PrairieSky Royalty Ltd.

Interim Condensed Financial Statements

(unaudited)

For the three and nine month periods ended September 30, 2016

CONDENSED STATEMENT OF FINANCIAL POSITION (UNAUDITED)

(millions)		As at September 30, 2016	As at December 31, 2015
Assets			
Current Assets			
Cash and cash equivalents		**$ 159.4**	$ 190.8
Accounts receivable and accrued revenue	*(Note 4)*	**34.7**	37.6
Income tax receivable		**2.3**	21.4
Prepaid expense		**0.7**	0.6
		197.1	250.4
Royalty assets, net	*(Note 6)*	**834.7**	918.6
Exploration and evaluation assets	*(Note 7)*	**1,136.9**	1,148.4
Other assets	*(Note 8)*	**4.8**	7.6
Goodwill		**613.2**	613.2
		$ 2,786.7	$ 2,938.2
Liabilities and Shareholders' Equity			
Current Liabilities			
Accounts payable and accrued liabilities	*(Note 9)*	**$ 15.3**	$ 14.2
Dividend payable	*(Note 10)*	**13.7**	24.7
		29.0	38.9
Share-based compensation payable	*(Note 11)*	**2.0**	2.8
Deferred income taxes		**186.1**	186.3
		217.1	228.0
Shareholders' Equity			
Shareholders' capital	*(Note 10)*	**3,075.6**	3,067.8
Paid in surplus		**2.7**	1.8
Deficit		**(508.7)**	(359.4)
Total Shareholders' Equity		**2,569.6**	2,710.2
Commitments	*(Note 17)*		
		$ 2,786.7	$ 2,938.2

See accompanying Notes to Interim Condensed Financial Statements

CONDENSED STATEMENT OF EARNINGS AND COMPREHENSIVE INCOME (UNAUDITED)

		Three months ended September 30		Nine months ended September 30	
(millions, except per share amounts)		**2016**	**2015**	**2016**	**2015**
Revenues					
Royalty revenue		**$ 52.2**	$ 42.1	**$ 138.6**	$ 130.2
Other revenue		**7.1**	1.9	**17.7**	40.0
Revenues		**59.3**	44.0	**156.3**	170.2
Expenses					
Production and mineral taxes		**1.3**	2.0	**3.3**	6.6
Depreciation, depletion and amortization	*(Note 6)*	**40.9**	22.9	**122.6**	70.9
Exploration and evaluation	*(Note 7)*	**2.6**	0.8	**5.4**	1.3
Administrative	*(Note 12)*	**7.6**	5.0	**22.9**	20.4
Net Earnings Before Finance Items and Income Taxes		**6.9**	13.3	**2.1**	71.0
Finance Items					
Finance income		**(0.6)**	(0.6)	**(1.8)**	(1.1)
Finance expense		**-**	0.3	**0.2**	0.5
Net Earnings Before Income Tax		**7.5**	13.6	**3.7**	71.6
Income tax expense (recovery)	*(Note 13)*	**(0.4)**	(0.5)	**(0.2)**	16.6
Net Earnings and Comprehensive Income		**$ 7.9**	$ 14.1	**$ 3.9**	$ 55.0
Net Earnings per Common Share	*(Note 10)*				
Basic and Diluted		**$ 0.03**	$ 0.09	**$ 0.02**	$ 0.36

See accompanying Notes to Interim Condensed Financial Statements

CONDENSED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY (UNAUDITED)

($ millions)		Shareholders' Capital	Paid In Surplus	Deficit	Total Shareholders' Equity
Balance at December 31, 2015		**$ 3,067.8**	**$ 1.8**	**$ (359.4)**	**$ 2,710.2**
Net earnings		**-**	**-**	**3.9**	**3.9**
Common shares issued:					
Pursuant to dividend reinvestment plan	*(Note 10)*	**15.6**	**-**	**-**	**15.6**
Pursuant to stock dividend plan	*(Note 10)*	**0.6**	**-**	**-**	**0.6**
Share issue costs, net of tax	*(Note 10)*	**0.1**	**-**	**-**	**0.1**
Common shares repurchased	*(Note 10)*	**(8.5)**	**-**	**(7.6)**	**(16.1)**
Share-based compensation	*(Note 11)*	**-**	**0.9**	**-**	**0.9**
Dividends on common shares	*(Note 10)*	**-**	**-**	**(145.6)**	**(145.6)**
Balance at September 30, 2016		**$ 3,075.6**	**$ 2.7**	**$ (508.7)**	**$ 2,569.6**

($ millions)		Shareholders' Capital	Reserve from Common Control	Paid In Surplus	Retained Earnings (Deficit)	Total Shareholders' Equity
Balance at December 31, 2014		$ 1,181.0	$ (255.7)	$ 0.7	$ 38.0	$ 964.0
Net earnings		-	-	-	55.0	55.0
Common shares issued:						
Pursuant to bought deal offering	*(Note 10)*	198.0				198.0
Share issue costs, net of tax	*(Note 10)*	(6.2)				(6.2)
Pursuant to stock option plan	*(Note 10)*	0.2	-	(0.2)	-	-
Pursuant to dividend reinvestment plan	*(Note 10)*	13.1	-	-	-	13.1
Pursuant to stock dividend plan	*(Note 10)*	5.8	-	-	-	5.8
Pursuant to an acquisition		0.5				0.5
Share-based compensation	*(Note 11)*	-	-	1.0	-	1.0
Dividends on common shares	*(Note 10)*	-	-	-	(147.9)	(147.9)
Balance at September 30, 2015		$ 1,392.4	$ (255.7)	$ 1.5	$ (54.9)	$ 1,083.3

