2016

ANNUAL REPORT

EXCELLENCE. TRUST. RESPECT. RESPONSIBILITY.

INTERNATIONALLY DIVERSIFIED | SUSTAINABLE GROWTH AND INCOME

VERMILION
ENERGY

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ANNUAL GENERAL MEETING

April 28, 2017
10:00 AM MST
The Ballroom
Metropolitan Centre
333 – 4th Avenue S.W.
Calgary, Alberta

ABBREVIATIONS

$M	thousand dollars
$MM	million dollars
AECO	the daily average benchmark price for natural gas at the AECO 'C' hub in southeast Alberta
bbl(s)	barrel(s)
bbls/d	barrels per day
bcf	billion cubic feet
boe	barrel of oil equivalent, including: crude oil, condensate, natural gas liquids, and natural gas (converted on the basis of one boe for six mcf of natural gas)
boe/d	barrel of oil equivalent per day
btu	British thermal units
DRIP	Dividend Reinvestment Plan
GJ	gigajoules
mbbls	thousand barrels
mboe	thousand barrel of oil equivalent
mcf	thousand cubic feet
mcf/d	thousand cubic feet per day
mmboe	million barrel of oil equivalent
mmbtu	million British thermal units
mmcf	million cubic feet
mmcf/d	million cubic feet per day
MWh	megawatt hour
NBP	the reference price paid for natural gas in the United Kingdom, quoted in pence per therm, at the National Balancing Point Virtual Trading Point. Our production in Ireland is priced with reference to NBP.
NGLs	natural gas liquids, which includes butane, propane, and ethane
PRRT	Petroleum Resource Rent Tax, a profit based tax levied on petroleum projects in Australia
TTF	the price for natural gas in the Netherlands, quoted in MWh of natural gas, at the Title Transfer Facility Virtual Trading Point
WTI	West Texas Intermediate, the reference price paid for crude oil of standard grade in US dollars at Cushing, Oklahoma

DISCLAIMER

Certain statements included or incorporated by reference in this document may constitute forward looking statements or financial outlooks under applicable securities legislation. Such forward looking statements or information typically contain statements with words such as "anticipate", "believe", "expect", "plan", "intend", "estimate", "propose", or similar words suggesting future outcomes or statements regarding an outlook. Forward looking statements or information in this document may include, but are not limited to: capital expenditures; business strategies and objectives; operational and financial performance; estimated reserve quantities and the discounted net present value of future net revenue from such reserves; petroleum and natural gas sales; future production levels (including the timing thereof) and rates of average annual production growth; exploration and development plans; acquisition and disposition plans and the timing thereof; operating and other expenses, including the payment and amount of future dividends; royalty and income tax rates; and the timing of regulatory proceedings and approvals.

Such forward looking statements or information are based on a number of assumptions, all or any of which may prove to be incorrect. In addition to any other assumptions identified in this document, assumptions have been made regarding, among other things: the ability of Vermilion to obtain equipment, services and supplies in a timely manner to carry out its activities in Canada and internationally; the ability of Vermilion to market crude oil, natural gas liquids, and natural gas successfully to current and new customers; the timing and costs of pipeline and storage facility construction and expansion and the ability to secure adequate product transportation; the timely receipt of required regulatory approvals; the ability of Vermilion to obtain financing on acceptable terms; foreign currency exchange rates and interest rates; future crude oil, natural gas liquids, and natural gas prices; and management's expectations relating to the timing and results of exploration and development activities.

Although Vermilion believes that the expectations reflected in such forward looking statements or information are reasonable, undue reliance should not be placed on forward looking statements because Vermilion can give no assurance that such expectations will prove to be correct. Financial outlooks are provided for the purpose of understanding Vermilion's financial position and business objectives, and the information may not be appropriate for other purposes. Forward looking statements or information are based on current expectations, estimates, and projections that involve a number of risks and uncertainties which could cause actual results to differ materially from those anticipated by Vermilion and described in the forward looking statements or information. These risks and uncertainties include, but are not limited to: the ability of management to execute its business plan; the risks of the oil and gas industry, both domestically and internationally, such as operational risks in exploring for, developing and producing crude oil, natural gas liquids, and natural gas; risks and uncertainties involving geology of crude oil, natural gas liquids, and natural gas deposits; risks inherent in Vermilion's marketing operations, including credit risk; the uncertainty of reserves estimates and reserves life and estimates of resources and associated expenditures; the uncertainty of estimates and projections relating to production and associated expenditures; potential delays or changes in plans with respect to exploration or development projects; Vermilion's ability to enter into or renew leases on acceptable terms; fluctuations in crude oil, natural gas liquids, and natural gas prices, foreign currency exchange rates and interest rates; health, safety, and environmental risks; uncertainties as to the availability and cost of financing; the ability of Vermilion to add production and reserves through exploration and development activities; the possibility that government policies or laws may change or governmental approvals may be delayed or withheld; uncertainty in amounts and timing of royalty payments; risks associated with existing and potential future law suits and regulatory actions against Vermilion; and other risks and uncertainties described elsewhere in this document or in Vermilion's other filings with Canadian securities regulatory authorities.

The forward looking statements or information contained in this document are made as of the date hereof and Vermilion undertakes no obligation to update publicly or revise any forward looking statements or information, whether as a result of new information, future events, or otherwise, unless required by applicable securities laws.

All oil and natural gas reserve information contained in this document has been prepared and presented in accordance with National Instrument 51-101 *Standards of Disclosure for Oil and Gas Activities* and the *Canadian Oil and Gas Evaluation Handbook*. The actual crude oil and natural gas reserves and future production will be greater than or less than the estimates provided in this document. The estimated future net revenue from the production of crude oil and natural gas reserves does not represent the fair market value of these reserves.

Natural gas volumes have been converted on the basis of six thousand cubic feet of natural gas to one barrel of oil equivalent. Barrels of oil equivalent (boe) may be misleading, particularly if used in isolation. A boe conversion ratio of six thousand cubic feet to one barrel of oil is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

Financial data contained within this document are reported in Canadian dollars, unless otherwise stated.

HIGHLIGHTS

- Vermilion's 2016 annual production volumes increased by 16%, or 10% on a per-share-basis, to 63,526 boe/d, above the upper-end of our guidance range of 62,500-63,500 boe/d. This annual production performance was achieved while reducing exploration and development ("E&D") capital spending by 50% as compared to 2015. Production volumes for Q4 2016 decreased by 4% as compared to the prior quarter, due to natural declines, timing of capital projects and actively managed production in Canada, Netherlands and Australia.

- Fund flows from operations in 2016 were $510.8 million ($4.41/basic share[1]) as compared to $516.2 million ($4.71/basic share) in 2015. Fund flows were negatively impacted by weaker commodity prices in 2016 but were largely offset by higher production. Q4 2016 fund flows from operations of $149.6 million ($1.27/basic share) increased 6% from $141.0 million ($1.21/basic share) in Q3 2016 as a result of higher commodity prices, partially offset by lower sales volumes.

- E&D capital expenditures totaled $242.4 million in 2016, slightly above our guidance of $240 million.

- On a per-unit basis, annual operating and administrative ("G&A") expenses decreased by 16% and 15% respectively, year-over-year. Profitability Enhancement Plan ("PEP") initiatives continue to deliver cost savings across our business units. Full-year PEP savings related to capital, operating and G&A expenditures exceeded $70 million in 2016.

- Total proved ("1P") reserves increased 9% to 175.8[2] mmboe in 2016, while total proved plus probable ("2P") reserves increased 11% to 290.1[2] mmboe. This represents year-over-year 1P and 2P per share reserves growth of 4% and 5%, respectively.

- Finding and Development ("F&D")[3] and Finding, Development and Acquisition ("FD&A")[3] costs, including Future Development Capital ("FDC")[3] for 2016 on a 2P basis decreased 38% to $5.57/boe and 34% to $6.62/boe, respectively. Our three-year F&D and FD&A costs, including FDC, on a 2P basis were $10.76/boe and $14.22/boe, respectively.

- Operating recycle ratio[4] (including FDC) increased to 4.9x in 2016, compared to 3.6x in 2015, as lower F&D costs more than offset the effect of lower commodity prices on netbacks.

- Our independent GLJ 2016 Resource Assessment[5] indicates risked low, best, and high estimates for contingent resources in the Development Pending category of 120.4[5] mmboe, 198.5[5] mmboe, and 309.4[5] mmboe, representing increases of 27%, 24% and 21%, respectively, compared to our GLJ 2015 Resource Assessment[6]. The GLJ 2016 Resource Assessment also indicates risked low, best, and high estimates for contingent resources in the Development Unclarified category of 9.9[5] mmboe, 19.5[5] mmboe, and 28.7[5] mmboe. Over 90% of our risked contingent resources reside in the Development Pending category, reflecting the high quality nature of our contingent resource base. Prospective resources were assessed at risked low, best and high estimates of 45.2[5] mmboe, 89.5[5] mmboe, and 147.9[5] mmboe.

- In France, we successfully executed our four-well Champotran drilling program and commenced drilling of a horizontal sidetrack well in the Vulaines field during Q4 2016, with completion and tie-in activities planned for Q1 2017. This is our fourth successive drilling campaign at Champotran since 2013.

- On December 19, 2016, Vermilion closed the acquisition of operated and non-operated interests in five oil and three gas producing fields from Engie E&P Deutschland GmbH, for total consideration of €32.5 million ($45.6 million), net of acquired product inventory and after closing adjustments. Vermilion has assumed operatorship of six of the eight producing fields, representing our first operated producing properties in Germany. The acquisition advances our objective of developing a material business unit in the country, and is complementary to the assets in our existing European portfolio.

- In the Netherlands, we completed the Langezwaag-3 well (42% working interest) in Q4 2016 and brought it on production at a restricted rate of 7.5 mmcf/d. During Q4 2016, we also acquired an incremental 30% working interest in the Drenthe VI production license for $28.3 million. This acquisition adds 30,000 net acres of land, including 26,000 net acres of undeveloped land and a 30% after payout interest in one well.

- Production from Corrib averaged 62.9 mmcf/d (10,486 boe/d), net to Vermilion, in Q4 2016, representing 97% of rated plant capacity. All six wells are available for production with lower downtime and better-than-expected well deliverability.

- Vermilion entered into a farm-in agreement in Slovakia with NAFTA, Slovakia's dominant exploration and production company. The farm-in agreement grants Vermilion a 50% working interest to jointly explore 183,000 acres on an existing license. The Slovakia farm-in offers access to a promising land position through modest seismic and well commitments over a five-year primary agreement term.

- During Q4 2016, we began prorating the Premium Dividend™ Component of our Premium Dividend™ and Dividend Reinvestment Plan by 25%, and announced a further 25% proration starting with the January 2017 dividend payment. We plan to increase the proration factor by a further 25% beginning with the April 2017 dividend payment, so that eligible shareholders who have elected to participate in the Premium Dividend™ Component will receive a 1.5% premium on 25% of their participating shares, and the regular cash dividend on the remaining 75% of their shares. Subject to unexpected changes in the commodity price outlook, we plan to discontinue the Premium Dividend™ Component of our Premium Dividend™ and Dividend Reinvestment Plan beginning with the July 2017 dividend payment, such that there would be no further equity issuance under this program. We also reduced the discount associated with the traditional component of our Premium Dividend™ and Dividend Reinvestment Plan from 3% to 2% beginning with the January 2017 dividend.

- Vermilion continued to be recognized for its environmental, social and governance ("ESG") initiatives in 2016. Vermilion was one of only five oil and gas companies in the world, and the only energy company in North America, to be awarded a position on CDP's Climate "A" List. We were also ranked 9th by Corporate Knights on the Future 40 Responsible Leaders in Canada list, the highest rated oil and gas company on the list of sustainable performers. For more information on our ESG initiatives and performance, please see our Sustainability Report at: http://sustainability.vermilionenergy.com

(1) Non-GAAP Financial Measure. Please see the "Non-GAAP Financial Measures" section of Management's Discussion and Analysis.

(2) Estimated proved and proved plus probable reserves attributable to the assets as evaluated by GLJ Petroleum Consultants Ltd. ("GLJ") in a report dated February 1, 2017 with an effective date of December 31, 2016 (the "2016 GLJ Reserves Evaluation")

(3) F&D (finding and development) and FD&A (finding, development and acquisition) costs are used as a measure of capital efficiency and are calculated by dividing the applicable capital expenditures for the period, including the change in undiscounted future development capital ("FDC"), by the change in the reserves, incorporating revisions and production, for the same period.

(4) Operating Recycle Ratio is a measure of capital efficiency calculated by dividing the Operating Netback by the cost of adding reserves (F&D cost). Operating Netback is calculated as sales less royalties, operating expense, transportation costs, PRRT and realized hedging gains and losses presented on a per unit basis.

(5) Vermilion retained GLJ to conduct an independent resource evaluation dated February 1, 2017 to assess contingent and prospective resources across all of the Company's key operating regions with an effective date of December 31, 2016 (the "GLJ 2016 Resource Assessment"). The aggregate associated chance of development for each of the low, best and high estimate for contingent resources in the Development Pending category are 84%, 83% and 82%, respectively. The aggregate associated chance of commerciality for each of the low, best and high estimate for prospective resources in the Prospect category are 25%, 26% and 26%, respectively. There is uncertainty that it will be commercially viable to produce any portion of the resources.

(6) Vermilion retained GLJ to conduct an independent resource evaluation dated February 8, 2016 to assess contingent resources across all of the Company's key operating regions with an effective date of December 31, 2015 (the "GLJ 2015 Resource Assessment"). The aggregate associated chance of development for each of the low, best and high estimate for contingent resources in the Development Pending category are 83%, 82% and 81%, respectively. There is uncertainty that it will be commercially viable to produce any portion of the resources.

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HIGHLIGHTS

	Three Months Ended			Year Ended	
($M except as indicated) Financial	Dec 31, 2016	Sep 30, 2016	Dec 31, 2015	Dec 31, 2016	Dec 31, 2015
Petroleum and natural gas sales	**259,891**	232,660	234,319	**882,791**	939,586
Fund flows from operations	**149,582**	140,974	136,441	**510,791**	516,167
Fund flows from operations ($/basic share) (1)	**1.27**	1.21	1.22	**4.41**	4.71
Fund flows from operations ($/diluted share) (1)	**1.25**	1.19	1.21	**4.36**	4.65
Net loss	**(4,032)**	(14,475)	(142,080)	**(160,051)**	(217,302)
Net loss ($/basic share)	**(0.03)**	(0.12)	(1.28)	**(1.38)**	(1.98)
Capital expenditures	**66,882**	41,039	128,996	**242,408**	486,861
Acquisitions	**78,713**	10,391	6,227	**98,524**	28,897
Asset retirement obligations settled	**3,327**	2,066	4,921	**9,617**	11,369
Cash dividends ($/share)	**0.645**	0.645	0.645	**2.580**	2.580
Dividends declared	**76,096**	75,465	71,965	**299,070**	283,575
% of fund flows from operations	**51%**	54%	53%	**59%**	55%
Net dividends (1)	**32,516**	24,553	25,201	**106,072**	128,542
% of fund flows from operations	**22%**	17%	18%	**21%**	25%
Payout (1)	**102,725**	67,658	159,118	**358,097**	626,772
% of fund flows from operations	**69%**	48%	117%	**70%**	121%
Net debt	**1,427,148**	1,343,923	1,381,951	**1,427,148**	1,381,951
Ratio of net debt to annualized fund flows from operations	**2.4**	2.4	2.5	**2.8**	2.7
Operational					
Production					
Crude oil and condensate (bbls/d)	**25,972**	27,842	31,304	**27,852**	30,408
NGLs (bbls/d)	**2,467**	2,478	2,739	**2,582**	2,308
Natural gas (mmcf/d)	**194.54**	199.66	162.09	**198.55**	133.24
Total (boe/d)	**60,863**	63,596	61,058	**63,526**	54,922
Average realized prices					
Crude oil, condensate and NGLs ($/bbl)	**60.58**	53.24	51.64	**51.73**	58.80
Natural gas ($/mcf)	**5.47**	3.98	4.55	**4.18**	4.98
Production mix (% of production)					
% priced with reference to WTI	**18%**	19%	22%	**19%**	25%
% priced with reference to AECO	**20%**	20%	24%	**22%**	22%
% priced with reference to TTF and NBP	**33%**	32%	20%	**30%**	19%
% priced with reference to Dated Brent	**29%**	29%	34%	**29%**	34%
Netbacks ($/boe)					
Operating netback(1)	**31.11**	27.88	28.44	**27.06**	32.09
Fund flows from operations netback	**26.43**	23.25	23.91	**21.91**	25.86
Operating expenses	**10.54**	9.05	11.50	**9.53**	11.32
Average reference prices					
WTI (US $/bbl)	**49.29**	44.94	42.18	**43.32**	48.80
Edmonton Sweet index (US $/bbl)	**46.18**	42.06	39.72	**40.11**	44.91
Dated Brent (US $/bbl)	**49.46**	45.85	43.69	**43.69**	52.46
AECO ($/mmbtu)	**3.09**	2.32	2.46	**2.16**	2.69
NBP ($/mmbtu)	**7.51**	5.29	7.41	**6.15**	8.33
TTF ($/mmbtu)	**7.21**	5.43	7.28	**6.00**	8.23
Average foreign currency exchange rates					
CDN $/US $	**1.33**	1.31	1.34	**1.33**	1.28
CDN $/Euro	**1.44**	1.46	1.46	**1.47**	1.42
Share information ('000s)					
Shares outstanding - basic	**118,263**	117,386	111,991	**118,263**	111,991
Shares outstanding - diluted (1)	**121,353**	120,183	115,025	**121,353**	115,025
Weighted average shares outstanding - basic	**117,840**	116,814	111,393	**115,695**	109,642
Weighted average shares outstanding - diluted (1)	**119,677**	118,177	112,543	**117,152**	111,051

(1) The above table includes non-GAAP financial measures which may not be comparable to other companies. Please see the "NON-GAAP FINANCIAL MEASURES" section of Management's Discussion and Analysis.

MESSAGE TO SHAREHOLDERS

The past three years have been a challenging time for the oil and gas industry, with oil and gas prices both hitting multi-year lows in 2016. As a result, we took a very cautious approach last year, adjusting our capital program on several occasions to ensure that capital expenditures and cash dividends were fully funded by fund flows from operations. We achieved this while maintaining our dividend, and also delivered strong production and 2P reserves[1] growth of 16% (10% on a per share basis) and 11% (5% on a per share basis), respectively. We delivered these results while investing half the amount of capital compared to the prior year, and approximately one-third of the amount from two years ago. We believe that this successful adaptation to a "lower-for-longer" world illustrates both the quality of our asset base and the competence of our personnel. Our diversified asset base and global commodity exposure are two risk-reducing qualities that set Vermilion apart from many of our peers during the downturn.

Vermilion has always been disciplined in the management of its balance sheet, typically operating with leverage ratios below the industry average. We entered the commodity price downturn in a position of relative financial strength, and proactively took a number of actions in 2015 and 2016 to preserve our balance sheet. In 2016, our payout ratio for E&D capital and cash dividends was 70% of fund flows from operations. We have designed our 2017 and 2018 capital programs to provide for continued self-funded growth. At the current commodity strip price, we expect fund flows from operations to exceed the combined cost of E&D expenditures and cash dividends. In line with our conservative approach to managing our balance sheet, we have the flexibility to direct the resulting surplus cash to further debt reduction.

In early 2015 we amended our existing Dividend Reinvestment Plan ("DRIP") to include a Premium Dividend™ Component. The Premium Dividend™ Component expanded our access to the lowest cost source of equity capital available during a period of commodity price weakness and uncertainty. During Q4 2016, we began prorating the Premium Dividend™ Component of our Premium Dividend™ and Dividend Reinvestment Plan by 25%, and announced a further 25% proration starting with the January 2017 dividend payment. We plan to increase the proration factor by a further 25% beginning with the April 2017 dividend payment, so that eligible shareholders who have elected to participate in the Premium Dividend™ Component will receive the 1.5% premium on 25% of their participating shares and the regular cash dividend on the remaining 75% of their shares. Subject to unexpected changes in the commodity price outlook, we plan to discontinue the Premium Dividend™ Component beginning with the July 2017 dividend payment, such that there would be no further equity issuance under this program. We also reduced the discount associated with the traditional component of our Premium Dividend™ and Dividend Reinvestment Plan from 3% to 2% beginning with the January 2017 payment. Our strategy aims to deliver consistent growth-and-income to our shareholders. These measures will reduce dilution, ensuring that value from future growth in production and cash flow more efficiently flows to our owners on a per-share-basis.

On a per unit basis, annual operating and G&A expenses decreased by 16% and 15% respectively, year-over-year, and are down 27% and 29% respectively over the past five years. Since implementing our Profitability Enhancement Plan ("PEP") in November 2014, we have realized over $160 million in cost savings across our business, including over $70 million achieved in 2016. It is our intent to embed these PEP cost reductions in our ongoing operations. As a result, we are discontinuing our formal PEP tracking, but will continue to identify new cost saving initiatives as part of our everyday business.

As a result of these ongoing cost reductions and capital efficiency improvements, we have been able to significantly reduce our planned capital investment program over the past several years while still growing production. The diversity of our asset base and commodity price exposures allows us to select and fund projects that will generate the highest return in a given commodity environment. These cost and capital efficiency improvements, combined with our expanding drilling inventory, provides greater visibility to growing our free cash flow[2] (FFO less E&D Capital). Based on current commodity strip prices, we project our 2017 and 2018 free cash flow[2] levels to be nearly three-to-four-times what they were during the 2012-to-2014 timeframe, when commodity prices were much higher. We are now in a stronger position than we have ever been before, with a deep inventory of high return projects to underpin our self-funded growth-and-income model over the long-term.

2016 Review

We delivered 16% year-over-year production growth in 2016, above the upper-end of our guidance range of 62,500-63,500 boe/d. This production performance was achieved while reducing our E&D capital program by 50% as compared to 2015. In addition, despite the commodity price weakness seen in 2016, we continued to deliver strong performance across all segments of our business.

Our latest independent reserve and resource evaluations illustrate the strong organic inventory in each of our business units. Total 1P reserves increased 9% to 175.8[1] mmboe in 2016, while total 2P reserves increased 11% to 290.1[1] mmboe. This represents year-over-year 1P and 2P per share reserves growth of 4% and 5%, respectively. Operating recycle ratio[3] (including FDC) increased to 4.9x in 2016, compared to 3.6x in 2015 and 3.2x in 2014. Despite a further deterioration in commodity prices, these increases in reserves and recycle ratio further demonstrate the improvement of our project inventory and execution over the past few years.

In addition to growing our reserve base, we also focus on activities that will expand our resource base to support our longer-term growth profile in production and reserves. Our independent GLJ 2016 Resource Assessment[4] indicates risked low, best, and high estimates for contingent resources in the Development Pending category of 120.4[4] mmboe, 198.5[4] mmboe, and 309.4[4] mmboe, representing increases of 27%, 24% and 21%, respectively, compared to our GLJ 2015 Resource Assessment[5]. The GLJ 2016 Resource Assessment also indicates risked low, best, and high estimates for contingent resources in the Development Unclarified category of 9.9[4] mmboe, 19.5[4] mmboe, and 28.7[4] mmboe. Over 90% of our risked contingent resources reside in the Development Pending category, reflecting the high quality nature of our contingent resource base. Prospective resources were assessed at risked low, best and high estimates of 45.2[4] mmboe, 89.5[4] mmboe, and 147.9[4] mmboe.

Europe

Production from Corrib averaged 62.9 mmcf/d (10,486 boe/d), net to Vermilion, in Q4 2016, representing 97% of rated plant capacity. All six wells are now available for production. The Corrib project has demonstrated lower-than-expected downtime and better-than-expected well deliverability thus far. Going forward, we expect Corrib to be a significant source of fund flows for Vermilion, stemming from its relatively high-priced gas product, absence of royalties, low operating expense, low maintenance capital requirements, and lack of cash income tax for the foreseeable future.

In France, we completed a four (4.0 net) well drilling program at Champotran and commenced drilling of a horizontal sidetrack well in the Vulaines field during Q4 2016, with completion and tie-in activities planned for the latter part of Q1 2017. This was our fourth successive drilling campaign at Champotran since 2013. In 2017, in addition to continuing our workover and optimization activities in France, we plan to drill our first four (4.0 net) wells in the Neocomian fields in the Paris Basin. After acquiring the Neocomian fields in 2012, we have increased production by approximately 50% through workovers and artificial lift optimizations.

In the Netherlands, we drilled two (0.9 net) wells in 2016. The Langezwaag-3 well (42% working interest) was completed and brought on production during Q4 2016 at a restricted rate of 7.5 mmcf/d. The Andel-6ST well (45% working interest) encountered a gas column of inadequate reservoir quality to justify completion. The Andel-6ST well is suspended while we evaluate the potential for another sidetrack to a location where higher quality gas zones may be encountered. During Q4 2016, we also acquired an incremental 30% working interest in the Drenthe VI production license for $28.3 million. This acquisition further consolidates our interest in the Drenthe VI production license, adding 30,000 net acres of land, including 26,000 net acres of undeveloped land and a 30% after payout interest in one well. In 2017, we plan to drill two (1.0 net) exploration wells and acquire 230 square kilometres of 3D seismic, representing a 50% increase in E&D capital investment compared to 2016.

On December 19, 2016, Vermilion closed the acquisition of operated and non-operated interests in five crude oil and three natural gas producing fields from Engie E&P Deutschland GmbH, for total consideration of €32.5 million ($45.6 million), net of acquired product inventory and after closing adjustments. The closing price was higher than the €28.3 million ($39.6 million) we estimated on December 19, 2016, primarily due to capital costs for a compression project that was installed before closing. Vermilion has assumed operatorship of six of the eight producing fields, representing our first operated producing properties in Germany. The acquisition advances our objective of developing a material business unit in the country, and is complementary to the assets in our existing European portfolio.

A portion of our 2017 capital program in Germany will be directed to investment in optimizations and other well work on the acquired Engie assets. In addition, further bolstering our operating presence in Germany, we have assumed the drilling operatorship for the Burgmoor Z5 well (25% working interest) in our Dümmersee-Uchte producing concession, which is expected to be drilled in 2018. Lastly, we will continue to advance our permitting, studies and other activities associated with the farm-in agreement we signed in mid-2015.

Vermilion added to its position in central and eastern Europe during Q4 2016 through a farm-in agreement in Slovakia with NAFTA, Slovakia's dominant exploration and production company. The farm-in agreement grants Vermilion a 50% working interest to jointly explore 183,000 acres on an existing license. The Slovakia farm-in offers access to a promising land position through modest seismic and well commitments over a five-year primary agreement term.

North America

During 2016, we drilled or participated in two (0.2 net) Cardium wells, 20 (12.0 net) Mannville wells, and seven (5.5 net) Midale wells. Our 2016 capital activities in Canada were focused on operated expiry wells and capital commitments on non-operated wells. Our Canadian assets provide significant flexibility to ramp activity levels up or down, with a diversified project inventory that provides exposure to oil, condensate and natural gas opportunities. Reflecting high project rates-of-return at current commodity prices, we are increasing our planned capital activity in Canada in 2017, targeting oil- and liquids-weighted projects. We plan to drill or participate in nine (6.0 net) Cardium wells, drill 23 (15.0 net) Mannville new wells and tie-in six (5.0 net) wells drilled in 2016, and drill 13 (11.3 net) new Midale wells and tie-in the four operated Midale wells we drilled in 2016.

In the United States, we continued development of the light oil Turner Sand in the Powder River Basin of Wyoming. In 2016, we completed two (2.0 net) wells drilled in 2015, and completed the Seedy Draw East Federal well drilled late in the year. In the Seedy Draw East Federal well, we drilled an approximately 1,400 metre horizontal lateral, and fracture stimulated 23 out of 32 planned frac stages before screening out. We plan to clean sand out of this well and put it on production during Q1 2017, leaving the remaining nine stages for potential stimulation at a later date. During 2017, we plan to drill and complete three (3.0 net) additional Turner Sand wells. Subsequent to year-end 2016, we purchased overriding royalty interests on our lands (ranging from 0.83% to 5%) for US$1.5 million, further consolidating our position in this play.

Australia

In Q2 2016, we drilled two horizontal sidetrack wells from our Wandoo B platform. Under restricted drawdown, these wells exhibit continued strong productive capability of a combined rate of approximately 4,300 bbls/d. The new sidetrack wells are produced intermittently to manage production levels and meet oil sales contract commitments. Given the strong results from our 2015 and 2016 drilling programs, we do not expect to drill additional wells in Australia until 2019.

Environmental, Social & Governance

During 2016, we were named to the CDP Climate "A" List, which recognizes companies for their actions in mitigating climate change. We were one of only five oil and gas companies in the world, and the only energy company in North America, to be awarded this distinction. CDP (formerly Carbon Disclosure Project), is a global, not-for-profit organization that manages the world's only global environmental disclosure system. Vermilion was the leading energy company on the Canadian Climate Disclosure Leadership Index (CLDI) for 2015, and the first Canadian energy company to achieve the top score of 100. To be named to the CDLI, a company must have a disclosure score within the top 10% of surveyed companies. We have voluntarily reported to CDP since 2012. We believe that by measuring and understanding our current environmental profile, we can direct our business strategy to operate in an even more environmentally and socially sustainable manner in the future.

