DESCRIPTION OF THE COMPANY

The following Management's Discussion and Analysis ("MD&A") of financial condition and results of operations for Virginia Hills Oil Corp. ("Virginia Hills" or the "Company") is a review of the operations, current financial position and condition for the years ended December 31, 2015 and 2014, and should be read in conjunction with the Company's audited consolidated financial statements and related notes for the year ended December 31, 2015. The financial statements have been prepared in Canadian dollars, in accordance with International Financial Reporting Standards ("IFRS"). Tabular amounts are in thousands of dollars, except where indicated otherwise, and oil and gas volumes, reserves and related performance measures are presented on a working-interest, before-royalties basis. This MD&A and the audited annual consolidated financial statements of Virginia Hills have been prepared by management and approved by the Company's Board of Directors as at March 30, 2016.

Virginia Hills is a Calgary, Alberta based petroleum and natural gas exploration, production and development company, with operations in the Canadian province of Alberta. Virginia Hills is a public company, incorporated and domiciled in Alberta and its shares trade on the TSX Venture Exchange ("TSX-V") under the symbol "VHO".

READER ADVISORIES

This MD&A contains financial measures that are not defined under IFRS and forward looking statements. Readers are cautioned that the MD&A should be read in conjunction with the Company's disclosure under "Non-GAAP Measures", "Forward-Looking Information" and "Future Oriented Financial Information" included at the end of this MD&A.

51-101 Advisory (BOE Conversion)

In accordance with National Instrument 51-101, Standards for Disclosure of Oil and Gas Activities ("NI 51-101"), petroleum and natural gas reserves and volumes are converted to an equivalent measurement basis referred to as a "barrel of oil equivalent" ("boe") on the basis of 6 thousand cubic feet of natural gas equal to 1 barrel of oil. This conversion is based on an energy equivalency conversion method applicable at the burner tip and does not represent a value equivalency at the wellhead. ***Readers are cautioned that boe may be misleading, particularly if used in isolation.***

CAPITAL REORGANIZATION

On April 15, 2015 (the "Effective Date"), the Company completed a corporate reorganization as part of a plan of arrangement (the "Arrangement") pursuant to section 193 of the *Business Corporations Act* (Alberta). Pursuant to the Arrangement, the common shareholders ("Pinecrest Shareholders") of Pinecrest Energy Inc. ("Pinecrest") became the shareholders of the Company and approximately 90% of Pinecrest's Alberta oil and gas assets, and substantially all of the other assets and liabilities were transferred to the Company. The common shares of Pinecrest were then sold to Cardinal Energy Ltd. ("Cardinal") for cash proceeds of $23.5 million, of which $1.0 million was placed into escrow to satisfy certain closing adjustments. The $1.0 million of cash in escrow is reported as restricted cash on the balance sheet as a current asset at December 31, 2015. The escrow period expires August 15, 2016. In addition to the upfront proceeds, the Company is entitled to receive an additional payment of $5.0 million if, during the period from April 16, 2015 to April 26, 2016, a front-month hedge is made available to Cardinal by one or more financial institutions, financial intermediate or credit branches at a price of $US65 WTI per barrel of oil for a minimum of twelve months. Should Cardinal establish a front-month hedge, the value of the proceeds will be known and the full amount will be recorded at such time.

As part of the Arrangement, Pinecrest Shareholders exchanged their shares on a basis of 100 shares for one common share of the Company ("Common Share"), and received eight (8) arrangement rights for each Common Share issued under the Arrangement. Each arrangement right entitled the Shareholders to acquire one (1) Common Share at $0.25 per share and expired on May 15, 2015. A total of 3,412,175 arrangement rights were exercised for gross proceeds of $0.9 million. All outstanding common share purchase warrants, performance warrants and share incentive plan awards of Pinecrest were cancelled for a nominal amount on the Effective Date. On April 15, 2015, a total of $22.6 million from the cash proceeds and exercise of the arrangement rights were used to repay outstanding bank debt. In connection with closing of the Arrangement, the Company organized a new bank facility with the senior lenders.

On the Effective Date, Virginia Hills and Pinecrest were considered to be under common control as the Virginia Hills shareholders are the former Pinecrest Shareholders, and therefore, the business of Virginia Hills is controlled by the same shareholders immediately before and after the Arrangement. The accounting for common control entities is not addressed under *IFRS 3 – Business Combinations*, which requires an entity to develop an accounting policy. Management has determined that the predecessor values method of accounting is the most appropriate, whereby the predecessor carrying values of Pinecrest are reported, without any step-up in fair value, if any. The difference between any consideration and the aggregate carrying value of the assets and liabilities acquired is recorded as a reserve from the common control transaction in shareholders' equity, if applicable. As such, the transaction was accounted for as a capital reorganization of Pinecrest, and comparative financial information of Virginia Hills is reported as a continuation of Pinecrest's historical accounting records. Virginia Hills, as a continuation of Pinecrest, reports its full interest in the properties until disposed on the Effective Date, and recorded a gain on the disposition of the Pinecrest shares during the second quarter of 2015 of $13.9 million. Unless otherwise indicated, all information presented prior to the Effective Date is that of Pinecrest.

A copy of the Arrangement Agreement and related documents are available on the Canadian Securities Administrators' System for Electronic Distribution and Retrieval ("SEDAR") website at www.sedar.com, under the Pinecrest Energy Inc. profile, or by contacting the Company at Suite 1500, 202-6th Avenue SW, Calgary, Alberta, T2P 2R9.

BUSINESS ACQUISITION

On April 27, 2015, the Company acquired all the issued and outstanding common shares of Dolomite Energy Inc. (the "Acquisition"), a private oil and gas producer by way of an amalgamation with its wholly owned subsidiary (the "Acquisition"). The Acquisition complements the Company's existing operations in the Red Earth area, with approximately 100 barrels of oil per day, and included approximately $51 million of tax pools.

The purchase price of $0.6 million was settled by the issuance of 10,600 common shares at a fair value of $0.48 per common share, 4.0 million common share purchase warrants with a fair value of $0.1592 per warrant, and the assumption of $11.5 million of net debt. Upon closing of the Acquisition, the Company's subsidiary entered into an amended and restated credit facility totaling $11.0 million. Results of operations from the Acquisition have been included in the annual consolidated financial statements from April 27, 2015.

OPERATIONS UPDATE AND OUTLOOK

Low commodity prices during 2015 presented a challenging business environment for the Canadian oil and gas industry, as the benchmark oil price of WTI decreased 48% from $US93.00 per barrel in fiscal 2014 to average $US48.80 per barrel in 2015. Historically, Virginia Hills' realized commodity prices have tracked the Canadian benchmark oil price due to its corporate production weighting of 97% light oil and natural gas liquids. The fourth quarter and annual 2015 realized average prices decreased to $67.57 per boe and $59.38, compared to $70.74 per boe and $88.31 per boe realized in the comparable periods of 2014, decreases of 4% and 33%, respectively. However, during 2015, the Company had physical, fixed price commodity contracts in place, which mitigated a decrease in revenues, had the Company been fully exposed to fluctuations in benchmark prices. If the commodity contracts had not been in place, the Company's realized prices would have been $52.94 per boe and $53.38 per boe for the fourth quarter and year ended December 31, 2015. The Company's realized commodity prices are expected to track the benchmark oil prices for 2016, as there are no price risk contracts currently in place. The Company continues to monitor the forward price expectations, and may enter into future contracts to protect the Company's cash flows.

Production volumes for the quarter and year ending December 31, 2015 averaged 1,464 boe/d and 1,515 boe/d, respectively, representing declines of 22% and 23% from 2014 levels. Production for the year was negatively impacted by both the sale of approximately 100 boe/d of net production which occurred in the second quarter and the shut in of 40 boe/d of uneconomic production throughout the year. In addition, the Company experienced a pipeline failure late in the fourth quarter of 2015 which resulted in gross production of approximately 200 boe/d net being shut in temporarily while clean-up and repair operations took place.

This negatively impacted the average fourth quarter daily production by approximately 43 boe/d. Approximately half of the shut in production related to the pipeline failure, came back online by January 1, 2016 (105 boe/d of oil production) with the remaining volumes back on line by March 1 2016. The Company is expecting its first quarter volumes to average between 1,425 boe/d and 1,475 boe/d with production rates exiting the first quarter of 1,550 to 1,600 boe/d (97% light oil and NGLs).

Total operating expenses (which include production and transportation costs) were $3.7 million and $15.0 million for the fourth quarter and year ended December 31, 2015 compared to $5.3 million and $20.7 million in the comparable periods of 2014, representing reductions of 30% and 28% respectively. On a per unit basis, total operating expenses dropped 9% and 6%, respectively in the fourth quarter of 2015 and year to date from 2014 levels to $27.67 per boe and $27.06 per boe, respectively. Year to date expense reductions were offset, in part, by net costs of approximately $0.8 million associated with the clean-up of emulsion pipeline failures and regulatory compliance work in 2015. These costs had a negative impact on operating costs of approximately $1.38 per boe for the year ended December 31, 2015. The Company anticipates having a similar level of expenditures on these items in the first half of 2016, however, as of March 1, 2016, the Company has suspended operations on approximately 16 kms of pipeline in the Red Earth area which it has deemed to have unacceptable environmental and regulatory risk. The Company does not anticipate a material negative impact on its cost structure from these pipeline suspensions as none of these pipelines facilitate a material amount of production. In addition the Company has the ability to repair and return these pipelines to operations at marginal cost as future development in the area dictates.

Virginia Hills' field netback for the fourth quarter of 2015, was $32.45 per boe compared to $26.21 per boe for the fourth quarter of 2014. Annual 2015 field netbacks were $26.61 per boe compared to $43.22 per boe in 2014. The decrease in netbacks realized in 2015 due to a decrease in production and commodity prices of 23% and 33%, respectively.

Through the optimization of its extensive Red Earth water flood project area, Virginia Hills believes it is positioned to add additional production and reserves with little incremental capital over the next 12 to 24 month period. These low cost water flood additions are expected to allow the Company to operate a capital program that is significantly below its free cash flow level providing the opportunity for meaningful debt reduction and value creation for its shareholders. The Company maintains a risked and total unrisked undeveloped light oil horizontal drilling inventory in its Red Earth core area of 108 net wells and 176 net wells, respectively, representing over 15 years of potential drilling activity. With this undeveloped light oil drilling inventory and its substantial operated water flood infrastructure foot print in the Red Earth area, Virginia Hills remains uniquely positioned to enter a more meaningful drilling and production growth phase when commodity prices return to more historical levels.

