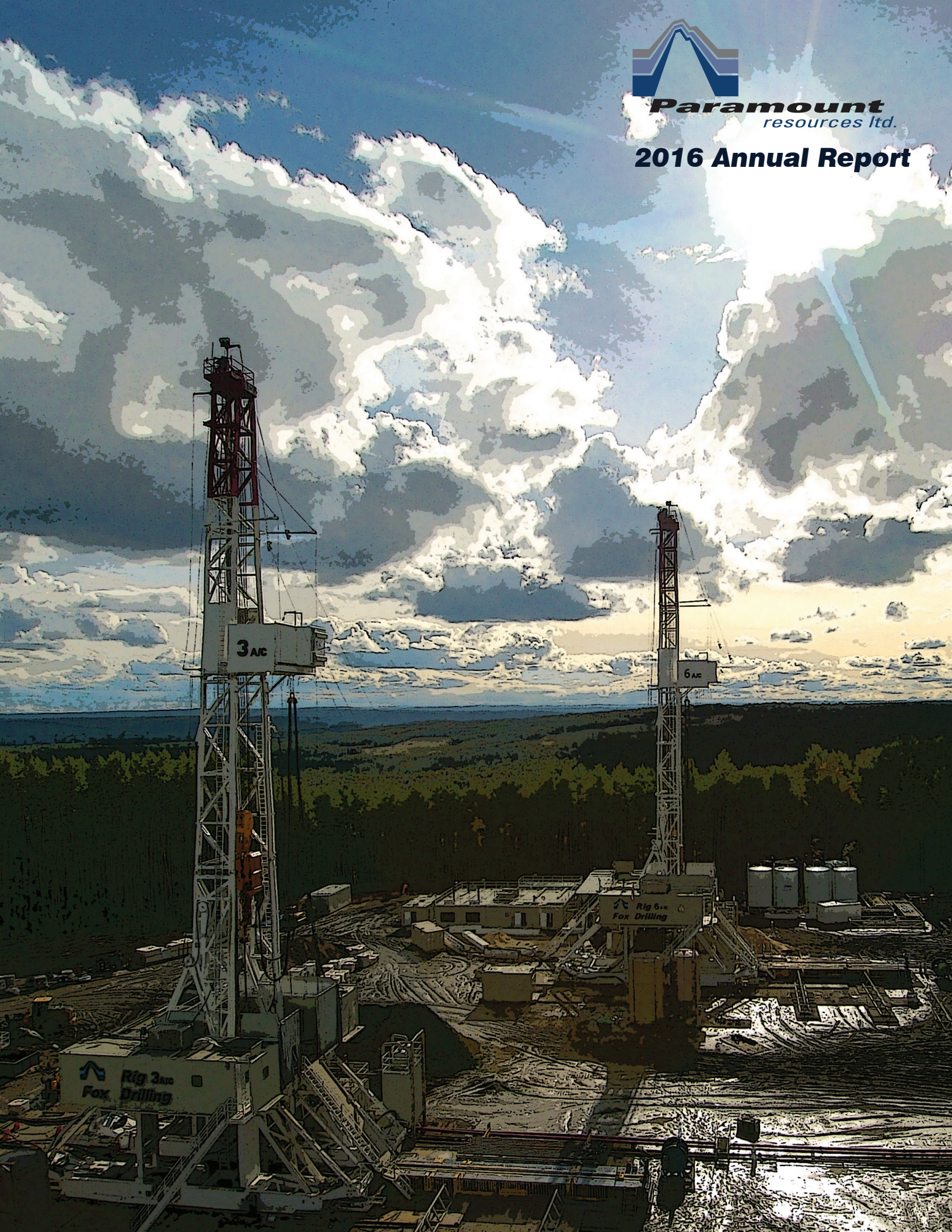


Paramount
resources Ltd.

2016 Annual Report





2016 Highlights	1
President & Chief Executive Officer's Message	3
2016 Overview	6
Review of Operations	8
Management's Discussion & Analysis	18
Financial Statements	49
Corporate Information	85

ANNUAL MEETING OF SHAREHOLDERS

Shareholders are cordially invited to attend the Annual Meeting of Shareholders to be held Wednesday, May 10, 2017 at 10:30 AM MDT at Centrium Place in the Conference Centre, 332 6th Avenue S.W., Calgary, Alberta.

Forward-Looking Statements and Information

This document includes forward-looking statements and information that is based on Paramount's current expectations, estimates, projections and assumptions. Actual results may differ materially from those expressed or implied by the forward-looking statements and information. Readers are referred to the forward-looking statements and other advisories contained at the end of Paramount's Management's Discussion and Analysis for the year ended December 31, 2016 contained herein which also includes supplemental advisories related to additional information included in this document.

2016 HIGHLIGHTS

FINANCIAL AND OPERATING ⁽¹⁾

(\$ millions, except as noted)

	Three months ended December 31			Twelve months ended December 31		
	2016	2015	% Change	2016	2015	% Change
Sales volumes						
Natural gas (MMcf/d)	47.5	52.5	(10)	48.6	50.8	(4)
Condensate and oil (Bbl/d)	2,943	3,359	(12)	2,688	2,807	(4)
Other NGLs (Bbl/d) ⁽²⁾	1,046	661	58	875	1,047	(16)
Ongoing Operations (Boe/d)	11,901	12,765	(7)	11,656	12,316	(5)
Musreau Assets (Boe/d)	—	32,701	(100)	20,204	31,814	(36)
Total (Boe/d)	11,901	45,466	(74)	31,860	44,130	(28)
Petroleum and natural gas sales	32.3	91.3	(65)	248.8	376.8	(34)
Netback	17.0	48.9	(65)	93.1	210.7	(56)
(\$/Boe)	15.53	11.70		7.99	13.08	
Funds flow from operations	14.3	21.0	(32)	35.7	93.2	(62)
per share – diluted (\$/share)	0.13	0.20		0.34	0.88	
Net income (loss)	212.4	(599.0)	NM	1,165.3	(901.3)	NM
per share – diluted (\$/share)	1.99	(5.64)		10.95	(8.52)	
Principal Properties Capital ⁽³⁾	78.2	64.7	21	171.0	429.9	(60)
Investments in other entities – market value ⁽⁴⁾⁽⁵⁾				208.7	130.8	60
Total assets				2,059.0	2,781.0	(26)
Net cash (debt)				565.9	(1,904.6)	NM
Common shares outstanding (thousands)				105,787	106,234	

(1) Readers are referred to the advisories concerning Non-GAAP Measures and Oil and Gas Measures and Definitions in the Advisories section of this document and to the reconciliations of such non-GAAP measures to their most directly comparable measure under GAAP in the applicable sections of this document. This table contains the following non-GAAP measures: Netback, Funds flow from operations, Principal Properties Capital, Investments in other entities – market value and Net cash (debt).

(2) Other NGLs means ethane, propane and butane.

(3) Principal Properties Capital includes capital expenditures and geological and geophysical costs related to the Company's Principal Properties, and excludes land acquisitions and capitalized interest.

(4) Based on the period-end closing prices of publicly-traded investments and the book value of the remaining investments.

(5) Excludes 3.8 million class A common shares of 7Gen classified as "Investments in Securities for Distribution" having a carrying value and market value of \$119.0 million as at December 31, 2016. These shares were distributed to Paramount's shareholders by way of dividend in January 2017.

NM Not meaningful

RESERVES ⁽¹⁾⁽²⁾⁽³⁾

	PRINCIPAL PROPERTIES ⁽⁴⁾					
	Proved			Proved plus Probable		
	2016	2015	% Change	2016	2015	% Change
Ongoing Operations						
Natural gas (Bcf)	238.0	99.6	139	463.3	165.8	179
NGLs (MBbl)	19,100	9,343	104	36,736	15,847	132
Light and Medium crude oil (MBbl)	882	741	19	1,219	1,021	19
Total Ongoing Operations (MBoe)	59,645	26,682	124	115,173	44,509	159
Musreau Assets (MBoe)	–	199,658	(100)	–	293,124	(100)
Total (MBoe)	59,645	226,340	(74)	115,173	337,633	(66)
Future Net Revenue NPV₁₀ (\$ millions)						
Ongoing Operations	424	154	175	810	265	206
Musreau Assets	–	1,454	(100)	–	2,790	(100)
Total	424	1,608	(74)	810	3,055	(73)
Principal Properties Finding and Development Costs ⁽⁵⁾		Three-Year Average		Three-Year Average		
Karr-Gold Creek (\$/Boe)	12.15	15.90		8.60	11.34	
Ongoing Operations (\$/Boe)	12.16	20.73		8.29	13.40	

(1) Readers are referred to the advisories concerning Oil and Gas Measures and Definitions in the Advisories section of this document.

(2) Reserves evaluated and reviewed, as applicable, by the Company's independent reserves evaluator, McDaniel & Associates Consultants Ltd. ("McDaniel") as of December 31, 2016 in accordance with National Instrument 51-101 definitions, standards and procedures. Amounts are working interest reserves before royalty deductions. Net present values of future net revenue were determined using forecast prices and costs and do not represent fair market value.

(3) Ongoing Operations excludes amounts attributable to the Musreau Assets. The estimates of reserves and future net revenue for individual properties may not reflect the same confidence level as estimates of reserves and future net revenue for all properties, due to the effects of aggregation.

(4) Excludes 93.5 MMBbl of probable bitumen reserves related to Hoole Grand Rapids Phase 1.

(5) Refer to the Principal Properties – Reserves and Finding and Development Costs section of this document.

PRESIDENT AND CHIEF EXECUTIVE OFFICER'S MESSAGE



To our Shareholders,

Over the past year, Paramount has undertaken a series of transformational transactions that repaid all of the Company's debt and provided balance sheet strength and financial flexibility. As we enter 2017, the Company is well positioned to develop its resource base, grow production and take advantage of new opportunities.

Paramount completed three major transactions in 2016, starting with the sale of our Musreau plant complex to Pembina Pipeline Corporation in April for \$560 million, which provided some much-needed financial flexibility at the time.

Then in August, the Company completed the sale of our Musreau area oil and gas properties, our largest operating development for \$2.1 billion, comprised of \$500 million in cash, 33.5 million Seven Generations Energy shares and the purchaser's assumption of our US\$450 million senior notes. Paramount subsequently sold 29.7 million of these shares for net proceeds of \$860 million, and later distributed the remaining 3.8 million shares to our shareholders by way of dividend. On a full-cycle basis, Paramount realized a gain of \$1.1 billion on the Musreau properties, after recovering \$2.2 billion of capital invested.

Finally, in December Paramount sold a royalty on our non-producing bitumen leases, held in our wholly-owned subsidiary Cavalier Energy, for cash proceeds of \$100 million.

In total, Paramount realized net proceeds of \$2.75 billion in 2016, which allowed us to repay all bank indebtedness and redeem our remaining long-term senior notes. The Company entered 2016 with total consolidated net debt of over \$1.9 billion. Twelve months later, Paramount had an extremely strong balance sheet comprised of over \$600 million of cash, zero debt outstanding and had a \$100 million undrawn bank credit facility. In addition, the Company paid out a \$120 million dividend in kind to our shareholders.

Full year production volumes were 31,860 Boe/d in 2016, down 28 percent from 2015 levels, which averaged 44,130 Boe/d. Paramount produced 11.7 million Boe in 2016, realizing average field netbacks of \$7.99/Boe and cash flow of \$3.06/Boe. Total netbacks in 2016 were \$93.1 million and cash flow was \$35.7 million, down materially from 2015 levels due to the reduction in sales volumes resulting from the sale of the Musreau properties and lower commodity prices. Operating costs increased to \$8.32/Boe in 2016 from \$5.59/Boe in 2015 as a result of the sale of the Musreau plant complex and fixed costs being applied over lower production levels. Capital spending was down materially, with \$205 million invested in 2016 compared to \$500 million in 2015.

Paramount entered 2016 producing over 50,000 Boe/d, but as capital spending was reduced in response to the collapse in commodity prices, production declines prevailed for the first half of the year and total corporate volumes averaged about 35,000 Boe/d at the time of the Musreau sale in August 2016. Sales volumes were approximately 10,000 Boe/d following the Musreau dispositions and the Company has grown production to over 16,000 Boe/d in February 2017 with new Montney wells coming on at Karr.

Paramount used the period of reduced field activities in 2015 and early 2016 to optimize its operations and update well designs, reducing per-meter well costs and improving well productivity. The Company's updated well designs incorporate longer horizontal sections, an increased number of completion stages and higher fracture proppant intensities, in keeping with overall industry trends.

The Company resumed its drilling and completion activities at Musreau in the spring of 2016 incorporating these new well designs, but sold the property before results from these enhancements were available. Following the Musreau sale, Paramount shifted its development focus to its Karr property directly north of Musreau, where these well design enhancements were incorporated in drilling and completion programs executed in the latter part of 2016. Well results and economics for these new Karr wells are materially better than past wells completed using previous designs. The Company has now completed six wells in the program, with initial per-well production results exceeding 2,000 Boe/d, which we estimate to be amongst the most prolific results in all of North America. Based on these improved results and strengthening commodity prices, Paramount quickly increased spending to take advantage of the availability of field services and lower input costs. As capital activity at Karr has accelerated, we have resumed production growth through the end of 2016 into early 2017.

Since mid-2016, Paramount has embarked on a capital program at Karr to drill 27 horizontal Montney wells by the end of 2017 and complete the expansion of our Karr facilities from 40 MMcf/d to 80 MMcf/d. Upon completion of this expansion and the newly drilled wells, the Company expects to see corporate production increase to over 30,000 Boe/d, reaching levels similar to those prior to the sale of the Musreau properties. The total cost of this program through the end of 2017 is estimated to be about \$300 million.

Paramount also plans to spend approximately \$125 million in its other operating areas in 2017, with the majority of these expenditures directed at its Resthaven and Birch plays. At Resthaven, plans are in place to drill and complete six wells, which will be tied in to Paramount's owned capacity in the third-party operated Smoky deep cut plant. In the Birch area, the Company plans to participate to its 50 percent working interest in nine new horizontal Montney wells and a facility expansion which will increase gross capacity to 40 MMcf/d from the current 20 MMcf/d. The 2017 capital program also includes spending at the Valhalla and Willesden Green areas to further our understanding of the economics and full development potential of these areas.

The Musreau disposition resulted in the sale of proved reserves of 199.7 MMBoe and proved plus probable reserves ("P+P") of 293.1 MMBoe, as estimated at December 31, 2015.

Proved reserves for Paramount's ongoing operations increased by 124 percent to 59.6 MMBoe in 2016 compared to 26.7 MMBoe in 2015 and P+P reserves increased 159 percent to 115.2 MMBoe in 2016 compared to 44.5 MMBoe in 2015. The Company replaced 2016 ongoing

operations production of 4.3 MMBoe by 9 times with proved reserves additions and 18 times with P+P reserves additions.

Paramount added reserves at a low cost in 2016, with finding and development costs for ongoing operations of \$12.16/Boe for proved reserves and \$8.29/Boe for P+P reserves. The net present value assigned to Paramount's ongoing operations reserves, discounted at ten percent, increased year over year by 175 percent to \$424 million for proved reserves and by 206 percent to \$810 million for P+P reserves.

Oil prices have reacted as worldwide supply and demand have become more balanced. The OPEC agreement to curtail oil production has accelerated the re-balancing of world oil markets, increasing prices to approximately US\$50/Bbl, incentivizing Paramount to resume investing capital in its plays. It is anticipated that in the near-term, structural improvements in worldwide supply costs will limit any material appreciation of oil prices. In the medium-term, the prolonged period of limited re-investment in the upstream industry since the collapse of oil prices in 2014 is expected to catch up with supply, prompting prices to increase further.

Natural gas pricing has structurally changed because of technological improvements, initially by the adoption of horizontal drilling and multi-stage fracturing, and more recently by continued refinements in proppant intensity and technological improvements which have reduced capital costs. Paramount is benefitting from these technological improvements, but so are the majority of unconventional resource companies.

Paramount looks forward to continued production growth through the balance of 2017. Forward guidance has been provided, which includes capital spending of \$325 million, significantly more than forecast cash flow. This capital program will increase production from about 12,000 Boe/d at the end of 2016 to over 30,000 Boe/d in the fourth quarter of 2017, a 150 percent increase in just 12 months. Production for 2017 is expected to average 20,000 Boe/d.

The Company will preserve its balance sheet strength and financial flexibility in 2017, with cash on hand projected to remain over \$400 million, assuming current commodity prices. Paramount will continue to work to develop its suite of development projects at Karr, Resthaven, Valhalla, Birch and Willesden Green and will continue to look to maximize value for our stakeholders by further improving cost structures and well performance. The Company will also prioritize business development activities, as our strong balance sheet has placed us in a position to take advantage of opportunities that may arise.

Paramount's Management and Board of Directors would like to thank all of our stakeholders for their continued support through the last several years, which has allowed us to transform the Company into what it is today.



James H. T. Riddell
President and Chief Executive Officer
March 2017

2016 OVERVIEW

OIL AND GAS OPERATIONS ⁽¹⁾

- Paramount's fourth quarter 2016 sales volumes averaged 11,901 Boe/d (34 percent liquids), including approximately 5,500 Boe/d (38 percent liquids) from Karr-Gold Creek. The Company's annual sales volumes were 31,860 Boe/d, including 11,656 Boe/d from Ongoing Operations and 20,204 Boe/d related to the Musreau Assets.
- Five new wells on the 4-19 and 15-27 pads at Karr-Gold Creek have produced a total of approximately 250,000 barrels of condensate since first production in late-December 2016.
- Paramount's sales volumes averaged approximately 16,000 Boe/d for the month of February 2017 (50 percent liquids).
- Four wells at the new 16-36 pad at Karr-Gold Creek are scheduled to be brought on production at the end of April. Karr-Gold Creek production will be constrained until the 40 MMcf/d 6-18 Facility expansion is completed in the second quarter.
- Principal Properties capital expenditures in the fourth quarter of 2016 totaled \$78.2 million, with the majority of spending directed towards the Company's Karr-Gold Creek development. Total Principal Properties capital spending for 2016 was \$171.0 million, including \$92.5 million at Karr-Gold Creek and \$52.5 million related to the Musreau Assets.
- In 2016, the Company closed dispositions of non-core properties for aggregate cash proceeds of approximately \$22.5 million.
- Paramount's 2017 capital program is expected to total approximately \$325 million, excluding land acquisitions, with about \$200 million directed towards Karr-Gold Creek.
- Development activities at Karr-Gold Creek are currently focused on a 27-well horizontal Montney drilling and completion program (the "Karr Program"). By the end of 2017, the Company expects to have completed up to 22 of the 27 wells, with the remaining wells to be completed in 2018. The Karr Program wells will be brought on production through 2017 and 2018 to fill the expanded 6-18 Facility.
- Sales volumes in 2017 are projected to average approximately 20,000 Boe/d, despite the scheduled outage of a third-party processing facility that is expected to shut-in Karr-Gold Creek production for most of September. Fourth quarter sales volumes are expected to average over 30,000 Boe/d.

(1) In August 2016, the Company sold the majority of its oil and gas properties in the Musreau/Kakwa area of west central Alberta (the "Musreau Assets") to Seven Generations Energy Ltd. ("7Gen") for total consideration of approximately \$2.1 billion (the "Musreau Disposition"). Disclosures of results and changes from prior periods for "Ongoing Operations" exclude amounts attributable to the Musreau Assets.

RESERVES — ONGOING OPERATIONS ⁽²⁾

- In 2016, proved reserves for Paramount's Ongoing Operations increased 124 percent to 59.6 MMBoe (replacement ratio of 9 times) and proved plus probable ("P+P") reserves increased 159 percent to 115.2 MMBoe (replacement ratio of 18 times), after production of 4.3 MMBoe.
- The increase in Ongoing Operations reserves in 2016 was driven by growth at Karr-Gold Creek, where proved reserves increased 216 percent to 48.8 MMBoe and P+P reserves increased 194 percent to 84.3 MMBoe.
- P+P finding and development ("F&D") costs for Ongoing Operations in 2016 were \$8.29 per Boe in total and \$8.60 per Boe for Karr-Gold Creek.
- The NPV₁₀ of future net revenue for Ongoing Operations increased 175 percent to \$424 million for proved reserves and 206 percent to \$810 million for P+P reserves.

CORPORATE

- The Company exited 2016 with cash and cash equivalents of \$622 million, no indebtedness and an undrawn \$100 million bank credit facility.
- Paramount realized total proceeds from the sale of its Musreau natural gas processing plant, the Musreau Assets, the Cavalier Royalty and non-core property dispositions of \$2.75 billion in 2016, recording aggregate pre-tax gains of \$1.5 billion.
- Funds flow from operations totaled \$14.3 million in the fourth quarter and \$35.7 million for 2016.
- In January 2017, Paramount distributed its remaining 3.8 million 7Gen common shares, valued at \$119.0 million at December 31, 2016, to shareholders by way of dividend.
- Paramount has hedged 2,000 Bbl/d of liquids at an average WTI price of C\$70.43/Bbl and 1,000 Bbl/d of liquids at a WTI price of US\$54.50/Bbl for 2017. The Company has also locked in US\$3.4 million of gains on natural gas hedging contracts that will be received over the remainder of 2017.

(2) The estimates of reserves and future net revenue for individual properties may not reflect the same confidence level as estimates of reserves and future net revenue for all properties, due to the effects of aggregation.

REVIEW OF OPERATIONS

Consistent with Paramount's long track record of early stage resource capture and delineation followed by strategic and creative value realization, the Company closed a series of transformative transactions in 2016, including the sale of its Musreau/Kakwa area assets, for aggregate proceeds of \$2.75 billion. With the completion of these transactions, Paramount has reset its operational base, repaid all indebtedness and secured the financial resources to continue with this strategy.

As of December 31, 2016, Paramount has a land base of over 1.2 million net acres. The Company's significant properties currently include:

- Karr-Gold Creek;
- Smoky/Resthaven;
- Valhalla;
- Birch/Umbach; and
- Willesden Green.

Paramount also holds a portfolio of emerging plays and strategic investments, including:

- exploratory shale gas assets in the Liard and Horn River Basins;
- northern frontier assets in the Central Mackenzie and the Mackenzie Delta;
- oil sands assets held through its wholly-owned subsidiary Cavalier Energy ("Cavalier");
- seven triple-sized rigs held through its wholly-owned subsidiary Fox Drilling Limited Partnership; and
- investments in other public and private oil and gas companies including, Trilogy Energy Corp. and MEG Energy Corp.

2016 OPERATING RESULTS ⁽¹⁾

(\$ millions, except as noted)

	Q4 2016		Q4 2015		2016		2015	
			<i>Ongoing Operations</i> ⁽²⁾		<i>Ongoing Operations</i> ⁽²⁾		<i>Ongoing Operations</i> ⁽²⁾	
Sales volumes by COU (Boe/d)								
Grande Prairie	6,901		8,813		6,579		7,146	
Kaybob	2,812		2,428		2,796		3,783	
Other	2,188		1,524		2,281		1,387	
Total	11,901		12,765		11,656		12,316	
Netback	\$/Boe		\$/Boe		\$/Boe		\$/Boe	
Petroleum and natural gas sales	32.3	29.52	27.5	23.45	98.9	23.17	112.7	25.07
Royalties	(0.1)	(0.08)	(1.2)	(1.06)	(0.3)	(0.08)	(4.1)	(0.92)
Operating expense	(10.9)	(10.00)	(13.1)	(11.12)	(50.8)	(11.91)	(54.4)	(12.09)
Transportation and NGLs processing ⁽³⁾	(4.3)	(3.91)	(2.6)	(2.24)	(20.4)	(4.78)	(12.2)	(2.71)
Netback	17.0	15.53	10.6	9.03	27.4	6.40	42.0	9.35
Principal Properties Capital By COU ⁽⁴⁾								
Grande Prairie	62.5		1.7		93.2		62.6	
Kaybob	3.7		2.5		9.9		29.9	
Other	8.1		6.0		15.4		70.6	
	74.3		10.2		118.5		163.1	

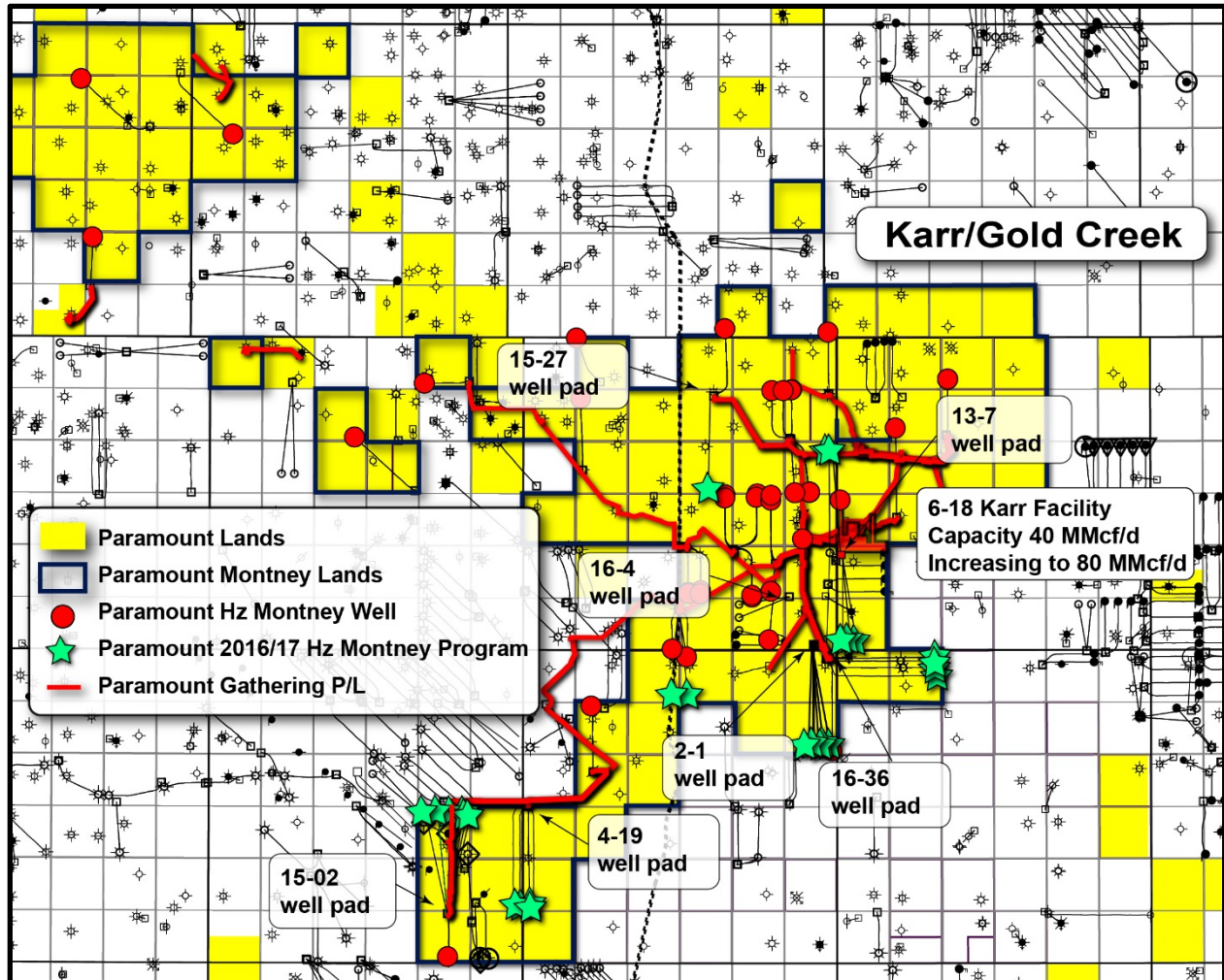
(1) Readers are referred to the advisories concerning Non-GAAP Measures and Oil and Gas Measures and Definitions in the Advisories section of this document and to the reconciliations of such non-GAAP measures to their most directly comparable measure under GAAP in the applicable sections of this document.

