



20 YEARS OF
DELIVERING
LOW RISK
ATTRACTIVE
RETURNS

Annual Report 2016

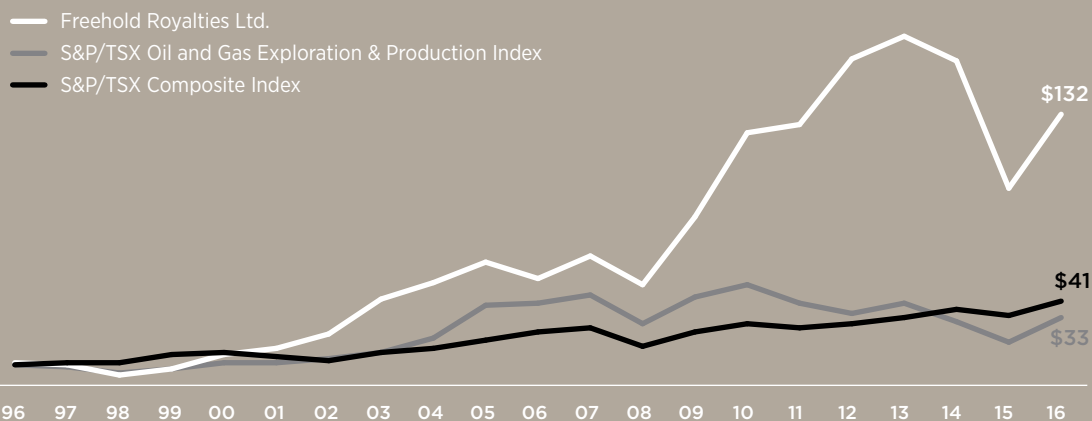
Freehold
ROYALTIES LTD.

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At the end of 2016, a \$10 investment in Freehold with dividends reinvested would be worth \$132

LONG TRACK RECORD OF DELIVERING ATTRACTIVE RETURNS (\$ per share) ⁽¹⁾



(1) From November 25, 1996 to December 31, 2010 reflects distributions paid on trust units of Freehold Royalty Trust, with distribution reinvestment, and from January 1, 2011 to the present reflects dividends paid on common shares of Freehold, with dividend reinvestment.

MESSAGE TO SHAREHOLDERS

2016 marked a strong year for Freehold as we achieved record production while managing our cash flows and debt levels.

Creating Value Through Acquisitions

We completed a transformational royalty acquisition in 2016, nearly doubling our royalty land base and adding two new key areas, southwest Saskatchewan and Grande Prairie.

Preserving and Delivering Value Through a Conservative Payout Ratio

With revised payout and debt targets as part of our strategy, Freehold has enhanced its ability to sustain its dividend.

Continued Gains in Operations

We achieved record production in 2016 with volumes averaging 12,219 boe per day, up 33% over the past two years. We are positioned in some of the most attractive resource plays in western Canada which continue to attract capital.

Recognizing Our Employees and Shareholders

We would like to thank all of the people involved in our 20-years of success including our employees and loyal shareholders.



THOMAS J. MULLANE
President and Chief Executive Officer
March 2, 2017



THOMAS J. MULLANE
President and Chief
Executive Officer



DARREN G. GUNDERSON
Vice-President,
Finance and Chief
Financial Officer



DAVID M. SPYKER
Vice-President,
Production



MICHAEL J. STONE
Vice-President,
Land

2016 PERFORMANCE HIGHLIGHTS

2016 represented another strong year for Freehold. We achieved continued growth in royalty production, driven by sustained development of our lands and a transformative acquisition that nearly doubled our royalty acres. Financially, while commodity prices continue to remain challenged, Freehold made inroads in lowering costs, while maintaining strength in our balance sheet, further enhancing the sustainability of our dividend.

	<i>Years ended December 31</i>	
	2016	2015
<i>(\$000s, except as noted)</i>		
Financial Highlights		
Royalty and other revenue	129,968	135,664
Net loss	(11,163)	(4,080)
Per share, basic and diluted (\$)	(0.10)	(0.05)
Funds from operations	94,211	103,820
Per share (\$)	0.85	1.15
Capital expenditures	5,218	22,295
Acquisitions	162,590	411,352
Net debt	73,161	146,949
Dividends declared	59,502	90,139
Per share (\$)	0.54	1.00
Average shares outstanding (000s)	110,391	90,505
Shares outstanding at year-end (000s)	117,918	98,940
Operational Highlights		
Average daily production (boe/d)	12,219	10,945
Average realized price (\$/boe)	28.37	33.20
Operating netback (\$/boe)	24.83	28.83

“On November 25, 2016, Freehold celebrated 20 years as a public company. Over our history, we have strived to maintain a consistent strategy, positioning ourselves as a low risk investment with upside to increasing oil prices”

20 YEAR ACHIEVEMENTS

Low Risk Income Vehicle

From a \$10 per share initial public offering, we have provided shareholders with a steady income stream returning almost \$1.5 billion in dividends or \$30.47 per share. We remain committed to providing a sustainable income stream for our shareholders.

Continued Growth in Production

2016 marked another record year of production with volumes averaging 12,219 boe per day. Driven by the quality of our royalty portfolio and execution of our acquisition strategy, we have grown production from less than 5,000 boe per day in 1996 to current levels.

Disciplined, Opportunistic Acquirer

Over our 20-year history, we have completed almost \$1.5 billion in acquisitions, adding approximately 10,000 boe per day in production. We are committed to remaining disciplined in our acquisition strategy with the goal of adding opportunities that further enhance the quality of our royalty portfolio now and in future years.

8%

Compound
Annual Total
Return

13%

Average
Return
on Capital
Employed

>\$30/share

Returned in
dividends

5%

Compound
Annual
Production
Growth

3 Year Track Record

- Increasing our focus towards royalties, targeting both higher percentage of royalty production and operating income
- Improving the sustainability of our dividend and debt
- Increasing our focus towards higher netback light oil
- Tax pools > \$1 billion

THE NEXT 20 YEARS – POSITIONED FOR SUCCESS

As a leading royalty focused oil and gas corporation, Freehold's objective is to continue to deliver long term attractive returns to shareholders.

Attractive Sustainable Yield

In late 2016 Freehold adopted a conservative, sustainable dividend policy of paying dividends within a 60%-80% adjusted payout ratio.

A 10+ Year Drilling Inventory on Royalty Lands

Freehold is pro-actively working with operators to identify and exploit new drilling opportunities.

Conservatively Managed With a Strong Balance Sheet

The Company prudently manages its long-term debt to maintain financial strength in the face of commodity price fluctuations.

Torque to Oil Upside

A \$10/bbl increase in WTI prices from \$50-\$60/bbl improves Freehold's free cash flow by 30%.

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following Management's Discussion and Analysis (MD&A) was prepared as of March 2, 2017 and is management's opinion about the consolidated operating and financial results of Freehold Royalties Ltd. and its wholly-owned subsidiaries (Freehold or the Company) for the year ended December 31, 2016 and previous periods, and the outlook for Freehold based on information available as of the date hereof.

The financial information contained herein was based on information in the consolidated financial statements, which have been prepared in accordance with International Financial Reporting Standards (IFRS), which are the Canadian generally accepted accounting principles (GAAP) for publicly accountable enterprises. All comparative percentages are between the years ended December 31, 2016 and 2015, and all dollar amounts are expressed in Canadian currency, unless otherwise noted. This MD&A should be read in conjunction with the audited financial statements and notes.

This MD&A contains non-GAAP financial measures and forward-looking statements that are intended to help readers better understand our business and prospects. Readers are cautioned that the MD&A should be read in conjunction with our disclosure under "Non-GAAP Financial Measures" and "Forward-looking Statements" included at the end of this MD&A.

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Business Overview

Freehold is a dividend-paying corporation incorporated under the laws of the Province of Alberta and trades on the Toronto Stock Exchange under the symbol FRU. Freehold is directly and indirectly involved in the development and production of oil and natural gas, predominantly in western Canada. We receive revenue from oil and natural gas properties as reserves are produced over the economic life of the properties. Our primary focus is acquiring and managing oil and natural gas royalties.