During 2016, we were ranked 9th by Corporate Knights on the Future 40 Responsible Corporate Leaders in Canada list (the highest ranking for an oil and gas company, and our second consecutive year of improved rankings). Between 2013 and 2016, Vermilion's MSCI ESG (environment, social and governance) rating increased from BB to BBB, and our score on MSCI's Governance Metrics Report ranks Vermilion in the 90th percentile globally. These recognitions reflect our continued focus on achieving robust shareholder returns combined with environmental, social and governance performance.

We released our third annual Sustainability Report in 2016 which details our efforts to generate environmental, social, and economic benefits for all stakeholders. The report describes our approach to sustainability in our operations, and details our progress and challenges in this regard. We are committed to providing increasingly complete information and objective assessment of our performance in this area on an annual basis. We firmly believe in the importance of measuring and understanding our current environmental impact. Furthermore, we believe the integration of sustainability principles into our business strategy increases shareholder returns and reduces long-term risks to our business model. Our 2016 Sustainability Report is available on our corporate website at www.vermilionenergy.com/sustainability.

Vermilion ranked third within the oil and gas sector, and among the top quartile of companies in the S&P/TSX Composite Index in the Globe and Mail Board Games. Additionally, Vermilion was listed in the 2016 Best Practices report by the Canadian Coalition for Good Governance for our Proxy Circular disclosure on director and board independence, and benefits and perquisites, demonstrating our best-in-class governance disclosure.

Since 2010, we have been recognized by the Great Place to Work® Institute as one of the Top 30 Best Workplaces in Canada and France. We were also recognized in 2016 as a Top 20 Best Workplace in the Netherlands, and a Top 5 Best Workplace in the Berlin-Brandenburg region of Germany. These rankings demonstrate our strong corporate culture and highly engaged staff.

Outlook

Prior to the end of 2016, we announced a $295 million E&D capital budget for 2017 with associated production guidance of 69,000 to 70,000 boe/d. Our budget funds development of high-return projects including our condensate-rich Mannville play in Canada, continued drilling in France, favorably-priced European natural gas projects in the Netherlands, and our emerging Turner Sands play in the United States. Due to permitting delays on certain projects in the Netherlands, we have reallocated modest amounts of capital from the Netherlands to Canada, with no impact on our 2017 corporate capital or production guidance. Please refer to our March 2017 corporate presentation for the new capital levels by business unit.

We also previously announced preliminary 2018 targets, with anticipated E&D capital of $335 million and production of 75,000 to 76,000 boe/d. Production at the top end of these ranges for 2017 and 2018 would deliver per share growth of approximately 6% for each year. In recognition of the addition of our new Slovakian project to our capital project portfolio, we are increasing our 2018 capital investment target by $5 million to $340 million.

("Anthony Marino")

Anthony Marino
Chief Executive Officer
February 24, 2017

(1) Estimated proved and proved plus probable reserves attributable to the assets as evaluated by GLJ Petroleum Consultants Ltd. ("GLJ") in a report dated February 1, 2017 with an effective date of December 31, 2016 (the "2016 GLJ Reserves Evaluation")

(2) The above discussion includes non-GAAP measures which may not be comparable to other companies. Please see the "NON-GAAP FINANCIAL MEASURES" section of Management's Discussion and Analysis.

(3) Operating Recycle Ratio is a measure of capital efficiency calculated by dividing the Operating Netback by the cost of adding reserves (F&D cost). Operating Netback is calculated as sales less royalties, operating expense, transportation costs, PRRT and realized hedging gains and losses presented on a per unit basis.

(4) Vermilion retained GLJ to conduct an independent resource evaluation dated February 1, 2017 to assess contingent and prospective resources across all of the Company's key operating regions with an effective date of December 31, 2016 (the "GLJ 2016 Resource Assessment"). The aggregate associated chance of development for each of the low, best and high estimate for contingent resources in the Development Pending category are 84%, 83% and 82%, respectively. The aggregate associated chance of commerciality for each of the low, best and high estimate for prospective resources in the Prospect category are 25%, 26% and 26%, respectively. There is uncertainty that it will be commercially viable to produce any portion of the resources.

(5) Vermilion retained GLJ to conduct an independent resource evaluation dated February 8, 2016 to assess contingent resources across all of the Company's key operating regions with an effective date of December 31, 2015 (the "GLJ 2015 Resource Assessment"). The aggregate associated chance of development for each of the low, best and high estimate for contingent resources in the Development Pending category are 83%, 82% and 81%, respectively. There is uncertainty that it will be commercially viable to produce any portion of the resources.

TM Denotes trademark of Canaccord Genuity Capital Corporation

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following is Management's Discussion and Analysis ("MD&A"), dated February 24, 2017, of Vermilion Energy Inc.'s ("Vermilion", "we", "our", "us" or the "Company") operating and financial results as at and for the three months and year ended December 31, 2016 compared with the corresponding periods in the prior year.

This discussion should be read in conjunction with the audited consolidated financial statements for the year ended December 31, 2016 and 2015, together with the accompanying notes. Additional information relating to Vermilion, including its Annual Information Form, is available on SEDAR at www.sedar.com or on Vermilion's website at www.vermilionenergy.com.

The audited consolidated financial statements for the year ended December 31, 2016 and comparative information have been prepared in Canadian dollars, except where another currency has been indicated, and in accordance with International Financial Reporting Standards ("IFRS" or, alternatively, "GAAP") as issued by the International Accounting Standards Board.

This MD&A includes references to certain financial and performance measures which do not have standardized meanings prescribed by IFRS. These measures include:

- Fund flows from operations: Fund flows from operations is a measure of profit or loss in accordance with IFRS 8 "Operating Segments". Please see SEGMENTED INFORMATION in the NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS for a reconciliation of fund flows from operations to net earnings. We analyze fund flows from operations both on a consolidated basis and on a business unit basis in order to assess the contribution of each business unit to our ability to generate income necessary to pay dividends, repay debt, fund asset retirement obligations and make capital investments.
- Netbacks: Netbacks are per boe and per mcf performance measures used in the analysis of operational activities. We assess netbacks both on a consolidated basis and on a business unit basis in order to compare and assess the operational and financial performance of each business unit versus other business units and also versus third party crude oil and natural gas producers.

In addition, this MD&A includes references to certain financial measures which are not specified, defined, or determined under IFRS and are therefore considered non-GAAP financial measures. These non-GAAP financial measures are unlikely to be comparable to similar financial measures presented by other issuers. For a full description of these non-GAAP financial measures and a reconciliation of these measures to their most directly comparable GAAP measures, please refer to "NON-GAAP FINANCIAL MEASURES".

VERMILION'S BUSINESS

Vermilion is a Calgary, Alberta based international oil and gas producer focused on the acquisition, exploration, development and optimization of producing properties in North America, Europe, and Australia. We manage our business through our Calgary head office and our international business unit offices.

This MD&A separately discusses each of our business units in addition to our corporate segment.

CHANGE IN PRESENTATION

Prior to 2016, we reported our condensate production in Canada and the Netherlands business units within the NGLs production line. Beginning in Q1 2016, we reported condensate production within the crude oil and condensate production line. We believe that this presentation better reflects the historical and forecasted pricing for condensate, which is more closely correlated with crude oil pricing than with pricing for propane, butane and ethane (collectively "NGLs" for the purposes of this report). Comparative periods have been adjusted to reflect this change.

2016 REVIEW AND 2017 GUIDANCE

On November 9, 2015, we announced preliminary 2016 capital expenditure guidance of $350 million and production guidance of between 63,000-65,000 boe/d. On January 5, 2016, in response to the continued weakness in commodity prices we reduced our 2016 capital expenditure guidance to $285 million with corresponding production guidance of 62,500-63,500 boe/d. On February 29, 2016, we further revised our 2016 capital expenditure guidance to $235 million as a result of continued commodity price deterioration. We maintained our production guidance of 62,500-63,500 boe/d. The February 29, 2016 reduction primarily reflected lower expected non-operated drilling activity in Canada, fewer workovers in France, and a deferral of our Netherlands pipeline twinning program. On August 8, 2016, we modestly increased our 2016 capital expenditure guidance to $240 million with the reinstatement of a four-well drilling program in the Champotran field in France and added drilling activity in Canada, partially offset by capital cost savings achieved to date. Actual 2016 capital spending of $242.4 million was within 1% of our guidance and 2016 production of 63,526 boe/d modestly exceeded the top end of our guidance range.

On October 31, 2016, we released our 2017 capital expenditure guidance of $295 million and associated production guidance of between 69,000-70,000 boe/d.

The following table summarizes our guidance:

	Date	Capital Expenditures ($MM)	Production (boe/d)
2016 Guidance			
2016 Guidance	November 9, 2015	350	63,000 to 65,000
2016 Guidance	January 5, 2016	285	62,500 to 63,500
2016 Guidance	February 29, 2016	235	62,500 to 63,500
2016 Guidance	August 8, 2016	240	62,500 to 63,500
2017 Guidance			
2017 Guidance	October 31, 2016	295	69,000 to 70,000

CONSOLIDATED RESULTS OVERVIEW

	Three Months Ended			% change		Year Ended		% change
	Dec 31, 2016	Sep 30, 2016	Dec 31, 2015	Q4/16 vs. Q3/16	Q4/16 vs. Q4/15	Dec 31, 2016	Dec 31, 2015	2016 vs. 2015
Production								
Crude oil and condensate (bbls/d)	**25,972**	27,842	31,304	(7%)	(17%)	**27,852**	30,408	(8%)
NGLs (bbls/d)	**2,467**	2,478	2,739	-	(10%)	**2,582**	2,308	12%
Natural gas (mmcf/d)	**194.54**	199.66	162.09	(3%)	20%	**198.55**	133.24	49%
Total (boe/d)	**60,863**	63,596	61,058	(4%)	-	**63,526**	54,922	16%
Sales								
Crude oil and condensate (bbls/d)	**26,610**	30,111	32,306	(12%)	(18%)	**28,005**	30,178	(7%)
NGLs (bbls/d)	**2,467**	2,478	2,739	-	(10%)	**2,582**	2,308	12%
Natural gas (mmcf/d)	**194.54**	199.66	162.09	(3%)	20%	**198.55**	133.24	49%
Total (boe/d)	**61,501**	65,865	62,061	(7%)	(1%)	**63,679**	54,692	16%
Build (draw) in inventory (mbbls)	**(58)**	(209)	(93)			**(55)**	84	
Financial metrics								
Fund flows from operations ($M)	**149,582**	140,974	136,441	6%	10%	**510,791**	516,167	(1%)
Per share ($/basic share)	**1.27**	1.21	1.22	5%	4%	**4.41**	4.71	(6%)
Net loss	**(4,032)**	(14,475)	(142,080)	(72%)	(97%)	**(160,051)**	(217,302)	(26%)
Per share ($/basic share)	**(0.03)**	(0.12)	(1.28)	(75%)	(98%)	**(1.38)**	(1.98)	(30%)
Net debt ($M)	**1,427,148**	1,343,923	1,381,951	6%	3%	**1,427,148**	1,381,951	3%
Cash dividends ($/share)	**0.645**	0.645	0.645	-	-	**2.580**	2.580	-
Activity								
Capital expenditures ($M)	**66,882**	41,039	128,996	63%	(48%)	**242,408**	486,861	(50%)
Acquisitions ($M)	**78,713**	10,391	6,227	658%	1,164%	**98,524**	28,897	241%
Gross wells drilled	**16.00**	6.00	8.00			**38.00**	53.00	
Net wells drilled	**12.02**	2.08	5.56			**25.50**	36.12	

Operational review

- Increased consolidated average production for the year ended December 31, 2016 by 16% versus 2015. This increase was primarily due to the addition of Corrib production in Ireland. For the three months ended December 31, 2016, production was relatively consistent with the comparable period in 2015 as the addition of Corrib production in Ireland was offset by natural declines and actively managed production in Canada, the Netherlands, and Australia.
- Achieved consolidated average production of 60,863 boe/d in Q4 2016, a 4% decrease from Q3 2016 due to natural declines, the timing of capital projects, and actively managed production in Canada, the Netherlands, and Australia.
- Incurred capital expenditures in Q4 2016 of $66.9 million primarily related to France and Canada. In France, capital expenditures of $31.1 million were incurred related to the drilling of four wells in Champotran and other development activities in the quarter. In Canada, capital expenditures of $16.9 million related primarily to drilling activity.
- For the year ended December 31, 2016, capital expenditures of $242.4 million primarily related to France, Canada, Australia, and the Netherlands. In France, capital expenditures of $68.5 million related to drilling activity and other development activities, including workover and optimization programs in the Aquitaine and Paris basins. In Canada, capital expenditures of $62.7 million related primarily to drilling activity. In Australia, capital expenditures of $59.9 million related primarily to drilling two sidetrack wells and our Wandoo Platforms Life Extension project. In the Netherlands, capital expenditures of $23.7 million related primarily to drilling activity.
- For the year ended December 31, 2016, acquisition spending of $98.5 million related primarily to Germany and the Netherlands. In Germany, acquisition spending of $48.4 million related to the acquisition of operated and non-operated interests in five oil and three gas producing fields. In the Netherlands, acquisition spending of $28.3 million related to the acquisition of an additional 30% working interest in the Drenthe VI production license, which adds 30,000 net acres of land, including 26,000 net acres of undeveloped land and a 30% after payout interest in one well.

Financial review

Net loss

- The net loss for Q4 2016 was $4.0 million ($0.03/basic share), compared to a net loss of $14.5 million ($0.12/basic share) in Q3 2016. The change in the net loss was primarily attributable to higher revenue as a result of higher commodity prices.
- The net loss for Q4 2016 was $4.0 million ($0.03/basic share), compared to a net loss of $142.1 million ($1.28/basic share) in Q4 2015. The change was a result of a non-cash gain on business combination recognized in the current quarter and the absence of a non-cash impairment charge recognized in Q4 2015, partially offset by an unrealized loss on derivative instruments.
- The net loss for the year ended December 31, 2016 of $160.1 million compared to a net loss of $217.3 million for 2015. The change was primarily a result of a lower non-cash impairment charge in 2016, partially offset by the impact of lower commodity prices and an unrealized loss on derivative instruments.

Fund flows from operations

- Generated fund flows from operations of $149.6 million during Q4 2016, an increase of 6% from Q3 2016. This quarter-over-quarter increase was primarily attributable to higher commodity prices, partially offset by lower sales volumes.
- Fund flows from operations increased by 10% in Q4 2016 as compared to Q4 2015 due to revenue from Ireland and higher crude oil pricing. For the year ended December 31, 2016, fund flows from operations was relatively consistent with the corresponding period in 2015 despite significantly lower commodity prices due to production from Ireland and a 16% reduction in per unit operating costs.

Net debt

- Net debt increased to $1.43 billion as at December 31, 2016 from $1.38 billion at December 31, 2015 primarily due to changes in net current derivatives, partially offset by a decrease in long term debt of $25.7 million as fund flows from operations generated in excess of capital expenditures, abandonment expenditures, net dividends, and acquisitions was used to reduce debt.

Dividends

- Declared dividends of $0.215 per common share per month during the fourth quarter of 2016, totalling $2.58 per common share for the year ended December 31, 2016. This was consistent with dividends declared of $2.58 per common share for the year ended December 31, 2015.

COMMODITY PRICES

	Three Months Ended			% change		Year Ended		% change
	Dec 31, 2016	Sep 30, 2016	Dec 31, 2015	Q4/16 vs. Q3/16	Q4/16 vs. Q4/15	Dec 31, 2016	Dec 31, 2015	2016 vs. 2015
Average reference prices								
Crude oil								
WTI (US $/bbl)	**49.29**	44.94	42.18	10%	17%	**43.32**	48.80	(11%)
Edmonton Sweet index (US $/bbl)	**46.18**	42.06	39.72	10%	16%	**40.11**	44.91	(11%)
Dated Brent (US $/bbl)	**49.46**	45.85	43.69	8%	13%	**43.69**	52.46	(17%)
Natural gas								
AECO ($/mmbtu)	**3.09**	2.32	2.46	33%	26%	**2.16**	2.69	(20%)
NBP ($/mmbtu)	**7.51**	5.29	7.41	42%	1%	**6.15**	8.33	(26%)
NBP (€/mmbtu)	**5.22**	3.63	5.07	44%	3%	**4.19**	5.87	(29%)
TTF ($/mmbtu)	**7.21**	5.43	7.28	33%	(1%)	**6.00**	8.23	(27%)
TTF (€/mmbtu)	**5.01**	3.73	4.98	34%	1%	**4.09**	5.80	(29%)
Henry Hub ($/mmbtu)	**3.98**	3.67	3.03	8%	31%	**3.27**	3.41	(4%)
Henry Hub (US $/mmbtu)	**2.98**	2.81	2.27	6%	31%	**2.46**	2.66	(8%)
Average foreign currency exchange rates								
CDN $/US $	**1.33**	1.31	1.34	2%	(1%)	**1.33**	1.28	4%
CDN $/Euro	**1.44**	1.46	1.46	(1%)	(1%)	**1.47**	1.42	4%
Average realized prices ($/boe)								
Canada	**33.48**	28.75	28.94	16%	16%	**26.81**	34.32	(22%)
France	**63.71**	55.88	54.20	14%	18%	**55.15**	62.67	(12%)
Netherlands	**40.84**	31.80	42.61	28%	(4%)	**34.15**	46.77	(27%)
Germany	**36.54**	30.47	39.68	20%	(8%)	**31.97**	43.10	(26%)
Ireland	**44.29**	28.68	-	54%	100%	**35.16**	-	100%
Australia	**69.05**	60.61	58.74	14%	18%	**60.33**	70.22	(14%)
United States	**53.58**	44.53	41.94	20%	28%	**43.70**	47.53	(8%)
Consolidated	**45.93**	38.40	41.04	20%	12%	**37.88**	47.07	(20%)
Production mix (% of production)								
% priced with reference to WTI	**18%**	19%	22%			**19%**	25%	
% priced with reference to AECO	**20%**	20%	24%			**22%**	22%	
% priced with reference to TTF and NBP	**33%**	32%	20%			**30%**	19%	
% priced with reference to Dated Brent	**29%**	29%	34%			**29%**	34%	

- Crude oil prices in Q4 2016 were higher as compared to both Q3 2016 and Q4 2015 as OPEC and select non-OPEC countries reached an agreement to cut output for the first six months of 2017. This coordinated effort to curb the surplus supply of crude oil resulted in an increase in WTI of 10% as compared to Q3 2016 and 17% as compared to Q4 2015. Similarly, Dated Brent increased 8% as compared to Q3 2016 and 13% as compared to Q4 2015.
- An early start to winter increased demand for AECO natural gas both domestically and for exports to the US. For the three months ended December 31, 2016, the AECO price increased 33% and 26%, respectively, versus Q3 2016 and Q4 2015. In Q4 2016, Henry Hub prices increased by 6% and 31% versus Q3 2016 and Q4 2015, respectively, as US supply/demand fundamentals showed signs of tightening.
- European natural gas prices increased in Q4 2016 as higher power sector demand, gas-in-storage constraints and lower-than-expected LNG imports resulted in tighter balances. For the three months ended December 31, 2016, NBP and TTF increased by 42% and 33%, respectively, in Canadian dollar terms versus Q3 2016, and were effectively unchanged versus Q4 2015.
- A highly anticipated 25 basis points rate hike by the US Federal Reserve in Q4 2016 resulted in the Canadian dollar weakening against the US dollar.

FUND FLOWS FROM OPERATIONS

	Three Months Ended						Year Ended			
	Dec 31, 2016		Sep 30, 2016		Dec 31, 2015		Dec 31, 2016		Dec 31, 2015	
	$M	$/boe	$M	$/boe	$M	$/boe	$M	$/boe	$M	$/boe
Petroleum and natural gas sales	**259,891**	**45.93**	232,660	38.40	234,319	41.04	**882,791**	**37.88**	939,586	47.07
Royalties	**(14,999)**	**(2.65)**	(12,969)	(2.14)	(16,285)	(2.85)	**(54,284)**	**(2.33)**	(65,920)	(3.30)
Petroleum and natural gas revenues	**244,892**	**43.28**	219,691	36.26	218,034	38.19	**828,507**	**35.55**	873,666	43.77
Transportation	**(9,565)**	**(1.69)**	(9,696)	(1.60)	(10,147)	(1.78)	**(39,511)**	**(1.70)**	(41,660)	(2.09)
Operating	**(59,616)**	**(10.54)**	(54,825)	(9.05)	(65,645)	(11.50)	**(222,185)**	**(9.53)**	(225,938)	(11.32)
General and administration	**(11,464)**	**(2.03)**	(12,295)	(2.03)	(12,431)	(2.18)	**(52,829)**	**(2.27)**	(53,584)	(2.68)
PRRT	**(1,568)**	**(0.28)**	272	0.04	(1,054)	(0.18)	**(1,568)**	**(0.07)**	(6,878)	(0.34)
Corporate income taxes	**(5,840)**	**(1.03)**	(3,546)	(0.59)	3,113	0.55	**(18,110)**	**(0.78)**	(44,237)	(2.22)
Interest expense	**(14,410)**	**(2.55)**	(14,150)	(2.34)	(16,584)	(2.90)	**(56,957)**	**(2.44)**	(59,852)	(3.00)
Realized gain on derivative instruments	**1,920**	**0.34**	13,532	2.23	21,164	3.71	**65,376**	**2.81**	41,356	2.07
Realized foreign exchange gain (loss)	**1,291**	**0.23**	2,073	0.34	(252)	(0.04)	**4,041**	**0.17**	623	0.03
Realized other income (expense)	**3,942**	**0.70**	(82)	(0.01)	243	0.04	**4,027**	**0.17**	32,671	1.64
Fund flows from operations	**149,582**	**26.43**	140,974	23.25	136,441	23.91	**510,791**	**21.91**	516,167	25.86

The following table shows a reconciliation of the change in fund flows from operations:

($M)	Q4/16 vs. Q3/16	Q4/16 vs. Q4/15	2016 vs. 2015
Fund flows from operations – Comparative period	**140,974**	**136,441**	**516,167**
Sales volume variance:			
Canada	(4,835)	(14,094)	(21,614)
France	(2,111)	(1,673)	699
Netherlands	(3,279)	(10,168)	8,917
Germany	135	(838)	(2,249)
Ireland	1,612	42,670	109,099
Australia	(11,171)	(15,327)	(3,500)
United States	(127)	(269)	3,343
Pricing variance on sales volumes:			
WTI	6,708	7,821	(26,730)
AECO	4,582	3,340	(19,719)
Dated Brent	13,504	15,915	(57,688)
TTF and NBP	22,213	(1,805)	(47,353)
Changes in:			
Royalties	(2,030)	1,286	11,636
Transportation	131	582	2,149
Operating	(4,791)	6,029	3,753
General and administration	831	967	755
PRRT	(1,840)	(514)	5,310
Corporate income taxes	(2,294)	(8,953)	26,127
Interest	(260)	2,174	2,895
Realized derivatives	(11,612)	(19,244)	24,020
Realized foreign exchange	(782)	1,543	3,418
Realized other income	4,024	3,699	(28,644)
Fund flows from operations – Current period	**149,582**	**149,582**	**510,791**

Fund flows from operations was $149.6 million during Q4 2016, an increase of 6% from Q3 2016. This quarter-over-quarter increase was primarily attributable to higher commodity prices, partially offset by lower sales volumes.

Fund flows from operations increased by 10% in Q4 2016 as compared to Q4 2015 due to revenue from Ireland and higher crude oil pricing. For the year ended December 31, 2016, fund flows from operations was relatively consistent with the corresponding period in 2015 despite significantly lower commodity prices due to production from Ireland and a 16% reduction in per unit operating costs.

Fluctuations in fund flows from operations may occur as a result of changes in commodity prices and costs to produce petroleum and natural gas. In addition, fund flows from operations may be significantly affected by the timing of crude oil shipments in Australia and France. When crude oil inventory is built up, the related operating expense, royalties, and depletion expense are deferred and carried as inventory on the consolidated balance sheet. When the crude oil inventory is subsequently drawn down, the related expenses are recognized.

CANADA BUSINESS UNIT

Overview

- Production and assets focused in West Pembina near Drayton Valley, Alberta and Northgate in southeast Saskatchewan.
- Potential for three significant resource plays sharing the same surface infrastructure in the West Pembina region in Alberta:
  - Cardium light oil (1,800m depth) – in development phase
  - Mannville condensate-rich gas (2,400 – 2,700m depth) – in development phase
  - Duvernay condensate-rich gas (3,200 – 3,400m depth) – in appraisal phase with no investment at present
- Canadian cash flows are fully tax-sheltered for the foreseeable future.

Operational and financial review

	Three Months Ended			% change		Year Ended		% change
Canada business unit ($M except as indicated)	Dec 31, 2016	Sep 30, 2016	Dec 31, 2015	Q4/16 vs. Q3/16	Q4/16 vs. Q4/15	Dec 31, 2016	Dec 31, 2015	2016 vs. 2015
Production and sales								
Crude oil and condensate (bbls/d)	**7,945**	8,984	10,413	(12%)	(24%)	**9,171**	11,357	(19%)
NGLs (bbls/d)	**2,444**	2,448	2,710	-	(10%)	**2,552**	2,301	11%
Natural gas (mmcf/d)	**75.12**	77.62	87.90	(3%)	(15%)	**84.29**	71.65	18%
Total (boe/d)	**22,910**	24,368	27,773	(6%)	(18%)	**25,771**	25,598	1%
Production mix (% of total)								
Crude oil and condensate	**35%**	37%	37%			**36%**	44%	
NGLs	**11%**	10%	10%			**10%**	9%	
Natural gas	**54%**	53%	53%			**54%**	47%	
Activity								
Capital expenditures	**16,895**	10,421	27,554	62%	(39%)	**62,706**	201,508	(69%)
Acquisitions	**1,378**	10,380	6,169			**13,309**	14,650	
Gross wells drilled	**11.00**	4.00	5.00			**29.00**	42.00	
Net wells drilled	**7.02**	1.20	2.56			**17.62**	26.01	
Financial results								
Sales	**70,573**	64,453	73,952	9%	(5%)	**252,867**	320,613	(21%)
Royalties	**(7,390)**	(4,817)	(7,146)	53%	3%	**(21,475)**	(28,144)	(24%)
Transportation	**(3,504)**	(3,978)	(3,784)	(12%)	(7%)	**(15,392)**	(16,326)	(6%)
Operating	**(18,161)**	(15,579)	(24,575)	17%	(26%)	**(71,543)**	(89,085)	(20%)
General and administration	**(2,035)**	(3,010)	(3,669)	(32%)	(45%)	**(11,826)**	(16,888)	(30%)
Fund flows from operations	**39,483**	37,069	34,778	7%	14%	**132,631**	170,170	(22%)
Netbacks ($/boe)								
Sales	**33.48**	28.75	28.94	16%	16%	**26.81**	34.32	(22%)
Royalties	**(3.51)**	(2.15)	(2.80)	63%	25%	**(2.28)**	(3.01)	(24%)
Transportation	**(1.66)**	(1.77)	(1.48)	(6%)	12%	**(1.63)**	(1.75)	(7%)
Operating	**(8.62)**	(6.95)	(9.62)	24%	(10%)	**(7.59)**	(9.54)	(20%)
General and administration	**(0.97)**	(1.34)	(1.44)	(28%)	(33%)	**(1.25)**	(1.81)	(31%)
Fund flows from operations netback	**18.72**	16.54	13.60	13%	38%	**14.06**	18.21	(23%)
Realized prices								
Crude oil and condensate ($/bbl)	**62.13**	53.96	53.44	15%	16%	**52.44**	57.71	(9%)
NGLs ($/bbl)	**18.12**	12.49	7.89	45%	130%	**11.75**	10.32	14%
Natural gas ($/mmbtu)	**3.05**	2.39	2.57	28%	19%	**2.14**	2.78	(23%)
Total ($/boe)	**33.48**	28.75	28.94	16%	16%	**26.81**	34.32	(22%)
Reference prices								
WTI (US $/bbl)	**49.29**	44.94	42.18	10%	17%	**43.32**	48.80	(11%)
Edmonton Sweet index (US $/bbl)	**46.18**	42.06	39.72	10%	16%	**40.11**	44.91	(11%)
Edmonton Sweet index ($/bbl)	**61.60**	54.89	53.04	12%	16%	**53.17**	57.43	(7%)
AECO ($/mmbtu)	**3.09**	2.32	2.46	33%	26%	**2.16**	2.69	(20%)

Production

- Q4 2016 average production in Canada decreased by 6% quarter-over-quarter and 18% year-over-year due to production declines, cold weather related issues and the voluntary curtailment of approximately 13 mmcf/d (2,350 boe/d) of gas weighted production during the quarter. Full year average production increased 1% versus 2015 primarily due to strong organic production in our Mannville condensate-rich gas play offsetting declines in our Cardium and Saskatchewan Midale light oil plays.

- Cardium production averaged approximately 6,100 boe/d in Q4 2016, a 7% decrease quarter-over-quarter. Full year 2016 production averaged approximately 6,700 boe/d.
- Mannville production averaged approximately 9,600 boe/d in Q4 2016 representing a 6% decrease quarter-over-quarter. Full year 2016 production averaged more than 11,000 boe/d.
- Production from southeast Saskatchewan averaged approximately 2,100 boe/d in Q4 2016, a decrease of 13% quarter-over-quarter.

Activity review

- Vermilion drilled seven (6.0 net) operated wells and participated in the drilling of five (1.5 net) non-operated wells during Q4 2016. During 2016, Vermilion drilled 14 (12.6 net) operated wells and participated in the drilling of 15 (5.0 net) non-operated wells in Canada.