FINANCIAL AND OPERATIONAL HIGHLIGHTS

December 31	Three months ended		Year ended	
	2015	2014 (1)	2015	2014 (1)
FINANCIAL				
Petroleum and natural gas sales	9,101	12,269	32,839	63,683
Funds flow from operations (2)	2,573	2,579	6,075	20,061
Per share - basic	0.13	1.19	0.43	8.97
Per share - diluted	0.13	1.19	0.43	8.97
Net loss	18,254	176,473	17,914	175,725
Per share - basic	0.93	81.24	1.28	80.90
Per share - diluted	0.93	81.24	1.28	80.90
Capital expenditures (3)	237	4,114	10,330	8,745
Net debt (2)(4)	108,520	115,502	108,520	115,502
Common Shares Outstanding (1)				
Weighted average – basic	19,724	2,172	13,984	2,172
Weighted average – diluted	19,724	2,188	13,984	2,188

OPERATING				
Number of days	*92*	*92*	*365*	*365*
Production				
Oil and NGL (bbl/d)	1,411	1,831	1,464	1,915
Natural gas (mcf/d)	320	322	308	364
Total production (boe/d)	1,464	1,885	1,515	1,976
Average realized price (5)				
Oil and NGL ($/bbl)	69.90	72.78	61.26	91.06
Natural gas ($/mcf)	1.05	0.16	0.93	0.33
Netback per boe ($)(2)				
Petroleum and natural gas sales	67.57	70.74	59.38	88.31
Royalties	(7.45)	(14.07)	(5.71)	(16.41)
Production and transportation expenses	(27.67)	(30.51)	(27.06)	(28.68)
Field netback (2)	32.45	26.16	26.61	43.22
Realized gain (loss) on derivative financial instruments	-	4.21	-	(1.17)
Operating netback (1)	32.45	30.37	26.61	42.05
Drilling				
Gross wells	-	-	2.0	-
Net wells	-	-	2.0	-

(1) Shares and per share amounts for comparative periods reflect the 100:1 share consolidation as though the consolidation took place at the beginning of the earliest period.
(2) Non-GAAP measure.
(3) Capital expenditures exclude amounts paid for acquisitions.
(4) Net debt is defined as current assets minus current liabilities, plus outstanding long term bank debt.
(5) Before the effects of derivative financial instruments, but includes gains or losses on fixed price, physical contracts that are not considered derivative instruments.

PRODUCTION

December 31	**Three months ended**			**Year ended**		
	2015	**2014**	**% Change**	**2015**	**2014**	**% Change**
Production						
Number of days	*92*	*92*		*365*	*365*	
Crude oil (bbls/d)	1,375	1,775	(23)	1,417	1,852	(23)
NGL (bbls/d)	36	56	(36)	47	63	(25)
Natural gas (mcf/d)	320	322	(1)	309	364	(15)
Total (boe/d)	**1,464**	**1,885**	**(22)**	**1,515**	**1,976**	**(23)**
Crude oil & NGL (%)	96	97	(1)	97	97	-
Production by Region						
Greater Red Earth	1,364	1,885	(28)	1,426	1,976	(28)
South Alberta	100	-	100	89	-	100
Total (boe/d)	1,464	1885	(22)	1,515	1,976	(23)

Production volumes for the quarter and year ended December 31, 2015 averaged 1,464 boe/d and 1,515 boe/d, respectively, representing declines of 22% and 23% from 2014 levels. Production for the year was negatively impacted by the sale of approximately 100 boe/d of production, which occurred in the second quarter of the year as part of the Arrangement and the shut in of 40 boe/d of uneconomic production throughout the year.

In addition, the Company experienced a pipeline failure late in the fourth quarter of 2015 which resulted in the temporary shut-in of approximately 200 bbl/d of oil production to permit clean-up and repair operations to take place. This negatively impacted the average fourth quarter daily production by approximately 43 bbl/d. Approximately half of the shut in production related to the pipeline failure came back online by January 1, 2016 (100 bbl/d of oil production), with the remaining volumes came back on line prior to the beginning of March 2016 (100 bbl/d of oil production).

The Company is expecting its first quarter 2016 volumes to average between 1,425 boe/d and 1,475 boe/d with production rates exiting the first quarter of 1,550 to 1,600 boe/d (97% light oil and NGL's).

REVENUE

December 31	Three months ended			Year ended		
	2015	2014	% Change	2015	2014	% Change
Crude oil sales	9,071	12,207	(25)	32,555	63,359	(49)
NGL sales	-	58	(99)	180	280	(35)
Natural gas sales	30	4		104	44	>100
Total Sales	**9,101**	**12,269**	**(26)**	**32,839**	**63,683**	**(48)**
Average Realized Prices						
Crude oil ($/bbl) [(1)]	71.79	74.75	(4)	62.94	93.73	(33)
NGL ($/bbl)	-	11.19	(100)	10.55	12.20	(13)
Natural gas ($/mcf)	1.09	0.16	>100	0.93	0.33	>100
Total ($/boe)	**67.57**	**70.74**	**(4)**	**59.38**	**88.31**	**(33)**
Crude oil physical hedge ($/bbl)[(1)]	15.98	-	100	6.44	-	100

[(1)]Realized gain on a physical commodity contracts for the quarter and year to date (from May 1, 2015 to Dec 31, 2015), based on delivery of 34,611 barrels per month of oil, which fixed the price based on United States Dollar ("USD"). This price is included in the average realized prices for crude oil for the three months and year ended December 31, 2015. See "Risk Management" below.

December 31	Three months ended			Year ended		
	2015	2014	% Change	2015	2014	% Change
Benchmark pricing						
Crude oil – WTI (US$/bbl)	42.18	73.15	(42)	48.80	93.00	(48)
Crude oil – Cdn light sweet (Cdn$/bbl)	52.55	75.33	(30)	57.42	94.23	(39)
Natural gas – AECO spot (Cdn$/mcf)	2.47	3.63	(32)	2.70	3.80	(29)
Exchange Rate – (US/Cdn)	0.749	0.880	(14)	0.783	0.905	(13)

Prices received for crude oil and natural gas production directly impact the Company's earnings, cash flow from operations and financial position. Sales were $9.1 million for the fourth quarter of 2015 compared to $12.3 million for the fourth quarter of 2014. Sales for the year ended December 31, 2015 were $32.8 million, a decrease of 48% from $63.7 million reported for the year ended December 31, 2014. During the second quarter of 2015, Virginia Hills entered into a series of physical commodity contracts which fixed the price received (before quality and transportation adjustments) in USD from May to December 2015 on a total of 34,611 barrels per month (See "Risk Management" below). These contracts are not considered financial instruments and any price difference to the benchmark oil price is recorded as part of the realized price for oil. Consequently, during the fourth quarter of 2015, Virginia Hills reported approximately $1.9 million ($15.98/bbl) and $3.2 million ($6.44/bbl) in additional oil revenues for the fourth quarter and year ended December 31, 2015, respectively.

Decreased sales for the quarter and the year are due to lower production volumes and significantly lower realized commodity prices for 2015 compared to 2014.

Virginia Hills' realized average oil price for the fourth quarter of 2015 was $71.79 per barrel, compared to $74.75 per barrel during the same period in 2014, and was $62.94 per barrel for the year ended December 31, 2015 compared to $93.73 per barrel realized in 2014. Prices received by Virginia Hills are based on the Canadian Light Sweet Crude price, adjusted for quality differentials, and have historically tracked the Canadian benchmark price at approximately 98%. Realized oil prices for the fourth quarter of 2015 and year ended December 31, 2015 include prices associated with physical delivery contracts, which fixed the price received based on USD, for a fixed amount of volume delivered per month. The Company does not currently have any such contracts in place for 2016.

Virginia Hills has a marketing arrangement to sell its gas and NGLs at the Evi plant gate, which attracts prices lower than benchmark price, but eliminates third party gas transportation and processing expenses.

Risk Management

Virginia Hills' management and its Board of Directors have established a risk management policy with the objective to reduce volatility in financial results, protect the Company's investment in its capital expenditure program and stabilize cash flow against the unpredictable commodity price environment. Exposures inherent in fluctuations in the price of crude oil and natural gas, the USD/Cdn dollar exchange rate and interest rates are monitored by management and the Board of Directors on a regular basis. Virginia Hills' risk management policy limits the term of any price risk contract to a maximum term of 24 months, up to a maximum of 70% of base production after royalties.

Virginia Hills accounts for commodity price risk contracts that are considered financial instruments, on a mark-to-market basis at each reporting period, with all fluctuations in value, realized or unrealized reported directly in the Statements of Loss and Comprehensive Loss. Virginia Hills recorded a $0.8 million gain and a $0.2 million loss on the oil price contracts that were outstanding during the fourth quarter and year ended December 31, 2014 respectively. The Company did not have any oil price risk contracts that were considered financial instruments outstanding during the year ended December 31, 2015.

December 31	**Three months ended**			**Year ended**		
	2015	**2014**	**% Change**	**2015**	**2014**	**% Change**
Realized loss (gain)	-	(730)	(100)	-	846	(100)
Unrealized loss (gain)	-	(109)	(100)	-	(615)	(100)
Total loss (gain)	-	**(839)**	(100)	-	**231**	(100)

Commodity contracts which commit the delivery of volumes are not considered financial instruments, and are not marked to market at each period end, rather any gain or loss on the contract pricing is directly included in sales revenue for the period. During the second quarter of 2015, the Company entered into commodity contracts which committed volumes for delivery at fixed prices. These contracts resulted in additional revenue of $1.9 million ($15.98/bbl) and $3.2 million ($6.44/bbl) being recognized directly in sales revenue for the fourth quarter and year ended December 31, 2015, respectively.

The following physical delivery contracts were outstanding during the year ended December 31, 2015 and 2014:

Year of Contract	Type of Contract	Term	Volume (bbl/d)	Price [3] (Cdn$/bbl)	Price[3] (US$/bbl)	Index
Commodity contracts [1]						
2015	Oil delivery	May 1, 2015 – Jun 30, 2015	1,135	-	$55.10	-
2015	Oil delivery	Jul 1, 2015 - Sep 30, 2015	1,128	-	$53.47	-
2015	Oil delivery	Oct 1, 2015 – Dec 31, 2015	1,128	-	$53.22	-
Price risk contracts [2]						
2014	Swap	Jan 2014 – Dec 2014	500	$98.79	-	WTI
2014	Collar	Jan 2014 – Jun 2014	500	$95.00 – $109.50	-	WTI

(1) Physical commodity contracts are not considered financial risk management instruments and are not marked to market at the period end. These contracts have a fixed price, payable in USD, adjusted for quality and transportation.

(2) Commodity price risk contracts are considered economic hedges. The Company does not apply hedge accounting; consequently, the contracts are revalued to fair value at the end of each reporting date resulting in unrealized gains and losses recognized directly into the Statements of Loss and Comprehensive Loss. When the contracts are settled the realized gains or losses are recorded. Per unit metrics include only the realized gains or losses.

(3) Prices are weighted average for the term.

ROYALTY EXPENSE

December 31	Three months ended			Year ended		
	2015	2014	% Change	2015	2014	% Change
Royalty expense	1,004	2,441	(59)	3,157	11,830	(73)
As a percentage of sales	11	20	(9)	9	19	(10)
$ Per boe	7.45	14.07	(47)	5.71	16.41	(65)

Royalty expense includes royalties paid to provincial governments, freehold land owners and overriding royalty owners. Royalties were $1.0 million (11% of revenues) for the fourth quarter of 2015 compared to $2.4 million for the fourth quarter of 2014. Royalties for the year ended December 31, 2015 were $3.2 million (9% of revenues) compared to $11.8 million in 2014. Royalties are lower in 2015 due to the decrease in production and realized pricing.

