CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015

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INDEPENDENT AUDITORS' REPORT

To the Shareholders of Madalena Energy Inc.

We have audited the accompanying consolidated financial statements of Madalena Energy Inc. which comprise the consolidated statements of financial position as at December 31, 2016 and December 31, 2015, the consolidated statements of loss and comprehensive loss, changes in shareholders' equity and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the 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 consolidated financial position of Madalena Energy Inc. as at December 31, 2016 and December 31, 2015, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards.

Emphasis of Matter

Without modifying our opinion, we draw attention to Note 2 in the consolidated financial statements which indicates that Madalena Energy Inc. generated a net loss of $32.1 million and has a working capital deficit of $4.4 million at December 31, 2016 and has financial commitments in the near term for development and exploration programs in excess of forecast available cash resources as well as uncertainty as to whether additional capital can be raised on terms acceptable to the Madalena Energy Inc. to meet the shortfall. These conditions, along with other matters as set forth in Note 2 to the consolidated financial statements, indicate the existence of a material uncertainty that may cast significant doubt about the Madalena Energy Inc.'s ability to continue as a going concern.

KPMG LLP

Chartered Professional Accountants

May 1, 2017
Calgary, Canada

Consolidated Statements of Financial Position

USD 000s	Note	As at December 31 2016	As at December 31 2015
		(note 5)	(note 5)
Assets			
Current assets			
Cash and cash equivalents		**4,071**	3,912
Trade and other receivables		**12,836**	17,882
Inventory		**1,432**	2,415
Assets held for sale	8	**1,265**	-
Other current assets		**465**	622
Available for sale securities	16	**-**	5,361
		20,069	30,192
Property, plant and equipment	6	**53,544**	89,365
Exploration and evaluation assets	7	**49,340**	43,767
Other long-term assets	10	**275**	593
		123,228	163,917
Liabilities			
Current liabilities			
Refundable deposit	21	**3,000**	-
Current portion of long-term debt	9	**1,619**	3,944
Trade and other payables		**15,098**	23,216
Taxes payable		**1,184**	2,570
Decommissioning obligations	12	**3,581**	-
		24,482	29,730
Convertible debentures	11	**1,143**	-
Long-term debt	9	**-**	1,972
Deferred income tax liability	19	**8,394**	9,906
Decommissioning obligations	12	**16,813**	20,641
Other long-term liabilities	21	**2,138**	1,575
		52,970	63,824
Shareholders' Equity			
Share capital	13	**238,973**	238,758
Contributed surplus		**16,066**	14,520
Equity component of convertible debentures	11	**76**	-
Accumulated other comprehensive loss		**(27,157)**	(32,062)
Deficit		**(157,700)**	(121,123)
		70,258	100,093
		123,228	163,917

Going concern (note 2)
Commitments and Other Long-term Liabilities (note 21)
Subsequent Events (notes 8, 9, 21 and 22)

See the accompanying Notes to the Consolidated Financial Statements

On behalf of the Board:

[signed] "Keith Macdonald"
Keith Macdonald
Director

[signed] "Eric Mark"
Eric Mark
Director

Madalena energy inc.

Consolidated Statements of Loss and Comprehensive Loss

USD 000s, except per share amounts	Note	Year ended December 31 2016	2015
		(note 5)	(note 5)
Revenues			
Oil and natural gas revenues		**50,152**	81,725
Royalties		**(8,039)**	(13,217)
Other income	16	**390**	13,857
		42,503	82,365
Expenses			
Operating	24	**23,567**	33,294
General and administrative	24	**9,858**	10,264
Finance (income) expenses	17	**3,122**	(1,251)
Share-based and long-term incentive compensation	14, 15	**1,549**	1,078
Depletion and depreciation	6	**19,805**	25,792
Gain on disposal of assets	8b, 21	**(2,227)**	-
Impairment	6, 7	**18,238**	8,400
		73,912	77,577
Income (Loss) before income taxes		**(31,409)**	4,788
Income tax recovery (expense)			
Current	19	**(2,203)**	(5,359)
Deferred	19	**1,512**	(5,593)
		(691)	(10,952)
Loss from continuing operations		**(32,100)**	(6,164)
Net loss from discontinued operations	5a	**(4,477)**	(7,541)
Net loss		**(36,577)**	(13,705)
Foreign currency translation adjustment		**820**	(5,081)
Available for sale securities	16	**(68)**	68
Comprehensive loss		**(35,825)**	(18,718)
Loss per share			
Basic and diluted - continuing	13	**(0.06)**	(0.01)
Basic and diluted - total	5a, 13	**(0.07)**	(0.03)

See the accompanying Notes to the Consolidated Financial Statements

Consolidated Statements of Changes in Shareholders' Equity

USD 000s	Share Capital (note 13)	Contributed Surplus	Equity Component of Convertible Debentures (note 11)	Accumulated Other Comprehensive Loss	Deficit	Total Equity
Balance at December 31, 2015	**238,758**	**14,520**	**-**	**(32,062)**	**(121,123)**	**100,093**
Net loss	**-**	**-**	**-**	**-**	**(36,577)**	**(36,577)**
Recycle of other comprehensive loss due to discontinued operations (note 5a)	**-**	**-**	**-**	**4,153**	**-**	**4,153**
Foreign currency translation adjustment	**-**	**-**	**-**	**820**	**-**	**820**
Share-based compensation (note 14)	**-**	**1,546**	**-**	**-**	**-**	**1,546**
Common shares issued	**215**	**-**	**-**	**-**	**-**	**215**
Equity component of convertible debentures		**-**	**76**	**-**	**-**	**76**
Available for sale securities (note 16)	**-**	**-**	**-**	**(68)**	**-**	**(68)**
Balance at December 31, 2016	**238,973**	**16,066**	**76**	**(27,157)**	**(157,700)**	**70,258**

Balance at December 31, 2014	237,928	13,555	-	(27,049)	(107,418)	117,016
Net loss	-	-	-	-	(13,705)	(13,705)
Foreign currency translation adjustment	-	-	-	(5,081)	-	(5,081)
Stock options exercised	830	(353)	-	-	-	477
Share-based compensation	-	1,318	-	-	-	1,318
Available for sale securities (note 16)	-	-	-	68	-	68
Balance at December 31, 2015	238,758	14,520	-	(32,062)	(121,123)	100,093

See the accompanying Notes to the Consolidated Financial Statements

Consolidated Statements of Cash Flows

USD 000s	Note	Year ended December 31 2016 (note 5)	Year ended December 31 2015 (note 5)
Cash provided by (used in):			
Operating			
Net loss		**(36,577)**	(13,705)
Items not affecting cash:			
Depletion and depreciation	5a, 6	**19,968**	26,318
Impairment	5a, 6, 7	**18,238**	13,758
Accretion	5a, 17	**255**	347
Fair value change on convertible debentures held	8b	**190**	-
Fair value change on assets held for sale	8a	**(14)**	-
Equity loss pick up	8a	**614**	-
Gain on disposal of assets	8b, 21	**(2,227)**	-
Unrealized loss on commodity contracts		**-**	150
Share-based and long-term incentive compensation	5a,14,15	**1,570**	1,077
Deferred income tax expense (recovery)	19	**(1,512)**	5,593
Unrealized gain on foreign exchange	17	**(161)**	(3,922)
Lease commitment liability	21	**908**	-
Non-cash reduction of contingent liability	21	**(29)**	(1,815)
Realized other comprehensive loss	5a	**4,153**	-
Loss on sale of discontinued operations	5b	**18**	-
Change in other long-term assets		**(718)**	(492)
Change in non-cash working capital	20	**8,178**	(5,468)
Decommissioning obligations settled		**-**	(4)
Cash flow from operating activities		**12,854**	21,837
Investing			
Property, plant and equipment additions	6	**(2,482)**	(32,872)
Evaluation and exploration assets additions	7	**(3,857)**	(8,545)
Proceeds on sale of assets		**54**	-
Change in other long-term assets		**-**	1,931
Change in non-cash working capital	20	**(4,766)**	972
Net cash used in investing activities		**(11,051)**	(38,514)
Financing			
Issue of common shares	13	**-**	477
Convertible debenture proceeds, net of fees	11	**1,241**	-
Investment disposal proceeds, net of fees	8b	**525**	-
Bank loan repayment	9	**(3,500)**	(1,323)
Bank loan proceeds	9	**-**	9,992
Net cash from (used in) financing activities		**(1,734)**	9,146
Change in cash and cash equivalents		**69**	(7,531)
Cash and cash equivalents, beginning of year		**3,912**	11,572
Impact of foreign exchange on cash balances		**90**	(129)
Cash and cash equivalents, end of year		**4,071**	3,912

See the accompanying Notes to the Consolidated Financial Statements

1. Reporting Entity

Madalena Energy Inc. (the "Company" or "Madalena") is involved in the exploration, development and production of oil and natural gas in Argentina and its principal place of business is Suite 200, 707 – 7th Avenue S.W., Calgary, Alberta, T2P 3H6.

The consolidated financial statements include the results of the following wholly-owned subsidiaries:

- Madalena Petroleum Ltd. (Canada) ("MPL")
- Madalena Austral S.A. (Argentina) ("MASA")
- Madalena Energy Argentina S.R.L. (Argentina) ("MEA")
- Madalena Petroleum Americas Limited (Barbados) ("MPAL")
- Madalena Petroleum Holdings Limited (Barbados)
- Madalena Ventures International Holding Company Inc. (Barbados)
- Madalena Ventures International Inc. (Barbados)
- Pet-Ja S.A. (Argentina)

On January 1, 2017, MEA and MASA were amalgamated into one legal entity, continuing under the name of MEA.

2. Basis of Preparation and Going Concern

These consolidated financial statements have been prepared on the basis that the Company is a going concern and will continue to realize its assets and discharge its liabilities in the normal course of operations for the foreseeable future. For the year ended December 31, 2016, the Company has reported a net loss from continuing operations of $32.1 million, had a working capital deficit of approximately $4.4 million at December 31, 2016 and significant future capital commitments to develop its properties. It is currently anticipated that forecasted cash flow from operating activities will not be sufficient to resolve the current working capital deficit and fund the anticipated capital commitments through 2017 as outlined in note 21.

The ability of the Company to continue as a going concern is dependent upon the Company's ability to access additional funding to resolve the current working capital deficit and to meet its anticipated capital commitments through 2017. Potential additional sources of capital include issuing shares, the sale of non-core assets, farming-out existing opportunities or attempting to obtain new credit facilities.

The need to access additional capital to fund the existing and ongoing operations creates a material uncertainty that may cast significant doubt about the Company's ability to continue as a going concern. These consolidated financial statements do not reflect adjustments in the carrying values of the assets and liabilities, expenses and the consolidated statements of financial position classifications that would be necessary if the going concern assumption were not appropriate. Such adjustments could be material.

Statement of Compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB"), and are presented in United States Dollars ("USD") unless otherwise indicated.

