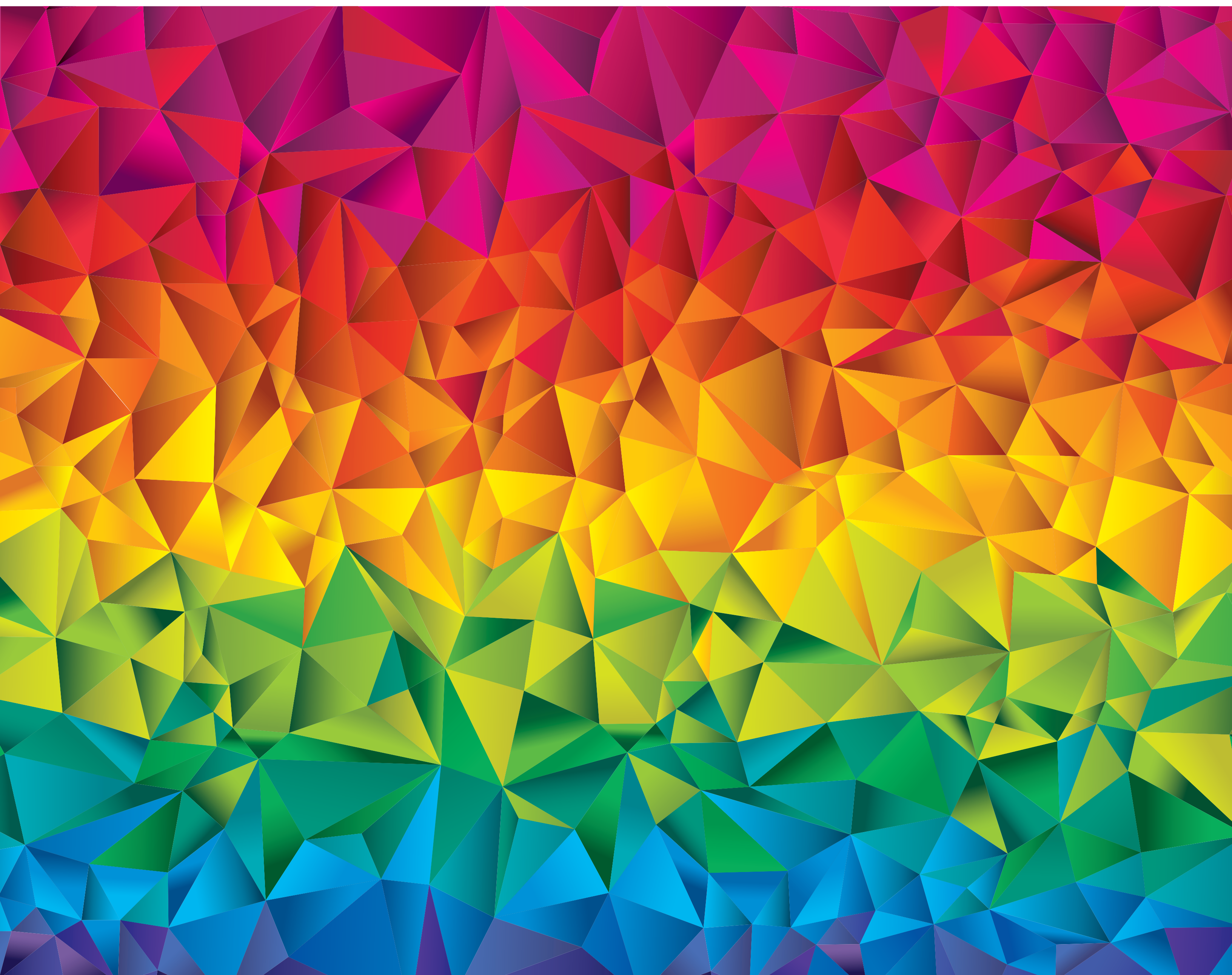
2015 ANNUAL RESULTS

PERPETUAL
ENERGY



2015 STRATEGIC PRIORITIES

Commodity prices declined close to 50 percent through 2015 substantially reducing revenues from oil, gas and natural gas liquids and profoundly impacting funds flow. Perpetual's focus through 2015 and continuing into 2016 shifted from capital investment and production growth to cost reductions, operating efficiencies and financial recapitalization.

Despite the challenges presented by low commodity prices and a depressed economic environment in 2015, significant progress was made to advance the Company's strategic priorities as outlined below.

Perpetual's top strategic priorities for 2015 included:

1. Reduce debt and improve debt to cash flow ratio;
2. Grow greater Edson liquids-rich gas production, cash flow, inventory, reserves and value;
3. Optimize value of Mannville heavy oil;
4. Maximize value of shallow gas; and
5. Refine elements of production growth strategy for 2017 to 2020.

Reduce debt and improve debt to cash flow ratio

- In April 2015 Perpetual swapped its 50 percent joint interest share in the West Edson asset with Tourmaline Oil Corp. ("Tourmaline" or "TOU") in exchange for 6.75 million common shares of Tourmaline ("TOU Shares"). The transaction included all joint interest lands Perpetual held with Tourmaline in West Edson, together with the associated wells and infrastructure (the "West Edson Property"). At the time of the swap, the TOU shares had a market value of approximately $258.7 million based on a closing price of the TOU Shares on the TSX on April 1, 2015 of $38.32/share. Low commodity prices and depressed market conditions were reflected in subsequent declines in the trading price to $22.35/share on December 31, 2015.
- Ownership of the TOU Shares provides Perpetual with exposure to the value creation potential inherent in Tourmaline's land and drilling inventory, along with participation in the ongoing results generated by Tourmaline's investment in its diversified oil and gas asset portfolio, funded by a strong balance sheet. At the same time, the liquidity inherent in the TOU Shares significantly enhances Perpetual's financial position, augmenting Perpetual's options to manage downside risk and enhancing Perpetual's ability to fund attractive investment opportunities during this period of low commodity prices.
- Other property dispositions generated net proceeds of $23.7 million in 2015 including the sale of certain fee simple lands and related seismic data in east central Alberta for gross proceeds of $21.0 million. Additional smaller transactions included the sale of non-core undeveloped land for proceeds of $0.8 million and net cash proceeds of $1.8 million received on an asset swap whereby Perpetual acquired an increased interest in reserves and undeveloped acreage on the Company's core East Edson property in exchange for a working interest in certain undeveloped lands.
- Commodity price contracts in place throughout 2015 for both oil and natural gas were utilized to protect against downside commodity price risk. Gains on price management contracts partially mitigated the erosion of funds flow. Perpetual's realized 2015 natural gas price with derivatives of $3.01/Mcf included $2.0 million of realized gains on natural gas derivatives and $3.1 million of gains realized on crystallizations of contracts before maturity. Similarly, Perpetual's realized oil price, including derivatives, of $52.48/bbl, was higher than the price before derivatives due to gains of $2.9 million recorded on financial crude oil derivative contracts and $3.8 million of gains realized on crystallizations of contracts before maturity.
- Significant corporate cost-savings initiatives throughout 2015 reduced operating, transportation and general and administrative expenses, which combined with royalty reductions, resulted in all-in cash costs 19 percent ($33.8 million) lower than 2014.
- Perpetual's exploration and development spending in 2015 of $75.4 million was financed primarily through bank debt. Spending was restricted during the fourth quarter of 2015 in response to the low commodity price environment, with only $0.8 million of residual spending on capital activities initiated earlier in the year and $2.4 million directed to abandonment and reclamation work. The Company is re-deploying operations personnel and utilizing Company-owned equipment to undertake pipeline and well abandonment projects at costs significantly below third party costs.
- Perpetual continues to focus on cost reduction strategies to preserve funds flow in a continuing depressed and uncertain commodity price environment, preserving optionality, value and inventory with a view to eventual commodity price recovery.
- Despite progress on cost reductions, the collapse in commodity prices eroded both 2015 funds flow to a minimal level ($2.0 million) as well as the market value of TOU Shares. During the second half of 2015, Perpetual sold 250,000 TOU Shares for proceeds of $8.6 million to provide liquidity to manage its margin loan obligations concurrent with the decline in TOU Share market values.
- To improve liquidity and address financial obligations due in the fourth quarter of 2015, Perpetual completed a series of recapitalization transactions which included a new financing arrangement that provided net proceeds of $18.2 million collateralized by one million TOU Shares, repayment of the outstanding 7.00% Convertible Debentures with 228.9 million common shares of Perpetual on December 31, 2015 and a $25.0 million fully backstopped rights offering (the "Rights Offering") which closed on January 18, 2016.
- In conjunction with the recapitalization transactions, the Company's bank credit facility was extended to October 31, 2016 with total borrowing capacity of $62 million, comprised of a $20 million demand loan and a $42 million margin loan secured by 5.5 million TOU Shares.
- A successful focus on cost reduction and debt management was reflected in a 39 percent reduction of total debt, net of working capital and the market value of TOU Shares, to $203.6 million at December 31, 2015, down $128.1 million from December 31, 2014. The reduction in total debt reflects settlement of the convertible debentures in shares and the inclusion of the period end value of the TOU Shares, offset by year to date 2015 capital spending and decommissioning expenditures funded primarily through increased bank indebtedness with limited funds flow during the year as a result of depressed oil, natural gas and NGL prices.

- With the successful closing of the Rights Offering and appreciation in the value of TOU Shares since year end, current total net debt as at the date of this annual report stands at approximately $150 - $160 million.

Grow greater Edson liquids-rich gas production, cash flow, inventory, reserves and value

- Over 90 percent of Perpetual's exploration and development spending in 2015 focused on liquids-rich gas development at East Edson. Spending of $67.5 million included drilling three (3.0 net) liquids-rich natural gas wells in the first quarter of 2015; a seven (7.0 net) well completion and tie-in program comprising wells drilled during the fourth quarter of 2014; construction and expansion of the new East Edson gas plant and 3D seismic activities at East Edson. Spending also included drilling, completion and tie-in of three (1.5 net) natural gas wells and a 3D seismic program at West Edson prior to the swap transaction with Tourmaline in April 2015.
- As a result of 2015 development activities, Perpetual has completed its short-term spending commitments under the East Edson joint venture entered into in July 2014, with only $18.5 million of further spending required prior to December 31, 2022 to fulfill the terms of the arrangements.
- The East Edson gas plant was brought online on July 15, 2015 at a capacity of 30 MMcf/d and expanded to 45 MMcf/d in mid-September 2015. Total project costs for the plant at the end of 2015 were $35.6 million and included construction of a ten inch sales pipeline to a newly constructed TransCanada meter station as well as construction costs for transmission lines and related facilities to supply power to the gas plant. An additional $2.9 million was spent to complete construction of an expanded gathering system, including a main gathering line to facilitate the flow of gas to the new facility.
- Perpetual achieved a 25 percent reduction in completion costs for the four wells completed during the third quarter as compared to the prior year, reflecting improved completion techniques and cost savings from suppliers. Incorporating an adjustment for actual 2015 capital execution costs as well as revised future costs to reflect improved drilling efficiencies due to changes to well design and drilling programs and forecast reduced labor costs for 2016 and 2017, future development costs ("FDC") for proved and probable reserves at East Edson were reduced by $85.7 million at December 31, 2015.
- Production growth from the East Edson development program and new facility more than offset natural declines and lost volumes associated with the exchange of the West Edson Property for TOU Shares. Production in greater Edson of 9,408 boe/d in 2015 was 23 percent higher than 2014 (7,652 boe/d) despite the disposition of 32.3 MMcf/d of gas production from West Edson effective April 1, 2015.
- McDaniel and Associates Consultants Ltd. ("McDaniel") recorded net positive technical reserve revisions of 5.5 MMboe related to performance at East Edson on a proved and probable basis in 2015, primarily attributable to well performance on East Edson wells drilled in 2014 and 2015 which outperformed the proved and probable type curves in the McDaniel 2014 reserve evaluation.
- Using McDaniel's commodity price assumptions at year end 2015, East Edson projects are forecast by McDaniel to generate annual operating cash flow in excess of the annual FDC, making the projects self-funding.
- East Edson represents Perpetual's lowest operating cost property. Highlighting increased efficiencies with the new East Edson gas plant, operating costs for East Edson in the fourth quarter of 2015 were $2.46/boe (Q4 2015 - $6.42/boe) with 73 percent of East Edson production processed through the new 100 percent owned and operated gas plant in the fourth quarter.

Optimize value of Mannville heavy oil

- Capital spending in 2015 included $1.4 million for the continuation of waterflood activities in Mannville heavy oil, which included converting and equipping a water source well, four horizontal well injector conversions as well as surface equipment and pipeline work to arrest production declines and reduce ongoing operating costs on two heavy oil pools.
- Perpetual currently has seven injectors online in the Sparky Upper Mannville I2I pool and six injectors online in the Upper Mannville B Lloyd pool. Results thus far continue to be encouraging.
- Drilling activities for Mannville heavy oil were deferred until crude oil prices recover to preserve value of the Company's drilling inventory.

Maximize value of shallow gas

- Capital spending on eastern Alberta shallow gas properties was concentrated on low-cost operations which mitigate production declines through facility optimization projects, workovers and uphole recompletions. In 2015, Perpetual allocated $1.9 million to optimization projects on shallow gas assets, thereby stabilizing shallow gas production with a low base decline rate of 12 percent year over year.
- Extensive operating cost reduction initiatives were implemented in eastern Alberta throughout 2015 to improve operating netbacks, including manpower reductions, maintenance deferrals and re-deployment of operations personnel in eastern Alberta to accelerate the abandonment and reclamation of inactive sites, thereby reducing maintenance costs, surface lease rentals and municipal taxes as well as future liabilities.
- Perpetual spent $7.6 million on abandonment and reclamation projects during 2015 mainly in eastern Alberta, including $1.0 million of internal labor costs and another $0.8 million for the purchase of idle used equipment. By utilizing internal labor and Company-owned equipment rather than third party services for various stages of reclamation and abandonment, the Company has driven improved efficiencies and realized substantial cost savings on 2015 projects. Capturing efficiencies and cost savings achieved in 2015 through its innovative approach to abandonment and reclamation activities, the Company reduced its estimate of undiscounted future abandonment liabilities by $59.9 million year over year.
- Municipal property taxes represented a significant portion ($9.7 million) of shallow gas operating costs in 2015, an average of $0.49/Mcf, or 20 percent of operating costs for shallow gas production. The calculation of property taxes for pipelines and wells is based on a prescribed formula methodology which disregards depletion and depreciation and results in a tax assessment base that grossly misrepresents the

value of Perpetual's shallow gas, mature pipeline assets in particular. The result is that high property taxes are completely eliminating positive operating cash flow on most shallow gas properties at current natural gas prices.

Refine elements of production growth strategy for 2017 to 2020

- After multiple delays related to transportation restrictions, production from the Company's non-operated Duvernay evaluation well at Waskahigan commenced in December of 2015, flowing at an average daily gross production rate for December of 289 bbl/d of oil/condensate with 277 Mcf/d of liquids-rich gas. A downhole pump assembly will be installed in the first quarter of 2016 to maintain steady production and continue to enhance the understanding of the long term production capability and flow characteristics of the Duvernay formation on this acreage. This well is the first test well on the Company's 6,240 acre block in the Waskahigan area that was farmed out in 2014. Perpetual retains a 35 percent working interest ("WI") in this well and 3,840 gross acres as well as a 100 percent working interest in an additional 2,400 acres. Perpetual estimates that full scale development could include between 50 and 70 future gross locations.
- The Company initiated further strategic technology evaluation at Panny during 2015, with spending of $4.6 million to complete a horizontal well with instrumentation and an electrical heater, drill two (2.0 net) observation wells and construct a bitumen battery related to the cyclic heat stimulation ("CHS") test, the first stage of the Low Pressure Electro Thermally Assisted Drive ("LEAD") pilot project. The project achieved first heat in the ground in mid-October with production expected in the first quarter of 2016 upon flowback after the initial heating cycle.
- The Company continued to closely monitor competitor activity and technical performance in the Colorado formation in the greater Mannville area of east central Alberta. Integrating learnings from new activity, the Company has fine-tuned the geological model, refined mapping, and modified forecast type curves to reflect new completion technologies. Perpetual is ready to execute a pilot project to evaluate the economic potential for full scale development of this shallow tight gas resource, pending recovery of natural gas prices. Perpetual has material exposure to the large resource in the Colorado formation in east central Alberta, with over 1,200 net prospective sections of land captured and an extensive plant and pipeline infrastructure in this shallow resource play fairway.
- Exploration, evaluation and development planning is ongoing for Perpetual's approximately 10,000 net acres of land prospective for horizontal development in multiple zones in the deep basin in the Columbia area of West Central Alberta.

2015 ANNUAL FINANCIAL AND OPERATING HIGHLIGHTS

- Perpetual's exploration and development spending in 2015 totaled $75.4 million, with $67.5 million focused on liquids-rich development at East Edson, $1.4 million for the continuation of waterflood activities in Mannville and $4.6 million at Panny to initiate the first phase of the planned technology pilot for bitumen extraction.
- Total natural gas, oil and NGL production for the year ended December 31, 2015 of 19,706 boe/d was four percent lower than 2014 (20,554 boe/d). Production volumes from the new East Edson gas plant largely offset lost production volumes associated the disposition of non-core Mannville heavy oil assets during the fourth quarter of 2014, the West Edson property swap which closed April 1, 2015 and natural declines with the Company's decision to defer development spending in response to the low commodity price environment.
- Perpetual's natural gas production of 104.2 MMcf/d increased slightly from 2014 (102.7 MMcf/d) reflecting production increases related to the 2014 and 2015 development program as well as production through the new East Edson gas plant which came online July 15, 2015.
- NGL production of 711 bbl/d in 2015 increased 32 percent from 537 bbl/d in 2014 primarily as a result of higher liquids yields from production processed through the new East Edson gas plant relative to 2014 when production was processed through West Edson. Reduced NGL production resulting from the second quarter 2015 West Edson swap and processing changes were offset by a 76 percent increase in East Edson NGL production relative to 2014.
- Oil production of 1,626 bbl/d for 2015 was 44 percent lower than 2014 (2,906 bbl/d) mainly due to the disposition of non-core Mannville heavy oil assets during the fourth quarter of 2014 combined with natural declines and the decision to defer crude oil drilling activities and waterflood spending in light of depressed crude oil prices.
- Revenues of $142.4 million in 2015 decreased 46 percent from 2014, primarily due to lower commodity prices with effectively flat year over year overall production performance.
- Royalty expense of $16.3 million in 2015 represented a combined royalty rate of 11.5 percent compared to 12.2 percent in 2014. Average crown royalty rates decreased to 3.1 percent in 2015 compared to 6.3 percent in 2014 as a result of lower commodity prices as well as increased production from new East Edson wells which benefited from reduced rates and credits received under the Crown's natural gas deep drilling program. Freehold and overriding royalty rates for the year ended December 31, increased from 6.0 percent in 2014 to 8.4 percent in 2015 as a result of the full year effect of the additional gross overriding royalties beginning July 1, 2014 with the payment of the East Edson royalties.
- Total production and operating expenses decreased 17 percent to $65.1 million ($9.06/boe) for 2015 compared to $78.1 million ($10.41/boe) for 2014, reflecting company-wide cost saving initiatives, the re-deployment of operations personnel to abandonment and reclamation projects, and start-up of the new low cost Company owned and operated gas plant at East Edson.
- Operating netbacks decreased 57 percent to $7.44/boe in 2015 (2014 - $17.44/boe) with the dramatic decrease in commodity prices more than offsetting lower operating costs and decreased royalties.
- Driven by the $106.6 million drop in revenue related to commodity price declines, funds flow was eroded to $2.0 million in 2015 (2014 - $81.4 million) despite consistent production levels year-over-year and significant corporate cost-savings initiatives throughout 2015 reducing operating, transportation costs and general and administrative expenses.
- The Corporation recorded a net loss of $89.3 million in 2015 which included a $104.8 million unrealized loss on the market value of TOU Shares based on the decrease in trading price from $38.32/share on April 1, 2015 to $22.35/share on December 31, 2015 as well as a

$23.7 impairment loss primarily recorded on the Company's shallow gas assets including the de-recognition of close to 20 Bcf of reserves previously shut-in due to the gas over bitumen regulatory issue.

2015 RESERVE HIGHLIGHTS

- Total proved and probable reserves of 77.8 MMboe at December 31, 2015 were effectively flat year over year, adjusting for the West Edson swap for TOU Shares of 23.5 MMboe and the de-recognition of 3.3 MMboe of probable shut-in Gas Over Bitumen ("GOB") reserves in 2015.
- Proved reserves of 44.4 MMboe at year-end 2015 reflected dispositions of 12.4 MMboe of proved reserves, primarily at West Edson and production of 7.1 MMboe, down from 56.5 MMboe at year end 2014.
- On a commodity basis, oil and NGL represent ten percent of Perpetual's total proved and probable reserves (nine percent of proved) at December 31, 2015.
- Positive technical proved reserve revisions in both eastern Alberta shallow gas assets and East Edson offset negative proved reserve revisions due to decreased forecast prices and annual production of 7.1 MMboe, highlighting positive operational performance in both the Company's mature, legacy shallow gas as well as its diversifying deep basin growth assets.
- Reserves from Perpetual's liquids-rich gas and NGL in East Edson area grew 14 percent, offsetting production of 2.9 MMboe to represent 73 percent of Perpetual's total proved and probable reserves at year end 2015.

Reserves Disclosure

Working interest reserves included herein refer to working interest reserves before royalty deductions. Reserves information is based on an independent reserves evaluation report prepared by McDaniel with an effective date of December 31, 2015 (the "McDaniel Report"), and has been prepared in accordance with National Instrument 51-101 ("NI 51-101") using McDaniel's forecast prices and costs. Complete NI 51-101 reserves disclosure including after-tax reserve values, reserves by major property and abandonment costs will be included in Perpetual's Annual Information Form ("AIF"), available on the Corporation's website at www.perpetualenergyinc.com and SEDAR at www.sedar.com. Perpetual's reserves at December 31, 2015 are summarized below.

Reserves Summary

Working Interest Reserves at December 31, 2015[(1)]

	Light and Medium Crude Oil (Mbbl)	Heavy Oil (Mbbl)	Conventional Natural Gas (MMcf)	Natural Gas Liquids (Mbbl)	Oil Equivalent (Mboe)
Proved Producing	60	1,227	94,819	550	17,641
Proved Non-Producing	-	53	9,375	5	1,621
Proved Undeveloped	10	355	138,410	1,688	25,122
Total Proved	**70**	**1,636**	**242,604**	**2,243**	**44,383**
Probable Producing	29	633	31,072	174	6,015
Probable Non-Producing	-	89	17,528	3	3,014
Probable Undeveloped	4	358	130,588	2,251	24,378
Total Probable	**33**	**1,081**	**179,188**	**2,428**	**33,407**
Total Proved and Probable	**103**	**2,716**	**421,792**	**4,671**	**77,790**

(1) May not add due to rounding

Future Development Capital[(1)]

($ millions)	2016	2017	2018	2019	2020	Remainder	Total
Eastern Alberta Shallow Gas	0.2	2.0	1.6	4.4	0.4	0.6	9.2
Mannville Heavy Oil	-	6.0	3.8	-	-	-	9.8
Greater Edson Wilrich	36.3	48.4	61.2	47.9	46.1	199.7	439.6
Total	**36.5**	**56.4**	**66.6**	**52.3**	**46.5**	**200.3**	**458.7**

(1) May not add due to rounding

NET ASSET VALUE

McDaniel's estimate of net present value (NPV8%) of Perpetual's reserves at year-end 2015 was $388.6 million, down from $479.1 million at year-end 2014 adjusted for the West Edson property swap for TOU Shares to which no reserves or value are allocated. The decrease in net present value of reserves reflected materially lower future commodity price forecasts, other asset dispositions and the de-recognition of GOB reserves. The effect of these adjustments were partially offset by lower future development costs ("FDC") in 2015 as a result of changes in well design and efficiencies supported by actual drilling experience.

Perpetual's reserve-based net asset value ("NAV") (discounted at eight percent) at year-end 2015 is estimated at $247.2 million ($0.65 per share). On a pro forma basis at December 31, 2015, after reflecting the shares issued and net proceeds of the Rights Offering, the estimated NAV is $0.26 per share. Giving effect to the Rights Offering and proposed twenty for one share consolidation, as described above, Perpetual's

NAV (discounted at eight percent) at year end 2015 is estimated at $5.15 per share. See table under the heading "Net Asset Value" below for a description of the Company calculates NAV.

The following net asset value table shows what is normally referred to as a "produce-out" NAV calculation under which the Corporation's reserves would be produced at forecast future prices and costs. The value is a snapshot in time and is based on various assumptions including commodity prices and foreign exchange rates that vary over time. It should not be assumed that the NAV represents the fair market value of Perpetual's shares. The calculations below do not reflect the value of the Corporation's prospect inventory to the extent that the prospects are not recognized within the NI 51-101 compliant reserve assessment, except as they are valued through the estimate of the fair market value of undeveloped land.

Pre-tax NAV at December 31, 2015[(1)]

		Discounted at			
($ millions, except as noted)	**Undiscounted**	**5%**	**8%**	**10%**	**15%**
Total Proved and Probable Reserves[(2)]	739.4	485.8	388.6	338.6	245.5
TOU Shares[(3)]	145.3	145.3	145.3	145.3	145.3
Fair Market Value of Undeveloped Land[(4)]	83.0	83.0	83.0	83.0	83.0
Warwick Gas Storage[(5)]	25.3	25.3	25.3	25.3	25.3
Net Bank Debt[(1,6)]	(55.8)	(55.8)	(55.8)	(55.8)	(55.8)
Financing Arrangement[(7)]	(21.3)	(21.3)	(21.3)	(21.3)	(21.3)
Senior Notes	(275.0)	(275.0)	(275.0)	(275.0)	(275.0)
Estimate of Additional Future Abandonment and Reclamation Costs[(8)]	(37.0)	(36.5)	(22.8)	(15.7)	(6.9)
Hedge Book[(9)]	(20.1)	(20.1)	(20.1)	(20.1)	(20.1)
NAV	**593.8**	**330.7**	**247.2**	**204.3**	**123.0**
Shares Outstanding (million) – basic	382.3	382.3	382.3	382.3	382.3
NAV per Share ($/share)	**1.55**	**0.87**	**0.65**	**0.53**	**0.32**

(1) Financial information is per Perpetual's 2015 consolidated financial statements.
(2) Reserve values per McDaniel Report as at December 31, 2015.
(3) TOU Share value based on 6.5 million shares at December 31, 2015 closing price ($22.35/share)
(4) Independent third party estimate, excludes undeveloped land in West Central Alberta with reserves assigned.
(5) Reflects 30% interest in Warwick Gas Storage at carrying amount on December 31, 2015.
(6) Includes bank debt, net of working capital.
(7) Reflects notional amount of financing arrangement.
(8) Amounts are in addition to amounts in the McDaniel report for future well abandonment costs, net of salvage value, related to developed reserves. See "ABANDONMENT AND RECLAMATION COSTS".
(9) Hedging adjustments as at December 31, 2015 relative to McDaniel price forecast.