Virginia Hills pays the majority of its royalties to the Government of Alberta, which has a favourable royalty environment for newly drilled horizontal oil wells, in which the wells pay a maximum royalty rate of 5% on production up to a maximum of 30 months, or 70,000 barrels, whichever comes first, and is a function of the total measured depth of the horizontal well. During 2014, the Company's royalty rate as a percentage of revenue was greater than 5% due to a number of wells that were off royalty holiday. The royalty rate as a percentage of revenue for 2015 is lower than 2014 due to the decrease in reference pricing and lower volumes for the quarter and year ended December 31, 2015.

OPERATING EXPENSE

Production expenses are comprised of costs to operate the wells, including emulsion and water trucking chemicals and minor work over costs. Transportation expenses are incurred for services related to moving production to sales points, and include clean oil trucking and pipeline tariffs.

December 31	Three months ended			Year ended		
	2015	2014	% Change	2015	2014	% Change
Production expense	3,314	4,730	(30)	13,100	18,610	(30)
Transportation expense	413	562	(27)	1,864	2,070	(10)
Total operating expense	**3,727**	**5,292**	**(30)**	**14,964**	**20,680**	**(28)**
$ Per boe, Production	24.60	27.27	(10)	23.69	25.81	(8)
$ Per boe, Transportation	3.07	3.24	(5)	3.37	2.87	17
$ Per boe	27.67	30.51	(9)	27.06	28.68	(6)

Production Expenses

Production expenses were $3.3 million ($24.60 per boe) in the fourth quarter of 2015 compared to $4.7 million ($27.27 per boe) recorded in the fourth quarter of 2014 and were $13.1 million ($23.69 per boe) for the year ended December 31, 2015 compared to $18.6 million ($25.81 per boe) in 2014. Production expenses decreased by 30% in the fourth quarter and for the year ended December 31, 2015, respectively, due to various operational efficiency initiatives and a decline in base production rates.

Year to date expense reductions were offset, in part, by non-recurring costs of approximately $0.8 million related to the clean-up of certain emulsion pipeline failures and environmental compliance work. These costs had a negative impact on operating costs of $1.38 per boe for the year ended December 31, 2015. The Company anticipates having a similar level of expenditures on these items in the first half of 2016, as clean up and repair operations are completed on the pipelines in question. In addition, during first quarter of 2016 the Company has completed the suspension of operations on approximately 16 km of operated pipelines in the Red Earth area which it has deemed as unacceptable environmental and regulatory risk. None of these pipelines transport a material amount of production and all of the pipelines can be repaired and brought back on production at marginal cost when the development requirements in the area require the capacity. Consequently Virginia Hills does not anticipate a material negative impact on its cost structure related to the pipeline suspensions.

Transportation Expenses

Transportation expenses for the quarter and year ended December 31, 2015 were $0.4 million and $1.9 million respectively and were lower compared to prior year periods mainly due to decreased volumes. Costs on a per unit basis have increased for the year ended December 31, 2015 due to the decrease of average production volumes compared to 2014.

OTHER OPERATING INCOME

December 31	Three months ended			Year ended		
	2015	2014	% Change	2015	2014	% Change
Other operating income	189	154	23	657	642	2
$ Per boe	1.40	0.75	86	1.19	0.89	34

Other operating income is comprised primarily of road use fee income, third party-processing fees and emulsion gathering fees, and have increased in 2015 due to review of existing road use agreements and adjustments to applicable rates.

EXPLORATION EXPENSE AND IMPAIRMENT

December 31	Three months ended			Year ended		
	2015	2014	% Change	2015	2014	% Change
Exploration expense	749	17,738	(96)	813	17,738	(95)
Exploration impairment	86	61,427	(99)	86	61,427	(99)
Total Exploration Expense	**835**	**79,165**	**(99)**	**899**	**79,165**	**(99)**
$ Per boe	6.20	465.43	(99)	1.63	109.78	(99)

Exploration expense includes costs associated with undeveloped lands that expire in the period and geological, geophysical and exploratory drilling expenditures that were incurred but determined not to be commercially viable to the Company. Virginia Hills recorded $0.7 million in exploration expense during the quarter ended December 31, 2015 which represented 45,845 net acres of undeveloped land that expired, or is expected to expire within the next year. During the year ended December 31, 2015, exploration expense of $0.8 million was recorded (December 31, 2014: $17.7 million (49,261 net acres)). In addition, an impairment loss of $0.1 million was recognized in the year ended December 31, 2015 to adjust the undeveloped land costs to approximate the expected net realizable value of the remaining 137,631 net undeveloped acres of land (December 31, 2014: a total of $61.4 million in impairment loss was recorded).

DEPLETION, DEPRECIATION & IMPAIRMENT EXPENSE

December 31	Three months ended			Year ended		
	2015	2014	% Change	2015	2014	% Change
Depletion & depreciation expense	3,093	6,897	(55)	14,387	22,985	(37)
Impairment, assets held for sale	485	-	100	485	-	100
Impairment property, plant & equipment	15,889	92,993	(83)	16,343	92,993	(82)
Depletion, depreciation & impairment	**19,467**	**99,890**	**(81)**	**31,215**	**115,978**	**(73)**
$ Per boe						
Depletion & depreciation expense	22.51	39.77	(43)	26.01	31.87	(18)
Impairment	121.57	536.16	(77)	30.43	128.96	(76)
Total	144.08	575.93	(75)	56.44	160.83	(65)

Depletion & depreciation

Depletion and depreciation expense decreased to $3.1 million and $14.4 million in the fourth quarter and year ended December 31, 2015 respectively. The decrease in depletion and depreciation expense is attributable to a lower cost base, due to sale of approximately 10% of the Company's assets and impairments in 2014 and lower production volumes.

Impairment

At December 31, 2015, Virginia Hills reclassified certain capital spare parts assets from property, plant and equipment to assets held for sale, and recognized an impairment of $0.5 million. In addition, The Company assessed its property, plant and equipment for impairment which resulted in an impairment loss of $16.3 million relating to the Company's Alberta-based oil cash generating unit ("CGU"). The 2014 impairment was also associated with the oil CGU.

To determine impairment, the Company compares the CGU's carrying costs to the CGU's estimated fair value less costs of disposal. The estimated fair value of the CGU was determined using future cash flows adjusted for risks specific to the CGU, discounted using an after-tax discount rate of 11%. A 1% increase in the discount rate would result in an additional $5.6 million of impairment, and a 10% decrease in operating cash flow would result in approximately an additional $9.1 million of impairment. The 2015 impairment loss was the result of adjustments to

future prices, whereas the 2014 impairment loss related to technical revisions and price and cost adjustments. A one percent increase in the discount rate would have increased the impairment loss in 2015 by approximately $5.6 million. The 2014 impairment loss of $93.0 million was based on a discount rate of 10%, and was due to technical revisions and changes in the future prices and costs as assigned at December 31, 2014 by the Company's independent reserve engineers.

GENERAL AND ADMINISTRATIVE EXPENSE ("G&A")

December 31	Three months ended			Year ended		
	2015	2014	% Change	2015	2014	% Change
Gross G&A	570	1,449	(61)	4,333	6,011	(28)
Overhead recoveries & capitalized G&A	(150)	(346)	(57)	(1,015)	(1,318)	(23)
Net G&A	420	1,103	(62)	3,318	4,693	(29)
Share based payments	27	(579)	>100	273	(12)	>100
Total G&A	**447**	**524**	**(14)**	**3,591**	**4,681**	**(23)**
$ Per boe, net G&A	3.42	6.37	(46)	6.00	6.51	(8)
$ Per boe, share based payments	0.21	(3.34)	>100	0.50	(0.02)	>100
$ Per boe	3.63	3.03	19	6.50	6.49	-

Net G&A costs were $0.4 million for the fourth quarter of 2015 compared to $1.1 million incurred in 2014. Fourth quarter costs were lower than the prior year mainly due to decreased legal and advisory costs, salaries and corporate office rent, resulting from the Arrangement in the second quarter of 2015. Net G&A was $3.3 million for the year ended December 31, 2015, a decrease of 29%, compared to $4.7 million in 2014, due to savings in legal expenses, staff reductions and reductions in software licensing costs. Overhead recoveries and capitalized G&A were lower in the fourth quarter and for the year ended December 31, 2015 due to cost savings realized on operating and capital costs, which directly impact overhead recoveries.

Share-based payment expense was $27 thousand in the fourth quarter of 2015 compared to a recovery of $0.6 million for the fourth quarter of 2014 and was $0.3 million for the year ended December 31, 2015 compared to recoveries of $12 thousand in 2014. Expenses were higher during the quarter and year ended December 31, 2015 as they reflect the fair value amortization of issued and outstanding stock options which were issued in the second quarter of 2015. Share-based payment expense was in a recovery position for the fourth quarter and year ended December 31, 2014, due to the forfeiture of unvested performance awards.

TRANSACTION COSTS

December 31	Three months ended			Year ended		
	2015	2014	% Change	2015	2014	% Change
Transaction costs	-	519	(100)	4,142	569	>100
$ Per boe	-	2.99	(100)	7.49	0.70	>100

During 2015, Virginia Hills incurred transaction costs of $4.1 million which relate to the Arrangement of Pinecrest ($2.4 million) and the acquisition of Dolomite ($1.7 million). Transaction costs incurred in the fourth quarter, and year ended December 31, 2014 related to the Arrangement. These costs include executive change of control pay, financial advisory services, and legal expenditures and are typically non-recurring in nature.

FINANCE EXPENSE

December 31	Three months ended			Year ended		
	2015	2014	% Change	2015	2014	% Change
Interest (cash)	1,526	1,738	(12)	5,975	6,209	(4)
Interest, amortization (non-cash)	349	-	100	1,475	72	>100
Total interest expense	1,875	1,738	8	7,450	6,281	19
Fair value of embedded derivative on convertible debt (non-cash)	(260)	-	100	(260)	-	100
Accretion (non-cash)	162	166	(2)	632	635	(-)
Total finance expense	**1,777**	**1,904**	**(7)**	**7,822**	**6,916**	13
$ Per boe, Interest	11.35	10.02	13	10.81	8.61	26
$ Per boe, Interest, amortization	2.59	-	100	2.67	0.10	>100
$ Per boe, Accretion on convertible debt	(1.93)	-	100	(0.47)	-	100
$ Per boe, Accretion	1.20	0.96	25	1.14	0.88	30
$ Per boe	13.21	10.98	20	14.15	9.59	48

Interest Expense (see Liquidity and Capital Resources)

Interest expense includes: cash interest paid on the credit facilities; standby fees, which are based on unused available credit; and amortization of deferred financing charges incurred to establish the credit facilities. Total interest expense for the fourth quarter of 2015 was $1.9 million compared to $1.7 million for the fourth quarter of 2014. Interest expense for the year ended December 31, 2015 was $7.5 million compared to $6.3 million during the same period in 2014. Cash interest expense was lower in both the quarter and year ended December 31, 2015 mainly due to reduction of outstanding debt by $22.6 million upon closing of the Arrangement on April 15, 2015, and a reduction in the prime borrowing rate in mid-July from 2.85% to 2.7% per annum. On a per boe basis, interest expense has increased due a decrease in the average daily production.