The Royalty Advantage

We manage one of the largest non-government portfolios of oil and natural gas royalties in Canada. Our total land holdings encompass approximately 6.1 million gross acres, greater than 95% of which are royalties. Of this, our mineral title lands (including royalty assumption lands), which we own in perpetuity, cover approximately 1.0 million acres. In addition, we have gross overriding royalty interests in approximately 4.9 million acres.

We have interests in more than 42,000 wells (of which over 40,000 are royalty wells including over 20,000 unitized wells). We receive royalty income from over 300 industry operators. Royalty rates vary from less than 1.0% (for some gross overriding royalties) to 22.5% (for some lessor royalties). This diversity lowers our risk, and as a royalty owner we benefit from the drilling activity of others on our lands.

As a royalty interest owner, we generally do not pay any of the capital costs to drill and equip the wells for production on most of our properties, nor do we incur costs to operate the wells, maintain production, and ultimately restore the land to its original state. Generally all of these costs are paid by others. On the majority of our production, we receive royalty income from gross production revenue (revenue before any royalty expenses and operating costs are deducted). Our high percentage of operating income from royalties (93% in 2016) results in strong netbacks.

When Freehold was formed in 1996, all of our royalty lands were leased to third parties and producing. Over the years, our unleased mineral title acreage has grown – through acquisitions, lease expiries, surrenders, and defaults. We now have approximately 380,000 acres of unleased mineral titles.

Our Strategy

As a leading royalty oil and gas corporation, Freehold's objective is to deliver growth and low risk attractive returns to shareholders over the long term. Freehold accomplishes this by:

- Creating value,
 - » Drive oil and gas development on our lands through our lease out programs.
 - » Acquire royalty assets with acceptable risk profiles and long economic life.
 - » Generate gross overriding royalties for revenue growth.
- Enhancing value,
 - » Maximize our royalty interests through a comprehensive audit program.
 - » Manage our debt prudently with a target of 0.5-1.5 times net debt to funds from operations.
- Delivering value,
 - » Target a dividend within an adjusted payout ratio of 60%-80%.

2016 Highlights

2016 marked a strong year for Freehold as the Company was able to achieve another record year of production while managing our cash flows and debt levels to ensure continued sustainability of our dividend for our shareholders. Reduction of our overall debt aided by our free cash flow and a continued trending down of our cash costs, improved our already strong cash margins. Moving forward, we expect to continue to position ourselves as a low risk entity, able to maintain sustainability through all commodity price cycles.

Operationally, Freehold had one of its best years with production reaching record highs averaging 12,219 boe/d and representing 12% growth year-over-year. Strength in production was associated with a major acquisition, an active comprehensive audit function, and growth within our existing royalty portfolio. We continue to see a higher percentage of drilling on our lands relative to the Western Canadian Sedimentary Basin, which is a testament to the quality of our royalty assets. In May 2016, we added a quality royalty portfolio from Husky Energy Inc. and certain of its affiliates (the Husky Transaction), nearly doubling our royalty land base and adding a low decline royalty stream. We see this acquisition as adding value for multiple years with drilling on the acquired lands already outpacing expectations.

ANNUAL HIGHLIGHTS

(\$000s, except as noted)

	2016	2015	2014
Royalty and other revenue	129,968	135,664	199,850
Revenue, net of royalty expense	128,651	133,367	194,184
Net income (loss)	(11,163)	(4,080)	66,447
Per share, basic and diluted (\$)	(0.10)	(0.05)	0.94
Funds from operations	94,211	103,820	138,447
Per share (\$)	0.85	1.15	1.95
Total assets	1,007,450	939,394	653,277
Long-term debt	84,000	152,000	139,000
Total long-term liabilities	108,637	179,826	205,447
Dividends declared	59,502	90,139	119,788
Per share (\$) ⁽¹⁾	0.54	1.00	1.68
Net debt	73,161	146,949	135,810
Weighted average shares outstanding, basic (000s)	110,391	90,505	71,029
Shares outstanding at year-end (000s)	117,918	98,940	74,919
Average daily production (boe/d) ⁽²⁾	12,219	10,945	9,180
Operating netback (\$/boe) ^{(2) (3)}	24.83	28.83	52.30

(1) Based on the number of shares issued and outstanding at each record date.

(2) See Conversion of Natural Gas to Barrels of Oil Equivalent (boe).

(3) See Non-GAAP Financial Measures.

- Achieved record production with volumes averaging 12,219 boe/d, representing a 12% increase versus the same period last year. Volumes were comprised of 58% oil and liquids and 42% natural gas. On the royalty side volumes averaged 9,936 boe/d, representing a 20% increase versus 2015.
- Funds from operations totaled \$94.2 million or \$0.85/share. This was down from \$103.8 million or \$1.15/share in 2015 reflecting continued weakness in commodity prices.
- Declared dividends were \$59.5 million (\$0.54/share), down from \$90.1 million (\$1.00/share) in 2015, reflecting lower funds from operations and a conservative payout strategy.

- Ended 2016 with net debt of \$73.2 million, implying net debt to funds from operations of 0.8 times. At year end we had nearly \$180 million in available room within our credit facility.
- Executed a major transaction, acquiring a \$162 million royalty package; further diversifying our land base by adding approximately 2.5 million acres of royalty land, increasing our total royalty lands to approximately 5.9 million acres.
- Proved plus probable reserves totaled 38.3 mmboc, up from 36.1 mmboc in 2015.

Outlook

Business Environment

2016 represented a year of both highs and lows for Freehold, mainly driven by volatility in the underlying commodity price environment. For the year, West Texas Intermediate (WTI) prices averaged US\$43.32/bbl, representing an 11% decline versus 2015 and significantly below the trailing three year average. Similarly, on the natural gas side, AECO prices averaged \$2.09/mcf, down 25% versus 2015. As a result of sustained commodity weakness, Freehold reduced its monthly dividend early in the year, however we have seen prices trend-up and stabilize through the back half of 2016 and we believe we are positioned to provide a sustainable dividend to our shareholders moving forward. Despite some of the challenges in the commodity price environment, Freehold's dividend-adjusted share price increased 35% through 2016, in-line with the returns of the TSX Energy Index and outpacing the TSX Composite Index.

In late January, the Petroleum Services Association of Canada (PSAC) updated its 2017 drilling forecast. The group is currently projecting 5,150 wells drilled through 2017, representing a 23% increase from the original 2017 forecast published in early November 2016. PSAC based its 2017 forecast on average natural gas prices of \$3.00/mcf AECO and a WTI price of U.S.\$52.50/bbl.

Drilling Activity

Including drilling associated with acquisitions, 281 (13.9 net) wells were drilled on our royalty lands in 2016, a 25% decrease versus 2015. The fourth quarter saw a resurgence in activity on our land with 125 gross (7.8 net) locations drilled, representing over 50% of our net annual total. Activity through the quarter was focused in the greater Dodsland area with the new operator accelerating activity and drilling 16 new locations. In southeast Saskatchewan we also saw traditional players increase activity with 25 wells drilled. In addition, incremental drilling also targeted prospects in the Alberta Viking, the Cardium and in heavy oil.

On the lands acquired in 2016, 56 locations were drilled, materially higher than our initial forecast for the year. Of these wells 37 were drilled in the fourth quarter, mostly in southwest Saskatchewan, in Alberta Viking and in the Deep Basin.

Subsequent Event

In keeping with our strategy of making accretive acquisitions that complement our existing portfolio, in February 2017 Freehold closed a \$34 million acquisition of various gross overriding royalties and mineral title lands in the greater Dodsland area of Saskatchewan. There were 32,000 acres of royalty land acquired with current estimated production of 185 boe/d (91% oil). The transaction strengthens our position in the Dodsland Viking play, with development expected to remain strong at current commodity price levels.