(2) Ongoing Operations represents Paramount's total results less amounts attributable to the Musreau Assets.

(3) Includes downstream natural gas, NGLs and oil transportation costs and NGLs fractionation costs incurred by the Company.

(4) Principal Properties Capital includes capital expenditures and geological and geophysical costs related to the Company's Principal Properties, excluding land acquisitions and capitalized interest. Excludes amounts attributable to the Musreau Assets

Karr-Gold Creek



Development activities at Karr-Gold Creek are currently focused on a 27 (27.0 net) well horizontal Montney drilling and completion program that commenced in mid-2016. The Company held approximately 92 (77 net) sections of Montney rights at Karr-Gold Creek at December 31, 2016.

The well completion design for Karr Program wells is outlined in the table below:

Karr Program Well Design		
Horizontal lateral – completed length (meters)	2,700 to 3,000	longer laterals
Completion fluids	Slickwater	lower fluid costs
Fracture stages	Up to 75	
Average inter-frack spacing (meters)	~ 40	tighter frack spacing
Proppant placed per stage (tonnes)	~ 100	increased tonnage per stage
Proppant loading (tonnes / meter)	2.3 – 2.5	higher proppant intensities per meter

The first well in the Karr Program, the 15-14 well on the 15-02 pad, was brought on production at controlled rates in September 2016. Four new wells on the 4-19 pad were completed in December 2016 and January 2017 and are currently flowing back on cleanup at restricted rates. An additional new well, the 3-22 well on the 15-27 pad, was completed and began flowing in February 2017. Production data from the wells to March 5, 2017 is shown in the following table:

	15-02 PAD	4-19 PAD				15-27 PAD
Wells	15-14	4-7	02/4-7	1-12	02/1-12	3-22
Completion Details						
Horizontal length (meters)	3,018	3,047	3,049	3,054	3,036	2,870
Completion stages	50	70	75	73	58	66
Proppant (tonnes)	5,000	7,000	7,500	7,300	5,800	6,600
Proppant intensity (tonnes / meter)	1.7	2.3	2.5	2.4	1.9	2.3
Production - Cumulative ⁽¹⁾						
Natural gas (MMcf)	1,098	220	125	90	94	72
Wellhead liquids (Bbl)	178,863	93,913	72,314	34,004	33,133	15,590
CGR ⁽²⁾ (Bbl/MMcf)	163	425	579	378	352	216
Days of flowback	173	65	34	29	26	22
Natural gas (MMcf/d)	6.3	3.4	3.7	3.1	3.6	3.3
Wellhead liquids (Bbl/d)	1,034	1,445	2,127	1,173	1,274	709
Production - Last 7 Producing Days ⁽¹⁾						
Natural gas (MMcf/d)	4.7	4.1	4.3	4.2	4.9	4.8
Wellhead liquids (Bbl/d)	775	1,389	2,120	1,465	1,761	856
CGR ⁽²⁾ (Bbl/MMcf)	166	338	494	350	362	179
Production - Last 24 Producing Hours ⁽¹⁾						
Natural gas (MMcf/d)	4.7	4.0	4.2	4.1	4.9	5.4
Wellhead liquids (Bbl/d)	778	1,340	2,077	1,408	1,772	942
CGR ⁽²⁾ (Bbl/MMcf)	167	338	497	344	362	173

- (1) Production volumes to March 5, 2017. Production volumes are the gross volumes measured at the wellhead separator for the specified period of: (i) cumulative volumes produced to March 5, 2017 ("Cumulative"); (ii) the most recent 168 producing hours ("Last 7 Producing Days"); or (iii) the last 24 producing hours ("Last 24 Producing Hours"). Excludes hours and days when the well did not produce. Natural gas sales volumes are approximately 10 percent lower and stabilized condensate sales volumes are expected to be approximately 15 percent lower due to shrinkage. The production rates and volumes shown are over a short period of time and, therefore, are not necessarily indicative of long-term performance or of ultimate recovery.
- (2) The condensate to natural gas ratio ("CGR") was calculated by dividing total wellhead separator liquids volumes by total wellhead separator natural gas volumes.

The Company continues to evaluate the performance of the higher intensity completions on the 4-19 and 15-27 pads. Early results indicate that higher intensity completions have resulted in enhanced productivity.

The status of the Karr Program to date is as follows:

	As of Mar 5/17	As of Dec 31/16
Wells Spud	20	20
Wells Rig Released	18	10
Wells Completed	6	2
Wells Producing	6	1

Four wells at the next new pad, the 16-36 pad, are scheduled to be brought on production at the end of April 2017. Paramount plans to spud an additional seven wells at Karr-Gold Creek in 2017. By the end of 2017, the Company expects to have completed up to 22 of the 27 wells, with the remaining wells to be completed in 2018. The Karr Program wells will be brought on production through 2017 and 2018 to fill the 6-18 compression and dehydration facility (the "6-18 Facility").

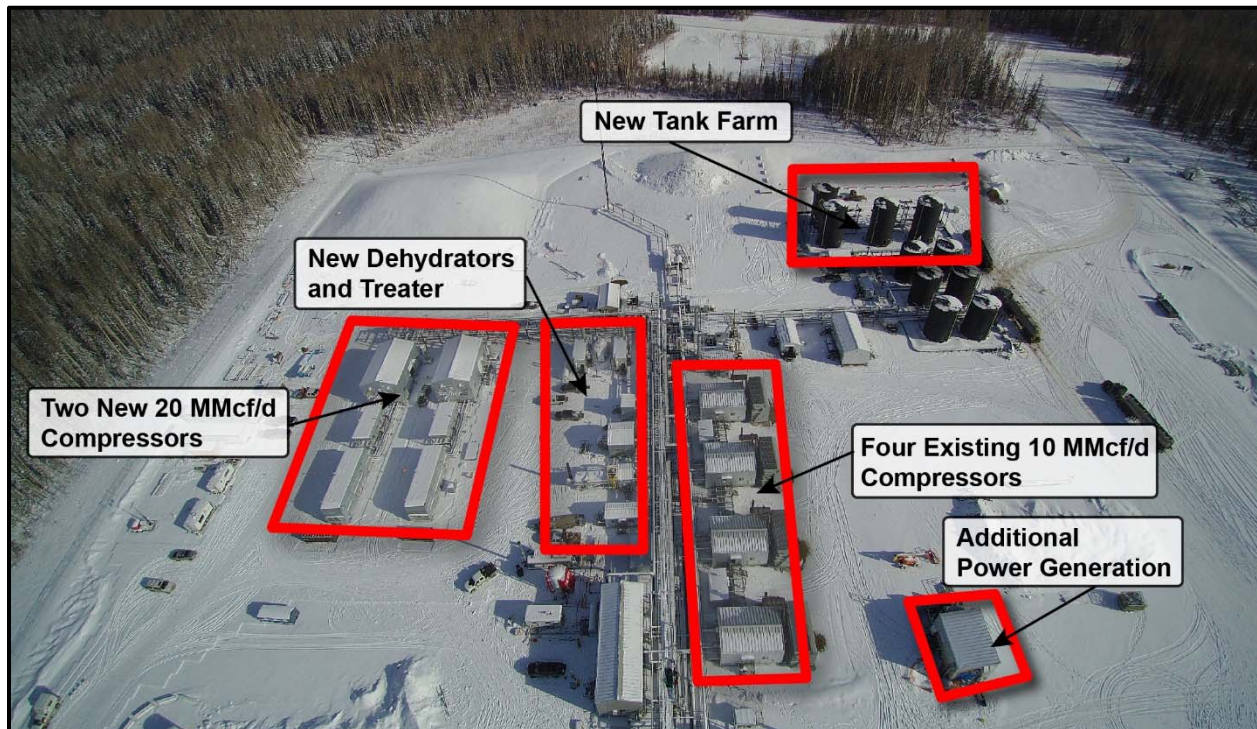
Production at Karr-Gold Creek is gathered through a Company-owned gas gathering system and compressed and dehydrated at the 40 MMcf/d 6-18 Facility. Volumes are then shipped via pipeline to a third-party natural gas processing facility (the "Third-party Facility") under a long-term firm-service arrangement to provide sales specification natural gas, condensate and C3+. The 6-18 Facility has been configured to facilitate the trucking-out of liquids so that volumes in excess of capacity at the Third-party Facility can be transported for processing at alternate locations. In addition, the 6-18 Facility is pipeline

connected to an alternate third-party facility in the area, which provides the Company with access to incremental natural gas processing capacity on an interruptible basis in the event there is insufficient capacity at the Third-party Facility during periods of maintenance downtime, temporary constraints or other service disruptions. Karr-Gold Creek sales volumes are anticipated to be impacted by a September 2017 planned shut-down of the Third-party Facility for the majority of the month.

The Company is doubling the capacity of the 6-18 Facility to 80 MMcf/d, which is on-schedule to be completed in the second quarter of 2017. The total cost of this expansion is estimated to be approximately \$35 million, of which \$20 million has been incurred to December 31, 2016.

The photograph below of the 6-18 Facility as of February 26, 2017 shows the progress made to date on the expansion:

Karr-Gold Creek 6-18 Compression and Dehydration Facility (February 26, 2017)



Other Areas

Smoky/Resthaven

Paramount held 116 (85 net) sections of Cretaceous rights and approximately 80 (78 net) sections of Montney rights at Smoky/Resthaven as of December 31, 2016. Since 2013, the Company has drilled 12 (12.0 net) wells in the region, focused on preserving mineral rights and delineation.

Paramount is executing a six-well exploration and delineation program targeting various Cretaceous zones at Smoky/Resthaven that commenced in 2016. The first well, a 1.4 mile horizontal Falher well, was completed at the end of February 2017. Three additional wells are currently being drilled, with the fifth well scheduled to commence drilling later in March.

Valhalla

At Valhalla, the Company held 63 (47 net) sections of Montney rights and 57 (43 net) sections of Doig rights as of December 31, 2016. A total of 17 (13.4 net) Montney and Doig wells are currently tied in. Prior to 2016, wells at Valhalla were completed with lower intensities of proppant over fewer stages.

The Company recently completed the 14-22 exploratory Montney well with a high-intensity frack, placing approximately 2,000 tonnes of proppant over 20 stages in the 1,300 meter lateral (1.5 tonnes per meter).

The Company is evaluating the potential economics of the opportunity at Valhalla based on the results of this initial high intensity well completion, results from offsetting operators and various alternatives to access natural gas processing infrastructure.

Birch

Activities at Birch, where the Company held approximately 60 (30 net) sections of Montney rights as of December 31, 2016, have mainly focused on drilling delineation wells to evaluate the reservoir.

The Company plans to drill a total of nine (4.5 net) horizontal Montney wells at Birch in 2017 and expand the existing 20 MMcf/d compression facility to 40 (20 net) MMcf/d. Five (2.5 net) wells have been drilled to date. Two (1.0 net) of these wells have been completed and are scheduled to be brought on production later in the first quarter of 2017.

Willesden Green

The Company held approximately 92 (92 net) sections of Duvernay rights at Willesden Green as of December 31, 2016, where a total of five Duvernay wells have been drilled on Paramount's lands. Three of these wells have been brought on production. A fourth well, the 102/13-5 well, was completed in the fourth quarter of 2016. The well was fracked using slickwater and 4,600 tonnes of proppant placed over 26 stages in the 2,000 meter lateral wellbore (2.3 tonnes per meter). Following completion, the well was flow-tested over an extended timeframe to obtain data for analysis of long-term reservoir performance. The Company continues to evaluate further development of the Duvernay formation at Willesden Green, including the preparation of a full-field development plan.

Other

In 2016, the Company closed dispositions of non-core properties for aggregate cash proceeds of approximately \$22.5 million.

OUTLOOK

Paramount's 2017 capital program is expected to total approximately \$325 million, excluding land acquisitions, with approximately \$200 million directed towards Karr-Gold Creek and the balance directed towards Smoky/Resthaven, Birch, and other areas.

Activities at Karr-Gold Creek will focus on the expansion of the 6-18 Facility, finishing the 27 well Montney drilling program and completing a portion of those wells to fill the expanded 6-18 Facility. At Smoky/Resthaven, Paramount plans to drill and complete six horizontal wells targeting various Cretaceous formations. At Birch, the Company plans to drill and complete a total of nine (4.5 net) wells and double compression and dehydration capacity to 40 MMcf/d (20 MMcf/d net).

Sales volumes in 2017 are projected to average approximately 20,000 Boe/d, despite the scheduled outage of a third-party processing facility that is expected to shut-in Karr-Gold Creek production for most of September. Fourth quarter sales volumes are expected to average over 30,000 Boe/d.

Annual operating costs for 2017 are anticipated to average approximately \$10.00 per Boe. Fourth quarter 2017 operating costs are projected to be lower than in the first part of the year because of the ramp-up in production volumes at Karr-Gold Creek.

PRINCIPAL PROPERTIES RESERVES AND FINDING & DEVELOPMENT COSTS

Proved reserves for the Company's Ongoing Operations increased 124 percent to 59.6 MMBoe in 2016 compared to 26.7 MMBoe in 2015. Ongoing operations proved plus probable ("P+P") reserves increased by 159 percent to 115.2 MMBoe in 2016 compared to 44.5 MMBoe in 2015.

	Proved ⁽¹⁾⁽²⁾			Proved plus Probable ⁽¹⁾⁽²⁾		
	2016	2015 ⁽³⁾	% Change	2016	2015 ⁽³⁾	% Change
Ongoing Operations						
Natural gas (Bcf)	238.0	99.6	139	463.3	165.8	179
NGLs (MBbl)	19,100	9,343	104	36,736	15,847	132
Light and Medium crude oil (MBbl)	882	741	19	1,219	1,021	19
Total Ongoing Operations (MMBoe)	59,645	26,682	124	115,173	44,509	159
Musreau Assets (MBoe)	—	199,658	(100)	—	293,124	(100)
Total (MMBoe)	59,645	226,340	(74)	115,173	337,633	(66)

(1) Readers are referred to the advisories concerning Oil and Gas Measures and Definitions in the Advisories section of this document. Principal Properties reserves exclude 93.5 MMBbl of probable bitumen reserves related to Cavalier's Hoole Grand Rapids Phase 1.

(2) Reserves evaluated and reviewed, as applicable, by McDaniel as of December 31, 2016 and December 31, 2015 in accordance with National Instrument 51-101 definitions, standards and procedures. Working interest reserves before royalty deductions.

(3) Reserves for Ongoing Operations in 2015 consist of Paramount's total reserves less amounts attributable to the Musreau Assets. The estimates of reserves and future net revenue for individual properties may not reflect the same confidence level as estimates of reserves and future net revenue for all properties, due to the effects of aggregation.

The following table summarizes Paramount's Principal Properties reserves as at December 31, 2016:

	Gross Principal Properties Reserves ⁽¹⁾⁽²⁾				Future Net Revenue Net Present Value ⁽¹⁾⁽³⁾ Before Tax (\$ millions)	
	Natural Gas (Bcf)	NGLs (MBbl)	Light & Medium Crude Oil (MBbl)	Total (MBoe)	Discount Rate	
					0%	10%
Proved						
Developed Producing	65.7	3,605	630	15,187	199	151
Developed Non-producing	0.5	26	253	368	9	6
Undeveloped	171.7	15,469	—	44,089	559	266
Total Proved	238.0	19,100	882	59,645	767	424
Total Probable	225.4	17,636	337	55,529	858	386
Total Proved plus Probable	463.3	36,736	1,219	115,173	1,625	810

(1) Columns may not add due to rounding.

(2) Working interest reserves before royalty deductions. Principal Properties reserves exclude 93.5 MMBbl of probable bitumen reserves related to Cavalier's Hoole Grand Rapids Phase 1.

(3) The estimated net present values of future net revenue disclosed in this document do not represent fair market value. Revenues and expenditures were calculated based on McDaniel's forecast prices and costs as of January 1, 2017.

The following table provides a reconciliation of Paramount's gross Principal Properties reserves for the year ended December 31, 2016. The Company's proved reserves were reduced by approximately 193 MMBoe and proved plus probable reserves were reduced by approximately 287 MMBoe as a result of the Musreau Disposition.

Principal Properties Reserves Reconciliation

	Proved ⁽¹⁾⁽²⁾			Proved plus Probable ⁽¹⁾⁽²⁾		
	Natural Gas	Oil & NGLs ⁽³⁾	Total	Natural Gas	Oil & NGLs ⁽³⁾	Total
	(Bcf)	(MBbl)	(MBoe)	(Bcf)	(MBbl)	(MBoe)
January 1, 2016	710.6	107,913	226,340	1,065.7	160,008	337,633
Extensions & discoveries	97.5	8,817	25,068	274.4	22,227	67,952
Technical revisions	65.1	2,749	13,604	47.8	651	8,617
Economic factors	(5.1)	(141)	(982)	(5.0)	(169)	(1,007)
Acquisitions	0.2	117	155	0.3	140	189
Dispositions	(592.1)	(94,200)	(192,879)	(881.5)	(139,630)	(286,550)
Production	(38.3)	(5,271)	(11,661)	(38.3)	(5,271)	(11,661)
December 31, 2016	238.0	19,982	59,645	463.3	37,955	115,173

(1) Columns and rows may not add due to rounding.

(2) Principal Properties reserves exclude 93.5 MMBbl of probable bitumen reserves related to Cavalier's Hoole Grand Rapids Phase 1.

(3) Light and medium crude oil and NGLs

Principal Properties Finding and Development Costs (F&D)

	2016					Three-Year Average ⁽⁵⁾
	Capital ⁽²⁾	Change in FDC ⁽³⁾	Total F&D Capital	Reserves Additions ⁽⁴⁾	F&D	
	(\$ millions)	(\$ millions)	(\$ millions)	(MMBoe)	(\$/Boe)	(\$/Boe)
Proved ⁽¹⁾						
Karr-Gold Creek	91.3	334.8	426.1	35.1	12.15	15.90
Principal Properties - Ongoing Operations	118.5	340.0	458.5	37.7	12.16	20.73
Proved plus Probable ⁽¹⁾						
Karr-Gold Creek	91.3	401.6	492.9	57.3	8.60	11.34
Principal Properties - Ongoing Operations	118.5	507.7	626.3	75.6	8.29	13.40

(1) F&D costs related to Ongoing Operations exclude capital costs, future development capital and reserves attributable to the Musreau Assets. Readers are referred to the advisories concerning Oil and Gas Measures and Definitions in the Advisories section of this document.

(2) Aggregate Principal Properties exploration and development costs incurred for the year ended December 31, 2016.

(3) Change in estimated future development costs from December 31, 2015 to December 31, 2016.

(4) Reserves additions were calculated as the aggregate of extensions & discoveries, technical revisions and economic factors for the year ended December 31, 2016. Excludes acquisitions and dispositions.

(5) Three-year average finding and development ("F&D") costs are calculated using the aggregate capital costs, changes in future development capital and reserves additions over the three-year period December 31, 2013 to December 31, 2016. Amounts for 2014 and 2015 were calculated on the same basis as for the year ended December 31, 2016.

The following table summarizes the undiscounted future development costs ("FDC") incorporated in the calculation of 2016 finding and development costs:

Future Development Costs – Principal Properties ⁽¹⁾⁽²⁾							
(Undiscounted, \$ millions)	2017	2018	2019	2020	2021	Remainder	Total
Total Proved	172	90	83	73	74	–	492
Total Proved plus Probable	215	104	94	80	85	158	736

(1) Columns may not add due to rounding.

(2) Excludes future development costs related to Cavalier Energy's Hoole Grand Rapids Phase 1.

Land

The following table sets forth Paramount's land position:

(thousands of acres)	December 31, 2016			December 31, 2015		
	Gross ⁽¹⁾	Net ⁽²⁾	Average Working Interest	Gross ⁽¹⁾	Net ⁽²⁾	Average Working Interest
Undeveloped land	1,970	1,061	54%	2,803	1,615	58%
Acreage assigned reserves	289	153	53%	351	190	54%
Total	2,259	1,214	54%	3,154	1,805	57%

(1) "Gross" acres means the total acreage in which Paramount has an interest. Gross acreage is calculated only once per lease or license of petroleum and natural gas rights ("Lease") regardless of whether or not Paramount holds a working and/or royalty interest, or whether or not the Lease includes multiple prospective formations. If Paramount holds more than one Lease under the same geographical area, Paramount records acreage for both Leases.

(2) "Net" acres means gross acres multiplied by Paramount's working interest therein.

STRATEGIC INVESTMENTS

Cavalier Energy

Cavalier's initial focus has been on the Grand Rapids formation in its 100 percent owned in-situ oil sands leases at Hoole, which is located 10 kilometers northeast of Wabasca-Desmarais, Alberta. Since 2004, approximately \$112 million has been invested in land acquisitions, stratigraphic drilling, engineering studies, and environmental field programs to bring this project (the "Hoole Project") to a stage capable of development. Front-end engineering and design work for the initial 10,000 Bbl/d phase of the Hoole Project ("Hoole Grand Rapids Phase 1") has been completed and the Alberta Energy Regulator approved the Hoole Grand Rapids Phase 1 project in the second quarter of 2014.

In December 2016, Cavalier granted a royalty (the "Cavalier Royalty") on its oil sands lands (the "Oil Sands Lands") to an unrelated third-party for cash consideration of \$100 million. The agreement governing the Cavalier Royalty does not impose any development commitments on Cavalier in respect of the Hoole Project or any of the other Oil Sands Lands, nor does it impose any terms or conditions on the use of the consideration paid for the Cavalier Royalty.

Production from the Oil Sands Lands will not be subject to any royalty when the Western Canadian Select ("WCS") price is below US\$50 per barrel. At a WCS price of US\$50 per barrel, the royalty rate will be two percent and the rate will increase linearly to a maximum of 20 percent at a WCS price of US\$140 per barrel. As of December 31, 2016, the WCS price was US\$37.62 per barrel. The Cavalier Royalty will be payable based on Cavalier's realized bitumen price, net of diluent, transportation and storage costs. The Cavalier Royalty is secured by a lien over the Oil Sands Lands. The Oil Sands Lands are at the early stages of their evaluation and development and currently have no production.

An updated evaluation of Hoole Grand Rapids Phase 1 was prepared by McDaniel, the Company's independent reserves evaluator, effective December 31, 2016. In the updated evaluation, 93.5 million barrels of probable undeveloped bitumen reserves were ascribed to Hoole Grand Rapids Phase 1 with a net present value of \$108 million (before tax, discounted at 10 percent). Development of the project is contingent upon Cavalier obtaining financing and certain additional regulatory approvals.

Shale Gas Properties

Paramount's shale gas holdings in the Liard and Horn River Basins in northeast British Columbia and the Northwest Territories include approximately 134 net sections of land with potential for natural gas production from the Besa River shale formation.

In 2015, the Company completed drilling operations at the Dunedin d-71-G vertical exploratory shale gas well and then moved to the c-37-D well at La Biche, where drilling operations continued until spring break-up. Drilling operations resumed at c-37-D in December 2015, and the well was drilled to target depth in March 2016. With the completion of drilling operations for the c-37-D well, the Company has secured its mineral rights in the region for up to another 10 years.

Fox Drilling

Fox Drilling owns seven triple-sized rigs, including two new walking rigs that were commissioned and brought into service in 2016. The Fox Drilling rigs are designed to drill the deep horizontal wells that industry is currently focusing on. All seven rigs were deployed on the Company's lands at the end of 2016, drilling wells at Karr-Gold Creek and Smoky/Resthaven.

Investments in Other Entities

Paramount holds securities in a number of publicly-traded and private corporations as part of its portfolio of Strategic Investments. The Company's investment in Trilogy Energy Corp. was principally obtained in the course of its spin-out from Paramount. Investments in shares of most other entities, including MEG Energy Corp., were received as consideration for properties sold to the entities. Paramount's investments are summarized below:

	December 31, 2016 ⁽¹⁾⁽²⁾			December 31, 2015 ⁽¹⁾		
	Shares (000's)	(\$ millions)	(\$/share)	Shares (000's)	(\$ millions)	(\$/share)
Trilogy Energy Corp.	19,144	144.5	7.55	19,144	70.1	3.66
MEG Energy Corp.	3,700	34.2	9.23	3,700	29.7	8.02
Other ⁽³⁾		30.0			31.0	
		208.7			130.8	

(1) Based on the period-end closing price of publicly traded investments and the book value of remaining investments.

(2) Excludes 3.8 million class A common shares of 7Gen classified as "Investments in Securities for Distribution" having a carrying value and market value of \$119.0 million as at December 31, 2016. These shares were distributed to Paramount's shareholders by way of dividend in January 2017.

(3) Includes investments in Marquee Energy Ltd., RMP Energy Inc., Strategic Oil & Gas Ltd. and other public and private corporations.