Cardium

- In 2016, we participated in the drilling of two (0.2 net) non-operated wells and three (0.5 net) non-operated wells were brought on production.
- In 2017, we plan to drill or participate in nine (6.0 net) wells.

Mannville

- During Q4 2016, we drilled seven (6.0 net) operated wells and participated in the drilling of four (1.5 net) non-operated wells.
- In 2016, we drilled or participated in 20 (12.0 net) wells.
- In 2017, we plan to drill or participate in 23 (15.0 net) wells and complete and tie-in six (5.0 net) wells drilled in 2016.

Saskatchewan

- During Q1 and Q2 2016, we drilled four (4.0 net) operated wells and participated in three (1.5 net) non-operated wells. We plan to complete and bring the four operated wells on production in Q1 2017. The non-operated wells were brought on production during the first half of 2016.
- In 2017, we plan to drill or participate in 13 (11.3 net) wells.

Sales

- The realized price for our crude oil and condensate production in Canada is linked to WTI, and is also subject to market conditions in western Canada. These market conditions can result in fluctuations in the pricing differential to WTI, as reflected by the Edmonton Sweet index price. The realized price of our NGLs in Canada is based on product specific differentials pertaining to trading hubs in the United States. The realized price of our natural gas in Canada is based on the AECO index in Canada.
- Q4 2016 sales per boe increased versus Q3 2016 and Q4 2015 due to stronger crude oil and natural gas pricing.
- Sales per boe for the year ended December 31, 2016 decreased versus the comparable period in 2015, primarily as a result of lower average crude oil and natural gas pricing.

Royalties

- Royalties as a percentage of sales for Q4 2016 increased to 10.5% as compared to 7.5% in Q3 2016 and 9.7% in Q4 2015 due to the impact of higher reference prices on the sliding scale used to determine royalty rates.
- Royalties as a percentage of sales for the year ended December 31, 2016 was 8.5% versus 8.8% in 2015 as the impact of lower reference prices more than offset wells coming off of incentive royalty rates after reaching specified production thresholds.

Transportation

- Transportation expense relates to the delivery of crude oil and natural gas production to major pipelines where legal title transfers.
- Transportation expense for Q4 2016 was lower than Q3 2016 and Q4 2015 due to lower production.
- Transportation expense for the year ended December 31, 2016 was 6% lower than the prior year while production increased 1%. This was due to a lower oil weighting, which incurs a higher per unit expense, and a reduction in transportation rates.

Operating

- Operating expense was higher on an absolute dollar and per boe basis in Q4 2016 versus Q3 2016. This was primarily due to the timing of project and maintenance activity that was executed in the current quarter.
- Operating expense for the three months and year ended December 31, 2016 decreased by 10% and 20% respectively on a per unit basis versus the comparable periods in 2015. Our continued focus on cost reduction initiatives including major project, transportation and other costs resulted in an annual reduction to operating expenses of $17.5 million while growing production by 1%.

General and administration

- General and administration expense fluctuation in Q4 2016 as compared to Q3 2016 was the result of timing of expenditures.
- Year-over-year, 2016 general and administration expense was 30% lower than 2015 due to initiatives to reduce our cost structure.

FRANCE BUSINESS UNIT

Overview

- Entered France in 1997 and completed three subsequent acquisitions, including two in 2012.
- Largest oil producer in France, constituting approximately three-quarters of domestic oil production.
- Low base decline producing assets comprised of large conventional oil fields with high working interests located in the Aquitaine and Paris Basins.
- Identified inventory of workover, infill drilling, and secondary recovery opportunities.

Operational and financial review

	Three Months Ended			% change		Year Ended		% change
France business unit ($M except as indicated)	**Dec 31, 2016**	Sep 30, 2016	Dec 31, 2015	Q4/16 vs. Q3/16	Q4/16 vs. Q4/15	**Dec 31, 2016**	Dec 31, 2015	2016 vs. 2015
Production								
Crude oil (bbls/d)	**11,220**	11,827	12,537	(5%)	(11%)	**11,896**	12,267	(3%)
Natural gas (mmcf/d)	**0.38**	0.42	1.36	(10%)	(72%)	**0.44**	0.97	(55%)
Total (boe/d)	**11,283**	11,897	12,763	(5%)	(12%)	**11,970**	12,429	(4%)
Sales								
Crude oil (bbls/d)	**12,209**	12,617	12,490	(3%)	(2%)	**12,157**	12,141	-
Natural gas (mmcf/d)	**0.38**	0.42	1.36	(11%)	(72%)	**0.44**	0.97	(54%)
Total (boe/d)	**12,272**	12,687	12,717	(3%)	(3%)	**12,231**	12,302	(1%)
Inventory (mbbls)								
Opening crude oil inventory	**239**	312	239			**243**	197	
Crude oil production	**1,032**	1,088	1,153			**4,354**	4,477	
Crude oil sales	**(1,123)**	(1,161)	(1,149)			**(4,449)**	(4,431)	
Closing crude oil inventory	**148**	239	243			**148**	243	
Activity								
Capital expenditures	**31,127**	11,110	24,085	180%	29%	**68,472**	92,265	(26%)
Acquisitions	**-**	-	79			**-**	317	
Gross wells drilled	**4.00**	-	-			**4.00**	4.00	
Net wells drilled	**4.00**	-	-			**4.00**	4.00	
Financial results								
Sales	**71,926**	65,221	63,411	10%	13%	**246,863**	281,422	(12%)
Royalties	**(6,692)**	(7,069)	(7,198)	(5%)	(7%)	**(27,091)**	(26,958)	-
Transportation	**(3,983)**	(3,586)	(4,275)	11%	(7%)	**(14,758)**	(15,378)	(4%)
Operating	**(11,482)**	(12,933)	(15,792)	(11%)	(27%)	**(50,000)**	(50,718)	(1%)
General and administration	**(5,101)**	(4,590)	(4,894)	11%	4%	**(19,101)**	(20,217)	(6%)
Other income	**3,822**	-	-	100%	100%	**3,822**	31,775	(88%)
Current income taxes	**(2,867)**	955	4,529	(400%)	(163%)	**(2,867)**	(23,764)	(88%)
Fund flows from operations	**45,623**	37,998	35,781	20%	28%	**136,868**	176,162	(22%)
Netbacks ($/boe)								
Sales	**63.71**	55.88	54.20	14%	18%	**55.15**	62.67	(12%)
Royalties	**(5.93)**	(6.06)	(6.15)	(2%)	(4%)	**(6.05)**	(6.00)	1%
Transportation	**(3.53)**	(3.07)	(3.65)	15%	(3%)	**(3.30)**	(3.42)	(4%)
Operating	**(10.17)**	(11.08)	(13.50)	(8%)	(25%)	**(11.17)**	(11.30)	(1%)
General and administration	**(4.52)**	(3.93)	(4.18)	15%	8%	**(4.27)**	(4.50)	(5%)
Other income	**3.39**	-	-	100%	100%	**0.85**	7.08	(88%)
Current income taxes	**(2.54)**	0.82	3.87	(410%)	(166%)	**(0.64)**	(5.29)	(88%)
Fund flows from operations	**40.41**	32.56	30.59	24%	32%	**30.57**	39.24	(22%)
Realized prices								
Crude oil ($/bbl)	**63.99**	56.14	54.88	14%	17%	**55.42**	63.31	(12%)
Natural gas ($/mmbtu)	**1.55**	1.58	2.81	(2%)	(45%)	**1.59**	2.52	(37%)
Total ($/boe)	**63.71**	55.88	54.20	14%	18%	**55.15**	62.67	(12%)
Reference prices								
Dated Brent (US $/bbl)	**49.46**	45.85	43.69	8%	13%	**43.69**	52.46	(17%)
Dated Brent ($/bbl)	**65.97**	59.84	58.34	10%	13%	**57.92**	67.09	(14%)

Production
- Q4 2016 production decreased 5% versus the prior quarter and 12% versus Q4 2015. Full year production decreased 4% versus 2015. Decreased production for the quarter and the year were primarily due to production declines, well downtime and third party restrictions impacting Vic Bilh gas production.

Activity review
- During Q4 2016, we drilled four wells in Champotran and commenced drilling of a horizontal sidetrack well in the Vulaines field, with completion and tie-in planned for early 2017.
- In 2016, additional activity included workover and optimization programs in the Aquitaine and Paris Basins.
- In 2017, we plan to drill our first four (4.0 net) wells in the Neocomian fields in the Paris Basin, in addition to continuing our workover and optimization activities.

Sales
- Crude oil in France is priced with reference to Dated Brent.
- Q4 2016 sales per boe increased versus Q3 2016 and Q4 2015 as a result of stronger Dated Brent pricing.
- Sales per boe for the year ended December 31, 2016, decreased versus the comparable period in 2015 as a result of lower average crude oil pricing.

Royalties
- Royalties in France relate to two components: RCDM (levied on units of production and not subject to changes in commodity prices) and R31 (based on a percentage of sales).
- Royalties as a percentage of sales of 9.3% for the three months ended December 31, 2016 was lower than Q3 2016 (10.8%) and Q4 2015 (11.3%) as a result of the impact of fixed RCDM royalties coupled with higher realized pricing in the current quarter. On a year-over-year basis, the royalty rate increased to 11.0% versus 9.6% in 2015 due to lower realized pricing in the current year.

Transportation
- Transportation expense per boe for Q4 2016 was higher than Q3 2016 and consistent with Q4 2015. The increase over Q3 2016 was due to the timing of project and maintenance activity executed in the current quarter.
- Transportation expense decreased by 4% for 2016 versus 2015 as a result of initiatives to reduce our cost structure, which included vessel cost renegotiation and lower project activity.

Operating
- Operating expense on a dollar and per boe basis decreased in Q4 2016 versus both Q3 2016 and Q4 2015 due to the timing of expenditures and a continued focus on initiatives to reduce costs.
- Year-over-year, operating expense decreased on a dollar and per boe basis in 2016 versus 2015 due to the continuation of focus on cost reduction initiatives identified in 2015 and new initiatives identified in 2016, which more than off-set unfavourable foreign exchange rates as the Canadian dollar weakened versus the Euro. After normalizing for the unfavorable foreign exchange, per unit costs decreased 4.5% in 2016.

General and administration
- General and administration expense for Q4 2016 was 11% higher than Q3 2016 and 4% higher than Q4 2015 due to the timing of expenditures and recoveries.
- Year-over-year, 2016 general and administration expense was 6% lower than 2015 due to the impact of cost reduction initiatives.

Other income
- In 2015, Vermilion was awarded a recovery of costs resulting from an oil spill at the Ambès oil terminal in France that occurred in 2007. The court awarded Vermilion approximately €25 million (before taxes), of which 50% was due immediately to Vermilion upon posting a surety bond. The payment was received in 2015, with the remainder due upon conclusion of the appeal process. Approximately 90% of the recovery was recorded as other income in 2015.
- In Q4 2016, the Court of Appeal of Versailles maintained this award. The remaining payment was received and Vermilion's surety bond was returned in 2017. The remaining amount of the recovery was recognized as other income in 2016.

Current income taxes
- In France, current income taxes are applied to taxable income, after eligible deductions, at a statutory rate of 34.4% for 2016.
- Current income taxes in Q4 2016 were higher compared to Q3 2016 due to increased sales and other income. Q4 2016 current income taxes were higher compared to Q4 2015 due to increased sales and the reversal of tax depletion impairments taken in Q4 2015.
- Current income taxes for the year ended December 31, 2016 were lower versus the comparative period in 2015 as a result of decreased sales and other income.

NETHERLANDS BUSINESS UNIT

Overview

- Entered the Netherlands in 2004.
- Second largest onshore gas producer.
- Interests include 24 onshore licenses and two offshore licenses.
- Licenses include more than 800,000 net acres of land, 95% of which is undeveloped.

Operational and financial review

Netherlands business unit ($M except as indicated)	Three Months Ended Dec 31, 2016	Three Months Ended Sep 30, 2016	Three Months Ended Dec 31, 2015	% change Q4/16 vs. Q3/16	% change Q4/16 vs. Q4/15	Year Ended Dec 31, 2016	Year Ended Dec 31, 2015	% change 2016 vs. 2015
Production and sales								
Condensate (bbls/d)	**57**	86	110	(34%)	(48%)	**88**	99	(11%)
Natural gas (mmcf/d)	**41.15**	47.62	56.34	(14%)	(27%)	**47.82**	44.76	7%
Total (boe/d)	**6,915**	8,023	9,500	(14%)	(27%)	**8,058**	7,559	7%
Activity								
Capital expenditures	**5,737**	6,441	18,810	(11%)	(70%)	**23,740**	47,325	(50%)
Acquisitions	**28,259**	-	-			**28,259**	-	
Gross wells drilled	**-**	2.00	-			**2.00**	2.00	
Net wells drilled	**-**	0.88	-			**0.88**	1.86	
Financial results								
Sales	**25,978**	23,470	37,243	11%	(30%)	**100,707**	129,057	(22%)
Royalties	**(294)**	(312)	(224)	(6%)	31%	**(1,462)**	(3,082)	(53%)
Operating	**(5,660)**	(4,854)	(6,263)	17%	(10%)	**(20,796)**	(22,746)	(9%)
General and administration	**(162)**	633	(813)	(126%)	(80%)	**(1,525)**	(4,158)	(63%)
Current income taxes	**100**	(1,264)	(2,930)	(108%)	(103%)	**(6,624)**	(12,152)	(45%)
Fund flows from operations	**19,962**	17,673	27,013	13%	(26%)	**70,300**	86,919	(19%)
Netbacks ($/boe)								
Sales	**40.84**	31.80	42.61	28%	(4%)	**34.15**	46.77	(27%)
Royalties	**(0.46)**	(0.42)	(0.26)	10%	77%	**(0.50)**	(1.12)	(55%)
Operating	**(8.90)**	(6.58)	(7.17)	35%	24%	**(7.05)**	(8.24)	(14%)
General and administration	**(0.26)**	0.86	(0.93)	(130%)	(72%)	**(0.52)**	(1.51)	(66%)
Current income taxes	**0.16**	(1.71)	(3.35)	(109%)	(105%)	**(2.25)**	(4.40)	(49%)
Fund flows from operations netback	**31.38**	23.95	30.90	31%	2%	**23.83**	31.50	(24%)
Realized prices								
Condensate ($/bbl)	**63.18**	49.43	48.30	28%	31%	**44.93**	49.98	(10%)
Natural gas ($/mmbtu)	**6.78**	5.27	7.09	29%	(4%)	**5.67**	7.79	(27%)
Total ($/boe)	**40.84**	31.80	42.61	28%	(4%)	**34.15**	46.77	(27%)
Reference prices								
TTF ($/mmbtu)	**7.21**	5.43	7.28	33%	(1%)	**6.00**	8.23	(27%)
TTF (€/mmbtu)	**5.01**	3.73	4.98	34%	1%	**4.09**	5.80	(29%)

Production

- Q4 2016 production decreased 14% quarter-over-quarter and 27% year-over-year due to production curtailments in accordance with extended well test plans and management of production to meet corporate production targets.
- Full year 2016 production increased 7% versus 2015, primarily due to production additions from Slootdorp-06/07 and Diever-02 wells, which were on extended production test.
- Production in the Netherlands is actively managed to optimize facility use and regulate declines.

Activity review

- During Q3 2016, Vermilion drilled two (0.9 net) wells. Langezwaag-3 (42% working interest) was completed and brought on production during Q4 2016, at a restricted rate of 7.5 mmcf/d. The Andel-6ST (45% working interest) encountered a large gas column of inadequate reservoir quality to justify completion.
- During Q4 2016, we acquired an additional 30% working interest in the Drenthe VI production license, adding 30,000 net acres of land, including 26,000 net acres of undeveloped land and a 30% after payout interest in one well.
- In 2017, we plan to drill two (1.0 net) exploration wells, acquire 230 square kilometres of 3D seismic and execute a major turnaround at the Garijp Treatment Centre.

Sales

- The price of our natural gas in the Netherlands is based on the TTF index.
- Q4 2016 sales per boe increased versus Q3 2016 consistent with an increase in the TTF reference price.
- Sales per boe for the three months ended December 31, 2016 were relatively consistent with the comparable period in 2015. For the year ended December 31, 2016, sales per boe decreased consistent with a decrease in the TTF reference price.

Royalties

- In the Netherlands, we pay overriding royalties on certain wells. As such, fluctuations in royalty expense in the periods presented relate to the amount of production from those wells subject to overriding royalties.

Transportation

- Our production in the Netherlands is not subject to transportation expense as gas is sold at the plant gate.

Operating

- Q4 2016 operating expense on a per boe basis increased versus Q3 2016 and Q4 2015 due to increased project activity and lower recoveries.
- Year-over-year, 2016 operating expense decreased by 9% on a dollar basis while growing production by 7% resulting in a 14% per unit decrease as a result of focus on initiatives to reduce our cost structure.

General and administration

- Variances in general and administration expense from quarter to quarter relate to timing of expenditures, including the timing of allocations from Vermilion's Corporate segment.
- Year-over-year the decrease in general and administration is primarily due to lower head office allocations.

Current income taxes

- In the Netherlands, current income taxes are applied to taxable income, after eligible deductions and a 10% uplift deduction applied to operating expenses, eligible G&A and tax deductions for depletion and abandonment retirement obligations, at a tax rate of 50%.
- Current income taxes in Q4 2016 were lower compared to Q3 2016 due to increased tax deductions for current year capital expenditures. Q4 2016 current income taxes were lower compared to Q4 2015 mainly due to decreased sales.
- Current income taxes for the year ended December 31, 2016 were lower versus the comparative period in 2015 due to decreased operating income in 2016, partially offset by additional tax deductions for capital expenditures in 2015.

GERMANY BUSINESS UNIT

Overview

- Vermilion entered Germany in February 2014.
- Hold a 25% interest in a four partner consortium. Associated assets include four gas producing fields spanning 11 production licenses as well as an exploration license in surrounding fields. Total license area comprises 204,000 gross acres, of which 85% is in the exploration license.
- Entered into a farm-in agreement in July 2015 that provides Vermilion with participating interest in 18 onshore exploration licenses in northwest Germany, comprising approximately 850,000 net undeveloped acres of oil and natural gas rights. Vermilion will operate 11 of the 18 licenses during the exploration phase.
- Awarded 110,000 net acres (100% working interest) across two exploration licenses in the Lower Saxony basin in 2015.
- In December 2016, Vermilion closed the acquisition of operated and non-operated interests in five oil and three gas producing fields from Engie E&P Deutschland GmbH. Vermilion will assume operatorship of six of the eight producing fields. During 2016, the assets produced approximately 2,000 boe/d (50% oil), representing our first operated producing properties in Germany.

Operational and financial review

Germany business unit ($M except as indicated)	Three Months Ended Dec 31, 2016	Sep 30, 2016	Dec 31, 2015	% change Q4/16 vs. Q3/16	Q4/16 vs. Q4/15	Year Ended Dec 31, 2016	Dec 31, 2015	% change 2016 vs. 2015
Production and sales								
Natural gas (mmcf/d)	**14.80**	14.52	16.17	2%	(8%)	**14.90**	15.78	(6%)
Total (boe/d)	**2,467**	2,420	2,695	2%	(8%)	**2,483**	2,630	(6%)
Activity								
Capital expenditures	**1,694**	978	(441)	73%	(484%)	**3,803**	5,363	(29%)
Acquisitions	**48,377**	-	-			**48,377**	-	
Gross wells drilled	**-**	-	-			**-**	1.00	
Net wells drilled	**-**	-	-			**-**	0.25	
Financial results								
Sales	**8,294**	6,783	9,840	22%	(16%)	**29,049**	41,384	(30%)
Royalties	**(12)**	(246)	(1,166)	(95%)	(99%)	**(2,089)**	(6,479)	(68%)
Transportation	**(375)**	(556)	(508)	(33%)	(26%)	**(2,869)**	(3,269)	(12%)
Operating	**(3,959)**	(3,321)	(4,788)	19%	(17%)	**(12,379)**	(10,956)	13%
General and administration	**(1,755)**	(1,657)	(3,032)	6%	(42%)	**(8,314)**	(7,386)	13%
Fund flows from operations	**2,193**	1,003	346	119%	534%	**3,398**	13,294	(74%)
Netbacks ($/boe)								
Sales	**36.54**	30.47	39.68	20%	(8%)	**31.97**	43.10	(26%)
Royalties	**(0.06)**	(1.10)	(4.70)	(95%)	(99%)	**(2.30)**	(6.75)	(66%)
Transportation	**(1.65)**	(2.50)	(2.05)	(34%)	(20%)	**(3.16)**	(3.41)	(7%)
Operating	**(17.44)**	(14.92)	(19.31)	17%	(10%)	**(13.62)**	(11.41)	19%
General and administration	**(7.73)**	(7.44)	(12.22)	4%	(37%)	**(9.15)**	(7.69)	19%
Fund flows from operations netback	**9.66**	4.51	1.40	114%	590%	**3.74**	13.84	(73%)
Reference prices								
TTF ($/mmbtu)	**7.21**	5.43	7.28	33%	(1%)	**6.00**	8.23	(27%)
TTF (€/mmbtu)	**5.01**	3.73	4.98	34%	1%	**4.09**	5.80	(29%)

Production

- Q4 2016 production remained consistent with the prior quarter, and decreased 8% versus Q4 2015 and 6% for the full year 2016 versus 2015 mainly due to natural declines.

Activity review

- In 2016, the majority of activity was associated with permitting and pre-drill activities for the Burgmoor Z5 well.
- During December 2016, we completed the acquisition of oil and gas producing properties from Engie E&P Deutschland GmbH, which provides us with our first operated production in the country.
- In 2017, we plan to continue our ongoing analysis of the geologic data associated with the farm-in assets and to continue integration activities associated with the Engie acquisition. We will also continue permitting and pre-drill activities associated our first operated well in Germany, Burgmoor Z5 well (25% working interest) in the Dümmersee-Uchte area, which we plan to drill in 2018.

Sales

- The price of our natural gas in Germany is based on the TTF index.
- Q4 2016 sales per boe increased versus Q3 2016, consistent with an increase in the TTF reference price. Q4 2016 sales per boe decreased versus Q4 2015 as a result of a decrease in the TTF month-ahead index on which sales in Germany are primarily based.
- For the year ended December 31, 2016, sales per boe decreased compared to 2015, consistent with a decline in the TTF reference price.

Royalties

- Our production in Germany is subject to state and private royalties on sales after certain eligible deductions.
- Q4 2016 royalties as a percentage of sales was a negligible amount versus 3.6% in Q3 2016 and 11.8% in Q4 2015. The decrease in Q4 2016 was due to favourable adjustments from prior periods.
- Full year 2016 royalties as a percentage of sales was 7.2% versus 15.7% in 2015 as a result of favourable prior year adjustments impacting 2016.

Transportation

- Transportation expense in Germany relates to costs incurred to deliver natural gas from the processing facility to the customer.
- Q4 2016 transportation expense decreased from Q3 2016 due to seasonal changes in the level of transportation facility maintenance, which is typically higher at the beginning of the year.
- Year-over-year transportation expense decreased due to a decrease in volumes and a reduction in unfavourable prior period adjustments in 2016.

Operating

- Operating expenses for Germany primarily relate to tariffs charged for facility operations and gas processing.
- Operating expense for Q4 2016 increased versus Q3 2016 due to increased project activity.
- Full year operating expense was higher on a dollar and per boe basis due to an unfavorable adjustment from the prior year recorded in 2016 and increased project activity.

General and administration

- Q4 2016 general and administration expense was higher than Q3 2016 and lower than Q4 2015 due to timing of head office allocations.
- Full year 2016 general and administration expense increased over 2015 due to higher staffing levels and office costs incurred to support our farm-in agreement as well as costs incurred to support asset acquisition activity.
- We expect per unit general and administration costs to improve as our production base in Germany grows.

IRELAND BUSINESS UNIT

Overview

- 18.5% non-operating interest in the offshore Corrib gas field located approximately 83 km off the northwest coast of Ireland.
- Project comprises six offshore wells, offshore and onshore sales and transportation pipeline segments as well as a natural gas processing facility.
- Production volumes reached full plant capacity of approximately 65 mmcf/d (10,900 boe/d), net to Vermilion, at the end of Q2 2016.

Operational and financial review

	Three Months Ended			% change		Year Ended		% change
Ireland business unit ($M except as indicated)	Dec 31, 2016	Sep 30, 2016	Dec 31, 2015	Q4/16 vs. Q3/16	Q4/16 vs. Q4/15	Dec 31, 2016	Dec 31, 2015	2016 vs. 2015
Production and sales								
Natural gas (mmcf/d)	**62.92**	59.28	0.12	6%	52,771%	**50.89**	0.03	169,547%
Total (boe/d)	**10,486**	9,879	20.00	6%	52,330%	**8,482**	5.00	169,540%
Activity								
Capital expenditures	**1,711**	2,416	12,493	(29%)	(86%)	**9,375**	66,409	(86%)
Financial results								
Sales	**42,727**	26,065	57	64%	74,860%	**109,156**	57	191,402%
Transportation	**(1,703)**	(1,576)	(1,580)	8%	8%	**(6,492)**	(6,687)	(3%)
Operating	**(5,148)**	(4,695)	(15)	10%	34,220%	**(18,646)**	(15)	124,207%
General and administration	**(1,523)**	(955)	(714)	59%	113%	**(4,772)**	(2,517)	90%
Fund flows from operations	**34,353**	18,839	(2,252)	82%	(1,625%)	**79,246**	(9,162)	(965%)
Netbacks ($/boe)								
Sales	**44.29**	28.68	-	54%	100%	**35.16**	-	100%
Transportation	**(1.77)**	(1.73)	-	2%	100%	**(2.09)**	-	100%
Operating	**(5.34)**	(5.17)	-	3%	100%	**(6.01)**	-	100%
General and administration	**(1.58)**	(1.05)	-	50%	100%	**(1.54)**	-	100%
Fund flows from operations netback	**35.60**	20.73	-	72%	100%	**25.52**	-	
Reference prices								
NBP ($/mmbtu)	**7.51**	5.29	7.41	42%	1%	**6.15**	8.33	(26%)
NBP (€/mmbtu)	**5.22**	3.63	5.07	44%	3%	**4.19**	5.87	(29%)

Production

- Natural gas began to flow from our Corrib gas project on December 30, 2015 and production volumes reached full plant capacity of approximately 65 mmcf/d (10,900 boe/d), net to Vermilion at the end of Q2 2016.
- Q4 2016 production increased 6% quarter-over-quarter due to reduced downtime. Full year production averaged 51 mmcf/d (8,482 boe/d) while ramping up to full capacity.
- Production results continued to benefit from better than expected well deliverability and minimal downtime.

Activity review

- Following the conclusion of a successful offshore work campaign in Q3 2016 that included laying a flowline to the P2 well, all six wells are now available for production.

Sales

- The price of our natural gas in Ireland is based on the NBP index.
- Q4 2016 sales per boe increased relative to Q3 2016, consistent with an increase in the NBP reference price.

Royalties

- Our production in Ireland is not subject to royalties.

Transportation

- Transportation expense in Ireland relates to payments under a ship-or-pay agreement related to the Corrib project.
- Q4 2016 transportation expense increased versus Q3 2016 and Q4 2015 due to a prior period adjustment in the current quarter offsetting the decrease in the ship-or-pay obligation.
- Full year 2016 transportation expense decreased versus 2015 due to the decrease in the ship or pay obligation.

Operating

- Q4 2016 operating expense on a per unit basis was consistent with Q3 2016, contributing to full year 2016 per unit costs of $6.01/boe.

General and administration

- General and administrative expense for the three months ended December 31, 2016 was higher versus Q3 2016 due to timing of expenditures.
- General and administrative expense for the three months and year ended December 31, 2016 was higher than the comparable periods in 2015 due to increased corporate support provided in the first full year of operations.

AUSTRALIA BUSINESS UNIT

Overview

- Entered Australia in 2005.
- Hold a 100% operated working interest in the Wandoo field, located approximately 80 km offshore on the northwest shelf of Australia.
- Production is operated from two off-shore platforms, and originates from 18 well bores and five lateral sidetrack wells.
- Wells that utilize horizontal legs (ranging in length from 500 to 3,000 plus metres) are located 600 metres below the seabed in approximately 55 metres of water depth.