These consolidated financial statements follow the same accounting policies and methods of computation for all periods presented as outlined in note 3.

The consolidated financial statements were approved and authorized for issue by the Company's Board of Directors on May 1, 2017.

Basis of Measurement
The consolidated financial statements have been prepared on the historical cost basis, except as described in the accompanying notes.

Functional and Presentation Currency
The presentation currency is the USD. The functional currency of the parent Company is the Canadian dollar (“CAD”). The USD is the functional currency of all subsidiaries.

Use of Estimates and Judgments
The preparation of consolidated financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the year in which the change is identified, and prospectively in future periods.

Critical Judgments in Applying Accounting Policies
The following are critical judgments that management has made in the process of applying accounting policies and that have the most significant effect on the amounts recognized in the consolidated financial statements.

- The Company’s assets are aggregated into cash-generating units for the purpose of calculating impairment. Cash generating units ("CGU" or "CGUs") are based on an assessment of the unit’s ability to generate independent cash inflows. The determination of these CGUs is based on management’s judgment in regard to shared infrastructure, geographical proximity of properties, commodity and/or petroleum type and similar exposure to market risk.

- Judgment is required when assessing if impairment indicators exist and therefore whether impairment testing is required. In determining the recoverable amount of assets, in the absence of quoted market prices, impairment tests are based on estimates of reserves, production rates, future oil and natural gas prices, future costs, discount rates, market value of land, and other relevant assumptions.

- The Company’s concessions in Argentina are, from time to time, subject to renewal which requires approval from regulatory authorities. As there is no indication that pending extensions will not be approved or revised contracts will not be entered into, management has used judgment to conclude that all extensions or a revised form of a block contract will be approved. If the Company fails to obtain block contract renewals, the carrying value of the Company’s property, plant and equipment and exploration and evaluation assets could be negatively impacted. Further, commitments entered into for concessions are based on the agreement signed at the time of concession entry, extension or renewal. To the extent that commitments have not been fulfilled by the expiry date, the Company may enter into negotiations to extend or renew. Should the concession not be extended or renewed, the Company may be responsible for any outstanding commitments.

- The application of the Company’s accounting policy for exploration and evaluation assets requires management to make certain judgments as to future events and circumstances as to whether economic quantities of reserves or commercial resources have been found.

- Management has exercised judgment in concluding that joint arrangements are subject to joint control. Specifically, judgment has been used in determining that decisions concerning the relevant activities of each arrangement require that the specified parties must act together even though the Company’s interests in these arrangements may not be the same as the other parties to the arrangement. Madalena has classified and accounted for its interests in joint arrangements as joint operations.

- Judgments are made by management to determine the likelihood of whether deferred income tax assets at the end of the reporting period will be realized from future taxable earnings.

- Determination of Functional Currency:

  Judgments made by management in determining the appropriate functional currency include an analysis of primary and secondary indicators, as follows:

  (1) Primary indicators of functional currency included the review of the currency that mainly influences sales prices; the currency whose competitive forces and regulations mainly determine sales price; and the currency that mainly influences labour, material and other costs. Specific relevant factors that management considered included:

  - the government of Argentina sets the benchmark price for oil in USD per barrel and although the benchmark prices do not always follow world oil price changes in a predictable manner, the government is aware of and takes into consideration world prices when establishing the benchmark;
  - although settled in the Argentina peso (“ARS”), all oil and gas sales are invoiced in USD and various credits and incentives that the Company is entitled to through the government of Argentina are expected to be denominated in USD;
  - the Company’s budget is prepared and managed in USD; and
  - the majority of anticipated spending in the next 3 – 5 years is expected to be weighted to USD denominated expenditures, mainly as a result of the anticipated capital spending budgets in Argentina, although influenced as well by USD denominated operating costs. The size of the expenditures being made will result in the engagement of international companies that will require USD as the invoicing currency.

  (2) Secondary indicators of functional currency determination include the currency in which funds from financing are generated; the currency in which funds from operations are retained; the degree of autonomy of the foreign operation; the frequency of the transactions with the reporting entity; the cash flow impact on the reporting entity and the ability of the foreign operation to finance its own activities. Relevant indicators considered in management’s assessment included:

  - as the expectation of growth existed, the anticipated financing currency was and continues to be the USD. Although ARS loans are available, given the Company’s planned growth, any financing of significance is expected to be USD denominated; and
  - funds retained in Argentina are in ARS.

While the above noted factors are mixed in support of both the USD and ARS, Management concludes that when considered collectively, it is appropriate to continue the conclusion that the USD is the appropriate functional currency for the Argentine subsidiaries.

Key Sources of Estimation Uncertainty

The following are key estimates and the assumptions made by management affecting the measurement of balances and transaction in these consolidated financial statements:

- Estimation of recoverable quantities of proven and probable and/or contingent reserves include estimates and assumptions regarding future commodity prices, exchange rates, discount rates and production and transportation costs for future cash flows as well as the interpretation of complex geological and geophysical models and data. These estimates are reviewed at least annually, through the engagement of qualified independent reserves evaluators. Changes in reported reserves can affect the impairment of assets, the decommissioning obligations, the economic feasibility of exploration and evaluation assets and the amounts reported for depletion, depreciation and amortization of property, plant and equipment.

- The Company estimates the decommissioning obligations for oil and natural gas wells and their associated production facilities, if applicable. In most instances, removal of assets and remediation occurs many years into the future. Amounts recorded for the decommissioning obligations and related accretion expense require assumptions regarding removal date, the extent of reclamation activities required, the engineering methodology for estimating cost, inflation estimates, and the estimate of the specific discount rates for these liabilities in order to determine the present value of these obligation settlements.

- In a business combination, management makes estimates of the fair value of assets acquired and liabilities assumed which includes assessing the value of oil and gas properties based upon the estimation of recoverable quantities of proven and probable and/or contingent reserves being acquired. These estimates impact the potential for recognizing goodwill or a bargain purchase gain, future depletion and impairment.

- A number of accounting policies and disclosures require that fair value measurements be determined, specifically, business combinations and financial instruments. In determining fair value, the Company uses observable market data as much as possible. The fair value hierarchy used:
  - Level 1 – Quoted prices in active markets for identical assets or liabilities. Cash and cash equivalents, and the refundable deposit are Level 1 financial instruments.
  - Level 2 – Observable prices for similar assets or liabilities, either directly or indirectly determined. Long-term debt is a Level 2 financial instrument.
  - Level 3 – Unobservable input sources. Convertible debentures issued and the convertible debenture asset are Level 3 financial instruments.

3. Significant Accounting Policies

(a) Basis of Consolidation

i. Subsidiaries

Subsidiaries are entities controlled by Madalena. The Company controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date on which control commences until the date on which control ceases.

Inter-company balances and transactions, including unrealized income and expenses arising from inter-company transactions, are eliminated in preparing the consolidated financial statements, unless IFRS indicates otherwise.

ii. Jointly Controlled Operations and Assets

Some of the Company’s oil and natural gas activities involve jointly controlled assets. The consolidated financial statements include the Company’s share of these jointly controlled assets and a proportionate share of the related revenue and related costs.

Madalena currently has 11 concessions in Argentina. Of the concessions owned by Madalena in Argentina, seven are governed by a Union Transitoria de Empresas (“UTE”), which is an agreement entered into between two or more parties with the purpose of gathering human, technological and economic resources temporarily, in order to develop or execute a project, render a service or provide a specific supply. The UTE parties maintain at all times their legal and economic independence. The UTE is not a separate legal entity and no separate legal entities are established by the parties of the UTE to conduct business on behalf of the UTE. The Company has determined these agreements to result in joint operations, and accounts for these operations in accordance with its proportionate working interest ("WI").

The Company's WI at December 31, 2016 in the UTEs is as follows:

- Surubi - (85%)
- Palmar Largo - (14%)
- El Vinalar – (100%)
- Santa Victoria – (100%)
- Coirón Amargo-Norte – (35%)
- Coirón Amargo-Sur Este – (90%)
- Curamhuele (90%)

iii. Associated companies

Associated companies are entities over which the Company has significant influence, but not control, generally accompanied by a shareholding giving rise to voting rights of 20% and above but not exceeding 50%. Investments in associated companies are accounted for in the consolidated financial statements using the equity method of accounting less impairment losses, if any.

Investments in associated companies are initially recognized at cost. The cost of an acquisition is measured at the fair value of the assets given, equity instruments issued or liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition.

In applying the equity method of accounting, Madalena's share of its associated companies' post-acquisition profits or losses are recognized in profit or loss and its share of post-acquisition other comprehensive income is recognized in other comprehensive income. These post-acquisition movements and distributions received from the associated companies are adjusted against the carrying amount of the investment. When Madalena's share of losses in an associated company equals or exceeds its interest in the associated company, including any other unsecured non-current receivables, Madalena does not recognize further losses, unless it has obligations or has made payments on behalf of the associated company.

Unrealized gains on transactions between the Company and its associated companies are eliminated to the extent of Madalena's interest in the associated companies. Unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. The accounting polices of associated companies have been changed where necessary to ensure consistency with the accounting policies adopted by the Company.

Gains and losses arising from partial disposals or dilutions in investments in associated companies are recognized in profit or loss.

Investments in associated companies are derecognized when the Company loses significant influence. Any retained interest in the entity is remeasured at its fair value. The difference between the carrying amount of the retained investment at the date when significant influence is lost and its fair value is recognized in profit or loss.

(b) Foreign Currency

Foreign currency transactions are translated into the respective functional currencies of Madalena and its subsidiaries using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at period end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in profit and loss.

The results and financial position of the parent company is translated into USD for presentation purposes as follows:

i. assets and liabilities for each statement of financial position presented are translated at the period end rate at the date of that balance sheet;
ii. income and expenses for each year are translated at average exchange rates (unless this is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated on the dates of the transactions); and
iii. all resulting exchange differences are recognized as a foreign currency translation adjustment in a separate component of equity called 'accumulated other comprehensive loss'.

When the settlement of a monetary item receivable from or payable to a foreign operation is neither planned nor likely in the foreseeable future, foreign currency gains and losses arising from such items are considered to form part of a net investment in the foreign operation and are recognized in other comprehensive income, and are presented in the foreign currency translation adjustment in equity. Where these are not considered to form part of the net investment, these foreign currency gains and losses are recognized as part of finance (income) expenses in the consolidated statements of loss.

When an operation with a functional currency other than the USD is disposed of, the proportionate share of the cumulative exchange differences previously recognized in equity would be recognized in the statement of loss, as part of the gain or loss on sale.

(c) Financial Instruments

i. Financial assets

Financial assets are classified as financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments or available-for-sale financial assets, as appropriate. The Company determines the classification of its financial assets at initial recognition.

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

Fair value through profit or loss
Financial assets or liabilities (including derivative assets) are classified in this category if they are held for trading. Financial assets at fair value through profit or loss are initially recognized at fair value with changes in fair value recorded through profit or loss. See also financial liabilities, fair value through profit or loss, below.