CORPORATE

Paramount realized total proceeds from the sale of its Musreau natural gas processing plant, the Musreau Assets, the Cavalier Royalty and non-core property dispositions of \$2.75 billion in 2016.

In 2016, the Company repaid its bank credit facilities, redeemed all \$450 million of its 7½ percent 2019 Notes and, in connection with the Musreau Disposition, 7Gen assumed all US\$450 million principal amount of Paramount's 6½ percent 2023 Notes.

Paramount exited 2016 with cash and cash equivalents of \$622 million, no indebtedness and an undrawn \$100 million bank credit facility.

In January 2017, Paramount distributed its remaining 3.8 million common shares of 7Gen received through the Musreau Disposition to shareholders by way of dividend.

Paramount implemented a normal course issuer bid in October 2016 under which it may purchase up to 5.4 million Common Shares for cancellation. To date, the Company has purchased 622,900 Common Shares for cancellation at a total cost of \$9.7 million.

MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management's Discussion and Analysis ("MD&A"), dated March 8, 2017, should be read in conjunction with the audited Consolidated Financial Statements of Paramount Resources Ltd. ("Paramount" or the "Company") as at and for the year ended December 31, 2016. Financial data included in this MD&A has been prepared in accordance with International Financial Reporting Standards ("IFRS" or "GAAP") and is stated in millions of Canadian dollars, unless otherwise noted. The Company's accounting policies have been applied consistently to all periods presented.

The disclosures in this document include forward-looking information, Non-GAAP measures and certain oil and gas measures. Readers are referred to the Advisories section of this document concerning such matters. Certain comparative figures have been reclassified to conform to the current years' presentation. Additional information concerning Paramount, including its Annual Information Form, can be found on the SEDAR website at www.sedar.com.

ABOUT PARAMOUNT

Paramount is an independent, publicly traded, Canadian energy company that explores and develops unconventional and conventional petroleum and natural gas prospects, including long-term unconventional exploration and pre-development projects, and holds a portfolio of investments in other entities. The Company's principal properties are primarily located in Alberta and British Columbia. Paramount's Class A common shares ("Common Shares") are listed on the Toronto Stock Exchange under the symbol "POU".

Paramount's operations are grouped into three business segments, which have been established by management to assist in resource allocation, to assess operating performance and to achieve long-term strategic objectives: i) Principal Properties; ii) Strategic Investments; and iii) Corporate.

Paramount's Principal Properties are divided into four Corporate Operating Units ("COUs"):

- the Grande Prairie COU, which includes Karr-Gold Creek, Valhalla and other properties in the Peace River Arch area of Alberta;
- the Kaybob COU, which includes Smoky/Resthaven and other properties in west central Alberta;
- the Northern COU, which includes Birch and other properties in northeast British Columbia and northern Alberta; and
- the Southern COU, which includes Willesden Green and other properties in southern Alberta.

Strategic Investments include: (i) investments in other entities; (ii) investments in exploration and development stage assets, where there is no near-term expectation of commercial production, but a longer-term value proposition based on spin-outs, dispositions, or future revenue generation, including oil sands and carbonate bitumen interests held by Paramount's wholly-owned subsidiary Cavalier Energy ("Cavalier"), and prospective shale gas acreage in the Liard and Horn River Basins (the "Shale Gas Properties"); and (iii) drilling rigs owned by Paramount's wholly-owned subsidiary, Fox Drilling Limited Partnership ("Fox Drilling").

The Corporate segment is comprised of income and expense items, including general and administrative expense, share-based compensation expense and interest expense, which have not been specifically allocated to Principal Properties or Strategic Investments.

2016 HIGHLIGHTS ⁽¹⁾

	2016	2015	2014
FINANCIAL			
Petroleum and natural gas sales	248.8	376.8	350.0
Net income (loss)	1,165.3	(901.3)	(71.7)
per share – basic (\$/share)	10.98	(8.52)	(0.71)
per share – diluted (\$/share)	10.95	(8.52)	(0.71)
Funds flow from operations	35.7	93.2	141.0
per share – basic & diluted (\$/share)	0.34	0.88	1.39
Principal Properties Capital ⁽²⁾	171.0	429.9	813.9
Investments in other entities – market value ⁽³⁾⁽⁴⁾	208.7	130.8	256.9
Total assets	2,059.0	2,781.0	3,199.4
Long-term debt	–	1,750.2	1,210.4
Net cash (debt)	565.9	(1,904.6)	(1,482.5)
OPERATIONAL			
Sales volumes			
Natural gas (MMcf/d)	104.8	160.7	110.5
Condensate and oil (Bbl/d)	7,733	8,610	3,986
Other NGLs (Bbl/d) ⁽⁵⁾	6,668	8,735	2,128
Total (Boe/d)	31,860	44,130	24,524
Net wells drilled	23	31	58
FUNDS FLOW FROM OPERATIONS (\$/Boe)			
Petroleum and natural gas sales	21.34	23.39	39.10
Royalties	(0.19)	(0.64)	(1.96)
Operating expense	(8.32)	(5.59)	(7.96)
Transportation and NGLs processing ⁽⁶⁾	(4.84)	(4.08)	(4.01)
Netback	7.99	13.08	25.17
Commodity contract settlements	3.91	0.78	(0.13)
Netback including commodity contract settlements	11.90	13.86	25.04
General and administrative – corporate	(1.68)	(1.12)	(1.80)
General and administrative – strategic investments	(0.54)	(0.36)	(0.87)
Interest and financing	(6.74)	(6.73)	(7.69)
Dividends from investments	–	–	0.82
Other	0.12	0.14	0.25
Funds flow from operations	3.06	5.79	15.75

(1) Readers are referred to the advisories concerning Non-GAAP measures and Oil and Gas Measures and Definitions in the Advisories section of this document and to the reconciliations of such Non-GAAP measures to their most directly comparable measure under GAAP in the applicable sections of this document. This table contains the following Non-GAAP measures: Funds flow from operations, Principal Properties Capital, Investments in other entities – market value, Net cash (debt) and Netback.

(2) Principal Properties Capital includes capital expenditures and geological and geophysical costs related to the Company's Principal Properties, and excludes land acquisitions and capitalized interest.

(3) Based on the period-end closing prices of publicly-traded investments and the book value of the remaining investments.

(4) Excludes 3.8 million class A common shares of Seven Generations Energy Ltd. classified as "Investments in Securities for distribution" having a carrying value and market value of \$119.0 million as at December 31, 2016. These shares were distributed to Paramount's shareholders by way of dividend in January 2017.

(5) Other NGLs means ethane, propane and butane.

(6) Includes downstream natural gas, NGLs and oil transportation costs and NGLs fractionation costs incurred by the Company.

CONSOLIDATED RESULTS

Net Income (Loss)

Year ended December 31	2016	2015	2014
Principal Properties	1,374.9	(418.2)	66.7
Strategic Investments	48.5	(281.8)	(37.4)
Corporate	(102.0)	(213.8)	(104.0)
Income tax recovery (expense)	(156.1)	12.5	3.0
Net income (loss)	1,165.3	(901.3)	(71.7)

In April 2016, Paramount sold its natural gas processing facility and related midstream assets at Musreau for net cash proceeds of \$560.3 million (the "Midstream Sale"), resulting in the recognition of a gain on sale of \$125.7 million within the Principal Properties business segment. The Midstream Sale included the 50 MMcf/d refrigeration natural gas processing facility, the 200 MMcf/d deep-cut natural gas processing facility, the condensate stabilizer and the amine train (collectively, the "Musreau Complex") and the sales gas pipeline connecting the Musreau Complex to TCPL, as well as the majority of Paramount's larger-diameter gathering system in the Musreau area. In connection with the Midstream Sale, the Company entered into a long-term natural gas processing arrangement with the purchaser (the "Processing Arrangement") that secured Paramount priority access to the sold capacity at the Musreau Complex.

In August 2016, the Company sold the majority of its oil and gas properties in the Musreau/Kakwa area of west central Alberta (the "Musreau Assets") to Seven Generations Energy Ltd. ("Seven Generations" or the "Acquiror") for total consideration of approximately \$2.1 billion (the "Musreau Disposition"), subject to customary post-closing adjustments. The consideration received at closing was comprised of: (i) \$496 million in cash; (ii) 33.5 million class A common shares of the Acquiror ("7Gen Shares") having a market value of approximately \$972 million based on the closing market price of the shares on the day prior to closing; (iii) the assumption by the Acquiror of all US\$450 million principal amount of the Company's 6 $\frac{7}{8}$ percent senior unsecured notes due in 2023 (the "2023 Notes"); and (iv) certain oil and gas properties of the Acquiror valued at approximately \$6 million. In connection with the Musreau Disposition, the Acquiror also assumed Paramount's processing and transportation commitments relating to the Musreau Assets, including the Processing Arrangement. A gain on sale of approximately \$1.2 billion was recorded in respect of the Musreau Disposition within the Principal Properties business segment.

In 2016, Paramount received \$861.1 million in aggregate net cash proceeds on the sale of 29.7 million of the 7Gen Shares it received through the Musreau Disposition, recording a net loss of \$0.8 million. The remaining 3.8 million 7Gen Shares were distributed to Paramount's shareholders by way of dividend in January 2017.

Paramount's results include amounts in respect of the Musreau Assets to August 18, 2016, the closing date of the Musreau Disposition. When used herein, "Ongoing Operations" represents Paramount's total results less amounts attributable to the Musreau Assets.

In December 2016, Cavalier granted a royalty (the "Cavalier Royalty") on its oil sands lands (the "Oil Sands Lands") to an unrelated third-party for cash consideration of \$100 million. A gain on sale of \$99.2 million was recorded in respect of the Cavalier Royalty within the Strategic Investments business segment.

Additional information concerning the Musreau Disposition can be found in Paramount's Annual Information Form, which is available on SEDAR at www.sedar.com.

Paramount recorded net income of \$1,165.3 million for the year ended December 31, 2016 compared to a net loss of \$901.3 million in the same period in 2015. Significant factors contributing to the change are shown below:

Year ended December 31	
Net Loss – 2015	(901.3)
• Gain on the sale of oil and gas assets primarily due to the Musreau Disposition and Midstream Sale in 2016	1,389.0
• Lower depletion and depreciation due to impairment reversals totaling \$133.2 million and asset dispositions in 2016 and because 2015 included impairment charges of \$263.7 million	547.5
• Exploration and evaluation income in 2016 because of a \$99.2 million gain recognized on the sale of the Cavalier Royalty compared to an expense in 2015 which included \$184.1 million of impairment charges	281.1
• Foreign exchange gain in 2016 compared to a loss in 2015, primarily related to the 2023 Notes	104.8
• Lower write-downs of investments in securities	70.6
• Lower interest and financing expense due to lower average debt balances in 2016	30.3
• Lower loss from equity-accounted investments	8.7
• Income tax expense in 2016 compared to a recovery in 2015	(168.6)
• Lower Netback in 2016 mainly due to lower sales volumes and lower commodity prices	(117.6)
• Lower gain on commodity contracts	(52.5)
• Higher debt extinguishment expense in 2016 due to the premiums paid on redemption of the 2019 Notes and the expensing of unamortized financing fees related to the senior unsecured notes	(15.6)
• Higher share-based compensation expense in 2016	(7.3)
• Other	(3.8)
Net Income – 2016	1,165.3

Paramount recorded a net loss of \$901.3 million for the year ended December 31, 2015, which included aggregate impairment charges of \$529.6 million consisting of \$287.8 million for Principal Properties, \$160.0 million for Strategic Investments and \$81.8 million related to investments in securities. The loss in 2015 also included a \$194.2 million de-recognition of deferred income tax assets. A net loss of \$71.7 million was recorded in the same period in 2014. Significant factors contributing to the change are shown below:

Year ended December 31	
Net Loss – 2014	(71.7)
• Higher impairment write-downs of property, plant and equipment in 2015	(231.0)
• Impairment write-downs of exploration and evaluation assets and goodwill in 2015	(184.1)
• Higher depletion and depreciation mainly due to higher sales volumes in 2015	(163.1)
• Loss on the sale of oil and gas properties in 2015 compared to a gain in 2014	(104.7)
• Higher write-downs of investments in securities	(66.2)
• Higher foreign exchange loss, primarily related to the 2023 Notes	(60.5)
• Higher interest and financing expense due to increased debt in 2015	(40.1)
• Higher loss from equity-accounted investments	(19.6)
• Lower Netback primarily due to lower commodity prices	(14.6)
• Debt extinguishment expense in 2015 due to the redemption of the 2017 Notes	(12.0)
• Higher gains on commodity contracts	49.9
• Higher income tax recovery	9.5
• Lower geological and geophysical expense in 2015	6.4
• Other	0.5
Net Loss – 2015	(901.3)

Funds Flow from Operations ⁽¹⁾

The following is a reconciliation of funds flow from operations to the nearest GAAP measure:

Year ended December 31	2016	2015	2014
Cash from operating activities	45.7	84.3	118.5
Change in non-cash working capital	(15.9)	(3.8)	5.4
Geological and geophysical expenses	4.1	6.1	12.5
Asset retirement obligations settled	1.8	6.6	4.6
Funds flow from operations	35.7	93.2	141.0
Funds flow from operations (\$/Boe)	3.06	5.79	15.75

(1) Refer to the advisories concerning Non-GAAP measures in the Advisories section of this document.

Funds flow from operations for the year ended December 31, 2016 was \$35.7 million compared to \$93.2 million in 2015. Significant factors contributing to the change are shown below:

Year ended December 31	
Funds flow from operations – 2015	93.2
• Lower Netback in 2016 mainly due to lower sales volumes and lower commodity prices	(117.6)
• Higher receipts from commodity contract settlements in 2016	33.0
• Lower interest and financing expense due to lower average debt balances in 2016	29.9
• Other	(2.8)
Funds flow from operations – 2016	35.7

Funds flow from operations for the year ended December 31, 2015 was \$93.2 million, \$47.8 million lower than 2014. Significant factors contributing to the change are shown below:

Year ended December 31	
Funds flow from operations – 2014	141.0
• Higher interest and financing expense due to increased debt	(39.6)
• Lower Netback primarily due to lower commodity prices	(14.6)
• Dividends from equity-accounted investments in 2014	(7.4)
• Receipts from commodity contract settlements in 2015 compared to payments in 2014	13.7
• Other	0.1
Funds flow from operations – 2015	93.2

PRINCIPAL PROPERTIES

Netback and Segment Income (Loss)

Year ended December 31	2016		2015	
	(\$/Boe) ⁽¹⁾		(\$/Boe) ⁽¹⁾	
Natural gas revenue	82.1	2.14	166.2	2.83
Condensate and oil revenue	138.1	48.78	166.0	52.83
Other NGLs revenue ⁽²⁾	27.4	11.24	41.2	12.92
Royalty and sulphur revenue	1.2	–	3.4	–
Petroleum and natural gas sales	248.8	21.34	376.8	23.39
Royalties	(2.2)	(0.19)	(10.4)	(0.64)
Operating expense	(97.0)	(8.32)	(90.0)	(5.59)
Transportation and NGLs processing ⁽³⁾	(56.5)	(4.84)	(65.7)	(4.08)
Netback	93.1	7.99	210.7	13.08
Commodity contract settlements	45.6	3.91	12.6	0.78
Netback including commodity contract settlements	138.7	11.90	223.3	13.86
Other principal property items (see below)	1,236.2		(641.5)	
Segment income (loss)	1,374.9		(418.2)	

(1) Natural gas revenue shown per Mcf.

(2) Other NGLs means ethane, propane and butane.

(3) Includes downstream natural gas, NGLs and oil transportation costs and NGLs fractionation costs incurred by the Company.

Petroleum and natural gas sales were \$248.8 million in 2016, a decrease of \$128.0 million from the prior year due to lower sales volumes and commodity prices.

The impact of changes in sales volumes and prices on petroleum and natural gas sales are as follows:

	Natural Gas	Condensate and Oil	Other NGLs	Royalty and Sulphur	Total
Year ended December 31, 2015	166.2	166.0	41.2	3.4	376.8
Effect of changes in sales volumes	(57.6)	(16.4)	(9.7)	–	(83.7)
Effect of changes in prices	(26.5)	(11.5)	(4.1)	–	(42.1)
Change in royalty and sulphur revenue	–	–	–	(2.2)	(2.2)
Year ended December 31, 2016	82.1	138.1	27.4	1.2	248.8

Sales Volumes

	Year ended December 31											
	Natural Gas (MMcf/d)			Condensate and Oil (Bbl/d)			Other NGLs (Bbl/d)			Total (Boe/d)		
	2016	2015	% Change	2016	2015	% Change	2016	2015	% Change	2016	2015	% Change
Grande Prairie ⁽¹⁾	26.1	29.0	(10)	1,922	1,969	(2)	303	353	(14)	6,579	7,146	(8)
Kaybob ⁽¹⁾	12.9	16.5	(22)	320	468	(32)	332	562	(41)	2,796	3,783	(26)
Northern	7.0	2.7	159	191	31	516	131	3	NM	1,484	479	210
Southern	2.6	2.6	–	255	339	(25)	109	129	(16)	797	908	(12)
Ongoing Operations	48.6	50.8	(4)	2,688	2,807	(4)	875	1,047	(16)	11,656	12,316	(5)
Musreau Assets	56.2	109.9	(49)	5,045	5,803	(13)	5,793	7,688	(25)	20,204	31,814	(36)
Total	104.8	160.7	(35)	7,733	8,610	(10)	6,668	8,735	(24)	31,860	44,130	(28)

(1) Excludes the results of the Musreau Assets

NM Not meaningful

Sales volumes from Ongoing Operations decreased 5 percent to 11,656 Boe/d in 2016 compared to 12,316 Boe/d in 2015. The decrease was primarily due to lower sales volumes at Smoky/Resthaven due to downtime at a third-party operated processing facility, lower production due to declines on existing wells in the Grande Prairie COU and the shut-in of the Valhalla property for a portion of the year due to low natural gas prices. These decreases were partially offset by production from new Montney formation wells brought on at Birch and at Karr-Gold Creek in 2016. Sales volumes for the Musreau Assets were lower in 2016 primarily due to the closing of the Musreau Disposition on August 18, 2016.

Commodity Prices

	2016	2015	% Change
Natural Gas			
Paramount realized price (\$/Mcf)	2.14	2.83	(24)
AECO daily spot (\$/GJ)	2.05	2.55	(20)
AECO monthly index (\$/GJ)	1.97	2.62	(25)
Malin (US\$/MMbtu)	2.38	2.56	(7)
Crude Oil			
Paramount average realized condensate and oil price (\$/Bbl)	48.78	52.83	(8)
Edmonton Light Sweet (\$/Bbl)	52.80	57.45	(8)
West Texas Intermediate (US\$/Bbl)	43.32	48.80	(11)
Foreign Exchange			
\$/CDN / 1 \$US	1.33	1.28	4

Paramount's average realized natural gas price decreased 24 percent in 2016 compared to the same period in 2015, generally consistent with decreases in benchmark natural gas prices. Paramount's natural gas portfolio primarily consists of sales priced at the Alberta, California and Chicago markets and is sold in a combination of daily and monthly contracts.

The Company's average realized condensate and oil price decreased 8 percent in 2016 compared to the same period in 2015, generally consistent with decreases in benchmark prices. Paramount sells its condensate volumes in both stabilized and unstabilized condition, depending upon the location of production and the availability of stabilization capacity. Stabilized condensate volumes delivered through pipelines typically receive prices for condensate quoted at Edmonton, which are generally higher than prices for unstabilized volumes, and are adjusted for applicable transportation, quality and density differentials. Unstabilized condensate volumes trucked to terminals typically receive prices based on the Edmonton Light Sweet crude oil price, which are generally lower than prices for stabilized volumes, and are adjusted for transportation, quality and density differentials.

Commodity Price Management

From time-to-time Paramount uses financial and physical commodity price contracts to manage exposure to commodity price volatility. The Company received \$45.6 million (2015 - \$12.6 million) on the settlement of commodity contracts in 2016.

Paramount had the following financial commodity contracts in place at December 31, 2016:

Instruments	Aggregate Notional	Average Fixed Price	Fair Value	Remaining Term
Gas – NYMEX Swaps (Sale)	40,000 MMBtu/d	US\$3.44/MMBtu	(3.5)	January 2017 – December 2017
Gas – NYMEX Swap (Purchase)	10,000 MMBtu/d	US\$3.04/MMBtu	2.9	January 2017 – December 2017
Oil – NYMEX WTI Swaps (Sale)	2,000 Bbl/d	CDN\$70.43/Bbl	(3.7)	January 2017 – December 2017
Oil – NYMEX WTI Swap (Sale)	1,000 Bbl/d	US\$54.50/Bbl	(0.9)	January 2017 – December 2017
			(5.2)	

In February 2017, the Company entered into the following financial commodity contracts:

Instruments	Aggregate Notional	Average Fixed Price	Remaining Term
Gas – NYMEX Swaps (Purchase)	30,000 MMBtu/d	US\$3.16/MMBtu	March 2017 – December 2017

Royalties

Year ended December 31	2016	Rate	2015	Rate
Royalties	2.2	0.9%	10.4	2.8%
<i>\$/Boe</i>	0.19		0.64	

Royalties decreased \$8.2 million to \$2.2 million in 2016 compared to \$10.4 million in 2015, primarily as a result of the Musreau Disposition, lower natural gas royalties due to lower prices and \$2.7 million of annual gas cost allowance adjustments recorded in 2016 that relate to prior periods. Excluding the impact of the gas cost allowance adjustments, the royalty rate was 2.0 percent in 2016 compared to 3.0 percent in 2015.

Operating Expense

Year ended December 31	2016	2015	% Change
Operating expense	97.0	90.0	8
<i>\$/Boe</i>	8.32	5.59	49

Operating expense increased \$7.0 million or 8 percent in 2016 to \$97.0 million in 2016 compared to \$90.0 million in 2015, primarily due to higher third-party processing fees related to the Processing Arrangement, lower processing income following the sale of the Musreau Complex and higher operating costs at Birch as a result of new production. These increases were partially offset by lower operating expenses at Smoky/Resthaven and Valhalla due to lower production and lower liquids handling costs and equalizations related to other properties. In connection with the Musreau Disposition, the Acquiror assumed Paramount's natural gas processing commitments related to the Musreau Assets, including the Processing Arrangement.

Transportation and NGLs Processing

Year ended December 31	2016	2015	% Change
Transportation and NGLs processing	56.5	65.7	(14)
<i>\$/Boe</i>	4.84	4.08	19

Transportation and NGLs processing includes the costs of downstream natural gas, NGLs and oil transportation and NGLs fractionation costs incurred by the Company.

Transportation and NGLs processing was \$56.5 million in 2016, a decrease of \$9.2 million compared to 2015. Transportation and NGLs processing decreased primarily as a result of the Musreau Disposition, partially offset by increased natural gas and Liquids transportation costs related to incremental firm service capacity contracted for the Company's Deep Basin production volumes. In connection with the Musreau Disposition, the Acquiror assumed Paramount's transportation and NGLs processing commitments related to the Musreau Assets.

Other Principal Property Items

Year ended December 31	2016	2015
Commodity contracts – net of settlements	(45.4)	40.2
Depletion and depreciation (excluding de-impairment / impairment)	(204.4)	(358.9)
Exploration and evaluation (excluding impairment)	(22.9)	(23.0)
De-impairment / (Impairment) of PP&E and E&E	133.2	(287.8)
Gain (loss) on sale of oil and gas assets	1,380.1	(9.2)
Accretion of asset retirement obligations	(4.3)	(5.4)
Other	(0.1)	2.6
Total – other principal property items	1,236.2	(641.5)

Depletion and depreciation expense (excluding de-impairment / impairment) decreased to \$204.4 million (\$17.53 per Boe) in 2016 compared to \$358.9 million (\$22.28 per Boe) in 2015, primarily due to the Musreau Disposition.

Exploration and evaluation ("E&E") expense in 2016 includes dry hole expense of \$13.8 million (2015 - \$14.8 million), expired undeveloped land leases costs of \$6.2 million (2015 - \$3.7 million) and geological and geophysical costs of \$2.9 million (2015 - \$4.5 million).

For the year ended December 31, 2016, the Company recorded a \$133.2 million reversal of previously recorded impairment charges related to petroleum and natural gas assets in the Grande Prairie cash-generating unit. The impairment reversal resulted from an increase in the estimated recoverable amount primarily due to an increase in development activities at Karr-Gold Creek following the Musreau Disposition, recent well performance, well results of other operators in the region, improved economic conditions and other factors.

The Company recorded aggregate property, plant and equipment impairment write-downs of \$263.7 million for the twelve months ended December 31, 2015 related to petroleum and natural gas assets in the Grande Prairie, Northern and Southern COUs. An impairment charge of \$24.1 million in respect of E&E assets was also recorded at December 31, 2015 related to a previously drilled exploratory well.

The gain on sale of oil and gas assets in 2016 includes \$1,233.6 million related to the Musreau Disposition, \$125.7 million related to the Midstream Sale and \$20.8 million related to other non-core property dispositions.

Ongoing Operations

The following tables set out the sales volumes and Netback for Paramount's Ongoing Operations, which exclude results of the Musreau Assets:

Year ended December 31	2016	2015	% Change
Natural gas (MMcf/d)	48.6	50.8	(4)
Condensate and oil (Bbl/d)	2,688	2,807	(4)
Other NGLs ⁽¹⁾ (Bbl/d)	875	1,047	(16)
Total (Boe/d)	11,656	12,316	(5)

(1) Other NGLs means ethane, propane and butane.

Year ended December 31	2016		2015	
		(\$/Boe) ⁽¹⁾		(\$/Boe) ⁽¹⁾
Natural gas revenue	44.4	2.50	51.2	2.76
Condensate and oil revenue	49.6	50.43	52.6	51.34
Other NGLs revenue ⁽²⁾	3.6	11.28	6.0	15.58
Royalty and sulphur revenue	1.3	–	2.9	–
Petroleum and natural gas sales	98.9	23.17	112.7	25.07
Royalties	(0.3)	(0.08)	(4.1)	(0.92)
Operating expense	(50.8)	(11.91)	(54.4)	(12.09)
Transportation and NGLs processing ⁽³⁾	(20.4)	(4.78)	(12.2)	(2.71)
Netback	27.4	6.40	42.0	9.35

(1) Natural gas revenue shown per Mcf.