The Company had two credit facilities in place; a $97.0 million senior credit facility and an $11.0 million credit facility. The senior credit facility bears interest at prime plus a sliding scale margin, which is based on the Company's trailing debt to earnings before interest, taxes, depletion and amortization ("EBITDA") ratio, ranging from 1% to 3%. In addition a 1% standby fee is paid on the portion of the unused credit facility. The second credit facility bears interest at prime plus 3%. At December 31, 2015, the interest rate on both facilities was 5.7%.

Non-cash interest charges include the amortization of deferred financing costs incurred to establish the Company's credit facilities and are greater for the quarter and year ended December 31, 2015 reflecting costs incurred to establish the new credit facilities for Virginia Hills, and the amended credit facility for Dolomite. It was determined that the fair value of the embedded derivative on the convertible subsidiary debt at December 31, 2015 was $nil, which resulted in a credit of $0.3 million to financing costs.

Accretion expense

Accretion expense was $0.2 million and $0.6 million for the quarter and year ended December 31, 2015, and has not changed significantly from 2014. Accretion expense on a per boe basis in 2015 has increased compared to 2014, reflecting a decrease in the average daily production. At December 31, 2015 the credit-adjusted risk free rate was 7.6% and the inflation rate was 2.0% (December 31, 2014: 7.8% and 2.0% respectively).

GAIN ON DISPOSITION

December 31	Three months ended			Year ended		
	2015	2014	% Change	2015	2014	% Change
Gain on disposition	-	-	-	13,882	-	100
$ Per boe	-	-	-	25.10	-	100

During the second quarter of 2015, Virginia Hills completed the Arrangement whereby all of the shares of Pinecrest were sold to Cardinal for proceeds of $23.5 million, which resulted in a gain of $13.9 million (see Capital Reorganization).

INCOME TAXES

Virginia Hills recorded a deferred tax recovery of $0.5 million in the year ended 2015, which represents reversal of the premium for flow-through shares associated with $1.9 million of expenditures that were incurred during 2015.

At December 31, 2015, the Company's estimated consolidated tax pools at December 31, 2015 are $173.6 million, which are available to be applied against future income for tax purposes. Based on the available pools, and current commodity prices Virginia Hills does not expect to be taxable in 2016.

	Deduction Rate	December 31, 2015
Canadian oil and gas property expense	10%	$ 97,306
Canadian development expense	30%	1,265
Canadian exploration expense	100%	20,212
Undepreciated capital cost	Ranges 8% - 25%	27,782
Share and debt issue costs	20% straight line	1,647
Cumulative eligible capital	7%	1,581
Non-capital loss carry forward		23,194
Total		**$ 173,633**

Non-capital losses of $23.2 million may be carried forward to reduce future income taxes payable and will begin to expire as follows:

2025	$ 842
2026	974
2027	1,062
2028	1,757
2029 and beyond	18,559
Total non-capital losses	$ 23,194

NET LOSS

December 31	Three months ended			Year ended		
	2015	2014	% Change	2015	2014	% Change
Net loss	**18,254**	**176,473**	**(90)**	**17,914**	**175,725**	**(90)**
$ Per share, basic [1]	0.93	81.24	(99)	1.28	$80.90	(98)
$ Per share, diluted [1]	0.93	81.24	(99)	1.28	$80.90	(98)

[1] *The weighted average shares outstanding and per share amounts prior to April 15, 2015 have been related to reflect the 100:1 share consolidation.*

Virginia Hills' recorded a net loss of $18.3 million in the fourth quarter of 2015 compared to net loss of $176.5 million recorded in the fourth quarter of 2014. The net loss reflects lower net revenues, higher interest costs, exploration expense and depletion, depreciation and impairment charges. Net loss for the year ended December 31, 2015 was $17.9 million compared to $175.7 million in 2014. The decrease in net loss for the year ended December 31, 2015 is due mainly to lower net revenues, one time transaction costs and higher interest charges, lower depletion, depreciation and impairment charges, offset by the gain on disposition of Pinecrest.

Netbacks [1]

December 31	Three months ended			Year ended		
$ Per boe	**2015**	**2014**	**% Change**	**2015**	**2014**	**% Change**
Average realized price	67.57	70.74	(4)	59.38	88.31	(33)
Royalty expense	(7.45)	(14.07)	(47)	(5.71)	(16.41)	(65)
Production & transportation expense	(27.67)	(30.51)	(9)	(27.06)	(28.68)	(6)
Field netback [1]	**32.45**	**26.16**	**24**	**26.61**	**43.22**	**(38)**
Realized loss on derivative financial instruments	-	4.21	(100)	-	(1.17)	(100)
Operating netback [1]	**32.45**	**30.37**	**7**	**26.61**	**42.05**	**(37)**
Less:						
Other income	(1.40)	(0.75)	86	(1.19)	(0.89)	34
Cash G&A expense	3.42	6.37	(46)	6.00	6.51	(7)
Cash financing	11.35	10.02	13	10.81	8.61	26
Cash flow netback [1]	**19.08**	**14.73**	**30**	**10.99**	**27.82**	**(60)**

[1] *Non-GAAP Measure*

Virginia Hills's operating netback was $32.45 per boe for the fourth quarter of 2015 compared to $30.37 per boe for the fourth quarter of 2014, and was $26.61 per boe for the year ended December 31, 2015, compared to $42.05 per boe for 2014. The fourth quarter 2015 operating netback was 7% higher than the prior year quarter, due to lower royalties and production and transportation costs. Operating netbacks for the year ended December 31, 2015 were lower than 2014 reflecting decreased average production volumes and lower realized prices, offset, in part by lower royalty rates.

CAPITAL EXPENDITURES

December 31	Three months ended			Year ended		
	2015	2014	% Change	2015	2014	% Change
Evaluation & exploration						
Undeveloped land, net of proceeds	59	38	55	523	204	>100
Drilling	-	1	(100)	-	3	(100)
	59	**39**	**51**	**523**	**207**	**>100**
Property, plant & equipment						
Drilling & completions	138	1,706	(91)	5,034	6,479	(22)
Equipment & facilities	172	2,274	(92)	4,566	1,559	>100
Capitalized administrative	(124)	95	>(100)	200	461	(57)
Corporate assets (1)	(8)	-	(100)	7	39	(82)
	178	**4,075**	**(96)**	**9,807**	**8,538**	**15**
Total capital expenditures	**237**	**4,114**	**(94)**	**10,330**	**8,745**	**18**
Proceeds on dispositions(2)	**-**	**-**	**-**	**(23,500)**	**-**	**100**
Total capital expenditures, net	**237**	**4,114**	**(94)**	**(13,170)**	**8,745**	**<100**

(1) *Corporate asset expenditures are net of proceeds of sale.*
(2) *Relates to proceeds received from Cardinal on completion of the Arrangement.*

Capital Expenditures & Drilling Results

Evaluation and exploration ("E&E") expenditures included lease rentals on undeveloped lands for the fourth quarters of 2015 and 2014. E&E expenditures for the year ended December 31, 2015 were $0.5 million and included land acquisition costs and lease rentals on undeveloped lands. During the fourth quarter of 2015, Virginia Hills spent $0.2 million, net of capitalized administrative costs on well work overs, compared to $4.1 million spent in the fourth quarter of 2014 which included costs on work overs, reclamation and acquisition of an interest in a gas transportation pipeline at the Evi 11-04 plant gate.

Capital expenditures were $9.8 million for the year ended December 31, 2015 compared to $8.5 million in 2014 and included costs to drill, complete and tie-in 2 gross (2 net) horizontal oil wells, projects to optimize operating costs and enhancements on the Company's water flood optimization project in the Otter field. In contrast, capital expenditures for the year ended December 31, 2014 included well optimizations, remediation work on certain producing wells and a credit relating to an equalization payment from a joint venture partner for water flood facilities in the Evi area. A total of 2.0 gross (2.0 net) oil wells were drilled during the year ended December 31, 2015, no wells were drilled in 2014. The Company recorded proceeds of $23.5 million from the sale of Pinecrest shares pursuant to the Arrangement, of which $22.6 million was used to pay down outstanding bank debt.

Land Holdings

As at December 31	2015		2014		% Change	
Acres	Gross	Net	Gross	Net	Gross	Net
Developed	23,968	13,729	20,320	13,527	18	1
Undeveloped	152,082	137,631	152,913	149,356	(1)	(8)
Total	**176,050**	**151,360**	**173,233**	**162,833**	**2**	**(7)**
Average working interest		**86%**		**94%**		**(8)**

Virginia Hills held a total of 151,360 net acres (237 sections) of land at December 31, 2015 with an average working interest of 86%. Total net acreage decreased from the prior year as a result of the Arrangement, which resulted in a disposition of approximately 10% of the Company's land holdings, offset in part by the Dolomite acquisition.

A total of 9,533 net undeveloped acres is included in the December 31, 2015 acreage that will expire in 2016, and has been recorded as exploration expense for the year ended December 31, 2015.

LIQUIDITY AND CAPITAL RESOURCES

Virginia Hills' ongoing development of its oil and gas asset base (growing production and reserves) is dependent on the Company's ability to secure sufficient funds from operations, credit facilities and capital markets. Liquidity is the Company's ability to meet the demands for cash to settle accounts payable and other liabilities as they come due. The Company's cash flows are highly dependent upon external market and risk factors, such as the volatility in commodity prices, changes in foreign currency exchange rates and pressures on service costs. Virginia Hills is focused on all aspects of operations and general and administrative cost structures to protect future cash flows to continue to meet its obligations with respect to ongoing operations. During the year ended December 31, 2015, the Company completed the Arrangement; entered into new and amended credit facilities in the amount of $108.0 million; closed a $3.0 million private placement equity offering; met its obligations under a farm-in arrangement and completed a corporate acquisition of a private oil and gas company. While these developments are positive, there can be no assurance that these initiatives are sufficient to meet the Company's commitments (See "Capital Structure and Going Concern" and "Contractual Obligations and Commitments").

At December 31, 2015, Virginia Hills had a working capital deficiency of $108.5 million (which included bank debt of $104.3 million) and an accumulated deficit of $24.3 million. During the year ended December 31, 2015, the Company reported a net loss of $17.9 million, but generated cash from operating activities of $3.1 million. At December 31, 2015, the Company was in breach of its production covenant and cumulative development capital expenditure covenant, which limits total cumulative development capital expenditures from April 1, 2015 to March 31, 2016 to $6.4 million. Subsequent to December 31, 2015, the Company and its lenders entered into an amending agreement and waiver, which redefined the Company's limits on capital spending to be an aggregate of $9.3 million from April 15, 2015 to March 31, 2016, limited capital spending from April 1, 2016 to September 30, 2016 to a maximum of $85,000, on a cash basis and waived the production default.

