC.
Notes to the Condensed Interim Consolidated Financial Statements (unaudited)
For the three months ended March 31, 2017
(All tabular amounts are in Cdn\$ thousands, except where otherwise noted)

1. REPORTING ENTITY

Perpetual Energy Inc. (the "Company") is a Canadian corporation engaged in the exploration, development and marketing of oil and natural gas based energy in Alberta, Canada. The Company operates a diversified asset portfolio that includes liquids-rich natural gas, shallow natural gas and conventional heavy oil producing properties, as well as undeveloped bitumen resource properties.

The address of the Company's registered office is 3200, 605 – 5 Avenue S.W., Calgary, Alberta, T2P 3H5.

The condensed interim consolidated financial statements of the Company as at and for the three months ended March 31, 2017 are comprised of the accounts of Perpetual Energy Inc. and its wholly owned subsidiaries: Perpetual Operating Corp., Perpetual Operating Trust, and Perpetual Energy Operating Corp, which are incorporated in Canada.

2. BASIS OF PREPARATION

These condensed interim consolidated financial statements have been prepared in accordance with IAS 34 Interim Financial Reporting and do not include all of the information required for full annual financial statements. These condensed interim consolidated financial statements should be read in conjunction with the Company's consolidated financial statements as at and for the year ended December 31, 2016 which were prepared in conformity with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB").

The accounting policies, basis of measurement, critical accounting judgments and significant estimates used to prepare the annual consolidated financial statements as at and for the year ended December 31, 2016 have been applied in the preparation of these condensed interim consolidated financial statements.

These condensed interim consolidated financial statements of the Corporation were approved and authorized for issue by the Board of Directors on May 8, 2017.

3. TOU SHARE INVESTMENT

	March 31, 2017		December 31, 2016	
	Shares (thousands)	Amount (\$thousands)	Shares (thousands)	Amount (\$thousands)
Balance, beginning of period	1,847	\$ 66,343	6,500	\$ 145,275
Sold	(180)	(5,687)	(250)	(7,354)
Exchange for senior notes	–	–	(4,403)	(130,475)
Unrealized change in fair value	–	(11,216)	–	58,897
Balance, end of period	1,667	\$ 49,440	1,847	\$ 66,343

During the first quarter of 2017, the Company sold 180,000 TOU shares at \$31.63 per TOU share for net cash proceeds of \$5.7 million.

At March 31, 2017, the Company held 1.67 million (December 31, 2016 – 1.85 million) TOU shares with a fair value of \$49.4 million (December 31, 2016 - \$66.3 million) based on a March 31, 2017 closing price of \$29.65 per share (December 31, 2016 - \$35.91 per share). Net income for the three months ended March 31, 2017 included an unrealized loss of \$11.2 million (2016 - \$34.0 million unrealized gain) representing the change in fair value of TOU shares held during the period.

At March 31, 2017, 1.5 million TOU shares (December 31, 2016 – 1.5 million TOU shares) were pledged as security for the TOU share margin loans (note 9).

As at March 31, 2017, a \$1.00 per share increase in the market price of TOU shares would increase the Company's after tax net income by \$1.7 million. The TOU share margin loans detailed in note 9 include put options that effectively protect the Company from potential TOU share price decreases on 0.9 million TOU shares below \$21.14 per share and 0.65 million TOU shares below \$27.38 per share.

4. PROPERTY, PLANT AND EQUIPMENT

	Oil and Gas Properties	Corporate Assets	Total
Cost			
December 31, 2015	\$ 2,430,568	\$ 7,090	\$ 2,437,658
Additions	14,170	92	14,262
Change in decommissioning obligations (note 11)	5,213	–	5,213
Dispositions	(1,838,905)	–	(1,838,905)
December 31, 2016	611,046	7,182	618,228
Additions	24,467	27	24,494
Change in decommissioning obligations (note 11)	664	–	664
Dispositions	(8)	–	(8)
March 31, 2017	\$ 636,169	\$ 7,209	\$ 643,378
Accumulated depletion, depreciation and impairment losses			
December 31, 2015	(2,083,135)	(6,620)	(2,089,755)
Depletion and depreciation	(54,034)	(283)	(54,317)
Dispositions	1,738,830	–	1,738,830
Impairment reversal	6,900	–	6,900
December 31, 2016	(391,439)	(6,903)	(398,342)
Depletion and depreciation	(7,074)	(51)	(7,125)
March 31, 2017	\$ (398,513)	\$ (6,954)	\$ (405,467)
Carrying amount			
December 31, 2016	\$ 219,607	\$ 279	\$ 219,886
March 31, 2017	\$ 237,656	\$ 255	\$ 237,911