See accompanying Notes to Interim Condensed Financial Statements

CONDENSED STATEMENT OF CASH FLOWS (UNAUDITED)

(millions)		Three months ended September 30 2016	Three months ended September 30 2015	Nine months ended September 30 2016	Nine months ended September 30 2015
Operating Activities					
Net earnings		**$ 7.9**	$ 14.1	**$ 3.9**	$ 55.0
Depreciation, depletion and amortization	*(Note 6)*	**40.9**	22.9	**122.6**	70.9
Exploration and evaluation	*(Note 7)*	**2.6**	0.8	**5.4**	1.3
Deferred income taxes	*(Note 13)*	**(0.4)**	(2.2)	**(0.2)**	0.9
Share-based compensation, net of cash settlements	*(Note 11)*	**2.4**	-	**4.1**	3.4
Non-cash other revenue		**(0.2)**	-	**(0.2)**	(16.4)
Net change in other assets		**1.0**	0.9	**2.8**	2.7
Net change in non-cash working capital	*(Note 16)*	**14.2**	19.9	**8.0**	7.0
Cash From Operating Activities		**68.4**	56.4	**146.4**	124.8
Investing Activities					
Royalty asset acquisitions	*(Note 6)*	**-**	(4.4)	**(21.9)**	(25.1)
Exploration and evaluation acquisitions	*(Note 7)*	**(4.8)**	(0.3)	**(10.5)**	(20.6)
Royalty business combination	*(Note 5)*	**(2.7)**	-	**11.8**	-
Net change in non-cash working capital	*(Note 16)*	**-**	-	**(0.6)**	-
Cash Used in Investing Activities		**(7.5)**	(4.7)	**(21.2)**	(45.7)
Financing Activities					
Dividends on common shares	*(Note 10)*	**(41.1)**	(39.6)	**(140.4)**	(127.8)
Share issuance, net of costs	*(Note 10)*	**-**	189.5	**0.2**	189.5
Financing costs		**-**	-	**-**	(0.1)
Common shares repurchased	*(Note 10)*	**(10.1)**	-	**(16.1)**	-
Net change in non-cash working capital	*(Note 16)*	**-**	-	**(0.3)**	-
Cash From (Used in) Financing Activities		**(51.2)**	149.9	**(156.6)**	61.6
Increase (Decrease) in Cash and Cash Equivalents		**9.7**	201.6	**(31.4)**	140.7
Cash and Cash Equivalents, Beginning of Period		**149.7**	2.2	**190.8**	63.1
Cash and Cash Equivalents, End of Period		**$ 159.4**	$ 203.8	**$ 159.4**	$ 203.8

See accompanying Notes to Interim Condensed Financial Statements

1. NATURE OF OPERATIONS

PrairieSky Royalty Ltd. ("PrairieSky" or the "Company") has a geologically and geographically diverse portfolio of fee simple mineral title, oil and natural gas gross overriding royalty interests and other acreage spanning British Columbia, Alberta, Saskatchewan and Manitoba (collectively, the "Royalty Properties"). The Company is focused on encouraging third parties to actively develop the Royalty Properties, while strategically seeking additional petroleum and natural gas royalty assets that provide the Company with medium-term to long-term value enhancement potential. The Company does not directly conduct operations to explore for, develop or produce petroleum or natural gas; rather, third party development of the titled or leased lands provides the Company with royalty revenue as petroleum and natural gas are produced from such properties.

The Company's shares are publicly traded on the Toronto Stock Exchange ("TSX") under the stock symbol "PSK". The location of the head and registered office of the Company is Suite 1700, 350 – 7th Avenue S.W., Calgary, Alberta, T2P 3N9.

2. BASIS OF PRESENTATION

A) STATEMENT OF COMPLIANCE

These unaudited interim condensed financial statements have been prepared in accordance with International Accounting Standard ("IAS") 34, "Interim Financial Reporting" and have been prepared following the same accounting policies and methods of computation as the audited annual financial statements. Certain information and disclosures normally included in the audited annual financial statements prepared in accordance with International Financial Reporting Standards ("IFRS") have been condensed or omitted. Accordingly, these interim condensed financial statements should be read in conjunction with the audited annual financial statements for the year ended December 31, 2015.

These unaudited interim condensed financial statements have been prepared on a historical cost basis, except for share-based payment transactions. The interim condensed financial statements have been prepared on a going concern basis and amounts are in millions of Canadian dollars unless otherwise stated.

These unaudited interim condensed financial statements were authorized for issuance by the Company's Audit Committee on October 25, 2016.

B) ESTIMATES

The timely preparation of the unaudited interim condensed financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the reported amounts of revenues and expenses during the period. Actual results may differ from these estimates.