Loans and receivables
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement at fair value, such financial assets are subsequently measured at amortized cost less impairment. Loans and receivables are comprised of trade and other receivables. Impairments are determined through review and assessment of collectability of the amounts, given the counterparty in question, aging and other relevant factors in the circumstances.

Held-to-maturity investments
These assets are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Company's management has the intention and ability to hold to maturity and include other long-term assets. These assets are measured at amortized cost. If there is objective evidence that the investment is impaired, determined by reference to external credit ratings and other relevant indicators, the financial asset is measured at the present value of estimated future cash flows. Any changes to the carrying amount of the investment, including impairment losses, are recognized in profit or loss.

Available-for-sale financial assets
Non-derivative financial assets not included in the above categories are classified as available-for-sale. They are carried at fair value with changes in fair value recognized as other comprehensive income and classified as a component of equity and include available for sale securities. Where a decline in the fair value of an available-for-sale financial asset constitutes objective evidence of impairment, the amount of the loss is removed from equity and recognized in the profit or loss. When financial assets classified as available for sale are sold, the accumulated fair value adjustments recognized in other comprehensive income are included in profit or loss.

ii. Financial liabilities

Financial liabilities are classified as financial liabilities at fair value through profit or loss and other financial liabilities, as appropriate. The Company determines the classification of its financial liabilities at initial recognition.

Fair value through profit or loss
This category comprises derivatives or liabilities acquired or incurred principally for the purpose of selling or repurchasing in the near term. They are carried in the statement of financial position at fair value with changes in fair value recognized in profit or loss.

Other financial liabilities
This category includes trade and other payables and taxes payable, which are recognized at amortized cost. Non-current liabilities are recorded at the amount at which they are expected to be settled or amortized cost, and includes long-term debt and convertible debentures.

(d) Cash and cash equivalents

Cash and cash equivalents in the statement of financial position comprise cash held at banks and short-term deposits with an original maturity of three months or less. For the purpose of the consolidated statement of cash flows, cash and cash equivalents consist of cash and cash equivalents as defined above, net of any outstanding bank overdrafts.

(e) Business combinations

Business combinations are accounted for using the acquisition method. The identifiable assets acquired and liabilities and contingent liabilities assumed are measured at their fair values at the acquisition date. The cost of an acquisition is measured as the aggregate consideration transferred, measured at the acquisition date fair value. If the cost of the acquisition is less than the fair value of the net assets acquired, the difference is recognized immediately in profit and loss. If the cost of the acquisition is more than the fair value of the net assets acquired, the difference is recognized on the statement of financial position as goodwill. Acquisition costs incurred are expensed.

(f) Property, Plant and Equipment and Exploration and Evaluation Assets

i. Pre-license costs

Exploration and evaluation ("E&E") costs incurred prior to receiving the legal rights to explore an area are expensed when incurred.

ii. Exploration and evaluation assets

Exploration licenses, unproved property acquisition costs, geological and geophysical costs and costs directly associated with an exploration well and appraisal activities are capitalized within E&E assets. The costs are accumulated in cost centers by well, field or exploration area pending determination of their technical feasibility and commercial viability. Upon determination of technical feasibility and commercial viability, E&E assets are first tested for impairment and then reclassified from E&E assets to property, plant and equipment. E&E assets are not depleted but are assessed for impairment when there are indicators of impairment.

Initial wells on an E&E property that are drilled for the purpose of proving the technical feasibility and commercial viability of a reserve are capitalized and the property remains in the E&E phase pending a decision to fully develop the property. Multiple wells may need to be drilled to determine whether the E&E property will be developed. A review of each exploration area is carried out to ascertain whether technical feasibility and commercial viability has been established and there is a reasonable assessment of the economics associated with the future production of those reserves, required government and regulatory approvals have been obtained, or are likely to be obtained and management has made the decision to proceed with development and production of the project by incurring the future capital costs attributed to them. Upon determination of technical feasibility and commercial viability, E&E assets attributable to those reserves, in that particular area, are first tested for impairment and then reclassified from E&E assets to property, plant and equipment. If the cost of the asset is greater than the fair value, then the excess is written off in profit or loss.

iii. Property, plant and equipment assets ("PP&E")

PP&E assets are measured at cost less accumulated depletion, depreciation and amortization and accumulated net impairment losses. Development and production assets are accumulated into major area cost centers and represent the cost of developing the commercial reserves and initiating production. Capitalized costs include the purchase price or construction cost of the asset, any costs directly attributable to bringing the asset into operation, the estimate of any decommissioning obligation and borrowing costs for qualifying assets, if any. The purchase price or construction cost is the aggregate amount paid and the fair value of any other consideration given to acquire the asset.

iv. Subsequent costs

Costs incurred subsequent to the determination of technical feasibility and commercial viability and the costs of replacing components of equipment are recognized as PP&E only when they increase the future economic benefits embodied in the specific asset to which they relate. All other expenditures are expensed as incurred. Such capitalized amounts generally represent costs incurred in developing proven and/or probable reserves and bringing in or enhancing production from such reserves, and are accumulated on a field or geotechnical area basis. The carrying amount of any replaced or sold component is derecognized. The costs of the day-to-day servicing of PP&E are recognized in profit or loss as incurred.

An asset within PP&E is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on de-recognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in profit or loss in the period in which the item is derecognized.

Exchanges of assets within PP&E are measured at fair value unless the exchange transaction lacks commercial substance or the fair value of neither the asset received nor the asset given up is reliably measurable. Unless the fair value of the asset received is more clearly evident, the cost of the acquired asset is measured at the fair value of the asset given up. Where fair value is not used, the cost of the acquired asset is measured at the carrying amount of the asset given up. The gain or loss on de-recognition of the asset given up is recognized in profit and loss.

v. Depletion and depreciation

Depletion of oil and natural gas properties and depreciation of production equipment are calculated based on the establishment of depletable components, using the unit-of-production method. Components are generally determined at a field level. The component's volumes of total proven and probable oil and natural gas reserves and production before royalties, as determined by independent petroleum reservoir engineers is the unit basis for calculating depletion. Natural gas reserves and production are converted to equivalent barrels of oil based upon the energy equivalent conversion ratio of six thousand cubic feet of natural gas to one barrel of oil, calculated in accordance with National Instrument 51-101 - *Standards of Disclosure for Oil and Gas Activities*. The depletion base includes all capitalized costs and estimated future development costs of proven and probable undeveloped reserves.

Corporate assets primarily consist of office furniture and equipment and leasehold improvements, which are stated at cost less accumulated depreciation and are depreciated over the estimated useful lives of the assets. Office furniture and equipment is depreciated at rates ranging from 10 to 33%.

vi. Impairment

The carrying amounts of the Company's PP&E and E&E assets are reviewed at each reporting date to determine whether an indication of impairment exists. If any such indication exists, then the asset's recoverable amount is estimated. In addition, E&E assets are assessed for impairment when they are reclassified to PP&E and also if facts and circumstances suggest that the carrying amount exceeds the recoverable amount.

For the purpose of impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets. The recoverable amount of an asset or a CGU is the greater of its value in use and its fair value less costs to sell.

Fair value less costs to sell is determined as the amount that would be obtained for the sale of a CGU in an arm's length transaction between knowledgeable and willing parties. Fair value less costs to sell of a CGU can also be determined by using assumptions that an independent market participant may take into account. This evaluation could use discounted future net cash flows of proved and probable reserves using forecast prices and costs including the development of prospective lands.

Madalena's management determines value in use for each CGU by estimating the present value of estimated future net cash flows from continued production through exploitation of its proved and probable reserves. Management applies a present value to these cash flows using a pre-tax discount rate range depending on the category of reserves being discounted. The discount rates reflect current market assessments and the risks specific to the assets.

E&E assets are allocated to related CGUs when they are assessed for impairment, both at the time of any triggering facts and circumstances as well as upon their eventual reclassification to PP&E.

An impairment loss is recognized if the carrying amount of an asset or its CGU exceeds its estimated recoverable amount. Impairment losses are recognized in profit or loss. Impairment losses recognized in respect of CGU's are allocated first to reduce the carrying amount of any goodwill, should it exist, allocated to the units, and then to reduce the carrying amounts of the other assets in the unit (group of units) on a pro rata basis.

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

(g) Share Based Compensation and Long-term Incentive Plan

i. Share based compensation

The grant date fair value of equity settled options granted to employees and directors is recognized as share-based compensation expense with a corresponding increase in contributed surplus over the vesting period. A forfeiture rate is estimated on the grant date and is subsequently adjusted each period to eventually reflect the actual number of options that vest. Upon exercise of the stock options, the consideration received plus the amount previously recorded in contributed surplus is recorded as an increase in share capital.

ii. Long-term incentive plan

For cash based incentive plans, units issued are recorded at fair value and recognized over the requisite service period. Changes in fair value each period are recognized in the statement of loss.

(h) Decommissioning Obligations

Obligations for dismantling, decommissioning and site disturbance remediation may arise as a result of the Company's activities. Once it is determined that an obligation exists, a decommissioning obligation is recorded for the estimated cost of site restoration, with the offset capitalized in the relevant asset category.

Decommissioning obligations are measured at the present value of management's best estimate of the expected expenditures, including the timing, that is required to remediate the property. The decommissioning obligation reflects current market assessments of the time value of money and the risks specific to the liability. The discount and inflation rates used to present value the obligation is based on the risk free rate associated with the currency by which payment is most influenced. Subsequent to the initial measurement, the obligation is adjusted at the end of each period to reflect the passage of time, changes in the estimated future cash flows underlying the obligation, and for changes in discount and inflation rates as required. These changes are accounted for prospectively. The increase in the decommissioning obligation due to the passage of time is recognized as finance costs (accretion) whereas increases/decreases due to changes in the estimated future cash flows are capitalized and amortized based on the methodology that is consistent with the asset to which it is capitalized. Actual costs incurred upon settlement of the decommissioning obligations are charged against the provision to the extent the provision was established. Should the asset to which the obligation is related, be disposed of, the decommissioning obligation associated with it is derecognized.

The Company does not recognize decommissioning obligations on facilities in Argentina where it has determined that there is no legal or constructive obligation to perform such activities.

(i) Revenue

Revenue from the sale of oil and natural gas is recorded when the significant risks and rewards of ownership of the product is transferred to the purchaser, which is when legal title passes to the purchaser and when collection is reasonably assured. This is generally at the time product enters the pipeline or is shipped.

(j) Income Taxes

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

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years. Current tax also includes the amounts paid or accrued for minimal presumed income tax, which is an Argentine tax on net assets, levied on those companies with no taxable income.