At March 31, 2017, property, plant and equipment included \$1.2 million (December 31, 2016 – \$1.4 million) of costs currently not subject to depletion.

a) Dispositions

Proceeds on dispositions

<i>(\$ thousands)</i>	Three months ended March 31,	
	2017	2016
Proceeds on dispositions of oil and gas properties	436	6,466
Proceeds on retained shallow gas marketing arrangements	538	–
Payments on fixed portion of retained shallow gas marketing arrangements	(929)	–
Net proceeds on dispositions	45	6,466

Loss (gain) on dispositions

<i>(\$ thousands)</i>	Three months ended March 31,	
	2017	2016
Realized gain on retained shallow gas marketing arrangements	(538)	–
Unrealized loss on retained shallow gas marketing arrangements	3,157	–
	2,619	–
Gain on oil and gas property dispositions	(428)	(7,073)
Loss (gain) on dispositions	2,191	(7,073)

Dispositions during the first quarter of 2017 consisted of gains of \$0.4 million related to the sale of certain gross overriding royalties and non-core undeveloped land for proceeds of \$0.4 million. During the first quarter of 2016, Perpetual disposed of certain undeveloped oil sands leases and surplus production equipment for cash proceeds of \$6.5 million, with net gains totaling \$7.1 million included in net income. Included in the gain was \$0.6 million in liabilities related to decommissioning obligations in excess of the carrying value of the assets disposed.

The Shallow Gas Disposition transaction which closed during the fourth quarter of 2016 included marketing arrangements whereby the Company provided floor price protection at \$2.58/GJ to the purchaser and retained price exposure to the extent average monthly AECO prices exceed \$2.81/GJ on 33,611 GJ/d through to August 31, 2018. The Company entered into marketing arrangements prior to closing to fix the cost of the floor price protection through to March 31, 2018. Realized and unrealized gains and losses on these marketing arrangements are recognized as adjustments to gains/losses on dispositions and included as cash flows from investing activities on the consolidated statement of cash flows.

As at March 31, 2017, the net retained shallow gas marketing arrangements have been summarized as follows:

Term	Volumes at AECO (GJ/d)	Floor price (\$/GJ)	Ceiling price (\$/GJ)	Fair value (\$ thousands)
April 2017 – August 2018	33,611	–	2.81	2,203
April 2018 – August 2018	33,611	2.58	–	(1,551)

5. EXPLORATION AND EVALUATION (“E&E”)

	March 31, 2017	December 31, 2016
Balance, beginning of year	\$ 47,159	\$ 56,407
Additions	96	318
Acquisitions	208	12
Dispositions	–	(6,851)
Non-cash exploration and evaluation expense	(1,313)	(2,727)
Balance, end of period	\$ 46,150	\$ 47,159

During the three months ended March 31, 2017, \$0.2 million (2016 – \$0.5 million) in costs were charged directly to E&E expense in net income (loss).

6. CAPITAL MANAGEMENT

The Company’s goal is to maintain a strong capital base to retain investor, creditor and market confidence and to support the execution of the Company’s business plan. The Company manages its capital structure and makes adjustments to its capital spending in light of changes in economic conditions and the risk characteristics of its underlying oil and natural gas assets. The Company considers its capital structure to include share capital, senior notes, bank indebtedness, Term Loan, TOU share margin loans and net working capital, with value and liquidity enhanced through the current ownership of TOU shares.

During the first quarter of 2017, the Company completed a number of financing transactions to strengthen Perpetual’s liquidity and debt repayment profile and secure funding for the Company’s 2017 and 2018 business plan. The significant financing transactions are as follows:

- Partial repayment and refinancing of its existing TOU share put option margin loan previously maturing in March 2017, reducing the loan amount outstanding to \$18.9 million, extending the maturity to August 1, 2017 and increasing the number of shares pledged as collateral to 0.9 million TOU shares, with a new floor price on these shares of \$21.14 per TOU share (note 9);
- Exchange of \$17.4 million aggregate principal amount of its existing Senior Notes maturing in 2018 and 2019 for new 8.75% Senior Notes having an extended maturity date of January 23, 2022 (the “2022 Senior Notes”) (note 10);
- Establishment of a \$45 million second lien senior secured term loan facility (the “Term Loan”) bearing annual interest at 8.1 percent and maturing March 14, 2021 (note 8). In addition, for no additional consideration, 5.4 million warrants were issued which entitle the holder to acquire common shares on a one for one basis for a period of up to three years, at an exercise price of \$2.34 per share;
- Issuance of 5.1 million common shares and 1.1 million warrants to purchase common shares on the same terms and conditions as above (collectively, the “Equity Units”) at \$1.75 per Equity Unit for aggregate gross proceeds of \$9 million; and
- Extension of the Company’s reserve based, revolving credit facility (the “Credit Facility”) to October 31, 2017, while providing for a \$14 million increase in total borrowing capacity under the credit facility to \$20 million (note 7).

Subsequent to March 31, 2017, Perpetual completed the early redemption of \$27.1 million aggregate outstanding principal amount of its 8.75% Senior Notes maturing March 15, 2018 and extended \$0.5 million to January 23, 2022 (note 10).

The Company will continue to regularly assess changes to its capital structure and repayment alternatives, with considerations for both short term liquidity, investment opportunities and longer term financial sustainability.

7. BANK INDEBTEDNESS

As at March 31, 2017, the Company has a reserve based revolving credit facility (“Credit Facility”) with a borrowing limit (the “Borrowing Limit”) of \$20.0 million (December 31, 2016 - \$6.0 million) under which \$4.0 million of letters of credit had been drawn (December 31, 2016 - \$4.0 million). The Credit Facility matures on October 31, 2017 with the next Borrowing Limit redetermination occurring on or before May 31, 2017.

Borrowings under the Credit Facility bear interest at its lenders’ prime rate or Banker’s Acceptance rates, plus applicable margins and standby fees. The applicable margins range between 1.25% and 4.75%. Borrowings are secured by general security agreements covering all of the Company’s assets with the exception of TOU shares pledged as security for the TOU share margin loans (note 9) and certain lands pledged to the gas over bitumen royalty financing counterparty.

For the period ended March 31, 2017 and 2016, if interest rates changed by one percent with all other variables held constant, the impact on interest expense and net income (loss) would be nominal, as the Company’s bank indebtedness, subject to floating interest rates, was minimal.

The Credit Facility is subject to a working capital covenant which requires the Company to maintain net working capital plus outstanding letters of credit not exceeding the Borrowing Limit. Net working capital includes the sum of cash and cash equivalents, restricted cash, accounts receivable, prepaid expenses and unpledged TOU shares less accounts payable and accrued liabilities and accrued interest on Senior Notes and the Term Loan up to the Credit Facility maturity date. The Company was in compliance with all Credit Facility covenants at March 31, 2017.

The credit facility also contains provisions which restrict the Company's ability to pay dividends on or repurchase its common shares.

8. TERM LOAN

On March 14, 2017, Perpetual entered into the Term Loan which included the issuance of 5.4 million warrants to purchase common shares (note 12).

	March 31, 2017
Balance, beginning of period	\$ —
Principal amount of Term Loan issued	35,000
Value allocated to warrants	(769)
Issue costs	(1,272)
Amortization of issue costs	29
Balance, end of period	\$ 32,988

The Term Loan matures on March 14, 2021 and bears interest at 8.1% per annum with semi-annual interest payments due June 30 and December 31 of each year. The Term Loan contains certain restrictions that limit the Company's ability to incur additional indebtedness, make restricted payments and dispose of certain assets.

The Term Loan is made available by way of two draws consisting of an initial draw of \$35 million completed upon closing with the remaining \$10 million to be drawn prior to November 30, 2017. Amounts borrowed under the Term Loan that are repaid or prepaid are not available for re-borrowing. The Company may not prepay the Term Loan prior to the second anniversary thereof, except with payment of a make whole premium.

The Term Loan is secured by a general security agreement over all present and future property of the Company and its subsidiaries on a second priority basis, subordinate only to liens securing loans under the Credit Facility and TOU shares secured in favor of the TOU share margin loan lenders.

The Term Loan is subject to the same working capital covenant as disclosed under the Credit Facility excluding adjustments for interest on the Term Loan up to the Credit Facility maturity date. The Company was in compliance with all Term Loan covenants at March 31, 2017.