(2) Other NGLs means ethane, propane and butane.

(3) Includes downstream natural gas, NGLs and oil transportation costs and NGLs fractionation costs incurred by the Company.

The Netback from Ongoing Operations for the year ended December 31, 2016 decreased primarily due to lower revenue as a result of lower realized prices and higher natural gas and Liquids transportation costs due to incremental firm service contracted for the Company's Deep Basin production volumes. Royalties were lower in 2016 due to lower prices and \$2.0 million of annual gas cost allowance adjustments recorded in 2016 that relate to prior periods

Outlook

Paramount's 2017 capital program is expected to total approximately \$325 million, excluding land acquisitions, with approximately \$200 million directed towards Karr-Gold Creek and the balance directed towards Smoky/Resthaven, Birch, and other areas.

Activities at Karr-Gold Creek will focus on the expansion of the 6-18 compression and dehydration facility (the "6-18 Facility"), finishing the planned 27 well Montney drilling program and completing a portion of those wells to fill the expanded 6-18 Facility. At Smoky/Resthaven, Paramount plans to drill and complete six horizontal wells targeting various Cretaceous formations. At Birch, the Company plans to drill and complete a total of nine (4.5 net) wells and double compression and dehydration capacity to 40 MMcf/d (20 MMcf/d net).

Sales volumes in 2017 are projected to average approximately 20,000 Boe/d, despite the scheduled outage of a third-party processing facility that is expected to shut-in Karr-Gold Creek production for most of September. Fourth quarter sales volumes are expected to average over 30,000 Boe/d.

Annual operating costs for 2017 are anticipated to average approximately \$10.00 per Boe. Fourth quarter 2017 operating costs are expected to be lower than in the first part of the year because of the ramp-up in production volumes at Karr-Gold Creek.

STRATEGIC INVESTMENTS

Year ended December 31	2016	2015
Loss on sale of oil and gas assets	(0.2)	–
General and administrative	(6.3)	(5.8)
Share-based compensation	(6.2)	(6.5)
Exploration and evaluation (expense) income	95.0	(161.9)
Depreciation	(4.3)	(0.8)
Interest and financing	(2.7)	(2.3)
Loss from equity-accounted investments	(14.3)	(23.0)
Write-down of investments in securities	(11.2)	(81.8)
Drilling rig revenue	0.2	1.1
Drilling rig expense	(1.2)	(0.6)
Other	(0.3)	(0.2)
Segment income (loss)	48.5	(281.8)

Strategic Investments at December 31, 2016 include:

- investments in the shares of Trilogy Energy Corp. ("Trilogy"), Seven Generations, MEG Energy Corp. ("MEG"), Marquee Energy Ltd. ("Marquee"), RMP Energy Inc. ("RMP Energy"), Strategic Oil & Gas Ltd. ("SOG") and other public and private corporations;
- oil sands and carbonate bitumen interests owned by Cavalier, including at Hoole, in the western portion of the Athabasca Oil Sands region, and carbonate bitumen holdings in northeast Alberta;
- seven triple-sized drilling rigs, including four built-for-purpose walking rigs, owned and operated by Fox Drilling; and
- shale gas holdings in the Liard and Horn River Basins in northeast British Columbia and the Northwest Territories.

In December 2016, Cavalier granted the Cavalier Royalty on the Oil Sands Lands to an unrelated third-party for cash consideration of \$100 million. A gain of \$99.2 million was recorded in respect of the sale, which is included in the net exploration and evaluation expense / income.

E&E expense in 2015 included aggregate impairment write-downs of \$160.0 million related to the E&E assets of Cavalier and MGM Energy and goodwill with a carrying value of \$21.6 million recorded on the acquisition of MGM Energy.

The loss from equity-accounted investments in 2016 primarily consists of a \$14.3 million (2015 – \$22.7 million) equity loss recorded in respect of the Trilogy investment.

Investments

Paramount holds investments in a number of publicly-traded and private corporations as part of its portfolio of Strategic Investments. The Company's investments in the shares of Trilogy were principally obtained in the course of its spin-out from Paramount. Investments in the shares of most other entities,

including MEG, were received as consideration for properties sold to the entities. Paramount's investments are summarized as follows:

As at December 31	Carrying Value		Market Value ⁽¹⁾	
	2016 ⁽²⁾	2015	2016 ⁽²⁾	2015
Trilogy	44.1	58.4	144.5	70.1
MEG	34.2	29.7	34.2	29.7
Other ⁽³⁾	30.0	31.0	30.0	31.0
Total	108.3	119.1	208.7	130.8

(1) Based on the period-end closing price of publicly traded investments and the book value of remaining investments.

(2) Excludes 3.8 million 7Gen Shares classified as "Investments in Securities for distribution" having a carrying value and market value of \$119.0 million as at December 31, 2016. These shares were distributed to Paramount's shareholders by way of dividend in January 2017.

(3) Includes investments in Marquee, RMP Energy, SOG and other public and private corporations.

For the year ended December 31, 2016, aggregate unrealized losses of \$11.2 million related to the Company's investments in MEG, Marquee and other securities previously recorded in other comprehensive income (loss) were charged to net income as a result of significant decreases in the market prices of the securities. Aggregate write-downs of \$81.8 million were recorded in 2015 as a result of decreases in the market values of certain securities, primarily consisting of a \$72.1 million write-down related to MEG.

Cavalier Oil Sands

Cavalier's initial focus has been on the Grand Rapids formation in its 100 percent owned in-situ oil sands leases at Hoole, which is located 10 kilometers northeast of Wabasca-Desmarais, Alberta. Since 2004, approximately \$112 million has been invested in land acquisitions, stratigraphic drilling, engineering studies, and environmental field programs to bring this project (the "Hoole Project") to a stage capable of development. Front-end engineering and design work for the initial 10,000 Bbl/d phase of the Hoole Project ("Hoole Grand Rapids Phase 1") has been completed and the Alberta Energy Regulator approved the Hoole Grand Rapids Phase 1 project in the second quarter of 2014.

Given the current commodity-price environment, no significant additional expenditures are planned for the Hoole Grand Rapids Phase 1 project in the near term. Development of the project is contingent upon Cavalier obtaining financing and certain additional regulatory approvals. The Oil Sands Lands are at the early stages of their evaluation and development, currently have no production, and there are no assurances that any of these lands will commence production, generate earnings, operate profitably or provide a return on investment at any time in the future.

The agreement governing the Cavalier Royalty does not impose any development commitments on Cavalier in respect of the Hoole Project or any of its other Oil Sands Lands, nor does it impose any terms or conditions on the use of the consideration paid for the Cavalier Royalty. Production from the Oil Sands Lands will not be subject to any royalty when the Western Canadian Select ("WCS") price is below US\$50 per barrel. At a WCS price of US\$50 per barrel, the royalty rate will be two percent and the rate will increase linearly to a maximum of 20 percent at a WCS price of US\$140 per barrel. As of December 31, 2016, the WCS price was US\$37.62 per barrel. The Cavalier Royalty will be payable based on Cavalier's realized bitumen price, net of diluent, transportation and storage costs. The Cavalier Royalty is secured by a lien over the Oil Sands Lands.

Shale Gas Properties

Paramount's shale gas holdings in the Liard and Horn River Basins in northeast British Columbia and the Northwest Territories include approximately 134 net sections of land with potential for natural gas production from the Besa River shale formation.

In 2015, the Company completed drilling operations at the Dunedin d-71-G vertical exploratory shale gas well and then moved to the c-37-D well at La Biche, where drilling operations continued until spring break-up. Drilling operations resumed at c-37-D in December 2015, and the well was drilled to target depth in March 2016. With the completion of drilling operations for the c-37-D well, the Company has secured its mineral rights in the region for up to another 10 years.

Fox Drilling

Fox Drilling owns seven triple-sized rigs, including two new walking rigs that were commissioned and brought into service in 2016. The Fox Drilling rigs are designed to drill the deep horizontal wells that industry is currently focusing on. All seven rigs were deployed on the Company's lands at the end of 2016, drilling wells at Karr-Gold Creek and Smoky/Resthaven.

CORPORATE

Year ended December 31	2016	2015
Interest and financing	77.6	108.4
Debt extinguishment	27.6	12.0
General and administrative	19.6	18.0
Share-based compensation	21.6	14.0
Foreign exchange	(43.7)	61.1
Other	(0.7)	0.3
Segment loss	102.0	213.8

The Corporate segment loss decreased to \$102.1 million in 2016 compared to \$213.8 million in 2015.

Interest and financing expense was \$77.6 million in 2016, a decrease of \$30.8 million from 2015, as a result of lower average debt balances in 2016. Debt extinguishment expense of \$27.6 million was recorded in 2016, including \$13.5 million of redemption premiums related to the senior unsecured notes due 2019 (the "2019 Notes") and \$13.9 million of unamortized financing fees related to the 2019 Notes redeemed and the 2023 Notes assumed by the Acquiror. In 2015, the Company recorded \$12.0 million of debt extinguishment expense related to the June 2015 redemption of the Company's senior unsecured notes due 2017 (the "2017 Notes").

Share-based compensation in 2016 includes \$13.8 million related to options cancelled in the year. The foreign exchange gain of \$43.7 million for the year ended December 31, 2016 mainly related to the US\$450 million 2023 Notes assumed by the Acquiror on the closing of the Musreau Disposition.

INCOME TAX

Income tax expense in 2016 totaled \$156.1 million. The Company recognized \$186.7 million of previously unrecognized deferred tax assets in 2016, which reduced income tax expense in the year.

Tax Pools

As at December 31, 2016	
Canadian resource pools and undepreciated capital cost	352.8
Non-capital losses	658.0
Financing costs and other	14.4
Total federal tax pools	1,025.2

EXPLORATION AND CAPITAL EXPENDITURES

Year ended December 31	2016	2015
Geological and geophysical	2.9	4.4
Drilling, completion and tie-ins	148.5	314.0
Facilities and gathering	19.6	111.5
Principal Properties Capital ⁽¹⁾	171.0	429.9
Land and property acquisitions and capitalized interest	11.0	8.1
Principal Properties including land and property acquisitions and capitalized interest	182.0	438.0
Strategic Investments ⁽²⁾	22.0	62.0
Corporate	1.1	1.3
	205.1	501.3
Principal Properties Capital by COU ⁽¹⁾		
Grande Prairie	94.9	66.2
Kaybob	63.0	293.1
Southern, Northern & Other	13.1	70.6
	171.0	429.9

(1) Principal Properties Capital includes capital expenditures and geological and geophysical costs related to the Company's Principal Properties, excluding land acquisitions and capitalized interest.

(2) Strategic Investments in 2015 included \$1.5 million of capitalized interest.

Principal Properties Capital was \$171.0 million in 2016, including \$52.5 million related to the Musreau Assets, compared to \$429.9 million in 2015. Development activities following the Musreau Disposition are focused on a planned 27 (27.0 net) well horizontal Montney drilling and completion program at Karr-Gold Creek that commenced in mid-2016 (the "Karr Program") and the expansion of the Karr-Gold Creek 6-18 Facility to double its capacity to 80 MMcf/d. The total cost of the expansion of the 6-18 Facility is estimated to be approximately \$35 million, of which \$20 million has been incurred to December 31, 2016.

Paramount has spud 20 wells in the Karr Program to date and plans to spud an additional seven wells at Karr-Gold Creek in 2017. By the end of 2017, the Company expects to have completed up to 22 of the 27 wells, with the remaining wells to be completed in 2018. The Karr Program wells will be brought on production through 2017 and 2018 to fill the expanded 6-18 Facility.

Strategic Investments capital expenditures in 2016 included \$19.3 million related to the Company's exploratory Shale Gas Properties in northeast British Columbia.

Wells drilled were as follows:

	2016		2015	
	Gross ⁽¹⁾	Net ⁽²⁾	Gross ⁽¹⁾	Net ⁽²⁾
Natural gas – Ongoing Operations	12	12	13	11
Natural gas – Musreau Assets	11	11	21	20
Total	23	23	34	31

(1) Gross is the number of wells in which Paramount has a working interest or a royalty interest that may be converted to a working interest.

(2) Net is the aggregate number of wells obtained by multiplying each gross well by Paramount's percentage of working interest.

LIQUIDITY AND CAPITAL RESOURCES

Paramount manages its capital structure to support current and future business plans and periodically adjusts the structure in response to changes in economic conditions and the risk characteristics of the Company's underlying assets and operations. Paramount may adjust its capital structure by issuing or repurchasing shares, altering debt levels, modifying capital spending programs, acquiring or disposing of assets, and participating in joint ventures, the availability of any such means being dependent upon market conditions.

Net Cash (Debt)

As at December 31	2016	2015
Adjusted working capital surplus (deficit) ⁽¹⁾	565.9	(37.9)
Limited-recourse demand facilities	–	(100.9)
Bank credit facility	–	(693.0)
2019 Notes ⁽²⁾	–	(450.0)
2023 Notes ⁽²⁾	–	(622.8)
Net cash (debt)	565.9	(1,904.6)

(1) Adjusted working capital excludes accounts payable and accrued liabilities relating to the Company's obligation to renounce qualifying expenditures for flow-through share issuances (December 31, 2016 – nil, December 31, 2015 – \$4.1 million), risk management assets and liabilities and limited-recourse demand facilities.

(2) Excludes unamortized issue premiums and financing costs.

Shareholders' Equity

As at December 31	2016	2015
Share capital	1,639.5	1,647.0
Accumulated deficit	(152.2)	(1,197.6)
Reserves	147.5	99.3
Total shareholders' equity	1,634.8	548.7

Paramount had an adjusted working capital surplus at December 31, 2016 of \$565.9 million compared to a deficit of \$37.9 million at December 31, 2015. The adjusted working capital surplus at December 31, 2016 included \$621.9 million of cash and cash equivalents, \$119.0 of Investments in Securities for distribution, \$23.9 million of accounts receivable, \$1.7 million of prepaid amounts, a dividend payable of \$119.0 million and \$81.6 million of accounts payable and accrued liabilities.

In April 2016, proceeds from the Midstream Sale were used to pay down the Company's bank credit facility. In August 2016, the Company repaid the remaining balance owing on its bank credit facility in connection with the Musreau Disposition.

Paramount expects to fund its planned 2017 operations, obligations and capital expenditures with cash and cash equivalents and funds flow from operations.

Limited-Recourse Demand Facilities

In June 2016, the Cavalier limited-recourse demand credit facility, which had an outstanding balance of \$37.5 million as at December 31, 2015, was repaid and cancelled.

In September 2016, the Fox Drilling limited-recourse demand credit facility, which had an outstanding balance of \$63.4 million as at December 31, 2015, was repaid and cancelled.

Bank Credit Facility

The Company has a \$100 million revolving bank credit facility (the "Facility"). Borrowings under the Facility bear interest at prime lending rates, US base rates, bankers' acceptance rates, or LIBOR rates, as selected at the discretion of the Company, plus an applicable margin which is dependent upon the Company's debt-to-cash flow ratio. The Facility is secured by a first fixed and floating charge over substantially all of the assets of Paramount, excluding the assets of Fox Drilling and Cavalier.

The borrowing base governs the maximum amount which can be drawn on the Facility. The borrowing base is subject to review and re-determination on a semi-annual basis and more frequently in certain other circumstances. The borrowing base amount is based on the Company's reserves, lenders' projections of future commodity prices and the value attributed to Paramount's equity investments and other assets, among other factors.

The current revolving period of the Facility ends on April 28, 2017. In the event the revolving period is not extended, any undrawn availability would be cancelled and any amounts then outstanding would be permitted to remain outstanding on a non-revolving basis until April 28, 2018, the current maturity date of the Facility.

At December 31, 2016, no amounts were drawn on the Facility. Paramount had undrawn letters of credit outstanding totaling \$20.4 million at December 31, 2016 that reduce the amount available to be drawn under the Facility.

Senior Notes

In 2016, the Company redeemed all \$450 million aggregate principal amount of its 7% percent 2019 Notes. The Company was discharged and released from all obligations and covenants under the 2019 Notes indenture and the 2019 Notes.

In connection with the Musreau Disposition, the Acquiror assumed all US\$450 million aggregate principal amount of Paramount's 2023 Notes in August 2016 and the Company was discharged and released from all obligations and covenants under the 2023 Notes indenture and the 2023 Notes.

Share Capital

Paramount's authorized share capital consists of an unlimited number of Common Shares without par value and an unlimited number of preferred shares issuable in series. At December 31, 2016, 105,784,070 (December 31, 2015 – 106,212,487) Common Shares were outstanding, net of 2,865 (December 31, 2015 – 21,508) Common Shares held in trust under the Company's stock incentive program, and no preferred shares were outstanding.

Paramount implemented a normal course issuer bid ("NCIB") on October 13, 2016. The NCIB will terminate on the earlier of: (i) October 12, 2017; and (ii) the date on which the maximum number of Common Shares that can be acquired pursuant to the NCIB are purchased. Purchases of Common Shares under the NCIB will be effected through the facilities of the TSX or alternative Canadian trading systems at the market price at the time of purchase. Paramount may purchase up to 5,441,602 Common Shares under the NCIB. Pursuant to the rules of the TSX, the maximum number of Common Shares that the Company may purchase under the NCIB in any one day is 188,705 Common Shares. Paramount may also make one block purchase per calendar week which exceeds such daily purchase restriction, subject to the rules of the TSX. Any Common Shares purchased pursuant to the NCIB will be cancelled by the Company. Any shareholder may obtain, for no charge, a copy of the notice in respect of the NCIB filed with the TSX by contacting the Company at 403-290-3600. To March 3, 2017, the Company has purchased and cancelled 622,900 Common Shares pursuant to the NCIB at a total cost of \$9.7 million.

In April 2015, pursuant to a private placement, Paramount issued 0.9 million Common Shares to arms-length investors on a "flow-through" basis in respect of Canadian exploration expenses at a price of \$41.35 per share for gross proceeds of \$37.2 million. The Company has incurred sufficient qualifying expenditures to satisfy commitments related to the issuance.

At March 3, 2017, Paramount had 106,138,675 Common Shares and 3,913,700 Paramount Options outstanding, of which 460,000 Paramount Options are exercisable.

FOURTH QUARTER 2016 RESULTS

Netback

Three months ended December 31	2016		2015		2015	
	(\$/Boe) ⁽²⁾		Total	Ongoing Operations ⁽¹⁾		
Natural gas revenue	13.5	3.10	37.3	2.57	11.8	2.44
Condensate and oil revenue	16.4	60.49	42.8	46.60	14.3	46.36
Other NGLs revenue ⁽³⁾	2.1	22.16	10.6	12.59	1.0	16.92
Royalty and sulphur revenue	0.3	–	0.6	–	0.4	–
Petroleum and natural gas sales	32.3	29.52	91.3	21.82	27.5	23.45
Royalties	(0.1)	(0.08)	(3.1)	(0.73)	(1.2)	(1.06)
Operating expense	(10.9)	(10.00)	(23.0)	(5.49)	(13.1)	(11.12)
Transportation and NGLs processing ⁽⁴⁾	(4.3)	(3.91)	(16.3)	(3.90)	(2.6)	(2.24)
Netback	17.0	15.53	48.9	11.70	10.6	9.03
Commodity contract settlements	8.2	7.54	4.9	1.18		
Netback including commodity contract settlements	25.2	23.07	53.8	12.88		

(1) Excludes the results of the Musreau Assets.

(2) Natural gas revenue shown per Mcf.

(3) Other NGLs means ethane, propane and butane.

(4) Includes downstream natural gas, NGLs and oil transportation costs and NGLs fractionation costs incurred by the Company.

Fourth quarter 2016 petroleum and natural gas sales were \$32.3 million, a decrease of \$59.0 million from the fourth quarter of 2015, primarily due to lower sales volumes because of the August 2016 Musreau Disposition, partially offset by higher commodity prices.

The impact of changes in sales volumes and prices on petroleum and natural gas sales are as follows:

	Natural Gas	Condensate and Oil	Other NGLs	Royalty and Sulphur	Total
Three months ended December 31, 2015	37.3	42.8	10.6	0.6	91.3
Effect of changes in sales volumes	(26.1)	(30.2)	(9.4)	–	(65.7)
Effect of changes in prices	2.3	3.8	0.9	–	7.0
Change in royalty and sulphur revenue	–	–	–	(0.3)	(0.3)
Three months ended December 31, 2016	13.5	16.4	2.1	0.3	32.3

Royalties decreased \$3.0 million to \$0.1 million in the fourth quarter of 2016, primarily as a result of the Musreau Disposition and gas cost allowance adjustments related to prior periods.

Operating expense decreased \$12.1 million to \$10.9 million in the fourth quarter of 2016 compared to \$23.0 million in the same period in 2015, primarily due to the Musreau Disposition and lower operating costs in the Grande Prairie COU related to lower rates for processing and lower production. Operating costs in the fourth quarter of 2016 were also reduced by \$2.5 million as a result of operating costs for prior quarters being lower than originally estimated, including costs related to the Musreau Assets. Excluding the impact of these differences, the Company's operating costs in the fourth quarter of 2016 were approximately \$12.30 per Boe.

Transportation and NGLs processing expense decreased \$12.0 million to \$4.3 million in the fourth quarter of 2016 compared to \$16.3 million in the same period in 2015, primarily due to the Musreau Disposition, partially offset by increased transportation costs related to incremental firm service capacity contracted for the Company's Deep Basin production volumes.

Sales Volumes

	Three months ended December 31											
	Natural Gas (MMcf/d)			Condensate and Oil (Bbl/d)			Other NGLs (Bbl/d)			Total (Boe/d)		
	2016	2015	% Change	2016	2015	% Change	2016	2015	% Change	2016	2015	% Change
Grande Prairie ⁽¹⁾	26.5	35.4	(25)	2,208	2,518	(12)	275	399	(31)	6,901	8,813	(22)
Kaybob ⁽¹⁾	11.5	11.3	2	336	392	(14)	561	153	267	2,812	2,428	16
Northern	6.9	3.2	116	113	101	12	100	8	NM	1,356	634	114
Southern	2.6	2.6	–	286	348	(18)	110	101	9	832	890	(7)
Ongoing Operations	47.5	52.5	(10)	2,943	3,359	(12)	1,046	661	58	11,901	12,765	(7)
Musreau Assets	–	105.3	(100)	–	6,632	(100)	–	8,514	(100)	–	32,701	(100)
Total	47.5	157.8	(70)	2,943	9,991	(71)	1,046	9,175	(89)	11,901	45,466	(74)

(1) Excludes the results of the Musreau Assets

NM Not meaningful

Sales volumes from Ongoing Operations decreased seven percent to 11,901 Boe/d in the fourth quarter of 2016 compared to 12,765 Boe/d in the same period in 2015. The decrease was primarily due to natural production declines on existing wells and non-core dispositions in the Grande Prairie COU, partially offset by sales volumes from new Montney formation wells brought on production at Karr-Gold Creek and at Birch and less downtime at a third-party operated processing facility disruptions at Smoky/Resthaven.

Commodity Prices

Key monthly average commodity price benchmarks and foreign exchange rates are as follows:

Three months ended December 31	2016	2015	% Change
Natural Gas			
Paramount realized price (\$/Mcf)	3.10	2.57	21
AECO daily spot (\$/GJ)	2.93	2.34	25
AECO monthly index (\$/GJ)	2.62	2.51	4
Malin (US\$/MMbtu)	3.02	2.29	32
Crude Oil			
Paramount average condensate and oil price (\$/Bbl)	60.49	46.60	30
Edmonton Light Sweet (\$/Bbl)	60.76	52.55	16
West Texas Intermediate (US\$/Bbl)	49.29	42.18	17
Foreign Exchange			
\$CDN / 1 \$US	1.33	1.34	(1)

Net Income (Loss)

Three months ended December 31	2016	2015
Petroleum and natural gas sales	32.4	91.3
Royalties	(0.1)	(3.1)
Revenue	32.3	88.2
Gain (loss) on financial commodity contracts	(6.3)	19.8
	26.0	108.0
(Expenses) Income		
Operating expense	(10.9)	(23.0)
Transportation and NGLs processing	(4.3)	(16.3)
General and administrative	(6.5)	(5.7)
Share-based compensation	(3.6)	(3.1)
Depletion and depreciation	112.0	(340.7)
Exploration and evaluation	93.6	(195.8)
Gain on sale of oil and gas assets	9.6	0.1
Interest and financing	(5.5)	(29.4)
Accretion of asset retirement obligations	(1.0)	(1.4)
Foreign exchange	(0.2)	(20.7)
Debt extinguishment	(9.3)	-
Loss from equity-accounted investments	(2.7)	(3.1)
Gain on sale of Investment in Securities	3.4	-
Write-own of Investment in Securities	(0.1)	(4.2)
Other income	0.8	2.6
Income tax recovery (expense)	11.1	(66.3)
	186.4	(707.0)
Net income (loss)	212.4	(599.0)

Three months ended December 31	2016	2015
Principal Properties	129.4	(305.7)
Strategic Investments	93.3	(170.9)
Corporate	(21.4)	(56.1)
Income tax recovery (expense)	11.1	(66.3)
Net income (loss)	212.4	(599.0)

Paramount recorded net income of \$212.4 million for the three months ended December 31, 2016, which included the reversal of \$133.2 million of previously recorded impairment charges related to petroleum and natural gas assets and a \$99.2 million gain recognized on the sale of the Cavalier Royalty. A net loss of \$599.0 million was recorded in the same period of 2015. Significant factors contributing to the change are shown below:

Three months ended December 31	
Net loss – 2015	(599.0)
<ul style="list-style-type: none"> • Lower depletion and depreciation due to impairment reversals totaling \$133.2 million and asset dispositions in 2016 and because 2015 included impairment charges of \$263.7 million • Exploration and evaluation income in 2016 because of a \$99.2 million gain in respect of the sale of the Cavalier Royalty compared to an expense in 2015 which included \$184.1 million of impairment charges • Income tax recovery in 2016 compared to an expense in 2015 • Lower interest and financing expense due to lower average debt balances in 2016 • Lower foreign exchange expense in 2016 • Gain on sale of oil and gas assets in 2016 mainly related to non-core asset dispositions • Lower write-downs of Investments in Securities in 2016 • Gain on sale of investments in securities in 2016 • Lower Netback primarily due to the Musreau Disposition • Loss on commodity contracts in 2016 compared to a gain in 2015 • Debt extinguishment expense in 2016 • Other 	<p style="text-align: right;">452.7</p> <p style="text-align: right;">289.4</p> <p style="text-align: right;">77.4</p> <p style="text-align: right;">23.9</p> <p style="text-align: right;">20.5</p> <p style="text-align: right;">9.5</p> <p style="text-align: right;">4.1</p> <p style="text-align: right;">3.4</p> <p style="text-align: right;">(31.9)</p> <p style="text-align: right;">(26.1)</p> <p style="text-align: right;">(9.3)</p> <p style="text-align: right;">(2.2)</p>
Net income – 2016	212.4

Funds Flow from Operations ⁽¹⁾

The following is a reconciliation of funds flow from operations to the nearest GAAP measure:

Three months ended December 31	2016	2015
Cash from (used in) operating activities	(6.4)	10.4
Change in non-cash working capital	19.6	7.2
Geological and geophysical expenses	0.2	2.2
Asset retirement obligations settled	0.9	1.2
Funds flow from operations	14.3	21.0
Funds flow from operations (\$/Boe)	13.10	5.02
Funds flow from operations (\$/share - diluted)	0.13	0.20

(1) Refer to the advisories concerning Non-GAAP measures in the Advisories section of this document.