Cash Flow from Operating Activities & Funds Flow from Operations [2]

December 31	Three months ended			Year ended		
	2015	2014	% Change	2015	2014	% Change
Cash flow from operating activities	**3,501**	**4,594**	**(24)**	**3,082**	**22,536**	**(86)**
Transaction costs	-	519	(100)	4,142	569	>100
Decommissioning expenditures	37	55	(33)	37	55	(33)
Change in non-cash working capital	(965)	(2,589)	63	(1,186)	(3,099)	61
Funds flow from operations [2]	**2,573**	**2,579**	**(-)**	**6,075**	**20,061**	**(70)**
Cash Flow						
$ Per share, basic [1]	0.18	2.12	(91)	0.22	10.30	(98)
$ Per share, diluted [1]	0.18	2.12	(91)	0.22	10.30	(98)
Funds Flow from Operations [2]						
$ Per share, basic [1]	0.13	1.19	(89)	0.43	8.97	(95)
$ Per share, diluted [1]	0.13	1.19	(89)	0.43	8.97	(95)

(1) *The weighted average shares outstanding and per share amounts prior to April 15, 2015 have been restated to reflect the 100:1 share consolidation.*
(2) *Non-GAAP Measure*

Cash Flow from Operating Activities: Cash flow from operating activities was $3.5 million and $3.1 million for the quarter and year ended December 31, 2015 compared to $4.6 million and $22.5 million for the comparative periods ended December 31, 2014. The decrease in 2015 cash flow is the result of lower production volumes and lower average realized prices, compounded by increased interest charges. In addition, transaction costs of $4.1 million and $0.6 million were incurred in 2015 and 2014, and related to the Arrangement and Dolomite acquisition. These costs are typically non-recurring.

Funds Flow from Operations: Funds flow from operations is a non-GAAP measure used by Virginia Hills to determine the Company's ability to fund its capital expenditures and repay its debt. Funds flow from operations represents cash flow from operating activities, a GAAP measure, adjusted for transaction costs, which are typically non-recurring, changes in non-cash working capital and settlement of decommissioning liabilities. Funds flow from operations was lower for the fourth quarter and year ended December 31, 2015 compared to 2014 due to lower production volumes, lower average realized prices and increased interest expense.

Capital Structure & Going Concern

The Company actively monitors its capital and operational spending activities in order to ensure that it can meet its future anticipated obligations incurred from normal ongoing operations, which may require the Company to make adjustments to its capital structure. The Company's capital structure includes working capital, bank debt and share capital. Regular reporting is provided to the Board of Directors and the Company's lender group. In order to maintain or adjust its capital structure, the Company may issue common shares, repay existing debt, seek additional debt financing, adjust its capital spending and/or seek strategic alternatives, if available upon acceptable terms.

The Company's cash flows and compliance with debt covenants are dependent upon realized current period net revenues. The Company's 2015 operating cash flows were lower than the prior year due to depressed commodity prices and lower production volumes. The recent decrease in revenues, operating cash flow and history of losses indicates the existence of a material uncertainty that may cast significant doubt about the Company's ability to continue as a going concern. In addition, the lending value of the credit facility is dependent upon the Company's reserves which are directly linked to oil and natural gas forecasted benchmark prices that are expected to remain low for the foreseeable future. The credit facilities are due on September 30, 2016, and there is no assurance the Credit Facilities will be renewed upon the current terms or levels once the bank review is completed.

Should the lenders not renew the credit facilities, the Company would need to seek alternate forms of debt or equity financing, which would be difficult in the current business environment, or dispose of certain assets. The inability of the Company to access sufficient capital for its operations could have a material adverse impact on the Company's financial position and results of operations. Virginia Hills' ability to continue as a going concern is dependent upon its ability to fund the repayment of existing borrowings, secure additional financing and generate positive cash flows from operations. These financial statements do not reflect the adjustments to the carrying values of assets and liabilities and reported revenues, expenses and balance sheet classifications that would be necessary if the Company were unable to realize its assets and settle its liabilities as a going concern in the normal course of operations. Such adjustments could be material.

Net Debt

On a quarterly basis, the Company assesses its ability to meet its on-going obligations using the non-GAAP measures of funds flow from operations, compared to net debt. This ratio is a key measure of liquidity and the management of capital resources. At December 31, 2015, the Company's net debt was $108.5 million.

Three months ended	December 31, 2015	December 31,2014
Funds flow from operations	2,573	2,579
Annualized funds flow from operations	10,292	10,316
As at December 31	**2015**	**2014**
Working capital deficit (excluding bank debt)	4,258	4,932
Bank debt, including deferred financing charges	104,262	110,570
Net Debt	**108,520**	**115,502**
Net debt to annualized funds flow from operations	**10.5**	**11.2**

Credit Facilities

At December 31, 2015, the Company had total credit facilities available of $108.0 million, of which a total of $105.3 million was outstanding. All credit facilities are due September 30, 2016, with no scheduled bank review between December 31, 2015 and September 30, 2016.

As at December 31,	2015	2014
Credit Facilities Available		
Senior bank debt	$ 97,000	$ 114,000
Subsidiary bank debt	11,000	-
Total credit facilties available	**108,000**	**114,000**
Bank debt outstanding		
Syndicated revolving facility	90,000	95,000
Operating facility	4,500	15,570
Senior bank debt outstanding	94,500	110,570
Operating loan – non-revolving	5,000	-
Operating loan – revolving term loan	5,818	-
Subsidiary bank debt outstanding	10,818	-
Total bank debt outstanding	**$ 105,318**	**$ 110,570**
Letters of credit outstanding	**123**	**50**
Available Credit		
Senior bank debt	2,500	3,380
Subsidiary bank debt	59	-
Available Credit at December 31, 2015	**$ 2,559**	**$ 3,380**

Senior Bank Debt:

The Company's $97.0 million credit facility is comprised of a $90.0 million syndicated revolving facility and a $7.0 million non-syndicated operating facility, together the "Facilities", both of which have a term to September 30, 2016. The Facilities are secured by a general security agreement and a first floating charge debenture of $300.0 million covering all of the Company's assets. Starting April 1, 2016, principal repayments are due on the syndicated facility based on the prior month's available cash flow.

Advances under the Facilities may be made by way of Canadian prime rate loans, US base rate loans and letters of credit. Amounts borrowed under the Facilities bear interest on a floating rate based on the applicable Canadian prime rate plus a sliding scale pricing grid tied to the Company's trailing debt to earnings before interest, taxes, depreciation and amortization ("EBITDA") ratio. The interest pricing margin ranges from 1% to 3% and is dependent upon the form of borrowing. If at any time, the Company is in default under the Facilities, the interest margin will be increased by 2%, at the discretion of the lenders. At December 31, 2015 the Facilities interest rate was 5.7%.

The Facilities contain the following non–financial covenants: monthly reporting requirements which include reporting actual monthly results against the bank approved business plan, permitted indebtedness, permitted hedging, permitted encumbrances and a requirement that daily production volumes may not vary below the bank approved business plan by more than 10% in any month.

The Company is subject to financial covenants, based on cash flow and EBITDA which restricts the variance from the bank-approved business plan over the periods from:

- April 1, 2015 to September 30, 2015 to a maximum of $0.7 million;
- October 1, 2015 to March 31, 2016 to the lesser of 25% and $1.5 million and
- April 1, 2016 to September 30, 2016 to the lesser of 25% and $2.0 million;

Other financial covenants include: a restriction on the Company's cumulative capital expenditures to a maximum of $9.3 million from April 1, 2015 to March 31, 2016, with maintenance capital limited to $2.9 million and development capital limited to $6.4 million, of which a maximum of $4.8 million may be spent on the commitment farm-in wells; limitation on the monthly amount of capital spent from April 1, 2016 to September 30, 2016 and a requirement that net debt not exceed $100.2 million.
During the year, and as a result of the cross-default provision in the credit agreement, the Company was in default due to Dolomite's breach of its financial covenant at each month end from April to October 2015. The Company received waivers from its lenders relating to this default. At December 31, 2015, the Company was in compliance with its covenants, except the allocation of capital expenditures between development and maintenance capital, and its minimum required production covenant. Subsequent to December 31, 2015, the Company and its lenders entered into an amending agreement and waiver, which redefined the Company's limits on capital spending to be an aggregate of $9.3 million from April 15, 2015 to March 31, 2016, limited capital spending from April 1, 2016 to September 30, 2016 to a maximum of $85,000, on a cash basis and waived the production default.

Subsidiary Bank Debt
Virginia Hills' subsidiary entered into an agreement to amend and restate its $11.0 million credit facility on April 27, 2015. The facility provides for a $6.0 million revolving operating loan and a $5.0 million non-revolving reducing term loan. Interest is payable on the loans based on Canadian prime plus 3%, at December 31, 2015 the interest rate was 5.7%. Both facilities are due on September 30, 2016.

From April 1, 2016 through to and including April 15, 2016, the lender, at their option, may convert up to $4.0 million of the non-revolving reducing term loan into common shares of Virginia Hills at a deemed price of the greater of $0.30 per share or the market price based on a 20-day volume weighted average price. This conversion feature is an embedded derivative and is reported separately as a current derivative financial liability on the Balance Sheets. The embedded derivative will be revalued and marked to market on each reporting date, with the resulting difference being recorded as a financing gain or loss in the Statements of Net Loss and Comprehensive Loss. At December 31, 2015, the derivative had a fair value of $nil. The bank debt is carried at amortized cost, using the effective interest method, which will accrete the liability up to full value of the outstanding bank debt at the expiry of the conversion feature; this amount is recorded as a non-cash finance expense.

The subsidiary is subject to customary monthly reporting covenants, and a financial covenant that restricts the subsidiary's monthly working capital deficit to a maximum of $1.3 million from November 30, 2015 to March 31, 2016, and $1.2 million from April 2016 to September 30, 2016. The Company was in compliance with its subsidiary bank debt financial covenant at December 31, 2015.

The senior debt and subsidiary debt agreements contain customary events of default, including: events based on bankruptcy and insolvency, non-payment of principal, interest or fees when due, change in control, material inaccuracy of representations and warranties, and a cross-default provision for breach of covenants. In the event of default, the total outstanding principal amounts of the credit facilities plus all accrued interest and costs become immediately due and payable by the Company, at the discretion and upon request from the lenders.

During 2015, the Company was in default of its financial covenant, which was based on a three-month rolling average available cash flow (as defined in the agreement), under the subsidiary credit agreement at each month end from April to October 2015. The Company received waivers from its lenders relating to this default, and during the fourth quarter of 2015 the lender and Dolomite amended the subsidiary bank debt agreement financial covenant to be based on a monthly minimum working capital deficit amount.