Operational and financial review

	Three Months Ended			% change		Year Ended		% change
Australia business unit ($M except as indicated)	Dec 31, 2016	Sep 30, 2016	Dec 31, 2015	Q4/16 vs. Q3/16	Q4/16 vs. Q4/15	Dec 31, 2016	Dec 31, 2015	2016 vs. 2015
Production								
Crude oil (bbls/d)	**6,388**	6,562	7,824	(3%)	(18%)	**6,304**	6,454	(2%)
Sales								
Crude oil (bbls/d)	**6,038**	8,041	8,873	(25%)	(32%)	**6,197**	6,351	(2%)
Inventory (mbbls)								
Opening crude oil inventory	**82**	218	172	(62%)	(52%)	**75**	37	103%
Crude oil production	**588**	604	720	(3%)	(18%)	**2,307**	2,356	(2%)
Crude oil sales	**(555)**	(740)	(817)	(25%)	(32%)	**(2,267)**	(2,318)	(2%)
Closing crude oil inventory	**115**	82	75			**115**	75	
Activity								
Capital expenditures	**5,236**	6,908	40,852	(24%)	(87%)	**59,910**	61,741	(3%)
Gross wells drilled	**-**	-	1.00			**2.00**	1.00	
Net wells drilled	**-**	-	1.00			**2.00**	1.00	
Financial results								
Sales	**38,352**	44,835	47,952	(14%)	(20%)	**136,835**	162,765	(16%)
Operating	**(14,905)**	(13,011)	(13,941)	15%	7%	**(47,507)**	(51,676)	(8%)
General and administration	**(1,998)**	(1,289)	(1,768)	55%	13%	**(6,400)**	(5,754)	11%
PRRT	**(1,568)**	272	(1,054)	(676%)	49%	**(1,568)**	(6,878)	(77%)
Current income taxes	**(2,703)**	(2,916)	1,201	(7%)	(325%)	**(7,522)**	(7,230)	4%
Fund flows from operations	**17,178**	27,891	32,390	(38%)	(47%)	**73,838**	91,227	(19%)
Netbacks ($/boe)								
Sales	**69.05**	60.61	58.74	14%	18%	**60.33**	70.22	(14%)
Operating	**(26.83)**	(17.59)	(17.08)	53%	57%	**(20.95)**	(22.29)	(6%)
General and administration	**(3.60)**	(1.74)	(2.17)	107%	66%	**(2.82)**	(2.48)	14%
PRRT	**(2.82)**	0.37	(1.29)	(862%)	119%	**(0.69)**	(2.97)	(77%)
Current income taxes	**(4.87)**	(3.94)	1.47	24%	(431%)	**(3.32)**	(3.12)	6%
Fund flows from operations netback	**30.93**	37.71	39.67	(18%)	(22%)	**32.55**	39.36	(17%)
Reference prices								
Dated Brent (US $/bbl)	**49.46**	45.85	43.69	8%	13%	**43.69**	52.46	(17%)
Dated Brent ($/bbl)	**65.97**	59.84	58.34	10%	13%	**57.92**	67.09	(14%)

Production

- Q4 2016 production decreased 3% quarter-over-quarter and 18% year-over-year. The year-over-year decrease is primarily due to production decline from the horizontal sidetrack well drilled and placed on production in Q4 2015. Full year 2016 production decreased 2% versus 2015.
- Production volumes are managed within corporate targets while meeting customer demands and the requirements of long-term supply agreements.
- We continue to plan for long-term production levels of between 6,000 and 8,000 bbls/d.

Activity review

- The two sidetrack wells we drilled during Q2 2016 continued to demonstrate strong productive capability with combined production rates of approximately 4,300 bbls/d when utilized. Vermilion intends to produce these wells intermittently to meet corporate production targets while seeking to optimize ultimate recoveries and oil pricing. Following our successful 2015 and 2016 drilling campaigns, we do not expect to drill any additional wells in Australia until 2019.
- Additional 2016 activity included work on our Wandoo Platforms Life Extension project, CALM buoy maintenance and subsea inspections.

Sales

- Crude oil in Australia is priced with reference to Dated Brent.
- Q4 2016 sales per boe increased versus Q3 2016 and Q4 2015 consistent with an increase in the Dated Brent reference price. This increase in price was offset by lower sold volumes due to an inventory build in Q4 2016, resulting in a decrease in sales.
- Sales per boe for the year ended December 31, 2016 decreased versus the comparable period in 2015 consistent with a decrease in the Dated Brent reference price.

Royalties and transportation

- Our production in Australia is not subject to royalties or transportation expense as crude oil is sold directly at the Wandoo B platform.

Operating

- Operating expense on a dollar per boe basis increased in Q4 2016 versus Q3 2016 and Q4 2015. The increase was a result of increased project and maintenance work being completed in the current quarter as a result of the drill program being executed earlier in the year.
- Operating expense on a dollar and per boe basis decreased in 2016 versus 2015 due to a continued focus on initiatives to reduce our cost structure resulting in lower diesel, vessel and maintenance costs.

General and administration

- Fluctuation in general and administration expense for Q4 2016 versus the comparable quarters was largely the result of the timing of expenditures. Full year 2016 general and administration expense increased due to higher employee benefit costs.

PRRT and corporate income taxes

- In Australia, current income taxes include both PRRT and corporate income taxes. PRRT is a profit based tax applied at a rate of 40% on sales less eligible expenditures, including operating expenses and capital expenditures. Corporate income taxes are applied at a rate of 30% on taxable income after eligible deductions, which include PRRT paid.
- Current income taxes in Q4 2016 were lower compared to Q3 2016 due to decreased sales. Q4 2016 current income taxes were higher compared to Q4 2015 as decreased sales were offset by lower tax deductions.
- Current income taxes for the year ended December 31, 2016 were slightly higher versus the comparable period in 2015 as lower sales were offset with increased deductions for PRRT and foreign exchange in 2015.
- PRRT in Q4 2016 was higher compared to Q3 2016 due to the impact of an increase in full year sales (resulting from a significant increase in crude oil pricing) compared to our forecast in Q3 2016. Q4 2016 PRRT was higher compared to Q4 2015 as lower sales were offset with higher deductions for capital expenditures in Q4 2015.
- PRRT for the year ended December 31, 2016, was lower versus the comparable period in 2015 as a result of decreased sales.

UNITED STATES BUSINESS UNIT

Overview

- Entered the United States in September 2014.
- Interests include approximately 97,200 net acres of land (97% undeveloped) in the Powder River Basin of northeastern Wyoming.
- Tight oil development targeting the Turner Sand at a depth of approximately 1,500 metres.

Operational and financial review

	Three Months Ended			% change		Year Ended		% change
United States business unit ($M except as indicated)	Dec 31, 2016	Sep 30, 2016	Dec 31, 2015	Q4/16 vs. Q3/16	Q4/16 vs. Q4/15	Dec 31, 2016	Dec 31, 2015	2016 vs. 2015
Production and sales								
Crude oil (bbls/d)	**362**	383	420	(5%)	(14%)	**393**	231	70%
NGLs (bbls/d)	**23**	30	29	(23%)	(21%)	**29**	7	314%
Natural gas (mmcf/d)	**0.18**	0.20	0.20	(10%)	(13%)	**0.21**	0.05	312%
Total (boe/d)	**414**	447	483	(7%)	(14%)	**457**	247	85%
Activity								
Capital expenditures	**4,037**	2,765	5,643	46%	(28%)	**13,539**	12,250	11%
Acquisitions	**377**	11	(21)			**5,935**	12,764	
Gross wells drilled	**1.00**	-	2.00			**1.00**	3.00	
Net wells drilled	**1.00**	-	2.00			**1.00**	3.00	
Financial results								
Sales	**2,041**	1,833	1,864	11%	9%	**7,314**	4,288	71%
Royalties	**(611)**	(525)	(551)	16%	11%	**(2,167)**	(1,257)	72%
Operating	**(301)**	(432)	(271)	(30%)	11%	**(1,314)**	(742)	77%
General and administration	**(877)**	(918)	(897)	(4%)	(2%)	**(3,624)**	(3,836)	(6%)
Fund flows from operations	**252**	(42)	145	700%	74%	**209**	(1,547)	114%
Netbacks ($/boe)								
Sales	**53.58**	44.53	41.94	20%	28%	**43.70**	47.53	(8%)
Royalties	**(16.05)**	(12.74)	(12.40)	26%	29%	**(12.95)**	(13.93)	(7%)
Operating	**(7.91)**	(10.50)	(6.11)	(25%)	29%	**(7.85)**	(8.23)	(5%)
General and administration	**(23.02)**	(22.30)	(20.18)	3%	14%	**(21.65)**	(42.51)	(49%)
Fund flows from operations netback	**6.60**	(1.01)	3.25	753%	103%	**1.25**	(17.14)	107%
Realized prices								
Crude oil ($/bbl)	**59.09**	51.29	47.59	15%	24%	**49.86**	50.49	(1%)
NGLs ($/bbl)	**19.48**	5.14	5.13	279%	280%	**7.38**	5.13	44%
Natural gas ($/mmbtu)	**1.93**	0.64	0.52	202%	271%	**0.85**	0.52	63%
Total ($/boe)	**53.58**	44.53	41.94	20%	28%	**43.70**	47.53	(8%)
Reference prices								
WTI (US $/bbl)	**49.29**	44.94	42.18	10%	17%	**43.32**	48.80	(11%)
WTI ($/bbl)	**65.75**	58.65	56.32	12%	17%	**57.42**	62.41	(8%)
Henry Hub (US $/mmbtu)	**2.98**	2.81	2.27	6%	31%	**2.46**	2.66	(8%)
Henry Hub ($/mmbtu)	**3.98**	3.67	3.03	8%	31%	**3.27**	3.41	(4%)

Production

- Q4 2016 production decreased 7% quarter-over-quarter and 14% year-over-year due to natural declines.
- Full year 2016 production increased 85% versus 2015 due to production from our two wells drilled in the East Finn prospect in Q4 2015.

Activity

- In Q4 2016, we completed the Seedy Draw East Federal well. The nearly 1,400 metre horizontal lateral was stimulated with 32 frac stages, but due to a screen-out during treatment, only 23 stages were completed. We plan to clean sand out of this well and put it on production during Q1 2017, leaving the remaining nine stages for potential stimulation at a later date.
- During 2016, we drilled one (1.0 net) well, and completed and tied-in two (2.0 net) wells drilled in Q4 2015.
- In 2017, we plan to drill and complete three (3.0 net) wells.

Sales

- The price of crude oil in the United States is directly linked to WTI, but is also subject to market conditions in the United States.
- Q4 2016 sales per boe increased versus Q3 2016 and Q4 2015 consistent with an increase in the WTI reference price.
- Sales per boe for the year ended December 31, 2016 decreased versus the comparable period in 2015, consistent with a decrease in the WTI reference price.

Royalties

- Our production in the United States is subject to federal and private royalties, severance tax, and ad valorem tax.
- Royalties (including severance and ad valorem taxes) as a percentage of sales are approximately 30% and has remained consistent across all periods.

Operating

- The decrease in operating expense for Q4 2016 compared to Q3 2016 and increase from Q4 2015 were primarily due to timing of maintenance and repair activity.
- On a year-over-year basis, per unit costs have decreased 5% due to production growth and initiatives to reduce our cost structure.

General and administration

- On a year-over-year basis initiatives taken to reduce our cost structure have resulted in a 6% reduction in costs while growing production 85%.

CORPORATE

Overview

- Our Corporate segment includes costs related to our global hedging program, financing expenses, and general and administration expenses that are primarily incurred in Canada and are not directly related to the operations of our business units. Expenditures relating to our activities in Central and Eastern Europe are also included in the Corporate segment.

Financial review

	Three Months Ended			Year Ended	
CORPORATE ($M)	Dec 31, 2016	Sep 30, 2016	Dec 31, 2015	Dec 31, 2016	Dec 31, 2015
General and administration recovery (expense)	**1,987**	(509)	3,356	**2,733**	7,172
Current income taxes	**(370)**	(321)	313	**(1,097)**	(1,091)
Interest expense	**(14,410)**	(14,150)	(16,584)	**(56,957)**	(59,852)
Realized gain on derivatives	**1,920**	13,532	21,164	**65,376**	41,356
Realized foreign exchange gain (loss)	**1,291**	2,073	(252)	**4,041**	623
Realized other income (expense)	**120**	(82)	243	**205**	896
Fund flows from operations	**(9,462)**	543	8,240	**14,301**	(10,896)

General and administration

- Fluctuations in general and administration costs for Q4 2016 versus all comparable periods is due to the timing of expenditures and allocations to the various business unit segments.

Current income taxes

- Taxes in our corporate segment relate to holding companies that pay current taxes in foreign jurisdictions.

Interest expense

- Interest expense in Q4 2016 was relatively consistent with Q3 2016.
- The decrease in interest expense for the three months and year ended December 31, 2016 compared to the same periods in 2015, was primarily due to the retiring of our 6.5% senior unsecured notes in February 2016 using funds from our revolving credit facility, partially offset by higher average borrowings under our revolving credit facility.

Hedging

- The nature of our operations results in exposure to fluctuations in commodity prices, interest rates and foreign currency exchange rates. We monitor and, when appropriate, use derivative financial instruments to manage our exposure to these fluctuations and reduce cash flow volatility. All transactions of this nature entered into are related to an underlying financial position or to future crude oil and natural gas production. We do not use derivative financial instruments for speculative purposes. We have elected not to designate any of our derivative financial instruments as accounting hedges and thus account for changes in fair value in net earnings at each reporting period. We have not obtained collateral or other security to support our financial derivatives as we review the creditworthiness of our counterparties prior to entering into derivative contracts.
- Our hedging philosophy is to hedge solely for the purposes of risk mitigation. Our approach is to hedge centrally to manage our global risk (typically with an outlook of 12 to 18 months) up to 50% of net of royalty volumes through a portfolio of collars and swaps. We currently have European gas contracts for 2019 as an exception to our typical horizon.
- We believe that our hedging philosophy and approach increases the stability of revenues, cash flows, and future dividends while also assisting us in the execution of our capital and development plans.
- The realized gain on derivatives in 2016 related primarily to amounts received on our European natural gas hedges.
- A listing of derivative positions as at December 31, 2016 is included in “Supplemental Table 2” of this MD&A.

FINANCIAL PERFORMANCE REVIEW

($M except per share)	Year Ended Dec 31, 2016	Dec 31, 2015	Dec 31, 2014
Total assets	**4,087,184**	4,209,220	4,386,091
Long-term debt	**1,362,192**	1,162,998	1,238,080
Petroleum and natural gas sales	**882,791**	939,586	1,419,628
Net (loss) earnings	**(160,051)**	(217,302)	269,326
Net (loss) earnings per share			
Basic	**(1.38)**	(1.98)	2.55
Diluted	**(1.38)**	(1.98)	2.51
Cash dividends ($/share)	**2.58**	2.58	2.58

	Three Months Ended							
($M except per share)	Dec 31, 2016	Sep 30, 2016	Jun 30, 2016	Mar 31, 2016	Dec 31, 2015	Sep 30, 2015	Jun 30, 2015	Mar 31, 2015
Petroleum and natural gas sales	**259,891**	232,660	212,855	177,385	234,319	245,051	264,331	195,885
Net (loss) earnings	**(4,032)**	(14,475)	(55,696)	(85,848)	(142,080)	(83,310)	6,813	1,275
Net (loss) earnings per share								
Basic	**(0.03)**	(0.12)	(0.48)	(0.76)	(1.28)	(0.76)	0.06	0.01
Diluted	**(0.03)**	(0.12)	(0.48)	(0.76)	(1.28)	(0.76)	0.06	0.01

The following table shows a reconciliation from fund flows from operations to net loss:

	Three Months Ended			Year Ended	
	Dec 31, 2016	Sep 30, 2016	Dec 31, 2015	Dec 31, 2016	Dec 31, 2015
Fund flows from operations	**149,582**	140,974	136,441	**510,791**	516,167
Equity based compensation	**(19,489)**	(15,642)	(21,533)	**(69,235)**	(75,232)
Unrealized (loss) gain on derivative instruments	**(74,943)**	332	27,393	**(137,993)**	43,548
Unrealized foreign exchange (loss) gain	**(2,457)**	2,899	(6,357)	**(792)**	8,787
Unrealized income (expense)	**-**	(24)	(234)	**(131)**	(1,008)
Accretion	**(6,308)**	(6,341)	(6,324)	**(24,783)**	(23,911)
Depletion and depreciation	**(126,855)**	(143,556)	(107,812)	**(528,002)**	(458,758)
Deferred taxes	**54,437**	6,883	(32,031)	**82,855**	47,728
Gain on business combination	**22,001**	-	-	**22,001**	-
Impairment	**-**	-	(131,623)	**(14,762)**	(274,623)
Net loss	**(4,032)**	(14,475)	(142,080)	**(160,051)**	(217,302)

The fluctuations in net income from period-to-period are caused by changes in both cash and non-cash based income and charges. Cash based items are reflected in fund flows from operations. Non-cash items include: equity based compensation expense, unrealized gains and losses on derivative instruments, unrealized foreign exchange gains and losses, accretion, depletion and depreciation expense, and deferred taxes. In addition, non-cash items may also include amounts resulting from business combinations or charges resulting from impairment or impairment reversals.

Equity based compensation

Equity based compensation expense relates primarily to non-cash compensation expense attributable to long-term incentives granted to directors, officers, and employees under the Vermilion Incentive Plan ("VIP").

Equity based compensation in Q4 2016 increased as compared to Q3 2016 due to a revision of performance estimates. For the three months and year ended December 31, 2016, the decrease in equity based compensation is primarily due to the lower average grant value.

Unrealized gain or loss on derivative instruments

Unrealized gain or loss on derivative instruments arise as a result of changes in forecasted future commodity prices. As Vermilion uses derivative instruments to manage the commodity price exposure of our future crude oil and natural gas production, we will normally recognize unrealized gains on derivative instruments when forecasted future commodity prices decline and vice-versa.

For the year ended December 31, 2016, we recognized an unrealized loss on derivative instruments of $138.0 million. This unrealized loss resulted from realizing gains on derivatives for contracts settled during the period, coupled with higher forward prices for European natural gas as at December 31, 2016. As at December 31, 2016, we have a net derivative liability position of $69.7 million.

Unrealized foreign exchange gain or loss

As a result of Vermilion's international operations, Vermilion has monetary assets and liabilities denominated in currencies other than the Canadian dollar. These monetary assets and liabilities include cash, receivables, payables, long-term debt, derivative instruments and intercompany loans, primarily denominated in the US dollar and Euro.

Unrealized foreign exchange gains and losses result from translating these monetary assets and liabilities from their underlying currency to the functional currency of Vermilion and its subsidiaries. Unrealized foreign exchange primarily results from the translation of Euro denominated financial assets and US dollar denominated financial liabilities. As such, an appreciation in the Euro against the Canadian dollar will result in an unrealized foreign exchange gain while an appreciation in the US dollar against the Canadian dollar will result in an unrealized foreign exchange loss (and vice-versa).

For the three months ended December 31, 2016, the Canadian dollar weakened against the US dollar and strengthened against the Euro, resulting in an unrealized foreign exchange loss of $2.5 million. For the year ended December 31, 2016, the Canadian dollar strengthened more significantly against the Euro than the US dollar, resulting in an unrealized foreign exchange loss of $0.8 million.

Accretion

Accretion expense is recognized to update the present value of the asset retirement obligation balance. Accretion expense was relatively consistent with all comparative periods.

Depletion and depreciation

Depletion and depreciation expense is recognized to allocate the capitalized cost of extracting natural resources and the cost of material assets over the useful life of the respective assets. Fluctuations in depletion and depreciation expense are primarily the result of changes in produced crude oil and natural gas volumes.

Depletion and depreciation on a per boe basis for Q4 2016 of $22.42 was relatively consistent as compared to $23.69 in Q3 2016.

For the three months ended December 31, 2016, depletion and depreciation on a per boe basis of $22.42 was higher than $18.88 in the same period of 2015 due to production from Ireland. For the year ended December 31, 2016, depletion and depreciation on a per boe basis of $22.65 was relatively consistent with $22.98 in the same period of 2015 as increased production from Ireland was offset by increased production from our Mannville condensate-rich gas properties.

Deferred tax

Deferred tax recovery arises primarily as a result of changes in the accounting basis and tax basis for capital assets and asset retirement obligations and changes in available tax losses.

Impairment

In 2015, as a result of declines in price forecasts for crude oil and Canadian natural gas, Vermilion recorded a non-cash impairment charge of $274.6 million ($219.8 million relating to capital assets and $54.8 million relating to E&E assets) in the Canada segment. The impairment charge related to the light crude oil play in Saskatchewan ($267.9 million based on a recoverable amount of $266.8 million) and shallow coal bed methane properties in Alberta ($6.7 million based on a recoverable amount of $19.7 million).

In the first quarter of 2016, as a result of declines in price forecasts for European natural gas, Vermilion recorded a non-cash impairment charge of $14.8 million (based on a recoverable amount of $737.3 million).

Gain on business combination

In December of 2016, we acquired, through a wholly-owned subsidiary, interests in production and exploration assets in Germany from Engie E&P Deutschland GmbH.

We recognized a non-cash gain on business combination of $22.0 million that resulted from the recognition of additional reserve value when the acquisition closed in December 2016, compared to the estimated value in June when Vermilion entered into a definitive purchase and sale agreement and the acquisition price was determined.

TAXES

Corporate income tax rates

Vermilion pays corporate income taxes in France, the Netherlands, and Australia. In addition, Vermilion pays PRRT in Australia. PRRT is a profit based tax applied at a rate of 40% on sales less operating expenses, capital expenditures, and other eligible expenditures. PRRT is deductible in the calculation of taxable income in Australia.

Taxable income was subject to corporate income tax at the following rates:

Jurisdiction	2016	2015
Canada [1]	27.0%	25.5% / 27.0%
France	34.4%	34.4%
Netherlands [2]	50.0%	50.0%
Germany	24.2%	24.2%
Ireland	25.0%	25.0%
Australia	30.0%	30.0%
United States	35.0%	35.0%

[1] Alberta corporate income tax rates increased from 10% to 12% effective July 1, 2015.
[2] In the Netherlands, an additional 10% uplift deduction is allowed against taxable income that is applied to operating expenses, eligible G&A and tax deductions for depletion and abandonment retirement obligations.

In 2012, the France government enacted a new 3% tax on dividend distributions made by entities subject to corporate income tax in France. The tax applies to any dividends paid on or after April 17, 2012 and is not recovered by any tax treaties or deductible for French corporate income tax purposes. In late December 2016, the French government passed legislation that will exempt any dividend distributions made by Vermilion after January 1, 2017 from the 3% tax. Vermilion did not pay any dividends from its French entities in 2016.

Tax pools

As at December 31, 2016, we had the following tax pools:

($M)	Oil & Gas Assets	Tax Losses	Other	Total
Canada	978,949 [1]	489,702 [5]	32,503	1,501,154
France	351,551 [2]	13,360 [6]	-	364,911
Netherlands	68,139 [3]	-	-	68,139
Germany	190,002 [3]	57,156 [7]	20,306	267,464
Ireland	942,129 [4]	403,779 [5]	-	1,345,908
Australia	276,911 [1]	-	-	276,911
United States	34,885 [1]	30,328 [5]	797	66,010
Total	2,842,566	994,325	53,606	3,890,497

[1] Deduction calculated using various declining balance rates
[2] Deduction calculated using a combination of straight-line over the assets life and unit of production method
[3] Deduction calculated using a unit of production method
[4] Deduction for current development expenditures and tax losses at 100% against taxable income
[5] Tax losses can be carried forward at 100% against taxable income
[6] Tax losses carried forward are available to offset the first Euro 1million of taxable income and 50% of taxable profits in excess each taxation year
[7] Tax losses carried forward are available to offset the first Euro 1million of taxable income and 60% of taxable profits in excess each taxations year

FINANCIAL POSITION REVIEW

Balance sheet strategy

We believe that our balance sheet supports our defined growth initiatives and our focus is on managing and maintaining a conservative balance sheet. To ensure that our balance sheet continues to support our defined growth initiatives, we regularly review whether forecasted fund flows from operations is sufficient to finance planned capital expenditures, dividends, and abandonment and reclamation expenditures. To the extent that forecasted fund flows from operations is not expected to be sufficient to fulfill such expenditures, we will evaluate our ability to finance any shortfall with debt (including borrowing using the unutilized capacity of our existing revolving credit facility), issue equity, or by reducing some or all categories of expenditures to ensure that total expenditures do not exceed available funds.

To ensure that we maintain a conservative balance sheet, we monitor the ratio of net debt to fund flows from operations and typically strive to maintain an internally targeted ratio of approximately 1.0 to 1.5 in a normalized commodity price environment. Where prices trend higher, we may target a lower ratio and conversely, in a lower commodity price environment, an acceptable ratio may be higher. At times, we will use our balance sheet to finance acquisitions and, in these situations, we are prepared to accept a higher ratio in the short term but will implement a strategy to reduce the ratio to acceptable levels within a reasonable period of time, usually considered to be no more than 12 to 24 months. This plan could potentially include an increase in hedging activities, a reduction in capital expenditures, an issuance of equity or the utilization of excess fund flows from operations to reduce outstanding indebtedness.

In the current low commodity price environment, Vermilion's net debt to fund flows from operations ratio is expected to be higher than the internally targeted ratio. During this period, Vermilion will remain focused on maintaining a strong balance sheet by aligning capital expenditures within forecasted fund flows from operations, which is continually monitored for revised forward price estimates, as well as by hedging additional European natural gas volumes to maintain a diversified commodity portfolio.

Long-term debt

Our long-term debt as at December 31, 2016 consists entirely of borrowings against our revolving credit facility. We redeemed the senior unsecured notes that came due on February 10, 2016 using funds drawn against the revolving credit facility.

The balances recognized on our balance sheet are as follows:

	As at	
($M)	Dec 31, 2016	Dec 31, 2015
Revolving credit facility	**1,362,192**	1,162,998
Senior unsecured notes	**-**	224,901
Long-term debt	**1,362,192**	1,387,899

Revolving Credit Facility

The following table outlines the current terms of our revolving credit facility:

	As at	
($M)	Dec 31, 2016	Dec 31, 2015
Total facility amount	**2,000,000**	2,000,000
Amount drawn	**(1,362,192)**	(1,162,998)
Letters of credit outstanding	**(20,100)**	(25,200)
Unutilized capacity	**617,708**	811,802

In addition, as at December 31, 2016, the revolving credit facility was subject to the following covenants:

		As at	
Financial covenant	**Limit**	**Dec 31, 2016**	**Dec 31, 2015**
Consolidated total debt to consolidated EBITDA	4.0	**2.36**	2.23
Consolidated total senior debt to total capitalization	55%	**46%**	36%

Our covenants include financial measures defined within our revolving credit facility agreement that are not defined under IFRS. These financial measures are defined by our revolving credit facility agreement as follows:

- Consolidated total debt: Includes all amounts classified as "Long-term debt", "Current portion of long-term debt", and "Finance lease obligation" on our balance sheet.
- Consolidated total senior debt: Defined as consolidated total debt excluding unsecured and subordinated debt.
- Consolidated EBITDA: Defined as consolidated net earnings before interest, income taxes, depreciation, accretion and certain other non-cash items.
- Total capitalization: Includes all amounts on our balance sheet classified as "Shareholders' equity" plus consolidated total debt as defined above.

Net debt
Net debt is reconciled to long-term debt, as follows:

($M)	As at Dec 31, 2016	As at Dec 31, 2015
Long-term debt	**1,362,192**	1,162,998
Current liabilities [1]	**290,862**	503,731
Current assets	**(225,906)**	(284,778)
Net debt	**1,427,148**	1,381,951
Ratio of net debt to fund flows from operations	**2.8**	2.7

[1] Current liabilities at December 31, 2015 includes $224,901 relating to the current portion of long-term debt.

As at December 31, 2016, long term debt decreased to $1.36 billion (December 31, 2015 - $1.39 billion, including the current portion of long-term debt) as fund flows from operations generated in excess of capital expenditures, abandonment expenditures, acquisitions, and cash dividends was used to reduce debt. The decrease in long-term debt was coupled with working capital changes, such that net debt increased from $1.38 billion at December 31, 2015 to $1.43 billion at December 31, 2016. Weaker commodity prices versus the prior period decreased fund flows from operations, resulting in the ratio of net debt to fund flows from operations increasing slightly from 2.7 to 2.8.

Shareholders' capital
During the year ended December 31, 2016, we maintained monthly dividends at $0.215 per share and declared dividends which totalled $299.1 million.

The following table outlines our dividend payment history:

Date	Monthly dividend per unit or share
January 2003 to December 2007	$0.170
January 2008 to December 2012	$0.190
January 2013 to December 31, 2013	$0.200
January 2014 to Present	$0.215

Our policy with respect to dividends is to be conservative and maintain a low ratio of dividends to fund flows from operations. During low commodity price cycles, we will initially maintain dividends and allow the ratio to rise. Should low commodity price cycles remain for an extended period of time, we will evaluate the necessity of changing the level of dividends, taking into consideration capital development requirements, debt levels, and acquisition opportunities.

In February of 2015, we amended our existing dividend reinvestment plan to include a Premium Dividend™ Component. The Premium Dividend™ Component, when combined with our continuing Dividend Reinvestment Component, increases our access to the lowest cost sources of equity capital available. While the Premium Dividend™ results in a modest amount of equity issuance, we believe it represents the most prudent approach to preserving near-term balance sheet strength. Both components of our program can be reduced or eliminated at the company's discretion, offering considerable flexibility.

As previously announced, we commenced proration of the Premium Dividend™ of our Dividend Reinvestment Plan by 25% beginning with our October dividend payment. Eligible shareholders who have elected to participate in the Premium Dividend™ component were then receiving the 1.5% premium on 75% of their participating shares and the regular cash dividend on the remaining 25% of their shares. We increased the proration factor by a further 25% beginning with the January 2017 dividend payment. Subject to unexpected changes in the commodity price outlook, we expect to continue to increase the proration by 25% per quarter during the first half of 2017, such that, by the beginning of the third quarter, there would be no further equity issuance under the Premium Dividend™ component of our Dividend Reinvestment Plan. We also reduced the discount associated with our traditional Dividend Reinvestment Plan from 3% to 2%, beginning with the January 2017 dividend payment.

Although we expect to be able to maintain our current dividend, fund flows from operations may not be sufficient during this low commodity price environment to fund cash dividends, capital expenditures, and asset retirement obligations. We will evaluate our ability to finance any shortfall with debt, issuances of equity, or by reducing some or all categories of expenditures to ensure that total expenditures do not exceed available funds.