Funds flow from operations in the fourth quarter of 2016 was \$14.3 million compared to \$21.0 million in the same period in 2015. Significant factors contributing to the change are shown below:

Three months ended December 31	
Funds flow from operations – 2015	21.0
• Lower Netback primarily due to the Musreau Disposition	(31.9)
• Lower interest and financing expense due to lower average debt balances in 2016	23.5
• Higher realized gains on financial commodity contracts	3.3
• Other	(1.6)
Funds flow from operations – 2016	14.3

Exploration and Capital Expenditures

Exploration and Capital expenditures for the Company's Principal Properties in the fourth quarter of 2016 totaled \$78.2 million, with the majority of spending directed towards drilling and completing horizontal Montney wells and advancing the 6-18 Facility expansion at the Company's Karr-Gold Creek development.

QUARTERLY INFORMATION

	2016				2015			
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Petroleum and natural gas sales	32.3	51.7	73.6	91.2	91.3	110.7	94.6	80.2
Net income (loss)	212.4	1,029.4	(30.6)	(46.0)	(599.0)	(171.8)	(60.2)	(70.3)
Per share – basic (\$/share)	2.01	9.69	(0.29)	(0.43)	(5.64)	(1.62)	(0.57)	(0.67)
Per share – diluted (\$/share)	1.99	9.64	(0.29)	(0.43)	(5.64)	(1.62)	(0.57)	(0.67)
Funds flow from operations	14.3	3.8	(4.9)	22.4	21.0	36.9	19.6	15.7
Per share – basic (\$/share)	0.14	0.04	(0.05)	0.21	0.20	0.35	0.19	0.15
Per share – diluted (\$/share)	0.13	0.04	(0.05)	0.21	0.20	0.35	0.19	0.15
Sales volumes								
Natural gas (MMcf/d)	47.5	88.6	129.8	153.9	157.8	181.8	154.4	148.6
Condensate and oil (Bbl/d)	2,943	5,335	9,490	13,245	9,991	10,214	7,595	6,583
Other NGLs (Bbl/d)	1,046	4,687	9,764	11,259	9,175	9,483	9,282	6,968
Total (Boe/d)	11,901	24,786	40,890	50,161	45,466	49,990	42,604	38,317
Average realized price								
Natural gas (\$/Mcf)	3.10	2.65	1.49	2.09	2.57	3.01	2.74	2.99
Condensate and oil (\$/Bbl)	60.49	51.15	52.83	42.28	46.60	52.43	65.66	48.16
Other NGLs (\$/Bbl)	22.16	11.11	11.19	10.31	12.59	11.42	12.18	16.43
Total (\$/Boe)	29.52	22.66	19.79	19.98	21.82	24.07	24.40	23.26

Significant Items Impacting Quarterly Results

Quarterly earnings variances include the impacts of changing production volumes and market prices.

- Fourth quarter 2016 earnings include a \$133.2 million reversal of impairments of oil and gas assets recorded in prior years, a \$99.2 million gain recorded in respect of the Cavalier Royalty and the recognition of \$61.0 million of previously unrecognized deferred tax assets.
- Third quarter 2016 earnings include the impacts related to the Musreau Disposition, including a \$1.2 billion gain on sale, lower depletion and depreciation expense, higher income tax expense and lower Netback.
- Second quarter 2016 earnings include a \$131.8 million gain on the sale of oil and gas assets primarily in respect of the Midstream Sale, partially offset by \$17.7 million of share-based compensation expense.
- First quarter 2016 earnings include a foreign exchange gain of \$40.3 million and a \$13.7 million gain on commodity contracts.
- Fourth quarter 2015 earnings include \$241.5 million of aggregate impairment write-downs of property, plant and equipment, \$184.1 million of impairment write-offs of exploration and evaluation assets and deferred tax income expense of \$66.3 million.
- Third quarter 2015 earnings include \$100.7 million of depletion and depreciation, a \$22.2 million impairment write-down of oil and gas properties, a \$73.0 million write-down of investments in securities and a foreign exchange loss of \$41.5 million, partially offset by \$38.1 million of gains on commodity contracts.
- Second quarter 2015 earnings include \$82.9 million of depletion and depreciation expense and \$12.0 million of debt extinguishment expense in respect of the redemption of the 2017 Notes, partially offset by an income tax recovery of \$38.5 million.
- First quarter 2015 earnings include \$77.4 million of depletion and depreciation expense and a \$8.9 million net loss on the sale of oil and gas properties.

OTHER INFORMATION

Related Party Transactions

Paramount engages in transactions with Trilogy in the normal course of business, including joint operations. Paramount accounts for its investment in Trilogy using the equity method of investment accounting as, in management's judgement, it has significant influence as a result of common directors and members of senior management. Because of this, Paramount is considered related to Trilogy. All transactions between Paramount and Trilogy are recorded at their exchange amounts.

During 2016, Paramount charged \$0.4 million (2015 – \$0.5 million) to Trilogy in respect of operational and administrative services. Paramount charged \$4.2 million (2015 – \$3.4 million) to Trilogy and was charged \$8.6 million (2015 – \$2.6 million) by Trilogy in respect of joint operations. As of December 31, 2016, Paramount had a net receivable balance due from Trilogy of \$0.2 million (2015 – net payable of \$0.2 million).

Contractual Obligations

Paramount had the following contractual obligations at December 31, 2016:

	2017	2018-2019	2020-2021	After 2021	Total
Processing and transportation commitments ⁽¹⁾	40	98	95	229	462
Asset retirement obligations ⁽²⁾	–	3	48	161	212
Operating leases and other	9	5	4	1	19
	49	106	147	391	693

(1) Certain transportation and processing commitments are secured by outstanding letters of credit totaling \$5.1 million at December 31, 2016 (2015 - \$104.6 million).

(2) Asset retirement obligations estimated as at December 31, 2016. Estimated costs and timing of settlement are revised from time-to-time based on new information.

Processing and transportation commitments mainly relate to long-term firm service arrangements for the processing and transportation of natural gas and Liquids.

Contingencies

In the normal course of Paramount's operations, the Company may become involved in, named as a party to, or be the subject of, various legal proceedings, including regulatory proceedings, tax proceedings and legal actions. The outcome of outstanding, pending or future proceedings cannot be predicted with certainty and may be determined adversely to the Company and as a result, could have a material adverse effect on the Company. Even if Paramount prevails in any such legal proceedings, they could be costly and time-consuming and divert the attention of management and key personnel from the Company's core business operations.

In 2016, a release occurred from a non-operated pipeline in which the Company owns a 50 percent interest. The operator, and owner of the remaining 50 percent, has initiated response, containment and remediation activities ("Response Activities"). Total costs to complete the Response Activities are estimated at approximately \$45 million. It is Paramount's assessment that it is not responsible for the costs of the Response Activities and as a result, no provision has been recorded in the Company's financial statements.

Risk Factors

A description of the most significant risk factors related to Paramount and its business is contained in Paramount's current Annual Information Form under the heading "Risk Factors".

The Company cannot fully protect against all of these potential risks. Some of them cannot be insured against, and the coverage that can be obtained with respect to those that are insurable will be subject to exclusions and monetary limits. Accordingly, Paramount may be exposed to liabilities that are outside the scope of its insurance, are only partially covered by it, or that Paramount could not insure against (either at all or because of high premium costs or for other reasons). The occurrence of a significant event against which Paramount is not fully insured could have a material adverse effect on the Company.

CHANGE IN ACCOUNTING POLICIES

There were no new or amended accounting standards adopted by the Company for the year ended December 31, 2016.

Future Changes in Accounting Standards

In May 2014, the International Accounting Standards Board ("IASB") issued IFRS 15 – *Revenue From Contracts With Customers*, which establishes a single revenue recognition framework that applies to contracts with customers. The standard requires an entity to recognize revenue to reflect the transfer of goods and services for the amount it expects to receive, when control is transferred to the purchaser. IFRS 15 is effective for years beginning on or after January 1, 2018. The Company is currently evaluating the impact of the IFRS on its Consolidated Financial Statements.

In July 2014, the IASB issued IFRS 9 – *Financial Instruments*, which sets out the recognition and measurement requirements for financial instruments and some contracts to buy or sell non-financial items. IFRS 9 proposes a single model of classifying and measuring financial assets and liabilities and provides for only two classification categories: amortized cost and fair value. IFRS 9 is effective for years beginning on or after January 1, 2018. The Company is currently evaluating the impact of the IFRS on its Consolidated Financial Statements.

In January 2016, the IASB issued IFRS 16 – *Leases*, which replaces IAS – 17 *Leases* and related interpretations. IFRS 16 eliminates the classification of leases as finance or operating and introduces a single lessee accounting model for recognition and measurement, which will require the recognition of assets and liabilities for most leases. IFRS 16 is effective for years beginning on or after January 1, 2019. The Company is currently evaluating the impact of the IFRS on its Consolidated Financial Statements.

DISCLOSURE CONTROLS AND PROCEDURES

As of the year ended December 31, 2016, an evaluation of the effectiveness of Paramount's disclosure controls and procedures, as defined by the rules of the Canadian Securities Administrators, was performed by the Company's management with the oversight of the chief executive officer and chief financial officer. Based upon that evaluation, the Company's chief executive officer and chief financial officer have concluded that as of the end of that fiscal year, the Company's disclosure controls and procedures are effective in ensuring that information required to be disclosed by the Company is (i) recorded, processed, summarized and reported within the time periods specified in Canadian securities law; and (ii) accumulated and communicated to the Company's management, including its chief executive officer and chief financial officer as appropriate, to allow timely decisions regarding required disclosure.

It should be noted that while the Company's chief executive officer and chief financial officer believe that the Company's disclosure controls and procedures provide a reasonable level of assurance that they are effective, they do not expect that the Company's disclosure controls and procedures or internal control over financial reporting will prevent all errors and fraud. A control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met.

INTERNAL CONTROLS OVER FINANCIAL REPORTING

Management has assessed the effectiveness of the Company's internal controls over financial reporting ("ICFR") as defined under National Instrument 52-109 "*Certification of Disclosure in Issuers' Annual and Interim Filings*" as at December 31, 2016. In making its assessment, Management used the Committee of Sponsoring Organizations of the Treadway Commission Framework in Internal Control – Integrated Framework (2013) to evaluate the effectiveness of the Company's ICFR. Based on this assessment, Management has concluded that the Company's ICFR was effective as of December 31, 2016.

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 policies or procedures may deteriorate.

Changes in Internal Control Over Financial Reporting

During the year ended December 31, 2016, there was no change in the Company's ICFR that materially affected, or is reasonably likely to materially affect, the Company's ICFR.

CRITICAL ACCOUNTING ESTIMATES

The timely preparation of financial statements requires Management to make judgments, estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and disclosures regarding contingent assets and liabilities. Estimates and assumptions are regularly evaluated and are based on Management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Changes in judgments, estimates and assumptions based on new information could result in a material change to the carrying amount of assets or liabilities and have a material impact on assets, liabilities, revenues and expenses recognized in future periods. The following is a description of the accounting judgments, estimates and assumptions that are considered significant.

Exploration or Development

The Company is required to apply judgment when designating a project as exploration and evaluation or development, including assessments of geological and technical characteristics and other factors related to each project.

Exploration and Evaluation Projects

The accounting for E&E projects requires Management to make judgments as to whether exploratory projects have discovered economically recoverable quantities of petroleum and natural gas, which requires the quantity and realizable value of such petroleum and natural gas to be estimated. Previous estimates are sometimes revised as new information becomes available. Where it is determined that an exploratory project did not discover economically recoverable petroleum and natural gas, the costs are written-off as E&E expense.

If hydrocarbons are encountered, but further appraisal activity is required, the exploratory costs remain capitalized as long as sufficient progress is being made in assessing whether the recovery of the petroleum and natural gas is economically viable. The concept of "sufficient progress" is a judgmental

area, and it is possible to have exploratory costs remain capitalized for several years while additional exploratory activities are carried out or the Company seeks government, regulatory or partner approval for development plans. Exploration and evaluation assets are subject to ongoing technical, commercial and Management review to confirm the continued intent to establish the technical feasibility and commercial viability of the discovery. When Management is making this assessment, changes to project economics, expected quantities of petroleum and natural gas, expected production techniques, drilling results, estimated capital expenditures and production costs, results of other operators in the region and access to infrastructure and potential infrastructure expansions are important factors. Where it is determined that an exploratory project is not economically viable, the costs are written-off as E&E expense.

Reserves Estimates

Reserves engineering is an inherently complex and subjective process of estimating underground accumulations of petroleum and natural gas. The process relies on judgments based on the interpretation of available geological, geophysical, engineering and production data. The accuracy of a reserves estimate is a function of the quality and quantity of available data, the interpretation of such data, the accuracy of various economic assumptions and the judgment of those preparing the estimate. Because these estimates depend on many assumptions, all of which may differ from actual results, reserves estimates, commodity price estimates and estimates of future net revenue will be different from the sales volumes ultimately recovered and net revenues actually realized. Changes in market conditions, regulatory matters, the results of subsequent drilling, testing and production and other factors may require revisions to the original estimates.

Estimates of reserves impact: (i) the assessment of whether a new well has found economically recoverable reserves; (ii) depletion rates; and (iii) the estimated recoverable amount of petroleum and natural gas properties used from time-to-time in impairment and impairment reversal assessments, all of which could have a material impact on earnings.

Estimates of Recoverable Amounts

Estimates of recoverable amounts used in impairment and impairment reversal tests often incorporate level three hierarchy inputs including estimated volumes and future net revenues from oil and natural gas reserves, contingent resource estimates, future net cash flow estimates related to other long-lived assets and internal and external market metrics used to estimate value based on comparable assets and transactions. By their nature, such estimates are subject to measurement uncertainty. Changes in such estimates, and differences between actual and estimated amounts, could have a material impact on earnings.

Determination of CGUs

The recoverability of the carrying value of oil and gas properties is generally assessed at the CGU level. The determination of the properties and other assets grouped within a particular CGU is based on Management's judgment with respect to the integration between assets, shared infrastructure and cash flows and the overall significance of individual properties. Changes in the assets comprising CGUs could have an impact on estimated recoverable amounts used in impairment assessments and could have a material impact on earnings.

Equity Accounted Investments

The Company accounts for its investment in Trilogy under the equity method of investment accounting although it holds less than 20 percent of the voting power because, in Management's judgment, it has significant influence as a result of common directors and members of senior management.

Investments in Securities

The Company's Investments in Securities that are accounted for as available-for-sale financial instruments are assessed at the end of each reporting period to determine whether there is any objective evidence of impairment. Management is required to exercise judgment in determining whether a decrease in the fair value of an investment below its carrying value is significant or prolonged, which would require an impairment charge to be recognized. Management is also required to exercise judgment in estimating the fair value of investments in the securities of private corporations that are not publicly traded.

Provisions

A provision is recognized where the Company has determined that it has a present obligation arising from past events and the settlement of the obligation is expected to result in an outflow of economic benefits. The determination of whether the Company has a present obligation arising from past events requires Management to exercise judgement as to the facts and circumstances of the event and the extent of any expected obligations of Paramount. Changes in facts and circumstances as a result of new information and other developments may impact Management's assessment of the Company's obligations, if any, in respect of such events. Changes in such estimates could have a material impact on assets, liabilities, revenues, expenses, and earnings.

Asset Retirement Obligations

Estimates of asset retirement costs are based on assumptions regarding the methods, timing, economic environment and regulatory standards that are expected to exist at the time assets are retired. Management adjusts estimated amounts periodically as assumptions are updated to incorporate new information. Actual payments to settle the obligations may differ materially from amounts estimated.

Share-Based Payments

The Company estimates the grant date value of stock options awarded using the Black-Scholes-Merton model. The inputs used to determine the estimated value of the options are based on assumptions regarding share price volatility, the expected life of the options, expected forfeiture rates and future interest rates. By their nature, these inputs are subject to measurement uncertainty and require Management to exercise judgment in determining which assumptions are the most appropriate.

Income Taxes

Accounting for income taxes is a complex process requiring Management to interpret frequently changing laws and regulations and make judgments and estimates related to the application of tax law, the timing of temporary difference reversals and the likelihood of realizing deferred income tax assets. All tax filings are subject to subsequent government audits and potential reassessment. These interpretations and judgments, and changes related to them, impact current and deferred tax provisions, the carrying value of deferred income tax assets and liabilities and could have a material impact on earnings.

ADVISORIES

Forward-looking Information

Certain statements in this document constitute forward-looking information under applicable securities legislation. Forward-looking information typically contains statements with words such as "anticipate", "believe", "estimate", "will", "expect", "plan", "schedule", "intend", "propose", or similar words suggesting future outcomes or an outlook. Forward-looking information in this document includes, but is not limited to:

- projected production and sales volumes and the timing thereof;
- forecast capital expenditures, operating costs (including anticipated reductions in per unit operating costs in the fourth quarter of 2017) and remaining cash on hand at the end of 2017;
- exploration, development and associated operational plans and strategies (including planned drilling and completion programs, well tie-ins and facility expansions, and the anticipated timing, costs and results thereof, including in terms of increased well productivity and reserves, capital and operational efficiencies and environmental benefits);
- scheduled outages of third-party processing facilities including the timing, duration and impact thereof;
- the timing and cost of future abandonment and reclamation obligations;
- estimated reserves and the undiscounted and discounted net present value of future net revenues therefrom; and
- general business strategies and objectives.

Such forward-looking information is based on a number of assumptions which may prove to be incorrect. Assumptions have been made with respect to the following matters, in addition to any other assumptions identified in this document:

- future natural gas and Liquids prices;
- royalty rates, taxes and capital, operating, general & administrative and other costs;
- foreign currency exchange rates and interest rates;
- general economic and business conditions;
- the ability of Paramount to obtain the required capital to finance its exploration, development and other operations;
- the ability of Paramount to obtain equipment, services, supplies and personnel in a timely manner and at an acceptable cost to carry out its activities;
- the ability of Paramount to secure adequate product processing, transportation, de-ethanization, fractionation, and storage capacity on acceptable terms;
- the ability of Paramount to market its natural gas and Liquids successfully to current and new customers;
- the ability of Paramount and its industry partners to obtain drilling success (including in respect of anticipated production volumes, reserves additions, Liquids yields and resource recoveries) and operational improvements, efficiencies and results consistent with expectations;
- the timely receipt of required governmental and regulatory approvals; and
- anticipated timelines and budgets being met in respect of drilling programs and other operations (including well completions and tie-ins and the construction, commissioning and start-up of new and expanded facilities).

Although Paramount believes that the expectations reflected in such forward-looking information is reasonable, undue reliance should not be placed on it as Paramount can give no assurance that such expectations will prove to be correct. Forward-looking information is based on expectations, estimates and projections that involve a number of risks and uncertainties which could cause actual results to differ materially from those anticipated by Paramount and described in the forward-looking information. The material risks and uncertainties include, but are not limited to:

- fluctuations in natural gas and Liquids prices;
- changes in foreign currency exchange rates and interest rates;
- the uncertainty of estimates and projections relating to future revenue, future production, reserve additions, Liquids yields (including condensate to natural gas ratios), resource recoveries, royalty rates, taxes and costs and expenses;
- the ability to secure adequate product processing, transportation, de-ethanization, fractionation, and storage capacity on acceptable terms;
- operational risks in exploring for, developing and producing natural gas and Liquids;
- the ability to obtain equipment, services, supplies and personnel in a timely manner and at an acceptable cost;
- potential disruptions, delays or unexpected technical or other difficulties in designing, developing, expanding or operating new, expanded or existing facilities (including third-party facilities);
- industry wide processing, pipeline, de-ethanization and fractionation infrastructure outages, disruptions and constraints;
- risks and uncertainties involving the geology of oil and gas deposits;
- the uncertainty of reserves estimates;
- general business, economic and market conditions;
- the ability to generate sufficient cash flow from operations and obtain financing at an acceptable cost to fund planned exploration, development and operational activities and meet current and future obligations (including costs of anticipated new and expanded facilities and other projects and product processing, transportation, de-ethanization, fractionation and similar commitments);
- changes in, or in the interpretation of, laws, regulations or policies (including environmental laws);
- the ability to obtain required governmental or regulatory approvals in a timely manner, and to enter into and maintain leases and licenses;
- the effects of weather;
- the timing and cost of future abandonment and reclamation obligations and potential liabilities for environmental damage and contamination;
- uncertainties regarding aboriginal claims and in maintaining relationships with local populations and other stakeholders;
- the outcome of existing and potential lawsuits, regulatory actions, audits and assessments; and
- other risks and uncertainties described elsewhere in this document and in Paramount's other filings with Canadian securities authorities.

The foregoing list of risks is not exhaustive. For more information relating to risks, see the section titled "RISK FACTORS" in Paramount's current annual information form. The forward-looking information contained in this document is made as of the date hereof and, except as required by applicable securities law, Paramount undertakes no obligation to update publicly or revise any forward-looking statements or information, whether as a result of new information, future events or otherwise.

Non-GAAP Measures

In this document "Funds flow from operations", "Netback", "Net Cash (Debt)", "Adjusted working capital", "Exploration and Capital Expenditures", "Principal Properties Capital", "Investments in other entities – market value" and "Finding and development costs", collectively the "Non-GAAP Measures", are used and do not have any standardized meanings as prescribed by IFRS.

Funds flow from operations refers to cash from operating activities before net changes in operating non-cash working capital, geological and geophysical expenses and asset retirement obligation settlements. Funds flow from operations is commonly used in the oil and gas industry to assist management and investors in measuring the Company's ability to fund capital programs and meet financial obligations. Refer to the Consolidated Results and Fourth Quarter 2016 Results sections of the Company's Management's Discussion and Analysis for the periods and the calculation. Netback equals petroleum and natural gas sales less royalties, operating costs and transportation and NGLs processing costs. Netback is commonly used by management and investors to compare the results of the Company's oil and gas operations between periods. Refer to the Principal Properties and Fourth Quarter 2016 Results sections of the Company's Management's Discussion and Analysis for the periods and the calculation.

Net Cash (Debt) is a measure of the Company's overall debt position after adjusting for certain working capital amounts and is used by management to assess the Company's overall leverage position. Refer to the Liquidity and Capital Resources section of the Company's Management's Discussion and Analysis for the period and for the calculation of Net Cash (Debt) and Adjusted Working Capital. Exploration and capital expenditures consist of the Company's spending on wells and infrastructure projects, other property, plant and equipment, land and property acquisitions, capitalized interest and geological and geophysical costs incurred. The closest GAAP measure to exploration and development expenditures is property, plant and equipment and exploration cash flows under investing activities in the Company's Consolidated Statement of Cash Flows, which includes all of the items included in exploration and capital expenditures, except for geological and geophysical costs for the year ended December 31, 2016 of \$4.1 million (2015 - \$6.1 million), which are expensed as incurred. Principal Properties Capital includes capital expenditures and geological and geophysical costs related to the Company's Principal Properties business segment, and excludes land acquisitions and capitalized interest. The Principal Properties Capital measure provides management and investors with information regarding the Company's Principal Properties spending on wells and infrastructure projects separate from land acquisition activity and capitalized interest. Refer to the Exploration and Capital Expenditures section of the Company's Management's Discussion and Analysis for the period. Investments in other entities – market value reflects the Company's investments in enterprises whose securities trade on a public stock exchange at their period end closing price (e.g. Trilogy, MEG, Marquee, RMP, SOG and others), and investments in all other entities at book value and excludes 3.8 million 7Gen Shares that were distributed to Paramount's shareholders by way of dividend in January 2017. Paramount provides this information because the market values of equity-accounted investments, which are significant assets of the Company, are often materially different than their carrying values. Refer to the Strategic Investments section of the Company's Management's Discussion and Analysis for information on carrying and market values. The Finding and development costs ("F&D") measure is commonly used by management and investors to assess the relationship between capital invested in oil and gas exploration and development projects and reserve additions associated with such projects. Refer to the Principal Properties Reserves and Finding & Development Costs section of this document for the calculation of F&D costs.

The Non-GAAP Measures should not be considered in isolation or construed as alternatives to their most directly comparable measure calculated in accordance with GAAP, or other measures of financial performance calculated in accordance with GAAP. The Non-GAAP Measures are unlikely to be comparable to similar measures presented by other issuers.

Oil and Gas Measures and Definitions

Abbreviations

Liquids

Bbl	Barrels
MBbl	Thousands of barrels
Bbl/d	Barrels per day
NGLs	Natural gas liquids
Condensate	Pentane and heavier hydrocarbons

Natural Gas

Mcf	Thousands of cubic feet
Bcf	Billions of cubic feet
MMcf/d	Millions of cubic feet per day
GJ	Gigajoule
MMbtu	Millions of British thermal units

Oil Equivalent

Boe	Barrels of oil equivalent
MBoe	Thousands of barrels of oil equivalent
MMBoe	Millions of barrels of oil equivalent
Boe/d	Barrels of oil equivalent per day

Measures

This document contains disclosures expressed as "Boe", "\$/Boe", MBoe, MMBoe and "Boe/d". All oil and natural gas equivalency volumes have been derived using the ratio of six thousand cubic feet of natural gas to one barrel of oil. Equivalency measures may be misleading, particularly if used in isolation. A conversion ratio of six thousand cubic feet of natural gas to one barrel of oil is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the well head. The term "Liquids" is used to represent oil, condensate and Other NGLs. The term "Other NGLs" means ethane, propane and butane.