Share Capital

The Company had the following outstanding common shares and equity instruments at December 31, 2015:

(000's)	**Common Shares**	**Warrants**	**Stock Options**
Balance, December 31, 2014 – Pinecrest Energy Inc.	217,212	23,270	-
Cancelled pursuant to the Arrangement (100:1) *(1) (2)*	(217,212)	(23,270)	-
Share consolidation pursuant to the Arrangement (100:1) *(1) (2)*	2,172	-	-
Issued pursuant to the exercise of Arrangement Rights *(2)*	3,412	-	-
Issued in Private Placement *(3)*	11,974	23,948	-
Issued pursuant to corporate acquisition *(4)*	11	4,000	-
Issued to settle debt relating to corporate acquisition *(5)*	2,155	-	-
Issued to the Company's senior lenders *(6)*	-	1,972	-
Issued to Company employees (stock options)*(7)*	-	-	1,773
Balance, December 31, 2015	**19,724**	**29,920**	**1,773**

(1) Effective April 15, 2015, under the terms of the Arrangement, each holder of Pinecrest common shares received one (1) Virginia Hills' common share for each 100 Pinecrest common shares held. All outstanding warrants were cancelled.

(2) On April 15, 2015, under the terms of the Arrangement, each holder of Common Shares received eight (8) arrangement rights for each Common Share held. A total of 3,412,175 Arrangement Rights were exercised as at May 15, 2015 for gross proceeds of $0.9 million.

(3) On April 15, 2015, the Company completed a private placement of 11,974,300 subscription receipts for gross proceeds of $2.9 million. Each subscription receipt entitled the holder to one Unit (as defined herein) upon the completion of the Dolomite Acquisition. On April 27, 2015, a total of 11,974,300 million flow-through units ("Unit") were issued upon conversion of the subscription receipts and the gross proceeds of $2.9 million were released to the Company. Each Unit was comprised of one (1) Common Share, issued on a flow-through basis, under the *Income Tax Act* (Canada), and two (2) common share purchase warrants (Series A Warrants and Series B Warrants). The Series A Warrants are exercisable at a price of $0.30 and the Series B Warrants are exercisable at $0.35. The warrants vest in tranches of 1/3 upon the 20-day weighted average trading price of the Company's share equaling or exceeding $0.35, $0.40 and $0.45 respectively and are outstanding for until April 27, 2020..

(4) On April 27, 2015 the Company completed the Acquistion by way of an amalgamation with its wholly owned subsidiary. A total of 10,600 Common Shares and 4.0 million common share purchase warrants ("Series C Warrants") to the shareholders of Dolomite. The warrants entitle the holders to acquire one (1) Common Share at a price of $0.50 per share until April 27, 2018.

(5) On April 27, 2015, as part of the Acquisition, certain payable obligations were settled by the issuance of Common Shares. A total of 983,624 Common Shares were issued at a price of $0.25 per Common Share for a total of $0.2 million, to the former executive officers of Dolomite as satisfaction of a portion of their change in control payments. The balance of the change in control payments of $0.6 million is due on April 27, 2016, and may be settled by the issuance of a maximum of an additional 1,229,530 Common Shares issued at a deemed price of the greater of $0.30 per share or the market price, at the time of issuance. Should the executives elect to be paid in cash, the payment is subject to approval by the Company's senior lenders.

In addition, a total of 1,171,332 Common Shares were issued at a price of $0.25 for a total of $0.3 million to certain third-party service providers as payment for services previously provided.

(6) Under the terms of the new Facilities, the Company's senior lenders were issued a total of 1,972,416 warrants (Series D Warrants) representing 10% of the issued and outstanding Common Shares at May 15, 2015. The Series D Warrants are exercisable at a price of $0.30 per common share for a period ending on the earlier of five years from the date of issue, or 30 days following the date on which the Facilities mature.

(7) A total of 1,844,614 options were issued at an average exercise price of $0.25 per share. The options vest in tranches of 1/3, on each of the first, second and third anniversary dates from grant and are outstanding for five years from date of grant. During the year, a total of 70,965 options were forfeited.

Additionally, under the terms of the Acquisition, Dolomite's lender has the option to convert up to $4.0 million of the non-revolving term facility into Common Shares at a deemed price of $0.30 per share, or the Market Price of the shares (as defined within the TSX-V policies), whichever is greater, until April 25, 2016, for a maximum of 13,333,333 Common Shares.

At March 30, 2016, Virginia Hills had the following equity instruments outstanding:

	(000's)
Common shares	19,724
Warrants	29,920
Stock Options	1,773
Total outstanding securities	51,417

BUSINESS RISKS

Virginia Hills' business, financial condition, results of operations and cash flows are impacted by a number of risks facing participants in the oil and gas industry. These risks cannot be eliminated, however, Virginia Hills management is committed to monitoring, and where possible, mitigating the following risks: operational; safety, environmental and regulatory; and financial.

1) Operational Risk

Development and Production Risk: Virginia Hills' production and exploration activities are concentrated in the Western Canadian Sedimentary Basin, where activity is highly competitive and includes a variety of different sized companies ranging from small junior producers to large integrated petroleum companies. Virginia Hills is exposed to the following development and production risk factors:

- finding and developing petroleum and natural gas reserves at economic costs;
- production of petroleum and natural gas in commercial quantities; and
- marketability of petroleum and natural gas produced.

The Company's future success is dependent upon its ability to develop or acquire additional oil and natural gas reserves that are economically recoverable at attractive costs. Except to the extent that Virginia Hills conducts successful activities or acquires properties containing proved reserves, or both, the proved reserves and production will generally decline as reserves are produced. If prevailing oil and natural gas prices were to increase significantly, the Company's costs to add reserves could be expected to increase. The drilling of oil and natural gas wells involves a high degree of risk, especially the risk of a well that is not sufficiently productive to provide an economic return on the capital expended to drill the well or of its ongoing operational costs.

In order to reduce exploration risk, Virginia Hills strives to employ highly qualified and motivated professional employees with demonstrated ability to generate quality proprietary geological and geophysical prospects. To help maximize drilling success and mitigate reserve replacement risk, the Company has focused its exploration in areas that afford multi-zone prospect potential, targeting a range of low to moderate exploration and development risk prospects.

Virginia Hills mitigates its risk related to producing hydrocarbons through the utilization of the most appropriate and up-to-date technology to enhance drilling and completions operations, control costs to maximize returns and has focused exploration in areas where the Company's management and employees have significant drilling and completions experience. In addition, Virginia Hills seeks operational control of its projects, where feasible. Advanced oil and gas related technologies such as three dimensional seismography and reservoir simulation studies might be utilized by Virginia Hills to improve its ability to find, develop and produce economical oil and gas reserves. Regardless of whether Virginia Hills combines technology and expertise, these risks may not be eliminated.

Other Operational risks: Oil and natural gas exploration operations are subject to risks such as explosions, blow-outs, fire and oil spills, each of which could result in substantial damage to oil and gas wells and facilities, other property, the environment or personal injury. In accordance with industry practice, Virginia Hills carries insurance coverage for general and comprehensive liability as well as limited pollution liability. The amount and terms of this insurance are reviewed on an ongoing basis and adjusted as necessary to reflect changing corporate requirements, as well as industry standards and government regulations. Virginia Hills' oil and natural gas exploration and development activities are dependent on the availability of drilling and related equipment in our core areas. Demand for such limited equipment or access restriction may affect the availability of such equipment and may delay exploration and development activities. Virginia Hills' operations require license and permits from various governmental authorities. There can be no assurance that the Company will be able to obtain all necessary licenses and permits that may be required to carry out exploration and development projects.

2) Safety, Environmental and Regulatory Risk

The oil and gas industry is subject to extensive government regulation (municipal, provincial and national). Environmental legislation provides for restrictions and prohibitions on spills, releases and/or emissions of various substances produced in association with oil and gas production. Petroleum and natural gas exploration and production can involve environmental risks such as pollution of the environment and destruction of natural habitat, as well as safety risks such as personal injury. In order to mitigate such risks, Virginia Hills conducts its operations at high standards and follows safety procedures intended to reduce the potential for personal injury to employees, contractors and the public at large. The Company maintains adequate insurance commensurate with industry standards to cover reasonable risk and potential liabilities associated with its activities.

The nature of these risks is such that liabilities could exceed policy limits, in which event the Company could incur significant costs that could have an adverse effect upon its financial condition. Virginia Hills has in place an environmental and safety policy that is designed at minimum to comply with current government regulations for the oil and gas industry. Changes to governmental regulations are monitored to ensure compliance. Environmental reviews are completed as part of the due diligence process when evaluating corporate and property acquisitions.

3) Financial Risk

Virginia Hills defines financial risk as the risk of loss or lost opportunity resulting from financial management and market conditions that could have a positive or negative impact on the Company's cash flows.

Commodity Price Risk: Recent market events and conditions, including global excess oil and natural gas supply, recent actions taken by OPEC, slowing growth in China and other emerging economies, market volatility and disruptions in Asia, and sovereign debt levels in various countries, have caused significant weakness and volatility in commodity prices. These events and conditions have caused a significant decrease in the valuation of oil and gas companies and a decrease in confidence in the oil and gas industry. These difficulties have been exacerbated in Canada by the recent changes in government at a federal level and, in case of Alberta, the provincial level and the resultant uncertainty surrounding regulatory, tax and royalty changes that may be implemented by the new governments. In addition, the inability to get the necessary approvals to build pipelines and other facilities to provide better access to markets for the oil and gas industry in western Canada has led to additional uncertainty and reduced confidence in the oil and gas industry in western Canada. Lower commodity prices may also affect the volume and value of the Company's reserves especially as certain reserves become uneconomic.

In addition, lower commodity prices have restricted, and are anticipated to continue to restrict, the Company's cash flow resulting in a reduced capital expenditure budget. As a result, the Company may not be able to replace its production with additional reserves and both the Company's production and reserves could be reduced on a year over year basis. Any decrease in value of the Company's reserves may reduce the borrowing base under its credit facilities, which, depending on the level of the Company's indebtedness, could result in the Company having to repay a portion of its indebtedness. Given the current market conditions and the lack of confidence in the Canadian oil and gas industry, the Company may have difficulty raising additional funds or if it is able to do so, it may be on unfavourable and highly dilutive terms.

In accordance with policies approved by the Board of Directors, Virginia Hills may, from time to time, manage these risks through the use of physical delivery contracts, swaps, collars or other financial instruments not to exceed 70% of net commodity production (after royalties). During the year ended December 31, 2015, Virginia Hills had the following fixed-price physical delivery contracts in place:

Term	Volume (bbl/d)	Fixed Price[(1)] (US$/bbl)
May 1, 2015 – Jun 30, 2015	1,135	$55.10
Jul 1, 2015 – Sep 30, 2015	1,128	$53.47
Oct 1, 2015 - Dec 31, 2015	1,128	$53.22

(1) *Pricing is adjusted on a monthly basis for quality and transportation*

Credit Risk: Credit risk is the risk of loss if purchasers or counterparties default on their financial obligations. The maximum exposure of the Company to credit risk at December 31, 2015 and December 31, 2014 is limited to trade and other receivable balances as reported on the consolidated Balance Sheets.