2017 Guidance Update

The table below summarizes our key operating assumptions for 2017:

- We have increased our production guidance from 11,000 boe/d to a range of 11,300 to 11,800 boe/d, due to production additions on our royalty lands along with recently added acquisition volumes. Volumes are expected to be weighted approximately 55% oil and natural gas liquids (NGL) and 45% natural gas. We continue to maintain our royalty focus with royalty production accounting for 84% of forecasted 2017 production and 91% of operating income.
- We have increased our WTI and WCS price assumptions from US\$50.00/bbl and \$46.00/bbl to US\$52.00/bbl and \$49.00/bbl respectively.
- We have revised downward our 2017 AECO natural gas price assumption from \$3.00/mcf to \$2.60/mcf.
- We have revised our G&A expense assumption from \$2.65/boe to \$2.60/boe reflecting the increased production guidance.
- After increasing our monthly dividend by 25% from \$0.04 to \$0.05 per share (see Change to Dividend), we expect our 2017 adjusted payout ratio ((cash dividends plus capital expenditures)/funds from operations) to be approximately 65%.
- We forecast year-end net debt to funds from operations of approximately 0.6 times based on our revised key operating assumptions.

KEY OPERATING ASSUMPTIONS

2017 Annual Average		Guidance Dated	
		Mar. 2, 2017	Nov. 8, 2016
Daily production	boe/d	11,300-11,800	11,000
WTI oil price	US\$/bbl	52.00	50.00
Western Canadian Select (WCS)	Cdn\$/bbl	49.00	46.00
AECO natural gas price	Cdn\$/Mcf	2.60	3.00
Exchange rate	Cdn\$/US\$	0.76	0.75
Operating costs	\$/boe	3.25	3.25
General and administrative costs ⁽¹⁾	\$/boe	2.60	2.65
Capital expenditures	\$ millions	6	6
Weighted average shares outstanding	millions	118	118

(1) Excludes share based compensation.

Recognizing the cyclical nature of the oil and gas industry, we continue to closely monitor commodity prices and industry trends for signs of changing market conditions. We caution that it is inherently difficult to predict activity levels on our royalty lands since we have no operational control. As well, significant changes (positive or negative) in commodity prices (including Canadian oil price differentials), foreign exchange rates, or production rates may result in adjustments to the dividend rate.

A sensitivity analysis of the potential impact of key variables on funds from operations per share is provided below. For the purposes of the sensitivity analysis, the effect of a change in a particular variable is calculated independently of any change in another variable. In reality, changes in one factor will contribute to changes in another, which can magnify or counteract the sensitivities. For instance, trends have shown a correlation between the movement in the foreign exchange rate of the Canadian dollar relative to the U.S. dollar and the benchmark WTI crude oil price.

Variable ⁽¹⁾	Change (+/-)	Estimated Change in Funds from Operations (\$/share)
WTI oil price	US\$1.00/bbl	0.03
Canadian/U.S. dollar exchange rate	US\$0.01	0.02
Edmonton Light Sweet/WCS differential	Cdn\$1.00/bbl	0.01
AECO natural gas price	Cdn\$0.25/Mcf	0.02
Interest rate	1%	0.01
Oil and NGL production	100 bbls/d	0.02
Natural gas production	1,000 Mcf/d	0.01

(1) Calculations are performed independently and may not be indicative of actual results that would occur when multiple variables change at the same time.

Change to Dividend

With stabilizing oil prices and increased production guidance, Freehold's Board of Directors (the Board) has approved an increase to its monthly dividend to \$0.05 per share from \$0.04 per share. The Board of Directors has declared a dividend of Cdn. \$0.05 per common share to be paid on April 17, 2017 to shareholders of record on March 31, 2017. The dividend is designated as an eligible dividend for Canadian income tax purposes.

The dividend increase is in-line with our previously stated dividend policy which outlined a 60% to 80% adjusted payout ratio based on forward looking funds from operations. Based on our current guidance and commodity price assumptions, and assuming no significant changes in the current business environment, we expect to maintain the revised monthly dividend rate through the next quarter. We will continue to evaluate the commodity price environment and adjust the dividend levels as necessary (subject to the quarterly review and approval of our Board of Directors – see Dividend Policy).

Quarterly Performance

Fourth Quarter Highlights

Freehold delivered strong operational results in the fourth quarter of 2016. Some of the highlights included:

- Freehold's production averaged a record 12,579 boe/d, a 6% improvement over Q4-2015 and 2% increase over Q3-2016. Gains in production were largely driven by volumes associated with the Husky Transaction, better than expected third party production additions and the strength of our audit function (over 400 boe/d of prior period adjustments in the quarter, which includes compensatory royalties on our mineral title lands).
- Royalty production was up 12% compared to Q4-2015 averaging 10,351 boe/d and accounted for 93% of operating income and 82% of production.
- Q4-2016 royalty and other revenue was up 18% to \$39.9 million versus \$33.8 million in the previous year due to increased production and higher average price realizations.
- Funds from operations totaled \$30.4 million, an increase of 19% due to higher volumes and commodity prices. On a per share basis, funds from operations were \$0.26/share in Q4-2016, up from \$0.21/share in Q3-2016.
- Net income was \$1.6 million compared to a \$7.4 million loss in Q4-2015, which resulted from an \$8.0 million impairment charge.

- Freehold generated \$14.1 million in free cash flow ⁽¹⁾, over and above our dividend, which we applied to outstanding debt. As a result, at December 31, 2016, net debt totaled \$73.2 million, down from \$87.3 million at September 30, 2016, implying a net debt to 12-month trailing funds from operations ratio of 0.8 times.
- Cash costs ⁽¹⁾ for the quarter totaled \$7.83/boe, up slightly from \$7.63/boe in Q4-2015, as we saw operating costs add approximately \$0.7 million (\$0.60/boe) for charges relating to prior periods.
- Wells drilled on our royalty lands totaled 125 (7.8 net) in the quarter, up from 48 (2.3 net) in the previous quarter.
- In Q4-2016, Freehold issued 9 leases; 93 leases were issued in 2016, 63 relating to the Q2-2016 Husky Transaction.
- Dividends declared for Q4-2016 totaled \$0.12 per share, unchanged from the previous quarter and down from \$0.21 per share one year ago.
- Basic payout ratio ⁽¹⁾ (dividends declared/funds from operations) for Q4-2016 totaled 46% while the adjusted payout ratio ⁽¹⁾ ((cash dividends plus capital expenditures)/funds from operations) for the same period was 53%.

(1) See Non-GAAP Financial Measures.

2016 Performance Compared to Guidance

Compared to Our November 2016 Guidance:

- Average production for the year was 219 boe/d higher than guidance due to better than expected production additions on our royalty lands and volumes added through our audit function.
- Average oil prices, both for WTI and WCS were slightly ahead of our forecasts as prices improved through the fourth quarter.
- Operating costs were slightly higher than forecast as we incurred charges relating to prior periods in the fourth quarter.
- General and administrative charges were somewhat lower than forecast reflecting increased royalty production.

2016 KEY OPERATING ASSUMPTIONS

2016 Annual Average	2016 Actual Results	Nov. 8, 2016	Aug. 4, 2016	May 11, 2016	Mar. 3, 2016	Nov. 12, 2016
Daily production	boe/d	12,219	12,000	11,700	11,400	9,800
WTI oil price	US\$/bbl	43.32	43.00	40.00	40.00	35.00
Western Canadian Select (WCS)	Cdn\$/bbl	38.90	38.00	34.00	34.00	31.00
AECO natural gas price	Cdn\$/Mcf	2.09	2.10	2.00	1.80	2.00
Exchange rate	Cdn\$/US\$	0.76	0.76	0.76	0.77	0.72
Operating costs	\$/boe	3.94	3.75	3.75	4.00	4.75
General and administrative costs ⁽¹⁾	\$/boe	2.28	2.35	2.40	2.50	2.65
Capital expenditures	\$ millions	5	6	7	7	15
Dividends paid in shares (DRIP) ⁽²⁾	\$ millions	5	5	5	8	13
Weighted average shares outstanding	millions	110	110	110	109	100

(1) Excludes share based compensation.

(2) Effective with the August 2016 dividend the Board approved the suspension of the DRIP pending further notice.