The reserves replacement disclosure herein was calculated in respect of Ongoing Operations for each of proved and proved plus probable reserves as the sum of extensions and discoveries, technical revisions and economic factors for the year divided by the sales volumes from Ongoing Operations for 2016.

During the year ended December 31, 2016, the value ratio between crude oil and natural gas was approximately 27:1. This value ratio is significantly different from the energy equivalency ratio of 6:1. Using a 6:1 ratio would be misleading as an indication of value.

CONSOLIDATED FINANCIAL STATEMENTS

MANAGEMENT'S REPORT

The accompanying Consolidated Financial Statements of Paramount Resources Ltd. (the "Company") are the responsibility of Management and have been approved by the Company's Board of Directors. The Consolidated Financial Statements have been prepared in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board and include certain estimates that reflect Management's best judgments. If alternate accounting methods exist, Management has chosen those policies it considers the most appropriate in the circumstances. Financial information included in the Company's annual report, including Management's Discussion and Analysis, is consistent with these Consolidated Financial Statements.

Management is also responsible for establishing and maintaining adequate internal control over the Company's financial reporting. The Company's internal control system was designed to provide reasonable assurance that all transactions are recorded that are necessary for the preparation and presentation of financial statements in accordance with International Financial Reporting Standards, that such transactions are recorded accurately and that the Company's assets are safeguarded.

The Board of Directors is responsible for ensuring that Management fulfills its responsibilities for financial reporting and internal control. The Board of Directors exercises this responsibility through the Audit Committee, which is comprised entirely of non-Management directors. The Audit Committee meets regularly with Management and the independent auditors to ensure that Management's responsibilities are properly discharged and to review the Consolidated Financial Statements. The Audit Committee reports its findings to the Board of Directors for consideration when approving the annual Consolidated Financial Statements for issuance. The Audit Committee also considers, for review by the Board of Directors and approval by the shareholders, the engagement or re-appointment of the independent auditors.

Ernst & Young LLP, independent auditors appointed by the shareholders of the Company, conducts an examination of the Consolidated Financial Statements in accordance with Canadian Generally Accepted Auditing Standards. Ernst & Young LLP has full and free access to the Board of Directors, the Audit Committee and Management.

/s/ J.H.T. Riddell
J.H.T. Riddell
President and Chief Executive Officer

/s/ B. K. Lee
B. K. Lee
Chief Financial Officer

March 8, 2017

INDEPENDENT AUDITORS' REPORT

To the shareholders of Paramount Resources Ltd.

We have audited the accompanying consolidated financial statements of Paramount Resources Ltd. which comprise the consolidated balance sheets as at 31 December, 2016 and 2015, and the consolidated statements of comprehensive income (loss), shareholders' equity and cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

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

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Paramount Resources Ltd. as at 31 December, 2016 and 2015 and of its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

Calgary, Canada

March 8, 2017

Ernst & Young LLP

Chartered Professional Accountants

CONSOLIDATED BALANCE SHEET

(\$ thousands)

As at December 31	Note	2016	2015
ASSETS			
Current assets			
Cash and cash equivalents	17	621,872	11,941
Investments in Securities for distribution	12	118,978	–
Accounts receivable	16	23,895	48,730
Prepaid expenses and other		1,715	5,049
Risk management	16	–	40,207
		766,460	105,927
Exploration and evaluation	5	301,530	363,724
Property, plant and equipment, net	6	882,724	2,034,353
Equity-accounted investments	7	44,053	58,370
Investments in Securities	8	64,193	60,714
Deferred income tax	15	–	154,823
Goodwill	6	–	3,124
		2,058,960	2,781,035
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities			
Limited-recourse demand facilities	9	–	100,911
Dividend payable	12	118,978	–
Accounts payable and accrued liabilities	16	81,585	107,624
Risk management	16	5,180	–
		205,743	208,535
Long-term debt	10	–	1,750,226
Asset retirement obligations	11	212,309	273,580
Deferred income tax	15	6,125	–
		424,177	2,232,341
Commitments and contingencies	20		
Shareholders' equity			
Share capital	12	1,639,466	1,646,984
Accumulated deficit		(152,182)	(1,197,627)
Reserves	13	147,499	99,337
		1,634,783	548,694
		2,058,960	2,781,035

See the accompanying notes to these Consolidated Financial Statements.

On behalf of the Board of Directors

/s/ C.H. Riddell
C.H. Riddell, Director

/s/ J.C. Gorman
J.C. Gorman, Director

March 8, 2017

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (LOSS)

(\$ thousands, except as noted)

Year ended December 31	Note	2016	2015
Petroleum and natural gas sales		248,828	376,799
Royalties		(2,211)	(10,388)
Revenue		246,617	366,411
Gain on commodity contracts	16	253	52,767
		246,870	419,178
Expenses			
Operating expense		97,040	90,043
Transportation and NGLs processing		56,465	65,724
General and administrative		25,877	23,857
Share-based compensation	14	27,771	20,504
Depletion and depreciation	6	76,415	623,889
Exploration and evaluation	5	(72,071)	208,992
(Gain) loss on sale of oil and gas assets	6	(1,379,965)	9,058
Interest and financing		80,324	110,663
Accretion of asset retirement obligations	11	4,622	5,695
Foreign exchange		(43,727)	61,109
Debt extinguishment	10	27,575	11,994
		(1,099,674)	1,231,528
Loss from equity-accounted investments	7	(14,316)	(23,018)
Write-down of Investments in Securities	8	(11,235)	(81,819)
Other income	4	376	3,388
Income (loss) before tax		1,321,369	(913,799)
Income tax expense (recovery)	15		
Current		—	11
Deferred		156,094	(12,509)
		156,094	(12,498)
Net income (loss)		1,165,275	(901,301)
Other comprehensive income (loss), net of tax			
Items that may be reclassified to net income (loss):			
Change in market value of securities		13,128	(42,180)
Reclassification of accumulated losses on securities to net income (loss)		11,235	81,819
Deferred tax on other comprehensive income related to securities		(1,276)	(1,314)
Comprehensive income (loss)		1,188,362	(862,976)
Net income (loss) per common share (\$/share)	12		
Basic		10.98	(8.52)
Diluted		10.95	(8.52)

See the accompanying notes to these Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

(\$ thousands)

Year ended December 31	Note	2016	2015
Operating activities			
Net income (loss)		1,165,275	(901,301)
Add (deduct):			
Items not involving cash	17	(1,161,287)	976,387
Asset retirement obligations settled	11	(1,753)	(6,641)
Debt extinguishment	10	27,575	11,994
Change in non-cash working capital		15,942	3,834
Cash from operating activities		45,752	84,273
Financing activities			
Net draw (repayment) of limited-recourse demand facilities	9	(100,911)	19,381
Net draw (repayment) of revolving long-term debt	10	(693,045)	295,372
Proceeds from issuance of 2023 Notes, net of issue costs	10	—	549,649
Redemption of Senior Notes	10	(463,521)	(380,175)
Common shares issued, net of issue costs		1,462	41,817
Common shares repurchased under NCIB	12	(9,704)	—
Other		(3,194)	(316)
Cash from (used in) financing activities		(1,268,913)	525,728
Investing activities			
Property, plant and equipment and exploration		(200,992)	(493,963)
Proceeds on sale of oil and gas assets		1,177,437	5,617
Cash acquired on corporate acquisition, net		—	740
Proceeds on sale of Investments in Securities, net of costs		862,931	—
Deposit	15	—	20,135
Change in non-cash working capital		(5,978)	(152,352)
Cash from (used in) investing activities		1,833,398	(619,823)
Net increase (decrease)		610,237	(9,822)
Foreign exchange on cash and cash equivalents		(306)	3,443
Cash and cash equivalents, beginning of year		11,941	18,320
Cash and cash equivalents, end of year		621,872	11,941
Supplemental cash flow information	17		

See the accompanying notes to these Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY

(\$ thousands, except as noted)

Year ended December 31	Note	2016		2015	
		<i>Shares (000's)</i>		<i>Shares (000's)</i>	
Share Capital					
Balance, beginning of year		106,212	1,646,984	104,843	1,603,436
Issued		176	2,060	1,337	43,175
Common shares repurchased under NCIB	12	(623)	(9,704)	-	-
Change in unvested common shares for stock incentive plan	14	19	126	32	373
Balance, end of year		105,784	1,639,466	106,212	1,646,984
Accumulated Deficit					
Balance, beginning of year			(1,197,627)		(296,326)
Net income (loss)			1,165,275		(901,301)
Dividend			(119,830)		-
Balance, end of year			(152,182)		(1,197,627)
Reserves					
Balance, beginning of year	13		99,337		46,172
Other comprehensive income			23,087		38,325
Contributed surplus			25,075		14,840
Balance, end of year			147,499		99,337
Total Shareholders' Equity			1,634,783		548,694

See the accompanying notes to these Consolidated Financial Statements.

1. Significant Accounting Policies

Paramount Resources Ltd. ("Paramount" or the "Company") is an independent, publicly traded, Canadian energy company that explores and develops unconventional and conventional petroleum and natural gas prospects, including long-term unconventional exploration and pre-development projects, and holds a portfolio of investments in other entities. The Company's principal properties are primarily located in Alberta and British Columbia. Paramount's operations are divided into three business segments: i) Principal Properties; ii) Strategic Investments; and iii) Corporate.

Paramount is the ultimate parent company of a consolidated group of companies and is incorporated and domiciled in Canada. The address of its registered office is 4700, 888 3rd Street S.W., Calgary, Alberta, Canada, T2P 5C5. The consolidated group includes wholly-owned subsidiaries Fox Drilling Limited Partnership ("Fox Drilling"), Cavalier Energy ("Cavalier"), and MGM Energy. Paramount also holds a 15 percent equity interest in Trilogy Energy Corp. ("Trilogy"), which is accounted for using the equity method of investment accounting.

These consolidated financial statements of the Company, as at December 31, 2016 and December 31, 2015 and for the years then ended (the "Consolidated Financial Statements"), were authorized for issuance by Paramount's Board of Directors on March 8, 2017.

Basis of Preparation

These Consolidated Financial Statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") and have been prepared on a historical cost basis, except for certain financial instruments. The Company's accounting policies have been applied consistently to all years presented. Amounts included in these Consolidated Financial Statements are stated in thousands of Canadian dollars, unless otherwise noted. Certain comparative figures have been reclassified to conform with the current year's presentation.

The financial statements of Paramount's subsidiaries and partnerships are prepared for the same reporting periods as the parent in accordance with the Company's accounting policies. All intercompany balances and transactions have been eliminated.

The preparation of these Consolidated Financial Statements requires the use of certain accounting estimates and also requires Management to exercise judgment in applying the Company's accounting policies. Areas involving a higher degree of judgment or complexity, and areas where assumptions and estimates are significant to the Consolidated Financial Statements, are described in Note 2.

a) Revenue Recognition

Petroleum and natural gas sales revenues are recognized when title passes to third parties and the significant risks and rewards of ownership have been transferred.

Drilling services are billed to customers on a per-day basis and revenues are recognized as services are rendered and collectability is reasonably assured. When the Company's drilling rigs (the "Rigs") drill on a property owned by Paramount, the Company capitalizes its working interest share of the drilling expenses and eliminates the associated drilling revenue.

b) Cash and Cash Equivalents

Cash and cash equivalents are recorded at cost and are comprised of cash in operating bank accounts, term deposits, certificates of deposit and other highly liquid investments.

c) Trade and Other Receivables

Accounts receivable are recorded as corresponding amounts of revenue are recognized or costs are incurred on behalf of partners in connection with joint operations. An allowance for doubtful accounts is recognized based on Management's best estimate of accounts that may not be collectible, which is reviewed and adjusted on a quarterly basis.

d) Exploration and Evaluation

Costs related to the exploration for and evaluation of hydrocarbon resources, including costs of acquiring unproved property, drilling and completing exploratory wells and estimated asset retirement costs, are initially capitalized, pending determination of technical feasibility and commercial viability. If hydrocarbons are found, but further appraisal activity is required to determine commercial viability, the exploration and evaluation ("E&E") costs continue to be recognized as an asset. All such costs are subject to technical, commercial, and Management review at least annually to confirm the continued intent to establish the technical feasibility and commercial viability of the discovery.

The Company's exploration and evaluation assets include Liard and Horn River Basins shale gas properties (the "Shale Gas Properties") and oil sands and carbonate bitumen properties within the Strategic Investments business segment. Net cash flows from the sale of production from wells on the Shale Gas Properties are applied against the capitalized costs of the properties until the overall project is deemed commercially viable. All direct costs related to pre-development activities in connection with oil sands properties are considered pre-operating and are capitalized, including the costs to acquire mineral rights, conduct delineation and pre-production drilling, and design and construct plant and equipment.

When the technical feasibility and commercial viability of a project has been established, the E&E costs are transferred to petroleum and natural gas assets, subject to an impairment assessment. When the Company determines that an E&E project is no longer viable or its carrying value exceeds its recoverable amount, an impairment charge is recognized.

Exploratory geological and geophysical costs, pre-license costs, and annual lease rentals are expensed as incurred.

e) Property, Plant and Equipment

Petroleum and natural gas assets are carried at cost, net of accumulated depletion, depreciation and impairments, and include costs related to drilling and completing development wells, infrastructure construction, successful E&E projects and estimated asset retirement costs.

Paramount's Rigs are carried at cost, net of accumulated depreciation. Costs incurred to improve the capabilities of the Rigs, extend their useful lives or replace significant components are capitalized. When a significant component is replaced, the carrying value of the replaced component is written-off. Costs incurred to maintain and repair the Rigs are expensed as incurred.

Other property, plant and equipment ("PP&E"), including leasehold improvements, are carried at cost net of accumulated depreciation.

Depletion and Depreciation

The capitalized costs of proved oil and gas properties are depleted over estimated volumes of proved developed reserves using the unit-of-production method. For purposes of these calculations, volumes of natural gas production and reserves are converted to barrels on an energy equivalent basis. Depletion rates are revised annually, or more frequently when events dictate. E&E costs are not depleted.

The capitalized costs of the majority of Paramount's gathering systems and production equipment are depleted on a unit-of-production basis over the proved developed reserves of the field to which they relate. Capitalized costs of processing plants and other major infrastructure assets are depreciated on a straight-line basis over their expected useful lives, which extend up to 40 years.

The Rigs are depreciated on a straight line basis by component over their expected useful lives, which range between 5 and 20 years.

Leasehold improvements are depreciated over the term of the related lease. Other assets are depreciated using the declining balance method at rates ranging between 35 and 50 percent.

f) Impairment of Non-Financial Assets

The carrying values of the Company's non-financial assets are reviewed at each reporting date to determine whether any indicators of impairment are present, or whether there is any indication that an impairment loss recognized in prior periods may no longer exist or may have decreased. For the purpose of impairment testing, non-financial assets are tested individually or, in certain circumstances, grouped together into a cash-generating unit ("CGU"), which consists of the smallest group of assets that generate cash inflows that are largely independent of the cash inflows of other assets or groups of assets. The Company's Principal Properties non-financial assets are grouped into two CGUs for the purpose of impairment testing, consisting of the Kaybob CGU and the Grande Prairie CGU. The Company's Strategic Investments non-financial assets associated with the Shale Gas Properties form a third CGU for the purposes of impairment testing.

If an indicator of impairment or impairment reversal is identified for a particular asset or CGU, its recoverable amount is estimated. If the carrying value of such asset or CGU exceeds its estimated recoverable amount, an impairment charge is recognized. If the estimated recoverable amount of an asset or CGU that was previously impaired exceeds its recoverable amount, impairment charges recognized in prior periods are reversed to a maximum of the carrying value that would have been determined, net of depletion and amortization, had no impairment charges been recognized for the CGU in prior periods.

The recoverable amount of an asset or CGU is the greater of its fair value less costs to sell ("FVLCS") and its value in use. In assessing FVLCS, the Company estimates the value a potential purchaser would ascribe to an asset or CGU. For oil and gas properties, the FVLCS is generally estimated based on expected after-tax future net cash flows from the production of proved and probable reserves volumes using forecast commodity prices and costs, discounted using market-based rates. Value in use is determined by estimating the present value of the future net cash flows expected to be derived from the continued use of the asset or CGU. When it is determined that there has been a subsequent increase in the recoverable amount ascribed to an oil and gas property or a CGU, reversals of impairments are recognized, net of any depletion and depreciation that would have been recorded since the date of the impairment charge.

g) Joint Arrangements

Paramount conducts its exploration and development activities independently, as well as jointly with others through jointly controlled assets and operations. All of the Company's current interests in joint arrangements are classified as joint operations. To account for these arrangements, Paramount recognizes its proportionate share of the related revenues, expenses, assets and liabilities of such joint operations.

Interests in joint ventures are accounted for using the equity method of accounting. The Company does not currently have any interests in joint arrangements that are classified as joint ventures.

h) Equity-Accounted Investments

Investments in entities in which Paramount has significant influence are accounted for using the equity method of investment accounting. An investor is presumed to have significant influence where it holds 20 percent or more of the voting power over an investee, or where significant influence can be clearly demonstrated. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but is not control or joint control of the entity. Factors that may demonstrate significant influence include representation on the board of directors of the investee, interchange of management personnel and participation in determining the significant policies of the investee.

Under the equity method, an investment is recognized at cost on acquisition, with the carrying amount being subsequently increased or decreased to reflect the investor's proportionate share of the profit or loss of the investee after the date of acquisition. Distributions received from an investee reduce the carrying amount of the investor's investment.

i) Business Combinations and Goodwill

Business combinations are accounted for using the acquisition method of accounting. Under this method, the net identifiable assets acquired are measured at fair value on acquisition date. Any excess of the consideration paid over the fair value of the net identifiable assets acquired is recognized as goodwill. Any deficiency in the consideration transferred versus the fair value of the net identifiable assets acquired is recognized in earnings. Costs incurred to complete the transaction are expensed.

Goodwill is tested for impairment at least annually, or when a potential impairment indicator is identified. To test goodwill for impairment, the carrying value of a CGU (or group of CGUs), including allocated goodwill, is compared to that CGU's (or group of CGUs) estimated recoverable amount. An impairment charge is recognized to the extent that the carrying amount of the CGU (or group of CGUs), including goodwill, exceeds its estimated recoverable amount. Impairment charges related to goodwill are not reversed in future periods.

j) Capitalized Borrowing Costs

Borrowing costs directly associated with the acquisition, construction or production of a qualifying asset are capitalized while the asset is being constructed or otherwise prepared for its intended productive use. All other borrowing costs are expensed in the period incurred.

k) Asset Retirement Obligations

Asset retirement obligations arise from legal and/or constructive obligations to retire assets, including oil and gas wells, gathering systems, processing plants and access roads, at the end of their productive

lives. The present value of an asset retirement obligation is recognized in the Consolidated Balance Sheet when incurred and a reasonable estimate of the cost of retirement can be made. The present value of the obligation is determined using the applicable period-end risk free discount rate, after applying an estimated cost inflation factor, and is adjusted for the passage of time, which is recognized as accretion expense. The present values of estimated future asset retirement costs are capitalized as part of the carrying value of the related long-lived asset and depreciated on the same basis as the underlying asset. Revisions to the timing, anticipated cost, discount rate and inflation rate relating to the estimated liability are accounted for prospectively by recording an adjustment to the asset retirement obligation liability, with a corresponding adjustment to the carrying value of the related asset.

Actual costs incurred to retire assets are applied against the asset retirement obligation liability. Differences between the actual costs incurred and the liability accrued are recognized in earnings when the reclamation of a property is fully completed.

l) Foreign Currency Translation

The functional and presentation currency of Paramount and its subsidiaries is the Canadian dollar.

m) Estimates of Fair Value

Inputs used to estimate fair values incorporated in the preparation of the Consolidated Financial Statements are categorized into one of three levels in a fair value hierarchy. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The three levels are defined as follows:

Level One – Inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that can be accessed at the measurement date.

Level Two – Inputs are based on information other than quoted prices included within Level One that are observable for the asset or liability, either directly or indirectly, including:

- a) quoted prices for similar assets or liabilities in active markets;
- b) quoted prices for identical or similar assets or liabilities in markets that are not active;
- c) inputs other than quoted prices that are observable for the asset or liability, for example:
 - i. interest rates and yield curves observable at commonly quoted intervals;
 - ii. implied volatilities; and
 - iii. credit spreads; and
- d) market-corroborated inputs.

Level Three – Inputs are unobservable. Unobservable inputs are developed using the best information available in the circumstances, which may incorporate Paramount's own internally generated data.

n) Financial Instruments and Other Comprehensive Income

Financial Instruments

Financial instruments are measured at fair value on initial recognition. The measurement of a financial instrument in subsequent periods is dependent upon whether it has been classified as "fair value through profit or loss", "available-for-sale", "loans and receivables", "held-to-maturity investments", or "financial

(Tabular amounts stated in \$ thousands, except as noted)

liabilities measured at amortized cost", as defined by the relevant standard. Paramount does not presently employ hedge accounting for any of its financial instruments.

The fair values of cash and cash equivalents, accounts receivable and accounts payable and accrued liabilities approximate their carrying amounts due to the short-term maturities of these instruments.

Paramount's risk management assets and liabilities are classified as fair value through profit or loss (held for trading). Fair value through profit or loss financial instruments are measured at fair value, with changes in their fair values over time being recognized in net earnings. The fair values of the Company's risk management assets and liabilities are estimated using a market approach incorporating level two fair value hierarchy inputs, including forward market curves and price quotes for similar instruments provided by financial institutions.

Investments in Securities are classified as available-for-sale. Available-for-sale financial assets are measured at fair value, with changes in such fair values being accumulated in other comprehensive income ("OCI") until the asset is realized or impaired, at which time a gain or loss is recognized in net earnings. Investments in publicly-traded securities are carried at their period-end trading price (level one fair value hierarchy estimate). Investments in the securities of private entities are carried at fair value, which is estimated using values based on equity issuances and other indications of value from time-to-time (level two and level three fair value hierarchy estimates).

Long-term debt balances outstanding from time-to-time are classified as loans and receivables. Loans and receivables, including related transaction costs, are measured at amortized cost using the effective interest method.

Other Comprehensive Income

For Paramount, OCI is comprised of changes in the market value of Investments in Securities. Amounts recorded in OCI each period are presented in the Consolidated Statement of Comprehensive Income (Loss). Cumulative changes in OCI are included in Reserves, which is presented within Shareholders' Equity in the Consolidated Balance Sheet.

An impairment charge is recognized in respect of an Investment in Securities where its fair value decreases below its carrying value, and the decline is considered to be significant or prolonged. A subsequent increase in the fair value of an Investment in Securities is recognized in OCI.

o) Income Taxes

Paramount follows the liability method of accounting for income taxes. Under this method, a deferred income tax asset or liability is recognized in respect of any temporary difference between the carrying amount of an asset or liability reported in the Consolidated Financial Statements and its respective tax basis, using substantively enacted income tax rates. Deferred income tax balances are adjusted to reflect changes in substantively enacted income tax rates expected to apply when the underlying assets are realized or liabilities are settled, with adjustments being recognized in deferred tax expense in the period in which the change occurs.

Deferred income tax assets are recognized to the extent future realization is considered probable. The carrying value of deferred income tax assets is reviewed at each reporting date taking into consideration historical and expected future taxable income, expected reversals of temporary differences, anticipated timing of realization, tax basis carry-forward periods and other factors. Deferred income tax assets are de-

recognized to the extent that estimated future taxable earnings are not sufficient to result in the asset being recovered.

p) Flow-Through Shares

The proceeds of flow-through share issuances are allocated between the sale of Paramount's class A common shares ("Common Shares") and the sale of tax benefits associated with the flow-through feature of the securities. Proceeds are first allocated to share capital based on the market price of Common Shares on the date the offering is priced, with the excess of the issue price over the market price of Common Shares being recorded in accounts payable and accrued liabilities. As qualifying expenditures intended for renunciation to subscribers are incurred, the Company recognizes a deferred tax liability, reduces the accounts payable and accrued liabilities amount and records any difference as deferred tax expense.

q) Share-Based Compensation

Paramount Stock Option Plan

Paramount has a stock option plan that enables its Board of Directors or Compensation Committee to grant options to acquire Common Shares of the Company ("Paramount Options") to key employees and directors. Paramount Options generally vest over five years and expire within six years after the grant date. The provisions of the plan permit the Company to settle the options in Common Shares of the Company or in cash.

The Company accounts for Paramount Options as equity-settled share-based compensation transactions. The aggregate grant date fair value of stock options awarded is recognized as share-based compensation expense over the applicable vesting period on a straight line basis, with a corresponding increase in Contributed Surplus. The grant date fair value of Paramount Options is estimated using the Black-Scholes-Merton model, and such value is not adjusted in future periods. The amount of share-based compensation expense recognized each period reflects the portion of the vesting term that has elapsed and the estimated number of options that are expected to vest. That estimate is adjusted each period such that the cumulative amount recognized on the vesting date reflects the actual number of Paramount Options that ultimately vest. Upon the exercise of a Paramount Option, the Company transfers the cumulative amount recognized in Contributed Surplus in respect of that option to Share Capital.

Cavalier Stock Option Plan

Cavalier has a stock option plan that enables its Board of Directors to grant options to acquire common shares of Cavalier ("Cavalier Options") to key employees and directors. Cavalier Options generally vest over five years and expire within seven years after the grant date. The provisions of the stock option plan permit Cavalier to settle Cavalier Options in common shares of Cavalier or in cash, at the discretion of Cavalier. Cavalier Options are accounted for as equity-settled share-based compensation transactions.

Stock Incentive Plan

Paramount's stock incentive plan ("SIP") provides that rights to Common Shares may be awarded to employees annually. Common Shares are purchased in the open market and held by an independent trustee until the completion of the vesting period. Generally, one third of an award vests immediately, with the remaining tranches vesting annually over two years. The unvested portion of an award is initially

recorded as a reduction of Paramount's Share Capital. The cost of the unvested Common Shares is then recognized over the vesting period as share-based compensation expense, with a corresponding increase to Share Capital.

r) Net Income Per Share

Basic net income per share is calculated by dividing net income by the weighted average number of Common Shares outstanding during the year. Diluted net income per share is calculated by adjusting the weighted average number of Common Shares outstanding for potentially dilutive Common Shares related to Paramount Options. The number of dilutive Common Shares is determined using the treasury method. As Paramount Options can be exchanged for Common Shares, they are considered potentially dilutive and are included in the Company's diluted per share amounts when they are dilutive to net income per share.