Deferred tax is recognized using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognized on the initial recognition of assets or liabilities in a transaction that is not a business combination. In addition, deferred tax is not recognized for taxable temporary differences arising on the initial recognition of goodwill. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognized to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized. Unrecognized deferred tax assets are reassessed at each reporting date and are recognized to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

(k) Earnings (Loss) Per Share

The Company presents basic and diluted earnings (loss) per share ("EPS") data for its common shares. Basic EPS is calculated by dividing the profit or loss attributable to common shareholders of the Company by the weighted average number of common shares outstanding during the period. Diluted EPS is determined by adjusting the profit or loss attributable to common shareholders and the weighted average number of common shares outstanding for the effects of all dilutive potential common shares.

(l) Inventory

Inventory consists of oil in tanks and third party pipelines, as well as supplies, and is valued at the lower of cost or market value. The cost of inventory is determined using the weighted average method. Oil inventories include expenditures incurred to produce, upgrade and transport the product to the storage facilities and include operating, depletion and depreciation expenses and cash royalties. Allocated to inventory is a relevant share of operating, royalty expense and depletion. Depending on inventory levels, this could increase or decrease inventory otherwise recorded.

(m) Assets held for sale

Non-current assets are classified as held for sale if it is highly probable that they will be recovered primarily through sale rather than through continuing use. Such assets are generally measured at the lower of their carrying amount and fair value less costs to sell. Impairment losses on initial classifiation as held for sale and subsequent gains and losses on remeasurement are recognized in profit or loss.

(n) Value added tax ("VAT")

VAT on purchases is applied against VAT on sales to reduce the amount paid to the Argentine government. VAT is recorded as a receivable when it is expected that it will be recovered through future sales. To the extent that amounts are expected to be recovered over a period greater than a year, the amount is discounted. VAT does not expire and may be carried forward indefinitely.

4. Accounting Changes

Future Accounting Pronouncements

- In January 2016, the IASB issued amendments to International Accounting Standard ("IAS") 7 (" Statement of Cash Flows") to be applied prospectively for annual periods beginning on or after January 1, 2017 with early adoption permitted. The amendments require disclosure of information enabling users of financial statements to evaluate changes in liabilities arising from financing activities, including changes from cash flows and non-cash changes such as foreign exchange gains or losses. The Company has reviewed these amendments and the impact is not expected to be significant, however will be reflected in the March 31, 2017 condensed interim consolidated financial statements.
- In January 2016, the IASB issued an amendment to IAS 12 ("Income Taxes") to be applied retrospectively for annual periods beginning on or after January 1, 2017. The amendments clarify the existence of deductible temporary differences on debt instruments measured at fair value are solely dependent on a comparison of the carrying amount and its tax base at the end of the reporting period, and is not affected by possible future changes in the carrying amount or expected manner of asset recovery. Madalena has reviewed these amendments and does not believe there will be an impact to our financial statements.
- As of January 1, 2018, Madalena will be required to adopt the following three standards and one interpretation and is evaluating the impact these standards/interpretations may have on Madalena’s consolidated financial statements.
    - In June 2016, the IASB issued amendments to IRFS 2 to clarify how to account for certain types of share – based payment transactions, including cash-settled share-based plans, share-based payments with net of tax settlements and modifications of share-based payments from cash-settled to equity-settled. Application of the changes is allowed prospectively or retroactively if information is available.
    - In July 2014, the IASB issued IFRS 9 "Financial Instruments" to replace IAS 39 "Financial Instruments Recognition and Measurement". The new standard replaces the current multiple classification and measurement models for financial instruments with a single model that has only two classifications categories: amortized cost and fair value. It introduces new requirements for the classification and measurement of financial assets, additional changes relating to financial liabilities and amends the impairment model with the introduction of a new expected credit loss calculation.
    - In May 2014, the IASB issued IFRS 15 "Revenue from Contracts with Customers" to replace IAS 18 "Revenue", IAS 11 "Construction Contracts", and related interpretations. The standard contains a single model that applies to contracts with customers and two approaches to recognizing revenue: at a point in time or over time. The model features a contract-based five-step analysis of transactions to determine whether, how much and when revenue is recognized. New estimates and judgmental thresholds have been introduced, which may affect the amount and/or timing of revenue recognized. The standard must be applied retrospectively, with some exemptions.
    - In December 2016, the IASB issued IFRIC Interpretation 22 ("Foreign Currency Transactions and Advance Consideration.") This Interpretation clarifies the date that should be used for

translation when a foreign currency transaction is involved in an advance payment or receipt. This interpretation may be applied retrospectively or prospectively.

- In January 2016, IASB issued IFRS 16 "Leases". The goal of the standard is to bring leases on the balance sheet for lessees for all leases with a term of more than 12 months, subject to materiality. The standard requires the recognition of a right-of-use asset and the related lease liability. This creates a single lease accounting model for all leases, as there will no longer be a classification test between finance and operating leases. As of January 1, 2019, Madalena will be required to adopt this standard. Madalena is evaluating the impact this standard may have on Madalena's consolidated financial statements.

5. Discontinued Operations

On June 28, 2016 and pursuant to a series of transactions, Madalena sold its Canadian petroleum and natural gas assets in exchange for 6,244,814 escrowed common shares of Point Loma Resources Ltd. ("Point Loma"), with a fair value of $1.9 million and a five-year $2.4 million subordinated secured convertible debenture, bearing interest at 3% per annum, plus an origination fee of 3% of the principal remaining on maturity, payable at the end of the debenture term. Madalena can convert all or part of the debenture plus accrued interest and origination fee into common shares, at Madalena's election, at a fixed price of CAD $0.50 per common share (note 8). The fair value of the convertible debenture at June 28, 2016 was $2.4 million, which included the fair value of the conversion feature, valued at $0.6 million.

These assets consist of the Canadian operating segment and are presented as discontinued operations. The consolidated statements of loss and comprehensive loss have been presented to show the discontinued operations as a single line item, and are therefore separated from continuing operations in the current and comparative periods. The consolidated statements of financial position reflect the disposition of the Canadian operating segment as at June 28, 2016, although the comparatives still contain the Canadian operating segment, as required under IFRS. The consolidated statements of cash flows contain the Canadian operating segment in the current and comparative period, with the cash flow results of the discontinued operation disclosed in note 5c.

a. Net loss from discontinued operations

USD 000s	For the years ended December 31 2016	2015
Revenues		
Oil and natural gas revenues	**430**	1,923
Royalties	**(7)**	(434)
	423	1,489
Expenses (recoveries)		
Operating	**395**	2,712
General and administrative	**127**	353
Finance (income) and expenses	**23**	82
Share-based compensation	**21**	(1)
Depletion and depreciation	**163**	526
Impairment	**-**	5,358
	729	9,030
Loss from operating activities of discontinued operations	**(306)**	(7,541)
Loss on sale of discontinued operations (note 5b)	**(18)**	-
Realized accumulated other comprehensive loss on disposition of Canadian operations[1]	**(4,153)**	-
Net loss from discontinued operations	**(4,477)**	(7,541)
Basic and Diluted EPS	**(0.01)**	(0.02)

(1) This is the cumulative translation adjustment on the sale of the Canadian assets that is recycled through the statement of loss on disposition.

Current and deferred taxes were not impacted by the disposal of the Canadian operating segment as no assets had previously been recognized on the Canadian tax pools.

b. Loss on sale of discontinued operations

USD 000s	
Proceeds (note 8):	
Common shares – Point Loma	1,918
Debenture including conversion feature	2,351
	4,269
Property, plant and equipment disposed of	(6,336)
Exploration and evaluation assets disposed of	(2,419)
Decommissioning liabilities disposed of	4,682
Transaction costs attributable to disposal	(214)
	(4,287)
Loss on sale of discontinued operation – June 28, 2016	(18)

c. Cash flows from (used in) discontinued operations

USD 000s	For the years ended December 31 2016	2015
Net cash used in operating activities	**(41)**	(923)
Net cash from (used in) investing activities	**12**	(3,104)
Net cash flow for period	**(29)**	(4,027)

6. Property, Plant and Equipment ("PP&E")

USD 000s	Oil and Natural Gas Assets	Corporate	Total
Cost			
At December 31, 2014	150,669	1,312	151,981
Additions	30,851	810	31,661
Effect of change in foreign exchange rates	(7,586)	(130)	(7,716)
At December 31, 2015	173,934	1,992	175,926
Additions	5,162	46	5,208
Disposals	(42,018)	-	(42,018)
Effect of change in foreign exchange rates	2,457	21	2,478
At December 31, 2016	**139,535**	**2,059**	**141,594**

USD 000s	Oil and Natural Gas Assets	Corporate	Total
Accumulated depreciation and depletion			
At December 31, 2014	(54,237)	(268)	(54,505)
Depreciation and depletion	(25,981)	(388)	(26,369)
Impairment	(11,651)	-	(11,651)
Effect of change in foreign exchange rates	5,918	46	5,964
At December 31, 2015	(85,951)	(610)	(86,561)
Depreciation and depletion	(18,934)	(498)	(19,432)
Impairment	(15,500)	-	(15,500)
Disposals	35,511	-	35,511
Effect of change in foreign exchange rates	(2,060)	(8)	(2,068)
At December 31, 2016	**(86,934)**	**(1,116)**	**(88,050)**

USD 000s			
Net book value			
At December 31, 2015	87,983	1,382	89,365
At December 31, 2016	**52,601**	**943**	**53,544**

On June 28, 2016 (note 5b), the net book value of PP&E assets associated with the Canadian operating segment amounting to $6.3 million were disposed.

(Tabular amounts are stated in thousands of United States dollars ("USD"), except per share amounts and as otherwise stated)

At December 31, 2016, Madalena determined that indicators of impairment existed in each of its Argentine CGUs due to pricing reductions associated with Argentine oil benchmarks moving toward world prices. CGUs at December 31, 2016 and 2015 were defined at the legal entity level and aggregated up to the concession level for the Argentine branches of MPL and MPAL. As a result, impairment tests were performed over each CGU and two (MASA and the Argentine branches of MPL/MPAL) were deemed to be impaired as at December 31, 2016 as their estimated recoverable amounts were lower than their carrying amounts. The recoverable amounts, calculated as $12.8 million and $5 million for MASA and the Argentine branches of MPL/MPAL, resulted in pre-tax impairment charges of $3 million and $3.2 million for the two CGU's, respectively during the last quarter of 2016. These charges are incremental to those booked during the third quarter of 2016, which amounted to $9.3 million for MEA, and collectively total $15.5 million for the year ended December 31, 2016.

The impaired CGU's recoverable values at December 31, 2016 were estimated using value in use calculations based on future net cash flows expected to be derived from the CGU's proven plus probable reserves from the externally prepared December 31, 2016 reserve report, using a pre-tax discount rate ranging from 22% to 28% depending on the category of reserves, and used the following forecast benchmark commodity price estimates:

Year	Brent Oil Price (1) (USD/bbl)	Argentina Domestic Gas Price (1) (USD/mmbtu)
2017	57.00	4.95
2018	61.00	4.95
2019	66.00	5.05
2020	70.00	5.15
2021	74.00	5.25
2022	77.00	5.36
2023	80.00	5.47
2024	83.00	5.57
2025	86.00	5.69
2026	89.64	5.80
2027+	+2.0%/yr	+2%/yr

(1) The forecast benchmark commodity prices listed above are adjusted for quality differentials, heat content, distance to market and other factors in performing our impairment tests.