The above evaluation includes future capital expenditure expectations required to bring undeveloped reserves recognized by McDaniel that meet the criteria for booking under NI 51-101 on production. The fair market value of undeveloped land does not reflect the value of the Company's extensive prospect inventory which is anticipated to be converted into reserves and production over time through future capital investment. Additionally, no value has been assigned to reflect the investment to date in the ongoing bitumen extraction pilot project at Panny.

The NAV calculated at December 31, 2015 does not include the impact of the Rights Offering, which closed on January 18, 2016, or the proposed share consolidation on a twenty for one basis, which is expected to be effective on or about March 24, 2016. As such, the following pro forma NAV is presented to illustrate the effect of these two items at December 31, 2015.

Pre-tax NAV at December 31, 2015 pro forma Rights Offering and Share Consolidation

		Discounted at			
($ millions, except as noted)	**Undiscounted**	**5%**	**8%**	**10%**	**15%**
NAV at December 31, 2015	**593.8**	**330.7**	**247.2**	**204.3**	**123.0**
Rights Offering Proceeds[(1)]	22.9	22.9	22.9	22.9	22.9
Pro Forma NAV	**616.7**	**353.6**	**270.1**	**227.2**	**145.9**
Shares Outstanding (million) – basic[(2)]	52.4	52.4	52.4	52.4	52.4
NAV per Share ($/share)	**11.77**	**6.75**	**5.15**	**4.34**	**2.78**

(1) Based on the estimated net proceeds of $22.9 million received by the Company on closing of the Rights Offering.
(2) Based on 382.1 million common shares at December 31, 2015 with an additional 665.4 million common shares issued on closing of the Rights Offering and reflecting the proposed share consolidation on the basis of twenty to one common share.

2016 OUTLOOK

In 2016, Perpetual's has identified its top four strategic priorities which include:

1. Reduce debt and restore cash flow;
2. Grow value and scope of Greater Edson liquids-rich gas;
3. Maximize value potential of Eastern Alberta assets; and
4. Advance high impact opportunities.

With projected further low commodity prices in 2016, Perpetual will prioritize liquidity management and preservation of its balance sheet through restricted spending and a focus on reducing costs and maximizing efficiencies in administration and operations. A diligent focus on reductions in all areas of spending, including operating, financing and administrative costs, will continue in order to establish a sustainable cost structure in this low commodity price environment.

In order to protect a base level of funds flow, Perpetual has commodity price contracts in place in 2016 on an estimated 70 percent of forecast production from the remainder of the year. These include both AECO and NYMEX natural gas contracts from April to December 2016 on close to 70,000 GJ/d at an estimated price of $2.19/GJ; and oil sales arrangements on 1,000 bbl/d protecting a floor price at WTI of $USD43.50/bbl.

In light of the continued deterioration of commodity prices since December 2015, Perpetual has reduced its capital spending program for 2016 and Perpetual's Board of Directors has restricted its approval to a first quarter capital expenditure budget of $6 million. Approved first quarter spending is limited to drilling one (1.0 net) well at East Edson with minimal additional capital allocated to continue strategic production testing at Panny and Waskahigan, critical facility maintenance and overhauls, and third party abandonment and reclamation activity. Completion and tie in of the new East Edson well along with additional capital activity for the remainder of the year will be deferred and assessed on a project economics basis as the year progresses.

Perpetual continues to target strategic asset sales in 2016. In early March, the Company closed a purchase and sale agreement for the disposition of 37 sections of its 425 net sections of oil sands leases in northeast Alberta in exchange for gross proceeds of $6.1 million and a one percent gross overriding royalty. Proceeds from the disposition were initially applied against outstanding debt.

FINANCIAL AND OPERATING HIGHLIGHTS

	THREE MONTHS Ended December 31			YEAR ENDED December 31,		
(Cdn$ thousands except volume and per share amounts)	**2015**	2014	Change	**2015**	2014	Change
Financial						
Oil and natural gas revenue	**33,044**	62,562	(47%)	**142,437**	262,790	(46%)
Funds flow(1)	**362**	17,316	(98%)	**2,004**	81,395	(98%)
Per share(1)(2)	**-**	0.12	(100%)	**0.01**	0.55	(98%)
Net earnings (loss)	**(93,539)**	(18,273)	(412%)	**(89,274)**	3,366	(2752%)
Per share(2)	**(0.61)**	(0.12)	(417%)	**(0.59)**	0.02	(3050%)
Total assets	**603,450**	750,602	(20%)	**603,450**	750,602	(20%)
Net bank debt outstanding(1)	**55,832**	21,867	155%	**55,832**	21,867	155%
Senior notes, at principal amount	**275,000**	275,000	-	**275,000**	275,000	-
Share forward financial obligation, at carrying amount	**18,059**	-	100%	**18,059**	-	100%
Carrying value of marketable securities	**(145,275)**	-	-	**(145,275)**	-	-
Convertible debentures, at principal amount	**-**	34,878	(100%)	**-**	34,878	(100%)
Total net debt(1)	**203,616**	331,745	(39%)	**203,616**	331,745	(39%)
Capital expenditures						
Exploration and development(3)	**715**	26,018	(97%)	**76,957**	116,457	34%
Dispositions, net of Acquisitions	**-**	(20,595)	(100%)	**(23,710)**	(70,351)	(66%)
Other	**25**	84	(70%)	**910**	614	48%
Net capital expenditures	**740**	5,507	(87%)	**54,157**	46,720	16%
Common shares outstanding (thousands)						
End of period	**382,288**	150,077	155%	**382,288**	150,077	155%
Weighted average	**151,638**	149,084	2%	**150,140**	149,084	1%
Operating						
Average production						
Natural gas (MMcf/d)(4)	**105.1**	122.5	(14%)	**104.2**	102.7	1%
Oil and NGL (bbl/d)(4)	**2,144**	3,262	(34%)	**2,337**	3,443	(32%)
Total (boe/d)	**19,661**	23,685	(17%)	**19,706**	20,554	(4%)
Average prices						
Natural gas, before derivatives ($/Mcf)	**2.74**	3.96	(31%)	**2.87**	4.50	(36%)
Natural gas, including derivatives ($/Mcf)	**2.92**	4.16	(30%)	**3.01**	4.36	(31%)
Oil, before derivatives ($/bbl)	**33.04**	59.80	(45%)	**41.27**	75.21	(45%)
Oil, including derivatives ($/bbl)	**39.81**	67.05	(41%)	**52.48**	71.55	(27%)
NGL ($/bbl)	**33.68**	59.63	(44%)	**33.72**	73.97	(54%)
Drilling (wells drilled gross/net)						
Gas	**-**	11/10.0		**6/4.5**	29/20.9	
Oil	**-**	-		**-**	20/17.8	
Observation/Service	**-**	-		**2/2.0**	-	
Total	**-**	11/10.0		**8/6.5**	49/38.7	
Success rate (%)	**-**	100/100		**100/100**	100/100	

(1) These are non-GAAP measures. Please refer to "Non-GAAP Measures" below.
(2) Based on weighted average basic common shares outstanding for the period.
(3) Exploration and development costs include geological and geophysical expenditures.
(4) Production amounts are based on the Corporation's interest before royalty expense.

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following is management's discussion and analysis ("MD&A") of Perpetual Energy Inc.'s ("Perpetual", the "Company" or the "Corporation") operating and financial results for the year ended December 31, 2015 as well as information and estimates concerning the Corporation's future outlook based on currently available information. This discussion should be read in conjunction with the Corporation's audited consolidated financial statements and accompanying notes for the years ended December 31, 2015 and 2014. The Corporation's consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles ("GAAP") which require publicly accountable enterprises to prepare their financial statements using International Financial Reporting Standards ("IFRS"). Readers are referred to the advisories for additional information regarding forecasts, assumptions and other forward-looking information contained in the "Forward Looking Information and Statements" section of this MD&A. The date of this MD&A is March 2, 2016.

NATURE OF BUSINESS: Perpetual is an oil and natural gas exploration, production and marketing company headquartered in Calgary, Alberta. Perpetual has a spectrum of opportunities in its resource-style portfolio of assets to support its value strategy, including liquids-rich natural gas assets in the deep basin of west central Alberta, heavy oil in eastern Alberta, oil sands leases in northern Alberta and an interest in a natural gas storage business, all of which complement the Corporation's legacy shallow gas production and resource base. Additional information on Perpetual, including the most recent filed Annual Information Form ("AIF"), can be accessed at www.sedar.com or from the Corporation's website at www.perpetualenergyinc.com.

ADVISORIES

NON-GAAP MEASURES: This document contains the following non-GAAP financial measures which do not have any standardized meaning prescribed by GAAP and are therefore unlikely to be comparable to similar measures presented by other issuers. Non-GAAP measures presented in this document should not be viewed as alternatives to measures of financial performance calculated in accordance with GAAP.

Operating netback: Perpetual considers operating netback an important performance measure as it demonstrates its profitability relative to current commodity prices. Operating netbacks are calculated by deducting royalties, operating costs, and transportation from realized revenue. Operating netbacks are also calculated on a per boe basis using average boe production for the period. Operating netbacks on a per boe basis can vary significantly for each of the Company's operating areas.

Funds flow: Management uses cash flow from operating activities before changes in non-cash working capital, changes in long term Crown receivable, settlement of decommissioning obligations and certain exploration and evaluation ("E&E") costs, but after payments on the gas over bitumen ("GOB") related financial obligation, as described below ("funds flow"), funds flow per share and annualized funds flow to analyze operating performance and leverage. Funds flow is reconciled to its closest GAAP measure, cash flow from operating activities, as follows:

Funds flow GAAP reconciliation

	Three months ended December 31,		Year ended December 31,	
(*$ thousands, except per share amounts*)	**2015**	2014	**2015**	2014
Cash flow from operating activities	**6,575**	17,666	**12,406**	82,082
Exploration and evaluation costs[1]	**(93)**	379	**1,526**	644
Payments on financial obligation[2]	**(826)**	(1,446)	**(3,704)**	(2,829)
Expenditures on decommissioning obligations	**2,395**	2,153	**7,589**	6,633
Long term Crown receivable adjustments	**–**	–	**–**	(10,997)
Changes in non-cash working capital	**(7,689)**	(1,436)	**(15,813)**	5,862
Funds flow	**362**	17,316	**2,004**	81,395
Funds flow per share[3]	**0.00**	0.12	**0.01**	0.55

(1) The Corporation expenses exploratory dry hole costs, geological and geophysical costs, lease rentals on undeveloped properties and the cost of expired leases in the period incurred. To make reported funds flow in this MD&A more comparable to industry practice the Corporation reclassifies dry hole costs, geological and geophysical costs from operating to investing activities in the funds flow reconciliation.

(2) These payments are indexed to GOB revenue and recorded as a reduction to the Corporations financial obligation in accordance with IFRS. To present GOB revenue net of these payments, the Corporation has reclassified these payments from financing to operating activities in the calculation of funds flow.

(3) Based on weighted average shares outstanding for the period.

Realized revenue: Realized revenue includes oil and natural gas revenue, realized gains (losses) on financial natural gas and crude oil contracts, and call option premiums received. Realized revenue is used by management to calculate the Corporation's net realized commodity prices taking into account monthly settlements on financial crude oil and natural gas forward sales, collars and basis differentials. These contracts are put in place to protect Perpetual's funds flow from potential volatility in commodity prices, and as such any related realized gains or losses are considered part of the Corporation's realized price.

GOB revenue, net of payments: GOB revenue, net of payments includes GOB revenue less monthly payments on the GOB related financial obligation. This is used by management to calculate the Corporation's net realized GOB revenue to reflect the substantive monetization of the future GOB royalty credits.

Adjusted working capital deficiency (surplus): Adjusted working capital deficiency (surplus) includes total current assets and current liabilities and long term Crown receivables excluding short-term derivative assets and liabilities related to the Corporation's risk management activities, current portion of financial obligation, current portion of TOU Share financial arrangement, current portion of provisions, current portion of convertible debentures, assets held for sale, liabilities associated with assets held for sale and current bank indebtedness.

Net debt and net bank debt: Net bank debt is measured as current and long term bank indebtedness including adjusted working capital deficiency (surplus). Net debt includes the carrying value of net bank debt and the TOU Share financial arrangement and the principal amount of senior notes and convertible debentures reduced for the mark-to-market value of common shares of Tourmaline Oil Corp. ("TOU Shares") held. Net bank debt and net debt are used by management to analyze leverage.

Total capitalization: Total capitalization is equal to net debt plus market value of issued equity and is used by management to analyze leverage. Total capitalization is not intended to represent the total funds from equity and debt received by the Corporation upon issuance.

VOLUME CONVERSIONS: Barrel of oil equivalent ("boe") may be misleading, particularly if used in isolation. In accordance with National Instrument 51-101 ("NI 51-101"), a conversion ratio for natural gas of 6 Mcf:1 bbl has been used, which is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. In addition, utilizing a conversion on a 6 Mcf:1 bbl basis may be misleading as an indicator of value as the value ratio between natural gas and crude oil, based on the current prices of natural gas and crude oil, differ significantly from the energy equivalency of 6 Mcf:1 bbl.

FORWARD-LOOKING INFORMATION AND STATEMENTS: Certain information and statements contained in this MD&A including management's assessment of future plans and operations and including the information contained under the heading "2016 Outlook" may constitute forward-looking information and statements within the meaning of applicable securities laws. This information and these statements relate to future events or to future performance. All statements other than statements of historical fact may be forward-looking information and statements. The use of any of the words "anticipate", "continue", "estimate", "expect", "may", "will", "project", "should", "believe", "outlook", "guidance", "objective", "plans", "intends", "targeting", "could", "potential", "strategy" and any similar expressions are intended to identify forward-looking information and statements.

In particular, but without limiting the foregoing, this MD&A contains forward-looking information and statements pertaining to the following: the quantity and recoverability of Perpetual's reserves; the timing and amount of future production; future prices as well as supply and demand for natural gas, natural gas liquids ("NGL") and oil; the existence, operations and strategy of the commodity price risk management program; the approximate amount of forward sales and financial contracts to be employed, and the value of financial forward natural gas, oil and other risk management contracts; the expected impact of cost-savings initiatives on operating and general and administrative expenses; funds flow sensitivities to commodity price, production, foreign exchange and interest rate changes; operating, general and administrative ("G&A"), and other expenses; the costs and timing of future abandonment and reclamation, asset retirement and environmental obligations; the use of exploration and development activity, prudent asset management, and acquisitions to sustain, replace or add to reserves and production or expand the Corporation's asset base; the Corporation's acquisition and disposition strategy and the existence of acquisition and disposition opportunities, the criteria to be considered in connection therewith and the benefits to be derived therefrom; Perpetual's ability to benefit from the combination of growth opportunities and the ability to grow through the capital expenditure program; expected compliance with credit facility covenants in 2016; the retention of, and benefits to be received from holding TOU Shares; expected book value and related tax value of the Corporation's assets and prospect inventory and estimates of net asset value; funds flow; ability to fund exploration and development; the corporate strategy; expectations regarding Perpetual's access to capital to fund its acquisition, exploration and development activities; the effect of future accounting pronouncements and their impact on the Corporation's financial results; future income tax and its effect on funds flow; intentions with respect to preservation of tax pools and taxes payable by the Corporation; funding of and anticipated results from capital expenditure programs; renewal of and borrowing costs associated with the credit facility; future debt levels, financial capacity, liquidity and capital resources; future contractual commitments; drilling, completion, facilities, construction and waterflood plans, and the effect thereof; the impact of Canadian federal and provincial governmental regulation on the Corporation relative to other issuers; Crown royalty rates; Perpetual's treatment under governmental regulatory regimes; business strategies and plans of management including future changes in the structure of business operations and debt reduction initiatives; and the reliance on third parties in the industry to develop and expand Perpetual's assets and operations.

The forward-looking information and statements contained in this MD&A reflect several material factors, expectations and assumptions of the Corporation including, without limitation, that Perpetual will conduct its operations in a manner consistent with its expectations and, where applicable, consistent with past practice; the general continuance of current or, where applicable, assumed industry conditions; the continuance of existing, and in certain circumstances, the implementation of proposed tax, royalty and regulatory regimes; the ability of Perpetual to obtain equipment, services, and supplies in a timely manner to carry out its activities; the accuracy of the estimates of Perpetual's reserve and resource volumes; the timely receipt of required regulatory approvals; certain commodity price and other cost assumptions; the timing and costs of storage facility and pipeline construction and expansion and the ability to secure adequate product transportation; the continued availability of adequate debt and/or equity financing and funds flow to fund the Corporation's capital and operating requirements as needed; and the extent of Perpetual's liabilities.

The Corporation believes the material factors, expectations and assumptions reflected in the forward-looking information and statements are reasonable but no assurance can be given that these factors, expectations and assumptions will prove to be correct. The forward-looking information and statements included in this MD&A are not guarantees of future performance and should not be unduly relied upon. Such information and statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking information or statements including, without limitation: volatility in market prices for oil and natural gas products; supply and demand regarding Perpetual's products; risks inherent in Perpetual's operations, such as production declines, unexpected results, geological, technical, or drilling and process problems; unanticipated operating events that can reduce production or cause production to be shut-in or delayed; changes in exploration or development plans by Perpetual or by third party operators of Perpetual's properties; reliance on industry partners; uncertainties or inaccuracies associated with estimating reserves volumes; competition for, among other things; capital, acquisitions of reserves, undeveloped lands, skilled personnel, equipment for drilling, completions, facilities and pipeline construction and maintenance; increased costs; incorrect assessments of the value of acquisitions; increased debt levels or debt service requirements; industry conditions including fluctuations in the price of natural gas and related commodities; royalties payable in respect of Perpetual's production; governmental regulation of the oil and gas industry, including environmental regulation; fluctuation in foreign exchange or interest rates; the need to obtain required approvals from regulatory authorities; changes in laws applicable to the Corporation, royalty rates, or other regulatory matters; general economic conditions in Canada, the United States and globally; stock market volatility and market valuations; limited, unfavorable, or a lack of access to capital markets, and certain other risks detailed from time to time in Perpetual's public disclosure documents. The foregoing list of risk factors should not be considered exhaustive.

The forward-looking information and statements contained in this MD&A speak only as of the date of this MD&A, and neither the Corporation nor any of its subsidiaries assumes any obligation to publicly update or revise them to reflect new events or circumstances, unless expressly required to do so by applicable securities laws.

RECAPITALIZATION TRANSACTIONS AND RECENT DEVELOPMENTS

To improve liquidity and address financial liabilities due in the fourth quarter of 2015, including a margin loan secured by the pledge of 5.5 million TOU Shares ("Margin Loan"), which was due on November 30, 2015 and the Company's 7.00% Convertible Debentures, which matured on December 31, 2015. Perpetual completed the following recapitalization transactions:

- The execution of a new financing arrangement during the fourth quarter that provided net proceeds of $18.2 million collateralized by one million TOU Shares ("TOU Share financial arrangement");
- Extension of Perpetual's current bank lending arrangements to October 31, 2016 with total borrowing capacity of $62 million, comprised of a $20.0 million demand loan and a $42.0 million margin loan secured by 5.5 million TOU shares;
- Settlement of its 7.00% Convertible Debentures due December 31, 2015 (the "Debentures") with approximately 228.9 million common shares of Perpetual; and
- A $25.0 million fully backstopped rights offering (the "Rights Offering") which closed on January 18, 2016. The Company issued 665.4 million common shares on closing of the Rights Offering.

The effect of these recapitalization transactions extended the term of the Company's earliest maturing debt to October 31, 2016, infused additional liquidity through the Rights Offering for ongoing capital programs and provided a reduction to debt. At the same time, the combined transactions preserve liquidity to manage downside risk while allowing for retention of potentially undervalued assets in the current low commodity price environment.

Following the closing of the Rights Offering on January 18, 2016, the Company had 1,047.7 million shares outstanding. Perpetual has provided notice to its shareholders of its annual and special meeting, scheduled to be held on March 24, 2016. At the meeting shareholders will vote on a proposed share consolidation which, if approved, would result in a consolidation of common shares on a twenty for one basis.

SELECTED ANNUAL INFORMATION

($ thousands, except per share amounts)	**2015**	2014	2013
Financial			
Oil and natural gas revenue	**142,437**	262,790	201,294
Net income (loss)	**(89,274)**	3,366	7,620
Per share[(1)]	**(0.59)**	0.02	0.05
Funds flow	**2,004**	81,395	58,468
Per share[(1) (2)]	**0.01**	0.55	0.39
Total assets	**603,450**	750,602	742,288
Total long term liabilities	**443,648**	507,296	513,836
Net bank debt	**55,832**	21,867	67,201
Senior notes, at principal amount	**275,000**	275,000	150,000
Carrying amount of share forward financial obligation	**18,059**	–	–
Carrying amount of marketable securities[(3)]	**(145,275)**	–	–
Convertible debentures, at principal amount	**–**	34,878	159,779
Total net debt	**203,616**	331,745	376,980
Capital expenditures			
Exploration and development	**75,431**	115,813	95,405
Geological and geophysical costs	**1,526**	644	1,279
Dispositions, net of acquisitions	**(23,710)**	(70,351)	(70,840)
Interest in Warwick Gas Storage (“WGS LP”)	**–**	–	19,129
Other	**910**	614	120
Net capital expenditures	**54,157**	46,720	45,093
Shares outstanding (thousands)			
End of period	**382,288**	150,077	148,490
Weighted average	**150,140**	149,084	148,144
Operating			
Average production			
Natural gas (MMcf/d)	**104.2**	102.7	88.9
Oil (bbl/d)	**1,626**	2,905	3,204
NGL (bbl/d)	**711**	537	656
Total average production (boe/d)	**19,706**	20,554	18,696
Average prices			
Natural gas – before derivatives ($/Mcf)	**2.87**	4.50	3.26
Natural gas – including derivatives ($/Mcf)	**3.01**	4.36	3.53
Oil – before derivatives ($/bbl)	**41.27**	75.21	68.90
Oil – including derivatives ($/bbl)	**52.48**	71.55	66.68
NGL	**33.72**	73.97	61.54
Wells drilled			
Natural gas – gross (net)	**6 (4.5)**	29 (20.9)	6 (3.0)
Crude oil – gross (net)	**– (–)**	20 (17.8)	37 (35.7)
Total – gross (net)	**6 (4.5)**	49 (38.7)	43 (38.7)

(1) Based on weighted average shares outstanding for the year.
(2) See “non-GAAP measure” in this MD&A.
(3) The carrying amount of marketable securities is based on the period end closing price per the Toronto Stock Exchange (“TSX”) ($22.35 per share) and 6.5 million TOU Shares held.

OVERALL PERFORMANCE

Perpetual focused on five key strategic priorities in 2015:

- Reduce debt and improve debt to cash flow ratio;
- Grow greater Edson liquids-rich gas production, cash flow, inventory, reserves and value;
- Optimize value of Mannville heavy oil;
- Maximize value of shallow gas; and
- Refine elements of production growth strategy for 2017 to 2020.

In April 2015 Perpetual swapped its joint interest share in its West Edson asset in West Central with Tourmaline in exchange for 6.75 million TOU Shares having a then current market value of approximately $258.7 million based on the closing price of the TOU Shares on the TSX on April 1, 2015. The transaction included all joint interest lands Perpetual held with Tourmaline in West Edson, together with the associated wells and infrastructure (the "West Edson Property"). Based on the Company's third party engineering report prepared by McDaniel and Associates Consultants Ltd., as at December 31, 2014, the disposition included 7.2 MMboe of recognized proved and probable developed natural gas and natural gas liquids reserves as well as 16.8 MMboe of proved and probable undeveloped reserves with $128 million of associated future development capital. Also included in the transaction were 9,600 net acres of undeveloped lands not currently assigned reserves at year-end 2014. Perpetual's production from the West Edson Property was approximately 5,750 boe/d.

Perpetual continued the development of its West Central liquids-rich natural gas throughout 2015 by maintaining focus on development activities in the East Edson area and meeting its commitments under the East Edson farm-in agreement executed in July 2014. Pursuant to the farm-in agreement, Perpetual committed to spend $30 million to drill, complete and tie-in approximately five wells prior to December 31, 2015. A portion of Perpetual’s first $30 million commitment was spent during 2014, with the balance of the required capital expended with the drilling of three (3.0 net) liquids-rich natural gas wells in the first quarter of 2015. In addition to drilling activities, Perpetual also satisfied its commitment to construct a new gas plant at East Edson. Construction of the new East Edson gas plant was substantially completed in the first half of 2015 and brought online on July 15, 2015 at a capacity of 30 MMcf/d. The new East Edson gas plant was expanded to 45 MMcf/d in mid-September 2015 bringing the total facility cost to $35.6 million. The completion and tie-in of wells drilled late in 2014 and early 2015 were scheduled around capacity availability and transportation restrictions with the start-up and expansion of the new plant. At December 31, 2015, Perpetual had also spent $11.5 million of its remaining $30 million commitment to drill, complete and tie-in approximately six more wells prior to December 31, 2022.

Perpetual's 2015 natural gas production of 104.2 MMcf/d and NGL production of 711 bbls/d increased one and 32 percent respectively from 2014 with new production from the East Edson development program more than offsetting production lost from the swap of the West Edson Property on April 1, 2015 and natural production declines in shallow gas producing areas. As commodity prices continued to decline in 2015, Perpetual chose to restrict further capital spending and deferred all crude oil drilling, resulting in a decrease in crude oil production as a result of natural declines and reflecting the disposition of heavy oil production in the fourth quarter of 2014.

Declining commodity prices through 2015 led to a substantial reduction in oil and natural gas revenues compared to the prior year and resulting 2015 funds flow from operations of $2.0 million in 2015 compared to $81.4 million in 2014. Perpetual's focus through the second half of 2015 and continuing into 2016 has shifted from capital investment and production growth to cost reductions, operating efficiencies and financial recapitalization.

2015 FINANCIAL RESULTS

Capital expenditures

(*$ thousands*)	**2015**	2014
Exploration and development	**75,431**	115,813
Geological and geophysical costs(1)	**1,526**	644
Dispositions, net of acquisitions	**(23,710)**	(70,351)
Other	**910**	614
Total	**54,157**	46,720

(1) Geological and geophysical expenditures and dry hole costs are expensed directly in the Corporation's statement of income (loss); they are considered by Perpetual to be more closely related to investing activities than operating activities, and therefore are included with capital expenditures for the purposes of this MD&A.

Perpetual's exploration and development spending in 2015 totaled $75.4 million, 89 percent of which was concentrated on the West Central Alberta deep basin assets. Capital expenditures included construction and expansion of the new East Edson gas plant and drilling eight (6.5 net) wells, with three (1.5 net) natural gas wells at West Edson prior to the swap transaction with Tourmaline, three (3.0 net) natural gas wells at East Edson and two (2.0 net) observation wells at Panny. Capital spending also included $1.5 million in geological and geophysical spending for completion of two 3D seismic surveys which were initiated in 2014 and completed in 2015 in East Edson and West Edson.