2. Significant Accounting Estimates, Assumptions & Judgments

The timely preparation of financial statements requires Management to make judgments, estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and disclosures regarding contingent assets and liabilities. Estimates and assumptions are regularly evaluated and are based on Management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Changes in judgments, estimates and assumptions based on new information could result in a material change to the carrying amount of assets or liabilities and have a material impact on assets, liabilities, revenues and expenses recognized in future periods. The following is a description of the accounting judgments, estimates and assumptions that are considered significant.

Exploration or Development

The Company is required to apply judgment when designating a project as exploration and evaluation or development, including assessments of geological and technical characteristics and other factors related to each project.

Exploration and Evaluation Projects

The accounting for E&E projects requires Management to make judgments as to whether exploratory projects have discovered economically recoverable quantities of petroleum and natural gas, which requires the quantity and realizable value of such petroleum and natural gas to be estimated. Previous estimates are sometimes revised as new information becomes available. Where it is determined that an exploratory project did not discover economically recoverable petroleum and natural gas, the costs are written-off as E&E expense.

If hydrocarbons are encountered, but further appraisal activity is required, the exploratory costs remain capitalized as long as sufficient progress is being made in assessing whether the recovery of the petroleum and natural gas is economically viable. The concept of "sufficient progress" is a judgmental area, and it is possible to have exploratory costs remain capitalized for several years while additional exploratory activities are carried out or the Company seeks government, regulatory or partner approval for development plans. Exploration and evaluation assets are subject to ongoing technical, commercial and Management review to confirm the continued intent to establish the technical feasibility and commercial viability of the discovery. When Management is making this assessment, changes to project economics, expected quantities of petroleum and natural gas, expected production techniques, drilling

results, estimated capital expenditures and production costs, results of other operators in the region and access to infrastructure and potential infrastructure expansions are important factors. Where it is determined that an exploratory project is not economically viable, the costs are written-off as E&E expense.

Reserves Estimates

Reserves engineering is an inherently complex and subjective process of estimating underground accumulations of petroleum and natural gas. The process relies on judgments based on the interpretation of available geological, geophysical, engineering and production data. The accuracy of a reserves estimate is a function of the quality and quantity of available data, the interpretation of that such data, the accuracy of various economic assumptions and the judgment of those preparing the estimate. Because these estimates depend on many assumptions, all of which may differ from actual results, reserves estimates, commodity price estimates and estimates of future net revenue will be different from the sales volumes ultimately recovered and net revenues actually realized. Changes in market conditions, regulatory matters, the results of subsequent drilling, testing and production and other factors may require revisions to the original estimates.

Estimates of reserves impact: (i) the assessment of whether a new well has found economically recoverable reserves; (ii) depletion rates; and (iii) the estimated recoverable amount of petroleum and natural gas properties used from time-to-time in impairment and impairment reversal assessments, all of which could have a material impact on earnings.

Estimates of Recoverable Amounts

Estimates of recoverable amounts used in impairment and impairment reversal tests often incorporate level three hierarchy inputs, including estimated volumes and future net revenues from oil and natural gas reserves, contingent resource estimates, future net cash flow estimates related to other long-lived assets and internal and external market metrics used to estimate value based on comparable assets and transactions. By their nature, such estimates are subject to measurement uncertainty. Changes in such estimates, and differences between actual and estimated amounts, could have a material impact on earnings.

Determination of CGUs

The recoverability of the carrying value of oil and gas properties is generally assessed at the CGU level. The determination of the properties and other assets grouped within a particular CGU is based on Management's judgment with respect to the integration between assets, shared infrastructure and cash flows and the overall significance of individual properties. Changes in the assets comprising CGUs could have an impact on estimated recoverable amounts used in impairment assessments and could have a material impact on earnings.

Equity Accounted Investments

The Company accounts for its investment in Trilogy under the equity method of investment accounting, although it holds less than 20 percent of the voting power because, in Management's judgment, it has significant influence as a result of common directors and members of senior management.

Investments in Securities

The Company's Investments in Securities that are accounted for as available-for-sale financial instruments are assessed at the end of each reporting period to determine whether there is any objective evidence of impairment. Management is required to exercise judgment in determining whether a decrease in the fair value of an investment below its carrying value is significant or prolonged, which would require an impairment charge to be recognized. Management is also required to exercise judgment in estimating the fair value of investments in the securities of private corporations that are not publicly traded.

Provisions

A provision is recognized where the Company has determined that it has a present obligation arising from past events and the settlement of the obligation is expected to result in an outflow of economic benefits. The determination of whether the Company has a present obligation arising from past events requires Management to exercise judgement as to the facts and circumstances of the event and the extent of any expected obligations of Paramount. Changes in facts and circumstances as a result of new information and other developments may impact Management's assessment of the Company's obligations, if any, in respect of such events. Changes in such estimates could have a material impact on assets, liabilities, revenues, expenses, and earnings.

Asset Retirement Obligations

Estimates of asset retirement costs are based on assumptions regarding the methods, timing, economic environment and regulatory standards that are expected to exist at the time assets are retired. Management adjusts estimated amounts periodically as assumptions are updated to incorporate new information. Actual payments to settle the obligations may differ materially from amounts estimated.

Share-Based Payments

The Company estimates the grant date value of stock options awarded using the Black-Scholes-Merton model. The inputs used to determine the estimated value of the options are based on assumptions regarding share price volatility, the expected life of the options, expected forfeiture rates and future interest rates. By their nature, these inputs are subject to measurement uncertainty and require Management to exercise judgment in determining which assumptions are the most appropriate.

Income Taxes

Accounting for income taxes is a complex process requiring Management to interpret frequently changing laws and regulations and make judgments and estimates related to the application of tax law, the timing of temporary difference reversals and the likelihood of realizing deferred income tax assets. All tax filings are subject to subsequent government audits and potential reassessment. These interpretations and judgments, and changes related to them, impact current and deferred tax provisions, the carrying value of deferred income tax assets and liabilities and could have a material impact on earnings.

3. Changes in Accounting Standards

There were no new or amended accounting standards adopted by the Company for the year ended December 31, 2016.

Future Changes in Accounting Standards

In May 2014, the International Accounting Standards Board ("IASB") issued IFRS 15 – *Revenue From Contracts With Customers*, which establishes a single revenue recognition framework that applies to contracts with customers. The standard requires an entity to recognize revenue to reflect the transfer of goods and services for the amount it expects to receive when control is transferred to the purchaser. IFRS 15 is effective for years beginning on or after January 1, 2018. The Company is currently evaluating the impact of the IFRS on its Consolidated Financial Statements.

In July 2014, the IASB issued IFRS 9 – *Financial Instruments*, which sets out the recognition and measurement requirements for financial instruments and some contracts to buy or sell non-financial items. IFRS 9 proposes a single model of classifying and measuring financial assets and liabilities and provides for only two classification categories: amortized cost and fair value. IFRS 9 is effective for years beginning on or after January 1, 2018. The Company is currently evaluating the impact of the IFRS on its Consolidated Financial Statements.

In January 2016, the IASB issued IFRS 16 – *Leases*, which replaces IAS 17 – *Leases* and related interpretations. IFRS 16 eliminates the classification of leases as finance or operating and introduces a single lessee accounting model for recognition and measurement, which will require the recognition of assets and liabilities for most leases. IFRS 16 is effective for years beginning on or after January 1, 2019. The Company is currently evaluating the impact of the IFRS on its Consolidated Financial Statements.

4. Segmented Information

Paramount's operations are grouped into three business segments, which have been established by Management to assist in resource allocation, to assess operating performance and to achieve long-term strategic objectives. The segments are divided based on the nature of activities and the Company's Management structure:

- **Principal Properties:** Principal properties include the Company's four Corporate Operating Units, which are involved in the exploration, development, production and marketing of natural gas, natural gas liquids and crude oil, generally having similar economic characteristics.
- **Strategic Investments:** Strategic investments include: (i) investments in other entities (ii) investments in exploration and development stage assets, where there is no near-term expectation of commercial production, but a longer-term value proposition based on spin-outs, dispositions, or future revenue generation, including oil sands and carbonate bitumen interests held by Cavalier, and prospective shale gas acreage in the Liard and Horn River Basins; and (iii) drilling rigs owned by Fox Drilling.
- **Corporate:** Corporate is comprised of income and expense items, including general and administrative expense, share-based compensation expense and interest expense, which have not been specifically allocated to Principal Properties or Strategic Investments.

(Tabular amounts stated in \$ thousands, except as noted)

Year ended December 31, 2016	Principal Properties	Strategic Investments	Corporate	Inter-segment Eliminations	Total
Revenue	246,617	-	-	-	246,617
Gain on commodity contracts	253	-	-	-	253
	246,870	-	-	-	246,870
Expenses					
Operating expense	97,040	-	-	-	97,040
Transportation and NGLs processing	56,465	-	-	-	56,465
General and administrative	-	6,261	19,616	-	25,877
Share-based compensation	-	6,172	21,599	-	27,771
Depletion and depreciation	71,136	9,411	932	(5,064)	76,415
Exploration and evaluation	22,888	(94,959)	-	-	(72,071)
(Gain) loss on sale of oil and gas assets	(1,380,136)	171	-	-	(1,379,965)
Interest and financing	-	2,693	77,631	-	80,324
Accretion of asset retirement obligations	4,257	365	-	-	4,622
Foreign exchange	-	-	(43,727)	-	(43,727)
Debt extinguishment	-	-	27,575	-	27,575
	(1,128,350)	(69,886)	103,626	(5,064)	(1,099,674)
Loss from equity-accounted investments	-	(14,316)	-	-	(14,316)
Write-down of Investments in Securities	-	(11,235)	-	-	(11,235)
Other	(277)	89	1,537	-	1,349
Drilling rig revenue	-	30,252	-	(30,029)	223
Drilling rig expense	-	(11,669)	-	10,473	(1,196)
	1,374,943	63,007	(102,089)	(14,492)	1,321,369
Inter-segment eliminations	-	(14,492)	-	14,492	-
Segment income (loss)	1,374,943	48,515	(102,089)	-	1,321,369
Income tax expense					(156,094)
Net income					1,165,275

Year ended December 31, 2015	Principal Properties	Strategic Investments	Corporate	Inter-segment Eliminations	Total
Revenue	366,411	-	-	-	366,411
Gain on commodity contracts	52,767	-	-	-	52,767
	419,178	-	-	-	419,178
Expenses					
Operating expense	90,043	-	-	-	90,043
Transportation and NGLs processing	65,724	-	-	-	65,724
General and administrative	-	5,833	18,024	-	23,857
Share-based compensation	-	6,521	13,983	-	20,504
Depletion and depreciation	622,581	4,265	480	(3,437)	623,889
Exploration and evaluation	47,130	161,862	-	-	208,992
(Gain) loss on sale of oil and gas assets	9,159	(101)	-	-	9,058
Interest and financing	-	2,251	108,412	-	110,663
Accretion of asset retirement obligations	5,448	247	-	-	5,695
Foreign exchange	-	-	61,109	-	61,109
Debt extinguishment	-	-	11,994	-	11,994
	840,085	180,878	214,002	(3,437)	1,231,528
Loss from equity-accounted investments	-	(23,018)	-	-	(23,018)
Write-down of Investments in Securities	-	(81,819)	-	-	(81,819)
Other	2,726	-	179	-	2,905
Drilling rig revenue	-	30,720	-	(29,631)	1,089
Drilling rig expense	-	(9,212)	-	8,606	(606)
	(418,181)	(264,207)	(213,823)	(17,588)	(913,799)
Inter-segment eliminations	-	(17,588)	-	17,588	-
Segment loss	(418,181)	(281,795)	(213,823)	-	(913,799)
Income tax recovery					12,498
Net loss					(901,301)

(Tabular amounts stated in \$ thousands, except as noted)

For the year ended December 31, 2016, the Company had sales to three customers which exceeded ten percent of total revenue. Such sales totaled \$58.7 million, \$48.2 million, and \$37.8 million respectively.

Total Assets

As at December 31	2016	2015
Principal Properties	902,084	2,200,981
Strategic Investments	635,280	411,694
Corporate	521,596	168,360
	2,058,960	2,781,035

Other Income

Year ended December 31	2016	2015
Gain on sale of investments	89	–
Other	1,260	2,905
Drilling rig revenue	223	1,089
Drilling rig expense	(1,196)	(606)
	376	3,388

5. Exploration and Evaluation

Year ended December 31	2016	2015
Balance, beginning of year	363,724	567,420
Additions	48,141	93,411
Change in asset retirement provision	2,942	2,550
Transfers to property, plant and equipment	(23,700)	(112,000)
Dry hole	(13,811)	(15,019)
Expired lease costs	(6,194)	(3,728)
Write-downs	(2,969)	(162,516)
Dispositions	(66,603)	(6,394)
Balance, end of year	301,530	363,724

Additions to E&E assets totaled \$29.0 million (2015 – \$60.4 million) for Principal Properties and \$19.1 million (2015 – \$33.0 million) for Strategic Investments.

Exploration and Evaluation Expense (Income)

Year ended December 31	2016	2015
Geological and geophysical	4,115	6,121
Dry hole	13,811	15,019
Expired lease costs	6,194	3,728
Write-down of exploration and evaluation assets and goodwill	2,969	184,124
Gain on sale of Cavalier Royalty	(99,160)	–
	(72,071)	208,992

In 2016, Cavalier granted a royalty (the "Cavalier Royalty") on its oil sands properties (the "Oil Sands Lands") to an unrelated third party for cash consideration of \$100 million. A gain of \$99.2 million was recorded in respect of the sale of the Cavalier Royalty, which is included in exploration and evaluation expense (income). The Cavalier Royalty is secured by a lien over the Oil Sands Lands.

(Tabular amounts stated in \$ thousands, except as noted)

In 2015, the Company recorded aggregate impairment charges of \$184.1 million related to E&E assets and goodwill, of which \$24.1 million related to the Principal Properties business segment and \$160.0 million related to the Strategic Investments business segment. The Principal Properties impairment charge resulted from the de-recognition of the carrying value of a previously drilled exploratory well which was assessed as being uneconomic to tie-in and bring on production. The Strategic Investments impairment charge resulted from the de-recognition of E&E assets related to Cavalier and MGM Energy due to, among other factors, lower forecast future oil and natural gas prices, an increase in the cost of obtaining capital to fund developments and limited activities in the Northwest Territories by MGM Energy and its partners. Goodwill with a carrying value of \$21.6 million recorded on the acquisition of MGM Energy was also written off as a result of the de-recognition of the E&E assets.

6. Property, Plant and Equipment

Year ended December 31, 2016	Petroleum and natural gas assets	Drilling rigs	Other	Total
Cost				
Balance, December 31, 2015	3,655,956	155,107	29,166	3,840,229
Additions	166,930	1,330	2,761	171,021
Transfers from exploration and evaluation	23,700	–	–	23,700
Dispositions	(1,873,123)	–	(1,492)	(1,874,615)
Change in asset retirement provision	8,975	–	–	8,975
Cost, December 31, 2016	1,982,438	156,437	30,435	2,169,310
Accumulated depletion, depreciation and write-downs				
Balance, December 31, 2015	(1,741,988)	(42,677)	(21,211)	(1,805,876)
Depletion and depreciation	(203,706)	(12,765)	(1,520)	(217,991)
Reversal of prior-years' write-downs	133,246	–	–	133,246
Dispositions	603,796	–	239	604,035
Accumulated depletion, depreciation and write-downs, December 31, 2016	(1,208,652)	(55,442)	(22,492)	(1,286,586)
Net book value, December 31, 2015	1,913,968	112,430	7,955	2,034,353
Net book value, December 31, 2016	773,786	100,995	7,943	882,724

(Tabular amounts stated in \$ thousands, except as noted)

Year ended December 31, 2015	Petroleum and natural gas assets	Drilling rigs	Other	Total
Cost				
Balance, December 31, 2014	3,189,927	127,410	28,082	3,345,419
Additions	379,948	27,697	1,396	409,041
Transfers from exploration and evaluation	112,000	–	–	112,000
Dispositions	(9,588)	–	(312)	(9,900)
Change in asset retirement provision	(16,331)	–	–	(16,331)
Cost, December 31, 2015	3,655,956	155,107	29,166	3,840,229
Accumulated depletion, depreciation and write-downs				
Balance, December 31, 2014	(1,117,596)	(38,722)	(20,536)	(1,176,854)
Depletion and depreciation	(360,654)	(3,955)	(959)	(365,568)
Write-downs	(263,738)	–	–	(263,738)
Dispositions	–	–	284	284
Accumulated depletion, depreciation and write-downs, December 31, 2015	(1,741,988)	(42,677)	(21,211)	(1,805,876)
Net book value, December 31, 2014	2,072,331	88,688	7,546	2,168,565
Net book value, December 31, 2015	1,913,968	112,430	7,955	2,034,353

At December 31, 2016, \$99.2 million (December 31, 2015 – \$81.2 million) of capitalized costs related to incomplete development wells and infrastructure projects were not subject to depletion or depreciation.

Additions to property, plant and equipment in 2016 were \$166.9 million (2015 – \$379.9 million) for Principal Properties, \$1.3 million (2015 – \$27.8 million) for Strategic Investments and \$2.8 million (2015 – \$1.3 million) for Corporate.

In April 2016, Paramount closed the sale of its natural gas processing facility and related midstream assets at Musreau within the Principal Properties business segment for net cash proceeds of \$560.3 million, resulting in the recognition of a gain on sale of \$125.7 million.

In August 2016, Paramount sold the majority of its oil and gas properties in the Musreau/Kakwa area of west central Alberta (the "Musreau Assets") to Seven Generations Energy Ltd. ("Seven Generations" or the "Acquiror") for total consideration of approximately \$2.1 billion (the "Musreau Disposition"), subject to customary post-closing adjustments. The consideration received at closing was comprised of: (i) \$496 million in cash; (ii) 33.5 million class A common shares of the Acquiror ("7Gen Shares") having a market value of approximately \$972 million based on the closing market price of the shares on the day prior to closing; (iii) the assumption by the Acquiror of all US\$450 million principal amount of the Company's senior unsecured notes due in 2023 (the "2023 Notes"); and (iv) certain oil and gas properties of the Acquiror valued at approximately \$6 million. In connection with the Musreau Disposition, the Acquiror also assumed Paramount's processing and transportation commitments relating to the Musreau Assets. Goodwill with a carrying value of \$3.1 million related to the sold properties was derecognized in connection with the disposition. A gain on sale of approximately \$1.2 billion was recorded in respect of the Musreau Disposition within the Principal Properties business segment.

In 2016, Paramount received \$861.1 million in aggregate net cash proceeds on the sale of 29.7 million of the 7Gen Shares it received through the Musreau Disposition, recording a net loss of \$0.8 million, which was included in other income.

(Tabular amounts stated in \$ thousands, except as noted)

In 2016, the Company sold certain non-core properties for aggregate proceeds of \$26.6 million. In the first quarter of 2015, the Company sold certain non-core properties in the Alder Flats area of Alberta for proceeds of \$5.2 million.

Depletion and Depreciation

Year ended December 31	2016	2015
Depletion and depreciation	216,087	365,568
Write-down (reversal of prior year write-downs) of property, plant and equipment	(133,246)	263,738
Inter-segment eliminations	(6,426)	(5,417)
	76,415	623,889

For the twelve months ended December 31, 2016, the Company recorded a \$133.2 million reversal of previously recorded impairment charges related to petroleum and natural gas assets in the Grande Prairie CGU (the "De-Impairment Amount"). These properties are included within the Principal Properties business segment. The impairment reversal resulted from an increase in the estimated recoverable amount of the Grande Prairie CGU at December 31, 2016 compared to December 31, 2015. The \$133.2 million De-Impairment Amount represents the amount required to increase the carrying value of the Grande Prairie CGU to the amount that would have been determined, net of depletion and amortization, had no impairment charges been recognized for the CGU in prior periods. The estimated recoverable amount of the Grande Prairie CGU at December 31, 2016 exceeded the total of the carrying amount of the CGU, including the recognition of the De-Impairment Amount.

The estimated recoverable amount of the Grande Prairie CGU was estimated based on expected after-tax discounted future net cash flows from the production of proved and probable reserves. The increase in the estimated recoverable amount was primarily due to an increase in development activities at Karr-Gold Creek in the Grande Prairie CGU following the Musreau Disposition, recent well performance, well results of other operators in the region, improved economic conditions and other factors.

The recoverable amount of the Grande Prairie CGU as at December 31, 2016 was estimated on a FVLCS basis, using a discounted cash flow method, which is an approach commonly used by market participants to value oil and gas properties (level 3 fair value hierarchy estimate). Cash flows were projected over the expected remaining productive life of the reserves assigned to the CGU, at an after-tax discount rate of 10 percent. Reserves estimates were prepared by Paramount's independent qualified reserves evaluator. The forecast prices used to determine the recoverable amount reflect the following benchmark prices, adjusted for basis differentials to determine local reference prices, transportation costs and quality:

(Average for the period)	2017	2018	2019	2020	2021	2022-2031	Thereafter
Natural Gas							
AECO (\$/MMBtu)	3.40	3.15	3.30	3.60	3.90	3.95 – 4.85	+2%/yr
Henry Hub (US\$/MMBtu)	3.40	3.20	3.35	3.65	4.00	4.05 – 4.85	+2%/yr
Crude Oil							
Edmonton Light (\$/Bbl)	69.80	72.70	75.50	81.10	86.60	88.30 – 105.50	+2%/yr
WTI (US\$/Bbl)	55.00	58.70	62.40	69.00	75.80	77.30 – 92.40	+2%/yr
Foreign Exchange							
\$US / 1 \$CDN	0.75	0.78	0.80	0.83	0.85	0.85	0.85

For the twelve months ended December 31, 2015, the Company recorded aggregate impairment write-downs of \$236.2 million related to petroleum and natural gas assets for the Grande Prairie CGU and

(Tabular amounts stated in \$ thousands, except as noted)

\$27.5 million for the Southern CGU. These properties are included within the Principal Properties business segment. The impairment write-down was recorded because the carrying value of the CGUs exceeded their estimated recoverable amounts. Recoverable amounts as at December 31, 2015 were estimated on a FVLCS basis, using a discounted cash flow method based on expected net discounted future cash flows from the production of proved and probable reserves (level 3 fair value hierarchy estimate).

Following the write-down of the Southern CGU in 2015, the Company determined that the Southern CGU no longer constituted a significant CGU and the Southern CGU petroleum and natural gas assets were included in the Kaybob CGU.

7. Equity-Accounted Investments

As at December 31	2016			2015		
	Shares (000's)	Carrying Value	Market Value ⁽¹⁾	Shares (000's)	Carrying Value	Market Value ⁽¹⁾
Trilogy	19,144	44,053	144,540	19,144	58,370	70,068

(1) Based on the period-end trading price (level one fair value hierarchy estimate).

Loss from equity-accounted investments is comprised of the following:

Year ended December 31	2016	2015
Equity loss	(14,308)	(22,676)
Dilution gain (loss)	(8)	111
Write-down of other equity-accounted investment	—	(453)
	(14,316)	(23,018)

As at December 31, 2016, Paramount owned a 15 percent equity interest in Trilogy (December 31, 2015 – 15 percent). Trilogy is a Canadian energy corporation that develops, produces and sells natural gas, crude oil and natural gas liquids. Trilogy is a publicly listed entity in Canada with its common shares trading on the Toronto Stock Exchange. The following tables summarize the assets, liabilities, equity, revenue and income of Trilogy and Paramount's investment in Trilogy:

As at December 31	2016	2015
Current assets	39,183	45,550
Non-current assets ⁽¹⁾	1,180,860	1,217,088
Current liabilities	(65,921)	(56,172)
Non-current liabilities	(794,895)	(762,578)
Equity ⁽¹⁾	359,227	443,888
Multiply by: Paramount's equity interest	15.2%	15.2%
Paramount's proportionate share of equity	54,537	67,431
Less: portion of share-based compensation recorded in equity of Trilogy	(10,484)	(9,061)
Carrying value of Paramount's investment	44,053	58,370

(1) Includes adjustments to Trilogy's carrying values required in the application of the equity method of investment accounting for shares of Trilogy purchased by the Company in the open market in prior years. Excluding such adjustments, Trilogy's non-current assets as at December 31, 2016 totaled \$1,185,531 (2015 – \$1,220,942) and equity totaled \$363,898 (2015 – \$447,742).

(Tabular amounts stated in \$ thousands, except as noted)

Year ended December 31	2016	2015
Revenue	182,464	268,458
Comprehensive loss ⁽¹⁾	(94,216)	(142,369)
Paramount's share of Trilogy's comprehensive loss	(14,308)	(21,620)

(1) Includes amortization of the adjustments to Trilogy's non-current assets required in the application of the equity method of investment accounting for shares of Trilogy purchased by the Company in prior years in the open market. Excluding such adjustments, Trilogy's comprehensive loss for the year ended December 31, 2016 was \$93,401 (2015 – comprehensive loss \$137,658).

Trilogy had 6.3 million stock options outstanding (2.4 million exercisable) at December 31, 2016 at exercise prices ranging from \$4.49 to \$26.87 per share.

Paramount's share of the income or loss from its other investees for the year ended December 31, 2016 was \$nil (2015 – net loss of \$1.1 million).

8. Investments in Securities

As at December 31	2016		2015	
	Shares (000's)	Market Value	Shares (000's)	Market Value
MEG Energy Corp.	3,700	34,151	3,700	29,674
Privateco		18,675		18,675
Other ⁽¹⁾		11,367		12,365
		64,193		60,714

(1) Includes investments in Marquee Energy Ltd., RMP Energy Inc., Strategic Oil & Gas Ltd., and other public corporations.

For the year ended December 31, 2016 aggregate unrealized losses of \$11.2 million related to the Company's investments in MEG Energy Corp., Marquee Energy Ltd., RMP Energy Inc., and other securities previously recorded in OCI were charged to net earnings as a result of significant decreases in the market prices of the securities. For the year ended December 31, 2015 aggregate unrealized losses of \$81.8 million related to the Company's investments in MEG Energy Corp., Marquee Energy Ltd., Strategic Oil & Gas Ltd. and other securities previously recorded in OCI were charged to net earnings.