Quarterly Performance and Seasonality

Quarterly variances in revenues, net income (loss) and funds from operations are caused mainly by fluctuations in commodity prices and production volumes. Crude oil prices are generally determined by global supply and demand factors, and the variances do not have seasonable predictability. Natural gas is a typically seasonal, weather-dependent fuel; demand is generally higher during the winter (for heating) and summer (for cooling), and lower during the spring and fall. Over most of the past eight quarters, this seasonality has been muted by ample supply.

Our financial results over the last eight quarters were influenced by the following significant changes:

- The decision by OPEC in late 2014 to keep production at existing levels resulted in a material retreat in worldwide crude oil prices with prices remaining weak through 2015 and 2016.
- Fluctuations in foreign exchange rates affected our oil price realizations, resulting in positive impacts on our Canadian dollar oil revenues relative to the benchmark WTI, which is referenced in U.S. dollars.
- AECO prices continue to be impacted by supply outstripping demand. Strong gains in North American natural gas supply associated with horizontal drilling within shale gas plays has resulted in increased production deliverability.
- The largest effect on our dividends is from funds from operations, which is mainly a function of revenues and cash expenses. The collapse in oil prices in 2015 and 2016 resulted in changes to our monthly dividend from \$0.14 to \$0.09 in Q1-2015, from \$0.09 to \$0.07 in Q3-2015, and from \$0.07 to \$0.04 in Q1-2016.
- Production has been affected by drilling activity and acquisitions, as well as a number of one-time adjustments. We use government reporting databases and past production receipts to estimate revenue accruals. Due to the large number of wells in which we have royalty interests, the nature of royalty interests, the lag in receiving production receipts, and our audit program, our reported royalty volumes usually include both positive and negative adjustments related to prior periods.
- Over the past eight quarters, we have acquired \$574 million of mainly royalty assets in Alberta and Saskatchewan. This activity affects our revenues, percentage royalty interests, oil/gas production split and debt levels, among others.

The accompanying table illustrates the fluctuations experienced over the past eight quarters and the resulting effect on our financial results. Additional information about our quarterly results is provided in our interim reports, copies of which are available on SEDAR and on our website.

QUARTERLY REVIEW

	2016				2015			
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Financial (\$000s, except as noted)								
Revenue, net of royalty expense	39,439	32,639	31,903	24,670	33,728	35,391	37,222	27,026
Funds from operations ⁽¹⁾	30,421	24,148	24,142	15,500	25,509	27,643	28,730	21,938
Per share, basic (\$)	0.26	0.21	0.23	0.16	0.26	0.28	0.32	0.29
Net income (loss) ⁽¹⁾	1,638	(1,962)	(2,249)	(8,590)	(7,423)	(22,193)	3,919	21,617
Per share, basic and diluted (\$)	0.01	(0.02)	(0.02)	(0.09)	(0.08)	(0.23)	0.04	0.29
Dividends declared	14,144	14,133	13,380	17,845	20,747	24,604	24,459	20,329
Per share (\$) ⁽²⁾	0.12	0.12	0.12	0.18	0.21	0.25	0.27	0.27
Basic payout ratio (%) ⁽³⁾	46	59	55	115	81	89	85	93
Operating Income ⁽³⁾	34,487	28,231	28,011	20,292	29,186	30,601	32,733	22,632
Operating income from royalties (%)	93	93	91	97	89	90	85	83
Dividends paid in shares (DRIP)	-	1,170	1,443	2,384	2,758	3,708	2,398	8,361
Average DRIP participation rate (%) ⁽⁴⁾	-	8	11	11	13	14	11	35
Acquisitions	92	68	162,211	219	(143)	815	342,310	68,370
Capital expenditures	2,172	209	753	2,084	5,607	7,969	2,750	5,969
Net debt	73,161	87,301	98,191	149,197	146,949	148,994	146,992	198,834
Shares outstanding								
Weighted average, basic (000s)	117,847	117,726	106,736	99,093	98,731	98,357	89,388	75,199
At quarter end (000s)	117,918	117,850	117,652	99,284	98,940	98,599	98,203	75,457
Operating (\$/boe, except as noted)								
Average daily production (boe/d) ⁽⁵⁾	12,579	12,281	12,041	11,974	11,815	11,266	10,617	10,058
Royalty interest (%)	82	83	81	79	78	78	76	71
Average selling price	33.72	28.69	28.48	22.23	30.34	34.11	38.63	29.80
Operating netback ⁽³⁾	29.80	24.99	25.57	18.62	26.85	29.52	33.88	25.01
Operating expenses	4.28	3.90	3.55	4.02	4.18	4.62	4.65	4.85
Working interest properties	24.16	22.69	18.47	19.41	19.24	20.78	19.14	16.87
General and administrative expenses ⁽⁶⁾	2.33	1.71	2.04	3.05	2.23	2.33	2.34	3.92
Benchmark Prices								
WTI crude oil (US\$/bbl)	49.29	44.94	45.59	33.45	42.18	46.43	57.94	48.64
Exchange rate (US\$/Cdn\$)	0.75	0.77	0.78	0.73	0.75	0.76	0.81	0.81
Edmonton Light Sweet crude oil (Cdn\$/bbl)	61.54	54.85	54.70	40.84	52.89	56.23	67.75	51.95
Western Canadian Select (WCS) (Cdn\$/bbl)	46.63	41.02	41.62	26.32	36.86	43.29	56.97	42.14
AECO natural gas (Cdn\$/Mcf)	2.81	2.20	1.25	2.11	2.65	2.80	2.67	2.95

(1) For the three months ended September 30, 2016, net loss and funds from operations include a \$1.1 million loss upon settlement of litigation.

(2) Based on the number of shares issued and outstanding at each record date.

(3) See Non-GAAP Financial Measures.

(4) The dividend reinvestment plan (DRIP) was suspended effective with the August 2016 dividend, pending further notice.

(5) Reported production for a period may include adjustments from previous production periods.

(6) Excludes share based compensation.

QUARTERLY REVIEW CONTINUED

	2016				2015			
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Share Trading Performance								
High (\$)	15.16	13.09	13.00	12.05	13.52	16.07	19.04	20.62
Low (\$)	11.68	10.61	9.66	8.29	9.00	8.73	15.86	16.14
Close (\$)	14.17	12.65	11.91	10.54	10.86	10.82	16.14	17.94
Volume (000s)	15,440	20,873	23,559	19,690	19,312	22,753	18,912	14,297

Revenues**Production**

As we hold primarily small royalty interests in over 40,000 wells, obtaining timely production data is extremely difficult. Thus, we use government reporting databases and past production receipts to estimate revenue accruals. Due to the large number of wells in which we have royalty interests, the nature of royalty interests, the lag in receiving production receipts, and our audit program, our reported royalty volumes usually include both positive and negative adjustments related to prior periods.

Our production was up 12% in 2016 due primarily to volumes added through acquisitions, production additions on our royalty lands and the strength of our audit function. Royalty interests comprised 81% of total production in 2016, up from 76% in 2015, as we added more royalty volumes through acquisitions and de-emphasized development of our working interest properties. Our production mix for 2016 was 42% natural gas, 16% heavy oil, 35% light and medium oil, and 7% NGLs. The Husky Transaction was the biggest reason for production increases in natural gas and NGLs.

Working interest production fell 13% in 2016 relative to 2015. Reduced volumes largely resulted from lower capital expenditures on development, as spending was \$5.2 million versus \$22.3 million in 2015.

PRODUCTION SUMMARY ⁽¹⁾

<i>(boe/d)</i>	2016	2015	Change
Royalty interest	9,936	8,310	20%
Working interest	2,283	2,635	-13%
Total	12,219	10,945	12%

(1) On certain properties where we have both a royalty interest and a working interest, production is allocated based on the applicable royalty and working interest percentages.

AVERAGE DAILY PRODUCTION BY PRODUCT TYPE

	2016	2015	Change
Light and medium oil (bbls/d)	4,293	3,956	9%
Heavy oil (bbls/d)	2,016	2,220	-9%
NGL (bbls/d)	804	581	38%
Total oil and NGL (bbls/d)	7,113	6,757	5%
Natural gas (Mcf/d)	30,632	25,123	22%
Oil equivalent (boe/d)	12,219	10,945	12%
Total annual production (Mboe)	4,472	3,995	12%
Potash (tonnes/d)	12	8	50%

Product Prices

The following table is a summary of average benchmark prices.