Property dispositions in 2015 included the sale of certain fee simple lands in east central Alberta, along with a working interest in related seismic data, for net proceeds of $21.0 million. Included in the disposition was 206,712 net acres of fee simple lands, a 75 percent ownership in certain proprietary 2D and 3D seismic and approximately 165 Mboe of reserves (82 percent natural gas) associated with royalty interests. The Company also disposed of its interest in certain non-core undeveloped lands for proceeds of $1.2 million and executed an asset swap to acquire an increased interest in existing reserves as well as undeveloped acreage in its core East Edson property in exchange for its working interest in certain undeveloped lands and net proceeds of $1.8 million.

Exploration and development spending by area

(*$ thousands*)	**2015**	2014
West Central liquids-rich gas	**67,501**	81,096
Mannville heavy oil	**1,360**	24,559
Panny bitumen	**4,625**	2,421
Shallow gas	**1,945**	7,737
Total	**75,431**	115,813

The majority of Perpetual's exploration and development spending during 2015 was focused on liquids-rich natural gas development activities in West Central Alberta. Spending on West Central liquids-rich gas projects for 2015 included $21.6 million for construction and first expansion of the East Edson gas plant, which was brought online on July 15, 2015 at a capacity of 30 MMcf/d and expanded to 45 MMcf/d in mid-September 2015. Total project costs for the plant at the end of 2015 were $35.6 million and included construction of a ten inch sales pipeline to a newly constructed TransCanada meter station as well as construction costs for transmission lines and related facilities to supply power to the gas plant. An additional $2.9 million was spent to complete construction of an expanded gathering system, including a main gathering line to facilitate the flow of gas to the new facility.

Development at East Edson in 2015 included drilling three (3.0 net) liquids-rich natural gas wells in the first quarter of 2015 and completion and tie-in of seven (7.0 net) wells including the remaining wells drilled during the fourth quarter of 2014. Three wells were brought online with initial start-up of the East Edson gas plant and two additional wells commenced flowing concurrent with completion of the expanded East Edson 45 MMcf/d gas plant in mid-September. The two remaining wells were brought online in late October and early November with easing of firm service restriction which had been limiting production through the new East Edson gas plant.

Prior to the West Edson swap, exploration and development expenditures in West Central Alberta of $9.0 million was allocated to West Edson to drill three (1.5 net) natural gas wells and complete two (1.0 net) wells in the first quarter of 2015. Wells drilled and completed at West Edson during the first quarter were included in the West Edson Property swap with Tourmaline effective April 1, 2015.

West Central exploration and development spending for 2015 also included $1.6 million for undeveloped land acquisitions and $1.2 million of equip and tie-in costs related to the Corporation's 35 percent working interest in a non-operated Duvernay formation horizontal volatile oil well at Waskahigan.

Waterflood activities continued at Mannville with Perpetual spending $1.4 million on conversion and equipping a water source well, four horizontal well injector conversions as well as surface equipment and pipeline work to arrest production declines and reduce ongoing operating costs on two heavy oil pools. The Corporation currently has seven injectors online in the Sparky Upper Mannville I2I pool and six injectors online in the Upper Mannville B Lloyd pool.

The Company initiated further strategic technology evaluation at Panny during 2015, with spending of $1.0 million to complete a horizontal well with instrumentation and an electrical heater, $1.5 million to drill two (2.0 net) observation wells and $2.1 million to complete construction of a bitumen battery related to the cyclic heat stimulation ("CHS") test, the first stage of the Low Pressure Electro Thermally Assisted Drive ("LEAD") pilot project. The project achieved first heat in the ground in mid-October with production expected in the first quarter of 2016 upon flowback after the initial heating cycle.

Expenditures on decommissioning obligations

During the second half of 2015, as part of a continued focus on cost reductions and value creation, Perpetual scaled up the redeployment of operational personal and internal resources to accelerate progress and drive efficiencies on the Company's abandonment and reclamation projects. Other capital expenditures for 2015 included $0.8 million for the purchase of equipment to be utilized in compliance as well as abandonment and reclamation work at a significant cost reduction to third party equipment rentals. Including an allocation of $1.0 million of costs for internal resources, Perpetual spent $7.6 million during 2015 on abandonment and reclamation projects mainly in eastern Alberta. Perpetual has achieved efficiencies and cost savings in 2015 by utilizing internal labor and equipment rather than third party services for various stages of reclamation and abandonment which resulted in a revision of estimated future abandonment liabilities for all oil and natural gas assets.

Production

	2015	2014
Natural gas (*MMcf/d*)		
Eastern – North	**31.3**	36.4
Eastern – South	**21.5**	23.8
West Central	**51.4**	42.5
Total natural gas	**104.2**	102.7
Crude oil (*bbl/d*)		
Eastern[1]	**1,595**	2,866
West Central	**31**	40
Total crude oil	**1,626**	2,906
Total NGL (*bbl/d*) [2]	**711**	537
Total production (*boe/d*)	**19,706**	20,554

(1) Primarily Mannville heavy oil.
(2) Primarily West Central liquids-rich gas.

Total natural gas, oil and NGL production for the year ended December 31, 2015 of 19,706 boe/d was four percent lower than 2014 (20,554 boe/d). Production volumes from the new East Edson gas plant largely offset lost production volumes associated with the disposition of non-core Mannville heavy oil assets during the fourth quarter of 2014, the West Edson Property swap which closed April 1, 2015 and natural declines with the Company's decision to defer development spending in response to the low commodity price environment.

Despite the disposition of 32.3 MMcf/d of gas production from West Edson effective April 1, 2015 and natural declines on shallow gas properties, Perpetual's natural gas production of 104.2 MMcf/d increased slightly from 2014 (102.7 MMcf/d) reflecting production increases related to the 2014 and 2015 development program as well as production through the new East Edson gas plant which came online July 15, 2015. Production through the facility was restricted to firm transportation commitment levels of 30 MMcf/d until completion of the 15 MMcf/d facility expansion in mid-September when firm transportation was shifted to the new plant. Production from the East Edson development program and facility expansion more than offset natural declines and volumes associated with the exchange of the West Edson Property for TOU Shares effective April 1, 2015. Perpetual's natural gas production is equally comprised of liquids-rich natural gas in West Central and stable shallow gas production in the Eastern areas with a low base decline rate of 12 percent year over year.

NGL production of 711 bbl/d in 2015 increased 32 percent from 537 bbl/d in 2014 primarily as a result of higher liquids yields from increased East Edson production relative to West Edson. Lost NGL volumes associated with the West Edson swap and processing changes were offset by a 76 percent increase in East Edson NGL production relative to 2014. Condensate production in 2015 increased 13 percent to 479 bbl/d compared to 425 bbl/d in 2014.

Oil production of 1,626 bbl/d for 2015 was 44 percent lower than 2014 (2,906 bbl/d) mainly due to the disposition of non-core Mannville heavy oil assets during the fourth quarter of 2014 combined with natural declines and the decision to defer crude oil drilling activities and waterflood spending in light of depressed crude oil prices.

Commodity prices

	2015	2014
Reference prices		
AECO Monthly Index (*$/GJ*)	**2.62**	4.19
AECO Daily Index (*$/GJ*)	**2.55**	4.27
Alberta Gas Reference Price (*$/GJ*)(1)	**2.44**	4.17
West Texas Intermediate ("WTI") light oil (*$USD/bbl*)	**48.79**	92.99
Western Canadian Select ("WCS") differential (*$USD/bbl*)	**(13.52)**	(19.40)
Average Perpetual prices		
Natural gas		
Before derivatives (*$/Mcf*)(2)(3)	**2.87**	4.50
Percent of AECO Monthly Index	**97**	98
Including derivatives (*$/Mcf*)	**3.01**	4.36
Percent of AECO Monthly Index	**102**	95
Oil		
Before derivatives (*$/bbl*)	**41.27**	75.21
Including derivatives (*$/bbl*)	**52.48**	71.55
NGL (*$/bbl*)	**33.72**	73.97

(1) Alberta Gas Reference Price is the price used to calculate Alberta Crown royalties.
(2) Natural gas price before derivatives includes physical forward sales contracts for which delivery was made during the reporting period but excludes realized gains and losses on financial derivatives.
(3) The average conversion ratio for Perpetual's 2015 natural gas production is 1.12 GJ:1 Mcf (2014 – 1.10 GJ:1 Mcf).

Significant declines in benchmark prices on all commodities continued to affect Perpetual's 2015 realized pricing compared to the prior year. Average AECO Monthly Index pricing of $2.62/GJ in 2015 was 37 percent lower than $4.19/GJ in 2014 as low weather-related demand and continued natural gas production growth extended the oversupply situation in North America. The decrease of WTI to $USD48.79/bbl in 2015 from $USD92.99/bbl in 2014 was partially offset by a narrowing of WTI to WCS differential pricing and a weaker Canadian dollar. Oversupply in the propane and butane market throughout 2015 has resulted in above average storage levels and amplified downward pressure on market NGL pricing.

Decreased AECO Monthly Index prices were reflected in Perpetual's natural gas price before derivatives of $2.87/Mcf, down 36 percent from $4.50/Mcf in 2014. Perpetual's average realized gas price, including derivatives, decreased 31 percent to $3.01/Mcf for the year ended December 31, 2015 from $4.36/Mcf in 2014. The Corporation's realized 2015 natural gas price with derivatives includes $2.0 million of realized gains on natural gas derivatives and $3.2 million of gains realized on crystallizations of contracts before maturity.

Perpetual's 2015 oil price, before derivatives, of $41.27/bbl decreased 45 percent compared to 2014 due primarily to the 48 percent decline in global oil pricing and includes adjustments related to the WTI to WCS differential and crude quality. Perpetual's realized oil price of $52.48/bbl, including derivatives, was higher than the price before derivatives due to gains of $2.9 million recorded on financial crude oil derivative contracts and $3.8 million of gains realized on crystallizations of contracts before maturity.

Perpetual's realized average NGL price decreased 54 percent from the prior year to $33.72/bbl, reflecting the drop in all NGL component prices as NGL supply growth has been bottlenecked by infrastructure in many regions of North America resulting in excess inventory levels.

Commodity price risk management

Perpetual's commodity price risk management strategy is focused on managing downside risk and increasing certainty in funds flow by mitigating the effect of commodity price volatility. Physical forward sales and financial derivatives are used to manage the balance sheet, to lock in economics on capital programs and acquisitions, and to take advantage of perceived anomalies in commodity markets. Perpetual also utilizes foreign exchange swaps and physical or financial swaps related to the differential between natural gas prices at the AECO and NYMEX trading hubs and oil basis differentials between WTI and WCS in order to mitigate the effects of fluctuations in foreign exchange rates and basis differentials on the Corporation's realized revenue.

Natural Gas

Perpetual has in place natural gas financial contracts on an estimated 70 percent of forecasted natural gas production for 2016. The following tables provide a summary of derivative natural gas contracts outstanding at March 2, 2016. Subsequent to December 31, 2015, Perpetual realized gains of $1.6 million on crystallizations of 60,000 mmbtu per day of 2017 NYMEX to AECO basis differential contracts.

The following table provides a summary of physical natural gas sales arrangements at AECO. Settlements on these physical sales contracts are recognized in oil and natural gas revenue.

Term	Volumes sold (bought) at AECO (GJ/d)	Average price ($CAD/GJ)(1)	Market prices ($CAD/GJ)(2)	Type of contract
January 2016	(5,000)	2.15	2.20	Physical
January 2016	15,000	2.19	2.20	Physical
February 2016	20,000	2.19	2.23	Physical
March 2016	20,000	2.02	1.58	Physical

(1) Average price calculated using weighted average price for net open contracts.
(2) Market prices are based on settled AECO Monthly Index prices.

The Corporation had entered into financial natural gas sales arrangements at AECO as follows:

Term	Volumes sold (bought) at AECO (GJ/d)	Average price ($CAD/GJ)(1)	Market prices ($CAD/GJ)(2)	Type of contract
January 2016	(10,000)	2.15	2.20	Financial
January 2016	95,249	2.03	2.20	Financial
February 2016	47,500	2.22	2.23	Financial
March 2016	(47,500)	2.13	1.58	Financial
March 2016	94,500	2.12	1.58	Financial
April 2016 – December 2016	32,500	2.32	1.59	Financial

(1) Average price calculated using weighted average price for net open contracts.
(2) Market prices for January to March are based on settled AECO Monthly Index prices. Market prices for subsequent months are based on forward AECO prices as of market close on March 2, 2016.

The Corporation had entered into financial natural gas sales arrangements at NYMEX as follows:

Term	Volumes sold (bought) at NYMEX (MMBTU/d)	Average price ($USD/MMBTU)(1)	Market prices ($USD/MMBTU)(2)	Type of contract
February 2016	(5,000)	2.26	2.19	Financial
February 2016	35,000	2.25	2.19	Financial
March 2016	30,000	2.15	1.71	Financial
April 2016 – December 2016	35,000	2.35	2.04	Financial
January 2017 – March 2017	10,000	2.77	2.63	Financial

(1) Average price calculated using weighted average price for net open contracts.
(2) Market prices for January to March are based on settled NYMEX prices. Market prices for subsequent months are based on forward NYMEX prices as of market close on March 2, 2016.

The following table provides a summary of basis differential contracts between AECO and NYMEX trading:

Term	Volumes (MMBTU/d)	AECO-NYMEX differential ($USD/MMBTU)	Market prices ($USD/MMBTU)(1)	Type of contract
February 2016	30,000	(0.74)	(0.51)	Financial
March 2016	30,000	(0.74)	(0.47)	Financial
April 2016 – December 2016	35,000	(0.73)	(0.79)	Financial
January 2017 – December 2017	50,000	(0.70)	(0.70)	Financial

(1) Market prices are based on forward AECO-NYMEX differential prices as of market close on March 2, 2016.

Crude Oil

The Corporation had entered into financial oil sales arrangements in $USD as follows:

Term	Volumes (bbl/d)	Floor price ($USD/bbl)	Ceiling price ($USD/bbl)	Market prices ($USD/bbl)(1)	Type of contract
January 2016 – December 2016	500	45.00	52.10	37.50	Financial
January 2016 – December 2016	500	42.00	50.70	37.50	Financial
January 2017 – December 2017	250	44.50	49.55	42.70	Financial

(1) Market prices are based on forward WTI oil prices as of market close on March 2, 2016.

The following table provides a summary of basis differential contracts between WTI and WCS trading:

Term	Volumes (bbl/d)	WTI-WCS differential ($USD/bbl)(1)	Market prices ($USD/bbl)(2)	Type of contract
January 2016 – December 2016	500	(13.68)	(13.00)	Financial

(1) Average price calculated using weighted average price for net open contracts; contracts settle at WTI index less a fixed basis amount.
(2) Market prices are based on forward WTI-WCS differential prices as of market close on March 2, 2016.

Foreign Exchange

The Corporation has the following U.S. dollar forward sales arrangement:

Term	Notional $USD/month	Strike rate ($CAD/$USD)	Market prices ($CAD/$USD)[1]	Type of contract
January 2016 – March 2018	3,500,000	1.25	1.31	Financial

(1) Market prices are based on forward $CAD/$USD exchange rates as of market close on March 2, 2016.

If the average monthly exchange rate is above the strike rate the Corporation pays $USD3,500,000 multiplied by the difference between the average monthly exchange rate and the strike rate. If the average monthly exchange rate is below than the strike rate the Corporation receives $USD3,500,000 multiplied by the difference between the average monthly exchange rate and the strike rate.

The Corporation has the following U.S. dollar forward sales arrangement:

Term	Notional $USD/month	Boosted notional[1] $USD / month	Strike rate ($CAD / $USD)	Market prices ($CAD/$USD)[2]	Type of contract
March 2016 – February 2018	1,000,000	3,000,000	1.25	1.34	Financial

(1) If the spot rate at expiry of each contract month is below the strike rate Perpetual pays $USD3,000,000 multiplied by the difference between the spot rate at expiry and the strike rate.
(2) Market prices are based on forward $CAD/$USD exchange rates as of market close on March 2, 2016.

If the spot rate at expiry of each contract month is above the strike rate the Corporation receives $USD1,000,000 multiplied by the difference between the spot rate at expiry and the strike rate. Cumulative receipts on this contract are limited to a total of $0.8 million.

Revenue

(*$ thousands, except as noted*)	**2015**	2014
Petroleum and natural gas revenue		
Natural gas[1]	**109,186**	168,521
Oil[1]	**24,497**	79,781
NGL	**8,754**	14,488
Total petroleum and natural gas revenue	**142,437**	262,790
Realized gains (losses) on derivatives	**4,626**	(9,127)
Realized revenue	**147,063**	253,663
Unrealized gains (losses) on derivatives	**(16,063)**	11,946
Total revenue	**131,000**	265,609
Realized revenue *($/boe)*	**20.45**	33.81
Total revenue *($/boe)*	**18.21**	35.41

(1) Includes revenues related to physical forward sales contracts which settled during the period.

Perpetual's petroleum and natural gas ("P&NG") revenue, before derivatives, for the year ended December 31, 2015 of $142.4 million decreased 46 percent from 2014, primarily due to lower commodity prices with only a marginal decrease in overall production.

Natural gas revenue, before derivatives, of $109.2 million for 2015 decreased 35 percent from $168.5 million in 2014 reflecting lower natural gas prices. Volumes associated with the West Edson Property swap completed on April 1, 2015 were more than offset through the 2014 and 2015 East Edson development program along with commissioning and expansion of the new East Edson gas plant in the third quarter of 2015.

Oil revenues of $24.5 million in 2015 were 69 percent lower than 2014 ($79.8 million) due to lower crude oil prices, reduced production as a result of the fourth quarter 2014 Mannville non-core heavy oil property disposition, natural declines, and the deferral of crude oil drilling programs. Oil index price declines were partially mitigated by a narrowing of WTI-WCS differentials and a lower $CAD to $USD exchange rate.

NGL revenue for the year declined 40 percent from 2014 to $8.8 million as lower commodity prices more than offset a 32 percent increase in production.

Realized gains on derivatives totaled $4.6 million for 2015 compared to losses of $9.1 million in 2014. Total gains in the current year were comprised of $5.1 million on natural gas derivatives and $6.7 million from oil derivatives, partially offset by $7.2 million of losses on forward foreign exchange arrangements.

The Corporation recorded unrealized losses on derivatives of $16.1 million during 2015 compared to unrealized gains of $11.9 million for 2014. Unrealized gains and losses represent the change in mark-to-market value of derivative contracts as forward commodity prices and foreign exchange rates change. Unrealized gains and losses on derivatives are excluded from the Corporation's calculation of funds flow as they are non-cash. Derivative gains and losses vary depending on the nature and extent of derivative contracts in place, which in turn, vary with the Corporation's assessment of commodity price risk, committed capital spending and other factors.

Royalties

(*$ thousands, except as noted*)	**2015**	2014
Crown	**4,394**	16,425
Freehold and overriding[(1)]	**11,950**	15,599
Total	**16,344**	32,024
Crown (*% of P&NG revenue*)	**3.1**	6.2
Freehold and overriding (*% of P&NG revenue*)	**8.4**	6.0
Total (*% of P&NG revenue*)	**11.5**	12.2
$/boe	**2.27**	4.27

(1) Includes payments of $6.9 million under the East Edson overriding royalty arrangement (2014 - $5.2 million).

Royalty expenses for 2015 were $16.3 million, representing a slight decrease in the effective combined average royalty rate on P&NG revenue to 11.5 percent from 12.2 percent in 2014. Average crown royalty rates decreased to 3.1 percent in 2015 compared to 6.2 percent in 2014 partially as a result of lower Alberta natural gas reference prices combined with declining oil and NGL prices. Crown royalty rates in 2015 were also reduced by increased production from new East Edson wells which benefited from reduced rates and credits received under the Crown's natural gas deep drilling program.

Freehold and overriding royalty rates for the year ended December 31, increased from 6.0 percent in 2014 to 8.4 percent in 2015 reflecting the full year effect of the additional gross overriding royalties beginning July 1, 2014 under Perpetual's 2014 East Edson royalty disposition and farm-in agreements which, in combination, entitle the partner to a maximum of 5.6 MMcf/d of natural gas from the East Edson property plus oil and associated NGLs on a monthly basis. Excluding royalty payments of $6.9 million under the East Edson overriding royalty arrangement (2014 - $5.2 million), the effective freehold and overriding royalty rate for the year ended December 31 was 3.5 percent compared to 4.0 percent in 2014.

Production and operating expenses

(*$ thousands, except as noted*)	**2015**	2014
Production and operating expenses	**65,133**	78,128
$/boe	**9.06**	10.41

Total production and operating expenses decreased 17 percent to $65.1 million for 2015 compared to $78.1 million for 2014, reflecting company-wide cost saving initiatives, the re-deployment of operations personnel to abandonment and reclamation projects, and start-up of the new low cost Company owned and operated gas plant at East Edson.

Municipal property taxes continue to represent a significant portion of corporate operating costs at $10.2 million, or $1.42 per boe (16 percent of total operating costs) for the year ended December 31, 2015. The calculation of property taxes for pipelines and wells is based on a prescribed formula methodology which results in a tax assessment base that is dramatically misrepresentative of the property value for the Company's mature assets. As a result, property taxes for Perpetual's shallow gas production in Eastern Alberta were $9.7 million ($0.49 per Mcf; $2.94 per boe) for 2015, which represents 20 percent of operating costs for shallow gas production and 130 percent of pre-municipal tax operating netbacks for these properties, excluding realized gains on derivatives, completely eliminating positive operating cash flow on most shallow gas properties. Property taxes were 103 percent of Eastern Alberta shallow gas pre-municipal tax operating netbacks, including allocation of realized gains on derivatives proportionate with production, for the year ended 2015.

Transportation costs

(*$ thousands, except as noted*)	**2015**	2014
Transportation costs	**12,058**	12,684
$/boe	**1.68**	1.69

Transportation costs include clean oil trucking and NGL transportation as well as costs to transport natural gas from the plant gate to commercial sales points. Consistent with the marginal decrease in production, transportation costs in 2015 decreased five percent to $12.1 million from $12.7 million for the same period in 2014, reflecting lower oil sales volumes and lower rates on clean oil trucking.

Operating netbacks

	2015	2014
Operating netback (*$ thousands*)		
Realized revenue[1]	**147,063**	253,663
Royalties[2]	**(16,344)**	(32,024)
Production and operating expenses	**(65,133)**	(78,128)
Transportation costs	**(12,058)**	(12,684)
Total operating netback	**53,528**	130,827
Boe operating netback (*$/boe*)		
Realized revenue[1]	**20.45**	33.81
Royalties[2]	**(2.27)**	(4.27)
Production and operating expenses	**(9.06)**	(10.41)
Transportation costs	**(1.68)**	(1.69)
Total operating netback	**7.44**	17.44

(1) See "Non-GAAP measures" in this MD&A.
(2) Includes payments of $6.9 million under the East Edson overriding royalty arrangement (2014 - $5.2 million).

Perpetual's 2015 operating netback of $7.44/boe ($53.5 million) decreased 59 percent from $17.44/boe ($130.8 million) in 2014, primarily as a result of decreased revenue reflecting lower commodity prices despite lower per boe royalties, operating expenses and transportation costs.

Gas over bitumen

(*$ thousands, except as noted*)	**2015**	2014
Gas over bitumen revenue	**3,153**	8,888
Payments on financial obligation[1]	**(3,704)**	(2,829)
Gas over bitumen, net of payments	**(551)**	6,059
$/boe	**(0.08)**	0.81

(1) At December 31, 2015, the fair value of the GOB financial obligation is estimated to be $10.0 million (2014 - $15.4 million).

Perpetual records revenue in relation to GOB royalty credits received under the Natural Gas Royalty Regulation as a result of its working interests in a number of natural gas wells which have been shut-in pursuant to shut-in orders issued by the Government of Alberta. During 2015, Perpetual recorded $3.2 million in GOB revenue; a decrease of $5.7 million from the same period in 2014 attributable to the 41 percent decrease in Alberta gas reference prices, combined with the annual 10 percent decline in deemed production.

GOB revenue earned throughout 2015 was offset by payments of $3.7 million in relation to the 2014 monetization of Perpetual's future GOB royalty credits. As part of the arrangement, Perpetual makes monthly payments to the purchaser, which from time to time will vary from the actual GOB revenue received in the period due to timing differences. The monthly payment commitment expires concurrent with the GOB Royalty Adjustment entitlements, with final expiries expected to occur in June 2021.

Under IFRS, the monetization of future GOB royalty credits in 2014 was recorded as a financial obligation; however entitlement to future revenue from GOB royalty credits are not recorded as an asset but as revenue with the passage of time as it is earned. As such, GOB revenue will continue to be recognized separately as revenue in accordance with Perpetual's accounting policies with the monthly payments recognized separately as a reduction to the GOB financial obligation. For purposes of this MD&A, the monthly payments have been included as a reduction to GOB revenue to reflect the substantive monetization of the future GOB royalty credits. During 2015 the GOB financial obligation was reduced by payments of $3.7 million and a gain of $1.7 million included in non-cash finance expense representing a reduction in the fair value of the GOB financial obligation compared to 2014, as a result of lower forecasted natural gas reference prices.

Exploration and evaluation

(*$ thousands*)	**2015**	2014
Lease rentals	**2,866**	3,165
Geological and geophysical costs[1]	**1,526**	644
Lease expiries	**6,338**	2,135
Total exploration and evaluation	**10,730**	5,944

(1) Geological and geophysical expenditures and dry hole costs are expensed directly in the Corporation's statement of income (loss); they are considered by Perpetual to be more closely related to investing activities than operating activities, and therefore are included with capital expenditures for the purposes of this MD&A.

Exploration and evaluation ("E&E") costs include lease rentals on undeveloped acreage, geological and geophysical costs and lease expiries. E&E costs of $10.7 million in 2015 were $4.8 million higher than 2014 with higher lease expiries and higher geological and geophysical expenditures in the current year. Geological and geophysical costs include the completion of two 3D seismic surveys which were initiated in 2014 and completed in 2015 in East Edson and West Edson.

General and administrative expenses

($ thousands, except as noted)	2015	2014
Cash general and administrative expense	**17,461**	22,371
Share based compensation expense (non-cash)	**3,774**	5,972
Total general and administrative expense	**21,235**	28,343
Cash general and administrative expense *($/boe)*	**2.43**	2.98
Share based compensation expense (non-cash) *($/boe)*	**0.52**	0.80

Cash G&A expense decreased 22 percent to $17.5 million in 2015 from $22.4 million in 2014 reflecting reductions in consulting fees and savings related to modified work schedules, elimination of annual bonuses and on-going cost saving initiatives implemented by the Corporation in response to the depressed commodity price environment. Cost savings initiatives were partially offset by reduced overhead recoveries in 2015 as a result of a reduced capital spending program compared to the prior year.