In preparing these unaudited interim condensed financial statements, the judgments made by management in applying the Company's accounting policies and the key sources of estimation uncertainty were the same as those applied to the financial statements as at and for the year ended December 31, 2015.

3. RECENT ACCOUNTING PRONOUNCEMENTS

New Standards Issued Not Yet Adopted

On May 28, 2014, the IASB issued IFRS 15, "Revenue from Contracts with Customers" which is the result of the joint project with Financial Accounting Standards Board ("FASB"). The new standard replaces the two main recognition standards IAS 18, "Revenue" and IAS 11, "Construction Contracts". The new standard provides a five step model framework as a core principal upon which an entity recognizes revenue and becomes effective January 1, 2018. On April 26, 2016, the IASB issued, "Clarifications to IFRS 15, Revenue from Contract with Customers", which is effective at the same time as IFRS 15. The Company intends to adopt IFRS 15 and the clarifications in its financial statements for the annual period beginning on January 1, 2018. The extent of the impact of adoption of the standard has not yet been determined.

On July 24, 2014, the IASB issued IFRS 9, "Financial Instruments", which replaces IAS 39, "Financial Instruments: Recognition and Measurement". The new standard introduces new requirements for the classification and measurement of financial assets and liabilities. Financial assets are classified and measured based on the business model in which they are held and the characteristics of their contractual cash flows. IFRS 9 amends the impairment model by introducing a new model for calculating impairment and includes a new hedge accounting model that better reflects risk management activities in the financial statements of entities that elect to apply hedge accounting. IFRS 9 will apply retrospectively, for annual periods beginning on or after January 1, 2018 and early adoption is permitted. The Company intends to adopt IFRS 9 in its financial statements for the annual period beginning on January 1, 2018. The Company does not expect the standard to have a material impact on the Company's financial statements.

On January 13, 2016, the IASB issued IFRS 16, "Leases". The standard is required to be adopted either retrospectively or by recognizing the cumulative effect of initially applying IFRS 16 as an adjustment to opening equity at the date of initial application. IFRS 16 is effective for fiscal years beginning on or after January 1, 2019, with earlier adoption permitted if IFRS 15 "Revenue from Contracts with Customers" has also been adopted. Under the new standard, companies will recognize new assets and liabilities, bringing off-balance sheet leasing arrangements onto the balance sheet. The Company intends to adopt IFRS 16 in its financial statements for the annual period beginning on January 1, 2019. The Company does not expect the standard to have a material impact on the financial statements.

4. ACCOUNTS RECEIVABLE AND ACCRUED REVENUE

		As at September 30, 2016	As at December 31, 2015
Trade receivables and accrued revenue		**$ 30.0**	$ 33.3
Current portion of royalty note receivable	*(Note 8)*	**3.7**	3.6
Production and mineral taxes receivable		**0.9**	0.5
Interest receivable		**0.1**	0.2
		$ 34.7	$ 37.6

Trade receivables and accrued revenue relate to lease and royalty payments receivable. The analysis of accounts receivable and accrued revenue that are past due but not impaired is as follows:

			Past due but not impaired	
	Total	Neither past due nor impaired	4 - 6 Months	7- 12 Months
As at September 30, 2016	**$ 34.7**	**$ 34.5**	**$ 0.1**	**$ 0.1**
As at December 31, 2015	$ 37.6	$ 37.0	$ 0.4	$ 0.2

At September 30, 2016, there was no allowance or provision made for doubtful accounts. In determining the recoverability of trade receivables that are past due but not impaired, the Company considers the age of the outstanding receivables and the credit worthiness of the counterparties. See Note 15 for further information about credit risk.

5. BUSINESS COMBINATIONS

On December 16, 2015, the Company completed an acquisition of royalty properties from a third party (the "Transaction") for cash consideration of $680.0 million, subject to closing adjustments, and the issuance of 44.4 million common shares at the December 16, 2015 share price of $22.16 per share. To finance a portion of the purchase price, PrairieSky completed a non-brokered private placement of 26,976,000 subscription receipts at a price of $25.20 per subscription receipt on December 2, 2015 for gross proceeds of $679.8 million. The subscription receipts converted to common shares on December 16, 2015, concurrently with closing of the Transaction. The effective date of the Transaction was October 1, 2015.

During the three months ended June 30, 2016, preliminary estimates of revenue on the royalty properties acquired from the effective date to the closing date of the Transaction were finalized. Actual revenue was $1.2 million greater than estimated, resulting in a decrease in goodwill and total consideration paid of $1.2 million. The Company does not anticipate any further adjustment in subsequent periods.

During the three months ended September 30, 2016, the Company paid $2.7 million related to the final settlement regarding the Transaction for the interim period between the effective date of October 1, 2015 and the closing date of December 16, 2015. During the nine months ended September 30, 2016, the Company collected $14.5 million in receivables in addition to the $2.7 million paid as noted above.