The following table reconciles the change in shareholders' capital:

Shareholders' Capital	Number of Shares ('000s)	Amount ($M)
Balance as at December 31, 2015	111,991	2,181,089
Shares issued for the DRIP[1]	4,671	192,998
Vesting of equity based awards	1,320	67,146
Share-settled dividends on vested equity based awards	87	3,242
Shares issued for equity based compensation	194	8,247
Balance as at December 31, 2016	118,263	2,452,722

[1] DRIP Refers to Vermilion's Premium Dividend™ and Dividend Reinvestment Plan.

As at December 31, 2016, there were approximately 1.7 million VIP awards outstanding. As at February 24, 2017, there were approximately 118.7 million common shares issued and outstanding.

CONTRACTUAL OBLIGATIONS AND COMMITMENTS

As at December 31, 2016, we had the following contractual obligations and commitments:

($M)	Less than 1 year	1 - 3 years	3 - 5 years	After 5 years	Total
Long-term debt	-	1,335,600	-	-	1,335,600
Operating lease obligations	12,683	21,087	18,228	1,657	53,655
Ship or pay agreement relating to the Corrib project	4,241	7,331	6,074	31,427	49,073
Purchase obligations	9,007	3,852	7	-	12,866
Drilling and service agreements	5,437	9,850	20,511	26,870	62,668
Total contractual obligations and commitments	31,368	1,377,720	44,820	59,954	1,513,862

ASSET RETIREMENT OBLIGATIONS

As at December 31, 2016, asset retirement obligations were $525.0 million compared to $305.6 million as at December 31, 2015.

The increase in asset retirement obligations is largely attributable to an overall decrease in the discount rates applied to the abandonment obligation, additional obligations recognized on our acquisition in Germany, and accretion expense.

RISKS AND UNCERTAINTIES

Crude oil and natural gas exploration, production, acquisition and marketing operations involve a number of risks and uncertainties including financial risks and uncertainties. These include fluctuations in commodity prices, exchange rates and interest rates as well as uncertainties associated with reserve and resource volumes, sales volumes and government regulatory and income tax regime changes. These and other related risks and uncertainties are discussed in additional detail below.

Commodity prices

Our operational results and financial condition is dependent on the prices received for crude oil and natural gas production. Crude oil and natural gas prices have fluctuated significantly during recent years and are determined by supply and demand factors, including weather and general economic conditions as well as conditions in other crude oil and natural gas producing regions.

Exchange rates

Much of our revenue stream is priced in U.S. dollars and as such an increase in the strength of the Canadian dollar relative to the U.S. dollar may result in the receipt of fewer Canadian dollars with respect to our production. In addition, we incur expenses and capital costs in U.S. dollars, Euros and Australian dollars and accordingly, the Canadian dollar equivalent of these expenditures as reported in our financial results is impacted by the prevailing exchange rates at the time the transaction occurs. We monitor risks associated with exchange rates and, when appropriate, use derivative financial instruments to manage our exposure to these risks.

Production and sales volumes

The operation of crude oil and natural gas wells and facilities involves a number of operating and natural hazards which may result in blowouts, environmental damage and other unexpected or dangerous conditions resulting in damage to us and possible liability to third parties. We maintain liability insurance, where available, in amounts consistent with industry standards. Business interruption insurance may also be purchased for selected operations, to the extent that such insurance is commercially viable. We may become liable for damages arising from such events against which we cannot insure or against which we may elect not to insure because of high premium costs or other reasons. Costs incurred to repair such damage or pay such liabilities may materially impact our financial results.

Continuing production from a property, and to some extent the marketing of produced volumes, is largely dependent upon the ability of the operator of the property. To the extent the operator fails to perform these functions properly, revenue may be reduced. Payments from production generally flow through the operator and there is a risk of delay and additional expense in receiving such revenues if the operator becomes insolvent. Although satisfactory title reviews are generally conducted in accordance with industry standards, such reviews do not guarantee or certify that a defect in the chain of title may not arise to defeat our claim to certain properties. Such circumstances could negatively affect our financial results.

An increase in operating costs or a decline in our production level could have an adverse effect on our financial results. The level of production may decline at rates greater than anticipated due to unforeseen circumstances, many of which are beyond our control. A significant decline in production could result in materially lower revenues.

Interest rates

An increase in interest rates could result in a significant increase in the amount we pay to service debt.

Reserve volumes

Our reserve volumes and related reserve values support the carrying value of our crude oil and natural gas assets on the consolidated balance sheets and provide the basis to calculate the depletion of those assets. There are numerous uncertainties inherent in estimating quantities of reserves and future net revenues to be derived therefrom, including many factors beyond our control. These include a number of assumptions relating to factors such as initial production rates, production decline rates, ultimate recovery of reserves, timing and amount of capital expenditures, marketability of production, future prices of crude oil, NGLs and natural gas, operating expenses, well abandonment and salvage values, royalties and any government levies that may be imposed over the producing life of the reserves. These assumptions were based on estimated prices in use at the date the evaluation was prepared, and many of these assumptions are subject to change and are beyond our control. Actual production and income derived therefrom will vary from these evaluations, and such variations could be material.

Asset retirement obligations

Our asset retirement obligations are based on environmental regulations and estimates of future costs and the timing of expenditures. Changes in environmental regulations, the estimated costs associated with reclamation activities and the related timing may impact our financial position and results of operations.

Government regulation and income tax regime

Our operations are governed by many levels of government, including municipal, state, provincial and federal governments, in Canada, France, the Netherlands, Australia, Germany, Ireland, Hungary, Croatia, Slovakia and the United States. We are subject to laws and regulations regarding environment, health and safety issues, lease interests, taxes and royalties, among others. Failure to comply with the applicable laws can result in significant increases in costs, penalties and even losses of operating licences. The regulatory process involved in each of the countries in which we operate is not uniform and regulatory regimes vary as to complexity, timeliness of access to, and response from, regulatory bodies and other matters specific to each jurisdiction. If regulatory approvals or permits are delayed or not obtained, there can also be delays or abandonment of projects and decreases in production and increases in costs, potentially resulting in us being unable to fully execute our strategy. Governments may also amend or create new legislation and regulatory bodies may also amend regulations or impose additional requirements which could result in increased capital, operating and compliance costs.

There can be no assurance that income tax laws and government incentive programs relating to the crude oil and natural gas industry in Canada and the foreign jurisdictions in which we operate, will not be changed in a manner which adversely affects the results of our operations.

A change in the royalty regime resulting in an increase in royalties would reduce our net earnings and could make future capital expenditures or our operations uneconomic and could, in the event of a material increase in royalties, make it more difficult to service and repay outstanding debt. Any material increase in royalties would also significantly reduce the value of the associated assets.

FINANCIAL RISK MANAGEMENT

To mitigate the aforementioned risks whenever possible, we seek to hire personnel with experience in specific areas. In addition, we provide continued training and development to staff to further develop their skills. When appropriate, we use third party consultants with relevant experience to augment our internal capabilities with respect to certain risks.
We consider our commodity price risk management program as a form of insurance that protects our cash flow and rate of return. The primary objective of the risk management program is to support our dividends and our internal capital development program. The level of commodity price risk management that occurs is highly dependent on the amount of debt that is carried. When debt levels are higher, we will be more active in protecting our cash flow stream through our commodity price risk management strategy.

When executing our commodity price risk management programs, we use derivative financial instruments encompassing over-the-counter financial structures as well as fixed/collar structures to economically hedge a part of our physical crude oil and natural gas production. We have strict controls and guidelines in relation to these activities and contract principally with counterparties that have investment grade credit ratings.

CRITICAL ACCOUNTING ESTIMATES

The preparation of financial statements in accordance with IFRS requires management to make estimates, judgments and assumptions that affect reported assets, liabilities, income and expenses, as well as disclosures of any possible contingencies. These estimates and assumptions are developed based on the best available information which management believed to be reasonable at the time such estimates and assumptions were made. As such, these assumptions are uncertain at the time estimates are made and could change, resulting in a material impact on our consolidated financial statements or financial performance. Estimates are reviewed by management on an ongoing basis, and as a result, certain estimates may change from period to period due to the availability of new information or changes in circumstances. Additionally, as a result of the unique circumstances of each jurisdiction in which we operate, the critical accounting estimates may affect one or more jurisdictions.

The following discussion outlines what management believes to be the most critical accounting policies involving the use of estimates and assumptions.

- Asset retirement obligations: Asset retirement obligations are based on judgments regarding regulatory requirements, estimates of future costs, and the expected timing of expenditures. The carrying balance of asset retirement obligations and accretion expense may differ due to changes in: laws and regulations, technology, the expected timing of expenditures, and market conditions affecting the discount rate applied.
- Determination of CGUs: CGU determination is subject to management's judgment of the lowest level at which there are identifiable cash inflows that are largely independent of the cash inflows of other groups of assets. The factors used by Vermilion to determine CGUs vary by jurisdiction due to their unique operating and geographic conditions. In general, Vermilion will assess the following factors: geographic proximity of the assets within a group to one another, geographic proximity of the group of assets to other groups of assets, homogeneity of the production from the group of assets and the sharing of infrastructure used to process and/or transport production. The composition of CGUs can directly impact the calculated recoverable amount of a CGU and the recorded impairment loss or recovery.
- Assessment of impairments or recovery of previous impairments: The calculation of the recoverable amount of a CGU is based on market factors and estimates of reserves and resources. Reserve and resource estimates are based on: engineering data, estimated future commodity prices, expected future rates of production, and assumptions regarding the timing and amount of future expenditures. Changes in these judgments, estimates and assumptions can directly impact the calculated recoverable amount of a CGU and the recorded impairment loss or recovery.
- Income Taxes: Tax interpretations, regulations, and legislation in the various jurisdictions in which Vermilion and its subsidiaries operate are subject to change and interpretation. Changes in laws and interpretations can affect the timing of the reversal of temporary tax differences, the tax rates in effect when such differences reverse and Vermilion's ability to use tax losses and other tax pools in the future. The Company's income tax filings are subject to audit by taxation authorities in numerous jurisdictions and the results of such audits may increase or decrease the tax liability. The determination of tax amounts recognized in the consolidated financial statements are based on management's assessment of the tax positions, which includes consideration of their technical merits, communications with tax authorities and management's view of the most likely outcome.

OFF BALANCE SHEET ARRANGEMENTS

We have certain lease agreements that are entered into in the normal course of operations, including operating leases for which no asset or liability value has been assigned to the consolidated balance sheet as at December 31, 2016.

We have not entered into any guarantee or off balance sheet arrangements that would materially impact our financial position or results of operations.

ACCOUNTING PRONOUNCEMENTS NOT YET ADOPTED

The following IFRS have been issued by the IASB but are not yet effective:

- IFRS 9 "Financial Instruments" will be adopted January 1, 2018. IFRS 9 includes changes to the classification and measurement of financial instruments and general hedge accounting.
- IFRS 15 "Revenue from Contracts with Customers" will be adopted January 1, 2018. IFRS 15 specifies recognition and measurement requirements for contracts with customers.
- IFRS 16 "Leases" will be adopted January 1, 2019. IFRS 16 requires lessees to recognize a lease obligation and right-of-use asset for the majority of leases.

On the adoption of IFRS 9, Vermilion does not currently anticipate changes to the measured amount of financial instruments and correspondingly does not currently anticipate material changes to net earnings.

In the adoption of IFRS 15, Vermilion has in place a transition team that will perform a detailed review of the Company's standard contracts with customers in accordance with the issued IFRS.

The impact of the adoption of IFRS 16 is currently being evaluated.

HEALTH, SAFETY AND ENVIRONMENT

We are committed to ensuring we conduct our activities in a manner that will protect the health and safety of our employees, contractors, and the public. Our health, safety, and environment ("HSE") vision is to fully integrate health, safety, and environment into our business, where our culture is recognized as a model by industry and stakeholders, resulting in a safe and healthy workplace. Our mantra is HSE: Everywhere. Everyday. Everyone.

We maintain health, safety and environmental practices and procedures in compliance with or exceeding regulatory requirements and industry standards. All of our personnel are expected to work safely and in accordance with established regulations and procedures, and we seek to keep our people safe and to reduce impacts to land, water and air. During 2016 we:

- Maintained clear priorities around 5 key focus areas of HSE Culture, Communication and Knowledge Management, Technical Safety Management, Incident Prevention and Operational Stewardship & Sustainability;
- Completed and published our Corporate Sustainability Report;
- Reported our CO_2e emissions to the Carbon Disclosure Project, achieving a position on the Climate "A" list. One of only 5 oil and gas companies world-wide to achieve this ranking.
- Completed a corporate wide HSE perception survey to monitor program progress and verify plan forward;
- Emphasized improving energy efficiency, greenhouse gas emissions reduction and water efficiency optimization;
- Further refined and expanded our enterprise wide corporate risk register;
- Developed and delivered a robust organization-wide HSE leadership training program to improve hazard identification and risk reduction;
- Maintained focus on our recently developed risk mitigation program around our top fatal risk and energy type exposures;
- Continued development of a robust hazard identification and risk mitigation program specific to environmentally sensitive areas;
- Implemented our Corporate Process Hazards Analysis Standard in support of our focus on process safety;
- Initiated the development of our Corporate Process Safety Management System;
- Further progressed our Asset Integrity Management System;
- Completed a comprehensive review of our Management of Change procedures across the organization;
- Reduced long-term environmental liabilities through decommissioning, abandoning and reclaiming well leases and facilities;
- Performed auditing, management inspections and workforce observations to identify potential hazards and apply risk reduction measures;
- Developed, communicated and measured against leading and lagging HSE key performance indicators;
- Further enhanced of our competency and training programs;
- Managed our waste products by reducing, recycling and recovering; and
- Continued risk management efforts in addition to detailed emergency-response planning.

We are a member of several organizations concerned with environment, health and safety, including numerous regional co-operatives and synergy groups. In the area of stakeholder relations, we work to build long-term relationships with environmental stakeholders and communities.

SUSTAINABILITY

As a responsible oil and gas producer, we consistently seek to deliver long-term shareholder value by operating in an economically, environmentally and socially sustainable manner that is recognized as a model in our industry.

Vermilion regularly communicates with its stakeholders, including shareholders and potential investors, and we continually monitor trends and best practices in stakeholder engagement. Reporting on sustainability, or corporate social responsibility, is an increasingly important way to reflect Company performance for shareholders and potential investors. As a result, Vermilion published its first sustainability report in August 2014, in compliance with the comprehensive option of the Global Reporting Initiative's G4 reporting framework. We continue to report on this basis annually, as it provides an opportunity to share how we identify our economic, environmental and social impacts, integrate their associated opportunities and risks into our business strategies, and chart our progress.

Our stakeholders expect us to deliver strong financial results in a responsible and ethical way. Reflecting this, we strive to operate in a manner that protects the health and safety of our staff and communities, provides responsible stewardship over the environment, and treats staff, contractors, partners and suppliers respectfully and fairly.

As a result, we align expectations for economic success with the elements of our sustainability commitments, leading us to prioritize our objectives as follows:

- The safety and health of our staff and those involved directly or indirectly in our operations.
- Our responsibility to protect the environment. We follow the Precautionary Principle introduced in 1992 by the United Nations "Rio Declaration on Environment and Development" by using environmental risk as part of our development decision criteria, and by continually seeking improved environmental performance in our operations.
- Economic success through a focus on operational excellence across our business, which includes technical and process excellence, efficiency, expertise and stakeholder relations.
- Vermilion's sustainability performance has earned consistently higher rankings. In 2016, Corporate Knights ranked Vermilion 9th in their Future 40 listing, up from 15th in 2015 and 32nd in 2014.

CORPORATE GOVERNANCE

We are committed to a high standard of corporate governance practices, a dedication that begins at the Board level and extends throughout the Company. We believe good corporate governance is in the best interest of our shareholders, and that successful companies are those that deliver growth and a competitive return along with a commitment to the environment, to the communities where they operate and to their employees.

We comply with the objectives and guidelines relating to corporate governance adopted by the Canadian Securities Administrators and the Toronto Stock Exchange. In addition, the Board monitors and considers the implementation of corporate governance standards proposed by various regulatory and non-regulatory authorities in Canada. A discussion of corporate governance policies is included each year in our proxy materials for our annual general meeting of shareholders, copies of which are available on SEDAR (www.sedar.com).

A summary of the significant differences between the governance practices of the Company and those required of U.S. domestic companies under the New York Stock Exchange listing standards can be found in the Governance section of the Company's website at http://www.vermilionenergy.com/about/governance.cfm.

DISCLOSURE CONTROLS AND PROCEDURES

Our officers have established and maintained disclosure controls and procedures and evaluated the effectiveness of these controls in conjunction with our filings.

As of December 31, 2016, we have evaluated the effectiveness of the design and operation of our disclosure controls and procedures. Based on this evaluation, the Chief Executive Officer and Chief Financial Officer have concluded and certified that our disclosure controls and procedures are effective.

INTERNAL CONTROL OVER FINANCIAL REPORTING

A company's internal control over financial reporting is a process to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

The Chief Executive Officer and the Chief Financial Officer of Vermilion have assessed the effectiveness of Vermilion's internal control over financial reporting as defined in Rule 13a-15 under the US Securities Exchange Act of 1934 and as defined in Canada by National Instrument 52-109, Certification of Disclosure in Issuers' Annual and Interim Filings. The assessment was based on the framework in *Internal Control – Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Chief Executive Officer and the Chief Financial Officer of Vermilion have concluded that Vermilion's internal control over financial reporting was effective as of December 31, 2016. The effectiveness of Vermilion's internal control over financial reporting as of December 31, 2016 has been audited by Deloitte LLP, as reflected in their report included in the 2016 audited annual financial statements filed with the US Securities and Exchange Commission. No changes were made to Vermilion's internal control over financial reporting during the year ended December 31, 2016, that have materially affected, or are reasonably likely to materially affect, the internal controls over financial reporting.

Supplemental Table 1: Netbacks

The following table includes financial statement information on a per unit basis by business unit. Natural gas sales volumes have been converted on a basis of six thousand cubic feet of natural gas to one barrel of oil equivalent.

	Three Months Ended December 31, 2016			Year Ended December 31, 2016			Three Months Ended Dec 31, 2015	Year Ended Dec 31, 2015
	Crude Oil, Condensate & NGLs $/bbl	Natural Gas $/mcf	Total $/boe	Crude Oil, Condensate & NGLs $/bbl	Natural Gas $/mcf	Total $/boe	Total $/boe	Total $/boe
Canada								
Sales	51.77	3.05	**33.48**	43.58	2.14	**26.81**	28.94	34.32
Royalties	(6.17)	(0.22)	**(3.51)**	(4.37)	(0.09)	**(2.28)**	(2.80)	(3.01)
Transportation	(2.34)	(0.18)	**(1.66)**	(2.36)	(0.17)	**(1.63)**	(1.48)	(1.75)
Operating	(9.49)	(1.32)	**(8.62)**	(8.05)	(1.20)	**(7.59)**	(9.62)	(9.54)
Operating netback	33.77	1.33	**19.69**	28.80	0.68	**15.31**	15.04	20.02
General and administration			**(0.97)**			**(1.25)**	(1.44)	(1.81)
Fund flows from operations netback			**18.72**			**14.06**	13.60	18.21
France								
Sales	63.99	1.55	**63.71**	55.42	1.59	**55.15**	54.20	62.67
Royalties	(5.95)	(0.36)	**(5.93)**	(6.08)	(0.34)	**(6.05)**	(6.15)	(6.00)
Transportation	(3.55)	-	**(3.53)**	(3.32)	-	**(3.30)**	(3.65)	(3.42)
Operating	(10.13)	(3.12)	**(10.17)**	(11.15)	(2.51)	**(11.17)**	(13.50)	(11.30)
Operating netback	44.36	(1.93)	**44.08**	34.87	(1.26)	**34.63**	30.90	41.95
General and administration			**(4.52)**			**(4.27)**	(4.18)	(4.50)
Other income			**3.39**			**0.85**	-	7.08
Current income taxes			**(2.54)**			**(0.64)**	3.87	(5.29)
Fund flows from operations netback			**40.41**			**30.57**	30.59	39.24
Netherlands								
Sales	63.18	6.78	**40.84**	44.93	5.67	**34.15**	42.61	46.77
Royalties	-	(0.08)	**(0.46)**	-	(0.08)	**(0.50)**	(0.26)	(1.12)
Operating	-	(1.49)	**(8.90)**	-	(1.19)	**(7.05)**	(7.17)	(8.24)
Operating netback	63.18	5.21	**31.48**	44.93	4.40	**26.60**	35.18	37.41
General and administration			**(0.26)**			**(0.52)**	(0.93)	(1.51)
Current income taxes			**0.16**			**(2.25)**	(3.35)	(4.40)
Fund flows from operations netback			**31.38**			**23.83**	30.90	31.50
Germany								
Sales	-	6.09	**36.54**	-	5.33	**31.97**	39.68	43.10
Royalties	-	(0.01)	**(0.06)**	-	(0.38)	**(2.30)**	(4.70)	(6.75)
Transportation	-	(0.28)	**(1.65)**	-	(0.53)	**(3.16)**	(2.05)	(3.41)
Operating	-	(2.91)	**(17.44)**	-	(2.27)	**(13.62)**	(19.31)	(11.41)
Operating netback	-	2.89	**17.39**	-	2.15	**12.89**	13.62	21.53
General and administration			**(7.73)**			**(9.15)**	(12.22)	(7.69)
Fund flows from operations netback			**9.66**			**3.74**	1.40	13.84
Ireland								
Sales	-	7.38	**44.29**	-	5.86	**35.16**	-	-
Transportation	-	(0.29)	**(1.77)**	-	(0.35)	**(2.09)**	-	-
Operating	-	(0.89)	**(5.34)**	-	(1.00)	**(6.01)**	-	-
Operating netback	-	6.20	**37.18**	-	4.51	**27.06**	-	-
General and administration			**(1.58)**			**(1.54)**	-	-
Fund flows from operations netback			**35.60**			**25.52**	-	-
Australia								
Sales	69.05	-	**69.05**	60.33	-	**60.33**	58.74	70.22
Operating	(26.83)	-	**(26.83)**	(20.95)	-	**(20.95)**	(17.08)	(22.29)
PRRT [1]	(2.82)	-	**(2.82)**	(0.69)	-	**(0.69)**	(1.29)	(2.97)
Operating netback	39.40	-	**39.40**	38.69	-	**38.69**	40.37	44.96
General and administration			**(3.60)**			**(2.82)**	(2.17)	(2.48)
Corporate income taxes			**(4.87)**			**(3.32)**	1.47	(3.12)
Fund flows from operations netback			**30.93**			**32.55**	39.67	39.36

	Three Months Ended December 31, 2016			Year Ended December 31, 2016			Three Months Ended Dec 31, 2015	Year Ended Dec 31, 2015
	Crude Oil, Condensate & NGLs $/bbl	Natural Gas $/mcf	Total $/boe	Crude Oil, Condensate & NGLs $/bbl	Natural Gas $/mcf	Total $/boe	Total $/bbl	Total $/boe
United States								
Sales	56.77	1.93	**53.58**	46.89	0.85	**43.70**	41.94	47.53
Royalties	(16.49)	(1.72)	**(16.05)**	(13.71)	(0.62)	**(12.95)**	(12.40)	(13.93)
Operating	(8.51)	-	**(7.91)**	(8.50)	-	**(7.85)**	(6.11)	(8.23)
Operating netback	31.77	0.21	**29.62**	24.68	0.23	**22.90**	23.43	25.37
General and administration			**(23.02)**			**(21.65)**	(20.18)	(42.51)
Fund flows from operations netback			**6.60**			**1.25**	3.25	(17.14)
Total Company								
Sales	60.58	5.47	**45.93**	51.73	4.18	**37.88**	41.04	47.07
Realized hedging gain	0.45	0.04	**0.34**	1.45	0.68	**2.81**	3.71	2.07
Royalties	(4.92)	(0.10)	**(2.65)**	(4.28)	(0.09)	**(2.33)**	(2.85)	(3.30)
Transportation	(2.33)	(0.19)	**(1.69)**	(2.22)	(0.20)	**(1.70)**	(1.78)	(2.09)
Operating	(13.33)	(1.34)	**(10.54)**	(11.88)	(1.23)	**(9.53)**	(11.50)	(11.32)
PRRT [1]	(0.59)	-	**(0.28)**	(0.14)	-	**(0.07)**	(0.18)	(0.34)
Operating netback	39.86	3.88	**31.11**	34.66	3.34	**27.06**	28.44	32.09
General and administration			**(2.03)**			**(2.27)**	(2.18)	(2.68)
Interest expense			**(2.55)**			**(2.44)**	(2.90)	(3.00)
Realized foreign exchange gain (loss)			**0.23**			**0.17**	(0.04)	0.03
Other income			**0.70**			**0.17**	0.04	1.64
Corporate income taxes [1]			**(1.03)**			**(0.78)**	0.55	(2.22)
Fund flows from operations netback			**26.43**			**21.91**	23.91	25.86

(1) Vermilion considers Australian PRRT to be an operating item and, accordingly, has included PRRT in the calculation of operating netbacks. Current income taxes presented above excludes PRRT.

Supplemental Table 2: Hedges

The prices in these tables may represent the weighted averages for several contracts. The weighted average price for the portfolio of options listed below may not have the same payoff profile as the individual contracts. As such, the presentation of the weighted average prices is purely for indicative purposes.

The following tables outline Vermilion's outstanding risk management positions as at December 31, 2016:

Crude Oil	Period	Exercise date[(1)]	Currency	Bought Put Volume (bbl/d)	Weighted Average Bought Put Price / bbl	Sold Call Volume (bbl/d)	Weighted Average Sold Call Price / bbl	Sold Put Volume (bbl/d)	Weighted Average Sold Put Price / bbl	Swap Volume (bbl/d)	Weighted Average Swap Price / bbl	Additional Swap Volume (mmbtu/d) [(2)]
Dated Brent												
3-Way Collar	Oct 2016 - Mar 2017		USD	500	50.00	500	60.00	500	42.50	-	-	-
3-Way Collar	Jan 2017 - Dec 2017		USD	2,500	51.00	2,500	60.50	2,500	41.50	-	-	-
3-Way Collar	Jul 2017 - Jun 2018		USD	2,000	55.00	2,000	64.06	2,000	45.00	-	-	-
Swap	Jan 2017 - Dec 2017		USD	-	-	-	-	-	-	1,250	55.50	-
Swaption	Jul 2017 - Jun 2018	Mar 31, 2017	USD	-	-	-	-	-	-	500	60.00	-
Swaption	Jul 2017 - Jun 2018	Jun 30, 2017	USD	-	-	-	-	-	-	1,000	60.00	-
WTI												
3-Way Collar	Jan 2017 - Dec 2017		CAD	1,500	70.00	1,500	75.00	1,500	55.00	-	-	-
3-Way Collar	Jan 2017 - Mar 2017		USD	2,500	50.00	2,500	55.00	2,500	42.50	-	-	-
3-Way Collar	Jul 2017 - Dec 2017		USD	1,500	53.67	1,500	63.00	1,500	45.00	-	-	-
Swap	Jan 2017 - Mar 2017		USD	-	-	-	-	-	-	2,500	53.10	-

North American Gas	Period	Exercise date[(1)]	Currency	Bought Put Volume (mmbtu/d)	Weighted Average Bought Put Price / mmbtu	Sold Call Volume (mmbtu/d)	Weighted Average Sold Call Price / mmbtu	Sold Put Volume (mmbtu/d)	Weighted Average Sold Put Price / mmbtu	Swap Volume (mmbtu/d)	Weighted Average Swap Price / mmbtu	Additional Swap Volume (mmbtu/d) [(2)]
AECO												
Collar	Nov 2016 - Oct 2017		CAD	7,109	2.18	9,478	2.86	-	-	-	-	-
Collar	Nov 2016 - Dec 2017		CAD	9,478	2.33	9,478	3.02	-	-	-	-	-
Collar	Jan 2017 - Dec 2017		CAD	4,739	2.37	4,739	3.25	-	-	-	-	-
Swap	Nov 2016 - Dec 2017		CAD	-	-	-	-	-	-	2,370	2.99	-
Swap	Jan 2017 - Mar 2017		CAD	-	-	-	-	-	-	7,109	3.35	-
Swap	Jan 2017 - Dec 2017		CAD	-	-	-	-	-	-	7,109	2.94	-
Swap	Apr 2017 - Oct 2017		CAD	-	-	-	-	-	-	7,109	3.01	-
Swap	Nov 2017 - Dec 2017		CAD	-	-	-	-	-	-	7,109	3.35	-
AECO Basis												
Swap	Jan 2017 - Dec 2017		USD	-	-	-	-	-	-	5,000	(0.75)	-
Swap	Jan 2018 - Dec 2018		USD	-	-	-	-	-	-	10,000	(0.83)	-
NYMEX												
Swap	Jan 2017 - Dec 2017		USD	-	-	-	-	-	-	5,000	3.00	-

European Gas	Period	Exercise date[(1)]	Currency	Bought Put Volume (mmbtu/d)	Weighted Average Bought Put Price / mmbtu	Sold Call Volume (mmbtu/d)	Weighted Average Sold Call Price / mmbtu	Sold Put Volume (mmbtu/d)	Weighted Average Sold Put Price / mmbtu	Swap Volume (mmbtu/d)	Weighted Average Swap price / mmbtu	Additional Swap Volume (mmbtu/d) [(2)]
NBP												
Collar	Apr 2016 - Mar 2017		GBP	2,500	4.00	2,500	4.77	-	-	-	-	-
Collar	Oct 2016 - Mar 2017		GBP	2,500	3.30	5,000	3.72	-	-	-	-	-
Collar	Oct 2016 - Sep 2017		GBP	5,000	3.25	10,000	4.03	-	-	-	-	-
Collar	Oct 2016 - Dec 2017		GBP	5,000	3.25	10,000	4.07	-	-	-	-	-
Collar	Jan 2017 - Dec 2017		GBP	5,000	3.30	7,500	3.77	-	-	-	-	-
Collar	Jan 2018 - Dec 2018		GBP	2,500	3.15	2,500	3.82	-	-	-	-	-
Put	Dec 2016 - Feb 2017		GBP	20,000	4.00	-	-	-	-	-	-	-
Call	Oct 2016 - Mar 2017		GBP	-	-	2,500	4.90	-	-	-	-	-
Swap	Jan 2017 - Dec 2017		GBP	-	-	-	-	-	-	2,500	4.22	2,500
Swap	Apr 2017 - Mar 2018		GBP	-	-	-	-	-	-	5,300	4.20	-
Swap	Jul 2017 - Dec 2017		GBP	-	-	-	-	-	-	2,500	3.95	-
Swap	Jan 2018 - Dec 2018		GBP	-	-	-	-	-	-	2,500	4.04	5,000
Swap	Jul 2016 - Mar 2017		EUR	-	-	-	-	-	-	2,457	5.73	-

(1) The sold swaption instrument allows the counterparty, at the specified date, to enter into a swap with Vermilion at the above detailed terms.