Had the discount rate used been 1% higher for the range of discount rates used, additional impairment charges of $1.2 million would have resulted for the year ended December 31, 2016.

An additional $1 decrease in the price deck would have resulted in further impairment charges of $1.6 million for the year ended December 31, 2016.

At December 31, 2015, Madalena determined that indicators of impairment existed in each of its Argentine CGUs. These indicators of impairment were a result of a decline in oil prices resulting in lower netbacks in certain CGUs in addition to the increase in discount rate to be applied in the CGU impairment calculations due to the increased country risk identified as at December 31, 2015. As a result, an impairment test was performed for each CGU. As at December 31, 2015, one of the three Argentine CGUs (MEA) was determined to be impaired as the estimated recoverable amount was lower than the carrying amount. The recoverable amount, calculated as $32.0 million, resulted in a pre-tax impairment charge of $8.4 million for the year ended December 31, 2015.

The impaired CGU's recoverable value was estimated using a value in use calculation based on future net cash flows expected to be derived from the CGU's proved plus probable reserves from the externally prepared December 31, 2015 reserve report using a pre-tax discount rate ranging from 22% to 28% depending on the category of reserves, and adjusted forecast benchmark commodity price estimate for oil ranging from $65.23 - $88.48/bbl, and natural gas prices ranging from $4.95 - $6.03/mcf, which incorporates Madalena's price differentials.

In assessing its Canadian CGU for impairment at December 31, 2015, the Company concluded that triggers for impairment existed due to the continued reduction in both short and long-term forward Canadian petroleum and natural gas prices. The Company's testing of its Canadian CGU recoverable value, established as fair value less costs to sell, relative to its carrying value, amounted to $1.8 million, and revealed a pre-tax impairment charge of $3.3 million. The recoverable amount was determined based on the amount that would be obtained for the sale of the CGU in an arm's length transaction between knowledgeable and willing parties.

The depletion expense calculation for the year ended December, 2016 included as part of the depletable base, $83.5 million (December 31, 2015 – $92.7 million) for estimated future development costs associated with proved and probable reserves in Argentina.

During the year ended December 31, 2016, approximately $1.3 million (2015 - $1.9 million) of directly attributable general and administration costs were capitalized to property, plant and equipment in Argentina. In addition, share-based compensation of $40 thousand was capitalized for the year ended December 31, 2016 (2015 - $0.2 million).

7. Exploration and Evaluation Assets ("E&E")

USD 000s	
Cost	
At December 31, 2014	37,824
Additions	8,716
Impairment	(2,107)
Effect of change in foreign exchange rates	(666)
At December 31, 2015	43,767
Additions	10,622
Impairment	(2,738)
Disposals	(2,450)
Effect of change in foreign exchange rates	139
At December 31, 2016	49,340

In October 2016, Madalena closed a transaction that was entered into in July 2016, whereby certain E&E land positions in the southwestern region of Coirón Amargo ("CA"), CA-Sur Oeste ("CASO"), which had no accounting value assigned to them, were exchanged for an increase in WI in the existing E&E property in the southeastern region of CA, CA-Sur Este ("CASE"). This non-cash transaction was evaluated to have commercial substance and the fair value of the land acquired of $5.6 million was recorded as an addition to E&E.

On June 28, 2016 (note 5b), the E&E assets associated with the Canadian operating segment amounting to $2.4 million were disposed.

At December 31, 2016, Madalena determined that no impairment triggers existed relating to its Argentine E&E assets. The Cortadera concession was officially relinquished to the Province of Neuquén in October 2016, prior to the release of the Company's third quarter results. Accordingly, the net book value of the Cortadera E&E assets of $2.7 million was written off and recorded as part of Impairment in the consolidated statements of loss during the third quarter, and is included in the year to date impairment for the year ended December 31, 2016.

At December 31, 2015, a trigger for impairment existed for the Canadian E&E assets. The Company's testing of its Canadian E&E assets' recoverable value, established as fair value less costs to sell, relative to its carrying value, amounted to $2.2 million, and revealed a pre-tax impairment charge of $2.1 million, of which $2.0 million had been recorded by September 30, 2015. The impairment was due to continued depressed commodity prices and continued decrease in crown land prices in its undeveloped land holdings in relation to current prices in the area.

At December 31, 2015, Madalena determined there were no triggers for impairment for any of its Argentine E&E assets.

8. Assets Held for Sale and Investments

As a result of the disposal of the Canadian assets on June 28, 2016 (note 5), the Company received the following investments as proceeds:

(a) 6.2 million escrowed common shares of Point Loma. On June 28, 2016, this common share ownership was recorded as an investment in an associate using the equity method of accounting. Madalena owned 23% of the common shares of Point Loma on that date. The initial value assigned on acquisition was $1.9 million. Equity losses for the period ended December 31, 2016 amounted to $0.6 million have been recorded to finance (income) expenses in the consolidated statements of loss for the year ended December 31, 2016.

At December 31, 2016, given the liquidity challenges faced by the Company and the intention to sell all of the common shares of Point Loma, these common shares have been accounted for as assets held for sale ("AHFS") and recorded at fair value. The fair value adjustment at December 31, 2016 amounted to a loss of $14 thousand, after equity accounting ceased as a result of the reclassification to AHFS, and is recorded as part of finance (income) expenses in the consolidated statements of loss for the year ended December 31, 2016.

Subsequent to December 31, 2016, the Company sold 1.6 million of the Point Loma common shares for net cash proceeds of approximately $0.5 million , and realized a gain on sale of approximately $0.1 million.

Pursuant to a purchase and sale agreement dated April 21, 2017 with an arms-length third party, the Company sold 4.7 million escrowed common shares in Point Loma for gross cash proceeds of $0.8 million. These common shares were acquired by Madalena pursuant to the sale of the Company's Canadian oil and gas assets in June 2016 and will be released from escrow in 20% increments in six month intervals commencing July 2017. Closing will take place in two equal tranches. The first tranche was completed on April 24, 2017 and the second tranche is expected to close on or about May 25, 2017.

(b) A five-year $2.4 million subordinated secured 3% convertible debenture from Point Loma, with principal and interest payable at the end of the debenture term. On December 20, 2016, Madalena sold this convertible debenture for cash proceeds of $0.5 million, resulting in a loss on disposal of $1.6 million, which is recorded as part of gain on disposal of assets in the consolidated statements of loss for the year ended December 31, 2016. This convertible debenture was a financial instrument and was designated as fair value through profit and loss as a level III financial asset, and was convertible at the Company's election, into Point Loma common shares. The value of the debenture on the closing date of June 28, 2016 was estimated to be $1.8 million using an annual interest rate of 12%. In addition, management estimated the fair value of the conversion feature to be $0.6 million at June 28, 2016, which factored in a 50% reduction in market price of Point Loma common shares given the limited time the shares have been listed. A Black Scholes pricing model was used to fair value the convertible debenture conversion feature. Fair value losses from June 28, 2016 to the date of sale on December 20, 2016 of $0.2 million, were recorded as part of finance (income) expenses in the consolidated statements of loss for the year ended December 31, 2016.

9. Long-term Debt

Argentina

On May 28, 2015, MEA obtained an ARS 90 million credit facility with Industrial and Commercial Bank of China (Argentina) S.A. ("ICBC"). These funds were utilized on an as needed basis to provide Madalena the necessary liquidity to execute its 2015 Argentine capital budget. The amount outstanding at December 31, 2016 was $1.6 million (December 31, 2015 - $5.9 million) and was fully repaid on February 3, 2017.

The loan bears interest at the variable rate of BADLAR plus approximately 8.8%, resulting in a current borrowing rate of 32.6%.

Security for the Argentine loan was provided by the assignment of the receivables of MEA that arise from the sale of crude oil. The facility includes a quarterly financial covenant, whereby MEA's ratio of debt to earnings before income taxes, depletion, interest and other non-cash items must be equal to or less that 1:1. The earnings before income taxes, depletion, interest and other non-cash items is calculated on a four quarter rolling basis. At December 31, 2016, MEA was in compliance with this covenant at 0.22.

Canada

The Company has no bank debt in Canada at December 31, 2016 and 2015.

10. Other Long-term Assets

Other long-term assets are comprised of long-term receivables for which the fair value approximates the carrying value. The long-term receivables primarily relate to ARS denominated taxes receivable of $0.2 million (December 31, 2015 – nil). In 2015, this account included receivable balances due from an Argentine provincial oil and gas company of $0.6 million and in 2016, amounts associated with this receivable were eliminated (note 21).

11. Convertible Debentures

On July 13, 2016, the Company completed a private placement of $1.2 million (CAD $1.6 million) 12% secured convertible debentures, net of fees, primarily to insiders or existing shareholders, with a June 30, 2019 maturity date. The debentures are convertible into common shares of the Company at a conversion price of CAD $0.25 per common share, any time after January 13, 2017. Interest on the debentures is payable semi-annually, in arrears, on December 31 and June 30. Interest accrued to December 31, 2016 amounting to $0.1 million was fully paid at year end. The Company may, at its option and upon providing notice to the debenture holders, repay the outstanding indebtedness. Such repayments involve premiums that reduce as the date to maturity approaches. Although insiders participated in the private placement, the terms and conditions were the same as those available to third parties.

These debentures are a level III financial liability with an embedded conversion feature. As a result, the equity and debt components must be bifurcated. The value assigned to the liability on July 13, 2016 was the present value of the contractually determined stream of future cash flows discounted at 15%, being the rate estimated to be equivalent to that which the market would apply to an instrument with comparable credit status and provide substantially the same cash flows, on the same terms, but without the conversion option. From the date of issuance, the liability component accretes up to its principal value using the effective interest method, with the charge recorded in finance (income) expenses in the consolidated statements of loss.

The following table reconciles the principal amount, liability and equity components of the convertible debentures:

USD 000s	Liability Component	Equity Component	Total
July 13, 2016 issuance	1,165	76	1,241
Accretion (note 17)	29	-	29
Impact of foreign exchange	(51)	-	(51)
Balance December 31, 2016	**1,143**	**76**	**1,219**

Transaction costs totaling $0.1 million were deducted from the amounts issued, on a pro-rata basis between the liability and equity components.

12. Decommissioning Obligations

	Year ended December 31	
USD 000s	**2016**	**2015**
Balance, beginning of year	**20,641**	21,858
Disposals	**(4,902)**	-
Additions from development activities	**381**	210
Additions from exploration activities	**475**	-
Accretion expense (note 5a, 17)	**203**	347
Revision of estimates	**3,302**	(1,028)
Obligations settled	**-**	(4)
Effect of change in foreign exchange rates	**294**	(742)
Balance, end of year	**20,394**	20,641
Current	**3,581**	-
Long-term	**16,813**	20,641
Total	**20,394**	20,641

The total undiscounted amount of cash flows required to settle Madalena's decommissioning obligations in Argentina only at December 31, 2016 is approximately $22.9 million (December 31, 2015 – $26.5 million) with the majority of the costs to be incurred between 2026 and 2027. At December 31, 2016, $3.6 million of the decommissioning obligations are recorded as a current liability and the remainder of $16.8 million as a long-term liability, given that the current obligations are expected to be incurred by December 31, 2017. The decommissioning obligations have been estimated using existing technology at current prices and discounted using discount rates that reflect current market assessments of the time value of money and the risks specific to each liability.