The Company's accounts receivable are subject to concentration of credit risk as all of the Company's customers are in the oil and gas sector. The majority of Company's trade and other receivables are from joint interest partners and crude oil and natural gas marketers. Receivables from oil and gas marketers are typically collected on the 25th day of the month following production. Virginia Hills attempts to mitigate this risk by assessing the financial strength of its counterparty to determine that they have a well-established credit history, and entering into relationships with more than one marketer. Receivables from joint interest partners are typically collected within one to three months from the joint venture billing date. The Company attempts to mitigate collection risk from joint interest partners by obtaining partner pre-approval of significant capital expenditures prior to initiation of the capital project. However, joint interest partners are exposed to various oil and gas industry risks that could impact the Company's ability to collect these amounts. The carrying amount of trade and other receivables represents the maximum credit exposure to the Company. In the event such entities fail to meet their contractual obligations to the Company, such failures may have a material adverse effect on the Company's business, financial condition, results of operations and prospects. In addition, poor credit conditions in the industry and of joint venture partners may affect a joint venture partner's willingness to participate in the Company's ongoing capital program, potentially delaying the program and the results of such program until the Company finds a suitable alternative partner. To the extent that any of such third parties go bankrupt, become insolvent or make a proposal or institute any proceedings relating to bankruptcy or insolvency, it could result in the Company being unable to collect all or portion of any money owing from such parties. Any of these factors could materially adversely affect the Company's financial and operational results

Liquidity Risk: Liquidity risk is the risk that the Company will not be able to meet its financial liabilities as they come due. Liquidity risk also includes the risk of the Company not being able to liquidate assets in a timely manner at a reasonable price. The Company monitors its liquidity requirements by anticipating operating, investing and financing activities and ensuring there are enough funds to cover these activities. Liquidity risks may necessitate the need for the Company to conduct equity issues or obtain debt financing. The Company prepares annual production and capital expenditure budgets, which are regularly monitored and updated when necessary to include a review of debt forecasts and working capital requirements. In addition, Virginia Hills uses authorization for expenditures for operated and non-operated capital projects to facilitate monitoring capital programs.

At December 31, 2015 there were a total of $115.3 million in liabilities outstanding; which was comprised of: bank overdraft of $0.2 million, trade and other payables of $10.5 million, flow through share premium of $0.3 million and $104.6 million outstanding on its credit facilities.

Foreign Currency Risk: World oil prices are quoted in USD and the price received is therefore affected by the Canadian/US dollar exchange rate, which will fluctuate over time. Recently, the Canadian dollar has weakened in value against the USD which positively impacts commodity prices valued in Canadian dollars, thereby indirectly increasing Virginia Hills' oil revenues and future value of reserves, as determined by independent evaluators. The Company has not entered into any foreign currency risk arrangements.

Interest Rate Risk: Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. The interest charged on Virginia Hills' credit facility fluctuates with the interest rates posted by lenders, plus a margin. The Company has not entered into any mitigating interest rate swaps or hedges as at December 31, 2015. Had the market interest rate been 1% (100 basis points) higher (or lower) and assuming all other variables remained constant for the year ended December 31, 2015, net loss would have been lower or higher by $0.8 million based on the average outstanding bank debt balance outstanding for the year ended December 31, 2015.

CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The preparation of financial statements requires management to make certain judgement, accounting estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, revenues and expenses. A summary of Virginia Hills's critical accounting estimates and judgements can be found in Note 4 and a summary of significant accounting policies can be found in Note 5 to the annual audited consolidated financial statements for the year ended December 31, 2015.

Virginia Hills' management reviews its estimates frequently; however, the emergence of new information and changed circumstances may result in actual results or changes to estimated amounts that differ materially from current estimates. Virginia Hills attempts to mitigate this risk by employing individuals with the appropriate skill set and knowledge to make reasonable estimates, developing internal control systems and comparing past estimates to actual results. Significant judgements, estimates and assumptions made by management in preparing the financial statements are described below:

Estimates

- The fair value of financial assets and liabilities is estimated, whenever possible, based on published market prices and if not available, on estimates from third party brokers as at the balance sheet date and may differ from what will eventually be realized;
- Depletion, depreciation and the assessment of asset recoverability (tests for impairment) are based on assumptions of grouping of assets into CGUs using estimates of crude oil and natural gas reserves and future cash flows;
- Revenues, operating expenses and royalties for which accruals have been recorded for actual revenues and costs which have been earned or incurred but have not yet been received;
- Decommissioning liability including estimates of future costs and the timing of the costs; and
- Share-based payments requires estimates about the share price volatility, forfeiture rates, option life, dividend yield, risk-free rate and forfeitures of options at the initial grant date.

Judgements

- Estimates of proven and probable petroleum and natural gas reserves include assumptions regarding production profile, commodity prices, exchange rates, remediation costs, timing and amount of future development costs, production, transportation and marketing costs for future cash flows. Estimated quantities of petroleum and natural gas reserves also include the interpretation of geological and engineering data;
- Identification of CGUs for purposes of impairment testing;

- Decisions regarding capital expenditures on projects that are in progress require judgements about the probable commercial reserves and the level of activities that constitute on-going evaluation determination;
- Deferred income taxes and the recoverability of deferred income tax assets have been recorded based on temporary differences between the carrying value and tax basis of the Company's assets and liabilities. These provisions require estimating the timing of these temporary differences and estimating whether tax assets will be realized before expiry; and
- Judgement is required when determining if Virginia Hills has joint control over an arrangement. This will impact whether the investment is accounted for on a proportionate basis, or by equity accounting.

ACCOUNTING CHANGES AND PRONOUNCEMENTS

Recent Accounting Pronouncements Issued

The following are new and amended accounting pronouncements that have been issued but are not yet effective. Management is currently assessing the impact of these new and amended standards on the Company's accounting policies and financial statement presentation or whether to early adopt any of the standards. These standards are not expected to have a material impact on the Company's financial statements.

- ***IFRS 9 Financial Instruments ("IFRS 9"):*** IFRS 9 was amended to introduce a single, forward-looking "expected loss" impairment model for financial assets which will require more timely recognition of expected credit losses, and a fair value through other comprehensive income category for financial assets that are debt instruments and supplements the new hedge accounting principles published in 2013. These amendments are effective for annual periods beginning on or after January 1, 2018 and are available for early adoption.

- ***IFRS 15 Revenue From Contracts With Customers ("IFRS 15")*****:** IFRS 15 provides clarification for recognizing revenue from contracts with customers and establishes a single revenue recognition and measurement framework and replaces *IAS 18 Revenue, IAS 11 Construction Contracts* and related interpretations The standard requires an entity to recognize revenue to reflect the transfer of goods and services for the amount it expects to receive, when control is transferred to the purchaser. The new standard will be effective for annual periods beginning on or after January 1, 2018, with early adoption permitted. The standard may be applied retrospectively, or using a modified retrospective approach.

- ***IFRS 16 Leases ("IFRS 16"):*** IFRS 16 replaces IAS 17 Leases with a single recognition and measurement model which will be applied to leases for lessees, with required recognition of assets and liabilities being required for most leases. The standard is effective for annual periods beginning on or after January 1, 2019, with early adoption permitted if the entity is also applying IFRS 15.

DISCLOSURE AND INTERNAL CONTROLS

Management is responsible for the preparation and integrity of the financial statements, including the maintenance of appropriate information systems, procedures and internal controls, and to ensure that information used internally or disclosed externally, including the financial statements and MD&A, is complete and reliable. Disclosure controls and procedures have been designed to provide reasonable assurance that information required to be disclosed by the Company is recorded, processed, summarized and reported within the time periods specified under the Canadian securities law. Virginia Hills' Chief Executive Officer and Chief Financial Officer have concluded, based on their evaluation, that the disclosure controls and procedures as of the end of December 31, 2015, are effective and provide reasonable assurance that material information related to the Company is made known to them by others within Virginia Hills.

It should be noted that a control system, including Virginia Hills' disclosure and internal controls and procedures, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system will be met and it should not be expected that the disclosure and internal controls and procedures will prevent all errors or fraud. There have been no changes to the Company's internal controls since year end December 31, 2014.

In connection with Exemption Orders issued in November 2007 by each of the securities commissions across Canada, Virginia Hills' certifying officers will file a Venture Issuer Basic Certificate with respect to the financial information contained in the unaudited interim financial statements and the audited annual financial statements and respective accompanying MD&A. The Venture Issuer Basic Certification includes a 'Notice to Reader' stating that the certifying officers do not make any representations relating to the establishment and maintenance of disclosure controls and procedures and internal control over financial reporting, as defined in National Instrument 52-109 – Certification of Disclosure in Issuers' Annual and Interim Filings.

OFF BALANCE SHEET ARRANGEMENTS

No off balance sheet arrangements existed at December 31, 2015.

RELATED PARTY TRANSACTIONS

The Company has retained the law firm of Burnet, Duckworth and Palmer LLP to provide legal services. The current Chairman of the Board is a partner and Corporate Secretary is an associate of the law firm. During the year ended December 31, 2015, the Company incurred legal fees and disbursements of $1.0 million (December 31, 2014: $0.5 million) related to general corporate matters, of which $0.2 million was outstanding at December 31, 2015 (December 31, 2014: $0.3 million). These transactions were in the normal course of business and have been measured at fair value.

CONTRACUTAL OBLIGATIONS AND COMMITMENTS

The Company had the following commitments at December 31, 2015.

	2016	2017	2018	2019	2020	Thereafter
Office lease rentals	145	145	193	16	-	-
Field office lease rental	39	16	-	-	-	-
Equipment rentals	11	12	10	-	-	-
Electrification agreements	288	288	-	-	-	-
Flow-through shares	1,000	-	-	-	-	-
Commitments	**1,483**	**461**	**203**	**16**	**-**	**-**

The Company has $0.6 million in commitments to install electrical service to a number of its well sites over the next 24 months. The agreements may be cancelled by the Company upon providing written notice at any time, but will be responsible for costs incurred by the vendor from date of contract up to date of cancellation.

During 2015, the Company issued the Units, at a price of $0.25 per Unit for gross proceeds of $3.0 million. As at December 31, 2015, the Company had incurred qualifying expenditures of $2.0 million, and is committed to spend $1.0 million on qualifying expenditures by December 31, 2016.

SUBSEQUENT EVENTS

Subsequent to December 31, 2015, the Company and its lenders entered into an amending agreement and waiver, which redefined the Company's limits on capital spending to be an aggregate of $9.3 million from April 15, 2015 to March 31, 2016 and waived the production default.

Subsequent to December 31, 2015, the Company sold certain capital spare parts to a third party for proceeds of $0.3 million.