9. TOU SHARE MARGIN LOANS

At March 31, 2017, \$18.5 million TOU share put option margin loans mature in August 2017 and \$16.5 million mature in November 2017. For the August 2017 maturity, 0.9 million TOU shares have been pledged as collateral with a put option floor price of \$21.14 per share. For the November 2017 maturity, 0.65 million TOU shares have been pledged as collateral with a put option floor price of \$27.38 per share.

The TOU share put option margin loans are hybrid financial instruments comprising a debt host with an embedded TOU put option derivative related to indexation of the future settlement amount to changes in the market price of TOU shares pledged as collateral. The Company has designated the TOU share put option margin loans as financial liabilities which are measured at fair value through profit and loss. For the three months ended March 31, 2017, an unrealized loss of \$0.9 million (2016 - \$2.0 million unrealized loss) is included in finance expense, representing the change in fair value of the TOU put options during the year.

10. SENIOR NOTES

	Maturity date	Interest rate	March 31, 2017		December 31, 2016	
			Principal	Carrying Amount	Principal	Carrying amount
2018 Senior Notes	March 15, 2018	8.75%	\$ 27,617	\$ 27,531	\$ 36,013	\$ 35,847
2019 Senior Notes	July 23, 2019	8.75%	15,572	15,425	24,560	24,273
2022 Senior Notes	January 23, 2022	8.75% ⁽¹⁾	17,384	16,885	—	—
			\$ 60,573	\$ 59,841	\$ 60,573	\$ 60,120

⁽¹⁾ Annual interest rate through to January 23, 2018 is 9.75% and 8.75% thereafter.

On January 23, 2017, the Company exchanged \$8.4 million and \$9.0 million aggregate principal amount of 2018 Senior Notes and 2019 Senior Notes respectively for \$17.4 million new 8.75% Senior Notes with a maturity date of January 23, 2022. Included in the exchange were \$3.7 million 2018 Senior Notes and \$4.3 million 2019 Senior Notes held by directors and officers of the Company or entities controlled by them. The 2022 Senior Notes bear a fixed rate of 9.75% for the first year of issuance and 8.75% thereafter, and have identical covenants and rights as the existing 2018 and 2019 Senior Notes.

On April 17, 2017, Perpetual completed the early redemption of \$27.1 million aggregate outstanding principal amount of its 8.75% Senior Notes maturing March 15, 2018 and exchanged \$0.5 million for an equal amount of 2022 Senior Notes. After giving effect to the early redemption and exchange, outstanding Senior Notes are as follows:

	Maturity date	Interest rate	Interest Payment dates	Principal
2019 Senior Notes	July 23, 2019	8.75%	January 23 & July 23	15,572
2022 Senior Notes	January 23, 2022	8.75% ⁽¹⁾	January 23 & July 23	17,918
				\$ 33,490

⁽¹⁾ Annual interest rate through to January 23, 2018 is 9.75% and 8.75% thereafter.

The Senior Notes are direct senior unsecured obligations of the Company, ranking pari passu with all other present and future unsecured and unsubordinated indebtedness of the Company. At any time prior to three years before the senior note maturity date, the Company can redeem up to 35 percent of the principal amount of the Senior Notes at a premium to face value. Within three years of maturity, the Company may redeem up to 100 percent of the Senior Notes at a premium to face value. Within one year of maturity, the Company may redeem up to 100 percent of the Senior Notes at the principal amount.

The Senior Notes have a cross-default provision with the Company's credit facility (note 7). In addition, the Senior Notes indenture contains restrictions on certain payments including dividends, retirement of subordinated debt and stock repurchases. The permitted amount of any restricted payment is limited to:

- i) To the extent the Company's Consolidated Debt (defined as the sum of the period end balance of bank indebtedness, Term Loan, TOU share margin loans and gas over bitumen royalty financing) to trailing twelve months income before interest, taxes, depletion and depreciation and non-cash items ("TTM EBITDA") is less than 3.0 to 1.0 (the "Consolidated Debt Ratio"), the sum of 50 percent of TTM EBITDA from January 1, 2011 to the end of the most recently completed fiscal quarter plus 100 percent of the fair market value of any equity contributions made to the Company during that period less the sum of all restricted payments during that period; and
- ii) To the extent the Company's Consolidated Debt Ratio is greater than or equal to 3.0 to 1.0 pro forma for the proposed restricted payment, \$50 million plus 100 percent of the fair market value of any equity contributions made to the Company.

The Company was in compliance with all covenants at March 31, 2017.