At December 31, 2016 an inflation rate of 1.5% was used (December 31, 2015 – 1%). The risk free rate used to discount the liability at December 31, 2016 was 2.8% (December 31, 2015 – 2.7%). The majority of the Argentine decommissioning obligations are expected to be invoiced in USD and settled through payments in ARS.

The revision of estimates which increased decommissioning liabilities by $3.3 million for the year ended December 31, 2016 (2015 - decrease of $1 million) is comprised of an increase of $2.8 million (2015 - $1.0 million decrease) for changes in well cost estimates, and an increase of $0.5 million (2015 - $0.3 million) relating to a change in the discount rate and a decrease of nil (2015 - $0.3 million) relating to reserve life changes.

13. Share Capital

The Company is authorized to issue an unlimited number of common shares and preferred shares. The holders of common shares are entitled to receive dividends as declared by the Company and are entitled to one vote per share. No preferred shares were outstanding at December 31, 2016 or 2015. No dividends have been declared by the Company.

	Number of Shares 000s	Share Capital 000s
Balance at December 31, 2014	539,783	237,928
Stock options exercised	2,300	830
Balance at December 31, 2015	542,083	238,758
Common shares issued	1,697	215
Balance at December 31, 2016	543,780	238,973

2016
On July 21, 2016, 1,696,970 common shares were issued at a price of CAD $0.165 pursuant to a settlement agreement with a former employee, reducing the contractual severance liability owed by $0.2 million.

2015
During 2015, 2.3 million stock options were exercised at prices ranging from CAD $0.21 - $0.35 for cash proceeds of $0.5 million.

Net Loss Per Share
As at December 31, 2016, there is no resulting dilutive impact of the convertible debentures or share options. The following table provides the weighted average number of common shares used in the per share calculations:

	Year ended December 31	
	2016	**2015**
Weighted average number of common shares - basic and diluted – 000s	**542,880**	541,017
Net loss from continuing operations - USD 000s	**(32,100)**	(6,164)
Per share – basic & diluted - continuing operations ($/share)	**(0.06)**	(0.01)

14. Share-based Compensation

Under the Company's stock option plan, directors, officers, employees and certain consultants are eligible to receive options to acquire common stock of the Company. The exercise price of the granted options is no less than the closing trading price per share on the last day preceding the date of the grant. Total options granted cannot exceed 10% of the issued and outstanding common shares of the Company. Options granted to directors, officers, employees and consultants vest over three years on each anniversary of the grant date. Options expire three to five years from the grant date. There are no cash settlement alternatives for employees under the Company's stock option plan.

During the year ended December 31, 2016, 8,650,000 (2015 – 15,963,000) options were granted to directors, officers, and employees of the Company, at an exercise price of CAD $0.27 per share (2015 – average of $0.30).

Movements in the number of stock options outstanding and their related weighted average exercise prices are summarized as follows:

	Number of options 000s	Weighted average exercise price
Outstanding at December 31, 2014	25,880	0.42
Granted	15,963	0.30
Exercised	(2,300)	0.26
Forfeited	(1,954)	0.39
Expired or cancelled	(2,770)	0.61
Outstanding at December 31, 2015	34,819	0.35
Granted	8,650	0.27
Forfeited	(7,329)	0.30
Expired or cancelled	(2,015)	0.53
Outstanding at December 31, 2016	34,125	0.34
Exercisable at December 31, 2016	20,173	0.35

The range of exercise prices of the outstanding options

Exercise price (CAD)	Number of Options Outstanding 000s	Weighted Average Contractual Life of options outstanding (years)	Number of outstanding options that are exercisable 000s
0.27	6,267	4.04	800
0.28	400	3.98	133
0.29	4,225	0.48	4,225
0.30	11,654	3.67	5,107
0.35	4,462	1.42	4,270
0.41	1,060	1.17	1,060
0.42	1,620	0.46	1,620
0.44	150	2.71	100
0.46	350	2.73	233
0.50	3,937	2.53	2,625
	34,125	2.32	20,173

(Tabular amounts are stated in thousands of United States dollars ("USD"), except per share amounts and as otherwise stated)

The fair value of options granted was estimated at the period end date using the Black-Scholes valuation model, resulting in a per option fair value of CAD $0.15 (2015 – CAD $0.18) with weighed average assumptions as follows:

Inputs used to fair value share options granted

	Year ended December 31	
	2016	**2015**
Share price (CAD $)	**0.27**	0.30
Exercise price (CAD $)	**0.27**	0.30
Expected Volatility (%)	**75**	80
Forfeiture rate (%)	**9.8**	9.8
Option life (years)	**4.05**	4.35
Risk-free interest rate (%)	**0.61**	0.59

Expected volatility is estimated by considering historic daily share price volatility. The forfeiture estimate is adjusted each period until the vesting date.

Share-based compensation expense, including amounts in discontinued operations of $21 thousand, arising from the issuance of stock options recognized for the year ended December 31, 2016 was $1.5 million (2015 - $1.1 million). In addition $40 thousand (2015 - $0.2 million capitalized) of share based compensation was capitalized during the year.

15. Long-term Incentive Plan

On August 25, 2016, the Board of Directors approved a long-term cash incentive plan ("LTIP"), whereby certain Argentine employees of the Company are provided an opportunity to benefit as a result of appreciation of the trading price of Madalena's common shares from the issue date, through the payment of cash upon vesting.

On August 26, 2016, 6,505,000 LTIP units (the "Units") were issued to Argentine personnel at an exercise price of CAD$0.145 per common share. The Units vest one-third on each of the first, second and third anniversary dates and are exercisable for a period no later than:

i) December 1 of the third year in which the Units vest; and
ii) Five years from the date of the grant of the Units.

The LTIP expense recorded as part of share-based and long-term incentive compensation expense in the consolidated statements of loss for the year ended December 31, 2016 was $64 thousand and is revalued at the end of each reporting period.

16. Other Income

Other income relates primarily to miscellaneous equipment sales of $0.4 million. In the comparative period other income of $13.9 million related primarily to proceeds from Petroleo Plus Settlement Bonds, of which $5.4 million was recorded in available for sale securities in the consolidated statements of financial position at December 31, 2015. The remaining bonds were sold in 2016 for amounts that approximated carrying value.

Amounts previously recorded in other comprehensive income due to fair value reporting relating to the Petroleo Plus Settlement Bonds of $68 thousand for the year ended December 31, 2015, were recycled through finance (income) expenses in the consolidated statements of loss and comprehensive loss for the year ended December 31, 2016.

17. Finance (Income) Expenses

Finance (Income) and Expenses are made up of the following:

	Year ended December 31	
USD 000s	**2016**	**2015**
Bank charges and fees	**1,229**	2,084
Foreign exchange gain	**(145)**	(3,922)
Decommissioning liability accretion (note 5a, 12)	**203**	265
Accretion of debt component of convertible debentures issued (note 11)	**29**	-
Interest and other expenses	**948**	322
Equity loss pick up (note 8 (a))	**614**	-
Fair value change on convertible debentures held (note 8 (b))	**190**	-
Fair value change on assets held for sale (note 8 (a))	**(14)**	-
Available for sale securities (note 16)	**68**	-
	3,122	(1,251)

	Year ended December 31	
USD 000s	**2016**	**2015**
Realized foreign exchange losses	**16**	-
Unrealized foreign exchange gains	**(161)**	(3,922)
Total	**(145)**	(3,922)
Currency exchange rate at period end:		
$1 USD = CAD	**$1.34**	$1.38
$1 USD = ARS	**15.89**	12.95

18. Related Parties

A director of the Company is a partner of a law firm that provides legal services to the Company. During the year ended December 31, 2016, the Company incurred fees of $0.8 million (2015 - $0.3 million) from this firm for legal services, of which $0.8 million (2015 – $40 thousand) is included in trade and other payables at December 31, 2016. The costs were expensed in general and administrative costs in the consolidated statements of loss.

A director of two of the Company's subsidiaries provides professional services to the Company. During the year ended December 31, 2016, the Company incurred fees of $45 thousand (2015 - nil), for professional fees, of which $45 thousand (2015 - nil) was included in trade and other payables at December 31, 2016.

Of the convertible debentures issued by Madalena in July 2016 (note 11), certain directors and officers of the Company subscribed to 18% of the total issuance.

The transactions arose during the normal course of business and have been recorded at the exchange amounts, which are the amounts agreed upon by the related parties. The terms and conditions of these transactions were no more favourable than those available, or which might reasonably be expected to be available in similar transactions with arm's length third parties.

(Tabular amounts are stated in thousands of United States dollars ("USD"), except per share amounts and as otherwise stated)

19. Income Taxes

The provision for income tax differs from the result that would be obtained by applying the combined Canadian federal and provincial tax rate of 27% (2015 – 26%) to the income (loss) before taxes. The difference results from the following:

	Year ended December 31	
	2016	**2015**
Income (Loss) before income tax – continuing operations	**(31,409)**	4,788
Tax rate	**27%**	26%
Expected income tax recovery (expense)	**8,480**	(1,245)
Recovery (expense) resulting from:		
Effect of foreign tax rates	**(1,130)**	(3,168)
Share-based compensation	**(441)**	(383)
Unrecognized deferred tax benefit and other	**(6,476)**	(9,667)
Canadian tax rate adjustments	**-**	2,020
Non-taxable portion of capital loss	**(234)**	-
Non-taxable differences on foreign operation	**(729)**	1,916
Minimum presumed foreign income tax	**(197)**	(375)
Other	**36**	(50)
Total income tax expense	**(691)**	(10,952)
Attributable to:		
Current tax expense	**(2,203)**	(5,359)
Deferred tax recovery (expense)	**1,512**	(5,593)
Total income tax expense	**(691)**	(10,952)

The current income tax expense relates to current income tax and minimum income tax incurred in Argentina.