9. Limited-Recourse Demand Facilities

As at December 31	2016	2015
Fox Drilling Facility	–	63,380
Cavalier Facility	–	37,531
	–	100,911

In June 2016, the Cavalier Facility was repaid and cancelled. The effective interest rate on the Cavalier Facility for the year ended December 31, 2016 was 3.6 percent (2015 – 3.4 percent). In September 2016, the Fox Drilling Facility was repaid and cancelled. The effective interest rate on the Fox Drilling Facility for the year ended December 31, 2016 was 4.0 percent (2015 – 4.0 percent).

(Tabular amounts stated in \$ thousands, except as noted)

10. Long-Term Debt

As at December 31	2016	2015
Bank credit facility	—	693,045
7% Senior Notes due 2019	—	450,000
6% US Senior Notes due 2023	—	622,800
		1,765,845
Unamortized financing costs, net of premiums and discounts	—	(15,619)
	—	1,750,226

Bank Credit Facility

The Company has a \$100 million revolving bank credit facility (the "Facility"). Borrowings under the Facility bear interest at prime lending rates, US base rates, bankers' acceptance rates, or LIBOR rates, as selected at the discretion of the Company, plus an applicable margin which is dependent upon the Company's debt-to-cash flow ratio. The Facility is secured by a first fixed and floating charge over substantially all of the assets of Paramount, excluding the assets of Fox Drilling and Cavalier.

The borrowing base governs the maximum amount which can be drawn on the Facility. The borrowing base is subject to review and re-determination on a semi-annual basis and more frequently in certain other circumstances. The borrowing base amount is based on the Company's reserves, lenders' projections of future commodity prices and the value attributed to Paramount's equity investments and other assets, among other factors.

The current revolving period of the Facility ends on April 28, 2017. In the event the revolving period is not extended, any undrawn availability would be cancelled and any amounts then outstanding would be permitted to remain outstanding on a non-revolving basis until April 28, 2018, the current maturity date of the Facility.

At December 31, 2016, no amounts were drawn on the Facility. Paramount had undrawn letters of credit outstanding totaling \$20.4 million at December 31, 2016 that reduce the amount available to be drawn under the Facility.

Senior Notes

In 2016, the Company redeemed all \$450 million aggregate principal amount of 7% percent senior unsecured notes due 2019 (the "2019 Notes"). The Company was discharged and released from all obligations and covenants under the 2019 Notes indenture and the 2019 Notes.

In connection with the Musreau Disposition, the Acquiror assumed all US\$450 million aggregate principal amount of Paramount's 2023 Notes in August 2016 and the Company was discharged and released from all obligations and covenants under the 2023 Notes indenture and the 2023 Notes.

Debt extinguishment expense for the year ended December 31, 2016 includes aggregate redemption premiums totaling \$13.5 million in respect of the 2019 Notes and \$13.9 million of unamortized financing fees related to the senior unsecured notes.

(Tabular amounts stated in \$ thousands, except as noted)

11. Asset Retirement Obligations

Year ended December 31	2016	2015
Asset retirement obligations, beginning of year	273,580	287,415
Retirement obligations incurred	6,616	5,010
Revisions to estimated retirement costs	5,301	(18,791)
Obligations settled	(1,753)	(6,641)
Dispositions	(76,057)	(119)
Assumed on corporate acquisition	—	1,011
Accretion expense	4,622	5,695
Asset retirement obligations, end of year	212,309	273,580

At December 31, 2016, the estimated undiscounted asset retirement obligations were \$212.3 million (December 31, 2015 - \$273.6 million), which have been discounted using a weighted average risk-free rate of 2.00 percent (December 31, 2015 – 2.00 percent) and an inflation rate of 2.00 percent (December 31, 2015 – 2.00 percent). These obligations will be settled over the useful lives of the assets, which extend up to 40 years.

12. Share Capital

Paramount's authorized share capital consists of an unlimited number of Common Shares without par value and an unlimited number of preferred shares issuable in series. At December 31, 2016, 105,784,070 (December 31, 2015 – 106,212,487) Common Shares were outstanding, net of 2,865 (December 31, 2015 – 21,508) Common Shares held in trust under the SIP, and no preferred shares were outstanding.

Paramount implemented a normal course issuer bid ("NCIB") on October 13, 2016. The NCIB will terminate on the earlier of: (i) October 12, 2017; and (ii) the date on which the maximum number of Common Shares that can be acquired pursuant to the NCIB are purchased. Paramount may purchase up to 5,441,602 Common Shares under the NCIB. Any Common Shares purchased pursuant to the NCIB will be cancelled by the Company. To December 31, 2016, the Company has purchased and cancelled 622,900 Common Shares under the NCIB at a total cost of \$9.7 million.

In December 2016, the Company's board of directors declared a dividend of 3.8 million 7Gen Shares to holders of record of Paramount's Common Shares on January 9, 2017 (the "January 2017 Dividend"), resulting in an entitlement of approximately 0.036 of a 7Gen Share for each Common Share, subject to rounding for fractions. As a result, a dividend payable of \$119.0 million (\$1.12 per Common Share) was recorded as at December 31, 2016, and the Company's investment in the 3.8 million 7Gen Shares was reclassified to current assets. The dividend was paid on January 16, 2017.

In April 2015, pursuant to a private placement, Paramount issued 0.9 million Common Shares to arms-length investors on a "flow-through" basis in respect of Canadian exploration expenses ("CEE") at a price of \$41.35 per share for gross proceeds of \$37.2 million. The Company incurred \$1.0 million of transaction costs in respect of the transaction, net of tax benefits of \$0.4 million. Paramount has incurred sufficient qualifying expenditures to satisfy commitments related to the issuance.

(Tabular amounts stated in \$ thousands, except as noted)

Weighted Average Common Shares

Year ended December 31	2016		2015	
	Wtd. Avg Shares (000's)	Net income	Wtd. Avg Shares (000's)	Net loss
Net income (loss) – basic	106,157	1,165,275	105,801	(901,301)
Dilutive effect of Paramount Options	235	–	–	–
Net income (loss) – diluted	106,392	1,165,275	105,801	(901,301)

Outstanding Paramount Options can be exchanged for the Company's Common Shares in accordance with the terms of the stock option plan. As a result, they are potentially dilutive and are included in Paramount's diluted per share calculations when they are dilutive to net income. The Company had 4.3 million Paramount Options outstanding at December 31, 2016 (December 31, 2015 – 7.2 million). For the year ended December 31, 2016, 2.3 million (2015 – 7.2 million) Paramount Options were anti-dilutive.

13. Reserves

Reserves at December 31, 2016 include unrealized gains and losses related to changes in the market value of Investments in Securities and contributed surplus amounts in respect of Paramount Options and Cavalier Options. The changes in reserves are as follows:

Year ended December 31, 2016	Unrealized gains on securities	Contributed surplus	Total reserves
Balance, beginning of year	8,637	90,700	99,337
Other comprehensive income	23,087	–	23,087
Share-based compensation	–	25,674	25,674
Options exercised	–	(599)	(599)
Balance, end of year	31,724	115,775	147,499

Year ended December 31, 2015	Unrealized gains (losses) on securities	Contributed surplus	Total reserves
Balance, beginning of year	(29,688)	75,860	46,172
Other comprehensive income	38,325	–	38,325
Share-based compensation	–	23,214	23,214
Options exercised	–	(8,374)	(8,374)
Balance, end of year	8,637	90,700	99,337

(Tabular amounts stated in \$ thousands, except as noted)

14. Share-Based Compensation

Paramount Options

Changes in outstanding Paramount Options are as follows:

	2016		2015	
	Number	Weighted average exercise price (\$/share)	Number	Weighted average exercise price (\$/share)
Balance, beginning of year	7,238,650	34.66	7,275,850	33.75
Granted	4,565,100	12.74	694,000	33.43
Exercised ⁽¹⁾	(175,840)	8.34	(435,950)	13.69
Cancelled	(6,227,300)	35.41	–	–
Forfeited	(148,040)	21.05	(291,000)	40.52
Expired	(930,450)	29.83	(4,250)	25.85
Balance, end of year	4,322,120	13.00	7,238,650	34.66
Options exercisable, end of year	811,740	8.26	3,991,050	34.85

(1) For Paramount Options exercised in 2016, the weighted average market price of Paramount's Common Shares on the dates exercised was \$16.41 (2015 – \$33.95).

Share-based compensation expense for the year ended December 31, 2016 includes \$13.8 million related to Paramount Options cancelled in the year.

The weighted average remaining contractual life and exercise prices of Paramount Options outstanding as of December 31, 2016 are as follows:

Exercise Prices	Awards Outstanding		
	Number	Remaining contractual life (years)	Weighted average exercise price
\$8.17	2,200,120	3.3	8.17
\$8.18 - \$18.23	2,122,000	5.3	18.01
	4,322,120	4.3	13.00

(Tabular amounts stated in \$ thousands, except as noted)

The grant date fair value of Paramount Options was estimated using the Black-Scholes-Merton model incorporating the following weighted average inputs:

	Options awarded in 2016	Options awarded in 2015
Weighted average exercise price (\$ / share)	12.74	33.43
Volatility (%)	53.9	41.9
Expected life of share options (years)	3.7	2.1
Pre-vest annual forfeiture rate (%)	6.1	3.7
Risk-free interest rate (%)	0.7	0.6
Expected dividend yield (%)	nil	nil
Weighted average fair value of awards per share (\$ / share)	4.79	8.02

The estimated expected life of Paramount Options is based on historical exercise patterns. Volatility is generally estimated based on the historical volatility of the trading price of the Company's Common Shares over the most recent period that is commensurate with the expected term of the option, and may be normalized for significant transactions and other factors.

Cavalier Options

During 2016, 0.5 million Cavalier Options were forfeited and 5.0 million Cavalier Options were cancelled. Share-based compensation expense for the year ended December 31, 2016 includes \$0.5 million related to the cancelled Cavalier Options. In the first quarter of 2017, 5.0 million new Cavalier Options were granted.

During 2015, no Cavalier Options were granted and a total of 0.4 million Cavalier Options were forfeited during the year, resulting in a net balance of 5.5 million Cavalier Options outstanding at December 31, 2015.

Stock Incentive Plan – Shares Held in Trust

Year ended December 31	2016		2015	
	Shares (000's)	Shares (000's)	Shares (000's)	Shares (000's)
Balance, beginning of year	22	135	54	508
Shares purchased	-	-	9	316
Change in vested and unvested shares	(19)	(126)	(41)	(689)
Balance, end of year	3	9	22	135

Employee Benefit Costs

Year ended December 31	2016	2015
Stock option plans	25,674	22,669
Stock incentive plan	2,097	(2,165)
Share-based compensation expense	27,771	20,504
Salaries and benefits, net of recoveries	18,015	16,366
	45,786	36,870

(Tabular amounts stated in \$ thousands, except as noted)

15. Income Tax

The following table reconciles income taxes calculated at the Canadian statutory rate to Paramount's recorded income tax expense (recovery):

Year ended December 31	2016	2015
Income (loss) before tax	1,321,369	(913,799)
Effective Canadian statutory income tax rate	27.0%	26.0%
Expected income tax expense (recovery)	356,770	(237,588)
Effect on income taxes of:		
Statutory and other rate differences	703	(20,710)
Gain on sale of oil and gas assets	(11,610)	–
Loss from equity-accounted investments	3,865	5,985
Write-down of Investments in Securities	3,034	21,273
Change in unrecognized deferred income tax asset	(186,657)	194,169
Goodwill impairment	–	5,620
Flow-through share renunciations	1,472	2,156
Share-based compensation	6,932	5,894
Foreign exchange on 2023 Notes	(13,995)	15,812
Non-deductible items and other	(4,420)	(5,109)
Income tax expense (recovery)	156,094	(12,498)

The following table summarizes the temporary differences that give rise to the deferred income tax asset (liability):

As at December 31	2016	2015
Property, plant and equipment	(241,779)	(138,790)
Investments	(2,673)	(1,397)
Asset retirement obligations	56,837	73,855
Non-capital losses	177,474	228,460
Other	4,016	(7,305)
Deferred income tax asset (liability)	(6,125)	154,823

The following table summarizes movements of the deferred income tax asset (liability) during the year:

Year ended December 31	2016	2015
Deferred income tax asset, beginning of year	154,823	152,487
Deferred income tax recovery (expense)	(156,094)	12,509
Deferred income tax expense included in other comprehensive income	(1,276)	(1,314)
Flow-through share renunciations	(4,065)	(6,582)
Other	487	(2,277)
Deferred income tax asset (liability), end of year	(6,125)	154,823

As of December 31, 2016, Paramount has \$658.0 million (2015 – \$1,565.6 million) of unused non-capital losses that expire between 2032 and 2035. The Company has \$311.0 million (2015 – \$307.1 million) of deductible temporary differences in respect of investments for which no deferred income tax asset has been recorded.

At each reporting date, Paramount assesses the recoverability of the deferred income tax asset to determine whether it is more likely than not that the carrying value of the asset will be realized. As at December 31, 2015, the Company concluded that a portion of the carrying value of the deferred income

(Tabular amounts stated in \$ thousands, except as noted)

tax asset was not probable of realization, and accordingly, a de-recognition of \$194.2 million of the deferred income tax asset was recorded.

In 2010, the Company received reassessments of its income taxes from the Canada Revenue Agency (the "CRA") and provincial tax authorities relating to a prior year transaction (the "Reassessments"). Paramount filed notices of objection to the Reassessments and, as a condition of its right to proceed with the objection, the Company was required to deposit approximately \$20 million with the CRA. In 2015, the Company's notices of objection were accepted by the CRA and the deposit, plus interest, was returned to Paramount.

16. Financial Instruments and Risk Management

Financial Instruments

Financial instruments at December 31, 2016 consisted of cash and cash equivalents, accounts receivable, Investments in Securities, accounts payable and accrued liabilities, and risk management liabilities.

Risk Management

The Company had the following financial commodity contracts in place as at December 31, 2016:

Instruments	Aggregate notional	Average fixed price	Fair Value	Remaining term
Gas – NYMEX Swaps (Sale)	40,000 MMBtu/d	US\$3.44/MMBtu	(3,497)	January 2017 – December 2017
Gas – NYMEX Swap (Purchase)	10,000 MMBtu/d	US\$3.04/MMBtu	2,897	January 2017 – December 2017
Oil – NYMEX WTI Swaps (Sale)	2,000 Bbl/d	CDN\$70.43/Bbl	(3,679)	January 2017 – December 2017
Oil – NYMEX WTI Swap (Sale)	1,000 Bbl/d	US\$54.50/Bbl	(901)	January 2017 – December 2017
			(5,180)	

In February 2017, the Company entered into the following financial commodity contracts:

Instruments	Aggregate notional	Average fixed price	Remaining term
Gas – NYMEX Swaps (Purchase)	30,000 MMBtu/d	US\$3.16/MMBtu	March 2017 – December 2017

(Tabular amounts stated in \$ thousands, except as noted)

Changes in the fair value of risk management assets and liabilities are as follows:

Year ended December 31	2016	2015
Fair value, beginning of year	40,207	–
Changes in fair value	253	55,215
Settlements (received)	(45,640)	(15,008)
Fair value, end of year	(5,180)	40,207

The gain on commodity contracts for the year ended December 31, 2015 includes \$2.5 million related to realized losses in respect of marketing activities.

Paramount is exposed to market risks where the fair values or future cash flows of financial instruments are impacted by changes in underlying market prices.

Commodity Price Risk

Paramount uses financial commodity contracts from time-to-time to manage exposure to commodity price volatility. The Company is exposed to commodity price risk on these instruments, as changes in underlying commodity prices will impact the market values of the contracts and ultimately the amounts received or paid upon settlement.

At December 31, 2016, assuming all other variables are held constant, the following table presents the impact of changes in commodity prices on Paramount's net earnings due to changes in the fair value of financial commodity contracts:

	US\$0.25/MMBtu increase	US\$0.25/MMBtu decrease
Natural Gas Contracts	(2,738)	2,738
	US\$5.00/Bbl increase	US\$5.00/Bbl decrease
Crude Oil Contracts	(6,100)	6,100

Foreign Currency Risk

Paramount is exposed to foreign currency risk on financial instruments denominated in US dollars including cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, and risk management assets and liabilities.

Sales prices for natural gas, crude oil and natural gas liquids and the value of financial commodity contracts denominated in Canadian dollars are determined with reference to US benchmark prices, therefore a weakening of the Canadian dollar relative to the US dollar will increase the revenue received in Canadian dollars for the sale of Company's production and the value of such financial commodity contracts. Paramount's expenditures are primarily in Canadian dollars, but include equipment and other items sourced from the United States and settled in US dollars.

Equity Price Risk

Paramount is exposed to equity price risk associated with changes in the market value of its investments.

(Tabular amounts stated in \$ thousands, except as noted)

Credit Risk

Paramount is exposed to credit risk on its financial instruments where a financial loss would be experienced if a counterparty to a financial asset failed to meet its obligations. The Company manages credit risk by endeavoring to enter into contracts with counterparties that possess high credit ratings, employing net settlement agreements, employing letters of credit and limiting available credit when necessary. The maximum credit risk exposure at December 31, 2016 is limited to the carrying value of cash and cash equivalents and accounts receivable.

Paramount's primary objectives with respect to cash and cash equivalents are to minimize financial risk and maintain high liquidity. The Company's cash and cash equivalents are deposited with financial institutions with investment grade credit ratings and are highly liquid. Accounts receivable include balances due from customers and partners in the oil and gas industry and are subject to normal industry credit risk. At December 31, 2016, Paramount had had balances due from one joint venture partner that represented approximately 12 percent of the Company's total accounts receivable.

Liquidity Risk

Liquidity risk is the risk that Paramount will be unable to meet its financial obligations. The Company manages liquidity risk by ensuring that it has sufficient cash and cash equivalents, credit facilities and other financial resources available to meet its obligations.

The Company forecasts cash flows for a period of at least 12 months to identify financial requirements. These requirements are met through a combination of cash flows from operations, cash and cash equivalents, and if required, credit facilities, the sale of assets and capital market transactions.

Accounts Payable and Accrued Liabilities

As at December 31	2016	2015
Trade and accrued payables	80,869	97,883
Joint operation and other payables	481	3,138
Interest payable and financing costs	235	2,538
Flow-through share renunciation obligations	–	4,065
	81,585	107,624

Trade and accrued payables and joint operation and other payables are non-interest bearing and are normally settled within 30 to 60 days.

Accounts Receivable

As at December 31	2016	2015
Revenue receivable	11,586	35,528
Joint operation receivable and other	12,309	13,202
	23,895	48,730

Revenue receivable and joint operation receivables are non-interest bearing and are generally settled on 30 day terms.

In estimating the recoverability of joint operation receivables, the Company performs a risk analysis considering the type and age of the outstanding receivables and the credit worthiness of the counterparties. The Company has determined that there was no impairment of joint operation receivables as at December 31, 2016.

(Tabular amounts stated in \$ thousands, except as noted)

17. Consolidated Statement of Cash Flows - Selected Information

Items Not Involving Cash

Year ended December 31	2016	2015
Commodity contracts	45,387	(40,207)
Share-based compensation	27,771	20,504
Depletion and depreciation	76,415	623,889
Exploration and evaluation	(76,186)	202,871
(Gain) loss on sale of oil and gas assets	(1,379,965)	9,058
Accretion of asset retirement obligations	4,622	5,695
Foreign exchange	(43,154)	59,984
Loss from equity-accounted investments	14,316	23,018
Write-down of Investments in Securities	11,235	81,819
Deferred income tax	156,094	(12,509)
Other	2,178	2,265
	(1,161,287)	976,387

Supplemental Cash Flow Information

Year ended December 31	2016	2015
Interest paid	71,070	107,839
Current tax refunded	—	(10)

Components of cash and cash equivalents

As at December 31	2016	2015
Cash	76,575	11,941
Cash equivalents	545,297	—
	621,872	11,941

18. Capital Structure

Paramount's primary objectives in managing its capital structure are to:

- i. maintain a flexible capital structure which optimizes the cost of capital at an acceptable level of risk;
- ii. maintain sufficient liquidity to support ongoing operations, capital expenditure programs, strategic initiatives and the repayment of debt obligations when due; and
- iii. maximize shareholder returns.

Paramount manages its capital structure to support current and future business plans and periodically adjusts the structure in response to changes in economic conditions and the risk characteristics of the Company's underlying assets and operations. Paramount monitors metrics such as the Company's debt-to-equity and debt-to-cash flow ratios, among others, to measure the status of its capital structure. The Company has not established fixed quantitative thresholds for such metrics. The capital structure may be adjusted by issuing or repurchasing shares, altering debt levels, modifying capital spending programs, acquiring or disposing of assets, and participating in joint ventures, the availability of any such means being dependent upon market conditions.

(Tabular amounts stated in \$ thousands, except as noted)

Paramount's capital structure consists of the following:

Net Cash (Debt)

As at December 31	2016	2015
Adjusted working capital surplus (deficit) ⁽¹⁾	565,897	(37,839)
Limited-recourse demand facilities	-	(100,911)
Facility	-	(693,045)
Senior notes ⁽²⁾	-	(1,072,800)
Net cash (debt)	565,897	(1,904,595)

(1) Adjusted working capital excludes accounts payable and accrued liabilities related to the Company's obligation to renounce qualifying expenditures for flow-through share issuances (December 31, 2016 - nil, December 31, 2015 - \$4.1 million), risk management assets and liabilities, and limited-recourse demand facilities.

(2) Excludes unamortized issue premiums and financing costs.

Shareholders' Equity

As at December 31	2016	2015
Share capital	1,639,466	1,646,984
Accumulated deficit	(152,182)	(1,197,627)
Reserves	147,499	99,337
Total shareholders' equity	1,634,783	548,694

19. Related Party Transactions

Service Agreements

Paramount engages in transactions with Trilogy in the normal course of business, including joint operations. All transactions between Paramount and Trilogy are recorded at their exchange amounts.

During 2016, Paramount charged \$0.4 million (2015 – \$0.5 million) to Trilogy in respect of operational and administrative services. Paramount charged \$4.2 million (2015 – \$3.4 million) to Trilogy and was charged \$8.6 million (2015 – \$2.6 million) by Trilogy in respect of joint operations. As of December 31, 2016, Paramount had a net receivable balance due from Trilogy of \$0.2 million (2015 – net payable of \$0.2 million).

Compensation of Key Management Personnel

Year ended December 31	2016	2015
Salaries and benefits	3,038	1,339
Share-based compensation	9,018	9,913
	12,056	11,252

(Tabular amounts stated in \$ thousands, except as noted)

20. Commitments and Contingencies

Paramount had the following commitments as at December 31, 2016:

	Within one year	After one year but not more than five years	More than five years
Petroleum and natural gas transportation and processing commitments ⁽¹⁾	39,918	192,863	229,248
Operating leases and other	8,886	9,242	1,250
	48,804	202,105	230,498

(1) Certain of the transportation and processing commitments are secured by outstanding letters of credit totaling \$5.1 million at December 31, 2016 (2015 – \$104.6 million).

Operating Lease Commitment

Paramount's head office lease expires in 2022. The Company incurred office lease costs of \$3.7 million in 2016 (2015 – \$3.7 million).

Contingencies

In the normal course of Paramount's operations, the Company may become involved in, named as a party to, or be the subject of, various legal proceedings, including regulatory proceedings, tax proceedings and legal actions. The outcome of outstanding, pending or future proceedings cannot be predicted with certainty. Paramount does not anticipate that these claims will have a material impact on its financial position.

In 2016, a release occurred from a non-operated pipeline in which the Company owns a 50 percent interest. The operator, and owner of the remaining 50 percent, has initiated response, containment and remediation activities ("Response Activities"). Total costs to complete the Response Activities are estimated at approximately \$45 million. It is Paramount's assessment that it is not responsible for the costs of the Response Activities and as a result, no provision has been recorded in the Consolidated Financial Statements.

Tax and royalty legislation and regulations, and government interpretation and administration thereof, continually changes. As a result, there are often tax and royalty matters under review by relevant government authorities. All tax and royalty filings are subject to subsequent government audit and potential reassessments. Accordingly, the final liability may differ materially from amounts estimated and recorded.

CORPORATE INFORMATION

OFFICERS

C. H. Riddell
Executive Chairman

J. H. T. Riddell
President and
Chief Executive Officer

B. K. Lee
Chief Financial Officer

G. W. P. McMillan
Corporate Operating Officer

D. S. Purdy
Corporate Operating Officer

J. Wittenberg
Corporate Operating Officer

M. S. Han
V.P. Information Services

P. R. Kinvig
V.P. Finance and Controller

M. Ockenden
V.P. Corporate Planning

P. G. Tahmazian
V.P. Midstream

E. M. Shier
General Counsel and
Corporate Secretary,
Manager Land

L. A. Friesen
Assistant Corporate Secretary

DIRECTORS

C. H. Riddell
Executive Chairman
Paramount Resources Ltd.
Calgary, Alberta

J. H. T. Riddell ⁽²⁾
President and
Chief Executive Officer
Paramount Resources Ltd.
Calgary, Alberta

J. G. M. Bell ^{(1) (3) (4)}
Chief Operating Officer
Founders Advantage Capital Corp.
Calgary, Alberta

J. C. Gorman ^{(1) (3) (4)}
Independent Businessman
Calgary, Alberta

D. Jungé C.F.A. ^{(2) (4)}
Chairman of the Board
Pitcairn Trust Company
Bryn Athyn, Pennsylvania

D. M. Knott ⁽⁴⁾
Managing General Partner
Knott Partners, L.P.
Syosset, New York

S. L. Riddell Rose
President and
Chief Executive Officer
Perpetual Energy Inc.
Calgary, Alberta

J. B. Roy ^{(1) (2) (3) (4)}
Independent Businessman
Calgary, Alberta

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

CORPORATE OFFICE

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BANK

Bank of Montreal
Calgary, Alberta

CONSULTING ENGINEERS

**McDaniel & Associates
Consultants Ltd.**
Calgary, Alberta

AUDITORS

Ernst & Young LLP
Calgary, Alberta

STOCK EXCHANGE LISTING

The Toronto Stock Exchange
("POU")