6. ROYALTY ASSETS, NET

	As at September 30, 2016	As at December 31, 2015
Cost		
Balance, Beginning of Period	**$ 1,039.7**	$ 557.4
Assets acquired through business combination	**-**	435.3
Transfers from exploration & evaluation assets	**16.6**	2.1
Other asset acquisitions	**22.1**	44.9
Balance, End of Period	**1,078.4**	1,039.7
Accumulated Depletion, Depreciation and Amortization		
Balance, Beginning of Period	**(121.1)**	(24.8)
Depletion, depreciation and amortization	**(122.6)**	(96.3)
Balance, End of Period	**(243.7)**	(121.1)
Net Book Value, End of Period	**$ 834.7**	$ 918.6

For the three and nine month periods ended September 30, 2016, asset acquisitions totaled $0.2 million (2015 - $4.4 million) and $22.1 million (2015 - $39.3 million), respectively, which are primarily acquisitions of fee land and producing gross overriding royalties. During the three and nine month period ended September 30, 2016, there was a non-monetary acquisition of fee lands valued at $0.2 million. During the nine month period ended September 30, 2015, there was a non-monetary acquisition of gross overriding royalty interest valued at $14.2 million.

7. EXPLORATION AND EVALUATION ASSETS

	As at September 30, 2016	As at December 31, 2015
Cost		
Balance, Beginning of Period	**$ 1,148.4**	$ 107.8
Assets acquired through business combination	**-**	1,016.7
Transfers to royalty assets	**(16.6)**	(2.1)
Other asset acquisitions	**10.5**	28.2
Land expiries	**(5.4)**	(2.2)
Balance, End of Period	**$ 1,136.9**	$ 1,148.4

For the three and nine month periods ended September 30, 2016, the Company acquired $4.8 million (2015 - $0.8 million) and $10.5 million (2015 - $22.6 million), respectively, of exploration and evaluation assets ("E&E"), which include seismic and land acquisitions. During the nine month period ended September 30, 2015, the Company exchanged lease issuance bonus proceeds for E&E assets valued at $1.5 million.

8. OTHER ASSETS

At September 30, 2016, other assets relate to the non-current portion of a royalty note receivable of $4.8 million (December 31, 2015 - $7.6 million), receivable in equal monthly instalments over the next 2.3 years bearing interest of four percent per annum. The current portion of the note receivable of $3.7 million (December 31, 2015 - $3.6 million) is included in accounts receivable and accrued revenue as disclosed in Note 4. During the three and nine month periods ended September 30, 2016, $0.1 million (2015 - $0.1 million) and $0.3 million (2015 - $0.4 million), respectively, of interest income was recorded related to the royalty note receivable. As at September 30, 2016, the royalty note receivable had a fair value of $8.5 million (December 31, 2015 - $11.1 million). The estimated fair value of other assets is categorized within Level 2 of the fair value hierarchy and has been determined based on market information where available using estimated interest rates based on the credit quality of the customer.

9. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	As at September 30, 2016	As at December 31, 2015
Trade payables	**$ 1.7**	$ 1.9
Production and mineral taxes payable	**4.5**	9.4
Accrued liabilities	**9.1**	2.9
	$ 15.3	$ 14.2

Accrued liabilities primarily include amounts related to salary and share-based compensation accruals.

10. SHARE CAPITAL

AUTHORIZED

The authorized share capital of the Company includes an unlimited number of common shares and an unlimited number of preferred shares issuable in series. The holders of the common shares are entitled to one vote in respect of each common share held at all meetings of shareholders, except meetings at which only holders of a specified class of share have the right to vote. The common shares have no par value.

ISSUED AND OUTSTANDING

	As at September 30, 2016		As at December 31, 2015	
	Number of Shares (millions)	Amount ($ millions)	Number of Shares (millions)	Amount ($ millions)
Common Shares Outstanding, Beginning of Period	**228.2**	**$ 3,067.8**	149.3	$ 1,181.0
Issued pursuant to dividend reinvestment plan	**0.8**	**15.6**	1.1	24.0
Issued pursuant to the stock dividend plan	**-**	**0.6**	0.1	6.3
Common shares repurchased	**(0.6)**	**(8.5)**	-	-
Issued pursuant to bought deal financing	**-**	**-**	6.3	198.0
Share issue costs, net of tax	**-**	**0.1**	-	(6.9)
Issued pursuant to an acquisition	**-**	**-**	-	0.5
Issued pursuant to business combination	**-**	**-**	44.4	984.9
Issued pursuant to the private placement	**-**	**-**	27.0	679.8
Issued pursuant to stock option exercise	**-**	**-**	-	0.2
Common Shares Outstanding, End of Period	**228.4**	**$ 3,075.6**	228.2	$ 3,067.8

NORMAL COURSE ISSUER BID ("NCIB")

On April 27, 2016, the Company announced the approval of its NCIB by the Toronto Stock Exchange ("TSX"). The NCIB allows the Company to purchase for cancellation up to a maximum of 1,600,000 common shares. The NCIB will continue until May 1, 2017, at which time the Company may apply to renew the NCIB at the same or at a higher/lower level for an additional 12-month period. Purchases will be made on the open market through the TSX or alternative platforms at the market price of such common shares. All common shares purchased under the NCIB will be cancelled.