Deferred tax assets have not been recognized on the following temporary differences and credits:

	Year ended December 31	
Canada	**2016**	**2015**
Property, plant and equipment	**21,785**	17,162
Decommissioning obligations	**-**	4,387
Share issue costs	**2,011**	3,601
Capital losses	**24,405**	22,692
Non-capital losses (expire 2026 to 2036)	**66,581**	58,956
Foreign tax credits	**40,485**	41,684
Other	**1,503**	-
Total unrecognized temporary differences	**156,770**	148,482

(Tabular amounts are stated in thousands of United States dollars ("USD"), except per share amounts and as otherwise stated)

	Year ended December 31	
Argentina	**2016**	**2015**
Decommissioning obligations	**10,278**	7,520
Non-capital losses (expire 2017 to 2020)	**4,820**	1,672
Accruals & Other	**7,471**	5,871
Minimum tax credits	**3,368**	5,229
Total unrecognized temporary differences	**25,937**	20,292
Barbados		
Non-capital losses (expire 2017 to 2023)	**706**	610
Total unrecognized temporary differences	**706**	610

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

	Year ended December 31				
	2014	**Recognized in statement of loss**	**2015**	**Recognized in statement of loss**	**2016**
Foreign exchange	(276)	(570)	(846)	**72**	**(774)**
Property, plant and equipment	(9,850)	(5,249)	(15,099)	**2,326**	**(12,773)**
Decommissioning obligations	3,574	(517)	3,057	**484**	**3,541**
Non-capital losses	1,548	492	2,040	**(670)**	**1,370**
Accruals and other	316	626	942	**(700)**	**242**
Minimum tax credits	375	(375)	-	**-**	**-**
	(4,313)	(5,593)	(9,906)	**1,512**	**(8,394)**

No deferred tax liability has been recognized for temporary differences associated with investments in subsidiaries and joint ventures as the Company is in a position to control the entities and it is considered probable that these timing differences will not reverse in the foreseeable future.

20. Supplemental Cash Flow Information

Changes in non-cash working capital

	Year ended December 31	
USD 000s	**2016**	**2015**
Available for sale securities	**5,361**	(5,361)
Trade and other receivables	**6,226**	(762)
Other current assets, including inventory	**648**	460
Assets held for sale (note 8)	**(1,265)**	-
Trade, tax and other payables	**(5,390)**	3,748
Impact of foreign exchange on working capital	**(2,168)**	(2,581)
Change in non-cash working capital[1]	**3,412**	(4,496)
Attributable to:		
Operating activities	**8,178**	(5,468)
Investing activities	**(4,766)**	972
	3,412	(4,496)

(1) Change in non-cash working capital excludes the current portion of long-term debt, as this is considered part of financing activities.

Other cash flow information- continuing operations

	Year ended December 31	
USD 000s	**2016**	**2015**
Interest paid	**1,621**	2,145
Interest received	**120**	694
Taxes paid	**3,788**	4,900

21. Commitments and Other Long-term Liabilities

Development and Exploration Commitments

Coirón Amargo ("CA")

Madalena and its partners at the CA concession in the province of Neuquén are responsible for paying 100% of the costs during the exploration and evaluation phase, with Gas y Petróleo del Neuquén S.A. ("GyP"), a provincial government entity, receiving a 10% carry whereby all other partners, including Madalena, are responsible for paying their proportionate share of GyP's WI. Currently, exploration and evaluation phases are contained in CA-Sur, in the southern portion of CA.

In an exploitation or development phase, GyP is responsible for its 10% interest of the incurred capital costs through an assignment of GyP's 10% interest in future production revenue streams to Madalena and its partners. The amounts due to Madalena from GyP are recorded on Madalena's books as a receivable. Currently, exploitation and development phases are contained in CA-Norte, in the northern portion of CA, for which there are no current ongoing commitments.

In conjunction with the sale of the Company's 35% WI at CASO and the concurrent acquisition of an additional 55% WI at CASE, the terms relating to the recovery of previously incurred capital costs at CA-Norte and a recovery of future capital costs to be incurred at CA-Norte, were adjusted.

CASE (90% WI – operated – see subsequent event details below)

Prior to July 11, 2016, Madalena held a 35% WI in the entire CA-Sur exploration and evaluation concession. Pursuant to a series of agreements dated July 11, 2016 and subject to government approvals and an Executive Decree, which were subsequently obtained in October 2016, CA-Sur was divided into two evaluation lots – CASE and CASO. Madalena sold its' interest in CASO in return for an additional 55% WI in CASE and became operator.

Pursuant to the new arrangements, Madalena work commitments at CASE were amended as follows:

USD 000s	**2016**	**2017[(1)]**	**Beyond**
Concession commitments at CASE	-	5,000	5,000[(2)]

(1) Committed values are reflected at 90% WI at December 31, 2016.
(2) Subject to the results in 2017 to be completed, before November 8, 2019.

The new exploration and evaluation permit for CASE expires on November 8, 2019, following which Madalena will be eligible to enter into a development concession.

The sale of its 35% WI in CASO resulted in a pre-tax gain of $3.7 million, net of adjustments relating to the recovery of the previously incurred capital costs referenced above, which has been recorded as part of gain on disposal of assets in the consolidated statements of loss for the year ended December 31, 2016. At December 31, 2016, the Company held a 90% WI in and GyP retained its 10% WI in the CASE block.

On December 7, 2016, the Company entered into agreements with Pan American Energy LLC, Sucursal Argentina ("PAE") relating to the Company's 90% WI at CASE. Pursuant to these agreements, Madalena would receive cash payments of an aggregate of $10 million on closing and sell a 55% WI and operatorship to PAE, thereby retaining a 35% non-operated WI in CASE. A 2017 work program ("Work Program") would be comprised of two well re-entries, which would be undertaken by PAE as the new operator of CASE. Madalena will be carried for the first $5.6 million of costs through this Work Program.

Concurrently, PAE agreed, subject to certain conditions, to provide Madalena with a loan of up to $40 million, on a limited recourse basis, to be drawn-down as required to fund CASE capital expenditures. This limited recourse loan would bear interest at 7% per annum and is repayable in five years from the net revenue generated from the capital expenditure program. The transaction closed on January 10, 2017.

A refundable deposit of $3 million was received on December 13, 2016. The remaining $7 million was received on January 10, 2017. To the extent that Madalena's share of the Work Program extends beyond $5.6 million, Madalena will be required to fund this incremental amount.

Curamhuele Block (90% WI-operated)
At Curamhuele, a concession in the province of Neuquén, the Company is responsible for paying 100% of the costs during the exploration and evaluation phase of a concession to maintain its 90% WI.

In December 2015, Madalena ratified an extension of its second exploration and evaluation term with the Province of Neuquén to September 9, 2016, after which a further extension was available. During the first quarter of 2016, the remaining work commitment relating to the block concession agreement was fulfilled by completing the Yapai.x 1001 well in the Mulichinco and Lower Agrio shale. A performance bond of $17.6 million relating to amounts committed under this exploration and evaluation permit, is posted by the Company. The assets of Madalena Austral S.A., a subsidiary of the Company, are held as security for the bond.

The Company has commenced discussions with the Province of Neuquén to obtain a four year extension of the exploration and evaluation block. The Company has proposed a horizontal multi-frac re-entry in CH.x-1 for $8.2 million to be incurred by March 9, 2019, to obtain this extension.

The Company is waiting on a provincial certification that the $17.6 million of work commitments have been fulfilled and a provincial decree on the new $8.2 million of work commitments. Upon receipt of the provincial certification, the Company anticipates that the $17.6 million performance bond will be cancelled and a new $8.2 million performance bond will be posted.

Puesto Morales Block (100% WI-operated)

USD 000s	**2016**	**2017**	**Beyond**
Concession commitments	4,400	13,300	13,100

The Company is awaiting written provincial approval to transfer $4.4 million of 2016 commitments to 2017.

Santa Victoria Block (100% WI - operated)
The contract can contain up to three exploration and evaluation phases, of which the second expired in April 2015. The second phase required additional work commitments of $4.0 million for which no qualifying expenditures have been made. A performance bond of $3.6 million is in place over the commitments under this exploration and evaluation permit. An application has been submitted and negotiations continue and are currently ongoing with the province of Salta to reach a multi-year extension agreement.

El Chivil Block (100% WI – operated)
The concession's one year extension expiry occurred on September 7, 2016 and during the fourth quarter of 2016, the province of Formosa granted a further six month extension to negotiate a 10-year development period extension, which expires on May 1, 2017. At May 1, 2017, the Company remains in discussions with the province of Formosa.

El Vinalar Block (100% WI – operated)
Salta province granted a block extension to file an investment plan, which expired on November 11, 2016. The Company has requested a further extension from the province of Salta and is awaiting further discussions.

Other Commitments
In November 2016, Madalena sub-leased its former corporate office premises to the end of 2018, with the expectation of further renewals or alternative sub-lease arrangements to the end of the head lease term of September 2022. The difference between the head lease payments under the existing contract and the sub-lease contract income expected over the period of the lease term, results in an onerous contract liability, which must be valued at present value, taking into consideration a discount rate consistent with similarly risked liabilities. The impact of the passage of time on the remaining liability will be recorded through profit and loss over the lease

term. A liability has been recognized of approximately $0.9 million, of which $0.1 million is recorded as part of Trade and other payables and $0.8 million is recorded as part of Other long-term liabilities in the consolidated statements of financial position at December 31, 2016. Without the sub-lease, the total liability would have been approximately $1.5 million. The expense associated with this liability of $0.9 million is recorded as part of general and administrative expenses in the consolidated statements of loss for the year ended December 31, 2016.

Other long-term liabilities
A continuity relating to these liabilities is as follows:

	Year ended December 31	
USD 000s	**2016**	**2015**
Balance, beginning of year	**1,575**	4,296
Lease liability [(1)]	**786**	-
LTIP liability	**64**	-
New contingencies	**19**	-
Settled through negotiation	**(29)**	(1,815)
Effect of change in foreign exchange rates	**(277)**	(906)
Balance, end of year	**2,138**	1,575

(1) Relates to "Other Commitments"

22. Financial Instruments and Risk Management

The Company is exposed to various risks that arise from its business environment and the financial instruments it holds. The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework, policies and procedures. The following outlines the Company's risk exposures and explains how these risks and its capital structure are managed.

Capital Management
The Company's objective has been to maintain its capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The Company manages its capital structure and makes adjustments to it, as it is able to, in light of changes in economic conditions and the risk characteristics of the underlying oil and natural gas assets. The Company considers its capital structure to include shareholders' equity and working capital. In order to maintain or adjust the capital structure, the Company may obtain issue shares, adjust its capital spending to manage current and projected debt levels, sell non-core assets, farm-out existing opportunities or attempt to obtain new credit facilities.

In order to facilitate the management of its capital structure, the Company prepares annual capital expenditure budgets, which are updated throughout the year depending on varying factors including current and forecast prices, actual capital deployment and general industry conditions, if necessary. The focus of the Company throughout 2016 was to access additional capital to enable continuation of the Company.

The Company has not paid or declared any dividends since the date of incorporation, nor are any contemplated in the next twelve months and there are no external restrictions on the Company's capital structure.

At December 31, 2016, the consolidated working capital deficit of the Company was $4.4 million (December 31, 2015 – positive working capital of $0.5 million), consisting of working capital deficiency of $3.4 million (December 31, 2015 - $0.4 million) in Argentina and a working capital deficiency of $1.0 million (December 31, 2015 – positive working capital of $0.9 million) in Canada.