At March 31, 2017 the Senior Notes are presented net of \$0.7 million in issue costs which are amortized using a weighted average effective interest rate of 9.2 percent.

11. PROVISIONS

	March 31, 2017	December 31, 2016
Decommissioning obligations, beginning of period	\$ 33,620	\$ 159,169
Obligations incurred	664	177
Obligations settled	(563)	(3,803)
Accretion (note 13)	191	2,643
Obligations disposed	–	(129,602)
Change in risk free interest rate	–	10,184
Change in estimates	–	(5,148)
Decommissioning obligations, end of period	33,912	33,620
Restructuring costs (b)	2,810	4,154
Balance, end of period	\$ 36,722	\$ 37,774
Provisions – current	4,265	7,656
Provisions – non-current	32,457	30,118
	\$ 36,722	\$ 37,774

a) Decommissioning obligations

The following significant assumptions were used to estimate the Company's decommissioning obligations:

	March 31, 2017	December 31, 2016
Undiscounted obligations	\$ 38,062	\$ 37,877
Average risk free interest rate	2.3%	2.3%
Inflation rate	1.5%	1.5%
Expected timing of settling obligations	1 to 25 years	1 to 25 years

b) Restructuring costs

	Employee downsizing costs	Onerous office lease contract	Lease inducement	Total
Balance, December 31, 2016	\$ 1,606	\$ 2,548	\$ –	\$ 4,154
Transferred	–	(1,764)	1,764	–
Payments	(1,047)	(261)	(36)	(1,344)
Balance, March 31, 2017	559	523	1,728	2,810
Restructuring costs – current	559	523	216	1,298
Restructuring costs – non-current	–	–	1,512	1,512
Total	\$ 559	\$ 523	\$ 1,728	\$ 2,810

On February 1, 2017, Perpetual entered into a new head office lease at its current location for a 98 month period expiring March 31, 2025. As consideration, the landlord agreed to release the Company from all remaining obligations under its existing lease with remaining term to March 31, 2018 with remaining payments of \$1.8 million deferred over the 98 month term of the new lease. This lease inducement is comprised of \$1.8 million related to surplus office space which was recognized as an onerous contract provision in 2016. The lease inducement will be amortized on a straight-line basis over the 98 month term of the new head office lease.

12. SHARE CAPITAL

	March 31, 2017		December 31, 2016	
	Shares (thousands)	Amount (\$thousands)	Shares (thousands)	Amount (\$thousands)
Balance, beginning of period	53,681	\$ 1,327,016	19,115	\$ 1,297,911
Issued pursuant to private placement (b)	5,143	8,791	491	839
Issued pursuant to share based payment plans	426	1,101	807	1,184
Issued pursuant to share purchase rights	–	–	33,268	27,082
Balance, end of period	59,250	\$ 1,336,908	53,681	\$ 1,327,016

a) Authorized

Authorized capital consists of an unlimited number of common shares.

b) Warrants and equity private placement

On March 14, 2017, the Company completed a private placement of 5.1 million equity units for gross proceeds of \$9.0 million, of which \$8.9 million has been allocated to share capital and \$0.1 million to warrants. Each equity unit consisted of 1 common share and 0.21 warrants. Included in the issuance were 1.6 million common shares and 0.4 million warrants issued to directors and officers of the Company or entities controlled by them, for proceeds of \$2.9 million. In addition, 5.4 million warrants valued at \$0.8 million were issued in connection with the Term Loan (note 8). Each warrant entitles the holder to acquire common shares on a one for one basis at an exercise price of \$2.34 per share prior to March 14, 2020.

If the volume weighted average price of Perpetual's common shares is greater than the Exercise Price for 60 consecutive calendar days, Perpetual shall have the option to require warrant holders to exercise all or any portion of the warrants at any time thereafter from time to time.

c) Per share information

	Three months ended March 31,	
	2017	2016
<i>(thousands, except per share amounts)</i>		
Net income (loss) – basic	\$ (14,172)	\$ 32,764
Effect of dilutive securities	–	–
Net income (loss) – diluted	\$ (14,172)	\$ 32,764
Weighted average shares		
Issued common shares	54,728	45,802
Effect of shares held in trust	(260)	(229)
Weighted average common shares outstanding – basic	54,468	45,573
Effect of dilutive securities	–	1,449
Weighted average common shares outstanding – diluted	54,468	47,022
Income (loss) per share - basic	\$ (0.26)	\$ 0.72
Income (loss) per share - diluted	\$ (0.26)	\$ 0.70

In computing per share amounts for the period ended March 31, 2017, potentially issuable common shares through the share based compensation plans and warrants were excluded as the Corporation had a net loss. In computing per share amounts for the period ended March 31, 2016, 0.9 million potentially issuable common shares through the share based compensation plans were excluded as they had an anti-dilutive effect on calculated per share amounts.