AVERAGE BENCHMARK PRICES

	2016	2015	Change
WTI crude oil (US\$/bbl)	43.32	48.80	-11%
Exchange rate (US\$/Cdn\$)	0.76	0.78	-3%
Edmonton Light Sweet crude oil (Cdn\$/bbl)	52.98	57.20	-7%
Western Canadian Select (Cdn\$/bbl)	38.90	44.81	-13%
WTI/Edmonton Light Sweet differential (\$/bbl)	9.66	8.40	15%
Edmonton Light Sweet/WCS differential (Cdn\$/bbl)	(14.08)	(12.39)	14%
AECO natural gas (Cdn\$/Mcf)	2.09	2.77	-25%

The price we receive for our oil production is primarily driven by the U.S. dollar price of West Texas Intermediate (WTI). Therefore, a decrease in the value of the Canadian dollar relative to the U.S. dollar will increase the revenue received. Acquisition and development activity in lighter oil properties resulted in a \$3.48/bbl premium to the benchmark WCS versus a \$2.19/bbl premium in 2015.

Our average selling prices reflect product quality and transportation differences from benchmark prices. On a boe basis, our average selling price was 15% lower in 2016 reflecting weakness across crude oil (WTI/Edmonton Light Sweet/WCS) and AECO natural gas, offset slightly by weakness in the US\$/Cdn\$ exchange rate.

AVERAGE SELLING PRICES

	2016	2015	Change
Oil (\$/bbl)	42.38	47.00	-10%
NGL (\$/bbl)	29.58	27.14	9%
Oil and NGL (\$/bbl)	40.93	45.29	-10%
Natural gas (\$/Mcf)	1.81	2.28	-21%
Oil equivalent (\$/boe)	28.37	33.20	-15%
Potash (\$/tonne)	332.59	416.86	-20%

Marketing and Hedging

Our production remained unhedged in 2016. Our hedging policy is reviewed quarterly with the Board of Directors.

Royalty interests

Our royalty lands consist of a large number of properties with generally small volumes per property. Many of our leases and royalty agreements allow us to take our share of oil and natural gas in-kind. As part of our risk mitigation program we carefully monitor our royalty receivables and may choose to take our royalty in-kind if there are benefits in doing so. In 2016 we took in-kind and marketed approximately 16% of our total royalty production using 30-day contracts.

Working interests

We market most of our working interest oil production using 30-day contracts to ensure competitive pricing. In 2016 approximately 60% of our working interest natural gas production was taken in-kind and sold under marketing arrangements tied to the Alberta monthly or daily spot price (AECO) or other indexed referenced price, with the balance being marketed with the operators' production.

Royalty and Other Revenue

Royalty and other revenue in 2016 was 4% lower than in 2015 largely due to lower realized pricing partially offset by higher production volumes. Royalty revenues increased by 4% whereas working interest revenues were down 26% versus 2015, due to our royalty production focus.

ROYALTY AND OTHER REVENUE BY PRODUCT

(\$000s)	2016	2015	Change
Royalty interest revenue			
Oil	76,482	76,135	0%
NGL	7,369	4,671	58%
Natural gas	16,953	16,735	1%
Other ⁽¹⁾	2,660	2,394	11%
	103,464	99,935	4%
Working interest revenue			
Oil	21,377	29,828	-28%
NGL	1,340	1,079	24%
Natural gas	3,351	4,182	-20%
Other ⁽¹⁾	436	640	-32%
	26,504	35,729	-26%
Total royalty and other revenue			
Oil	97,859	105,963	-8%
NGL	8,709	5,750	51%
Natural gas	20,304	20,917	-3%
Other ⁽¹⁾	3,096	3,034	2%
	129,968	135,664	-4%

(1) Other includes potash, sulphur, lease rentals, and other revenue for royalty interest revenue, and processing fees, interest and other revenue for working interest revenue.

The accompanying table demonstrates the net effect of price and volume variances on royalty and other revenue. Weakness in both oil and natural gas prices accounted for the bulk of the negative variance in 2016, but this was offset partially by our increased production.

REVENUE VARIANCES

(\$000s)	2016 vs. 2015	2015 vs. 2014
Oil and NGL		
Production increase	5,618	16,316
Price decrease	(10,763)	(72,553)
Net decrease	(5,145)	(56,237)
Natural gas		
Production increase	3,694	3,892
Price decrease	(4,307)	(12,371)
Net decrease	(613)	(8,479)
Other ⁽¹⁾	62	530
Royalty and other revenue decrease	(5,696)	(64,186)

(1) Other includes potash, sulphur, lease rentals, processing fees, interest and other.

Other Income (Loss)

In May 2009, a statement of claim was filed against Freehold for \$9 million. The claim involved disputed land interests and royalty obligations. During the year ended December 31, 2016 Freehold settled the claim with a \$0.9 million payment and removed \$0.2 million of associated accounts receivable, recognizing a total loss of \$1.1 million.

During the year ended December 31, 2015 Freehold recognized \$0.8 million of other income as a result of a settlement with Canpar Holdings Ltd. on certain lands where both companies have a mineral title interest (see Related Party Transactions).

Expenses

Royalty Expense and Mineral Taxes

Oil and gas producers pay royalties to the owners of mineral rights from whom they have acquired leases. These are paid to the Crown (provincial and federal governments) and freehold mineral title owners. Crown royalty rates are tied to commodity prices and the level of oil and gas sales.

We do not incur royalty expense on production from our royalty interest lands, other than minor freehold mineral taxes. As the royalty owner, we receive the royalty as income from other companies. Royalty expense dropped by 43% largely due to a decrease in production and revenue on our working interest properties.

ROYALTY EXPENSES ⁽¹⁾

(\$000s, except as noted)	2016	2015	Change
Working interest	1,226	2,109	-42%
Per boe (\$)	1.47	2.19	-33%
Royalty interest	91	188	-52%
Per boe (\$)	0.03	0.06	-50%
Total	1,317	2,297	-43%
Per boe (\$)	0.29	0.57	-49%

(1) Royalty expense includes both Crown charges and royalty payments to third parties.

Operating Expenses

Operating expenses are comprised of direct costs incurred and costs allocated among oil, natural gas, and NGL production. Overhead recoveries associated with operated properties are included in operating expenses and accounted for as a reduction to general and administrative (G&A) expenses. A percentage of operating expense is fixed and, as such, per boe operating expenses are highly variable to production volumes.

On a total production per boe basis, operating expense decreased 14% in 2016, largely due to an increase in our percentage of production from royalties, which have no operating expense. Working interest operating expenses increased by 11% on a per boe basis largely as a result of the effect of fixed costs on decreasing production and approximately \$0.7 million of prior period charges.

OPERATING EXPENSES

<i>(\$000s, except as noted)</i>	2016	2015	Change
Working interest	17,630	18,215	-3%
Per boe (\$)	21.10	18.94	11%
Royalty interest ⁽¹⁾	-	-	-
Per boe (\$)	-	-	-
Total operating expenses	17,630	18,215	-3%
Per boe (\$)	3.94	4.56	-14%

(1) We do not incur operating expenses on production from our royalty lands.

Netback Analysis

As a royalty owner, we share in production revenue without incurring the operational costs, risks, and responsibilities typically associated with oil and natural gas operations. The following tables demonstrate the advantage of our royalty lands, which have no operating or royalty expenses other than minor freehold mineral taxes. Royalty interests accounted for 80% of royalty and other revenue in 2016 and more importantly contributed 93% of operating income.