Liquidity risk

Liquidity risk is the risk that the Company will not meet its financial obligations as they become due. The Company's approach to managing liquidity risk is to ensure, as far as reasonable, that it will have sufficient liquidity to meet its liabilities when due. The Company has a working capital deficit of $4.4 million at December 31, 2016 and continued to face liquidity challenges during 2016. Unless the Company is able to raise additional capital or renegotiate its commitments, it does not expect that forecasted cash flows from operating activities will be sufficient to meet its anticipated capital commitments through 2017 and resolve the current working capital deficit (see note 1).

In early January 2017, the Company closed the sale of a 55% WI in the CASE exploration concession for $10 million, of which $3 million was received in December 2016 and the balance in January 2017. In addition, the Company sold 1.6 million common shares in Point Loma in January 2017 for net cash proceeds of approximately $0.5 million. These transactions have temporarily reduced the current liquidity restraints by enabling the Company to pay a significant portion of amounts due to creditors.

In addition, as disclosed in Note 8, the Company sold 4.7 million escrowed common shares in Point Loma for gross cash proceeds of $0.8 million. Closing will take place in two equal tranches. The first tranche was completed on April 24, 2017 and the second tranche is expected to close on or about May 25, 2017.

At December 31, 2016, all of Madalena's cash and cash equivalents of $4.1 million was deposited with banks in Argentina (December 31, 2015 - $2.1 million, 54%), and is held in ARS.

Repatriation of Funds to Canada

Madalena's corporate office is in Canada. Funds are required to enable the Company to maintain its Canadian corporate office and manage the regulatory, reporting, audit, legal and tax requirements of a TSX-V listed company. Prior to the decline in commodity prices, Canadian oil and gas revenues were sufficient to fund the corporate costs incurred. In 2015, with the majority of the Canadian production shut in, it was necessary for the Company to repatriate funds from Argentina. During 2016, $0.7 million (2015 - $7.8 million) was repatriated from Argentina. Notwithstanding this, the Company increased its investment in one of its Argentine subsidiaries by $0.8 million (2015 - nil).

Credit risk

The Company's primary operations are conducted in Argentina. The Company is exposed to credit risk in relation to its cash and cash equivalents, trade and other receivables, and other long-term assets.

Cash and cash equivalents are held with highly rated international and Canadian banks, and therefore the Company does not believe these financial instruments are subject to material credit risk.

Other long-term assets relate to amounts due from various governments in Argentina primarily as it relates to VAT and is collected as revenue is earned. Although collection is slow, it is expected.

In Argentina, the majority of the Company's oil production is sold to the Argentine subsidiaries of major international oil and gas companies. The Company's policy to mitigate credit risk associated with these balances is to establish marketing relationships with large purchasers.

During 2016, a provision for doubtful accounts of $0.2 million has been recorded. No provision was recorded at December 31, 2015.

Maximum exposure to credit risk for trade and other receivables by type of customer

	Year Ended December 31	
USD 000s	**2016**	2015
Oil and natural gas marketing companies	**5,505**	6,903
Other trade receivables	**2,458**	5,015
Total trade receivables	**7,963**	11,918
Taxes receivable	**4,873**	5,964
Total trade and other receivables	**12,836**	17,882

Amounts due from oil and gas marketing companies were subsequently collected by the Company, with the exception of $0.2 million, which is deemed collectible. Of the $2.5 million recorded in other trade receivables, $2.1 million has been collected subsequent to year end, with the remaining balance deemed to be collectible. The taxes receivable balance of $4.9 million relates to current amounts owed from various governments in Argentina for VAT. These are collectible on future revenue.

Aged trade and other receivables

	Year Ended December 31	
USD 000s	**2016**	2015
Current (less than 90 days)	**6,984**	10,878
Past due (more than 90 days)	**979**	1,040
Total	**7,963**	11,918

Amounts totaling $1 million over 90 days were not provided for and $0.9 million has been collected subsequent to year end. The remaining $0.1 million is deemed to be collectible.

Market risk

Changes in commodity prices, interest rates and foreign currency exchange rates can expose the Company to fluctuations in its net earnings and in the fair value of its financial assets and liabilities.

Commodity price risk

The Government of Argentina sets the benchmark (Medanito) price for oil. Although the Argentine refiners used by the Company have paid an average unofficial crude oil price of $60.09 per barrel for the year ended December 31, 2016, official Medanito crude oil averaged $67.50 per barrel for the year ended December 31, 2016 (2015 - $75.00). In January 2017, Madalena was advised that a majority of producers and refiners in Argentina, at the request of the government, have signed a 2017 Medanito crude oil pricing agreement (the "Agreement") allowing for convergence with international Brent pricing over the coming months. International Brent oil prices have been trading at approximately $55.00 per barrel to date in 2017. The 2017 Medanito pricing therefore declines from $59.40/bbl in January 2017 to $55.00/bbl from July 2017 to December 2017. Should international Brent pricing be reached and remain higher than $1.00 above the monthly Medanito floor price for 10 consecutive days, the Agreement will be suspended and international Brent pricing adopted. Should international Brent pricing fall below $45.00 for 10 consecutive days, the Agreement will be reviewed. Although Medanito is set by the government, there can be no certainty that the official oil price will not be further adjusted, nor any assurance that the refiners will not further discount the amount paid.

Gas prices in Argentina are subject to seasonal demand and are negotiated between the producer and the buyer. Summer pricing for the period from October 2016 to April 2017 was set at $4.30/mmbtu. (October 2015 - April 2016 - $4.20/mmbtu). For the winter season from May to September 2017, the price has been set at $5.40/mmbtu (May to September 2016 - $5.35/mmbtu).

Interest rate risk

Had the BADLAR rate associated with the Argentina long-term debt changed by 5%, the associated interest expense would have changed by $0.2 million for the year ended December 31, 2016.

Foreign currency exchange risk

The majority of the Company's exploration and development activities are conducted in Argentina and the majority of the Company's cash and cash equivalents are denominated in ARS. The Company is exposed to currency risk to the extent that revenue, expenses and monetary assets and liabilities are denominated in currencies that differ from the functional currency of the respective entity within the Company.

The impact of a 10% change in foreign exchange rates on gains and losses recorded on financial instruments, when translating from ARS and/or CAD to USD at December 31, 2016 would have changed the unrealized foreign exchange gain recorded in the consolidated statements of loss by $0.5 million for the year ended December 31, 2016. The amount recorded as foreign currency translation adjustment in comprehensive income in the consolidated statements of comprehensive loss would have changed by $0.1 million for the year ended December 31, 2016 as it relates to loans owed from Argentina that are not considered part of the net investment in the subsidiaries.

Fair value of financial instruments

The Company's financial instruments include cash and cash equivalents, trade and other receivables, other long-term assets, refundable deposit, current portion of long-term debt, trade and other payables, taxes payable, convertible debentures issued and long-term debt, the carrying values of which approximate their fair values due to their short-term nature with the exception of: (i) long-term debt, which approximates fair value as a result of its variable interest rate; (ii) convertible debentures issued, which relates to the debt component of these instruments and is accreted up to their principal value over the term of the debenture using the effective interest rate method; (iii) available for sale securities which are recorded at fair value through the statement of other comprehensive loss, and recycled into the statements of loss and comprehensive loss when sold; and (iv) other long-term assets whose calculated fair value approximates its carrying value.

23. Segmented information

The Company is engaged in the exploration and development of oil and gas. With the disposition of the Canadian operating segment on June 28, 2016 (note 5), Madalena's continuing operations are represented by its Argentine petroleum and natural gas producing assets which form one reportable segment and its corporate costs in Canada, which form a second segment. The Company does not have separate operations in Barbados. Barbados entities hold a direct interest in the Argentine businesses and the chief operating decision maker views Barbados as an extension of the Argentine operations. Together they collectively comprise the Argentine operating segment.

	As at and for the year ended December 31, 2016			
USD 000s	Argentina	Corporate	Intersegment Eliminations	Total
Total assets	121,520	24,307	(22,599)	123,228
Total liabilities	70,996	4,573	(22,599)	52,970
Oil and natural gas revenues	50,152	-	-	50,152
Operating expenses	23,567	-	-	23,567
General & administrative expenses	4,906	4,952	-	9,858
Depletion and depreciation	19,574	231	-	19,805
Impairment	18,238	-	-	18,238
Current income tax expense	2,203	-	-	2,203
Net loss – continuing operations	22,725	9,375	-	32,100
Capital expenditures(1)	6,339	-	-	6,339

	As at and for the year ended December 31, 2015			
USD 000s	Argentina	Corporate(2)	Intersegment Eliminations	Total
Total assets	152,977	23,951	(21,978)	154,950
Total liabilities	80,118	625	(21,978)	58,765
Oil and natural gas revenues	81,725	-	-	81,725
Other income	13,857	-	-	13,857
Operating expenses	33,294	-	-	33,294
General & administrative expenses	6,305	3,959	-	10,264
Depletion and depreciation	25,578	214	-	25,792
Impairment	8,400	-	-	8,400
Current income tax expense	5,359	-	-	5,359
Net loss	5,959	205	-	6,164
Capital expenditures(1)	40,899	37	-	40,936

(1) Capital expenditures include cash additions to PP&E and E&E.
(2) For comparative purposes, the Canadian operations have been removed from these amounts (note 5).

For the year ended December 31, 2016, three customers within the Argentine operating segment individually accounted for more than 10% of oil and natural gas revenues, and amounted to $20.1 million, $8.4 million and $6.8 million. For the year ended December 31, 2015, three customers within the Argentina operating segment each individually accounted for more than 10% of oil and natural gas revenues and amounted to $32.9 million, $24.3 million and $8.5 million.

Intersegment eliminations relate to intercompany loans between Canada and Argentina.

24. Supplemental disclosure

(a) Madalena's consolidated statements of loss and comprehensive loss are prepared primarily by nature of expenses, with the exception of employee compensation costs which are included in both the operating and general and administrative expense line items in the consolidated statements of loss and comprehensive loss. The following table details the amount of total employee compensation costs included in the operating and general and administrative expenses line items in the consolidated statements of loss and comprehensive loss.

	Year ended December 31	
USD 000s	**2016**	**2015**
Operating expenses		
Compensation costs	**4,067**	5,000
Transportation and processing	**7,474**	10,865
Maintenance, workovers and others	**12,026**	17,429
	23,567	33,294
General & Administrative expenses		
Compensation costs	**5,221**	6,389
Other	**4,637**	3,875
	9,858	10,264

(b) Key management personnel of the Company consist of its directors and executive officers. As at December 31, 2016, the Company had seven directors and three officers (2015 – 8 directors and 5 officers). The table below summarizes all key management personnel compensation paid and payable during the years ended December 31, 2016 and 2015.

	Year ended December 31	
USD 000s	**2016**	**2015**
Short-term employee benefits, including wages and management fees	**884**	1,683
Severance payments	**774**	-
Share-based compensation	**1,236**	966
	2,894	2,649