13. FINANCE EXPENSE

The components of finance expense are as follows:

	Three months ended March 31, 2017	2016
Cash interest		
Interest on bank indebtedness	180	918
Interest on TOU share margin loans	214	–
Interest on Term Loan	145	–
Interest on Senior Notes	1,358	6,015
Total cash interest	1,897	6,933
Non-cash finance expense		
Amortization of debt issue costs	94	263
Accretion on decommissioning obligations (note 11)	191	917
Change in fair value of gas over bitumen royalty financing	(1,239)	(1,578)
Change in fair value of TOU share margin loans (note 9)	921	2,041
Total non-cash finance expense	(33)	1,643
Finance expenses recognized in net income (loss)	1,864	8,576

14. FINANCIAL RISK MANAGEMENT

Realized gains on commodity price derivatives recognized in net income for the three months ended March 31, 2017 were \$0.7 million (2016 – \$8.0 million). The realized gains on commodity price derivatives for the three months ended March 31, 2017 included early settlement of fixed oil contracts and foreign exchange contracts for a loss of \$5.2 million which was offset by gains of \$4.9 million related to the early settlement of natural gas basis differential contracts.

Natural gas contracts

At March 31, 2017 the Company had entered into the following physical fixed natural gas sales arrangements at AECO:

Term	Sold/bought	Volumes (GJ/d)	Average price (\$/GJ)	Fair Value (\$ thousands)
April 2017	Sold	35,000	2.66	209
May 2017	Sold	15,000	2.47	(57)
May 2017 – December 2017	Sold	20,000	3.14	2,163
November 2017 – March 2018	Sold	12,500	2.94	(36)

At March 31, 2017 the Company had entered into the following financial fixed natural gas sales arrangements at AECO:

Term	Sold/bought	Volumes (GJ/d)	Average price (\$/GJ)	Fair Value (\$ thousands)
April 2017	Sold	15,000	2.43	(20)
April 2017 - December 2017	Sold	7,500	3.16	1,005

Natural gas contracts - sensitivity analysis

As at March 31, 2017, if future natural gas prices changed by \$0.25 per GJ with all other variables held constant, the fair value of commodity price derivatives and after tax net income for the period would change by \$0.1 million. Fair value sensitivity was based on published forward AECO and NYMEX prices.

Oil contracts

At March 31, 2017, the Company had entered into the following costless collar oil sales arrangements which settle in \$USD.

Term	Volumes at WTI (bbls/d)	Floor price (\$USD/bbl)	Ceiling price (\$USD/bbl)	Fair Value (\$ thousands)
April 2017 – December 2017	250	50.00	61.50	300
April 2017 – December 2017	500	50.00	59.40	176

At March 31, 2017, the Company had entered into the following oil basis differential contracts between WTI and WCS trading.

Term	Volumes at WTI (bbls/d)	WTI-WCS differential (\$USD/bbl)	Fair Value (\$ thousands)
April 2017 – December 2017	250	(14.85)	(95)
April 2017 – December 2017	500	(15.40)	(281)

Oil contracts - sensitivity analysis

As at March 31, 2017, if future oil prices increased by \$5.00 per boe with all other variables held constant, the fair value of commodity price derivatives and after tax net income for the period would increase by \$1.4 million. If future oil prices decreased by \$5.00 per boe with all other variables held constant, the fair value of commodity price derivatives and after tax net income for the period would decrease by \$0.3 million. Fair value sensitivity was based on published forward WTI and WCS prices.