Non-cash compensation expenses for the year ended December 31 decreased $2.2 million compared to the same period in 2014 as a result of performance multiplier adjustments related to performance share rights issued and outstanding.

Gains on dispositions and asset swaps

Perpetual recorded gains on property transactions of $146.6 million for the year ended December 31, 2015. Transactions included the West Edson Property swap completed on April 1, 2015 in exchange for TOU shares, the disposition of certain fee simple lands and related seismic data for proceeds of $21.0 million. Also included in gains on dispositions in 2015 were net gains recognized on non-monetary transactions including the carried farm-in investment on undeveloped Duvernay lands in the Waskahigan area, as well as an asset swap to acquire an increased interest in existing reserves and undeveloped acreage in its core East Edson property in exchange for its interest in certain non-core undeveloped lands.

Depletion and depreciation

($ thousands, except as noted)	2015	2014
Depletion and depreciation	**88,364**	94,736
$/boe	**12.29**	12.63

Perpetual recorded $88.4 million of depletion and depreciation expense for the year ended December 31, 2015 (2014 - $94.7 million). On a per boe basis, 2015 depletion and depreciation expense of $12.29/boe was three percent lower than depletion and depreciation expense of $12.63/boe recorded in 2014.

Impairment losses

At December 31, 2015, indicators of potential impairment were identified related to the reduction in commodity prices and future commodity price forecasts estimated by third party independent engineers. Perpetual measured the carrying values of each of its cash generating units ("CGUs"), less the corresponding decommissioning obligations, against the estimated recoverable amount based on value in use which Perpetual deemed to be higher compared to fair value less cost to sell. A net impairment loss of $23.7 million was recorded for 2015 which included a $6.5 million impairment loss in Birchwavy East CGU and a $2.5 million impairment loss in Birchwavy West CGU as a result of lower forecasted oil and natural gas prices. The Corporation also determined that future production from the shut-in GOB wells is unlikely in the continued absence of a technical solution or permitted production. Impairment losses for 2015 further included $14.7 million for de-recognition of the GOB CGU, net of $3.8 million for de-recognition of the provision for estimated future repayments of GOB credits received.

In 2014, Perpetual recorded net impairments of $21.4 million in the Birchwavy East and Birchwavy West CGUs.

Finance expenses

Interest

($ thousands)	2015	2014
Cash interest		
Senior notes	**24,062**	17,670
Convertible debentures	**2,441**	8,912
Bank debt	**4,143**	3,373
Total cash interest	**30,646**	29,955
Non-cash interest		
Amortization of debt issue costs	**2,036**	4,896
Total interest	**32,682**	34,851

Total cash interest expense of $30.6 million for the year ending December 31, 2015 was consistent with the prior year ($30.0 million). Increased cash interest on senior notes resulted from the full year effect of the issuance of an additional $125 million 8.75 percent senior notes on July 23, 2014. Higher interest on senior debt was partially offset by reduced interest on convertible debentures due to the full repayment of the 7.25% convertible debentures in August 2014 and partial repayment of $25 million of the 7.00% Debentures on December 31, 2014. The repayment of debentures also contributed to a reduction in period over period non-cash debt issue cost amortization.

Other finance expenses

(*$ thousands*)	**2015**	2014
Accretion on decommissioning obligations	**4,034**	5,400
Accretion and change in estimate on GOB obligation	**498**	376
Change in fair value of financial obligation	**(1,675)**	(3,035)
Change in fair value of TOU Share financial arrangement	**(171)**	–
Change in carrying amount of Rights derivative	**(7,478)**	–
Other finance expenses	**(4,792)**	2,741

Other finance expenses for the year ended December 31, 2015 included accretion on decommissioning obligations of $4.0 million (2014 - $5.4 million) and accretion and change in estimate on the GOB obligation of $0.5 million (2014 – $0.4 million), partially offset by a gain of $1.7 on the change in fair value of the GOB financial obligation, a gain of $0.2 million on a the change in fair value of the TOU Share financial arrangement and a $7.5 million non-cash gain related to the Rights Offering. Under IFRS, the Corporation initially recognized a derivative liability (the "Rights derivative") in conjunction with filing of the final prospectus on December 7, 2015 which was transferred to equity on December 22, 2015 with determination of the number of common shares to be issued for each Right. A non-cash gain of $7.5 million is included in non-cash finance expenses related to the change in the carrying amount of the Rights derivative between December 7, 2015 and December 22, 2015.

Change in fair value of marketable securities

During 2015, the Corporation recorded an unrealized loss of $104.8 million related to the change in fair value of marketable securities, which represents the change in value of 6.5 million TOU Shares held from closing on of the West Edson property swap on April 1 ($38.32 per share) and December 31, 2015 ($22.35 per share).

Share of net income (loss) of equity-method investment

For the year ended December 31, 2015, Perpetual recorded income of $0.2 million on its equity investment in WGS LP compared to a loss of $3.2 million for the same period in 2014. There were no dividends declared or received for the year ended December 31, 2015 or 2014.

Funds flow

Low commodity prices continued to have a dramatic impact on financial results with the Corporation recognizing funds flow of $2.0 million for the year ended December 31, 2015, compared to $81.4 million of funds flow recorded in 2014. Commodity price declines have led to a drastic reduction in 2015 funds flow despite consistent production levels year-over-year and significant corporate cost-savings initiatives throughout 2015. Through reductions in operating, transportation costs and general and administrative expenses, combined with royalty reductions, all-in cash costs were 19 percent ($33.8 million) lower than 2014. Despite these significant cost reductions, the 42 percent drop in realized revenue virtually eliminated cash flow margins and translated to a 98 percent decrease in funds flow year over year.

	2015		2014	
	($ thousands)	***($/boe)***	(*$ thousands*)	(*$/boe*)
Realized revenue(1)	**147,063**	**20.45**	253,663	33.81
Royalties(2)	**(16,344)**	**(2.27)**	(32,024)	(4.27)
Production and operating expenses	**(65,133)**	**(9.06)**	(78,128)	(10.41)
Transportation costs	**(12,058)**	**(1.68)**	(12,684)	(1.69)
Operating netback(1)	**53,528**	**7.44**	130,827	17.44
GOB revenue net of payments	**(551)**	**(0.08)**	6,059	0.81
Exploration and evaluation – lease rentals (3)	**(2,866)**	**(0.40)**	(3,165)	(0.42)
Cash G&A	**(17,461)**	**(2.43)**	(22,371)	(2.98)
Interest(3)	**(30,646)**	**(4.26)**	(29,955)	(3.99)
Funds flow(1)	**2,004**	**0.28**	81,395	10.86

(1) See "Non-GAAP measures" in this MD&A.
(2) Includes payments of $6.9 million under the East Edson overriding royalty arrangement (2014 - $5.2 million).
(3) Excludes non-cash items.

Net Income (Loss)

Perpetual recorded a net loss of $89.3 million ($12.41 per boe) for the year ended December 31, 2015, compared to income of $3.4 million ($0.45 per boe) for 2014 primarily as a result of lower funds flow, unrealized losses on marketable securities and derivatives and impairment losses, which were partially offset by gains on dispositions.

	2015		2014	
	(*$ thousands*)	**(*$/boe*)**	(*$ thousands*)	(*$/boe*)
Funds flow[1]	**2,004**	**0.28**	81,395	10.86
Unrealized gains (losses) on derivatives	**(16,063)**	**(2.23)**	11,946	1.59
Payments on financial obligation	**3,704**	**0.51**	2,829	0.38
Exploration and evaluation[2]	**(7,864)**	**(1.09)**	(2,779)	(0.37)
Compensation expense, non-cash	**(3,774)**	**(0.52)**	(5,972)	(0.80)
Gain on dispositions	**146,632**	**20.39**	42,944	5.72
Depletion and depreciation	**(88,364)**	**(12.29)**	(94,736)	(12.63)
Impairment losses	**(23,700)**	**(3.30)**	(21,400)	(2.85)
Finance expense, non-cash	**2,756**	**0.38**	(7,637)	(1.02)
Change in fair value of marketable securities	**(104,828)**	**(14.57)**	–	–
Share of net income (loss) of equity-method investment	**223**	**0.03**	(3,224)	(0.43)
Net income (loss)	**(89,274)**	**(12.41)**	3,366	0.45

(1) See "Non-GAAP measures" in this MD&A.
(2) Includes non-cash exploration and evaluation expense from expired leases and geological and geophysical costs.

SUMMARY OF QUARTERLY RESULTS

($ thousands, except where noted)	**Q4 2015**	Q3 2015	Q2 2015	Q1 2015
Financial				
Oil and natural gas revenues	**33,044**	35,460	32,129	41,804
Funds flow[(1)]	**362**	(2,514)	2,635	1,521
Per share – basic	**0.00**	(0.02)	0.02	0.01
Net income (loss)	**(93,539)**	(67,139)	104,121	(32,717)
Per share – basic	**(0.62)**	(0.44)	0.70	(0.22)
– diluted	**(0.62)**	(0.44)	0.66	(0.22)
Capital expenditures				
Exploration and development	**808**	14,670	13,069	46,886
Geological and geophysical	**(93)**	16	105	1,498
Acquisitions	**–**	–	240	3
Dispositions	**–**	(2,630)	(21,337)	11
Other	**25**	584	280	21
Net capital expenditures	**740**	12,640	(7,643)	48,419
Common shares (*thousands*)				
Weighted average – basic	**151,638**	150,980	149,368	148,531
Weighted average – diluted	**151,638**	150,980	157,594	148,531
Operating				
Daily average production				
Natural gas (*MMcf/d*)	**105.1**	105.5	86.0	120.4
Oil (*bbl/d*)	**1,278**	1,426	1,766	2,045
NGL (*bbl/d*)	**866**	741	522	713
Total (*boe/d*)	**19,661**	19,758	16,621	22,819
Average prices				
Natural gas – before derivatives (*$/Mcf*)	**2.74**	2.91	2.80	3.01
Natural gas – including derivatives (*$/Mcf*)	**2.92**	2.86	3.10	3.14
Oil – before derivatives (*$/bbl*)	**33.04**	40.58	52.35	37.37
Oil – including derivatives (*$/bbl*)	**39.81**	41.40	74.33	49.41
NGL (*$/bbl*)	**33.68**	28.07	38.64	36.15

(1) See "Non-GAAP measures" in this MD&A.

($ thousands, except where noted)	Q4 2014	Q3 2014	Q2 2014	Q1 2014
Financial				
Oil and natural gas revenues	62,562	63,126	72,348	64,754
Funds flow[(1)]	17,316	20,831	25,864	17,384
Per share – basic	0.12	0.14	0.17	0.12
Net income (loss)	(18,723)	36,414	2,549	(17,324)
Per share – basic	(0.12)	0.24	0.02	(0.12)
– diluted	(0.12)	0.23	0.02	(0.12)
Capital expenditures				
Exploration and development	25,639	46,583	12,251	31,340
Geological and geophysical	379	34	218	13
Acquisitions	756	–	91	151
Dispositions	(21,351)	(46,998)	(3,000)	–
Other	84	347	108	75
Net capital expenditures	5,507	(34)	9,668	31,579
Common shares (*thousands*)				
Weighted average – basic	149,084	149,574	148,835	148,448
Weighted average – diluted	149,084	160,282	157,555	148,448
Operating				
Daily average production				
Natural gas (*MMcf/d*)	122.5	97.8	97.8	92.1
Oil (*bbl/d*)	2,638	2,894	3,185	2,911
NGL (*bbl/d*)	624	430	553	540
Total (*boe/d*)	23,685	19,640	20,053	18,794
Average prices				
Natural gas – before derivatives (*$/Mcf*)	3.96	4.35	4.95	4.90
Natural gas – including derivatives (*$/Mcf*)	4.16	4.35	4.66	4.35
Oil – before derivatives (*$/bbl*)	59.80	78.37	83.20	77.43
Oil – including derivatives (*$/bbl*)	67.05	74.55	73.31	70.71
NGL (*$/bbl*)	59.63	77.56	82.36	79.33

(1) See "Non-GAAP measures" in this MD&A.

FOURTH QUARTER FINANCIAL AND OPERATING RESULTS

Perpetual restricted spending on exploration and development activities during the fourth quarter of 2015 in response to the low commodity price environment with $0.8 million spent in the period for residual spending on capital activities initiated earlier in the year. An additional $2.4 million was directed to the Company's abandonment and reclamation activities in the fourth quarter. The Corporation focused on cost-reduction initiatives while preserving optionality, value and inventory with a view to eventual commodity price recovery.

Perpetual's production in the fourth quarter of 19,661 boe/d was 17 percent lower than 2014 (23,685 boe/d), reflecting lost volumes associated with the fourth quarter 2014 disposition of heavy oil assets at Mannville, the second quarter 2015 West Edson Property swap, and natural declines which were partially offset by a 106 percent increase in East Edson production related to the Company's drilling program and facilities expansion in the area.

Realized revenue decreased 47 percent during the fourth quarter of 2015 compared to the same period in 2014 reflecting the precipitous decline in natural gas, oil and NGL prices. Lower royalty expenses related to the decline in Alberta reference pricing along with reductions in operating and general and administrative costs somewhat mitigated the effect of the commodity price decline, resulting in Perpetual recording funds flow of $0.4 million for the fourth quarter of 2015 compared to $17.3 million in 2014. A net loss of $93.5 million ($0.62 per share) was recorded for the fourth quarter of 2015.

LIQUIDITY, CAPITALIZATION AND FINANCIAL RESOURCES

Perpetual targets to maintain a strong capital base to retain investor, creditor and market confidence, and to sustain the future development of the business. The Corporation strives to manage its capital structure and makes adjustments in light of changes in economic conditions and the risk characteristics of its underlying oil and natural gas assets. Perpetual's capital structure includes share capital, bank debt, senior notes, and adjusted working capital, with value and liquidity enhanced through the current ownership of TOU Shares. In order to manage its capital structure, the Corporation may from time to time issue equity or debt securities, enter into business transactions including the sale of assets and adjust its capital spending to manage current and projected debt levels.

During the second quarter of 2015 Perpetual closed the West Edson Property swap for TOU shares. The transaction positioned Perpetual to capture the upside of the West Edson Property through ownership of the TOU Shares and also exposed Perpetual shareholders to the value creation potential inherent in Tourmaline's extensive land and drilling opportunity inventory and strong balance sheet in this period of low commodity prices. It also materially strengthened Perpetual's financial situation, augmenting the Company's potential to optimize the shareholder value inherent in its existing diversified portfolio of assets. The TOU Shares also provide greater flexibility to capture and evaluate other new high impact opportunities and pursue strategic initiatives. At the same time, the liquidity inherent in the TOU Shares significantly enhances Perpetual's financial position, augmenting the Company's options to manage downside risk and enhancing Perpetual's ability to fund attractive investment opportunities through this period of low commodity prices. During the third quarter and early in the fourth quarter, Perpetual sold a total of 250,000 TOU Shares for total proceeds of $8.6 million ($34.23 per share) to provide liquidity to manage its margin loan obligations.

To improve liquidity and address financial obligations due in the fourth quarter of 2015, Perpetual completed a series of recapitalization transaction which included:

- The execution of the TOU Share financing arrangement during the fourth quarter that provided net proceeds of $18.2 million collateralized by 1.0 million TOU shares;
- Extension of Perpetual's current bank lending arrangements to October 31, 2016 with total borrowing capacity of $62 million, comprised of a $20.0 million demand loan and a $42.0 million margin loan secured by 5.5 million TOU shares;
- Settlement of the 7.00% Convertible Debentures due December 31, 2015 (the "Debentures") with the issuance of approximately 228.9 million common shares of Perpetual; and
- A $25.0 million fully backstopped rights offering (the "Rights Offering") which closed on January 18, 2016. The Company issued 665.4 million common shares on closing of the Rights Offering.

The effect of these recapitalization transactions extended the term of the Company's earliest maturing debt to October 31, 2016, infused additional liquidity through the Rights Offering for ongoing capital programs and provided a reduction to debt and preserved liquidity to manage downside risk while allowing for retention of potentially undervalued assets in the current low commodity price environment. These transactions provided a number of benefits consistent with Perpetual's strategic priorities including:

- Providing the Corporation with a stronger financial foundation and capital structure to operate within the current uncertain commodity price and operating environment;
- Reducing total indebtedness resulting in future interest savings;
- Providing new equity capital to be contributed towards Perpetual's 2016 capital program; and
- Preserving the Corporation's portfolio of strategic assets for future growth, including its East Edson asset in west central Alberta and the ownership of 6.5 million TOU Shares.

Capital Management

($ thousands, except as noted)	December 31, 2015	December 31, 2014
Bank indebtedness	**42,000**	–
Senior notes, measured at principal amount	**275,000**	275,000
Convertible debentures, measured at principal amount	**–**	34,878
Carrying amount of share forward financial obligation	**18,059**	
Carrying amount of marketable securities(1)	**(145,275)**	–
Adjusted working capital deficiency (surplus)(2)	**13,832**	21,867
Net debt(2)	**203,616**	331,745
Shares outstanding at end of period (*thousands*)	**382,288**	150,077
Market price at end of period (*$/share*)	**0.05**	1.14
Market value of shares	**19,114**	171,088
Total capitalization(2)	**222,730**	502,833
Net debt as a percentage of total capitalization	**91**	66
Trailing twelve months funds flow(2)	**2,004**	81,395
Net debt to funds flow ratio(3)	**101.6**	4.1

(1) The carrying amount of marketable securities is based on the period end closing price per the TSX ($22.35 per share) and 6.5 million TOU Shares held.
(2) See "Non-GAAP measures" in this MD&A.
(3) Net debt to funds flow is calculated based on trailing funds flow for the most recent four quarters.

The Corporation monitors capital based on the ratio of net debt to trailing twelve months ("TTM") funds flow. As at December 31, 2015, the Corporation's ratio of net debt to TTM funds flow had increased from year end 2014, to 101.6 to 1 (December 31, 2014 – 4.1 to 1). The increase reflects the significant impact of declining commodity prices at the end of 2014 and continuing through 2015 which negatively impacted funds flow and resulted in higher levels of bank debt. The increase was partially offset by the inclusion of the period end value of the TOU shares and the settlement of the Debentures with equity, combined with a significant decline in the market value of Perpetual's shares as at December 31, 2015 which marked a 56 percent reduction to total capitalization compared to the prior year.

The ratio of net debt to TTM funds flow is monitored continuously by the Corporation and varies based on such factors as acquisitions or dispositions, commodity prices, forecasts of future commodity prices, price management contracts, projected cash flows, capital expenditure programs and timing of such programs. As part of the management of this ratio, the Corporation prepares annual capital expenditure budgets and monthly funds flow forecasts, which are updated as necessary depending on varying factors including current and forecast prices, successful capital deployment, acquisition and development activities and general industry conditions. Capital spending budgets are approved by the Board of Directors.

At December 31, 2015, Perpetual had total debt net of working capital and the market value of TOU Shares of $203.6 million, down $128.1 million (39 percent) from December 31, 2014. The reduction reflects settlement of the convertible debentures and the inclusion of the period end value of the TOU shares, offset by year to date 2015 capital spending and decommissioning expenditures funded primarily through increased bank indebtedness with limited funds flow during the year as a result of depressed oil, natural gas and NGL prices.

Perpetual's adjusted working capital deficit at December 31, 2015 was $13.8 million compared to $21.9 million at December 31, 2014. Accounts payables and restricted cash balances decreased from year-end 2014 due to clearing of unapplied cash calls to fund the remaining portion of the partner's share of drilling activities in East Edson in early 2015 followed by reduced capital spending in the fourth quarter of 2015. The decrease in accounts payable was mostly offset by a decrease in accounts receivables as a result of lower commodity prices.

Reconciliation of net debt

($ millions)	
Net debt, December 31, 2014(1)	331.7
Capital expenditures(2)	77.9
Expenditures on decommissioning obligations	7.6
Dispositions, net of acquisitions	(23.7)
Period end balance of marketable securities(3)	(145.3)
Funds flow(1)	(2.0)
Settlement of convertible debentures	(34.9)
Proceeds on sale of marketable securities	(8.6)
Other	0.9
Net debt, December 31, 2015(1)	**203.6**

(1) See "Non-GAAP measures" in this MD&A.
(2) Capital expenditures consist of exploration and development spending including geological and geophysical costs and corporate assets.
(3) The period end balance of marketable securities is based on the closing price per the TSX and 6.5 million share pledge under the Corporation's credit facility agreement.

Bank indebtedness

The Corporation's credit facility and margin loan is with a syndicate of Canadian chartered banks. On April 1, 2015, as part of the lender's semi-annual review of the borrowing base and in conjunction with the West Edson swap, total availability was reduced from $105 million to $100 million consisting of a margin loan of $75 million secured by the pledge of 6.75 million TOU Shares, and a revolving credit facility of $25 million which included a $10 million demand loan and $15 million working capital facility. On December 24, 2015, as part of Perpetual's recapitalization transactions, Perpetual's lenders adjusted the total borrowing capacity to $62 million consisting of a margin loan of $42 million secured by the pledge of 5.5 million TOU Shares, and a revolving credit facility of $20 million which includes a $5 million demand loan and $15 million working capital facility.

Revolving Credit Facility

Advances under the credit facility are made in the form of Banker's Acceptances ("BA"), prime rate loans or letters of credit at the Corporation's option. At December 31, 2015, cash and cash equivalents are shown net of a $5.0 million BA outstanding on the revolving credit facility (December 31, 2014 – nil). The Corporation also had outstanding letters of credit in the amount of $5.4 million (December 31, 2014 – $8.8 million). Collateral for the revolving credit facility is provided by a floating-charge debenture covering all existing and acquired property of the Corporation, as well as unconditional full liability guarantees from all subsidiaries in respect of amounts borrowed under the credit facility.

The credit facility bears interest at its lenders' prime rate or BA rates, plus applicable margins and standby fees. The applicable margins range between 1.25% and 4.75% depending on the form of borrowing and changes in the Corporation's ratio of consolidated debt to income before interest, taxes, and non-cash items ("Consolidated Debt Ratio") for the most recently completed reporting period. Consolidated debt is defined as the sum of the period end balance of the credit facility, senior notes and outstanding letters of credit.

The revolving feature of the credit facility expires on October 31, 2016. The next semi-annual redetermination is set to occur on this date.

Margin Loan

Beginning April 1, 2015, as part of the semi-annual borrowing base review, Perpetual's lending commitment included a $75 million margin loan which was secured by the pledge of 6.75 million TOU Shares. The sale of 0.25 million TOU Shares in the second half of 2015 and establishment of the share forward financial obligation, combined with the decline of Tourmaline's share price over the third and fourth quarters impacted the value of the collateralized TOU shares resulting in a series of reductions from the initial $75.0 million margin loan to $42.0 million. At December 31, Perpetual had a margin loan of $42 million collaterized by 5.5 million TOU Shares. The Corporation is required to maintain a 1 to 3 lending ratio based on the daily closing market value of TOU Shares.

The margin loan had an initial maturity date of November 30, 2015 which was extended to October 31, 2016 in conjunction with the recapitalization transactions. Collateral for the margin loan is provided by a securities pledge agreement relating to the TOU Shares obtained in conjunction with the swap of the West Edson Property. The margin loan bears interest at its lenders' prime rate plus applicable margins ranging from 1.25% to 4.75% depending on changes in the Corporation's Consolidated Debt Ratio for the most recently completed reporting period.

Covenants

At December 31, 2015, the Corporation has a working capital covenant restricting the sum of borrowings under the revolving credit facility plus net working capital liabilities to a total of $40 million (excluding amounts drawn under the margin loan). Net working capital liabilities includes cash and cash equivalents, accounts receivable, prepaid expenses and deposits and accounts payable and accrued liabilities, plus an adjustment for accrued interest on Senior Notes payable from the date of the calculation up to and including expiry of the credit facility (October 31, 2016).

The Corporation also has maintenance covenants that require consolidated senior debt to TTM income before interest, taxes, depletion and depreciation and non-cash items ("EBITDA") to be maintained within certain thresholds. Consolidated senior debt is defined as the sum of the Corporation's period end balance of the margin loan, credit facility and outstanding letters of credit reduced by the lesser of the mark to market value or the quarterly average value of 5.5 million TOU Shares pledged to the credit facility. The existing covenant limiting the ratio of consolidated senior debt to TTM EBITDA remains at 3.0 to 1.0 except in the quarters ended June 30 and September 30, 2016 where the limit has been increased to 3.5 to 1.0.

The Corporation was in compliance with the lender's covenants at December 31, 2015.

Convertible Debentures

On November 20, 2015, pursuant to the terms of the Convertible Debentures, Perpetual provided notice to exercise its right to repay the outstanding principal amount of the 7.00% Convertible Debentures of $34.9 million in equity. On December 31, 2015, Perpetual settled the 7.00% Convertible Debentures through the issuance of approximately 228.9 million common shares. The number of common shares issued was determined by dividing the principal amount of Convertible Debentures currently outstanding by 95% of the volume weighted average trading price of Common Shares for the 20 consecutive trading days ending on December 22, 2015, the fifth trading day preceding the Maturity Date. All accrued and unpaid interest on the Convertible Debentures was paid in cash at the maturity date of December 31, 2015.

Senior Notes

At December 31, 2015, Perpetual had $275 million of senior notes outstanding. Additional information on the senior notes is as follows:

	Maturity date	Principal	Interest rate	Carrying amount December 31, 2015	December 31, 2014
2011 senior notes[1]	March 15, 2018	150,000	8.75%	**148,724**	148,223
2014 senior notes[2]	July 23, 2019	125,000	8.75%	**122,934**	122,467
		275,000		**271,658**	270,690

[1] Issued March 15, 2011, interest payable semi-annually on September 15 and March 15 of each year.
[2] Issued July 23, 2014, interest payable semi-annually on January 23 and July 23 of each year.

The fair market value of the senior notes at March 2, 2016 was $149.9 million.

The senior notes are direct senior unsecured obligations of Perpetual, ranking pari passu with all other present and future unsecured and unsubordinated indebtedness of the Corporation. The Corporation can redeem up to 35 percent of the principal amount of the senior notes at a premium to face value with proceeds from common share offerings up to three years prior to maturity. Within three years of maturity the Corporation can repay the senior notes at a premium to face value based on the date of repayment.

The senior notes have a cross-default provision with the Corporation's credit facility which has a working capital covenant restricting the sum of borrowings under the revolving credit facility plus net working capital liabilities to a total of $40 million (excluding amounts drawn under the margin loan). Net working capital liabilities include accounts receivable, prepaid expenses and deposits and accounts payable and accrued liabilities.