During the three and nine months ended September 30, 2016, the Company purchased for cancellation 390,500 common shares ($25.98 per common share) and 633,000 common shares ($25.50 per common share), respectively. The total cost paid, including commissions and fees, was first charged to share capital to the extent of the average carrying value of the common shares purchased and the excess of $7.6 million was charged to the deficit for the nine month period.

DIVIDENDS

During the three month period ended September 30, 2016, PrairieSky declared dividends of $41.1 million (September 30, 2015 - $50.8 million) or $0.18 per common share (September 30, 2015 - $0.32499) and paid dividends of $41.1 million (September 30, 2015 - $39.6 million) or $0.18 per common share (September 30, 2015 - $0.32499).

During the nine month period ended September 30, 2016, PrairieSky declared dividends of $145.6 million (September 30, 2015 - $147.9 million) or $0.63666 per common share (September 30, 2015 - $0.97497) and paid dividends of $140.4 million (September 30, 2015 - $127.8 million) or $0.68499 per common share (September 30, 2015 - $0.97244). Of the total dividends paid in 2016, $140.4 million (September 30, 2015 - $127.8 million) was settled in cash and an additional $16.2 million (September 30, 2015 - $18.9 million) was settled in common shares in lieu of cash dividends under the dividend reinvestment plan ("DRIP") and stock dividend plan ("SDP").

On February 29, 2016, the Company reduced its dividend to $0.72 per common share per annum and suspended the DRIP and the SDP, all effective for the March 31, 2016 record date. On September 15, 2016, the Board of Directors declared a dividend of $0.06 per common share payable on October 17, 2016 to common shareholders of record as of September 30, 2016.

EARNINGS PER COMMON SHARE

The following table presents the computation of net earnings per common share:

	Three months ended September 30		Nine months ended September 30	
	2016	**2015**	**2016**	**2015**
Net Earnings	**$ 7.9**	$ 14.1	**$ 3.9**	$ 55.0
Number of Common Shares:				
Weighted Average Common Shares Outstanding - Basic	**228.6**	155.6	**228.7**	151.5
Effect of Dilutive Securities	**0.2**	0.4	**0.2**	0.4
Weighted Average Common Shares Outstanding - Diluted	**228.8**	156.0	**228.9**	151.9
Net Earnings per Common Share				
Basic and Diluted	**$ 0.03**	$ 0.09	**$ 0.02**	$ 0.36

11. SHARE-BASED COMPENSATION PLANS

The Company has a number of share-based compensation arrangements under which the Company awards various types of long-term incentive grants to eligible employees, officers and directors. They include stock options, performance share units ("PSUs"), restricted share units ("RSUs"), and deferred share units ("DSUs").

The Company accounts for stock options granted to Company employees and officers as equity-settled share-based payment transactions and accrues compensation costs over the vesting period based on the fair values determined at the grant date.

The Company accounts for PSUs, RSUs and DSUs held by Company employees, officers and directors as cash-settled share-based payment transactions and accrues compensation costs and dividends over the vesting period based on the fair value of the rights. The Company may make an election to settle vested share unit awards with either a cash payment equal to the five-day weighted average trading price for the common shares multiplied by the number of common shares or issue the number of common shares. PSUs vest following the completion of a three year performance period provided the employee remains actively employed with the Company on the vesting date. RSUs granted to employees at the time of the initial public offering ("IPO") vest 30% after the second anniversary of the date of grant and the remaining 70% vest after the third anniversary, while subsequent grants vest evenly over a three year period, provided the employee remains actively employed with the Company on the vesting date. RSUs granted to officers of the Company at the time of the IPO fully vest three years from the date of grant, while subsequent grants vest evenly over a three year period provided the officer remains actively employed with the Company on the vesting date. DSUs are fully vested as of the grant date.

The Company has recognized the following share-based compensation costs:

	Three months ended September 30		Nine months ended September 30	
	2016	**2015**	**2016**	**2015**
Compensation costs of transactions classified as equity-settled	**$ 0.3**	$ 0.2	**$ 0.9**	$ 1.0
Compensation costs of transactions classified as cash-settled	**2.1**	(0.2)	**4.9**	3.1
Total share-based compensation expense	**$ 2.4**	$ -	**$ 5.8**	$ 4.1

The Company has recognized the following liability for share-based payment transactions:

	As at September 30, 2016	**As at December 31, 2015**
Liability for unvested cash-settled plans	**$ 6.0**	$ 2.8
Liability for vested cash-settled plans	**1.7**	1.7
Liability for cash-settled plans	**$ 7.7**	$ 4.5

As at September 30, 2016, $5.7 million (December 31, 2015 - $1.7 million) of the liability for cash-settled plans, which represents the value of the PSUs, RSUs and DSUs that are expected to be settled in the next twelve months, is included in accounts payable and accrued liabilities. The remaining $2.0 million (December 31, 2015 - $2.8 million) is a long-term liability and is reported as the share-based compensation payable.

A) STOCK OPTIONS

The Company has a Stock Option Plan that provides for granting of stock options to officers and certain employees. Stock options vest over a three year period and expire five years after the date of the grant.