2016 OPERATING INCOME ⁽¹⁾

(\$000s)	Royalty Interest	Working Interest	Total
Royalty and other revenue ⁽²⁾	103,464	26,504	129,968
Royalty expense ⁽³⁾	(91)	(1,226)	(1,317)
Net revenue	103,373	25,278	128,651
Operating expense	-	(17,630)	(17,630)
Operating income	103,373	7,648	111,021
Percentage by category	93%	7%	100%

2016 OPERATING NETBACK ⁽¹⁾

(\$ per boe)	Royalty Interest	Working Interest	Total
Royalty and other revenue ⁽²⁾	28.45	31.72	29.06
Royalty expense ⁽³⁾	(0.03)	(1.47)	(0.29)
Net revenue	28.42	30.25	28.77
Operating expense	-	(21.10)	(3.94)
Operating netback	28.42	9.15	24.83

2016 VS. 2015 OPERATING NETBACK ⁽¹⁾

(\$ per boe)	2016	2015	Change
Royalty interest	28.42	32.89	-14%
Working interest	9.15	16.02	-43%
Total	24.83	28.83	-14%

(1) See Non-GAAP Financial Measures.

(2) Royalty and other revenue includes oil and NGLs, natural gas, potash, sulphur, lease rentals, processing fees, interest, and other.

(3) Royalty expense includes both Crown charges and royalty payments to third parties.

General and Administrative Expenses

We have significant land administration, accounting and auditing requirements to administer and collect royalty payments, including systems to track development activity on the royalty lands. General and administrative (G&A) expenses include direct costs and reimbursement of G&A expenses incurred by Rife Resources Management Ltd. (the Manager) on behalf of Freehold (see Related Party Transactions).

In 2016, on a total dollar basis, G&A expenses were down 4% with cost reduction initiatives more than offsetting increased acquisition integration costs. On a per boe basis costs were down 14% year over year aided by increased production volumes.

GENERAL AND ADMINISTRATIVE EXPENSES

(\$000s, except as noted)	2016	2015	Change
General and administrative expenses,			
before capitalized and overhead recoveries	11,772	12,299	-4%
Less: capitalized and overhead recoveries	(1,588)	(1,656)	-4%
General and administrative expense	10,184	10,643	-4%
Per boe (\$)	2.28	2.66	-14%

Management Fees

The Manager (see Related Party Transactions) receives a management fee in shares. In accordance with the previous amended and restated management agreement, the issue of shares from treasury related to the DRIP and equity offerings resulted in pro-rata increases in the number of shares issued as the management fee (see Shareholders' Capital). This agreement was amended in November 2015 (filed on SEDAR) and as a result the management fee was capped at 71,912 shares per quarter for 2016 and will be reduced to a level of 5,500 shares by 2023. The value associated with the management fee was down 4% compared to 2015 even though the number of shares increased, due to the effect of a lower Freehold share price. The quarterly management fee for 2017 will be 55,000 shares per quarter.

MANAGEMENT FEES (PAID IN SHARES)

	2016	2015	Change
Shares issued in payment of management fees	287,648	269,978	7%
Ascribed value (\$000s) ⁽¹⁾	3,543	3,693	-4%
Per boe (\$)	0.79	0.92	-14%

(1) The ascribed value of the management fees is based on the closing share price at the end of each quarter.

Share Based Compensation

Long-Term Incentive Plan

We are responsible for funding a portion of the long-term incentive compensation plan (the LTIP) for employees of the Manager. The 2013 LTIP grants vested in the first quarter of 2016 and \$0.1 million of share based compensation was paid out. The 2012 LTIP grants vested in the first quarter of 2015 and \$0.5 million was paid out. In 2016 there was \$0.8 million of net LTIP expense largely due to Freehold's increase in share price over the course of the year.

Deferred Share Unit Plan

Fully-vested deferred share units (DSUs) are granted annually in the first quarter to non-management directors and are redeemable for an equal number of shares (less tax withholdings if necessary) after the director's retirement. Dividends declared prior to redemption are assumed to be reinvested in notional share units on the dividend payment date. In 2016 Freehold expensed \$0.4 million (2015 - \$0.7 million) of share based compensation with a corresponding offset to contributed surplus.

For the year-end December 31, 2016, retired directors redeemed a total of 84,567 DSUs, resulting in the issuance of 59,198 shares from treasury. In payment of withholding tax, a total of 25,369 DSUs were cancelled and the cash value of \$0.3 million was remitted to Canada Revenue Agency. For the year ended December 31, 2015 no DSUs were redeemed.

In January 2017 a retired director redeemed 63,418 DSUs, resulting in the issuance of 44,393 shares from treasury. In payment of withholding tax, 19,025 DSUs were cancelled and the cash value of \$0.3 million was remitted to Canada Revenue Agency.

As at December 31, 2016, there were 148,499 DSUs outstanding, and as at March 2, 2017, there were 113,373 DSUs outstanding.

Retirement Benefit Plan

Freehold pays its proportionate share of a retirement benefit for certain former employees of the Manager. The retirement benefit is payable in four equal installments upon retirement. Service costs are amortized on a straight-line basis over the expected average remaining service lifetime.

SHARE BASED COMPENSATION

<i>(\$000s, except as noted)</i>	2016	2015	Change
Gross LTIP	928	61	1421%
Less: capitalized portion	(167)	(11)	1418%
Net LTIP	761	50	1422%
Deferred share unit plan	442	705	-37%
Retirement benefit	5	11	-55%
Share based and other compensation	1,208	766	58%
Per boe (\$)	0.27	0.19	42%

Related Party Transactions

Freehold does not have any employees. Rife Resources Management Ltd. (the Manager) is the manager of Freehold. The Manager is a wholly-owned subsidiary of Rife Resources Ltd. (Rife), and two of Rife's directors are also directors of Freehold. Rife is 100% owned by the CN Pension Trust Funds (the pension funds for the employees of the Canadian National Railway Company), which in turn is a shareholder of Freehold. The Manager recovers its general and administrative costs and a portion of its long-term incentive plan and retirement benefit costs, and receives a quarterly management fee paid in shares. Canpar Holdings Ltd. (Canpar) is also managed by Rife and owned 100% by the CN Pension Trust Funds, and two of Canpar's directors are also directors of Freehold.

(a) Rife Resources Management Ltd.

The Manager provides certain services for a fee based on a specified number of shares per quarter, pursuant to the amended and restated management agreement. The amended and restated management agreement caps the management fee at 71,912 shares per quarter for 2016 and the number of shares to be issued per quarter as payment of the management fee decreases to a level of 5,500 shares per quarter by 2023. For the year ended December 31, 2016, Freehold issued 287,648 shares (2015 - 269,978) as payment of the management fee to the Manager pursuant to the management agreement. For the year ended December 31, 2016, the ascribed value of \$3.5 million (2015 - \$3.7 million) was based on the closing price of the shares on the last trading day of each quarter.

For the year ended December 31, 2016, the Manager charged \$9.0 million in general and administrative costs (2015 - \$9.0 million). At December 31, 2016, there was \$0.9 million (2015 - \$0.7 million) in accounts payable and accrued liabilities relating to these costs.

(b) Rife Resources Ltd.

Freehold maintains ownership interests in certain oil and gas properties operated by Rife. A portion of net operating revenues and capital expenditures represent joint operations amounts from Rife. At December 31, 2016, there was \$0.1 million (2015 - \$nil) in accounts receivable related to these transactions. At December 31, 2016, there was \$nil (2015 - \$nil) in accounts payable and accrued liabilities relating to these transactions.

In addition, Freehold receives royalties from Rife pursuant to various royalty agreements. For the year ended December 31, 2016, Freehold received royalties of approximately \$0.9 million (2015 - \$1.5 million). At December 31, 2016, there was \$0.1 million (2015 - \$0.1 million) in accounts receivable relating to these transactions.

(c) Canpar Holdings Ltd.

Freehold and Canpar share mineral title ownership rights in a substantial land base in western Canada. Generally, Canpar owns mineral rights that were below the deepest producing formation at the time that Freehold was created, and Freehold holds the balance of the mineral rights. Given the nature of the mineral rights, which are dependent upon hydrocarbon pool formation classification as well as third party drilling data which is subject to change and revision, significant uncertainty can exist with respect to the royalty ownership of wells drilled and completed on lands where both Freehold and Canpar hold the mineral rights.

During 2015, Freehold and Canpar evaluated certain of these royalty interests where, among other factors, the identification of the reservoir formation was not straight forward and therefore ultimate ownership of the royalty interest wells was uncertain between Freehold and Canpar. The project relating to the evaluation of these interests resulted in a settlement of \$0.8 million recognized in other income in 2015.