The cross-default provision also applies to the maintenance covenants that require consolidated senior debt to TTM EBITDA to be maintained within certain thresholds. Consolidated senior debt is defined as the sum of the Corporation's period end balance of the margin loan, credit facility and outstanding letters of credit reduced by the lesser of the mark to market value of the TOU Shares or the TOU Share quarterly average value. The existing covenant limiting the ratio of consolidated senior debt to TTM EBITDA remains at 3.0 to 1.0 except in the quarters ended June 30 and September 30, 2016 where the limit has been increased to 3.5 to 1.0.

The senior notes indenture also 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 Corporation's Consolidated Debt Ratio is less than 3.0 to 1.0, the sum of 50 percent of income before interest, taxes, depletion and depreciation and non-cash items 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 Corporation during that period less the sum of all restricted payments during that period; and

ii) To the extent the Corporation'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 Corporation.

The Corporation was in compliance with the lender's covenants at December 31, 2015 and estimates that it will be in compliance with all covenants through to the maturity of the credit facility at current commodity prices.

At December 31, 2015 the carrying value of the senior notes are presented net of $3.3 million in issue costs which are amortized using a weighted average effective interest rate of 9.2 percent.

TOU Share financial arrangement

In November 2015, the Corporation executed a new financial arrangement that provided $18.2 million of proceeds, net of a fee paid to enhance the collateral value of 1.0 million TOU Shares pledged as security for the arrangement. The arrangement matures on November 16, 2016 and can be repaid in cash or with the transfer of the TOU Shares pledged as security. The repayment amount changes in response to changes in the market price of the underlying security, subject to a maximum re-payment amount of $21.3 million at maturity.

Equity

As part of the recapitalization transactions undertaken in the fourth quarter of 2015, Perpetual issued approximately 228.9 million common shares on December 31, 2015 in settlement of outstanding Convertible Debentures pursuant to the terms of the indenture agreement.

On December 7, 2015, Perpetual filed a short form prospectus with the security regulatory authorities in connection with a fully backstopped Rights Offering to issue common shares of Perpetual for gross proceeds of $25 million.

Pursuant to the Rights Offering, each registered holder of common shares as of December 16, 2015 received one right (a "Right") for each common share held. Each Right entitled the holder to acquire 4.3386 common shares upon payment of the exercise price of $0.1630 per Right. The number of common shares received for each right was calculated following the close of trading of the common shares on the Toronto Stock Exchange ("TSX") on December 22, 2015 based upon the volume weighted average price of the common shares for the preceding 20 consecutive trading days, being November 25, 2015 through to and including December 22, 2015. The Rights traded on the TSX under the symbol PMT.RT from December 23, 2015 to January 15, 2016.

At December 31, 2015, a total of 153.2 million Rights were issued and outstanding. Upon closing of the Rights Offering on January 18, 2016, Perpetual issued an aggregate of 665.4 million common shares of the Company, including 427.4 million common shares issued to entities controlled by the Chairman of Perpetual's Board of Directors for proceeds of $16.1 million. After completion of the Rights Offering on January 18, 2016 and the repayment of the convertible debentures with common shares on December 31, 2015, there are 1,047.7 million common shares outstanding.

Perpetual has provided notice to its shareholders of its annual and special meeting, scheduled to be held on March 24, 2016. At the meeting shareholders will vote on a proposed share consolidation which, if approved, would result in a consolidation of common shares on a twenty for one basis.

2016 OUTLOOK

In 2016, Perpetual's top four strategic priorities include:

- Reduce debt and restore cash flow;
- Grow value and scope of Greater Edson liquids-rich gas;
- Maximize value potential of Eastern Alberta assets; and
- Advance high impact opportunities.

With projected further low commodity prices in 2016, Perpetual will prioritize liquidity management and preservation of its balance sheet through restricted spending and a focus on reducing costs and maximizing efficiencies in administration and operations. A diligent focus on reductions in all areas of spending, including operating, financing and administrative costs, will continue in order to establish a sustainable cost structure in this low commodity price environment.

In order to protect a base level of funds flow, Perpetual has commodity price contracts in place in 2016 on an estimated 70 percent of forecast production from the remainder of the year. These include both AECO and NYMEX natural gas contracts from April to December 2016 on close to 70,000 GJ/d at an estimated price of $2.19/GJ; and oil sales arrangements on 1,000 bbl/d protecting a floor price at WTI of $USD43.50/bbl.

In light of the continued deterioration of commodity prices since December 2015, Perpetual has reduced its capital spending program for 2016 and Perpetual's Board of Directors has restricted its approval to a first quarter capital expenditure budget of $6 million. Approved first quarter spending is limited to drilling one (1.0 net) well at East Edson with minimal additional capital allocated to continue strategic production testing at Panny and Waskahigan, critical facility maintenance and overhauls, and third party abandonment and reclamation activity. Completion and tie in of the new East Edson well along with additional capital activity for the remainder of the year will be deferred and assessed on a project economics basis as the year progresses.

Perpetual continues to target strategic asset sales in 2016. In late February, the Company entered into a purchase and sale agreement for the disposition of 37 sections of its 425 net sections of oil sands leases in northeast Alberta in exchange for gross proceeds of $6.1 million and a one percent gross overriding royalty. Closing is scheduled prior to March 15, 2016. Proceeds from the disposition will be initially applied against outstanding debt.

CONTRACTUAL OBLIGATIONS AND COMMITMENTS

Perpetual has contractual agreements comprised of office lease costs and related sublease recoveries, as well as long-term commitments to utilize drilling rigs and pay for gas transportation on certain major pipeline systems in western Canada. As of December 31, 2015, the future minimum payments under these contractual agreements consisted of:

($thousands)	**Drilling Commitments**	**Pipeline commitments**	**Operating lease commitments**
2016	3,826	11,121	2,242
2017	1,056	6,540	2,179
2018	–	5,950	545
2019	–	4,209	–
2020	–	2,369	–
Total	**$ 4,882**	**$ 30,189**	**$ 4,966**

OFF BALANCE SHEET ARRANGEMENTS

Perpetual has no off balance sheet arrangements.

FUTURE ACCOUNTING PRONOUNCEMENTS

The International Accounting Standards Board (IASB) and the IFRS Interpretations Committee regularly issue new and revised accounting pronouncements which have future effective dates and therefore are not reflected in Perpetual's financial statements. Once adopted these new and amended pronouncements may have an impact on Perpetual's consolidated financial statements. Perpetual's analysis of recent accounting pronouncements is included in the notes to the consolidated financial statements at December 31, 2015.

CORPORATE GOVERNANCE

The Corporation is committed to maintaining high standards of corporate governance. Each regulatory body, including the Toronto Stock Exchange and the Canadian provincial securities commissions, has a different set of rules pertaining to corporate governance. The Corporation fully conforms to the rules of the governing bodies under which it operates.

RISK FACTORS

The business risks the Corporation is exposed to are those inherent in the oil and gas industry as well as those governed by the individual nature of Perpetual's operations. Risks impacting the business which influence controls and management of the Corporation include, but are not limited to, the following:

1. geological and engineering risks;
2. the uncertainty of discovering commercial quantities of new reserves;
3. commodity prices, interest rate and foreign exchange risks;
4. competition; and
5. changes to government regulations including shut in of GOB assets, royalty regimes and tax legislation.

Perpetual manages these risks by:

1. attracting and retaining a team of highly qualified and motivated professionals who have a vested interest in the success of the Corporation;
2. prudent operation of oil and natural gas properties;
3. employing risk management instruments and policies to manage exposure to volatility of commodity prices, interest rates and foreign exchange rates;
4. maintaining a flexible financial position;
5. maintaining strict environment, safety and health practices; and
6. active participation with industry organizations to monitor and influence changes in government regulations and policies.

A complete discussion of risk factors is included in the Corporation's 2015 AIF available on the Corporation's website at www.perpetualenergyinc.com or on sedar at www.sedar.com.

DISCLOSURE CONTROLS AND PROCEDURES AND INTERNAL CONTROL OVER FINANCIAL REPORTING

Perpetual's Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") have designed, or caused to be designed under their supervision, disclosure controls and procedures ("DC&P") and Internal controls over financial reporting ("ICOFR") as defined in National Instrument 52-109 Certification of Disclosure in Issuer's Annual and Interim Filings in order to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the financial statements for external purposes in accordance with IFRS.

Disclosure controls and procedures

The DC&P have been designed to provide reasonable assurance that material information relating to Perpetual is made known to the CEO and CFO by others and that information required to be disclosed by Perpetual in its annual filings, interim filing or other reports filed or submitted by Perpetual under securities legislation.

Perpetual's CEO and CFO have concluded, based on their evaluation at December 31, 2015, that DC&P are effective to provide reasonable assurance that material information related to the issuer is made known to them by others within the Corporation, as such information is recorded, processed, summarized and reported in the reports filed or sent to securities regulatory authorities within the time periods specified under Canadian securities laws.

Management's annual report on internal controls over financial reporting

Management is responsible for establishing and maintaining adequate ICOFR, which is a process designed by, or under the supervision of, the CEO and CFO, and effected by the board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS.

Under the supervision and with the participation of management, including the CEO and CFO, an evaluation of the effectiveness of the internal control over financial reporting was conducted as of December 31, 2015 based on criteria described in "Internal Control – Integrated Framework" issued in 2013 by the Committee of Sponsoring Organization of the Treadway Commission. Based on this assessment, management determined that, as of December 31, 2015, the internal control over financial reporting was effective.

Changes to internal controls over financial reporting

There were no changes in the Corporation's internal control over financial reporting during the period beginning on January 1, 2015 and ended December 31, 2015 that have materially affected, or are reasonably likely to materially affect, internal control over financial reporting.

CEO and CFO certifications

Perpetual's CEO and CFO have filed with the Canadian securities regulators regarding the quality of Perpetual's public disclosures relating to its fiscal 2015 report filed with the Canadian securities regulators.

CRITICAL ACCOUNTING ESTIMATES

Perpetual makes assumptions in applying certain critical accounting estimates that are uncertain at the time the accounting estimate is made and may have a significant effect on the consolidated financial statements. Critical accounting estimates include oil and natural gas reserves, derivative financial instruments, provisions, the amount and likelihood of contingent liabilities and income taxes. Critical accounting estimates are based on variable inputs including:

- Estimation of recoverable oil and natural gas reserves and future cash flows from reserves;
- Forward market prices;
- Geological interpretations, success or failure of exploration activities, and Perpetual's plans with respect to property and financial ability to hold the property;
- Risk free interest rates;
- Estimation of future abandonment and reclamation costs;
- Facts and circumstances supporting the likelihood and amount of contingent liabilities; and
- Interpretation of income tax laws.

A change in a critical accounting estimate can have a significant effect on net income as a result of their impact on the depletion rate, provisions, impairments, losses and income taxes. A change in a critical accounting estimate can have a significant effect on the value of property, plant, and equipment, provisions, derivative financial instruments and accounts payable. A complete discussion of critical accounting estimates is included in the notes to the consolidated financial statements at December 31, 2015.

MANAGEMENT'S REPORT

The consolidated financial statements of Perpetual Energy Inc. ("Perpetual" or "the Corporation") are the responsibility of Management and have been approved by the Board of Directors of Perpetual. These consolidated financial statements have been prepared by Management in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and the Interpretations of the IFRS Interpretations Committee.

The consolidated financial statements are audited and have been prepared using accounting policies in accordance with IFRS. The preparation of Management's Discussion and Analysis is based on Perpetual's financial results which have been prepared in accordance with IFRS. It compares Perpetual's financial performance in 2015 to 2014 and should be read in conjunction with the consolidated financial statements and accompanying notes.

Management is responsible for establishing and maintaining adequate internal control over Perpetual's financial reporting. Management believes that the system of internal controls that have been designed and maintained at Perpetual provide reasonable assurance that financial records are reliable and form a proper basis for preparation of financial statements. The internal accounting control process includes Management's communication to employees of policies which govern ethical business conduct.

Internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

The Board of Directors has appointed an Audit Committee consisting of unrelated, non-management directors which meets at least four times during the year with Management and independently with the external auditors and as a group to review any significant accounting, internal control and auditing matters in accordance with the terms of the charter of the Audit Committee as set out in the Annual Information Form. The Audit Committee reviews the consolidated financial statements and Management's Discussion and Analysis before the consolidated financial statements are submitted to the Board of Directors for approval. The external auditors have free access to the Audit Committee without obtaining prior Management approval.

With respect to the external auditors, the Audit Committee approves the terms of engagement and reviews the annual audit plan, the Auditors' Report and results of the audit. It also recommends to the Board of Directors the firm of external auditors to be appointed by the shareholders.

The independent external auditors, KPMG LLP, have been appointed by the Board of Directors on behalf of the shareholders to express an opinion as to whether the consolidated financial statements present fairly, in all material respects, Perpetual's financial position, results of operations and cash flows in accordance with IFRS. The report of KPMG LLP outlines the scope of their examination and their opinion on the consolidated financial statements.

Susan Riddell Rose

Susan L. Riddell Rose
President &
Chief Executive Officer

Cameron R. Sebastian
Vice President, Finance &
Chief Financial Officer

March 2, 2016

INDEPENDENT AUDITORS' REPORT

To the Shareholders and Board of Directors of Perpetual Energy Inc.

We have audited the accompanying consolidated financial statements of Perpetual Energy Inc., which comprise the consolidated statements of financial position as at December 31, 2015 and December 31, 2014, the consolidated statements of income (loss) and comprehensive income (loss), changes in equity and cash flows for the years then ended, and notes, comprising 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.

Auditors' 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 our 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, we consider internal control relevant to the Corporation'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 consolidated financial position of Perpetual Energy Inc. as at December 31, 2015 and December 31, 2014, and its consolidated financial performance and its consolidated cash flows for the years then ended, in accordance with International Financial Reporting Standards.

KPMG LLP

Chartered Professional Accountants
Calgary, Canada
March 2, 2016

PERPETUAL ENERGY INC.
Consolidated Statements of Financial Position

As at	December 31, 2015	December 31, 2014
(*Cdn$ thousands*)		
Assets		
Current assets		
Cash and cash equivalents	**$ 2,116**	$ 11,497
Restricted cash (note 5)	**–**	6,552
Accounts receivable	**19,532**	50,297
Marketable securities (note 4)	**145,275**	–
Prepaid expenses and deposits	**3,141**	1,635
Derivatives (note 19)	**2,319**	9,315
	172,383	79,296
Derivatives (note 19)	**1,411**	–
Property, plant and equipment (note 5)	**347,903**	561,956
Exploration and evaluation (note 6)	**56,407**	84,227
Equity-method investment (note 7)	**25,346**	25,123
Total assets	**$ 603,450**	$ 750,602
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	**$ 38,621**	$ 91,859
Derivatives (note 19)	**9,353**	2,398
Bank indebtedness (note 8)	**42,000**	–
Convertible debentures (note 9)	**–**	33,810
Financial obligation (note 10)	**2,604**	3,584
TOU Share financial arrangement (note 11)	**18,059**	–
Provisions (note 13)	**1,981**	5,372
	112,618	137,023
Derivatives (note 19)	**7,395**	3,872
Senior notes (note 12)	**271,658**	270,690
Financial obligation (note 10)	**7,407**	11,806
Provisions (note 13)	**157,188**	220,928
Total liabilities	**556,266**	644,319
Equity		
Share capital (note 14)	**1,297,911**	1,258,840
Shares held in trust (note 15)	**(1,177)**	(1,387)
Rights (note 14)	**5,290**	–
Equity component of convertible debentures (note 9)	**–**	3,174
Contributed surplus	**38,300**	36,754
Deficit	**(1,293,140)**	(1,191,098)
Total equity	**47,184**	106,283
Total liabilities and equity	**$ 603,450**	$ 750,602

Subsequent events (note 14).

See accompanying notes. The notes are an integral part of the Corporation's annual consolidated financial statements.

Robert A. Maitland
Director

Geoffrey C. Merritt
Director

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

	Year Ended December 31, 2015	2014
(*Cdn$ thousands, except per share amounts*)		
Revenue		
Oil and natural gas	**$ 142,437**	$ 262,790
Royalties	**(16,344)**	(32,024)
	126,093	230,766
Change in fair value of commodity price derivatives (note 19)	**(11,437)**	2,819
Gas over bitumen (note 3i)	**3,153**	8,888
	117,809	242,473
Expenses		
Production and operating	**65,133**	78,128
Transportation	**12,058**	12,684
Exploration and evaluation (note 6)	**10,730**	5,944
General and administrative	**21,235**	28,343
Gains on dispositions (notes 5)	**(146,632)**	(42,944)
Depletion and depreciation (note 5)	**88,364**	94,736
Impairment losses (note 5)	**23,700**	21,400
Income from operating activities	**43,221**	44,182
Finance expenses (note 17)	**(27,890)**	(37,592)
Change in fair value of marketable securities (note 4)	**(104,828)**	–
Share of net income (loss) of equity-method investment (note 7)	**223**	(3,224)
Net income (loss) and comprehensive income (loss)	**(89,274)**	3,366
Income (loss) per share (note 14)		
Basic and diluted	**$ (0.59)**	$ 0.02

See accompanying notes. The notes are an integral part of the Corporation's annual consolidated financial statements.

PERPETUAL ENERGY INC.
Consolidated Statements of Changes in Equity

(*Cdn$ thousands*)	Share capital (*thousands*)	(*$thousands*)	Shares held in trust	Rights	Equity component of convertible debentures	Contributed surplus	Deficit	Total equity
Balance at December 31, 2014	150,077	$ 1,258,840	$ (1,387)	$ –	$ 3,174	$ 36,754	$ (1,191,098)	$ 106,283
Net loss and comprehensive loss	–	–	–	–	–	–	(89,274)	(89,274)
Common shares issued pursuant to share based compensation plans	3,283	1,019	1,319	–	–	(2,239)	–	99
Share based compensation expense (note 16)	–	–	–	–	–	3,785	–	3,785
Redemption of convertible debentures (note 9)	228,928	38,052	–	–	(3,174)	–	–	34,878
Recapitalization transactions (note 14)	–	–	–	5,290	–	–	(12,768)	(7,478)
Change in shares held in trust (note 15)	–	–	(1,109)	–	–	–	–	(1,109)
Balance at December 31, 2015	**382,288**	**$ 1,297,911**	**$ (1,177)**	**$ 5,290**	**$ –**	**$ 38,300**	**$(1,293,140)**	**$ 47,184**

(*Cdn$ thousands*)	Share capital (*thousands*)	(*$thousands*)	Shares held in trust	Rights	Equity component of convertible debentures	Contributed surplus	Deficit	Total equity
Balance at December 31, 2013	148,490	$ 1,257,315	$ –	$ –	$ 13,971	$ 21,474	$ (1,194,464)	$ 98,296
Net income and comprehensive income	–	–	–	–	–	–	3,366	3,366
Common shares issued pursuant to share based compensation plans	1,587	1,544	–	–	–	(1,489)	–	55
Share based compensation expense (note 16)	–	–	–	–	–	5,972	–	5,972
Redemption of convertible debentures (note 9)	–	–	–	–	(10,797)	10,797	–	–
Change in shares held in trust (note 15)	–	(19)	(1,387)	–	–	–	–	(1,406)
Balance at December 31, 2014	150,077	$ 1,258,840	$ (1,387)	$ –	$ 3,174	$ 36,754	$ (1,191,098)	$ 106,283

See accompanying notes. The notes are an integral part of the Corporation's annual consolidated financial statements.

PERPETUAL ENERGY INC.
Consolidated Statements of Cash Flows

	Year Ended December 31, 2015	2014
(*Cdn$ thousands*)		
Cash flows from (used in) operating activities		
Net income (loss)	**$ (89,274)**	$ 3,366
Adjustments to add (deduct) non-cash items:		
Depletion and depreciation	**88,364**	94,736
Exploration and evaluation (note 6)	**6,338**	2,135
Share based compensation expense (note 16)	**3,774**	5,972
Change in fair value of commodity price derivatives (note 19)	**16,063**	(11,946)
Change in fair value of marketable securities (note 4)	**104,828**	–
Finance expenses (note 17)	**(2,756)**	7,637
Share of net (income) loss of equity-method investment	**(223)**	3,224
Gains on dispositions	**(146,632)**	(42,944)
Impairment losses	**23,700**	21,400
Long-term Crown receivable adjustments	**–**	10,997
Expenditures on decommissioning obligations (note 13)	**(7,589)**	(6,633)
Change in non-cash working capital (note 18)	**15,813**	(5,862)
Net cash from operating activities	**12,406**	82,082
Cash flows from (used in) financing activities		
Change in bank indebtedness	**42,000**	(70,618)
Repayment of convertible debentures (note 9)	**–**	(124,903)
Net proceeds on senior notes issuance (note 12)	**–**	122,292
Change in financial obligation (note 10)	**(3,704)**	18,425
Proceeds on TOU Share financial arrangement (note 11)	**18,230**	–
Transactions with trustee (note 15)	**(1,109)**	(1,406)
Common shares issued	**99**	55
Change in non-cash working capital (note 18)	**–**	1,527
Net cash from (used in) financing activities	**55,516**	(54,628)
Cash flows from (used in) investing activities		
Acquisitions	**(243)**	(998)
Capital expenditures	**(76,341)**	(116,427)
Proceeds on dispositions	**23,953**	71,349
Proceeds on sale of marketable securities (note 4)	**8,557**	–
Change in non-cash working capital (note 18)	**(33,229)**	30,119
Net cash used in investing activities	**(77,303)**	(15,957)
Change in cash and cash equivalents	**(9,381)**	11,497
Cash and cash equivalents, beginning of year	**11,497**	–
Cash and cash equivalents, end of year	**$ 2,116**	$ 11,497
Interest paid	**$ 30,273**	$ 28,443

See accompanying notes. The notes are an integral part of the Corporation's annual consolidated financial statements.

1. REPORTING ENTITY

Perpetual Energy Inc. ("Perpetual" or the "Corporation") is a Canadian corporation engaged in the exploration, development and marketing of oil and gas based energy in Alberta, Canada. The Corporation operates a diversified asset portfolio that includes shallow gas in Eastern Alberta, conventional heavy oil, liquids-rich gas in the Alberta deep basin, and several long-term bitumen resource properties.

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

The consolidated financial statements of the Corporation are comprised of the accounts of Perpetual and its wholly owned subsidiaries, Perpetual Energy Operating Corp. and Perpetual Operating Trust, which are incorporated in Canada.

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").

The consolidated financial statements of the Corporation were approved and authorized for issue by the Board of Directors on March 2, 2016.

The consolidated financial statements have been prepared on a historical cost basis except for the financial obligation (note 10), TOU Share financial arrangement (note 11) and derivative financial instruments (note 19) that have been measured at fair value. The consolidated financial statements are presented in Canadian dollars which is the functional currency of the Corporation and its subsidiaries.

a) Critical accounting judgments and significant estimates

The preparation of the consolidated financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and reported amounts of assets, liabilities, revenue and expenses. These judgments, estimates, and assumptions are continuously evaluated and are based on management's experience and all relevant information available to the Corporation at the time of financial statement preparation. As the effect of future events cannot be determined with certainty the actual results may differ from estimates. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

Information about the critical judgments and significant estimates made by management are described below and also in the relevant notes to the financial statements.

b) Critical accounting judgments:

The following are the critical judgments that management has made in the process of applying the Corporation's accounting policies. These judgments have the most significant effect on the amounts reported in the consolidated financial statements.

i) Cash-generating units

The Corporation allocates its oil and natural gas properties to cash generating units ("CGUs") identified as the smallest group of assets that generate cash flows independent of the cash flows of other assets or groups of assets. Determination of the CGUs is subject to management's judgement and is based on geographical proximity, shared infrastructure, and similar exposure to market risk.

ii) Identification of impairment indicators

Judgment is required to assess when significant indicators of impairment or reversals exist and whether calculation of the recoverable amount of an asset is necessary. Management considers internal and external sources of information that suggest the carrying amount of an asset is impaired, or in the case of a previously impaired asset, whether the carrying amount of the asset has been restored.

iii) Componentization

For the purposes of depletion the Corporation allocates its oil and natural assets to components with similar useful lives and depletion methods. The grouping of assets is subject to management's judgment and is performed on the basis of geographical proximity and similar reserve life. The Corporation's oil and gas assets are depleted on a unit of production basis.

iv) Exploration and evaluation expenditures

Costs associated with acquiring oil and natural gas licenses and exploratory drilling are accumulated as exploration and evaluation ("E&E") assets pending determination of technical feasibility and commercial viability. Establishment of technical feasibility and commercial viability is subject to judgment and involves management's review of project economics, resource quantities, expected production techniques, production costs and required capital expenditures to confirm continued intent to develop and extract the underlying resources. Management uses the establishment of commercial reserves within the exploration area as the basis for determining technical feasibility and commercial viability. Upon determination of commercial reserves, E&E assets attributable to those reserves are tested for impairment and reclassified from E&E assets to a separate category within property, plant and equipment referred to as oil and natural gas properties.

v) Joint arrangements

Judgment is required to determine when the Corporation has joint control over an arrangement. In establishing joint control the Corporation considers whether unanimous consent is required to direct the activities that significantly affect the returns of the arrangement, such as the capital and operating activities of the arrangement.

Once joint control has been established judgment is also required to classify a joint arrangement. The type of joint arrangement is determined through analysis of the rights and obligations arising from the arrangement by considering its structure, legal form, and terms agreed upon by the parties sharing control. An arrangement where the controlling parties have rights to the assets and revenues, and obligations for the liabilities and expenses, is classified as a joint operation. Arrangements where the controlling parties have rights to the net assets of the arrangement are classified as joint ventures.

c) Significant estimates:

The following assumptions represent the key sources of estimation uncertainty at the end of the reporting period. As future confirming events occur the actual results may differ from estimated amounts.

i) Reserves

The Corporation uses estimates of natural gas, oil, and natural gas liquids ("NGL" or "liquids") reserves in the calculation of depletion and also for value in use ("VIU") and fair value less costs of disposal ("FVLCD") calculations of non-financial assets. Estimates of economically recoverable natural gas, oil, and liquids reserves and their future net cash flows are based upon a number of variable factors and assumptions, such as geological, geophysical, and engineering assessments of hydrocarbons in place on the Corporation's lands, historical production from the properties, production rates, future commodity prices, ultimate reserve recovery, timing and amount of capital expenditures, marketability of oil and natural gas, royalty rates, the assumed effects of regulation by government agencies and future operating costs. The geological, economic and technical factors used to estimate reserves may change from period to period. Changes in the reported reserves could have a material impact on the carrying values of the Corporation's oil and natural gas properties, the calculation of depletion and depreciation and the timing of decommissioning cash flows.