The following table summarizes the change in stock options outstanding:

	Number (thousands)	Weighted average exercise price ($)
Issued and Outstanding, December 31, 2014	**511.5**	**29.01**
Granted	**354.7**	**30.10**
Exercised	**(54.9)**	**28.00**
Forfeited	**(18.0)**	**28.93**
Issued and Outstanding, December 31, 2015	**793.3**	**29.57**
Granted	**371.3**	**22.55**
Forfeited	**(116.8)**	**(31.73)**
Issued and Outstanding, September 30, 2016	**1,047.8**	**26.83**

The following weighted average assumptions were used to determine the fair value of stock options granted by the Company during the period:

	September 30, 2016	September 30, 2015
Risk free interest rate	**0.73%**	0.75%
Dividend yield	**5.76%**	4.22%
Expected volatility rate	**36%**	25%
Forfeiture rate	**6.4%**	6.4%
Expected life	**5 yrs**	5 yrs
Weighted average grant price	**$22.55**	$30.81
Fair value per option on grant date	**$3.62**	$3.93

The following table summarizes information regarding stock options outstanding at September 30, 2016:

Range Of Exercise Prices Per Common Share	Number of options outstanding	Weighted average remaining life (years)	Weighted average exercise price for options outstanding ($/share)	Number of options exercisable	Weighted average exercise price for options exercisable ($/share)	Weighted average fair value for options outstanding ($/share)
$22.50-$28.00	**786,355**	**3.44**	**25.52**	**238,636**	**28.00**	**3.74**
$30.80-$30.88	**261,404**	**3.41**	**30.81**	**78,421**	**30.81**	**3.93**

The following table summarizes information regarding stock options outstanding at December 31, 2015:

Range Of Exercise Prices Per Common Share	Number of options outstanding	Weighted average remaining life (years)	Weighted average exercise price for options outstanding ($/share)	Number of options exercisable	Weighted average exercise price for options exercisable ($/share)	Weighted average fair value for options outstanding ($/share)
$25.90-$28.00	448,352	3.58	27.76	119,318	28.00	3.82
$30.80-$39.03	344,936	4.09	31.93	14,063	39.03	4.24

For the three and nine month periods ended September 30, 2016, administrative expense includes $0.3 million (September 30, 2015 - $0.2 million) and $0.9 million (September 30, 2015 - $1.0 million), respectively, of compensation costs related to stock options.

B) PERFORMANCE SHARE UNITS

PSUs have been granted to officers and entitle the officer to receive upon vesting a cash payment that is equal to the value of one common share of the Company for each PSU held, plus accrued dividends over the period from the date of grant to vesting, or the equivalent number of shares at the election of the Company.

The ultimate value of the PSUs will depend upon the Company's performance relative to predetermined corresponding performance targets measured over a three-year period. Performance is based on the Company's total shareholder return ("TSR"), defined as share price appreciation plus dividends, relative to the TSR for a predetermined performance peer group. Based on this assessment, a range of zero to two times the original PSU grant, at the discretion of the Board of Directors, may be eligible to vest in respect of the three year trailing period being measured.

The following table summarizes information related to the PSUs:

Outstanding PSUs (thousands of units)	**September 30, 2016**	**December 31, 2015**
Outstanding, Beginning of Period	**140.8**	67.8
Granted	**89.4**	84.5
Deemed eligible to vest	**(11.1)**	(16.5)
Forfeited	**(19.7)**	-
Units, in lieu of dividends	**4.4**	5.0
Issued and Outstanding, End of Period	**203.8**	140.8

For the three and nine month periods ended September 30, 2016, the Company recorded a compensation expense of $0.9 million (September 30, 2015 - recovery of $0.1 million) and compensation expense of $1.0 million (September 30, 2015 - $1.2 million), respectively, related to outstanding PSUs. The market common share price used in the PSU fair value calculation at September 30, 2016 was $26.75 (September 30, 2015 - $25.36). The remaining weighted average life is 1.6 years.

C) RESTRICTED SHARE UNITS

RSUs have been granted to eligible employees and entitle the employee to receive upon vesting a cash payment that is equal to the value of one common share for each RSU held, plus accrued dividends over the period from the date of grant to vesting, or the equivalent number of shares at the election of the Company.

The following table summarizes information related to the RSUs:

Outstanding RSUs (thousands of units)	**September 30, 2016**	**December 31, 2015**
Outstanding, Beginning of Period	**206.2**	112.3
Granted	**118.6**	130.2
Deemed eligible to vest	**(5.5)**	(9.1)
Forfeited	**(23.0)**	(35.1)
Exercised	**(55.1)**	-
Units, in lieu of dividends	**5.5**	7.9
Issued and Outstanding, End of Period	**246.7**	206.2

For the three and nine month periods ended September 30, 2016, the Company recorded compensation costs of $1.0 million (September 30, 2015 - $0.1 million) and $2.9 million (September 30, 2015 - $1.5 million), respectively, related to outstanding RSUs. The market common share price used in the RSU fair value calculation at September 30, 2016 was $26.75 (September 30, 2015 - $25.36). The remaining weighted average life is 1.0 years.