(2) On the last business day of each month, the counterparty has the option to increase the contracted volumes for the following month.

European Gas	Period	Exercise date[1]	Currency	Bought Put Volume (mmbtu/d)	Weighted Average Bought Put Price / mmbtu	Sold Call Volume (mmbtu/d)	Weighted Average Sold Call Price / mmbtu	Sold Put Volume (mmbtu/d)	Weighted Average Sold Put Price / mmbtu	Swap Volume (mmbtu/d)	Weighted Average Swap price / mmbtu	Additional Swap Volume (mmbtu/d) [2]
TTF												
3-Way Collar	Apr 2017 - Sep 2017		EUR	9,827	4.18	9,827	5.06	9,827	3.08	-	-	-
3-Way Collar	Oct 2017 - Dec 2019		EUR	7,370	4.59	7,370	5.42	7,370	2.93	-	-	-
3-Way Collar	Jan 2018 - Dec 2018		EUR	9,827	4.67	9,827	5.42	9,827	3.22	-	-	-
3-Way Collar	Jan 2018 - Dec 2019		EUR	3,685	4.74	3,685	5.52	3,685	3.13	-	-	-
Collar	Apr 2016 - Mar 2017		EUR	4,913	5.57	9,827	6.70	-	-	-	-	-
Collar	Jul 2016 - Mar 2017		EUR	2,457	5.35	4,913	6.92	-	-	-	-	-
Collar	Jul 2016 - Mar 2018		EUR	2,457	5.61	4,913	6.90	-	-	-	-	-
Collar	Oct 2016 - Dec 2017		EUR	2,457	5.28	2,457	6.21	-	-	-	-	-
Collar	Jan 2017 - Dec 2017		EUR	9,827	5.06	22,111	6.37	-	-	-	-	-
Collar	Apr 2017 - Sept 2017		EUR	2,457	3.81	4,913	4.47	-	-	-	-	-
Collar	Jan 2018 - Dec 2018		EUR	4,913	4.40	4,913	5.31	-	-	-	-	-
Call	Oct 2016 - Mar 2017		EUR	-	-	2,457	6.36	-	-	-	-	-
Swap	Jul 2016 - Jun 2018		EUR	-	-	-	-	-	-	2,559	5.89	-
Swap	Jan 2017 - Dec 2017		EUR	-	-	-	-	-	-	2,457	5.32	2,457
Swap	Oct 2017 - Dec 2018		EUR	-	-	-	-	-	-	17,197	4.80	-
Swap	Oct 2017 - Dec 2019		EUR	-	-	-	-	-	-	7,370	4.87	-
Swap	Jan 2018 - Dec 2019		EUR	-	-	-	-	-	-	1,228	5.00	-
Swap	Jan 2019 - Dec 2019		EUR	-	-	-	-	-	-	2,457	4.92	-
Put Spread	Apr 2017 - Sep 2017		EUR	14,740	4.40	-	-	14,740	3.15	-	-	-
Swaption	Apr 2017 - Jun 2018	Mar 31, 2017	EUR	-	-	-	-	-	-	4,913	4.55	-

Fuel and Electricity	Period	Currency	Swap Volume (unit/d)	Weighted Average Swap price / unit
AESO (mwh)				
Swap	Jan 2017 - Dec 2017	CAD	65	33.47

Interest Rate	Period	Currency	Notional amount	Rate (%)
CDOR Swap	Sep 2015 - Sep 2019	CAD	100,000,000	1.00
CDOR Swap	Oct 2015 - Oct 2019	CAD	100,000,000	1.10

Cross Currency Interest Rate	Period	Receive Notional amount (USD)	Rate (US%)	Pay Notional amount (CAD)	Rate (CAD%)
Swap	Jan 2017 - Feb 2017	891,088,800	3.52	1,195,800,000	3.17

(1) The sold swaption instrument allows the counterparty, at the specified date, to enter into a swap with Vermilion at the above detailed terms.

(2) On the last business day of each month, the counterparty has the option to increase the contracted volumes for the following month.

(3) In January 2017, Vermilion repaid $1.2 billion of borrowings on the revolving credit facility bearing interest at CDOR plus applicable margins and simultaneously borrowed US $0.9 billion on the revolving credit facility bearing interest at LIBOR plus applicable margins.

Supplemental Table 3: Capital Expenditures and Acquisitions

By classification ($M)	Three Months Ended Dec 31, 2016	Sep 30, 2016	Dec 31, 2015	Year Ended Dec 31, 2016	Dec 31, 2015
Drilling and development	**66,437**	41,039	128,996	**241,545**	486,861
Exploration and evaluation	**445**	-	-	**863**	-
Capital expenditures	**66,882**	41,039	128,996	**242,408**	486,861
Property acquisition	**78,713**	10,391	6,227	**98,524**	28,897
Acquisitions	**78,713**	10,391	6,227	**98,524**	28,897

By category ($M)	Three Months Ended Dec 31, 2016	Sep 30, 2016	Dec 31, 2015	Year Ended Dec 31, 2016	Dec 31, 2015
Land	**59**	(36)	819	**1,555**	3,793
Seismic	**1,757**	1,110	4,217	**10,458**	8,243
Drilling and completion	**38,233**	18,694	58,327	**121,322**	212,358
Production equipment and facilities	**26,768**	18,046	55,662	**86,664**	218,963
Recompletions	**3,293**	603	6,338	**8,262**	26,689
Other	**(3,228)**	2,622	3,633	**14,147**	16,815
Capital expenditures	**66,882**	41,039	128,996	**242,408**	486,861
Acquisitions	**78,713**	10,391	6,227	**98,524**	28,897
Total capital expenditures and acquisitions	**145,595**	51,430	135,223	**340,932**	515,758

By country ($M)	Three Months Ended Dec 31, 2016	Sep 30, 2016	Dec 31, 2015	Year Ended Dec 31, 2016	Dec 31, 2015
Canada	**18,273**	20,801	33,723	**76,015**	216,158
France	**31,127**	11,110	24,164	**68,472**	92,582
Netherlands	**33,996**	6,441	18,810	**51,999**	47,325
Germany	**50,071**	978	(441)	**52,180**	5,363
Ireland	**1,711**	2,416	12,493	**9,375**	66,409
Australia	**5,236**	6,908	40,852	**59,910**	61,741
United States	**4,414**	2,776	5,622	**19,474**	25,014
Corporate	**767**	-	-	**3,507**	1,166
Total capital expenditures and acquisitions	**145,595**	51,430	135,223	**340,932**	515,758

Supplemental Table 4: Production

	Q4/16	Q3/16	Q2/16	Q1/16	Q4/15	Q3/15	Q2/15	Q1/15	Q4/14	Q3/14	Q2/14	Q1/14
Canada												
Crude oil & condensate (bbls/d)	**7,945**	8,984	9,453	10,317	10,413	11,030	11,843	12,163	12,681	12,755	14,108	10,390
NGLs (bbls/d)	**2,444**	2,448	2,687	2,633	2,710	2,678	2,094	1,706	1,444	1,005	1,364	1,118
Natural gas (mmcf/d)	**75.12**	77.62	87.44	97.16	87.90	71.94	64.66	61.78	58.36	57.07	57.59	49.53
Total (boe/d)	**22,910**	24,368	26,713	29,141	27,773	25,698	24,713	24,165	23,851	23,272	25,070	19,763
% of consolidated	**38%**	37%	42%	44%	45%	47%	48%	48%	49%	47%	49%	42%
France												
Crude oil (bbls/d)	**11,220**	11,827	12,326	12,220	12,537	12,310	12,746	11,463	11,133	11,111	11,025	10,771
Natural gas (mmcf/d)	**0.38**	0.42	0.54	0.44	1.36	1.47	1.03	-	-	-	-	-
Total (boe/d)	**11,283**	11,897	12,416	12,293	12,763	12,555	12,917	11,463	11,133	11,111	11,025	10,771
% of consolidated	**19%**	19%	19%	19%	21%	22%	25%	23%	22%	22%	21%	23%
Netherlands												
Condensate (bbls/d)	**57**	86	96	114	110	109	112	63	81	63	96	69
Natural gas (mmcf/d)	**41.15**	47.62	49.18	53.40	56.34	53.56	32.43	36.41	31.35	38.07	40.35	43.15
Total (boe/d)	**6,915**	8,023	8,293	9,015	9,500	9,035	5,517	6,132	5,306	6,407	6,822	7,260
% of consolidated	**11%**	13%	13%	14%	16%	16%	11%	12%	11%	13%	13%	16%
Germany												
Natural gas (mmcf/d)	**14.80**	14.52	14.31	15.96	16.17	14.00	16.18	16.80	17.71	15.38	16.13	10.64
Total (boe/d)	**2,467**	2,420	2,385	2,660	2,695	2,333	2,696	2,801	2,952	2,563	2,689	1,773
% of consolidated	**4%**	4%	4%	4%	4%	4%	5%	6%	6%	5%	5%	4%
Ireland												
Natural gas (mmcf/d)	**62.92**	59.28	47.26	33.90	0.12	-	-	-	-	-	-	-
Total (boe/d)	**10,486**	9,879	7,877	5,650	20	-	-	-	-	-	-	-
% of consolidated	**17%**	16%	12%	9%	-	-	-	-	-	-	-	-
Australia												
Crude oil (bbls/d)	**6,388**	6,562	6,083	6,180	7,824	6,433	5,865	5,672	6,134	6,567	6,483	7,110
% of consolidated	**10%**	10%	9%	9%	13%	11%	11%	11%	12%	13%	12%	15%
United States												
Crude oil (bbls/d)	**362**	383	458	368	420	226	123	153	195	-	-	-
NGLs (bbls/d)	**23**	30	26	39	29	-	-	-	-	-	-	-
Natural gas (mmcf/d)	**0.18**	0.20	0.20	0.26	0.20	-	-	-	-	-	-	-
Total (boe/d)	**414**	447	518	450	483	226	123	153	195	-	-	-
% of consolidated	**1%**	1%	1%	1%	1%	-	-	-	-	-	-	-
Consolidated												
Crude oil, condensate & NGLs (bbls/d)	**28,439**	30,320	31,129	31,871	34,043	32,786	32,783	31,220	31,668	31,501	33,076	29,458
% of consolidated	**47%**	48%	48%	49%	56%	58%	63%	62%	64%	63%	63%	63%
Natural gas (mmcf/d)	**194.54**	199.65	198.93	201.11	162.09	140.97	114.29	115.00	107.42	110.52	114.08	103.32
% of consolidated	**53%**	52%	52%	51%	44%	42%	37%	38%	36%	37%	37%	37%
Total (boe/d)	**60,863**	63,596	64,285	65,389	61,058	56,280	51,831	50,386	49,571	49,920	52,089	46,677

	2016	2015	2014	2013	2012	2011
Canada						
Crude oil & condensate (bbls/d)	**9,171**	11,357	12,491	8,387	7,659	4,701
NGLs (bbls/d)	**2,552**	2,301	1,233	1,666	1,232	1,297
Natural gas (mmcf/d)	**84.29**	71.65	55.67	42.39	37.50	43.38
Total (boe/d)	**25,771**	25,598	23,001	17,117	15,142	13,227
% of consolidated	**40%**	46%	47%	41%	40%	38%
France						
Crude oil (bbls/d)	**11,896**	12,267	11,011	10,873	9,952	8,110
Natural gas (mmcf/d)	**0.44**	0.97	-	3.40	3.59	0.95
Total (boe/d)	**11,970**	12,429	11,011	11,440	10,550	8,269
% of consolidated	**19%**	23%	22%	28%	28%	23%
Netherlands						
Condensate (bbls/d)	**88**	99	77	64	67	58
Natural gas (mmcf/d)	**47.82**	44.76	38.20	35.42	34.11	32.88
Total (boe/d)	**8,058**	7,559	6,443	5,967	5,751	5,538
% of consolidated	**13%**	14%	13%	15%	15%	16%
Germany						
Natural gas (mmcf/d)	**14.90**	15.78	14.99	-	-	-
Total (boe/d)	**2,483**	2,630	2,498	-	-	-
% of consolidated	**4%**	5%	5%	-	-	-
Ireland						
Natural gas (mmcf/d)	**50.89**	0.03	-	-	-	-
Total (boe/d)	**8,482**	5	-	-	-	-
% of consolidated	**13%**	-	-	-	-	-
Australia						
Crude oil (bbls/d)	**6,304**	6,454	6,571	6,481	6,360	8,168
% of consolidated	**10%**	12%	13%	16%	17%	23%
United States						
Crude oil (bbls/d)	**393**	231	49	-	-	-
NGLs (bbls/d)	**29**	7	-	-	-	-
Natural gas (mmcf/d)	**0.21**	0.05	-	-	-	-
Total (boe/d)	**457**	247	49	-	-	-
% of consolidated	**1%**	-	-	-	-	-
Consolidated						
Crude oil, condensate & NGLs (bbls/d)	**30,433**	32,716	31,432	27,471	25,270	22,334
% of consolidated	**48%**	60%	63%	67%	67%	63%
Natural gas (mmcf/d)	**198.55**	133.24	108.85	81.21	75.20	77.21
% of consolidated	**52%**	40%	37%	33%	33%	37%
Total (boe/d)	**63,526**	54,922	49,573	41,005	37,803	35,202

Supplemental Table 5: Segmented Financial Results

	Three Months Ended December 31, 2016								
($M)	Canada	France	Netherlands	Germany	Ireland	Australia	United States	Corporate	Total
Drilling and development	16,895	31,127	5,737	1,694	1,711	5,236	4,037	-	66,437
Exploration and evaluation	-	-	-	-	-	-	-	445	445
Oil and gas sales to external customers	70,573	71,926	25,978	8,294	42,727	38,352	2,041	-	259,891
Royalties	(7,390)	(6,692)	(294)	(12)	-	-	(611)	-	(14,999)
Revenue from external customers	63,183	65,234	25,684	8,282	42,727	38,352	1,430	-	244,892
Transportation	(3,504)	(3,983)	-	(375)	(1,703)	-	-	-	(9,565)
Operating	(18,161)	(11,482)	(5,660)	(3,959)	(5,148)	(14,905)	(301)	-	(59,616)
General and administration	(2,035)	(5,101)	(162)	(1,755)	(1,523)	(1,998)	(877)	1,987	(11,464)
PRRT	-	-	-	-	-	(1,568)	-	-	(1,568)
Corporate income taxes	-	(2,867)	100	-	-	(2,703)	-	(370)	(5,840)
Interest expense	-	-	-	-	-	-	-	(14,410)	(14,410)
Realized gain on derivative instruments	-	-	-	-	-	-	-	1,920	1,920
Realized foreign exchange gain	-	-	-	-	-	-	-	1,291	1,291
Realized other income	-	3,822	-	-	-	-	-	120	3,942
Fund flows from operations	39,483	45,623	19,962	2,193	34,353	17,178	252	(9,462)	149,582

	Year Ended December 31, 2016								
($M)	Canada	France	Netherlands	Germany	Ireland	Australia	United States	Corporate	Total
Total assets	1,522,243	835,141	220,350	292,885	756,893	267,183	61,195	131,294	4,087,184
Drilling and development	62,706	68,472	23,740	3,803	9,375	59,910	13,539	-	241,545
Exploration and evaluation	-	-	-	-	-	-	-	863	863
Oil and gas sales to external customers	252,867	246,863	100,707	29,049	109,156	136,835	7,314	-	882,791
Royalties	(21,475)	(27,091)	(1,462)	(2,089)	-	-	(2,167)	-	(54,284)
Revenue from external customers	231,392	219,772	99,245	26,960	109,156	136,835	5,147	-	828,507
Transportation	(15,392)	(14,758)	-	(2,869)	(6,492)	-	-	-	(39,511)
Operating	(71,543)	(50,000)	(20,796)	(12,379)	(18,646)	(47,507)	(1,314)	-	(222,185)
General and administration	(11,826)	(19,101)	(1,525)	(8,314)	(4,772)	(6,400)	(3,624)	2,733	(52,829)
PRRT	-	-	-	-	-	(1,568)	-	-	(1,568)
Corporate income taxes	-	(2,867)	(6,624)	-	-	(7,522)	-	(1,097)	(18,110)
Interest expense	-	-	-	-	-	-	-	(56,957)	(56,957)
Realized gain on derivative instruments	-	-	-	-	-	-	-	65,376	65,376
Realized foreign exchange gain	-	-	-	-	-	-	-	4,041	4,041
Realized other income	-	3,822	-	-	-	-	-	205	4,027
Fund flows from operations	132,631	136,868	70,300	3,398	79,246	73,838	209	14,301	510,791

NON-GAAP FINANCIAL MEASURES

This MD&A includes references to certain financial measures which do not have standardized meanings and may not be comparable to similar measures presented by other issuers. These financial measures include fund flows from operations, a measure of profit or loss in accordance with IFRS 8 "Operating Segments" (please see SEGMENTED INFORMATION in the NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS) and net debt, a measure of capital in accordance with IAS 1 "Presentation of Financial Statements" (please see CAPITAL DISCLOSURES in the NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS).

In addition, this MD&A includes financial measures which are not specified, defined, or determined under IFRS and are therefore considered non-GAAP financial measures and may not be comparable to similar measures presented by other issuers. These non-GAAP financial measures include:

Capital expenditures: The sum of drilling and development and exploration and evaluation from the Consolidated Statement of Cash Flows. We consider capital expenditures to be a useful measure of our investment in our existing asset base. Capital expenditures are also referred to as E&D capital.

Cash dividends per share: Represents cash dividends declared per share and is a useful measure of the dividends a common shareholder was entitled to during the period.

Covenants: The financial covenants on our revolving credit facility contain non-GAAP measures. The definitions for these financial covenants are included in FINANCIAL POSITION REVIEW.

Diluted shares outstanding: The sum of shares outstanding at the period end plus outstanding awards under the VIP, based on current estimates of future performance factors and forfeiture rates.

Free cash flow: Represents fund flows from operations in excess of capital expenditures. We consider free cash flow to be a key measure as it is used to determine the funding available for investing and financing activities, including payment of dividends, repayment of long-term debt, reallocation to existing business units, and deployment into new ventures.

Fund flows from operations per basic and diluted share: Management assesses fund flows from operations on a per share basis as we believe this provides a measure of our operating performance after taking into account the issuance and potential future issuance of Vermilion common shares. Fund flows from operations per basic share is calculated by dividing fund flows from operations by the basic weighted average shares outstanding as defined under IFRS. Fund flows from operations per diluted share is calculated by dividing fund flows from operations by the sum of basic weighted average shares outstanding and incremental shares issuable under the VIP as determined using the treasury stock method.

Net dividends: We define net dividends as dividends declared less proceeds received for the issuance of shares pursuant to the dividend reinvestment and Premium Dividend™ plans. Management monitors net dividends and net dividends as a percentage of fund flows from operations to assess our ability to pay dividends.

Operating netback: Sales less royalties, operating expense, transportation costs, PRRT, and realized hedging gains and losses presented on a per unit basis. Management assesses operating netback as a measure of the profitability and efficiency of our field operations. In contrast, fund flows from operations netback also includes general and administration expense, corporate income taxes and interest. Fund flows from operations netback is used by management to assess the profitability of our business units and Vermilion as a whole.

Payout: We define payout as net dividends plus drilling and development costs, exploration and evaluation costs, dispositions, and asset retirement obligations settled. Management uses payout to assess the amount of cash distributed back to shareholders and re-invested in the business for maintaining production and organic growth.

The following tables reconcile net dividends, payout, and diluted shares outstanding from their most directly comparable GAAP measures as presented in our financial statements:

	Three Months Ended			Year Ended	
($M)	Dec 31, 2016	Sep 30, 2016	Dec 31, 2015	Dec 31, 2016	Dec 31, 2015
Dividends declared	**76,096**	75,465	71,965	**299,070**	283,575
Shares issued for the DRIP[(1)]	**(43,580)**	(50,912)	(46,764)	**(192,998)**	(155,033)
Net dividends	**32,516**	24,553	25,201	**106,072**	128,542
Drilling and development	**66,437**	41,039	128,996	**241,545**	486,861
Exploration and evaluation	**445**	-	-	**863**	-
Asset retirement obligations settled	**3,327**	2,066	4,921	**9,617**	11,369
Payout	**102,725**	67,658	159,118	**358,097**	626,772

(1) DRIP Refers to Vermilion's dividend reinvestment and Premium Dividend™ plans.

	As at		
('000s of shares)	Dec 31, 2016	Sep 30, 2016	Dec 31, 2015
Shares outstanding	**118,263**	117,386	111,991
Potential shares issuable pursuant to the VIP	**3,090**	2,797	3,033
Diluted shares outstanding	**121,353**	120,183	115,024

MANAGEMENT'S REPORT TO SHAREHOLDERS

Management's Responsibility for Financial Statements

The accompanying consolidated financial statements of Vermilion Energy Inc. are the responsibility of management and have been approved by the Board of Directors of Vermilion Energy Inc. The consolidated financial statements have been prepared in accordance with the accounting policies detailed in the notes to the consolidated financial statements and are prepared in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board. Where necessary, management has made informed judgments and estimates of transactions that were not yet completed at the balance sheet date. Financial information throughout the Annual Report is consistent with the consolidated financial statements.

Management ensures the integrity of the consolidated financial statements by maintaining high-quality systems of internal control. Procedures and policies are designed to provide reasonable assurance that assets are safeguarded and transactions are properly recorded, and that the financial records are reliable for preparation of the consolidated financial statements. Deloitte LLP, Vermilion's Independent Registered Public Accounting Firm, have conducted an audit of the consolidated financial statements in accordance with Canadian generally accepted auditing standards and the standards of the Public Company Accounting Oversight Board (United States) and have provided their report.

The Board of Directors is responsible for ensuring that management fulfills its responsibility for financial reporting and internal control. The Board carries out this responsibility principally through the Audit Committee, which is appointed by the Board and is comprised entirely of independent Directors. The Committee meets periodically with management and Deloitte LLP to satisfy itself that each party is properly discharging its responsibilities and to review the consolidated financial statements, the Management's Discussion and Analysis and the Report of the Independent Registered Public Accounting Firm before they are presented to the Board of Directors.

Management's Report on Internal Control Over Financial Reporting

Management is responsible for establishing and maintaining an adequate system of internal control over financial reporting. Management conducted an evaluation of the effectiveness of the system of internal control over financial reporting based on the criteria established in "Internal Control – Integrated Framework (2013)" issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, management has assessed the effectiveness of Vermilion's internal control over financial reporting as defined in Rule 13a-15 under the US Securities Exchange Act of 1934 and as defined in Canada by National Instrument 52-109, Certification of Disclosure in Issuers' Annual and Interim Filings. Management concluded that Vermilion's internal control over financial reporting was effective as of December 31, 2016. The effectiveness of Vermilion's internal control over financial reporting as of December 31, 2016 has been audited by Deloitte LLP, the Company's Independent Registered Public Accounting Firm, who also audited the Company's consolidated financial statements for the year ended December 31, 2016.

("Anthony Marino")

Anthony Marino
President & Chief Executive Officer
February 24, 2017

("Curtis W. Hicks")

Curtis W. Hicks
Executive Vice President & Chief Financial Officer

Report of Independent Registered Public Accounting Firm

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

We have audited the internal control over financial reporting of Vermilion Energy Inc. and subsidiaries (the "Company") as of December 31, 2016, based on the criteria established in *Internal Control—Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on the criteria established in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with Canadian generally accepted auditing standards and the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements as of and for the year ended December 31, 2016 of the Company and our report dated February 24, 2017 expressed an unmodified/unqualified opinion on those financial statements.

("/s/ Deloitte LLP")

Chartered Professional Accountants
February 24, 2017
Calgary, Canada

Report of Independent Registered Public Accounting Firm

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

We have audited the accompanying consolidated financial statements of Vermilion Energy Inc. and subsidiaries (the "Company"), which comprise the consolidated balance sheet as at December 31, 2016 and December 31, 2015, and the consolidated statements of net loss and comprehensive loss, cash flows, and changes in shareholders' equity for the years then ended, and 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 as issued by the International Accounting Standards Board, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Vermilion Energy Inc. and subsidiaries as at December 31, 2016 and December 31, 2015, and their financial performance and their cash flows for the years then ended in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board.

Other Matter

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of December 31, 2016, based on the criteria established in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 24, 2017 expressed an unqualified opinion on the Company's internal control over financial reporting.

("/s/ Deloitte LLP")

Chartered Professional Accountants
February 24, 2017
Calgary, Canada

CONSOLIDATED BALANCE SHEET
(THOUSANDS OF CANADIAN DOLLARS)

	Note	December 31, 2016	December 31, 2015
ASSETS			
Current			
Cash and cash equivalents	20	**62,775**	41,676
Accounts receivable		**131,719**	160,499
Crude oil inventory		**14,528**	13,079
Derivative instruments	9	**4,336**	55,214
Prepaid expenses		**12,548**	14,310
		225,906	284,778
Derivative instruments	9	**1,157**	13,128
Deferred taxes	11	**152,046**	135,753
Exploration and evaluation assets	7	**274,830**	308,192
Capital assets	6	**3,433,245**	3,467,369
		4,087,184	4,209,220
LIABILITIES			
Current			
Accounts payable and accrued liabilities		**181,557**	248,747
Current portion of long-term debt	12	**-**	224,901
Dividends payable	13	**25,426**	24,077
Derivative instruments	9	**47,660**	-
Income taxes payable		**36,219**	6,006
		290,862	503,731
Derivative instruments	9	**27,484**	-
Long-term debt	12	**1,362,192**	1,162,998
Finance lease obligation	10	**19,628**	23,565
Asset retirement obligations	8	**525,022**	305,613
Deferred taxes	11	**283,533**	354,654
		2,508,721	2,350,561
SHAREHOLDERS' EQUITY			
Shareholders' capital	13	**2,452,722**	2,181,089
Contributed surplus		**101,788**	107,946
Accumulated other comprehensive income		**30,339**	113,647
Deficit		**(1,006,386)**	(544,023)
		1,578,463	1,858,659
		4,087,184	4,209,220

APPROVED BY THE BOARD

(Signed "Catherine L. Williams")

Catherine L. Williams, Director

(Signed "Anthony Marino")

Anthony Marino, Director

CONSOLIDATED STATEMENTS OF NET LOSS AND COMPREHENSIVE LOSS (THOUSANDS OF CANADIAN DOLLARS, EXCEPT SHARE AND PER SHARE AMOUNTS)

	Note	Year Ended December 31, 2016	Year Ended December 31, 2015
REVENUE			
Petroleum and natural gas sales		**882,791**	939,586
Royalties		**(54,284)**	(65,920)
Petroleum and natural gas revenue		**828,507**	873,666
EXPENSES			
Operating	20	**222,185**	225,938
Transportation		**39,511**	41,660
Equity based compensation	15	**69,235**	75,232
Loss (gain) on derivative instruments	9	**72,617**	(84,904)
Interest expense		**56,957**	59,852
General and administration	20	**52,829**	53,584
Foreign exchange gain		**(3,249)**	(9,410)
Other income	16	**(3,896)**	(31,663)
Accretion	8	**24,783**	23,911
Depletion and depreciation	6, 7	**528,002**	458,758
Impairment	6, 7	**14,762**	274,623
Gain on business combination	5	**(22,001)**	-
		1,051,735	1,087,581
LOSS BEFORE INCOME TAXES		**(223,228)**	(213,915)
TAXES	11		
Deferred		**(82,855)**	(47,728)
Current		**19,678**	51,115
		(63,177)	3,387
NET LOSS		**(160,051)**	(217,302)
OTHER COMPREHENSIVE (LOSS) INCOME			
Currency translation adjustments		**(83,308)**	107,925
COMPREHENSIVE LOSS		**(243,359)**	(109,377)
NET LOSS PER SHARE	17		
Basic		**(1.38)**	(1.98)
Diluted		**(1.38)**	(1.98)
WEIGHTED AVERAGE SHARES OUTSTANDING ('000s)	17		
Basic		**115,695**	109,642
Diluted		**115,695**	109,642

CONSOLIDATED STATEMENTS OF CASH FLOWS
(THOUSANDS OF CANADIAN DOLLARS)

	Note	Year Ended December 31, 2016	Year Ended December 31, 2015
OPERATING			
Net loss		**(160,051)**	(217,302)
Adjustments:			
Accretion	8	**24,783**	23,911
Depletion and depreciation	6, 7	**528,002**	458,758
Impairment	6, 7	**14,762**	274,623
Gain on business combination	5	**(22,001)**	-
Unrealized loss (gain) on derivative instruments	9	**137,993**	(43,548)
Equity based compensation	15	**69,235**	75,232
Unrealized foreign exchange loss (gain)		**792**	(8,787)
Unrealized other expense		**131**	1,008
Deferred taxes	11	**(82,855)**	(47,728)
Asset retirement obligations settled	8	**(9,617)**	(11,369)
Changes in non-cash operating working capital	20	**8,366**	(60,390)
Cash flows from operating activities		**509,540**	444,408
INVESTING			
Drilling and development	6	**(241,545)**	(486,861)
Exploration and evaluation	7	**(863)**	-
Property acquisitions	5, 6, 7	**(98,524)**	(28,897)
Changes in non-cash investing working capital	20	**(12,298)**	(25,980)
Cash flows used in investing activities		**(353,230)**	(541,738)
FINANCING			
Increase in long-term debt	12	**202,617**	138,341
Repayment of senior unsecured notes	12	**(225,000)**	-
Decrease in finance lease obligation	10	**(4,270)**	(2,246)
Cash dividends	13	**(104,723)**	(127,535)
Cash flows (used in) from financing activities		**(131,376)**	8,560
Foreign exchange (loss) gain on cash held in foreign currencies		**(3,835)**	10,041
Net change in cash and cash equivalents		**21,099**	(78,729)
Cash and cash equivalents, beginning of year		**41,676**	120,405
Cash and cash equivalents, end of year	20	**62,775**	41,676
Supplementary information for cash flows from operating activities			
Interest paid		**60,221**	62,911
Income taxes (received) paid		**(10,535)**	92,907

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY (THOUSANDS OF CANADIAN DOLLARS)

	Note	Year Ended December 31, 2016	Year Ended December 31, 2015
SHAREHOLDERS' CAPITAL			
Balance, beginning of period		**2,181,089**	1,959,021
Shares issued for the DRIP[1]	13	**192,998**	155,033
Vesting of equity based awards	13, 15	**67,146**	56,855
Equity based compensation	13, 15	**8,247**	2,619
Share-settled dividends on vested equity based awards	13, 15	**3,242**	7,561
Balance, end of period	13	**2,452,722**	2,181,089
CONTRIBUTED SURPLUS			
Balance, beginning of period		**107,946**	92,188
Equity based compensation	15	**60,988**	72,613
Vesting of equity based awards	13, 15	**(67,146)**	(56,855)
Balance, end of period		**101,788**	107,946
ACCUMULATED OTHER COMPREHENSIVE INCOME			
Balance, beginning of period		**113,647**	5,722
Currency translation adjustments		**(83,308)**	107,925
Balance, end of period		**30,339**	113,647
DEFICIT			
Balance, beginning of period		**(544,023)**	(35,585)
Net loss		**(160,051)**	(217,302)
Dividends declared	13	**(299,070)**	(283,575)
Share-settled dividends on vested equity based awards	13, 15	**(3,242)**	(7,561)
Balance, end of period		**(1,006,386)**	(544,023)
TOTAL SHAREHOLDERS' EQUITY		**1,578,463**	1,858,659

[1] DRIP refers to Vermilion's dividend reinvestment and Premium Dividend™ plans.