Reserve engineers are engaged at least annually to independently evaluate or review the recoverable quantities and estimated future cash flows from the Corporation's interest in petroleum and natural gas properties. This evaluation of proved and proved plus probable reserves is prepared in accordance with the reserve definitions contained in National Instrument 51-101 and the COGE Handbook.

ii) Provisions for decommissioning obligations

Decommissioning, abandonment, and site reclamation expenditures for production facilities, wells and pipelines are expected to be incurred by the Corporation over many years into the future. Amounts recorded for decommissioning obligations and the associated accretion are calculated based on estimates of the extent and timing of decommissioning activities, future site remediation regulations and technologies, inflation, liability specific discount rates and related cash flows. The provision represents management's best estimate of the present value of the future abandonment and reclamation costs required. Actual abandonment and reclamation costs could be materially different from estimated amounts.

iii) Derivative financial instruments

Derivatives are measured at fair value on each reporting date. Fair value is the price that would be received or paid to exit the position as of the measurement date. The Corporation uses estimated external forward market price curves available at period end and the contracted volumes over the contracted term to determine the fair value of each contract. Changes in market pricing between period end and settlement of the derivative contracts could have a material impact on financial results related to the derivatives.

iv) Financial obligation

The financial obligations are measured at fair value on each reporting date. Fair value is the price that would be paid to exit the position as of the measurement date.

The fair value of the financial obligation is estimated by discounting future cash payments based on the forecasted Alberta gas reference price multiplied by the contracted deemed volume. Changes in market pricing between period end and settlement of the hybrid financial obligations could have a material impact on financial results related to the financial obligation.

v) TOU Share financial arrangement

The fair value of the TOU Share financial arrangement is estimated using market pricing for identical financial instruments adjusted for provisions specific to the contract such as the maximum repayment amount and the notional amount of shares pledged as security. Changes in the market pricing of the shares could have a material impact on financial results related to the TOU Share financial arrangement and the measurement of the cash payment at maturity.

3. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to all periods presented in these annual consolidated financial statements, and have been applied consistently by the Corporation, its subsidiaries, and its equity method investee.

a) Basis of consolidation

i) Subsidiaries

Subsidiaries are entities controlled by the Corporation. Control exists when the Corporation has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that are currently exercisable are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

ii) Business combinations

The acquisition method of accounting is used to account for acquisitions of subsidiaries and assets that meet the definition of a business under IFRS. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of acquisition of control. Identifiable assets acquired and liabilities assumed in a business combination are measured at their recognized amounts (generally fair value) at the acquisition date. The excess of the cost of acquisition over the recognized amounts of the identifiable assets acquired and liabilities assumed is recorded as goodwill. If the cost of acquisition is less than the recognized amount of the net assets acquired, the difference is recognized as a bargain purchase gain in net income or loss.

iii) Joint venture

The Corporation's investment in Warwick Gas Storage Limited Partnership ("WGS LP") is structured through a separate vehicle whereby joint control is established and the contractual arrangement provides the parties with rights to the net assets of WGS LP. Perpetual's investment in WGS LP is accounted for as an investment in a jointly controlled entity using the equity-method of accounting.

On initial recognition of the investment, any excess of the Corporation's share of the fair value of WGS LP's net assets over the cost of the investment is included in the determination of the Corporation's share of WGS LP's profit or losses. The Corporation's share of WGS LP's profits or losses is recognized in net income or loss. Appropriate adjustments to the Corporation's share of WGS LP profits or losses are also made to account for depreciation of assets based on their fair values at the date of initial recognition. Dividends receivable are recognized as a reduction to the carrying amount of the investment and are included in cash flows from operating activities.

When the Corporation's cumulative share of losses equals or exceeds the Corporation's carrying amount of the investment, the Corporation does not recognize further losses unless the Corporation has incurred obligations or made payments on behalf of WGS LP.

An impairment loss in respect of an equity-method accounted investee is measured by comparing the recoverable amount of the investment with its carrying amount. An impairment loss is recognized in profit or loss, and is reversed if there is a favorable change in the estimates used to determine the recoverable amount.

iv) Joint operations

Many of the Corporation's oil and natural gas activities involve jointly controlled operations which are not conducted through a separate vehicle. The consolidated financial statements include the Corporation's proportionate share of these jointly controlled assets, liabilities, revenues and expenses.

v) Transactions eliminated on consolidation

Intercompany balances and transactions, and any unrealized income and expenses arising from intercompany transactions, are eliminated in preparing the consolidated financial statements.

b) Financial instruments

Financial instruments are initially recognized at fair value on the statement of financial position. Subsequent measurement of financial instruments is based on their initial classification into one of the following categories: financial assets and liabilities measured at fair value through profit or loss, loans and receivables, held to maturity investments, available-for-sale financial assets, or other financial liabilities.

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

i) Non-derivative financial assets

Financial Instrument	Category	Subsequent Measurement
Accounts receivable	Loans and receivables	Amortized cost
Marketable securities	Financial assets	Fair value through profit or loss

The Corporation's accounts receivable are initially recognized on the date they originate and are measured at amortized cost using the effective interest method, less any impairment losses.

Marketable securities are non-derivative financial instruments measured at fair value through profit or loss ("FVTPL") as the Corporation manages such investments and makes decisions based on their fair value in accordance with the Corporation's risk management or investment strategy.

ii) Derivative assets and liabilities

The Corporation has entered into certain financial derivative contracts in order to manage the exposure to market risks from fluctuations in commodity prices and currency rates. The Corporation has not designated its financial derivative contracts as effective accounting hedges, and thus not applied hedge accounting, even though the Corporation considers all commodity and currency contracts to be economic hedges. As a result, all financial derivative contracts are designated as fair value through profit or loss and recorded as derivatives on the statement of financial position at fair value. Changes in the fair value of the commodity price and currency rate derivatives are recognized in net income or loss.

The Corporation has accounted for its forward physical delivery fixed-price sales contracts as derivative financial instruments. Accordingly, such forward physical delivery fixed-price sales contracts are designated as fair value through profit or loss and recorded as derivatives on the statement of financial position at fair value.

Transaction costs on derivatives are recognized in net income or loss when incurred.

Embedded derivatives are separated from the host contract and accounted for separately if the economic characteristics and risks of the host contract and the embedded derivative are not closely related, a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative and the combined instrument is not measured at fair value through profit or loss. Changes in the fair value of separable embedded derivatives are recognized immediately in net income or loss.

iii) Non-derivative financial liabilities

Financial Instrument	Category	Subsequent Measurement
Accounts payable and accrued liabilities	Financial liabilities	Amortized cost
Bank indebtedness	Financial liabilities	Amortized cost
Senior notes	Financial liabilities	Amortized cost
Convertible debentures	Financial liabilities	Amortized cost
Financial obligation	Financial liabilities	Fair value through profit or loss
TOU Share financial arrangement	Financial liabilities	Fair value through profit or loss

Accounts payable and accrued liabilities, bank indebtedness and senior notes are recognized initially at fair value and are subsequently measured at amortized cost using the effective interest method.

The Corporation's convertible debentures are classified as debt with a portion of the proceeds allocated to equity representing the conversion feature. If the debentures are converted, a portion of debt and conversion feature components are transferred to share capital. The debt component associated with the convertible debentures accretes over time to the amount owing on maturity and such increases in the debt component are reflected as non-cash interest expense in net income or loss. The convertible debentures are carried net of issue costs on the statement of financial position. The issue costs are amortized to net income or loss using the effective interest rate method.

iv) Share capital

Incremental costs directly attributable to the issue of common shares and share options are recognized as a deduction from equity, net of any tax effects.

c) Property, plant and equipment

i) Production and development costs

Items of property, plant and equipment, which include oil and natural gas development and production assets, are measured at cost less accumulated depletion and depreciation and accumulated impairment losses. The initial cost of property, plant and equipment includes the purchase price or construction costs, costs that are directly attributable to bringing the asset into commercial operations, the initial estimate of decommissioning costs, and borrowing costs for qualifying assets.

Significant parts of an item of property, plant and equipment, including oil and natural gas properties, that have different useful lives from the life of the area or facility in general, are accounted for as separate items.

Gains and losses on disposition of an item of property, plant and equipment, including oil and natural gas properties, are determined by comparing the proceeds from disposition with the carrying amount of property, plant and equipment and are recognized in net income or loss. The carrying amount of any replaced or disposed item of property, plant and equipment is derecognized.

ii) Subsequent costs

Costs incurred subsequent to the determination of technical feasibility and commercial viability and the costs of replacing parts of property, plant and equipment are recognized as property, plant and equipment only when they increase the future economic benefits embodied in the specific asset to which they relate. All other expenditures are recognized in net income or loss as incurred. Such capitalized property, plant and equipment generally represent costs incurred in developing proved and/or probable reserves and bringing on or enhancing production from such reserves, and are accumulated on a field or geotechnical area basis. The costs of the day-to-day servicing of property, plant and equipment are recognized in net income or loss as incurred.

iii) Depletion and depreciation

The net carrying amount of development or production assets is depleted using the unit of production method by reference to the ratio of production in the period to the related proved and probable reserves, taking into account estimated future development costs necessary to bring those reserves into production and future decommissioning costs. Future development and decommissioning costs are estimated taking into account the level of development required to produce the reserves. The future development cost estimates are reviewed by independent reserve engineers at least annually.

Costs associated with office furniture, information technology, and leasehold improvements are carried at cost and are depreciated on a straight line basis over a period ranging from one to three years.

Costs associated with abandonment equipment and turnaround equipment at major facilities are carried at cost and are depreciated on a straight line basis over a period ranging from five to seven years.

Depreciation methods, useful lives and residual values are reviewed at each period end date for all classes of property, plant, and equipment.

d) Exploration and evaluation expenditures

Pre-license costs, geological and geophysical costs and lease rentals of undeveloped properties are recognized in net income or loss as incurred.

E&E costs, consisting of the costs of acquiring oil and natural gas licenses, are capitalized initially as E&E assets according to the nature of the assets acquired. Costs associated with drilling exploratory wells in an undeveloped area are capitalized as E&E costs. The costs are accumulated in cost centers by well, field or exploration area pending determination of technical feasibility and commercial viability. When technical feasibility and commercial viability are determined, the relevant expenditure is transferred to oil and gas properties after impairment is assessed and any applicable impairment loss is recognized in net income or loss.

The Corporation's E&E assets consist of undeveloped land, exploratory drilling assets, and bitumen evaluation assets. Gains and losses on disposition of E&E assets are determined by comparing the proceeds from disposition with the carrying amount and are recognized in net income or loss.

e) Assets held for sale

Non-current assets, or disposal groups consisting of assets and liabilities ("disposal groups"), are classified as held for sale if their carrying amounts will be recovered principally through a sale transaction rather than through continuing use. Assets and liabilities qualifying as held for sale must be available for immediate sale in their present condition subject to normal terms and conditions and their sale must be highly probable.

Non-current assets, or disposal groups, are measured at the lower of the carrying amount and fair value less costs of disposal, with impairments recognized in net income or loss. Non-current assets or disposal groups held for sale are presented in current assets and liabilities within the statement of financial position. Assets held for sale are not subject to depletion and depreciation.

f) Impairment

i) Financial assets

Financial assets are assessed at each period end date to determine whether there is any objective evidence that they are impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset.

An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate.

Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar credit risk characteristics.

All impairment losses are recognized in net income or loss. An impairment loss is reversed when there is objective evidence that the value of the financial asset has been partially or fully restored. For financial assets measured at amortized cost the reversal is recognized in net income or loss.

ii) Non-financial assets

The carrying amounts of the Corporation's non-financial assets, other than E&E assets, are reviewed at each period end date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. E&E assets are assessed for impairment when they are reclassified to property, plant and equipment, as oil and natural gas properties, and also if facts and circumstances suggest that the carrying amount exceeds the recoverable amount.

For the purpose of impairment testing, assets are grouped together at a CGU level which is the smallest group of assets that generates cash inflows from continuing use and are largely independent of the cash inflows of other assets or groups of assets. The recoverable amount of an asset or a CGU is determined based on the higher of its FVLCD and its VIU. FVLCD is determined as the amount that would be obtained from the sale of a CGU in an arm's length transaction between knowledgeable and willing parties. The FVLCD of oil and gas properties is generally determined as the net present value of estimated future cash flows expected to arise from the continued use of the CGU and its eventual disposition, using assumptions that an independent market participant may take into account. These cash flows are discounted by an appropriate discount rate which would be applied by such a market participant to arrive at a new present value of the CGU. In determining value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Value in use is generally determined by reference to the present value of the future cash flows expected to be derived from production of proved and probable reserves.

E&E assets are assessed for impairment both at the time of any triggering facts and circumstances as well as upon their eventual reclassification to oil and natural gas properties in property, plant and equipment. If a test is required as a result of triggering facts and circumstances, the Corporation considers whether the combined recoverable amount of oil and natural gas properties and E&E assets at the total company level is sufficient to cover the combined carrying value of E&E and oil and natural gas assets. E&E assets are tested for impairment on reclassification to oil and natural gas properties.

An impairment loss is recognized if the carrying amount of an asset or its CGU, including the related decommissioning obligation, exceeds its estimated recoverable amount. Impairment losses recognized in respect of CGUs are allocated to reduce the carrying amount of assets in the unit (group of units) on a pro rata basis. Impairment losses are recognized in net income or loss.

In respect of other assets, impairment losses recognized in prior years are assessed at each period end date for any indication that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depletion and depreciation, if no impairment loss had been recognized.

g) Shares held in trust

The Corporation has a compensation program whereby employees may be entitled to receive shares of the Corporation purchased on the open market by a trustee controlled by Perpetual. Shares acquired and held by the trustee for the benefit of employees that have not yet been issued to employees are presented as a separate category of equity. The balance of shares held in trust represents the cumulative cost of shares held by the trustee. Upon the issuance of shares to the employee, the amount attributable to an employee is deducted from the balance of shares held in trust and transferred to contributed surplus.

h) Share based payments

Awards granted under share based payment plans and agreements are equity-settled and are measured at grant-date fair value. Fair values are determined by means of an option pricing model using the exercise price of the equity instrument granted, the share price at the grant date, the expected life of the grant based on the vesting date and expiry date, estimates of volatility and interest rates over its expected life. A forfeiture rate is estimated on the grant date and is subsequently adjusted to reflect the actual number of options that vest.

The costs of the equity-settled share based payments are recognized within general and administrative expenses, or property, plant and equipment to the extent they are directly attributable, with a corresponding increase in contributed surplus over the vesting period. Upon exercise or settlement of an equity-based instrument, consideration received and associated amounts previously recorded in contributed surplus are recorded to share capital.

i) Provisions

Provisions are recognized when the Corporation has a current legal or constructive obligation as a result of a past event, which can be reliably estimated, and will require the outflow of economic resources to settle the obligation. A non-current provision is determined using the estimated future cash flows discounted at a rate that reflects current market conditions and liability specific risks.

i) Decommissioning obligations

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

Decommissioning obligations are measured at the present value of management's estimate of expenditures required to settle the present obligation at the statement of financial position date and using a risk free interest rate not adjusted for credit risk. Subsequent to the initial measurement, the obligation is adjusted at the end of each period to reflect the passage of time, changes in the estimated future cash flows underlying the obligation and changes in the risk free rate. The accretion of the provision due to the passage of time is recognized in net income or loss whereas changes in the provision arising from changes in estimated cash flows or changes in the risk free rate are capitalized. Actual costs incurred upon settlement of the decommissioning obligations are charged against the provision to the extent the provision was established.

ii) Gas over bitumen provision

The Corporation's entitlement to gas over bitumen royalty adjustments under the Natural Gas Royalty Regulation (2004) with respect to foregone production (deemed production) from gas wells shut-in for the benefit of bitumen producers in the Athabasca oil sands area is recognized as gas over bitumen revenue in the period that deemed production occurs.

The gas over bitumen royalty adjustment reduces the Corporation's gas Crown royalties ("royalty adjustments") otherwise payable. To the extent that royalty adjustments exceed gas Crown royalties payable in a given period, the amount is recorded as a receivable when there is reasonable assurance that it will be recovered and classified as current to the extent that the amounts are expected to be recovered within one year.

To the extent that these gas wells are allowed to return to production, the Corporation will be subject to gross overriding royalty of one percent for each year the gas over bitumen royalty adjustment was received to a maximum of 10 percent. The Corporation records a provision reflecting the present value of the expected repayments of the gas over bitumen royalty adjustments received by the Corporation under the Natural Gas Royalty Regulation (2004) should the related properties resume production. The expected repayments of the gas over bitumen royalty adjustments are estimated based on the present value of the expected gross overriding royalty on future revenues from the production of proved and probable reserves. Accretion of the provision due to the passage of time and change in estimated cash flows are recognized in net income or loss. Actual repayments, if any, will be charged against the provision as incurred.

j) Revenue

Revenue and royalty expense from the sale of oil and natural gas is recorded when the significant risks and rewards of ownership of the product are transferred to the buyer which is usually when legal title passes to the external party. This is generally at the time product enters a third party transmission pipeline.

Royalty income is recognized as it accrues in accordance with the terms of the overriding royalty agreements. Gas over bitumen adjustments are recognized as revenue to the extent that they offset gas Crown royalties otherwise payable in a given period.

k) Income tax

Income tax expense comprises current and deferred components. Income tax expense is recognized in net income or loss except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the period end date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognized on the initial recognition of assets or liabilities in a transaction that is not a business combination. In addition, deferred tax is not recognized for taxable temporary differences arising on the initial recognition of goodwill. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the period end date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

A deferred tax asset is recognized to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilized. Deferred tax assets are reviewed at each period end date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

l) Income or loss per share amounts

Basic income or loss per share is calculated by dividing the net income or loss by the weighted average number of common shares outstanding during the period. For the dilutive net income or loss per share calculation, the weighted average number of shares outstanding is adjusted for the potential number of shares which may have a dilutive effect on net income or loss.

Diluted income or loss per share is calculated giving effect to the potential dilution that would occur if outstanding Share Options, Restricted Rights, Performance Share Units, or potential dilutive convertible debentures were exercised or converted into common shares. The weighted average number of diluted shares is calculated in accordance with the treasury stock method for Share Options, Restricted Rights and Performance Share Units and the if-converted method for potentially issuable common shares through the convertible debentures. The treasury stock method assumes that the proceeds received from the exercise of all potentially dilutive instruments are used to repurchase common shares at the average market price. The if-converted method assumes conversion of convertible securities at the beginning of the reporting period**.**

m) Recent pronouncements issued

Perpetual will be required to adopt the following new standards and amendments as issued by the IASB. The Corporation is currently evaluating the impact on the consolidated financial statements as discussed below.

i) IFRS 11, "Interests in Joint Operations" was amended in May 2014 to require the application of business combination accounting on acquisitions of interests in a joint operation that constitutes a business. The amendments apply prospectively for annual periods beginning on or after January 1, 2016.

ii) IFRS 15, "Revenue from Contracts with Customers" was issued in May 2014 and introduces a single model that applies to contracts with customers and two approaches to recognizing revenue: at a point in time or over time. The new model features a contract-based five-step analysis of transactions to determine whether, how much and when revenue is recognized. New estimates and judgmental thresholds have been introduced, which may affect the amount and/or timing of revenue recognized. The new standard applies to contracts with customers. It does not apply to insurance contracts, financial instruments or lease contracts, which fall in the scope of other IFRSs. The new standard is effective for annual periods beginning on or after January 1, 2018 with early adoption permitted.

iii) IFRS 9, "Financial Instruments" was issued in July 2014 and introduces new requirements for the classification and measurement of financial assets. Under the new standard, financial assets are classified and measured based on the business model in which they are held and the characteristics of their contractual cash flows. The standard amends the impairment model by introducing a new 'expected credit loss' model for calculating impairment. The mandatory effective date of IFRS 9 is for annual periods beginning on or after January 1, 2018 and must be applied retrospectively with some exemptions. The restatement of prior periods is not required and is only permitted if information is available without the use of hindsight.

iv) IFRS 16, "Leases" was issued in January 2016 and replaces IAS 17 "Leases". Under the new standard, a single recognition and measurement model for leases is introduced which would require the recognition of most leases with a term greater than twelve months on the statement of financial position. The new standard is effective for annual periods beginning on or after January 1, 2019. Early adoption is permitted for entities that apply IFRS 15 "Revenue from Contracts with Customers" at or before the initial adoption date of January 1, 2018.

Perpetual has not applied any of these new standards as of December 31, 2015. The Corporation is currently evaluating the extent of the impact that adoption will have on the consolidated financial statements.

4. MARKETABLE SECURITIES

On April 1, 2015, the Corporation received 6.75 million common shares of Tourmaline Oil Corp. ("TOU Shares") in exchange for the Corporation's West Edson asset (Note 5). During the year ended December 31, 2015, the Corporation sold 250,000 TOU Shares for total proceeds of $8.6 million which resulted in total holdings at December 31, 2015 of 6.5 million TOU Shares. At December 31, 2015, 5.5 million shares were pledged as security for the margin loan with the remaining 1.0 million pledged as security for the TOU Share financial arrangement.

At December 31, 2015 the fair market value of the 6.5 million TOU Shares was $145.3 million based on a December 31, 2015 closing price of $22.35 per share. Net loss for the year ended December 31, 2015 includes an unrealized loss of $104.8 million representing the change in value between closing on April 1, 2015 of $38.32 per share and the period end closing price of $22.35 per share.

5. PROPERTY, PLANT AND EQUIPMENT

	Oil and Gas Properties	Corporate Assets	Total
Cost			
December 31, 2013	$ 2,560,503	$ 6,407	$ 2,566,910
Additions	111,823	614	112,437
Non-monetary additions	9,362	–	9,362
Change in decommissioning obligations (note 13)	11,476	–	11,476
Transfers from exploration and evaluation (note 6)	5,495	–	5,495
Acquisitions	826	–	826
Dispositions	(65,585)	–	(65,585)
December 31, 2014	2,633,900	7,021	2,640,921
Additions	69,086	69	69,155
Non-monetary additions	3,700	–	3,700
Change in decommissioning obligations (note 13)	(58,313)	–	(58,313)
Transfers from exploration and evaluation (note 6)	692	–	692
Acquisitions	3	–	3
Dispositions	(218,500)	–	(218,500)
December 31, 2015	**2,430,568**	**7,090**	**2,437,658**
Accumulated depletion, depreciation and impairment losses			
December 31, 2013	$ (1,983,978)	$ (5,978)	$ (1,989,956)
Depletion and depreciation	(94,391)	(345)	(94,736)
Dispositions	27,127	–	27,127
Impairment	(26,400)	–	(26,400)
Impairment reversal	5,000	–	5,000
December 31, 2014	(2,072,642)	(6,323)	(2,078,965)
Depletion and depreciation	(87,898)	(466)	(88,364)
Dispositions	105,096	–	105,096
Impairment	(27,522)	–	(27,522)
December 31, 2015	**(2,082,966)**	**(6,789)**	**(2,089,755)**
Carrying amount			
December 31, 2014	$ 561,258	$ 698	$ 561,956
December 31, 2015	**347,602**	**301**	**347,903**

At December 31, 2015, property, plant and equipment included $6.1 million (December 31, 2014 – $35.0 million) of costs currently not subject to depletion and nil (December 31, 2014 – $19.6 million) related to shut-in gas over bitumen reserves which are not being depleted due to the non-producing status of the wells in the affected properties.

During the year ended December 31, 2015, the Corporation disposed of oil and natural gas properties for net proceeds of $24.0 million (2014 - $71.3 million).

On April 1, 2015, the Corporation closed an arrangement with Tourmaline Oil Corp. ("Tourmaline") to swap its joint interest share in its West Edson assets in West Central Alberta in exchange for 6.75 million TOU Shares. Non-monetary gross proceeds of $258.7 million were calculated based on the market value of the TOU Shares determined using the April 1, 2015 closing price on the Toronto Stock Exchange ("TSX"). Gains on dispositions totaling $146.6 million (2014 - $42.9 million) were recorded in net income.

The Corporation undertook additional property transactions throughout the year including the disposition of certain fee simple lands in east central Alberta, along with a working interest in related seismic data, for net proceeds of $21.0 million. The Corporation also disposed of its interest in certain non-core undeveloped lands for proceeds of $1.2 million and executed an asset swap to acquire an increased interest in existing reserves as well as undeveloped acreage in its core East Edson property in exchange for its working interest in certain undeveloped lands and net proceeds of $1.8 million.

In July 2014, the Corporation closed an arrangement with a partner which resulted in the disposition of a portion of lands in the East Edson area of the Corporation's West Central CGU. Net proceeds consisted of $17.0 million of unrestricted cash and $30 million held in escrow to be used to drill, complete and tie-in approximately five wells in the East Edson property prior to December 31, 2015. As at December 31, 2015, the amount held in Perpetual's escrow account was nil (2014 - $6.6 million) and the drilling commitment had been satisfied. The Corporation also recognized $9.4 million in deemed proceeds related to the partner's $70 million farm-in investment which was committed to the drilling, completion and tie-in of approximately 14 wells pursuant to a farm-in agreement. The net book value of assets disposed included $21.7 million property, plant, and equipment and $1.2 million of exploration and evaluation assets.

In conjunction with the arrangement, the Corporation has additional capital commitments totaling $60 million following spending of the $70 million farm-in investment by the partner. This includes $30 million for the construction of a new gas plant which was completed and operational during the third quarter of 2015 and $30 million to drill, complete and tie-in approximately six more wells prior to December 31, 2022. As at December 31, 2015, the Corporation had total capital commitments of $18.5 million remaining pursuant to the arrangement.

Impairments and reversals

For the year ended December 31, 2015, Perpetual conducted an assessment of impairment indicators for the Corporation's CGUs. In performing the review management determined that the recent decline in commodity pricing and the impact these price declines have on the economic performance of the Corporation's CGUs justified calculation of the recoverable amount of all CGUs. The recoverable amount of the CGUs was based on the higher of VIU and FVLCD. The impairment test was completed using estimates of VIU for each CGU.

VIU was determined based on the net present value of cash flows from the CGUs oil, natural gas, and NGL reserves using estimates of total proved plus probable reserves evaluated or reviewed by Perpetual's independent reserves evaluators along with the associated year-end commodity price forecast, and an estimate of market discount rates between 12 and 20 percent to consider risks specific to the asset. At December 31, 2015, the Corporation determined that the carrying amount of the Birchwavy East and Birchwavy West CGUs exceeded their recoverable amounts net of decommissioning obligations of $28.9 million and a net obligation of $6.3 million, respectively. Accordingly, an impairment charge of $9.0 million is included in net income for the year related to oil and natural gas assets in the Birchwavy East and West CGUs.