D) DEFERRED SHARE UNITS

Directors receive an annual compensation amount in DSUs and have the option to receive Board and Committee retainers and fees in the form of DSUs, which vest immediately. These DSUs are equivalent to a common share plus accrued dividends over the period from date of grant and vesting to the date of redemption and are settled in cash. DSUs can only be redeemed following departure from the Company and must be redeemed prior to December 15th of the year following departure. For the three and nine month periods ended September 30, 2016, the majority of the Directors elected to receive their annual Board and Committee retainers and fees in the form of DSUs.

The following table summarizes information related to the DSUs:

Outstanding DSUs (thousands of units)	**September 30, 2016**	**December 31, 2015**
Outstanding, Beginning of Period	**33.0**	22.8
Granted	**30.2**	18.8
Exercised	**-**	(9.8)
Units, in lieu of dividends	**1.7**	1.2
Issued and Outstanding, End of Period	**64.9**	33.0

For the three and nine month periods ended September 30, 2016, the Company recorded a compensation expense of $0.2 million (September 30, 2015 - recovery of $0.2 million) and compensation expense of $1.0 million (September 30, 2015 - $0.4 million), respectively, related to outstanding DSUs.

12. ADMINISTRATIVE EXPENSE

		Three months ended September 30		**Nine months ended September 30**	
		2016	**2015**	**2016**	**2015**
Salaries and benefits		$ **3.2**	$ 3.0	$ **10.9**	$ 10.9
Share-based compensation	*(Note 11)*	**2.4**	-	**5.8**	4.1
Office expense		**1.2**	1.2	**3.8**	3.1
Public company expense		**0.2**	0.2	**0.8**	1.0
Information technology and other		**0.6**	0.6	**1.6**	1.3
Administrative Expense		$ **7.6**	$ 5.0	$ **22.9**	$ 20.4

13. INCOME TAXES

	Three months ended September 30		**Nine months ended September 30**	
	2016	**2015**	**2016**	**2015**
Current tax expense	**$ -**	$ 1.7	**$ -**	$ 15.7
Deferred tax expense (recovery)	**(0.4)**	(2.2)	**(0.2)**	0.9
Income tax expense (recovery)	**$ (0.4)**	$ (0.5)	**$ (0.2)**	$ 16.6

14. CAPITAL MANAGEMENT

The Company's objective when managing its capital structure is to maintain financial flexibility in order to distribute cash to shareholders in the form of dividends after consideration of the Company's financial requirements for its business and future growth opportunities. As a royalty company, PrairieSky does not have capital expenditure commitments, which enhances its financial flexibility.

The Company's capital structure is comprised of shareholders' equity and working capital. The Company's capital structure is managed by taking into account operating activities, dividends paid to shareholders, common share repurchases, taxes, available Credit Facility (Note 15), share issuance costs and other factors. The Company's operating results and capital structure are impacted by the level of development activity by third parties on the Fee Lands and other royalty lands and the resultant royalty revenue, level of costs incurred by the Company and commodity prices.

	As at September 30, 2016	As at December 31, 2015
Shareholders' equity	**$ 2,569.6**	$ 2,710.2
Working capital	**168.1**	211.5

The Company's capital structure is managed through its financial and operating forecast process. The forecast of the Company's future cash flows is based on estimates of production, crude oil, natural gas and NGL prices, production and mineral tax expense, administrative expenses and other investing and financing activities. The forecast is regularly updated based on changes in commodity prices, production expectations and other factors that in the Company's view could impact cash flow.

15. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

A) FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES

The fair values of cash and cash equivalents, accounts receivable and accrued revenue, accounts payable and accrued liabilities and dividends payable approximate their carrying amount due to the short-term maturity of those instruments. Refer to Note 8 for the fair value of the royalty note receivable.

B) RISKS ASSOCIATED WITH FINANCIAL ASSETS AND LIABILITIES

The Company is exposed to financial risks arising from its financial assets and liabilities. Financial risks include market risk (such as commodity price and interest rate risk), credit risk and liquidity risk.

Commodity Price Risk

Commodity price risk is the risk the Company will encounter fluctuations in its future royalty revenue with changes in commodity prices. Commodity prices for crude oil, NGL and natural gas are influenced by macroeconomic events that dictate the levels of supply and demand. The Company does not hedge its commodity price risk.

Interest Rate Risk

Interest rate risk arises from changes in market interest rates that may affect the fair value or future cash flows from the Company's financial assets or liabilities.

At September 30, 2016, the Company had no interest bearing liabilities. The Company's royalty note receivable (Note 8) earns interest at a fixed rate. The cash balance on deposit at September 30, 2016 earns interest at variable rates.

Credit Risk

Credit risk arises from the potential that the Company may incur a loss if a counterparty to a financial instrument fails to meet its obligation in accordance with agreed terms. A substantial portion of the Company's accounts receivable are from royalty agreements with oil and gas industry operators and are subject to normal industry credit risks. The Company's diversified revenue stream limits the size of any one property or industry operator with respect to total receivables. In addition, the Company takes its production in kind to mitigate credit risk as appropriate.

As at September 30, 2016, there were no counterparties whose accounts receivable individually accounted for more than 10% of the total accounts receivable balance. The maximum credit risk exposure associated with accounts receivable and accrued revenue is the total carrying value. For the periods presented, the Company did not have an allowance for doubtful accounts nor did it provide for any doubtful accounts.