At December 31, 2016, there was \$nil (2015 - \$nil) in accounts receivable and accounts payable and accrued liabilities relating to transactions with Canpar.

(d) CN Pension Trust Funds

Concurrent with the closing of the bought deal public equity offering completed by Freehold on May 25, 2016, CN Pension Trust Funds invested approximately \$20 million through the purchase of 1,732,000 common shares on a non-brokered private placement basis. The price paid per common share by CN Pension Trust Funds pursuant to the private placement was the same price paid per common share by purchasers pursuant to the bought deal public equity offering.

Concurrent with the closing of the bought deal public equity offering completed by Freehold on May 6, 2015, CN Pension Trust Funds invested approximately \$33 million in Freehold through the purchase of 1,833,334 common shares on a non-brokered private placement basis. The price paid per common share by CN Pension Trust Funds pursuant to the private placement was the same price paid per common share by purchasers pursuant to the bought deal public equity offering.

All amounts owing to/from the Manager, Rife, and Canpar are unsecured, non-interest bearing and due on demand. All transactions were in the normal course of operations and were measured at the amount of consideration established and agreed to by both parties.

Expenses relating to compensation for key management personnel, considered to be Freehold's Board of Directors and Senior Management, are as follows:

KEY MANAGEMENT PERSONNEL COMPENSATION

<i>(\$000s)</i>	December 31, 2016	December 31, 2015
Short-term benefits (including employee wages and directors fees)	966	1,346
Share based compensation	640	723
Total	1,606	2,069

Interest and Financing

In 2016, interest and financing expense decreased due to lower debt levels. The average effective interest rate on advances under our credit facilities during 2016 was 2.9% (2015 – 2.9%).

INTEREST AND FINANCING

<i>(\$000s, except as noted)</i>	2016	2015	Change
Interest on operating line or other	5	-	-
Interest on long-term debt	4,573	5,696	-20%
Interest and financing expense	4,578	5,696	-20%
Per boe (\$)	1.02	1.43	-29%

Depletion and Depreciation

Petroleum and natural gas interests, including the costs of production equipment, future capital costs, estimated decommissioning costs, and directly attributable general and administrative costs, are depleted on the unit-of-production method based on estimated proved plus probable oil and gas reserves (see Critical Accounting Estimates). Reserves are independently evaluated at year-end. For December 31, 2016, the estimate of proved plus probable reserves was based on the independent evaluation dated December 31, 2016, adjusted for acquisitions, development, and production. The increase in depletion from 2015 to 2016 is a result of increased production volumes.

DEPLETION AND DEPRECIATION

<i>(\$000s, except as noted)</i>	2016	2015	Change
Depletion and depreciation	104,159	95,703	9%
Per boe (\$)	23.29	23.96	-3%

Impairment

There were no indicators of impairment or impairment reversal in any of Freehold's Cash Generating Units (CGUs) for the year ended December 31, 2016. As a result no impairment or impairment reversal testing was conducted.

At December 31, 2015 Freehold tested its two working interest CGUs for impairment due to the continued drop in expected future commodity prices as recognized by industry reserve evaluators. Freehold estimated the recoverable amount as the value in use based on discounted future net cash flows of proved and probable reserves using forecast prices and costs, discounted at 10% (pre-tax). In determining the discount rate, Freehold considered an estimated industry weighted cost of capital and the resource composition of the assets. The estimate was based on Freehold's December 31, 2015 reserve report. Management recognizes that all assumptions and estimates affecting the value are subject to a high degree of uncertainty.

In 2015 Freehold recognized a non-cash impairment charge on its Southeast Saskatchewan Working Interest CGU of \$8.0 million as the carrying value exceeded the estimated value in use. The Southeast Saskatchewan Working Interest CGU contains all of Freehold's working interest properties in southeast Saskatchewan. The estimated recoverable amount of the Southeast Saskatchewan CGU at December 31, 2015 is \$29.1 million. In addition, Freehold recognized a non-cash impairment charge on its Other Working Interest CGU of \$30.8 million as the carrying value exceeded the estimated value in use. The Other Working Interest CGU contains Freehold's diverse group of working interest properties outside of the Southeast Saskatchewan Working Interest CGU. The estimated recoverable amount of the Other Working Interest CGU at December 31, 2015 is \$54.7 million.

Income Tax

As a corporation, taxable income is based on revenues (which will vary depending on commodity prices and production volumes) less allowable expenses including claims for both accumulated tax pools and tax pools associated with current year expenditures. In 2016 corporate federal and provincial income tax rates for Freehold were approximately 27% (2015- 26%).

In 2016 Freehold had no current tax expense, and a \$3.1 million deferred tax recovery, as use of tax pools offset Freehold's income. Freehold had a deferred income tax asset of \$26.4 million at December 31, 2016 partially as a result of the corporate acquisition described below.

Freehold's 2015 tax expense was affected by a corporate acquisition that created a \$55.4 million deferred income tax asset based on approximately \$220 million of tax pools and a statutory rate of approximately 25% at the time of the transaction. The difference between the consideration paid and the net assets acquired resulted in a non-cash accounting gain of \$24.3 million. The deferred tax asset resulting from the corporate acquisition was further adjusted upwards by a change in 2015 to Alberta's corporate tax rate for future periods to 27% and the tax effect of the impairment charge at 27%. The current income tax recovery of \$5.1 million in 2015 was the result of additional deductions for prior tax years made upon actual filing of our tax returns.

Tax Pools

We are entitled to claim certain tax deductions available to all owners of oil and gas properties. Freehold's tax pools increased in 2016 primarily associated with acquisition activity. The tax pools below are deductible at various rates.

TAX POOLS ⁽¹⁾

(\$000s)	2016	2015	Change
Canadian oil and gas property expense (10% declining balance)	747,912	668,256	12%
Canadian development expense (30% declining balance)	60,867	85,406	-29%
Capital cost allowance (generally 25%)	24,864	30,738	-19%
Share issue costs	17,917	16,351	10%
Non-capital losses	176,445	165,356	7%
Total	1,028,005	966,107	6%

(1) These amounts, subject to review by Canada Revenue Agency, represent Freehold's direct tax pools as well as the tax pools of its subsidiaries.

Liquidity and Capital Resources

We define capital as long-term debt, shareholders' equity, and working capital. We manage our capital structure taking into account operating activities, debt levels, debt covenants, capital expenditures, DRIP participation, dividend levels, and taxes, among others. We also consider changes in economic conditions and commodity prices as well as the risk characteristics of our assets. We have a depleting asset base, and ongoing development activities and acquisitions are necessary to replace production and extend reserve life. From time to time, we may issue shares or adjust capital spending to manage current and projected debt levels.

Operating Activities

In 2016 there was a net loss of \$11.2 million compared to a \$4.1 million net loss in 2015. The larger loss was a result of lower revenues and higher depletion and depreciation expense from our higher production volumes, offset somewhat by lower income tax expense. In addition, 2015 was affected by a \$24.3 million gain on corporate acquisition offset by a \$38.8 million impairment charge.

Funds from operations in 2016 were \$94.2 million versus \$103.8 million in 2015. The decrease was caused by lower commodity prices which caused lower revenues, even with increased production rates. 2015 was affected positively by a \$5.1 million current income tax recovery but there was no current income tax expense or recovery in 2016. We consider funds from operations to be a key measure of operating performance as it demonstrates Freehold's ability to generate necessary funds to fund capital expenditures, sustain dividends and repay debt. We believe that such a measure provides a useful assessment of Freehold's operations on a continuing basis by eliminating certain non-cash charges. Funds from operations per share is calculated based on the weighted average number of shares outstanding consistent with the calculation of net income per share.