The independent reserves evaluator's commodity price estimates were used in the VIU calculations as at December 31, 2015:

Year	WTI Crude Oil (US$/bbl)	USD/CDN exchange rate (US$/Cdn$)	Alberta heavy crude oil (Cdn$/bbl)	AECO natural gas (Cdn$/mmbtu)
2016	45.00	0.73	40.50	2.70
2017	53.60	0.75	47.50	3.20
2018	62.40	0.80	52.10	3.55
2019	69.00	0.80	57.80	3.85
2020	73.10	0.83	59.50	3.95
2021	77.30	0.83	63.10	4.20
2022	81.60	0.83	66.70	4.45
2023	86.20	0.83	70.60	4.70
2024	87.90	0.83	72.00	4.80
2025	89.60	0.83	73.40	4.90
2026	91.40	0.83	74.90	5.00
2027	93.30	0.83	76.40	5.10
2028	95.10	0.83	77.90	5.20
2029	97.00	0.83	79.40	5.30
2030	99.00	0.83	81.10	5.40

Escalate 2.0 percent per year thereafter

Included in impairment losses for the year ended December 31, 2015 is $14.7 million related to de-recognition of the Corporation's gas over bitumen CGU. Perpetual determined that future production from the shut-in gas over bitumen wells is no longer likely in the absence of a technical solution or permitted production. Accordingly, Perpetual has de-recognized $18.5 million related to the carrying amount of property, plant and equipment offset by $3.8 million related to the gas over bitumen provision (note 13) for estimated future repayments of gas over bitumen credits received.

For the year ended December 31, 2014, the Corporation determined that the carrying amount of the Birchwavy East CGU exceeded its recoverable amount using estimates of VIU; accordingly, an impairment charge of $26.4 million is included in net income. The Corporation also determined that the recoverable amount using estimates of VIU of the Birchwavy West CGU exceeded its carrying amount by $5.0 million; accordingly, a reversal of $5.0 million was recognized in net income representing a partial reversal of previously recorded impairments. This reversal is a result of the underlying assets demonstrating sustainable operational performance since the last calculation of the recoverable amount.

6. EXPLORATION AND EVALUATION

	2015	2014
Balance, beginning of year	**$ 84,227**	$ 88,177
Additions	**7,186**	3,990
Non-monetary additions	**5,880**	6,000
Acquisitions	**240**	172
Dispositions	**(34,096)**	(6,482)
Transfers to property, plant and equipment (note 5)	**(692)**	(5,495)
Non-cash exploration and evaluation expense	**(6,338)**	(2,135)
Balance, end of year	**$ 56,407**	$ 84,227

During the year ended December 31, 2015, the Corporation disposed of $8.8 million in undeveloped lands in connection with the West Edson asset swap for 6.75 million TOU Shares (note 5) and $23.3 million in certain fee simple lands in east central Alberta, along with a working interest in related seismic data. The Corporation also disposed of $2.0 million in undeveloped lands and recognized non-monetary proceeds of $5.9 million based on the carried farm-in investment on undeveloped Duvernay lands in the Waskahigan area.

During the year ended December 31, 2015, $4.4 million (2014 – $3.8 million) in costs were charged directly to E&E expense in net income (loss).

7. EQUITY-METHOD INVESTMENT

Perpetual's equity-method investment consists of a 30 percent interest in WGS LP which operates a gas storage facility in Alberta, Canada.

For the year ended December 31, 2015, transactions between Perpetual and WGS LP totaled $1.6 million (December 31, 2014 - $1.7 million) consisting primarily of fees earned for the provision of management and operational services. No dividends were declared by WGS LP during the year (2014 - nil).

Summary financial information for the Corporation's equity-method investment in WGS LP is as follows:

As at	**December 31, 2015**	December 31, 2014
Current assets	**$ 1,292**	$ 676
Non-current assets	**114,677**	119,128
Total assets	**115,969**	119,804
Current liabilities[1]	**12,252**	13,164
Non-current liabilities	**23,302**	27,177
Total liabilities	**35,554**	40,341
Net assets	**80,415**	79,463
Corporation's share of net assets	**24,125**	23,839
Adjustments on acquisition of interest in WGS LP	**1,221**	1,284
Equity-method investment	**$ 25,346**	$ 25,123

(1) Includes current bank indebtedness of $10.9 million (December 31, 2014 – $11.4 million).

For the year ended	**December 31, 2015**	December 31, 2014
Revenue	**$ 10,251**	$ 3,827
Depreciation	**(3,440)**	(3,421)
Other expenses	**(9,881)**	(8,626)
Unrealized gain (loss) on gas storage obligation derivative	**4,023**	(2,527)
Net income (loss)	**953**	(10,747)
Share of net income (loss)	**286**	(3,224)
Amortization of fair value adjustment on acquisition of interest in WGS LP	**(63)**	–
Share of net income (loss) of equity method investment	**$ 223**	$ (3,224)

8. BANK INDEBTEDNESS

The Corporation's credit facility and margin loan is with a syndicate of Canadian chartered banks. At December 31, 2015, the total borrowing capacity was set at $62 million consisting of a margin loan of $42 million secured by the pledge of 5.5 million TOU Shares, and a revolving credit facility of $20 million which includes a $5 million demand loan and $15 million working capital facility.

Revolving Credit Facility

Advances under the credit facility are made in the form of Banker's Acceptances ("BA"), prime rate loans or letters of credit at the Corporation's option. At December 31, 2015, cash and cash equivalents are shown net of a $5.0 million BA outstanding on the revolving credit facility (December 31, 2014 – nil). The Corporation also has outstanding letters of credit in the amount of $5.4 million (December 31, 2014 – $8.8 million). Collateral for the revolving credit facility is provided by a floating-charge debenture covering all existing and acquired property of the Corporation, as well as unconditional full liability guarantees from all subsidiaries in respect of amounts borrowed under the credit facility.

The credit facility bears interest at its lenders' prime rate or BA rates, plus applicable margins and standby fees. The applicable margins range between 1.25% and 4.75% depending on the form of borrowing and changes in the Corporation's ratio of consolidated debt to income before interest, taxes, and non-cash items ("Consolidated Debt Ratio") for the most recently completed reporting period. Consolidated debt is defined as the sum of the period end balance of the credit facility, senior notes and outstanding letters of credit.

The revolving feature of the credit facility expires on October 31, 2016. The next semi-annual redetermination is set to occur on or before this date.

Margin Loan

On April 1, 2015, as part of the lender's semi-annual borrowing base review, Perpetual's lending commitment included a $75 million margin loan which was secured by the pledge of 6.75 million TOU Shares. During the remainder of 2015, the margin loan was reduced to $42 million in conjunction with a decline in the market value of 5.5 million TOU Shares pledged as security. The Corporation is required to maintain a 1 to 3 lending ratio based on the daily closing market value of 5.5 million TOU shares.

The margin loan has a maturity date of October 31, 2016. Collateral for the margin loan is provided by a securities pledge agreement relating to 5.5 million TOU Shares. The margin loan bears interest at its lenders' prime rate plus applicable margins ranging from 1.25% to 4.75% depending on changes in the Corporation's Consolidated Debt Ratio for the most recently completed reporting period.

Covenants

At December 31, 2015, the Corporation has a working capital covenant restricting the sum of borrowings under the revolving credit facility plus net working capital liabilities to a total of $40 million (excluding amounts drawn under the margin loan). Net working capital liabilities includes cash and cash equivalents, accounts receivable, prepaid expenses and deposits and accounts payable and accrued liabilities, plus an adjustment for accrued interest on Senior Notes payable from the date of the calculation up to and including expiry of the credit facility (October 31, 2016).

The Corporation also has maintenance covenants that require consolidated senior debt to trailing twelve months income before interest, taxes, depletion and depreciation and non-cash items ("TTM EBITDA") to be maintained within certain thresholds. Consolidated senior debt is defined as the sum of the Corporation's period end balance of the margin loan, credit facility and outstanding letters of credit reduced by the lesser of the mark-to-market value or the quarterly average value of 5.5 million TOU Shares pledged to the credit facility. The existing covenant limiting the consolidated senior debt to TTM EBITDA ratio remains at 3.0 to 1.0 except in the quarters ended June 30 and September 30, 2016 where the limit has been increased to 3.5 to 1.0.

The Corporation was in compliance with the lender's covenants at December 31, 2015.

9. CONVERTIBLE DEBENTURES

On August 25, 2014, the Corporation redeemed all of the outstanding 7.25% Convertible Debentures. Redemption of the total principal amount of $99.9 million and accrued interest of $0.5 million was funded from proceeds on the issuance of new senior notes (see note 12). Interest expense for 2014 includes a $0.2 million loss on redemption related to unamortized original issue discount and unamortized debt issuance costs. On December 31, 2014, the Corporation redeemed $25.0 million of the outstanding principal of the 7.00% Convertible Debentures.

On December 31, 2015, the Corporation redeemed all of the outstanding 7.00% Convertible Debentures. The Corporation elected to satisfy the total principal amount of $34.9 million through the issuance of 228.9 million common shares in accordance with the indenture agreement. The carrying amount of the 7.00% Convertible Debentures and the related equity component of convertible debentures were transferred to share capital at redemption on December 31, 2015.

All accrued and unpaid interest on the 7.00% Convertible Debentures was paid in cash on December 31, 2015.

Series	**7.25%**	**7.00%**	**Total**
Trading symbol (TSX)	**PMT.DB.D**	**PMT.DB.E**	
Carrying amount			
Balance, December 31, 2013	$ 98,108	$ 56,388	$ 154,496
Accretion	707	1,077	1,784
Amortization of debenture issue fees	339	579	918
Redemptions	(99,154)	(24,234)	(123,388)
Balance, December 31, 2014	–	33,810	33,810
Accretion	–	695	695
Amortization of debenture issue fees	–	373	373
Redemptions	–	(34,878)	(34,878)
Balance, December 31, 2015	**$ –**	**$ –**	**$ –**
Market Value			
December 31, 2014	$ –	$ 35,052	$ 35,052
December 31, 2015	**$ –**	**$ –**	**$ –**
Principal amount outstanding			
December 31, 2014	$ –	$ 34,878	$ 34,878
December 31, 2015	**$ –**	**$ –**	**$ –**

10. FINANCIAL OBLIGATION

		2015		2014
Balance, beginning of year	$	**15,390**	$	–
Additions		**–**		21,254
Payments		**(3,704)**		(2,829)
Change in fair value of financial obligation		**(1,675)**		(3,035)
Balance, end of year	$	**10,011**	$	15,390
Financial obligation – current	$	**2,604**	$	3,584
Financial obligation – non-current		**7,407**		11,806
	$	**10,011**	$	15,390

During 2014, the Corporation entered into an agreement whereby the Corporation received cash proceeds of $21.3 million in exchange for an obligation to make a monthly cash payment equivalent to a portion of the Corporation's monthly GOB Royalty Adjustment entitlements until final expiries in June 2021. Monthly payments under the arrangement are due on the 25th day following the entitlement month.

At the inception of the arrangement, the estimated future payments were determined using the same formula as the Corporation's monthly GOB Royalty Adjustment entitlements under the Alberta Natural Gas Royalty Regulation based on a January 1, 2014 forecast for the Alberta gas reference price ("base cash payment"). In the event that the actual Alberta gas reference price for a month causes the actual monthly cash payment under the arrangement to differ from the base cash payment, the Corporation is required to (a) pay 65 percent of any increase from the base cash payment, or (b) deduct 100 percent of any decrease from the base cash payment. Security for the financial obligation is provided by an interest in certain lands of the Corporation and by the Corporation's entitlement to future GOB Royalty Adjustments.

This financial obligation is a hybrid financial instrument comprising of a debt host with an embedded derivative related to indexation of the future cash payments to changes in the future Alberta gas reference price. The Corporation has designated the financial obligation as a financial liability which is measured at fair value through profit and loss. For the year ended December 31, 2015, an unrealized gain of $1.7 million (December 31, 2014 - $3.0 million) is included in finance expense related to the change in fair value of the financial obligation. See note 19 for a description of the valuation methodology used to estimate the fair value of the financial obligation.

As at December 31, 2015, if future natural gas prices changed by $0.25 per GJ with all other variables held constant, the fair value of the financial obligation and after tax net loss for the period would change by $1.2 million (December 31, 2014 - $1.3 million). Fair value sensitivity is based on published forward AECO prices.

11. TOU SHARE FINANCIAL ARRANGEMENT

In November 2015, the Corporation executed a new financial arrangement that provided $18.2 million of proceeds, net of an amount paid to enhance the collateral value of 1.0 million TOU Shares pledged as security for the arrangement. The arrangement matures on November 16, 2016 and can be repaid in cash or with the transfer of the TOU Shares pledged as security. The repayment amount changes in response to changes in the market price of TOU Shares pledged as security, subject to a maximum payment of $21.3 million at maturity.

The TOU Share financial arrangement is a hybrid financial instrument comprising of a debt host with an embedded derivative related to indexation of the future settlement amount to changes in the market price of TOU Shares pledged as security. The Corporation has designated the TOU Share financial arrangement as a financial liability which is measured at fair value through profit and loss. For the year ended December 31, 2015, an unrealized gain of $0.2 million (December 31, 2014 – nil) is included in finance expense, representing the change in fair value of the TOU Share financial arrangement between inception and year end.

As at December 31, 2015, the carrying amount of the 1.0 million TOU Shares pledged as security was $22.4 million based on a December 31, 2015 closing price of $22.35 per share.

12. SENIOR NOTES

				Carrying amount	
	Maturity date	**Principal**	**Interest rate**	**December 31, 2015**	December 31, 2014
2011 senior notes(1)	March 15, 2018	150,000	8.75%	**148,724**	148,223
2014 senior notes(2)	July 23, 2019	125,000	8.75%	**122,934**	122,467
		275,000		**271,658**	270,690

(1) Issued March 15, 2011, interest payable semi-annually on September 15 and March 15 of each year.
(2) Issued July 23, 2014, interest payable semi-annually on January 23 and July 23 of each year.

The senior notes are direct senior unsecured obligations of Perpetual, ranking pari passu with all other present and future unsecured and unsubordinated indebtedness of the Corporation. The Corporation can redeem up to 35 percent of the principal amount of the senior notes at a premium to face value with proceeds from common share offerings up to three years prior to maturity. Within three years of maturity the Corporation can repay the senior notes at a premium to face value based on the date of repayment.

The senior notes have a cross-default provision with the Corporation's credit facility (note 8) which has a working capital covenant restricting the sum of borrowings under the revolving credit facility plus net working capital liabilities to a total of $40 million (excluding amounts drawn under the margin loan). Net working capital liabilities include accounts receivable, prepaid expenses and deposits and accounts payable and accrued liabilities.

The Corporation also has maintenance covenants that require consolidated senior debt to TTM EBITDA to be maintained within certain thresholds. Consolidated senior debt is defined as the sum of the Corporation's period end balance of the margin loan, credit facility and outstanding letters of credit reduced by the lesser of the mark to market value of the TOU Shares or the TOU Share quarterly average value. The existing covenant limiting the consolidated senior debt to TTM EBITDA ratio remains at 3.0 to 1.0 except in the quarters ended June 30 and September 30, 2016 where the limit has been increased to 3.5 to 1.0.

The senior notes indenture also 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 Corporation's Consolidated Debt Ratio is less than 3.0 to 1.0, the sum of 50 percent of income before interest, taxes, depletion and depreciation and non-cash items 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 Corporation during that period less the sum of all restricted payments during that period; and

ii) To the extent the Corporation'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 Corporation.

The Corporation was in compliance with the lender's covenants at December 31, 2015 and estimates that it will be in compliance with all covenants through to the maturity of the credit facility at current commodity prices.

At December 31, 2015 the senior notes are presented net of $3.3 million (December 31, 2014 - $4.3 million) in issue costs which are amortized using a weighted average effective interest rate of 9.2 percent.

13. PROVISIONS

	2015	2014
Decommissioning obligations, beginning of year	**$ 222,976**	$ 213,906
Obligations acquired	**–**	85
Obligations incurred	**1,442**	3,067
Obligations disposed	**(1,939)**	(1,173)
Change in risk free rate	**617**	14,343
Change in estimates	**(60,372)**	(6,019)
Obligations settled	**(7,589)**	(6,633)
Accretion (note 17)	**4,034**	5,400
Decommissioning obligations, end of year	**159,169**	222,976
Gas over bitumen provision	**–**	3,324
Balance, end of year	**$ 159,169**	$ 226,300
Provisions – current	**1,981**	5,372
Provisions – non-current	**157,188**	220,928
	$ 159,169	$ 226,300

a) Decommissioning obligations

Total future decommissioning obligations are estimated based on the Corporation's net ownership interest in all wells and facilities, estimated costs to reclaim and abandon these wells and facilities and the estimated timing of the costs to be incurred in future periods.

The Corporation adjusts the decommissioning obligations on each period end date for changes in the risk free rate. Accretion is calculated on the adjusted balance after taking into account additions and dispositions to property, plant, and equipment. Decommissioning obligations are also adjusted annually for revisions to future costs and the estimated timing of costs to be incurred in future years.

During the quarter ended December 31, 2015, the Corporation achieved efficiencies and cost savings by utilizing internal labor and equipment rather than third party services for various stages of reclamation and abandonment. This resulted in a revision to estimated future abandonment liabilities for all oil and natural gas assets.

At December 31, 2015, the Corporation estimated the net present value of its total decommissioning obligations to be $159.2 million (December 31, 2014 – $223.0 million) based on an undiscounted total future liability of $179.3 (December 31, 2014 – $239.2 million). These payments are expected to be made over the next 25 years with the majority of costs incurred between 2025 and 2035. At December 31, 2015, the Corporation used a weighted average risk free rate of 1.89 percent (December 31, 2014 – 1.98 percent) to calculate the present value of the decommissioning obligation.

b) Gas over bitumen provision

The gas over bitumen provision represents the present value of expected repayments to the Crown for the gas over bitumen royalty adjustments received or receivable by the Corporation under the Natural Gas Royalty Regulation (2004) in the event the shut-in gas over bitumen assets resume production. The cash flows are based on the estimated timing of future revenues and the related overriding royalties that will be incurred in future periods.

At December 31, 2015, the Corporation determined that future production from the shut-in gas over bitumen wells is no longer likely in the absence of a technical solution or permitted production. Accordingly, Perpetual has de-recognized $18.5 million related to the carrying amount of property, plant and equipment offset by $3.8 million related to the gas over bitumen provision (note 5). A net amount of $14.7 million has been included in impairment losses for the year ended December 31, 2015.

For the year ended December 31, 2015, the Corporation recognized accretion of $0.5 million (2014 – $0.4 million) prior to de-recognizing the gas over bitumen provision at December 31, 2015. Accretion was based on a liability specific discount rate of 15.0 percent (December 31, 2014 – 15.0 percent).

14. SHARE CAPITAL

a) Authorized

Authorized capital consists of an unlimited number of common shares.

b) Per share information

	Year ended December 31, **2015**	2014
(thousands, except per share amounts)		
Net income (loss) – basic	**$ (89,274)**	$ 3,366
Effect of dilutive securities	**–**	–
Net income (loss) – diluted	**$ (89,274)**	$ 3,366
Weighted average shares		
Issued common shares	**151,954**	149,371
Effect of shares held in trust	**(1,814)**	(287)
Weighted average common shares outstanding – basic	**150,140**	149,084
Effect of dilutive securities	**–**	7,521
Weighted average common shares outstanding – diluted	**150,140**	156,605
Income (loss) per share - basic and diluted	**$ (0.59)**	$ 0.02

In computing per share amounts for the year ended December 31, 2015, 1.6 million potentially issuable common shares through the share based compensation plans (2014 – 0.8 million) were excluded because they were anti-dilutive.

c) Redemption of convertible debentures

On December 31, 2015, the Corporation redeemed all of the outstanding 7.00% Convertible Debentures. The Corporation elected to satisfy the total principal amount of $34.9 million through the issuance of 228.9 million common shares in accordance with the indenture agreement.

d) Rights

On December 7, 2015, the Corporation filed a short form prospectus with the security regulatory authorities in connection with a fully backstopped rights offering to issue common shares of Perpetual for gross proceeds of $25 million.

Pursuant to the rights offering, each registered holder of common shares as of December 16, 2015 received one right (a "Right") for each common share held. Each Right entitled the holder to acquire 4.3386 common shares upon payment of the exercise price of $0.1630 per Right. The number of common shares received for each right was calculated following the close of trading of the common shares on the Toronto Stock Exchange ("TSX") on December 22, 2015 based upon the volume weighted average price of the common shares for the preceding 20 consecutive trading days, being November 25, 2015 through to and including December 22, 2015.

For the year ended December 31, 2015, the Corporation recorded a gain of $7.5 million included in non-cash finance expense (note 17) related to the change in the carrying amount of the Rights derivative between filing of the prospectus on December 7, 2015 and determination of the number of common shares to be issued for each Right on December 22, 2015.

Upon closing of the Rights Offering on January 18, 2016, Perpetual issued an aggregate of 665.4 million Common Shares of the Company including 427.4 million issued to entities controlled by the Chairman of Perpetual's Board of Directors for proceeds of $16.1 million.

15. SHARES HELD IN TRUST

	December 31, 2015 Shares *(thousands)*	December 31, 2015 Amount *($thousands)*	December 31, 2014 Shares *(thousands)*	December 31, 2014 Amount *($thousands)*
Balance, beginning of year	**978**	**$ 1,387**	–	$ –
Shares purchased and held in trust	**1,030**	**1,109**	989	1,406
Disbursements to employees	**(1,061)**	**(1,319)**	(11)	(19)
Balance, end of year	**947**	**$ 1,177**	978	$ 1,387

The Corporation has compensation agreements in place with employees whereby they may be entitled to receive shares of the Corporation purchased on the open market by a trustee. The balance of shares held in trust represents the cumulative cost of shares held by the trustee for the benefit of employees that have not yet been issued to employees.

16. SHARE BASED PAYMENTS

a) Share Option Plan

The purpose of the Share Option Plan is to provide an effective long-term incentive to eligible participants and to reward them on the basis of the Corporation's long-term performance. The Board of Directors administers the Share Option Plan and determines participants, number of Share Options and terms of vesting. The exercise price of the Share Options granted shall not be less than the value of the weighted average trading price for Perpetual's common shares for the five trading days immediately preceding the date of grant. At December 31, 2015, the Corporation had 14.9 million (2014 – 15.0 million) shares reserved for issuance under the Share Option and Restricted Right Plan.

Participants in the Share Option Plan may offer to surrender their options to the Corporation in exchange for a cash payment not to exceed the in-the-money value of the Share Options. The Corporation has the right to accept or refuse such offers. For the year ended December 31, 2015, the Corporation recorded $1.2 million in share based compensation expense related to Share Options (2014 – $1.3 million), with no cash payments made in 2015 (2014 – nil).

The Corporation used the trinomial option pricing model to calculate the estimated fair value of the outstanding Share Options. The following assumptions were used to arrive at the estimate of fair value as at the date of grant:

	2015	2014
Dividend yield (%)	**0.0**	0.0
Forfeiture rate (%)	**20.6**	15.1
Expected volatility (%)	**49.8**	53.1
Risk-free interest rate (%)	**0.4**	1.3
Expected life (years)	**3.2**	2.5 – 3.5
Vesting period (years)	**4.0**	3.0
Contractual life (years)	**5.0**	4.0
Weighted average grant date fair value	**$ 0.18**	$ 0.72

The following tables summarize information about Share Options outstanding at December 31, 2015:

	2015 Average Exercise Price ($/share)	**2015 Share Options (thousands)**	2014 Average Exercise Price ($/share)	2014 Share Options (thousands)
Balance, beginning of year	**1.33**	**12,819**	$ 1.20	11,201
Granted	**0.69**	**2,150**	2.06	2,200
Exercised	**0.62**	**(65)**	0.81	(343)
Cancelled/forfeited	**1.23**	**(50)**	1.19	(133)
Expired	**3.59**	**(60)**	4.23	(106)
Balance, end of year	**1.23**	**14,794**	$ 1.33	12,819

Range of Exercise Prices	**Options Outstanding: Number of Share Options (thousands)**	**Options Outstanding: Average Contractual Life (years)**	**Options Outstanding: Weighted Average Exercise Price ($/share)**	**Options Exercisable: Number of Share Options (thousands)**	**Options Exercisable: Weighted Average Exercise Price ($/share)**
$0.62 to $0.86	3,099	3.31	$ 0.67	936	$ 0.62
$0.87 to $1.07	4,968	0.56	1.03	4,954	1.03
$1.08 to $1.15	2,445	1.64	1.11	1,630	1.11
$1.16 to $1.66	1,399	0.48	1.25	1,379	1.26
$1.67 to $3.18	2,882	2.15	2.28	1,412	2.51
Total	**14,793**	**1.62**	**$ 1.23**	**10,311**	**$ 1.24**

b) Restricted Rights Plan

The Corporation has a Restricted Rights Plan for certain officers, employees and direct and indirect service providers. Restricted Rights granted under the Restricted Rights Plan may be exercised during a period (the "Exercise Period") not exceeding five years from the date upon which the Restricted Rights were granted. The Restricted Rights typically vest on a graded basis over two years. At the expiration of the Exercise Period, any Restricted Rights which have not been exercised shall expire and become null and void. Upon vesting, the plan participant is entitled to receive the vested common shares at no cost.

For the year ended December 31, 2015, share based compensation expense in respect of Restricted Rights outstanding was nil (2014 – $0.1 million).

The following table shows changes in the Restricted Rights outstanding under the Restricted Rights Plan:

	2015	2014
(thousands)		
Balance, beginning of year	**618**	1,311
Granted	**2,727**	740
Exercised	**(3,280)**	(1,369)
Forfeited	**(25)**	(64)
Balance, end of year	**40**	618

c) Performance Share Rights Plan

The Corporation has a Performance Share Rights Plan for the Corporation's senior management team. Performance Share Rights granted under the Performance Share Rights Plan vest two years after the date upon which the Performance Share Rights were granted. The Performance Share Rights that vest and become redeemable are a multiple of the Performance Share Rights granted dependent upon the achievement of certain performance metrics over the vesting period. Vested Performance Share Rights can be settled in cash or Restricted Rights, at the discretion of the Board of Directors. Should participants of the Performance Share Rights Plan leave the organization other than through retirement or termination without cause prior to the vesting date, the Performance Share Rights would be forfeited.

At December 31, 2015, the Corporation had 2.3 million Performance Share Rights issued and outstanding under the Performance Share Rights Plan (December 31, 2014 – 2.3 million).

For the year ended December 31, 2015, share based compensation expense in respect of the Performance Share Rights outstanding was nil (2014 – $2.6 million) as a result of performance multiplier adjustments related to performance share units issued and outstanding.

d) Compensation awards

The Corporation has agreements in place with certain employees whereby over a period of three years they may be entitled to receive shares of the Corporation purchased on the open market by an independent trustee if they remain employees of Perpetual during such time. This does not dilute equity or involve the issuance of shares from treasury. The shares purchased by the Trustee are reported as shares held in trust (note 15).

At December 31, 2015, the Corporation had 4.0 million of these awards issued and outstanding (2014 – 2.5 million).

For the year ended December 31, 2015, $0.6 million in share based compensation expense was recorded in respect of the awards (2014 – $0.4 million).

The Corporation also has agreements in place with directors and certain employees whereby, in the case of directors, upon retirement from the board of directors, or in the case of employees, over a period of two years if they remain employees of Perpetual during such time, may be entitled to receive at the discretion of the Board, cash, a grant of restricted rights or shares of the Corporation purchased on the open market by an independent trustee.