Liquidity Risk

Liquidity risk is the risk that the Company will encounter difficulties in meeting a demand to fund financial liabilities as they come due. The Company manages its liquidity risk using cash and debt management programs. The Company has unused capacity under its Credit Facility, described below, for up to $25 million.

The timing of expected cash outflows relating to accounts payable and accrued liabilities of $15.3 million and dividend payable of $13.7 million is less than one year.

On May 18, 2016, the Company elected to voluntarily eliminate the $75 million revolving credit facility (the “Revolving Facility”), such that the total syndicated facility commitment is zero. The Company has retained the unsecured $25 million extendible operating credit facility (the “Credit Facility”). The Credit Facility matures on May 29, 2018.

The Credit Facility includes borrowing options of Canadian prime rate-based advances, U.S. based rate advances, LIBOR loans, bankers’ acceptances and letters of credit, and bears interest on a variable grid based on certain financial ratios, over the prevailing applicable rate for the type of loan. The Credit Facility is unsecured. The Credit Facility is for a two-year terms and, subject to certain requirements, is extendible annually. As at September 30, 2016, the Credit Facility is undrawn.

16. SUPPLEMENTARY INFORMATION

NET CHANGE IN NON-CASH WORKING CAPITAL

	Three months ended September 30		Nine months ended September 30	
	2016	**2015**	**2016**	**2015**
Source (use) of cash:				
Accounts receivable and accrued revenue	**$ 1.6**	$ 16.5	**$ (8.9)**	$ 35.7
Prepaid assets	**0.7**	0.2	**(0.1)**	(0.4)
Income taxes receivable	**12.8**	-	**19.1**	-
Accounts payable and accrued liabilities	**(0.9)**	1.1	**(3.0)**	(10.1)
Income taxes payable	**-**	2.1	**-**	(18.2)
Changes in non-cash working capital	**$ 14.2**	$ 19.9	**$ 7.1**	$ 7.0
Related to operating activities	**14.2**	19.9	**8.0**	7.0
Related to investing activities	**-**	-	**(0.6)**	-
Related to financing activities	**-**	-	**(0.3)**	-
Changes in non-cash working capital	**$ 14.2**	$ 19.9	**$ 7.1**	$ 7.0

SUPPLEMENTARY CASH FLOW INFORMATION

	Three months ended September 30		Nine months ended September 30	
	2016	**2015**	**2016**	**2015**
Interest Paid	**$ -**	$ 0.1	**$ 0.1**	$ 0.3
Interest Received	**0.6**	0.6	**1.8**	1.1
Income Taxes Paid	**-**	(3.0)	**-**	33.9
Income Taxes Received	**12.8**	-	**19.1**	-

17. COMMITMENTS

The following table outlines the Company's commitments as at September 30, 2016:

($ millions)	Expected Future Payments						
(undiscounted)	**2016**	**2017**	**2018**	**2019**	**2020**	**Thereafter**	**Total**
Office lease commitments	**$ 0.3**	**$ 1.4**	**$ 1.4**	**$ 1.4**	**$ 1.4**	**$ 4.7**	**$10.6**

The Company has in place three royalty acquisition agreements with unrelated parties. The agreements expire on December 31, 2016, August 1, 2017, and July 31, 2018 with remaining commitments, subject to numerous conditions, of $0.8 million, $2.7 million, and $5.0 million, respectively.

CORPORATE INFORMATION

BOARD OF DIRECTORS

James M. Estey(1)(2)(3)(4)
Andrew M. Phillips
Sheldon B. Steeves(2)(3)(4)
Margaret A. McKenzie(3)(4)
Grant Zawalsky(2)(4)

(1) Chair of the Board.
(2) Member of the Governance and Compensation Committee. Mr. Estey is the Chair of the Governance and Compensation Committee.
(3) Member of the Audit Committee. Ms. McKenzie is the Chair of the Audit Committee.
(4) Member of the Reserves Committee. Mr. Steeves is the Chair of the Reserves Committee. Mr. Estey is an ex-officio non-voting member of the Reserves Committee.

OFFICERS

Andrew M. Phillips, President & Chief Executive Officer
Cameron M. Proctor, Chief Operating Officer
Pamela Kazeil, Vice President, Finance & Chief Financial Officer
Michelle L. Radomski, Vice-President, Land

AUDITORS

KPMG LLP

BANKERS

Toronto-Dominion Bank
Canadian Imperial Bank of Commerce

TORONTO STOCK EXCHANGE TRADING SYMBOL

PSK

INDEPENDENT RESERVE EVALUATORS

GLJ Petroleum Consultants Ltd.
Sproule Associates Limited

TRANSFER AGENT

TMX Equity Transfer Services

ABBREVIATIONS

bbls – barrels
bbls/d – barrels per day
boe – barrels of oil equivalent (6mcf = 1bbl)
boe/d – barrels of oil equivalent per day
mcf – thousand cubic feet
mcf/d – thousand cubic feet per day
mmcf – million cubic feet
mmcf/d – million cubic feet per day
NGL – natural gas liquids
WTI – West Texas Intermediate

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