The following table is a summary of the fair value of the Company's financial contracts by type:

	March 31, 2017	December 31, 2016
Physical natural gas contracts	2,483	1,876
Financial natural gas contracts	985	4,606
Financial oil contracts	100	(1,138)
Financial foreign exchange contracts	–	(5,022)
Fixed portion of retained shallow gas marketing arrangements ⁽¹⁾	(3,769)	(4,698)
Non-fixed portion of retained shallow gas marketing arrangements	652	3,809
Fair value of derivatives	451	(567)
Derivative assets – current	5,123	8,326
Derivative assets – non-current	–	2,351
Derivative liabilities – current	(3,769)	(9,221)
Derivative liabilities – non-current	(903)	(2,023)
Fair value of derivatives	451	(567)

⁽¹⁾ At March 31, 2017 the term of the put option between the periods of April 1, 2017 and March 31, 2018 was fixed at a cost of \$3.8 million which settles monthly over the term. This portion of the contract is recorded at amortized cost. During the three months ended March 31, 2017, payments of \$0.9 million were recorded as a reduction to this liability.

The following table details the Company's changes in fair value of commodity price derivatives:

	Three months ended March 31,	
	2017	2016
Unrealized gain (loss) on financial oil contracts	1,238	(381)
Unrealized gain (loss) on financial natural gas contracts	(3,621)	5,589
Unrealized gain on physical natural gas contracts	607	170
Unrealized gain on forward foreign exchange contracts	5,022	5,635
Unrealized change in fair value of commodity price derivatives	3,246	11,013
Realized gain (loss) on financial oil contracts	(973)	1,263
Realized gain on financial natural gas contracts	5,898	8,004
Realized loss on forward foreign exchange contracts	(4,178)	(1,264)
Change in fair value of commodity price derivatives	3,993	19,016

Fair value of financial assets and liabilities

The Company's fair value measurements are classified as one of the following levels of the fair value hierarchy:

Level 1 – inputs represent unadjusted quoted prices in active markets for identical assets and liabilities. An active market is characterized by a high volume of transactions that provides pricing information on an ongoing basis.

Level 2 – inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These valuations are based on inputs that can be observed or corroborated in the marketplace, such as market interest rates or forward prices for commodities.

Level 3 – inputs for the asset or liability are not based on observable market data.

The Company aims to maximize the use of observable inputs when preparing calculations of fair value. Classification of each measurement into the fair value hierarchy is based on the lowest level of input that is significant to the fair value calculation.

The fair value of cash and cash equivalents, restricted cash, accounts receivable, and accounts payable and accrued liabilities approximate their carrying amounts due to their short terms to maturity. Bank indebtedness bears interest at a floating market rate and accordingly the fair market value approximates the carrying amount.

The fair value of the gas over bitumen royalty financing is estimated by discounting future cash payments based on the forecasted Alberta gas reference price multiplied by the contracted deemed volume. This fair value measurement is classified as level 3 as significant unobservable inputs, including the discount rate and forecasted Alberta gas reference prices, are used in determination of the carrying amount. The discount rate of 12.2% was determined on inception of the agreement based on the characteristics of the instrument. The forecasted Alberta gas reference prices for the remaining term are based on AECO forward market pricing with adjustments for historical differences between the Alberta reference price and market prices.

The fair value of the TOU share margin loans are estimated using significant unobservable inputs including discount rates and measures of future volatility required to fair value the embedded TOU share price put options. This fair value measurement is classified as level 3 as significant unobservable inputs, including discount rates and measures of future volatility are used in determination of the carrying amount.

The fair value of financial assets and liabilities, excluding working capital, is attributable to the following fair value hierarchy levels:

As at March 31, 2017	Gross	Netting ⁽¹⁾	Carrying Amount	Fair value		
				Level 1	Level 2	Level 3
Financial assets						
Fair value through profit and loss						
TOU share investment	49,440	–	49,440	49,440	–	–
Derivatives – current	5,636	(513)	5,123	–	5,123	–
Derivatives – non-current	648	(648)	–	–	–	–
Financial liabilities						
Financial liabilities at amortized cost						
Senior Notes – current	27,531	–	27,531	–	27,617	–
Senior Notes – non-current	32,310	–	32,310	–	32,830	–
Term Loan – non-current	32,988	–	32,988	–	–	32,988
Fair value through profit and loss						
Derivatives – current	4,282	(513)	3,769	–	3,769	–
Derivatives – non-current	1,551	(648)	903	–	903	–
Gas over bitumen royalty financing – current	2,682	–	2,682	–	–	2,682
Gas over bitumen royalty financing – non-current	3,607	–	3,607	–	–	3,607
TOU share margin loans – current	35,039	–	35,039	–	–	35,039

⁽¹⁾ Derivative assets and liabilities presented in the statement of financial position are shown net of offsetting assets or liabilities where the arrangement provides for the legal right and intention for net settlement exists.