At December 31, 2015, the Corporation had 3.5 million of these awards issued and outstanding (2014 – 2.8 million).

For the year ended December 31, 2015, $2.1 million in share based compensation expense was recorded in respect of the compensation awards granted (2014 – $1.6 million).

17. FINANCE EXPENSE

The components of finance expense are as follows:

	Year ended December 31, 2015	2014
Cash interest		
Interest on senior notes	**24,062**	17,670
Interest on convertible debentures	**2,441**	8,912
Interest on bank indebtedness	**4,143**	3,373
Total cash interest	**30,646**	29,955
Non-cash finance expense		
Amortization of debt issue costs	**2,036**	4,896
Accretion on decommissioning obligations (note 13)	**4,034**	5,400
Accretion on gas over bitumen provision (note 13)	**498**	442
Change in estimate on gas over bitumen provision (note 13)	**–**	(66)
Change in carrying amount of Rights derivative (note 14)	**(7,478)**	–
Change in fair value of financial obligation (note 10)	**(1,675)**	(3,035)
Change in fair value of TOU Share financial arrangement (note 11)	**(171)**	–
Finance expenses recognized in net income (loss)	**27,890**	37,592

18. NON-CASH WORKING CAPITAL INFORMATION

	Year ended December 31, 2015	2014
Restricted cash	**$ 6,552**	$ (6,552)
Accounts receivable	**30,765**	(14,198)
Prepaid expenses and deposits	**(1,506)**	(266)
Accounts payable and accrued liabilities	**(53,227)**	46,800
Change in non-cash working capital	**$ 17,416**	$ 25,784

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

	Year ended December 31, 2015	2014
Operating	**$ 15,813**	$ (5,862)
Financing	–	1,527
Investing	**(33,229)**	30,119
Change in non-cash working capital	**$ 17,416**	$ 25,784

19. FINANCIAL RISK MANAGEMENT

The Corporation has exposure to credit risk, liquidity risk and market risk from its use of financial instruments.

This note presents information about the Corporation's exposure to each of the above risks, the Corporation's objectives, policies and processes for measuring and managing risk, and the Corporation's management of capital. Further quantitative disclosures are included throughout these annual consolidated financial statements.

The Board of Directors has overall responsibility for the establishment and oversight of the Corporation's risk management framework. The Board of Directors has implemented and monitors compliance with risk management policies.

The Corporation's risk management policies are established to identify and analyze the risks faced by Perpetual, to set appropriate risk limits and controls, and to monitor risks and adherence to market conditions and the Corporation's activities.

a) Credit risk

Credit risk is the risk of financial loss to the Corporation if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Corporation's receivables from joint venture partners, oil and natural gas marketers and derivative contract counterparties.

Receivables from oil and natural gas marketers are normally collected on the 25th day of the month following production. The Corporation's policy to mitigate credit risk associated with these balances is to establish marketing relationships with large, well established purchasers. The Corporation historically has not experienced any significant collection issues with its oil and natural gas marketing receivables. Joint venture receivables are typically collected within one to three months of the joint venture bill being issued to the partner. The Corporation attempts to mitigate the risk from joint venture receivables by obtaining partner approval of significant capital expenditures prior to expenditure. However, the receivables are generally from participants in the oil and natural gas sector, and collection of the outstanding balances is dependent on industry factors such as commodity price fluctuations, escalating costs, the risk of unsuccessful drilling and oil and gas production; in addition, further risk exists with joint venture partners as disagreements occasionally arise that increase the potential for non-collection. The Corporation does not typically obtain collateral from oil and natural gas marketers or joint venture partners, however, the Corporation does have the ability in some cases to withhold production or amounts payable to joint venture partners in the event of non-payment.

The Corporation manages the credit exposure related to derivatives by engaging in risk management transactions with counterparties with investment grade credit ratings, and periodically monitoring the changes in such credit ratings.

During the year ended December 31, 2015, credit risk did not have any impact on the change in fair value of financial assets and liabilities classified as fair value through profit or loss.

The carrying amount of cash and cash equivalents, accounts receivable and fair value of derivative assets represents the Corporation's maximum credit exposure. The Corporation's allowance for doubtful accounts as at December 31, 2015 is $0.6 million (December 31, 2014 – $0.7 million). The amount of the allowance was determined by assessing the probability of collection for each past due receivable. The Corporation is currently involved in negotiations with the joint venture partners involved to recover the full amount of the receivables in question. The total amount of accounts receivables 90 days past due amounted to $0.9 million as at December 31, 2014 (December 31, 2014 – $1.3 million).

b) Liquidity risk

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

The Corporation anticipates that cash flows including cash flow from operating activities, proceeds from closed and potential future asset dispositions and available funds from the Corporation's credit facility will provide the required funds to discharge the Corporation's obligations, carry out exploration and development programs and fund ongoing operations for the foreseeable future.

The following are the contractual maturities of financial liabilities and associated interest payments as at December 31, 2015:

Contractual repayments of financial liabilities	**Total**	**2016**	**2017**	**2018-2020**	**Thereafter**
Accounts payable and accrued liabilities	**$ 38,621**	$ 38,621	$ –	$ –	$ –
Derivatives	**16,748**	9,353	7,395	–	–
Bank indebtedness	**42,000**	42,000	–	–	–
Senior notes – principal	**275,000**	–	–	275,000	–
Financial obligation	**10,011**	2,604	2,460	4,542	405
TOU Share financial arrangement	**18,059**	18,059	–	–	–
Total	**$ 400,439**	$ 110,637	$ 9,855	$ 279,542	$ 405

c) Market risk

Market risk is the risk that changes in market prices such as foreign exchange rates, equity prices, commodity prices and interest rates will affect the Corporation's net income or the value of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable limits, while maximizing returns.

The Corporation utilizes both financial derivatives and fixed-price physical delivery sales contracts to manage market risks related to commodity prices and foreign currency rates. All such transactions are conducted in accordance with the Corporation's Risk Management Policy, which has been approved by the Board of Directors.

i) Foreign currency exchange rate risk

Foreign currency exchange rate risk is the risk that the fair value or future cash flows of the Corporation will fluctuate as a result of changes in foreign exchange rates. The majority of the Corporation's oil and natural gas sales are denominated in Canadian dollars. Due to the fact that the demand for oil and natural gas is substantially driven by the demand in the United States, the Corporation's exposure to US dollar foreign exchange risk is indirectly driven by the price of oil and natural gas. From time to time the Corporation also uses foreign exchange contracts to mitigate the effects of fluctuations in exchange rates on the Corporation's cash flows.

ii) Commodity price risk

Commodity price risk is the risk that the fair value or future cash flows will fluctuate as a result of changes in commodity prices. Commodity prices for oil and natural gas are impacted by world economic events that dictate the levels of supply and demand. The Corporation has attempted to mitigate commodity price risk through the use of various financial derivatives and fixed-price physical delivery sales contracts.

The Corporation's policies as they relate to economic risk management are as follows:

Restrictive policy	Contract type	Limit
Internal Risk Management Policy[(1)]	Financial or forward physical oil or natural gas liquids-based volumes	100 percent of the forecasted future oil and condensate production volumes after royalties for the corresponding Prompt Months[(2)] of the oil or condensate-based Price Management Transactions[(4)], and; 75 percent of the forecasted future oil and condensate production volumes after royalties for the corresponding Forward Months[(3)] of the oil or condensate-based Price Management Transactions[(4)].
Internal Risk Management Policy[(1)]	Financial or forward physical natural gas-based volumes	100 percent of the average forecasted future natural gas production volume after royalties for the corresponding Prompt Months[(2)] of the natural gas-based Price Management Transactions[(4)], and; 75 percent of the average forecasted future natural gas production volume after royalties for the corresponding Forward Months[(3)] of the natural gas-based Price Management Transactions[(4)].

(1) The internal risk management policy supports compliance with the hedging restrictions set forth under the Corporation's credit facility.
(2) "Prompt Month" means the calendar month commencing less than 40 days from the transaction date of a Price Management Transaction.
(3) "Forward Month" means a single calendar month commencing after the Prompt Month.
(4) "Price Management Transaction" means any physical or financial obligation, including a commodity swap, basis trade, differential trade, option, swaption or futures contract for a given commodity.

As at December 31, 2015, the Corporation has variable priced physical natural gas sales contracts based on future market prices. These contracts are not classified as non-financial derivatives due to the fact that the settlement price corresponds directly with fluctuations in natural gas prices.

Realized gains on commodity price derivatives recognized in net income for the year ended December 31, 2015 were $4.6 million (2014 – losses of $9.1 million). The realized gains on commodity price derivatives for the year ended December 31, 2015, included gains of $6.9 million in respect of the settlement of contracts prior to maturity (2014 – $0.4 million).

Natural gas contracts

At December 31, 2015, the Corporation had entered into financial and forward natural gas sales arrangements at AECO as follows:

Term	Perpetual sold/bought	Volumes at AECO (GJ/d)	Price ($/GJ)	Type of contract
January 2016	Bought	10,000	2.15	Financial
January 2016	Bought	5,000	2.15	Physical
January 2016	Sold	(72,749)	1.95	Financial
January 2016	Sold	(15,000)	2.19	Physical
January 2016 – December 2016	Sold	(22,500)	2.26	Financial
February 2016	Sold	(25,000)	2.18	Financial
February 2016	Sold	(20,000)	2.19	Physical
March 2016	Sold	(40,000)	2.17	Financial
March 2016	Sold	(10,000)	2.18	Physical
March 2016	Bought	17,500	2.14	Financial
April 2016 – December 2016	Sold	(10,000)	2.45	Financial

At December 31, 2015, the Corporation had entered into financial natural gas sales arrangements to fix the basis differential between the New York Mercantile Exchange ("NYMEX") and AECO trading hubs. The price at which these contracts settle is equal to the NYMEX index less a fixed basis amount.

Term	Perpetual sold/bought	Volumes at NYMEX-AECO (MMBtu/d)	Average price ($USD/MMBtu)	Type of contract
February 2016 – December 2016	Sold	(30,000)	(0.74)	Financial
April 2016 – December 2016	Sold	(5,000)	(0.65)	Financial
January 2017 – December 2017	Sold	(60,000)	(0.65)	Financial

At December 31, 2015, the Corporation had entered into financial natural gas sales arrangements at the NYMEX trading hub as follows:

Term	Perpetual sold/bought	Volumes at NYMEX (MMBtu/d)	Average price ($USD/MMBtu)	Type of contract
February 2016	Sold	(20,000)	2.27	Financial
February 2016	Bought	5,000	2.26	Financial
April 2016 – December 2016	Sold	(5,000)	2.54	Financial

Oil contracts

At December 31, 2015 the Corporation had entered into the following costless collar oil sales arrangements which settle in $USD:

Term	Volumes at WTI (bbl/d)	Floor price ($USD/bbl)	Ceiling price ($USD/bbl)	Type of contract
January 2016 – December 2016	500	45.00	52.10	Collar
January 2016 – December 2016	500	42.00	50.70	Collar
January 2017 – December 2017	250	44.50	49.55	Collar

At December 31, 2015, the Corporation had entered into financial oil sales arrangements to fix the basis differential between the West Texas Intermediate ("WTI") and Western Canadian Select ("WCS") trading hubs. The price at which this contract settles is equal to the WTI index less a fixed basis amount.

Term	Perpetual sold/bought	Volumes at WTI-WCS (bbl/d)	Differential ($USD/bbl)	Type of contract
January 2016 – December 2016	Sold	500	(13.68)	Financial

Foreign exchange contracts

At December 31, 2015, the Corporation had entered into the following U.S. dollar forward sales arrangement:

Term	Notional $USD/month	Strike rate ($CAD/$USD)	Type of contract
January 2016 – March 2018[1]	3,500,000	1.25	Financial

[1] If the average monthly exchange rate is greater than the strike rate, the Corporation pays $USD 3,500,000 multiplied by the difference between the average monthly exchange rate and the strike rate.

The following table reconciles the Corporation's change in fair value of commodity derivatives:

	Year ended December 31, **2015**	2014
Realized gain (loss) on financial oil contracts	**$ 6,651**	$ (3,884)
Realized gain (loss) on financial natural gas contracts	**5,161**	(5,107)
Realized loss on forward foreign exchange contracts	**(7,186)**	(136)
Unrealized gain (loss) on financial oil contracts	**(4,409)**	14,190
Unrealized gain on physical oil contracts	**–**	519
Unrealized gain (loss) on financial natural gas contracts	**(3,165)**	1,408
Unrealized loss on physical natural gas contracts	**(80)**	(115)
Unrealized loss on forward foreign exchange contracts	**(8,409)**	(4,056)
Change in fair value of commodity price derivatives	**$ (11,437)**	$ 2,819

Natural gas price sensitivity analysis

As at December 31, 2015, 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 loss for the period would change by $7.0 million. Fair value sensitivity is based on published forward AECO and NYMEX prices.

Oil price sensitivity analysis

As at December 31, 2015, 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 $1.1 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 $1.7 million. Fair value sensitivity is based on published forward WTI and WCS prices.

Foreign exchange rate sensitivity analysis

As at December 31, 2015, if future exchange rates changed by $0.10 $CAD/$USD with all other variables held constant, the fair value of foreign exchange derivatives and after tax net loss for the period would change by $11.8 million. Fair value sensitivity is based on published forward $CAD/$USD rates.

iii) Interest rate risk

The Corporation utilizes a credit facility which bears a floating rate of interest and as such is subject to interest rate risk. Increased future interest rates will decrease future cash flows and net income or loss, thereby potentially affecting the Corporation's capital investments. The Corporation had no interest rate swap or financial contracts in place as at or during the year ended December 31, 2015 (December 31, 2014 – nil).

The Corporation's senior notes were issued at a fixed interest rate and as such these securities are not materially impacted by market interest rate fluctuations. To ensure accounts payable and accrued liabilities are settled on a timely basis, the Corporation manages liquidity risk as previously outlined in this note, thus limiting exposure to interest rate fluctuations and other penalties potentially resulting from past due payables.

Interest rate sensitivity analysis

For the year ended December 31, 2015, if interest rates changed by one percent with all other variables held constant, the impact on interest expense and net loss would be $0.6 million.

The impact on net loss as a result of interest rate fluctuations is based on the assumption that the lender increases or decreases the fixed term BA rate consistently, based on a market interest rate change of one percent.

d) Fair value of financial assets and liabilities

Perpetual'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 Corporation 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, accounts payable and accrued liabilities approximate their carrying amounts due to their short terms to maturity. Bank debt bears interest at a floating market rate and accordingly the fair market value approximates the carrying amount.

The fair value of the financial obligation is estimated by discounting future cash payments based on the forecasted Alberta gas reference price (see note 10) 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 financial arrangement is estimated using significant unobservable inputs including discount rates and measures of future volatility. 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 (see note 11).

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

				Fair value		
As at December 31, 2015	**Gross**	**Netting[1]**	**Carrying Amount**	**Level 1**	**Level 2**	**Level 3**
Financial assets						
Fair value through profit and loss						
Marketable securities	**145,275**	**–**	**145,275**	**145,275**	**–**	**–**
Derivatives – current	**2,667**	**(348)**	**2,319**	**–**	**2,319**	**–**
Derivatives – non-current	**1,411**	**–**	**1,411**	**–**	**1,411**	**–**
Financial liabilities						
Financial liabilities at amortized cost						
Senior notes	**271,658**	**–**	**271,658**	**–**	**168,000**	**–**
Fair value through profit and loss						
Derivatives – current	**9,701**	**(348)**	**9,353**	**–**	**9,353**	**–**
Derivatives – non-current	**7,395**	**–**	**7,395**	**–**	**7,395**	**–**
Financial obligation – current	**2,604**	**–**	**2,604**	**–**	**–**	**2,604**
Financial obligation – non-current	**7,407**	**–**	**7,407**	**–**	**–**	**7,407**
TOU Share financial arrangement – current	**18,059**	**–**	**18,059**	**–**	**–**	**18,059**

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

As at December 31, 2014	Gross	Netting[1]	Carrying Amount	Fair value Level 1	Level 2	Level 3
Financial assets						
Fair value through profit and loss						
Derivatives – current	9,595	(280)	9,315	–	9,315	–
Derivatives – non-current	149	(149)	–	–	–	–
Financial liabilities						
Financial liabilities at amortized cost						
Convertible debentures	33,810	–	33,810	35,052	–	–
Senior notes	270,690	–	270,690	–	260,000	–
Fair value through profit and loss						
Derivatives – current	2,678	(280)	2,398	–	2,398	–
Derivatives – non-current	4,021	(149)	3,872	–	3,872	–
Financial obligation – current	3,584	–	3,584	–	–	3,584
Financial obligation – non-current	11,806	–	11,806	–	–	11,806

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

20. CAPITAL MANAGEMENT

The Corporation's goal is to maintain a strong capital base so as to retain investor, creditor and market confidence and to sustain the future development of the business. The Corporation manages its capital structure and makes adjustments in light of changes in economic conditions and the risk characteristics of its underlying oil and natural gas assets. The Corporation considers its capital structure to include share capital, bank indebtedness, senior notes and adjusted working capital, with value and liquidity enhanced through the current ownership of TOU Shares. In order to maintain or adjust the capital structure, the Corporation may from time to time issue shares or debt securities and adjust its capital spending to manage current and projected debt levels.

The Corporation monitors capital based on the ratio of net debt to trailing twelve months cash flow from operations. This ratio is monitored continuously by the Corporation, and the targeted range of net debt to cash flow varies based on such factors as acquisitions or dispositions, commodity prices, forecasts of future commodity prices, price management contracts, projected cash flows, dividends, capital expenditure programs and timing of such programs. As a part of the management of this ratio, the Corporation prepares annual capital expenditure budgets, which are updated as necessary depending on varying factors including current and forecast prices, successful capital deployment and general industry conditions. Capital spending budgets are approved by the Board of Directors.

21. COMMITMENTS

Perpetual has contractual agreements comprised of office lease costs and related sublease recoveries, as well as drilling commitments and long-term commitments to pay for gas transportation on certain major pipeline systems in western Canada. As of December 31, 2015, the future minimum payments under these contractual agreements consisted of:

	Drilling Commitments	Pipeline commitments	Operating lease commitments
2016	3,826	11,121	2,242
2017	1,056	6,540	2,179
2018	–	5,950	545
2019	–	4,209	–
2020	–	2,369	–
Total	**$ 4,882**	**$ 30,189**	**$ 4,966**

22. DEFERRED INCOME TAXES

The provision for income taxes in the financial statements differs from the result that would have been obtained by applying the combined federal and provincial tax rate to the Corporation's loss before income tax. This difference results from the following items:

	Year ended December 31, **2015**	2014
Net income (loss) before income tax	**$ (89,274)**	$ 3,366
Combined federal and provincial tax rate	**26.0%**	25.0%
Computed income tax expense (recovery)	**$ (23,211)**	$ 842
Increase (decrease) in income taxes resulting from:		
Non-deductible expenses	**981**	1,493
Non-taxable capital (gain) loss	**13,635**	(411)
Unrecognized tax asset	**16,653**	(2,795)
Change in tax rate	**(8,745)**	–
Other	**687**	871
Deferred income taxes	**$ –**	$ –

Income tax rates increased to 26.0 percent in 2015 (2014 – 25.0 percent) as a result of increased Alberta provincial tax rates in 2015 with no changes to federal statutory income tax rates.

The components of the Corporation's and its subsidiaries' deferred income tax liabilities are as follows:

	Year ended December 31, **2015**	2014
Property, plant and equipment	**$ 34,609**	$ 34,795
Other	**3,205**	4,036
Gas over bitumen royalty obligation	**–**	(831)
Decommissioning obligations	**(37,814)**	(38,000)
	$ –	$ –

The temporary deductible differences included in the Corporation's unrecognized deferred income tax assets are as follows:

	Year ended December 31, **2015**	2014
Non-capital losses	**$ 163,404**	$ 128,702
Capital losses	**161,625**	160,969
Decommissioning obligation	**30,985**	70,975
Financial obligations	**10,011**	15,390
Marketable securities	**104,460**	–
Other	**4,752**	7,607
	$ 475,237	$ 383,643

The tax losses expire between 2016 and 2035. The deductible temporary differences do not expire under current tax legislation. Deferred tax assets have not been recognized in respect of these temporary differences because it is not probable that future taxable profit will be available against which the Corporation can utilize the benefits. The petroleum and natural gas properties and facilities owned by the Corporation and its subsidiaries have an approximate tax basis of $276 million (December 31, 2014 – $507 million) available for future use as deductions from taxable income.

23. KEY MANAGEMENT PERSONNEL

The Corporation has defined key management personnel as executive officers and vice presidents, as well as the Board of Directors, as they have the collective authority and responsibility for planning, directing and controlling the activities of the Corporation. The following table outlines the total compensation expense for key management personnel:

	Year ended December 31, **2015**	2014
Short-term fees and other short-term benefits	**$ 2,562**	$ 3,572
Share based compensation expense	**1,128**	3,675
	$ 3,690	$ 7,247

24. SUPPLEMENTAL DISCLOSURE

The Corporation's consolidated statements of income (loss) and comprehensive income (loss) are prepared primarily by nature of expense, with the exception of employee compensation costs which are included in both production and operating and general and administrative expenses.

The following table details the amount of total employee compensation costs included in production and operating and general and administrative expenses in the consolidated statements of income (loss) and comprehensive income (loss).

	Year ended December 31,	
	2015	2014
Production and operating	**$ 8,319**	$ 8,802
General and administrative	**20,343**	26,423
	$ 28,662	$ 35,225

During the year ended December 31, 2015, total employee compensation costs included share based compensation expense of $3.8 million (2014 – $6.0 million) with the remainder being short-term fees and other short-term benefits.

DIRECTORS

Clayton H. Riddell
Executive Chairman

Susan L. Riddell Rose
President, Chief Executive Officer and Director(4)

Karen A. Genoway
Independent Director(2)(3)

Randall E. (Randy) Johnson
Independent Director(1)(3)

Robert A. Maitland
Independent Director(1)(3)

Geoffrey C. Merritt
Independent Director(1)(2)(4)

Donald J. Nelson
Independent Director(2)(4)

Howard R. Ward
Independent Director(3)(4)

(1) Member of Audit Committee
(2) Member of Reserves Committee
(3) Member of Compensation and Corporate Governance Committee
(4) Member of Environmental, Health & Safety Committee

OFFICERS

Susan L. Riddell Rose
President, Chief Executive Officer and Director

Cameron R. Sebastian
Vice President, Finance and Chief Financial Officer

Vicki L. Benoit
Vice President, Production Operations

Jeffrey R. Green
Vice President, Corporate and Engineering Services

Gary C. Jackson
Vice President, Land, Acquisitions and Divestitures

Linda L. McKean
Vice President, Exploitation

Marcello M. Rapini
Vice President, Marketing

HEAD OFFICE

3200, 605 – 5 Avenue SW
Calgary, Alberta Canada T2P 3H5

403.269.4400 PHONE
800.811.5522 TOLL FREE
403.269.4444 FAXinfo@perpetualenergyinc.com EMAIL
www.perpetualenergyinc.com WEB

STOCK EXCHANGE LISTING | TSX **|** PMT

CONVERTIBLE DEBENTURES | PMT.DB.E

AUDITORS

KPMG LLP

BANKERS

Bank of Montreal
Canadian Imperial Bank of Commerce
The Bank of Nova Scotia
National Bank of Canada
ATB Financial

RESERVE EVALUATION CONSULTANTS

McDaniel & Associates Consultants Ltd.

REGISTRAR AND TRANSFER AGENT

Computershare Trust Company of Canada

Forward-Looking Information

Certain information regarding Perpetual in this report including management's assessment of future plans and operations may constitute forward-looking information or statements under applicable securities laws. The forward looking information includes, without limitation, statements made under the heading "2016 Outlook"; anticipated amounts and allocation of capital spending; statements pertaining to funds flow levels, self-funding, future development and capital efficiencies; statements regarding estimated production and timing thereof; prospective drilling locations, forecast average production; completions and development activities; infrastructure expansion and construction; anticipated effect of commodity prices on reserves; estimates of gross recoverable gas sales; estimated net asset value as at December 31, 2015 and on a pro forma basis; prospective oil and natural gas liquids production capability; projected realized natural gas prices and funds flow; estimated asset retirement obligations; anticipated effect of commodity prices on future development capital and reserves; commodity prices and foreign exchange rates; and gas price management. Various assumptions were used in drawing the conclusions or making the forecasts and projections contained in the forward-looking information contained in this press release, which assumptions are based on management's analysis of historical trends, experience, current conditions and expected future developments pertaining to Perpetual and the industry in which it operates as well as certain assumptions regarding the matters outlined above. Forward-looking information is based on current expectations, estimates and projections that involve a number of risks, which could cause actual results to vary and in some instances to differ materially from those anticipated by Perpetual and described in the forward-looking information contained in this press release. Undue reliance should not be placed on forward-looking information, which is not a guarantee of performance and is subject to a number of risks or uncertainties, including without limitation those described under "Risk Factors" in Perpetual's MD&A for the year-ended December 31, 2015 and those included in other reports on file with Canadian securities regulatory authorities which may be accessed through the SEDAR website (www.sedar.com) and at Perpetual's website (www.perpetualenergyinc.com). Readers are cautioned that the foregoing list of risk factors is not exhaustive. Forward-looking information is based on the estimates and opinions of Perpetual's management at the time the information is released and Perpetual disclaims any intent or obligation to update publicly any such forward-looking information, whether as a result of new information, future events or otherwise, other than as expressly required by applicable securities law. For more information, please refer to "Forward-Looking Information" on page 8 of this report.

Uncertainties in Estimating Reserves

There are numerous uncertainties inherent in estimating quantities of crude oil, natural gas and NGL reserves and the future funds flows attributed to such reserves. The reserve and associated funds flow information set forth above are estimates only. In general, estimates of economically recoverable crude oil, natural gas and NGL reserves and the future net funds flows therefrom are based upon a number of variable factors and assumptions, such as historical production from the properties, production rates, ultimate reserve recovery, timing and amount of capital expenditures, marketability of oil and natural gas, royalty rates, the assumed effects of regulation by governmental agencies and future operating costs, all of which may vary materially. For those reasons, estimates of the economically recoverable crude oil, NGL and natural gas reserves attributable to any particular group of properties, classification of such reserves based on risk of recovery and estimates of future net revenues associated with reserves prepared by different engineers, or by the same engineers at different times, may vary. The Company's actual production, revenues, taxes and development and operating expenditures with respect to its reserves will vary from estimates thereof and such variations could be material.

PERPETUAL
ENERGY

STOCK EXCHANGE LISTING | TSX | **PMT**

www.perpetualenergyinc.com

3200, 605 – 5 Avenue SW
Calgary, Alberta CANADA T2P 3H5

800.811.5522 TOLL FREE
403.269.4400 PHONE
info@perpetualenergyinc.com EMAIL