DESCRIPTION OF EQUITY RESERVES

Shareholders' capital
Represents the recognized amount for common shares when issued, net of equity issuance costs and deferred taxes.

Contributed surplus
Represents the recognized value of equity based awards that are settled in shares. Once vested, the value of the awards are transferred to shareholders' capital.

Accumulated other comprehensive income
Represents currency translation adjustments resulting from translating financial statements of subsidiaries with a foreign functional currency to Canadian dollars at period-end rates. These amounts may be reclassified to net earnings if there is a disposal or partial disposal of a subsidiary.

Deficit
Represents the cumulative net earnings and losses less distributed earnings of Vermilion Energy Inc.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2016 AND 2015
(TABULAR AMOUNTS IN THOUSANDS OF CANADIAN DOLLARS, EXCEPT SHARE AND PER SHARE AMOUNTS)

1. BASIS OF PRESENTATION

Vermilion Energy Inc. and its subsidiaries (the "Company" or "Vermilion") are engaged in the business of petroleum and natural gas exploration, development, acquisition, and production.

Vermilion was incorporated in Canada and the Company's registered office and principal place of business is located at 3500, 520, 3rd Avenue SW, Calgary, Alberta, Canada.

These consolidated financial statements were approved and authorized for issuance by Vermilion's Board of Directors on February 24, 2017.

2. SIGNIFICANT ACCOUNTING POLICIES

Accounting Framework
The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB").

Principles of Consolidation
The consolidated financial statements include the accounts of Vermilion Energy Inc. and its subsidiaries. Transactions between Vermilion Energy Inc. and its subsidiaries have been eliminated.

Vermilion accounts for joint operations by recognizing the Company's share of assets, liabilities, income and expenses.

Exploration and Evaluation Assets
Vermilion classifies costs as Exploration and Evaluation ("E&E") assets when they relate to exploring and evaluating an area for which the Company has the licence or right to explore and extract resources. E&E costs may include geological and geophysical costs, land acquisition costs, and costs for drilling, completion, and testing of exploration wells.

E&E costs are reclassified to capital assets if the technical feasibility and commercial viability of the area can be determined. E&E assets are assessed for impairment prior to any reclassification. The technical feasibility and commercial viability of extracting the reserves is considered to be determinable when proved and probable reserves are identified.

Costs incurred prior to the acquisition of the legal rights to explore an area are expensed as incurred. If reserves are not found within the license area or the area is abandoned, the related E&E costs are amortized over a period not greater than five years. If an exploration license expires prior to the commencement of exploration activities, the cost of the exploration license is written off through depletion in the year of expiration.

Capital Assets
Vermilion recognizes capital assets at cost less accumulated depletion, depreciation and impairment losses. Costs include directly attributable costs incurred for the drilling and completion of wells and the construction of production and processing facilities.

When components of capital assets are replaced, disposed of, or no longer in use, they are derecognized. Gains and losses on disposal of capital assets are determined by comparing the proceeds of disposal compared to the carrying amount.

Depletion and Depreciation
Capital assets are grouped into depletion units, which are groups of assets within a specific production area that have similar economic lives. Depletion units represent the lowest level of disaggregation for which costs are accumulated for the purposes of calculating depletion and depreciation.

The net carrying value of each depletion unit is depleted using the unit of production method by reference to the ratio of production in the period to the total proved and probable reserves, taking into account the future development costs necessary to bring the applicable reserves into production.

For the purposes of the depletion calculations, oil and gas reserves are converted to a common unit of measure on the basis of their relative energy content based on a conversion ratio of six thousand cubic feet of natural gas to one barrel of oil equivalent.

Impairment of Capital Assets and Exploration and Evaluation Assets
Depletion units are aggregated into cash generating units ("CGUs") for impairment testing. CGUs are the lowest level for which there are identifiable cash inflows that are largely independent of cash inflows of other groups of assets. CGUs are reviewed for indicators of potential impairment at each reporting date.

E&E assets are tested for impairment when reclassified to capital assets or when indicators of potential impairment are identified. E&E assets are reviewed for indicators of potential impairment at each reporting date. If indicators of potential impairment are identified, E&E assets are tested for impairment as part of the CGU attributable to the jurisdiction the exploration area resides.

If an indicator of potential impairment exists, the CGU's carrying value is compared to its recoverable amount. A CGU's recoverable amount is the higher of its fair value less costs of disposal and its value in use. If the carrying amount of a CGU exceeds its recoverable amount, an impairment loss is recognized to reduce the carrying value of the CGU to its recoverable amount.

If an impairment loss has been recognized in a prior period, an assessment is performed at each reporting date to determine if the circumstances which led to the impairment loss have reversed. If the change in circumstances leads to the recoverable amount being higher than the carrying value after the impairment loss, then the impairment loss (net of depletion that would otherwise have been recorded) is reversed.

Finance leases
Finance leases are leases which transfer substantially all of the risks and rewards incidental to legal ownership of the leased asset to Vermilion. A finance lease obligation is recognized at the commencement of the lease term at the lower of fair value of the leased asset or the present value of the minimum lease payments.

Cash and Cash Equivalents
Cash and cash equivalents include cash on deposit with financial institutions and guaranteed investment certificates.

Crude Oil Inventory
Crude oil inventory is valued at the lower of cost or net realizable value. Cost of crude oil inventory produced is determined on a weighted-average basis and includes related operating expenses, royalties, and depletion.

Asset Retirement Obligations
Vermilion recognizes a provision for asset retirement obligations when an event occurs giving rise to an obligation of uncertain timing or amount. Asset retirement obligations are recognized on the consolidated balance sheet as a long-term liability with a corresponding increase to E&E or capital assets.

Asset retirement obligations reflect the present value of estimated future settlement costs. The discount rate used to calculate the present value is specific to the jurisdiction the obligation relates to and is reflective of current market assessment of the time value of money and risks specific to the liabilities that have not been reflected in the cash flow estimates.

Asset retirement obligations are remeasured at each reporting period to reflect changes in discount rates and estimated future settlement costs. Asset retirement obligations are increased each reporting period to reflect the passage of time with a corresponding charge to accretion expense.

Revenue Recognition
Revenues associated with the sale of petroleum and natural gas are recorded when title passes to the customer. Revenue is recognized when all the following conditions have been satisfied:

- Vermilion has transferred the significant risks and rewards of ownership of the petroleum and natural gas to the customer;
- Vermilion retains no continuing managerial involvement to the degree usually associated with ownership or effective control over the petroleum or natural gas sold;
- The amount of the revenue can be reliably measured;
- It is probable that the economic benefits associated with the transaction will flow to Vermilion; and
- The costs incurred or to be incurred in respect of the transaction can be measured reliably.

Financial Instruments
Financial instruments are measured at fair value on initial recognition. Measurement in subsequent periods depends on the classification of the financial instrument as described below:

- Held for trading: Held for trading financial instruments are subsequently measured at fair value on the consolidated balance sheet and gains and losses are recognized in net earnings. Cash and cash equivalents and derivatives assets and liabilities are classified as held for trading.
- Loans and receivables and other financial liabilities: Loans and receivables and other financial liabilities are subsequently measured at amortized cost. Accounts receivable are classified as loans and receivables. Accounts payable and accrued liabilities, dividends payable, finance lease, and long-term debt are classified as other financial liabilities.

Equity Based Compensation
Equity based compensation expense results from equity-settled awards issued under Vermilion's long-term share-based compensation plan (the "Vermilion Incentive Plan" or "VIP") as well as the grant date fair value of Vermilion common shares issued under the Company's bonus and employee share savings plans.

Equity-settled awards issued under the VIP vest over a period of one to three years and awards outstanding are adjusted upon vesting by a performance factor determined by the Company's Board of Directors. Equity based compensation expense for the VIP is recognized over the vesting period with a corresponding adjustment to contributed surplus. The expense recognized is based on the grant date fair value of the VIP awards, an estimate of the performance factor that will be achieved, and an estimate of forfeiture rates based on historical vesting data. Dividends notionally accrue to the VIP awards and are excluded in the determination of grant date fair values. Upon vesting, the amount recognized in contributed surplus is reclassified to shareholders' capital.

The grant date fair value of the equity-settled awards issued under the VIP and the grant date fair value of Vermilion common shares issued under the Company's bonus and employee share savings plans are determined as the closing price of Vermilion's common shares on the Toronto Stock Exchange on the grant date.

Per Share Amounts
Basic net loss per share is calculated by dividing net loss by the weighted-average number of shares outstanding during the period.

Diluted net loss per share is calculated by dividing net loss by the diluted weighted-average number of shares outstanding during the period. The diluted weighted-average number of shares outstanding is the sum of the weighted-average number of shares outstanding and, to the extent inclusion reduces net earnings per share, the number of shares issuable under the VIP determined using the treasury stock method. The treasury stock method assumes that the unrecognized equity based compensation expense are deemed proceeds used to repurchase Vermilion common shares at the average market price during the period.

Foreign Currency Translation
Vermilion Energy Inc.'s functional and presentation currency is the Canadian dollar. Vermilion has subsidiaries that transact and operate in countries other than Canada and have functional currencies other than the Canadian dollar.

Foreign currency translations include the translation of foreign currency transactions and the translation of foreign operations.

Foreign currency translations occur when translating transactions in foreign currencies to the applicable functional currency of Vermilion Energy Inc. and its subsidiaries. Gains and losses from foreign currency transactions are recorded as foreign exchange gains or losses. Translations occur as follows:

- Income and expenses are translated at the prevailing rates on the date of the transaction
- Non-monetary assets or liabilities are carried at the prevailing rates on the date of the transaction
- Monetary items are translated at the prevailing rates at the balance sheet date

Foreign operation translations occur when translating the financial statements of non-Canadian functional currency subsidiaries to the Canadian dollar and when translating intercompany loans that are deemed to represent net investments in a foreign subsidiary. Gains and losses from foreign operation translations are recorded as currency translation adjustments. Translations occur as follows:

- Income and expenses are translated at the average exchange rates for the period
- Assets and liabilities are translated at the prevailing rates on the balance sheet date.

Income Taxes
Deferred taxes are calculated using the balance sheet method. Deferred tax is recognized for the estimated effect of any temporary differences between the amounts recognized on Vermilion's consolidated balance sheet and the respective tax basis. This calculation uses enacted or substantively enacted tax rates that are expected to be in effect when the temporary differences are expected to reverse. The effect of a change in tax rates on deferred taxes is recognized in the period the related legislation is substantively enacted.

Deferred tax assets are recognized to the extent that it is probable that future taxable profits will be available against which the deductible temporary differences can be used. Deferred tax assets are reviewed at each reporting date and are reduced to the extent it is no longer probable that the related tax benefit will be realized.

Management Judgments and Estimation Uncertainty
The preparation of the consolidated financial statements in accordance with IFRS requires management to make judgments, estimates, and assumptions that affect the reported amount of assets, liabilities, income and expenses. Actual results could differ significantly from these estimates.

Key areas where management has made judgments, estimates, and assumptions include:

- Asset retirement obligations: Asset retirement obligations are based on judgments regarding regulatory requirements, estimates of future costs, and the expected timing of expenditures. The carrying balance of asset retirement obligations and accretion expense may differ due to changes in: laws and regulations, technology, the expected timing of expenditures, and market conditions affecting the discount rate applied.
- Determination of CGUs: CGU determination is subject to management's judgment of the lowest level at which there are identifiable cash inflows that are largely independent of the cash inflows of other groups of assets. The factors used by Vermilion to determine CGUs vary by jurisdiction due to their unique operating and geographic conditions. In general, Vermilion will assess the following factors: geographic proximity of the assets within a group to one another, geographic proximity of the group of assets to other groups of assets, homogeneity of the production from the group of assets and the sharing of infrastructure used to process and/or transport production. The composition of CGUs can directly impact the calculated recoverable amount of a CGU and the recorded impairment loss or recovery.
- Assessment of impairments or recovery of previous impairments: The calculation of the recoverable amount of a CGU is based on market factors (including estimated future commodity prices) and estimates of reserves and resources. Reserve and resource estimates are based on: engineering data, estimated future commodity prices, expected future rates of production, and assumptions regarding the timing and amount of future expenditures. Changes in these judgments, estimates and assumptions can directly impact the calculated recoverable amount of a CGU and the recorded impairment loss or recovery.
- Income Taxes: Tax interpretations, regulations, and legislation in the various jurisdictions in which Vermilion and its subsidiaries operate are subject to change and interpretation. Changes in laws and interpretations can affect the timing of the reversal of temporary tax differences, the tax rates in effect when such differences reverse and Vermilion's ability to use tax losses and other tax pools in the future. The Company's income tax filings are subject to audit by taxation authorities in numerous jurisdictions and the results of such audits may increase or decrease the tax liability. The determination of tax amounts recognized in the consolidated financial statements are based on management's assessment of the tax positions, which includes consideration of their technical merits, communications with tax authorities and management's view of the most likely outcome.

3. CHANGES TO ACCOUNTING PRONOUNCEMENTS

The following IFRS have been issued by the IASB but are not yet effective:

- IFRS 9 "Financial Instruments" will be adopted January 1, 2018. IFRS 9 includes changes to the classification and measurement of financial instruments and general hedge accounting.
- IFRS 15 "Revenue from Contracts with Customers" will be adopted January 1, 2018. IFRS 15 specifies recognition and measurement requirements for contracts with customers.
- IFRS 16 "Leases" will be adopted January 1, 2019. IFRS 16 requires lessees to recognize a lease obligation and right-of-use asset for the majority of leases.

On the adoption of IFRS 9, Vermilion does not currently anticipate changes to the measured amount of financial instruments and correspondingly does not currently anticipate material changes to net earnings.

In the adoption of IFRS 15, Vermilion has in place a transition team that will perform a detailed review of the Company's standard contracts with customers in accordance with the issued IFRS.

The impact of the adoption of IFRS 16 is currently being evaluated.

4. SEGMENTED INFORMATION

Vermilion has a decentralized business unit structure designed to manage assets in each country the Company operates in. Excluding the Corporate segment, each of the below operating segments derives its revenues solely from the production and sale of petroleum and natural gas.

Vermilion's Corporate segment aggregates costs incurred at the Company's Corporate head office located in Calgary, Alberta, Canada as well as costs incurred relating to Vermilion's exploration activities in Central and Eastern Europe. These operating segments have similar economic characteristics as they do not currently generate revenue.

Vermilion's Chief Operating Decision maker regularly reviews fund flows from operations generated by each of Vermilion's operating segments. Fund flows from operations is a measure of profit or loss that provides the Chief Operating Decision maker with the ability to assess the operating segments' profitability and, correspondingly, the ability of each operating segment to fund its share of dividends, asset retirement obligations, and capital investments.

Vermilion has three major customers with revenues in excess of 10% of consolidated revenues within the France, Netherlands, and Ireland operating segments. Substantially all sales in the France, Netherlands, and Ireland operating segments for the years ended December 31, 2016 and 2015 were to one customer in each respective segment.

	Year Ended December 31, 2016								
($M)	Canada	France	Netherlands	Germany	Ireland	Australia	United States	Corporate	Total
Total assets	1,522,243	835,141	220,350	292,885	756,893	267,183	61,195	131,294	4,087,184
Drilling and development	62,706	68,472	23,740	3,803	9,375	59,910	13,539	-	241,545
Exploration and evaluation	-	-	-	-	-	-	-	863	863
Oil and gas sales to external customers	252,867	246,863	100,707	29,049	109,156	136,835	7,314	-	882,791
Royalties	(21,475)	(27,091)	(1,462)	(2,089)	-	-	(2,167)	-	(54,284)
Revenue from external customers	231,392	219,772	99,245	26,960	109,156	136,835	5,147	-	828,507
Transportation	(15,392)	(14,758)	-	(2,869)	(6,492)	-	-	-	(39,511)
Operating	(71,543)	(50,000)	(20,796)	(12,379)	(18,646)	(47,507)	(1,314)	-	(222,185)
General and administration	(11,826)	(19,101)	(1,525)	(8,314)	(4,772)	(6,400)	(3,624)	2,733	(52,829)
PRRT	-	-	-	-	-	(1,568)	-	-	(1,568)
Corporate income taxes	-	(2,867)	(6,624)	-	-	(7,522)	-	(1,097)	(18,110)
Interest expense	-	-	-	-	-	-	-	(56,957)	(56,957)
Realized gain on derivative instruments	-	-	-	-	-	-	-	65,376	65,376
Realized foreign exchange gain	-	-	-	-	-	-	-	4,041	4,041
Realized other income	-	3,822	-	-	-	-	-	205	4,027
Fund flows from operations	132,631	136,868	70,300	3,398	79,246	73,838	209	14,301	510,791

	Year Ended December 31, 2015								
($M)	Canada	France	Netherlands	Germany	Ireland	Australia	United States	Corporate	Total
Total assets	1,609,180	863,304	212,749	167,908	908,453	235,139	42,927	169,560	4,209,220
Drilling and development	201,508	92,265	47,325	5,363	66,409	61,741	12,250	-	486,861
Oil and gas sales to external customers	320,613	281,422	129,057	41,384	57	162,765	4,288	-	939,586
Royalties	(28,144)	(26,958)	(3,082)	(6,479)	-	-	(1,257)	-	(65,920)
Revenue from external customers	292,469	254,464	125,975	34,905	57	162,765	3,031	-	873,666
Transportation	(16,326)	(15,378)	-	(3,269)	(6,687)	-	-	-	(41,660)
Operating	(89,085)	(50,718)	(22,746)	(10,956)	(15)	(51,676)	(742)	-	(225,938)
General and administration	(16,888)	(20,217)	(4,158)	(7,386)	(2,517)	(5,754)	(3,836)	7,172	(53,584)
PRRT	-	-	-	-	-	(6,878)	-	-	(6,878)
Corporate income taxes	-	(23,764)	(12,152)	-	-	(7,230)	-	(1,091)	(44,237)
Interest expense	-	-	-	-	-	-	-	(59,852)	(59,852)
Realized gain on derivative instruments	-	-	-	-	-	-	-	41,356	41,356
Realized foreign exchange gain	-	-	-	-	-	-	-	623	623
Realized other income	-	31,775	-	-	-	-	-	896	32,671
Fund flows from operations	170,170	176,162	86,919	13,294	(9,162)	91,227	(1,547)	(10,896)	516,167

Reconciliation of fund flows from operations to net loss

	Year Ended	
($M)	Dec 31, 2016	Dec 31, 2015
Fund flows from operations	**510,791**	516,167
Accretion	**(24,783)**	(23,911)
Depletion and depreciation	**(528,002)**	(458,758)
Impairment	**(14,762)**	(274,623)
Gain on business combination	**22,001**	-
Unrealized (loss) gain on derivative instruments	**(137,993)**	43,548
Equity based compensation	**(69,235)**	(75,232)
Unrealized foreign exchange (loss) gain	**(792)**	8,787
Unrealized other expense	**(131)**	(1,008)
Deferred taxes	**82,855**	47,728
Net loss	**(160,051)**	(217,302)

5. BUSINESS COMBINATIONS

In December of 2016, Vermilion acquired, through a wholly-owned subsidiary, interests in production and exploration assets in Germany from Engie E&P Deutschland GmbH. The acquisition includes operated and non-operated interests in five oil and three gas producing fields, along with an operated interest in one exploration license. The acquisition provides Vermilion its first operated producing properties in Germany, and advances the Company's objective of developing a material business unit in this country.

The acquisition was accounted for as a business combination. The total consideration paid and the fair value of the assets acquired and liabilities assumed at the date of acquisition are summarized as follows:

($M)	Consideration
Cash paid to vendor	48,377
Total consideration	48,377

($M)	Allocation of Consideration
Capital assets	142,350
Asset retirement obligations	(66,965)
Deferred taxes	(7,767)
Crude oil inventory	2,760
Net assets acquired	70,378
Gain on business combination	(22,001)
Total net assets acquired, net of gain on business combination	48,377

In calculating the fair value of capital assets, Vermilion considered the net present value of after-tax cash flows from proved plus probable reserves using applicable price decks published by reserve engineering firms (refer to Financial Statement Note 6) and an after-tax discount rate of 12%.

The determination of asset retirement obligations was based on a total undiscounted future liability of $182.3 million. These payments are expected to be made between 2027 and 2049, with the majority of spending occurring between 2043 and 2049 ($78.8 million). The inflation rate used in determining the cash flow estimates was 1.28%. The present value of the obligations was calculated using a credit-adjusted risk-free rate, calculated using a credit spread of 3.8% added to a risk-free rate of 0.9%. Refer to Financial Statement Note 8 for additional information regarding asset retirement obligations.

As the acquisition of control occurred late in 2016, the results of operations from the assets acquired were not significant to Vermilion's consolidated financial statements for the year ended December 31, 2016. Had the acquisition occurred on January 1, 2016, management estimates that consolidated revenues would have increased by $29.3 million and consolidated fund flows from operations would have increased by $8.1 million for the year ended December 31, 2016. Fund flows from operations is Vermilion's measure of profit or loss in accordance with IFRS 8 "Operating Segments". Please see Financial Statement Note 4 for a reconciliation of fund flows from operations to net earnings.

The gain on business combination resulted from the recognition of additional reserve value when the acquisition closed in December 2016, compared to the estimated value in June when Vermilion entered into a definitive purchase and sale agreement and the acquisition price was determined.

6. CAPITAL ASSETS

The following table reconciles the change in Vermilion's capital assets:

($M)	2016	2015
Balance at January 1	**3,467,369**	3,511,092
Additions	**241,545**	486,861
Property acquisitions	**189,853**	27,731
Changes in asset retirement obligations	**149,492**	(78,429)
Depletion and depreciation	**(491,508)**	(438,342)
Recognition of finance lease asset	**960**	31,028
Impairment	**(14,762)**	(219,808)
Foreign exchange	**(109,704)**	147,236
Balance at December 31	**3,433,245**	3,467,369
Cost	**6,256,485**	5,682,461
Accumulated depletion and depreciation	**(2,823,240)**	(2,215,092)
Carrying amount at December 31	**3,433,245**	3,467,369

Impairment
As at December 31, 2016, Vermilion did not identify any indicators of impairment. However, Vermilion recorded an impairment in the three months ended March 31, 2016.

In assessing the recoverable value of a CGU, Vermilion considers the higher of its fair value less costs of disposal and its value in use. For the periods ended March 31, 2016 and December 31, 2015, Vermilion considered the net present value of after-tax cash flows from proved plus probable reserves based on the applicable price decks published by GLJ Petroleum Consultants, Sproule, and McDaniel and Associates. In both 2016 and 2015, Vermilion applied an after-tax discount rate of 9%.

In addition, where applicable, Vermilion also considered:
- The fair value of undeveloped land determined based on orderly land transactions with similar characteristics as Vermilion's undeveloped land.
- The net present value of contingent and prospective resources, discounted at an after-tax discount rate of 15%.

Amounts calculated using fair value less costs of disposal are categorized as a Level 3 fair value measurements due to the use of unobservable inputs in the calculation.

In 2015, as a result of declines in price forecasts for crude oil and Canadian natural gas, Vermilion recorded a non-cash impairment charge of $274.6 million ($219.8 million relating to capital assets and $54.8 million relating to E&E assets) in the Canada segment. The impairment charge related to the light crude oil play in Saskatchewan ($267.9 million based on a recoverable amount of $266.8 million) and shallow coal bed methane properties in Alberta ($6.7 million based on a recoverable amount of $19.7 million).

In the first quarter of 2016, as a result of declines in price forecasts for European natural gas, Vermilion recorded a non-cash impairment charge of $14.8 million (based on a recoverable amount of $737.3 million) in the Ireland segment.

The following table outlines the forward commodity price estimates that were used to assess impairment as at December 31, 2016, as well as to determine the fair value of capital assets for the business combination discussed in Financial Statement Note 5.

	Forward Commodity Price Assumptions									
	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026 [1]
NBP (€/mmbtu)[2]	5.63	5.86	5.98	6.43	6.61	6.75	6.88	7.02	7.16	7.30
WTI (US $/bbl)[3]	55.00	60.90	65.47	69.13	73.21	75.19	77.19	79.23	81.28	83.39
Brent (US $/bbl)[3]	56.00	61.90	66.47	70.50	74.58	76.56	78.56	80.60	82.68	84.98
AECO ($/mmbtu)[3]	3.43	3.17	3.26	3.67	3.86	3.97	4.11	4.23	4.31	4.41

[1] Escalated at 2.0% per year thereafter.
[2] Source: Average of GLJ Petroleum Consultants and Sproule price forecasts, effective January 1, 2017.
[3] Source: Average of GLJ Petroleum Consultants, Sproule, and McDaniel & Associates Consultants price forecasts, effective January 1, 2017.

The determination of impairment is sensitive to changes in key judgements, including reserve revisions, changes in forward commodity prices and exchange rates, and changes in costs and timing of development. Changes in these key judgments would impact the recoverable amounts of CGUs, therefore resulting in additional impairment charges and reversals. The following table demonstrates the impact of a 5% decrease in commodity price estimates and a 1% increase in discount rate assumptions on the recorded impairment as at December 31, 2016:

($M)	1% Increase in Discount Rate	5% Decrease in Commodity Prices
Saskatchewan light crude oil	-	(8,304)
Alberta shallow coal bed methane	-	(853)
Ireland natural gas	-	-
Impairment	-	(9,157)

7. EXPLORATION AND EVALUATION ASSETS

The following table reconciles the change in Vermilion's exploration and evaluation assets:

($M)	2016	2015
Balance January 1	**308,192**	380,621
Additions	**863**	-
Property acquisitions	**2,644**	1,166
Changes in asset retirement obligations	**14**	(130)
Depreciation	**(35,238)**	(21,893)
Impairment[(1)]	**-**	(54,815)
Foreign exchange	**(1,645)**	3,243
Balance December 31	**274,830**	308,192
Cost	**333,835**	362,919
Accumulated depreciation	**(59,005)**	(54,727)
Carrying amount at December 31	**274,830**	308,192

(1) Refer to Financial Statement Note 6 – Capital Assets

8. ASSET RETIREMENT OBLIGATIONS

The following table reconciles the change in Vermilion's asset retirement obligations:

($M)	2016	2015
Balance at January 1	**305,613**	350,753
Additional obligations recognized	**68,288**	3,550
Changes in estimates	**3,454**	1,117
Obligations settled	**(9,617)**	(11,369)
Accretion	**24,783**	23,911
Changes in discount rates	**144,729**	(83,226)
Foreign exchange	**(12,228)**	20,877
Balance at December 31	**525,022**	305,613

Vermilion has estimated the asset retirement obligations based on a total undiscounted future liability of $1.4 billion (2015 - $1.3 billion). These payments are expected to be made between 2017 and 2065, with the majority of spending occurring between 2030 and 2037 ($348.2 million) and between 2044 and 2048 ($241.5 million). Inflation rates used in determining the cash flow estimates were between 0.5% and 2.2% (2015 - between 0.6% and 2.4%). Vermilion calculated the present value of the obligations using a credit-adjusted risk-free rate, calculated using a credit spread of 3.8% (2015 - 7.0%) added to risk-free rates based on long-term, risk-free government bonds.