SUPPLEMENTAL QUARTERLY INFORMATION

	2015				2014			
	Dec 31 Q4	Sep 30 Q3	Jun 30 Q2	Mar 31 Q1	Dec 31 Q4	Sep 30 Q3	Jun 30 Q2	Mar 31 Q1
FINANCIAL								
Oil & gas sales	9,101	8,302	8,287	7,149	12,269	15,018	18,167	18,229
Funds flow from operations [1]	2,573	1,079	2,393	31	2,579	4,243	5,952	7,285
Per share – basic [4]	$0.13	$0.05	$0.17	$0.01	$1.19	$1.95	$2.74	$3.35
Per share – diluted [4]	$0.13	$0.05	$0.17	$0.01	$1.19	$1.92	$2.68	$3.28
Cash flow from operations	3,501	(72)	(1,114)	767	4,594	4,594	7,417	5,931
Per share – basic [4]	$0.18	$(0.00)	$(0.08)	$0.35	$2.12	$2.12	$3.41	$2.73
Per share – diluted [4]	$0.18	$(0.00)	$(0.08)	$0.35	$2.12	$2.12	$3.34	$2.67
Net income (loss) [2]	(18,254)	(3,098)	7,671	(4,233)	(176,473)	51	407	290
Per share – basic [4]	$(0.93)	$(0.16)	$0.55	$(1.95)	$(81.24)	$0.02	$0.19	$0.13
Per share – diluted [4]	$(0.93)	$(0.16)	$0.55	$(1.95)	$(81.24)	$0.02	$0.18	$0.13
Capital expenditures, net	237	7,246	1,866	981	4,115	2,846	777	1,008
Property dispositions	-	(1,000)	(22,500)	-	-	-	-	-
Total assets	100,330	121,101	120,313	116,340	121,101	296,960	300,889	306,700
Net debt [1][4]	108,520	110,949	105,786	116,562	115,502	113,627	115,837	121,405
OPERATING								
Average daily production								
Oil & NGL's (bbls/d)	1,411	1,416	1,426	1,607	1,831	1,756	1,994	2,082
Natural gas (mcf/d)	320	325	325	261	322	316	457	366
Total (boe/d)	1,464	1,470	1,480	1,650	1,885	1,808	2,070	2,143
Average prices								
Oil & NGL's (bbls/d)	69.90	63.44	63.66	49.38	72.78	92.92	100.01	97.21
Natural gas (mcf/d)	1.05	1.18	0.96	0.43	0.16	0.10	0.55	0.43
Netbacks ($/boe) [1]								
Average prices	67.57	61.36	64.54	48.15	70.74	90.24	96.45	94.51
Royalties	(7.45)	(6.53)	(2.22)	(6.51)	(14.07)	(18.44)	(18.80)	(14.41)
Production & transp.	(27.67)	(29.85)	(26.02)	(24.88)	(30.51)	(32.06)	(24.97)	(27.72)
Field netback [1]	32.45	24.98	33.30	16.76	26.15	39.74	52.68	52.38
Realized gain (loss) on derivative contracts	-	-	-	-	4.21	(1.95)	(3.94)	(2.64)
Operating netback	32.45	24.98	33.30	16.76	30.37	37.79	48.74	49.74

(1) *Non-GAAP measure..*

(2) *Prior periods have been restated to conform with current period classification.*

(3) *Net loss for the quarters ended December 31, 2015 and September 30, 2015 include impairment losses of $16.4 million and $0.5 million respectively. Net income for the quarter ended June 30, 2015 includes a $13.9 million gain on disposition of Pinecrest . to Cardinal pursuant to the Arrangement. Net loss for the quarter ended December 31, 2014 includes exploration and evaluation asset expense and impairment of $79.2 million and an asset impairment of $93.0 million.*

(4) *Net debt is defined as working capital (current assets less current liabilities) plus outstanding long term bank debt.*

(5) *Pursuant to the Arrangement, the weighted average shares outstanding and per share amounts prior to April 15, 2015 have been restated to reflect the 100:1 share consolidation.*

SELECTED ANNUAL INFORMATION

For the year ended December 31,	2015	2014	2013
Oil & gas sales[(1)]	32,839	63,683	108,872
Net loss[(2)]	17,914	175,725	171,046
Per share – basic	$1.28	$80.90	79.15
Per share – diluted	$1.28	$80.90	78.54
As At December 31,	**2015**	**2014**	**2013**
Total assets	100,330	121,101	311,567
Total non-current liabilities[(3)]	9,365	11,245	146,821
Total net debt[(4)]	108,520	115,502	126,721

(1) Oil and gas sales have declined year over year due to: a decline in average annual production volumes, from 3,332 boe/d in 2013, (which includes production from the drilling of 15 (14.3 net) wells) with average realized prices of $89.51/boe. 2014 average daily production was 1,976 boe/d, lower than 2013 as there were no new wells drilled and 11 (11 net) wells were converted from oil producers to water injector wells at an average realized price of $88.31/boe. 2015 average annual production of 1,515 boe/d reflects the sale of approximately 10% of the assets in the second quarter of 2015 with an average realized price of $59.38/boe.

(2) Net loss in 2013 includes an asset impairment of $176.7 million and exploration expense of $16.3 million, Net loss in 2014 includes an asset impairment of $93.0 million and exploration expense and impairment of $79.2 million and Net loss in 2015 includes an impairment loss of $16.3 million.

(3) Total non-current liabilities in 2013 include bank debt of $121.5 million, all other years include the Company's decommissioning provision

(4) Total net debt for 2013 includes working capital deficit of $5.2 million and bank debt of 121.5 million; Net debt for 2014 includes working capita' deficit of $115.5 of which a total of $110.6 million is outstanding bank debt. Net debt for 2015 of $108.5 million includes outstanding bank debt of $104.3 million.

NON-GAAP MEASUREMENTS

The Company uses certain financial measures referred to in this MD&A to quantify its results that are not prescribed by Generally Accepted Accounting Principles ("GAAP"). The following terms: "funds flow from operations", "funds flow from operations per share", "field netback", "operating netback", "operating netback per boe", "cash flow netback" and "cash flow netback per boe" are not recognized measures under GAAP and may not be comparable to that reported by other companies. Virginia Hills uses funds flow from operations to analyze operating performance, and considers this to be a key measure that demonstrates the Company's ability to generate cash necessary to fund future capital expenditures and repay its debt. Operating netback is a measure of operating margin used in capital allocation decisions. The following outlines the definitions that Virginia Hills uses for each measure:

- Funds flow from operations is calculated based on cash flow from operating activities before changes in non-cash working capital, decommissioning expenditures and transaction costs;
- Funds flow from operations per share is calculated using the weighted-average basic and diluted shares outstanding, used in calculating earnings per share;
- field netback as average realized price less: royalties, transportation and production expenses. Operating netback is defined as field netback, plus (or minus) any realized gain (or loss) on derivative commodity contracts;
- Operating netback per boe is calculated by dividing operating netback by total boe produced for the applicable period. Cash flow netback is a measure of operating netback, plus other operating income less net cash administrative expenses, less cash interest expenses;

- Cash flow netback per boe is calculated by dividing cash flow netback by the total boe produced during the applicable period;
- Net debt: current assets, less current liabilities, plus outstanding total bank debt; and
- Total market capitalization is total outstanding common shares, stock options and warrants multiplied by the period end market price per share.

Management believes that, in addition to net income and cash flow from operating activities, these measures are useful supplemental measures as they provide an indication of Virginia Hills's operating performance, and leverage. ***Readers are cautioned that these measures should not be construed as an alternative to net income (loss), or cash flow from operating activities as calculated under GAAP, as an indication of the Company's performance.***

FORWARD LOOKING STATEMENTS

Certain statements in this MD&A constitute forward-looking statements and forward-looking information (collectively "forward-looking statements") within the meaning of applicable Canadian securities laws. All statements other than statements of present or historical fact are forward-looking statements. Forward-looking information is often, but not always, identified by the use of words such as: "anticipate", "believe", "continuous", "estimate", "expect", "intend", "may", "objective", "ongoing", "plan", "should", or similar words suggesting future outcomes. In particular, this MD&A contains forward-looking statements relating, but not limited to:

- *anticipated exit and average production rates and production mix, including performance characteristics of the Company's oil and natural gas properties for the first quarter of 2016;*
- *anticipated operating costs and administrative expenses and other financial and operating results;*
- *average corporate royalty rates for 2016;*
- *anticipated production and transportation costs for 2016;*
- *future land expiries;*
- *interest expense for 2016;*
- *business strategy, goals and management focus;*
- *drilling and development plans and the timing thereof;*
- *anticipated facility upgrades;*
- *plans to pursue additional land in core areas;*
- *forecast capital expenditures, the allocation of capital expenditures and the results therefrom;*
- *sources of funds for the Company's ongoing operations and capital expenditures;*
- *future liquidity and the Company's access to sufficient debt and equity capital;*
- *asset base and future prospects for development and growth;*
- *expectations regarding the business environment, industry conditions and future commodity prices;*
- *expectations regarding the Company's tax horizon and the tax pool that will be available to the Company;*
- *the impact of any changes to the Company's credit facilities resulting from periodic review;*
- *treatment under governmental and other regulatory regimes and tax, environmental and other laws.*

Such statements are based on assumptions of future events and actual results could vary from these assumptions. Events or circumstances may cause actual results to differ materially from those predicted as a result of numerous known and unknown risks, uncertainties and other factors, many of which are beyond the control of the Company. These include, but are not limited to, risks associated with petroleum and natural gas exploration, production, marketing and transportation, such as loss of market, volatility of commodity prices, currency fluctuations, imprecision of reserve estimates, imprecision of accounting estimates, environmental risk, and competition from other producers and ability to access sufficient capital from internal and external sources.

Although management believes that the expectations reflected in such forward-looking statements and information are reasonable, it can give no assurance that such expectations will prove to be accurate, as results and future events could differ materially from those expected or estimated in such statements. As such, readers are cautioned not to place undue reliance on these forward-looking statements. The forward-looking statements contained in this MD&A are made as of the date hereof for the purposes of providing the readers with the Company's expectations for the coming year. The forward-looking statements and information may not be appropriate for other purposes.

Furthermore, the Company undertakes no obligation to update or revise these forward-looking statements or information as a result of new information or future events, other than as required by applicable securities laws. However, in the event that subsequent events are reasonably likely to cause actual results to differ materially from forward-looking statements previously disclosed by the Company for a period that is not yet complete, Virginia Hills will provide disclosure on such events and the anticipated impact of such events.

FUTURE ORIENTED FINANCIAL INFORMATION

This MD&A, in particular the information in respect of the future estimated production, production and transportation expenses, general and administrative expenses, and interest expense may contain Future Oriented Financial Information ("FOFI") within the meaning of applicable securities laws. The FOFI has been prepared by management to provide an outlook of the Company's activities and results and may not be appropriate for other purposes. The FOFI has been prepared based on a number of assumptions including the assumptions discussed under the heading "Forward-Looking Statements" and assumptions with respect to production rates and commodity prices. The actual results of operations and the resulting financial results may vary from the amounts set forth herein, and such variations may be material. Management believes that the FOFI has been prepared on a reasonable basis, reflecting management's best estimates and judgments

Frequently Used Terms:

Term	Description
AECO	A natural gas storage facility located at Suffield, Alberta
bbl	Barrel(s)
bbl/d	Barrel(s) per day
boe	Barrel(s) of oil equivalent
boe/d	Barrel(s) of oil equivalent per day
mcf	Thousand cubic feet
mcf/d	Thousand cubic feet per day
Mmbtu	Million British thermal units
NGL	Natural gas liquids
WTI	West Texas Intermediate, reference price paid in US$ at Cushing Oklahoma for crude oil of standard grade