The risk-free rates used to discount the obligations were as follows:

	Dec 31, 2016	Dec 31, 2015
Canada	**2.3%**	2.2%
France	**1.7%**	2.1%
Netherlands	**(0.3%)**	0.1%
Germany	**0.9%**	0.7%
Ireland	**0.5%**	1.0%
Australia	**3.2%**	3.3%
USA	**2.6%**	2.5%

A 0.5% increase/decrease in the credit spread would decrease/increase asset retirement obligations by approximately $40.0 million.

9. DERIVATIVE INSTRUMENTS

The following table reconciles the change in the fair value of Vermilion's derivative instruments:

	Year Ended	
($M)	Dec 31, 2016	Dec 31, 2015
Fair value of contracts, beginning of year	68,342	24,794
Reversal of opening contracts settled during the year	(55,214)	(23,391)
Realized gain on contracts settled during the year	65,376	41,356
Unrealized gain during the year on contracts outstanding at the end of the year	(82,779)	66,939
Net receipt from counterparties on contract settlements during the year	(65,376)	(41,356)
Fair value of contracts, end of year	(69,651)	68,342
Comprised of:		
Current derivative asset	4,336	55,214
Current derivative liability	(47,660)	-
Non-current derivative asset	1,157	13,128
Non-current derivative liability	(27,484)	-
Fair value of contracts, end of year	(69,651)	68,342

The loss (gain) on derivative instruments for 2016 and 2015 were comprised of the following:

	Year Ended	
($M)	Dec 31, 2016	Dec 31, 2015
Realized gain on contracts settled during the year	(65,376)	(41,356)
Reversal of opening contracts settled during the year	55,214	23,391
Unrealized loss (gain) during the year on contracts outstanding at the end of the year	82,779	(66,939)
Loss (gain) on derivative instruments	72,617	(84,904)

10. LEASES

Vermilion had the following future commitments associated with its operating leases:

	As at	
($M)	Dec 31, 2016	Dec 31, 2015
Less than 1 year	12,683	12,535
1 - 3 years	21,087	22,049
4 - 5 years	18,228	16,617
After 5 years	1,657	9,288
Total minimum lease payments	53,655	60,489

A solution gas facility used in Vermilion's southeast Saskatchewan operations has been recorded as a finance lease. The assets are to be used for a minimum period of 10 years, with an option to renew for successive one year terms. As at December 31, 2016, the carrying amount of the asset included in capital assets is $26.1 million.

Vermilion had the following future commitments associated with its finance lease:

	As at	
($M)	Dec 31, 2016	Dec 31, 2015
Less than 1 year	6,495	6,285
1 - 3 years	12,990	12,571
4 - 5 years	6,043	9,515
After 5 years	4,501	6,984
Total minimum lease payments	30,029	35,355
Amounts representing interest	(3,894)	(5,940)
Present value of net minimum lease payments	26,135	29,415
Current portion of finance lease obligation	(6,507)	(5,850)
Non-current portion of finance lease obligation	19,628	23,565

11. TAXES

The following table reconciles Vermilion's deferred tax asset and liability:

	As at	
($M)	Dec 31, 2016	Dec 31, 2015
Deferred tax liabilities:		
Derivative contracts	-	(18,452)
Capital assets	(265,772)	(331,176)
Non-capital losses	20,561	102,209
Asset retirement obligations	(20,577)	(82,586)
Unrealized foreign exchange	(15,386)	(16,291)
Other	(2,359)	(8,358)
Deferred tax liabilities	(283,533)	(354,654)
Deferred tax assets:		
Derivative contracts	18,806	-
Capital assets	(55,718)	58,846
Non-capital losses	155,447	72,846
Asset retirement obligations	28,960	3,583
Unrealized foreign exchange	(72)	-
Other	4,623	478
Deferred tax assets	152,046	135,753

Income tax expense differs from the amount that would have been expected if the reported earnings had been subject only to the statutory Canadian income tax rate as follows:

	Year Ended	
($M)	Dec 31, 2016	Dec 31, 2015
Loss before income taxes	(223,228)	(213,915)
Canadian corporate tax rate(1)	27.0%	26.2%
Expected recovery	(60,272)	(56,046)
Increase (decrease) in taxes resulting from:		
Petroleum resource rent tax rate (PRRT) differential (2)	1,064	8,310
Foreign tax rate differentials (2), (3)	(16,675)	(8,096)
Equity based compensation expense	14,987	14,000
Amended returns and changes to estimated tax pools and tax positions	6,451	(6,856)
Statutory rate changes and the estimated reversal rates associated with temporary differences	(53,150)	1,733
De-recognition	46,253	51,736
Adjustment for uncertain tax positions	3,675	-
Other non-deductible items	(5,510)	(1,394)
Provision for income taxes	(63,177)	3,387

(1) The corporate tax rate increased to 27.0% in 2016 from 26.2% in 2015 as a result of the 2016 full year impact from the Alberta corporate tax rate increase of 2.0% effective July 1, 2015.
(2) In Australia, current taxes include both corporate income tax rates and PRRT. Corporate income tax rates were applied at a rate of 30% and PRRT was applied at a rate of 40%.
(3) The combined tax rate was 34.4% in France, 50.0% in the Netherlands, 24.2% in Germany, 25% in Ireland, and 35% in the United States.

At December 31, 2016, Vermilion has $1.0 billion (2015 - $0.8 billion) of unused tax losses of which $520 million expire between 2030 and 2035.

At December 31, 2016, Vermilion de-recognized $96.1 million (2015 - $51.7 million) of deferred tax assets, relating to certain non-expiring non-capital losses for which there is uncertainty as to the Company's ability to fully utilize such losses when applying forecasted commodity prices in effect as at December 31, 2016.

The aggregate amount of temporary differences associated with investments in subsidiaries for which deferred tax liabilities have not been recognized as at December 31, 2016 is approximately $1.5 billion (2015 – approximately $1.4 billion).

12. LONG-TERM DEBT

The following table summarizes Vermilion's outstanding long-term debt:

	As at	
($M)	Dec 31, 2016	Dec 31, 2015
Revolving credit facility	**1,362,192**	1,162,998
Senior unsecured notes [1]	**-**	224,901
Long-term debt	**1,362,192**	1,387,899

[1] The senior unsecured notes were included in the current portion of long-term debt as at December 31, 2015. The senior unsecured notes, which had a principal balance of $225.0 million, matured and were repaid on February 10, 2016.

Revolving Credit Facility

At December 31, 2016, Vermilion had in place a bank revolving credit facility maturing May 31, 2019 with the following terms:

	As at	
($M)	Dec 31, 2016	Dec 31, 2015
Total facility amount	**2,000,000**	2,000,000
Amount drawn	**(1,362,192)**	(1,162,998)
Letters of credit outstanding [1]	**(20,100)**	(25,200)
Unutilized capacity	**617,708**	811,802

[1] Included in letters of credit outstanding is a $17.8 million surety bond issued pursuant to the recovery of costs discussed in Financial Statement Note 16.

The facility is extendable from time to time, but not more than once per year, for a period not longer than four years, at the option of the lenders and upon notice from Vermilion. If no extension is granted by the lenders, the amounts owing pursuant to the facility are due at the maturity date. The facility bears interest at a rate applicable to demand loans plus applicable margins. The facility is secured by various fixed and floating charges against the subsidiaries of Vermilion.

As at December 31, 2016, the revolving credit facility was subject to the following financial covenants:

		As at	
Financial covenant	**Limit**	Dec 31, 2016	Dec 31, 2015
Consolidated total debt to consolidated EBITDA	4.0	**2.36**	2.23
Consolidated total senior debt to total capitalization	55%	**46%**	36%

The financial covenants include financial measures defined within the revolving credit facility agreement that are not defined under IFRS. These financial measures are defined by the revolving credit facility agreement as follows:

- Consolidated total debt: Includes all amounts classified as "Long-term debt", "Current portion of long-term debt", and "Finance lease obligation" on our balance sheet.
- Consolidated total senior debt: Defined as consolidated total debt excluding unsecured and subordinated debt.
- Consolidated EBITDA: Defined as consolidated net earnings before interest, income taxes, depreciation, accretion and certain other non-cash items.
- Total capitalization: Includes all amounts on the balance sheet classified as "Shareholders' equity" plus consolidated total debt as defined above.

13. SHAREHOLDERS' CAPITAL

The following table reconciles the change in Vermilion's shareholders' capital:

	2016		2015	
Shareholders' Capital	Shares ('000s)	Amount ($M)	Shares ('000s)	Amount ($M)
Balance as at January 1	**111,991**	**2,181,089**	107,303	1,959,021
Shares issued for the DRIP	**4,672**	**192,998**	3,338	155,033
Vesting of equity based awards	**1,320**	**67,146**	1,158	56,855
Shares issued for equity based compensation	**193**	**8,247**	57	2,619
Share-settled dividends on vested equity based awards	**87**	**3,242**	135	7,561
Balance as at December 31	**118,263**	**2,452,722**	111,991	2,181,089

Vermilion is authorized to issue an unlimited number of common shares with no par value.

Dividends declared to shareholders for the year ended December 31, 2016 were $299.1 million or $2.58 per common share (2015 - $283.6 million or $2.58 per common share). Dividends are approved by the Board of Directors and are paid monthly.

Vermilion has a dividend reinvestment plan ("DRIP") with a Premium Dividend™ component. The DRIP allows eligible holders of common shares to purchase additional common shares at a discount to market by reinvesting their cash dividends. The Premium Dividend™ component allows eligible holders of common shares to reinvest their dividends in new common shares that are exchanged for a premium cash payment equal to 101.5% of the reinvested dividends.

Subsequent to the end of year-end and prior to the consolidated financial statements being authorized for issue on February 24, 2017, Vermilion declared dividends totalling $51.0 million or $0.215 per share for each of January and February of 2017.

14. CAPITAL DISCLOSURES

Vermilion defines capital as net debt (long-term debt plus net working capital) and shareholders' capital.

In managing capital, Vermilion reviews whether fund flows from operations (refer to Financial Statement Note 4 - Segmented Information) is sufficient to fund capital expenditures, dividends, and asset retirement obligations. To the extent that forecasted fund flows from operations are not sufficient in relation to these expenditures, Vermilion will reduce some or all categories of these expenditures or evaluate its ability to fund the expenditures with the issuance of debt or equity.

To manage capital, Vermilion monitors the ratio of net debt to fund flows from operations. Vermilion has historically maintained a ratio of between 1.0 to 1.5. However, as a result of the decline in commodity prices in 2015 and 2016 and the corresponding reduction to fund flows from operations, this ratio has increased to 2.7 times and 2.8 times, respectively. Vermilion has responded to this increase by reducing capital expenditures and implementing the Premium Dividend™ component of the Dividend Reinvestment Plan.

Vermilion's revolving credit facility has financial covenants described in Financial Statement Note 12 - Long-Term Debt. As at December 31, 2016 and 2015, Vermilion was in compliance with these financial covenants.

The following table calculates Vermilion's ratio of net debt to fund flows from operations:

	Year Ended	
($M except as indicated)	Dec 31, 2016	Dec 31, 2015
Long-term debt	**1,362,192**	1,162,998
Current liabilities	**290,862**	503,731
Current assets	**(225,906)**	(284,778)
Net debt	**1,427,148**	1,381,951
Fund flows from operations	**510,791**	516,167
Ratio of net debt to fund flows from operations	**2.8**	2.7

15. EQUITY BASED COMPENSATION

The following table summarizes the number of awards outstanding under the Vermilion Incentive Plan ("VIP"):

Number of Awards ('000s)	2016	2015
Opening balance	1,711	1,775
Granted	777	609
Vested	(628)	(587)
Modified	11	-
Forfeited	(133)	(86)
Closing balance	1,738	1,711

For the year ended December 31, 2016, the awards granted had a weighted average fair value of $38.41 (2015 - $53.80). Equity based compensation expense is calculated based on the VIP awards outstanding multiplied by the estimated performance factor that will be realized upon vesting (2016 - 1.9; 2015 - 1.9) adjusted by an estimated annual forfeiture rate (2016 - 4.6%; 2015 - 4.8%). Equity based compensation expense of $61.0 million was recorded during the year ended December 31, 2016 (2015 - $72.6 million) related to the VIP.

16. OTHER INCOME

In 2015, Vermilion was awarded a recovery of costs resulting from an oil spill at the Ambès oil terminal in France that occurred in 2007. The French court awarded Vermilion approximately €25 million (before taxes), of which 50% was due immediately to Vermilion upon posting a surety bond. The payment was received in 2015, with the remainder due upon conclusion of the appeal process. Approximately 90% of the recovery was recorded as other income in 2015.

In the fourth quarter of 2016, the Court of Appeal of Versailles maintained this award. The remaining payment was received and Vermilion's surety bond was returned in 2017. While further appeal may be possible to the Supreme Court in France, Vermilion is virtually certain that the award will be upheld. Following the decision by the Court of Appeal, Vermilion recognized the remaining amount of the recovery (approximately $3.8 million) as other income in 2016.

17. PER SHARE AMOUNTS

Basic and diluted net loss per share have been determined based on the following:

	Year Ended	
($M except per share amounts)	Dec 31, 2016	Dec 31, 2015
Net loss	(160,051)	(217,302)
Basic weighted average shares outstanding ('000s)	115,695	109,642
Dilutive impact of VIP ('000s)	-	-
Diluted weighted average shares outstanding ('000s)	115,695	109,642
Basic loss per share	(1.38)	(1.98)
Diluted loss per share	(1.38)	(1.98)

The impact of shares issuable under the VIP is anti-dilutive and has been excluded from the calculation of diluted loss per share. The number of shares issuable under the VIP calculated using the treasury stock method for the year ended December 31, 2016 is 1,457 thousand (2015 – 1,409 thousand).

18. FINANCIAL INSTRUMENTS

Classification of Financial Instruments

The following table summarizes information relating to Vermilion's financial instruments

	As at Dec 31, 2016		As at Dec 31, 2015	
	Carrying value	Fair value	Carrying value	Fair value
FINANCIAL ASSETS				
Held for trading				
Cash and cash equivalents	**62,775**	**62,775**	41,676	41,676
Derivative assets	**5,493**	**5,493**	68,342	68,342
Loans and receivables				
Accounts receivable	**131,719**	**131,719**	160,499	160,499
FINANCIAL LIABILITIES				
Held for trading				
Derivative liabilities	**(75,144)**	**(75,144)**	-	-
Other financial liabilities				
Accounts payable and accrued liabilities	**(181,557)**	**(181,557)**	(248,747)	(248,747)
Dividends Payable	**(25,426)**	**(25,426)**	(24,077)	(24,077)
Long-term debt	**(1,362,192)**	**(1,362,192)**	(1,387,899)	(1,387,998)

Fair value measurements are categorized into a fair value hierarchy based on the lowest level input that is significant to the fair value measurement.

- Level 1 inputs are determined by reference to unadjusted quoted prices in active markets for identical assets or liabilities. Inputs used in fair value measurement of cash and cash equivalents are categorized as Level 1.
- Level 2 inputs are determined based on inputs other than unadjusted quoted prices that are observable, either directly or indirectly. The fair value of Vermilion's derivative assets and liabilities are determined using pricing models that incorporate future price forecasts (supported by prices from observable market transactions) and credit risk adjustments. The fair value of Vermilion's senior unsecured notes (included in the fair value of long-term debt as at December 31, 2015) was determined using pricing models that incorporated market rates for similar instruments.
- Level 3 inputs are not based on observable market data. Vermilion does not have any financial instruments classified as Level 3.

There were no transfers between levels in the hierarchy in the years ended December 31, 2016 and 2015.

The carrying value of accounts receivable, accounts payable and accrued liabilities, and dividends payable are a reasonable approximation of their fair value due to the short maturity of these financial instruments. The carrying value of long-term debt outstanding on the revolving credit facility approximates its fair value due to the use of short-term borrowing instruments at market rates of interest.

Nature and Extent of Risks Associated with Financial Instruments

Vermilion is exposed to financial risks from its financial instruments. These financial risks include: market risk, credit risk, and liquidity risk.

Market Risk

Market risk includes: commodity price risk, interest rate risk, and currency risk.

Commodity price risk

Vermilion is exposed to commodity price risk on its derivative assets and liabilities which are used as part of the Company's risk management program to mitigate the effects of changes in commodity prices on future cash flows. While transactions of this nature relate to a forecasted future petroleum and natural gas production, Vermilion does not designate these derivative assets and liabilities as accounting hedges. As such, changes in commodity prices impact the fair value of derivative instruments and the corresponding gains or losses on derivative instruments.

Currency risk

Vermilion is exposed to currency risk on its financial instruments denominated in foreign currencies. These financial instruments include cash and cash equivalents, accounts receivables, and accounts payables. As crude oil is typically sold in US dollars and as result of the Company's operations in Europe, Vermilion is primarily exposed to the US Dollar and Euro. The impact related to working capital is somewhat mitigated as a result of the offsetting effects of foreign exchange fluctuations on assets and liabilities. Vermilion monitors its exposure to currency risk and reviews whether the use of derivative financial instruments is appropriate to manage potential fluctuations in foreign exchange rates.

Interest rate risk

Vermilion is exposed to interest rate risk on its long-term debt. As at December 31, 2016, long-term debt was comprised solely of borrowings under the revolving credit facility. As these borrowings consist of short-term borrowing instruments that bear interest at market rates, changes in interest rates could result in an increase or decrease in the amount paid by Vermilion to service this debt. In both 2015 and 2016, Vermilion had in place interest rate swaps that mitigate some of the effects of changes in variable interest rates.

The following table summarizes the increase (positive values) or decrease (negative values) to comprehensive income before tax impact due to a change in the value of Vermilion's financial instruments as a result of a change in the relevant market risk variable. This analysis does not attempt to reflect any interdependencies between the relevant risk variables.

($M)	Dec 31, 2016	Dec 31, 2015
Currency risk - Euro to Canadian		
5% increase in strength of the Canadian dollar against the Euro	**1,338**	(1,986)
5% decrease in strength of the Canadian dollar against the Euro	**(1,338)**	1,986
Currency risk - US $ to Canadian		
5% increase in strength of the Canadian dollar against the US $	**(59,280)**	3,423
5% decrease in strength of the Canadian dollar against the US $	**59,280**	(3,423)
Commodity price risk		
US $5.00/bbl increase in crude oil price used to determine the fair value of derivatives	**(26,513)**	(3,262)
US $5.00/bbl decrease in crude oil price used to determine the fair value of derivatives	**18,882**	3,263
€ 0.5/GJ increase in European natural gas price used to determine the fair value of derivatives	**(36,999)**	(23,813)
€ 0.5/GJ decrease in European natural gas price used to determine the fair value of derivatives	**33,019**	21,754
Interest rate risk		
1% increase in average Canadian prime interest rate	**(11,674)**	(10,543)
1% decrease in average Canadian prime interest rate	**11,674**	10,543

The above table shows the before tax effect on comprehensive income for a 5% change in the US dollar to Canadian dollar exchange rate based on derivative instruments, long-term debt, and other financial instruments as at December 31, 2016. The $59.3 million increase or decrease shown above is primarily driven by US $0.9 billion notional of cross currency interest rate swaps outstanding as at December 31, 2016 and effective for January 2017.

Subsequent to December 31, 2016, Vermilion repaid $1.2 billion of borrowings on the revolving credit facility bearing interest at CDOR (Canadian Dollar Offered Rate) plus applicable margins and simultaneously borrowed US $0.9 billion on the revolving credit facility bearing interest at LIBOR plus applicable margins. As this transaction occurred subsequent to the balance sheet date, it is not included in the calculations shown in the above table. If included, the before tax effect on comprehensive income for a 5% increase/decrease in strength of the Canadian dollar against the US dollar as at December 31, 2016 would be an increase/decrease of $0.5 million.

Credit Risk:

Vermilion is exposed to credit risk on accounts receivable and derivative assets in the event that customers, joint operation partners, or counterparties fail to discharge their contractual obligations. As at December 31, 2016, Vermilion's maximum exposure to receivable credit risk was $137.2 million (December 31, 2015 - $228.8 million) which is the value of accounts receivable and derivative assets on the balance sheet.

Vermilion's accounts receivable primarily relates to customers and joint operations partners in the petroleum and natural gas industry. These amounts are subject to normal industry payment terms and credit risks. Vermilion manages these risks by monitoring the creditworthiness of customers and joint operations partners and, where appropriate, obtaining assurances such as parental guarantees and letters of credit. As at the balance sheet date, approximately 2.1% of the accounts receivable balance was outstanding for more than 90 days. Vermilion considers the balance of accounts receivable to be collectible.

Vermilion's derivative assets primarily relates to the fair value of financial instruments used as part of the Company's risk management program to mitigate the effects of changes in commodity prices on future cash flows. Vermilion manages this risk by monitoring the creditworthiness of counterparties, transacting primarily with counterparties that have investment grade third party credit ratings, and by limiting the concentration of financial exposure to individual counterparties. As a result, Vermilion has not obtained collateral or other security to support its financial derivatives.

Vermilion's cash deposited in financial institutions and guaranteed investment certificates are also subject to counterparty credit risk. Vermilion mitigates this risk by transacting with financial institutions with high third party credit ratings.

Liquidity Risk:

Liquidity risk is the risk that Vermilion will encounter difficulty in meeting obligations associated with its financial liabilities. Vermilion does not consider this to be a significant risk as its financial position and available committed borrowing facility provide significant financial flexibility and allow Vermilion to meet its obligations as they come due.

The following table summarizes Vermilion's undiscounted non-derivative financial liabilities and their contractual maturities:

($M)	1 month	1 month to 3 months	3 months to 1 year	1 year to 5 years
December 31, 2016	79,509	120,233	7,241	1,377,819
December 31, 2015	112,890	353,934	33,663	1,180,486

19. RELATED PARTY DISCLOSURES

The compensation of directors and management is reviewed annually by the independent Governance and Human Resources Committee against industry practices for oil and gas companies of similar size and scope.

The following table summarizes the compensation of directors and other members of key management personnel during the years ended December 31, 2016 and December 31, 2015:

	Year Ended	
($M)	Dec 31, 2016	Dec 31, 2015
Short-term benefits	**4,748**	5,460
Share-based payments	**20,169**	20,310
	24,917	25,770
Number of individuals included in the above amounts	**18**	20

20. SUPPLEMENTAL INFORMATION

Changes in non-cash working capital was comprised of the following:

	Year Ended	
($M)	Dec 31, 2016	Dec 31, 2015
Changes in:		
Accounts receivable	28,780	11,321
Crude oil inventory	1,311	(3,569)
Prepaid expenses	1,762	2,577
Accounts payable and accrued liabilities	(67,190)	(49,449)
Income taxes payable	30,213	(38,457)
Foreign exchange	1,192	(8,793)
Changes in non-cash working capital	(3,932)	(86,370)
Changes in non-cash operating working capital	8,366	(60,390)
Changes in non-cash investing working capital	(12,298)	(25,980)
Changes in non-cash working capital	(3,932)	(86,370)

Cash and cash equivalents was comprised of the following:

	As at	
($M)	Dec 31, 2016	Dec 31, 2015
Cash on deposit with financial institutions	62,614	31,175
Guaranteed investment certificates	161	10,501
Cash and cash equivalents	62,775	41,676

Wages and benefits included in operating expenses and general and administration expenses were:

	Year Ended	
($M)	2016	2015
Operating expense	45,061	47,738
General and administration expense	35,347	40,391
Wages and benefits	80,408	88,129

DIRECTORS

Lorenzo Donadeo [1]
Calgary, Alberta

Larry J. Macdonald [2, 3, 4, 5, 6]
Chairman & CEO, Point Energy Ltd.
Calgary, Alberta

Claudio A. Ghersinich [3, 6]
Executive Director, Carrera Investments Corp.
Calgary, Alberta

Loren M. Leiker [6]
Houston, Texas

William F. Madison [5, 6]
Sugar Land, Texas

Timothy R. Marchant [5, 6]
Calgary, Alberta

Anthony Marino
Calgary, Alberta

Robert Michaleski [3]
Calgary, Alberta

Sarah E. Raiss [4, 5]
Calgary, Alberta

Catherine L. Williams [3, 4]
Calgary, Alberta

[1] Chairman of the Board
[2] Lead Director
[3] Audit Committee
[4] Governance and Human Resources Committee
[5] Health, Safety and Environment Committee
[6] Independent Reserves Committee

ABBREVIATIONS

$M	thousand dollars
$MM	million dollars
AECO	the daily average benchmark price for natural gas at the AECO 'C' hub in southeast Alberta
bbl(s)	barrel(s)
bbls/d	barrels per day
bcf	billion cubic feet
boe	barrel of oil equivalent, including: crude oil, condensate, natural gas liquids, and natural gas (converted on the basis of one boe for six mcf of natural gas)
boe/d	barrel of oil equivalent per day
btu	British thermal units
CGU	Cash generating unit, the basis upon which Vermilion's assets are evaluated for potential impairments
DRIP	Dividend Reinvestment Plan
GJ	gigajoules
HH	Henry Hub, a reference price paid for natural gas in US dollars at Erath, Louisiana
mbbls	thousand barrels
mboe	thousand barrel of oil equivalent
mcf	thousand cubic feet
mcf/d	thousand cubic feet per day
mmboe	million barrel of oil equivalent
mmbtu	million British thermal units
mmcf	million cubic feet
mmcf/d	million cubic feet per day
MWh	megawatt hour
NBP	the reference price paid for natural gas in the United Kingdom, quoted in pence per therm, at the National Balancing Point Virtual Trading Point operated by National Grid. Our production in Ireland is priced with reference to NBP.
NGLs	natural gas liquids, which includes butane, propane, and ethane
PRRT	Petroleum Resource Rent Tax, a profit based tax levied on petroleum projects in Australia
TTF	the day-ahead price for natural gas in the Netherlands, quoted in MWh of natural gas, at the Title Transfer Facility Virtual Trading Point operated by Dutch TSO Gas Transport Services
WTI	West Texas Intermediate, the reference price paid for

OFFICERS AND KEY PERSONNEL

CANADA

Anthony Marino
President & Chief Executive Officer

Curtis W. Hicks
Executive Vice President & Chief Financial Officer

Mona Jasinski
Executive Vice President, People and Culture

Michael Kaluza
Executive Vice President & Chief Operating Officer

Dion Hatcher
Vice President Canada Business Unit

Terry Hergott
Vice President Marketing

Daniel Goulet
Director Corporate HSE

Bryce Kremnica
Director Field Operations – Canada Business Unit

Kyle Preston
Director Investor Relations

Mike Prinz
Director Information Technology & Information Systems

Jenson Tan
Director Business Development

Robert (Bob) J. Engbloom
Corporate Secretary

UNITED STATES

Daniel G. Anderson
Managing Director – U.S. Business Unit

Timothy R. Morris
Director U.S. Business Development – U.S. Business Unit

EUROPE

Gerard Schut
Vice President European Operations

Darcy Kerwin
Managing Director - France Business Unit

Scott Seatter
Managing Director - Netherlands Business Unit

Albrecht Moehring
Managing Director - Germany Business Unit

Bryan Sralla
Managing Director - Central & Eastern Europe Business Unit

AUSTRALIA

Bruce D. Lake
Managing Director - Australia Business Unit

AUDITORS

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Calgary, Alberta

BANKERS

The Toronto-Dominion Bank

Bank of Montreal

Canadian Imperial Bank of Commerce

National Bank of Canada

Royal Bank of Canada

The Bank of Nova Scotia

HSBC Bank Canada

Wells Fargo Bank N.A., Canadian Branch

La Caisse Centrale Desjardins du Québec

Alberta Treasury Branches

Bank of America N.A., Canada Branch

BNP Paribas, Canada Branch

Citibank N.A., Canadian Branch - Citibank Canada

JPMorgan Chase Bank, N.A., Toronto Branch

Union Bank, Canada Branch

Barclays Bank PLC

Canadian Western Bank

Goldman Sachs Lending Partners LLC

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EXCELLENCE

We aim for exceptional results in everything we do.

TRUST

At Vermilion, we operate with honesty and fairness, and can be counted on to do what we say we will.

RESPECT

We embrace diversity, value our people and believe every employee and business associate worldwide deserves to be treated with the utmost dignity and respect.

RESPONSIBILITY

Vermilion continually shows its commitment to the care of our people and environment, and enrichment of the communities in which we live and work.

VERMILION
ENERGY

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