<i>(\$000s, except as noted)</i>	2016	2015	Change
Net loss	(11,163)	(4,080)	174%
Per share, basic and diluted (\$)	(0.10)	(0.05)	100%
Funds from operations	94,211	103,820	-9%
Per share (\$)	0.85	1.15	-26%

Financing Activities

We retain working capital primarily to fund capital expenditures or acquisitions and reduce bank indebtedness. In the oil and gas industry, accounts receivable from industry partners are typically settled in the following month. However, due to administrative issues, payments to royalty owners are often delayed longer. Also, working capital can fluctuate significantly due to volume and price changes at each period end and unpaid capital expenditures. Working capital at December 31, 2016 was \$10.8 million, up \$5.8 million from year-end 2015, due to a combination of higher accounts receivable caused by higher oil prices and lower dividends payable resulting from the lower dividend rate.

COMPONENTS OF WORKING CAPITAL

<i>(\$000s)</i>	<i>As at December 31</i>		
	2016	2015	Change
Cash	892	876	2%
Accounts receivable	24,064	21,046	14%
Current taxes receivable	-	73	-100%
Current assets	24,956	21,995	13%
Dividends payable	(4,716)	(6,924)	-32%
Accounts payable and accrued liabilities	(9,219)	(9,826)	-6%
Current portion of share based compensation	(182)	(194)	-6%
Current liabilities	(14,117)	(16,944)	-17%
Working capital	10,839	5,051	115%

At December 31, 2016, Freehold had a \$245 million extendible revolving term credit facility with a syndicate of four Canadian chartered banks, on which \$84 million was drawn. In addition, Freehold had available a \$15 million extendible revolving operating facility.

At December 31, 2016 the facilities are secured with \$400 million demand debentures over Freehold's petroleum and natural gas assets but do not contain any financial covenants. The lenders at any time can request a redetermination of the borrowing base, which may require a repayment to the lenders within 90 days of receiving notice, of an amount that the indebtedness is in excess of the redetermined borrowing base. The facilities are extendible annually with the latest review completed in May 2016. Freehold's borrowing base is dependent on the lenders annual review and interpretation of Freehold's reserves and future commodity prices, with the next renewal to occur by May 2017. In the event that the lenders do not consent to an extension, the revolving credit facility would revert to a two-year, non-revolving term facility with equal quarterly principal repayments. The first quarterly payment would commence on January 1 of the year following the end of the revolving period. Borrowings under the facilities bear interest at the bank's prime lending rate, bankers' acceptance or LIBOR rates plus applicable margins and standby fees.

In 2016 net debt was reduced as a result of our equity financing, which was in excess of our acquisition, and excess free cash flow over above our dividends.

DEBT ANALYSIS

(\$000s)	2016	2015	Change
Long-term debt	84,000	152,000	-45%
Short-term debt (operating line)	-	-	-
Total debt	84,000	152,000	-45%
Working capital	(10,839)	(5,051)	115%
Net debt	73,161	146,949	-50%

We are bound by non-financial covenants on our credit facilities and we monitor these monthly to ensure compliance. Under our credit facility, we are restricted from declaring dividends if we are or would be in default under the credit facility or if our borrowings thereunder exceed our borrowing base, which was \$260 million at December 31, 2016. As at December 31, 2016, we were in compliance with all such covenants.

Net debt to funds from operations was 0.8 times and net debt was 8% of total capitalization at the end of 2016.

FINANCIAL LEVERAGE AND COVERAGE RATIOS

	2016	2015	Change
Net debt to funds from operations (times)	0.8	1.4	-43%
Net debt to dividends (times)	1.2	1.6	-25%
Dividends to interest expense (times)	13	16	-19%
Net debt to net debt plus equity (%)	8	17	-53%

Non-Derivative Financial Liabilities

Freehold's non-derivative financial liabilities include its dividends payable, accounts payable and accrued liabilities, share based compensation payable and long-term debt. Freehold has no derivative financial liabilities. The following table outlines cash flows associated with contractual maturities of Freehold's non-derivative financial liabilities as at December 31, 2016.

(\$000s)	Less than 1 Year	2-3 Years	Total
Dividends payable	4,716	-	4,716
Accounts payable and accrued liabilities	9,219	-	9,219
Share based compensation payable	182	932	1,114
Long-term debt	-	84,000	84,000
Total	14,117	84,932	99,049

Shareholders' Capital

As at December 31, 2016, there were 117,918,274 shares outstanding and as at March 2, 2017, there were 117,962,667 shares outstanding.

On May 25, 2016 Freehold closed a bought deal equity offering, issuing 16,428,900 common shares and a private equity offering with CN Pension Trust Funds (see Related Party Transactions) issuing 1,732,000 common shares, both at a price of \$11.55 per share for gross proceeds of \$209.8 million. The issue costs including the underwriter fees were \$8.0 million (\$5.8 million net of a tax effect). The funds were used for the Husky Transaction which closed on the same date and to repay a portion of bank indebtedness.

On May 6, 2015, Freehold closed a bought deal equity offering, issuing 20,700,000 common shares and a private equity offering to CN Pension Trust Funds issuing 1,833,334 common shares, both at a price of \$18.00 per share for gross proceeds of \$405.6 million. The issue costs including the underwriter fees were \$15.4 million (\$11.2 million net of a tax effect). The funds were used for the royalty acquisition which closed on the same date and to repay a portion of bank indebtedness.

During 2016, Freehold issued 287,648 shares (2015 – 269,978 shares) for payment of the management fee (see Related Party Transactions).

In 2016, participation in Freehold's DRIP was 8% (2015 – 18%). We issued 0.5 million (2015 – 1.2 million) shares related to the DRIP. The ascribed value of \$5.0 million (2015 – \$17.2 million) was based on the weighted average closing price for the 10 trading days preceding each payment date. Effective with the August 31, 2016 dividend the Board approved the suspension of the DRIP pending further notice.

As at December 31, 2016, there were 148,499 deferred share units (DSUs) outstanding (2015 – 177,012). During 2016 there were 59,198 shares issued for redemption of DSUs (2015 – nil DSUs redeemed and nil shares issued). On January 1, 2017, the Board granted a total of 27,521 DSUs to eligible directors as part of their annual compensation. Each eligible director received 4,234 DSUs and the Chair of the Board received 6,351 DSUs. In January 2017 a retired director redeemed 63,418 DSUs, resulting in the issuance of 44,393 shares from treasury. As at March 2, 2017, there were 113,373 DSUs outstanding. (See Share Based Compensation).

For the year ended December 31, 2016 and 2015, DSUs were excluded from the calculation of diluted net loss per share as their effect was anti-dilutive.

SHARES OUTSTANDING

	2016	2015	Change
Weighted average			
Basic	110,391,160	90,504,786	22%
Diluted	110,391,160	90,504,786	22%
At December 31	117,918,274	98,940,152	19%

Dividend Policy

The Board reviews and determines the monthly dividend rate on a quarterly basis, or as conditions necessitate, after considering expected commodity prices, foreign exchange rates, economic conditions, production volumes, DRIP participation levels, tax payable, and our capacity to finance operating and investing obligations. The dividend rate is established with the intent of absorbing short-term market volatility over several months. It also recognizes our intention to fund capital expenditures primarily through funds from operations and to maintain a strong balance sheet to take advantage of acquisition opportunities and withstand potential commodity price declines.

The payment of dividends by a corporation is governed by the liquidity and insolvency tests described in the *Business Corporations Act* (Alberta) (ABCA). Pursuant to the ABCA, after the payment of a dividend, we must be able to pay our liabilities as they become due and the realizable value of our assets must be greater than our liabilities and the legal stated capital of our outstanding securities. As at December 31, 2016, our legal stated capital was \$1.0 billion (2015 – \$1.0 billion).

2016 DIVIDENDS DECLARED

Record Date	Payment Date	Dividend Amount (\$ per share)
January 31, 2016	February 15, 2016	0.07
February 29, 2016	March 15, 2016	0.07
March 31, 2016	April 15, 2016	0.04
April 30, 2016	May 16, 2016	0.04
May 31, 2016	June 15, 2016	0.04
June 30, 2016	July 15, 2016	0.04
July 31, 2016	August 15, 2016	0.04
August 31, 2016	September 15, 2016	0.04
September 30, 2016	October 17, 2016	0.04
October 31, 2016	November 15, 2016	0.04
November 30, 2016	December 15, 2016	0.04
December 31, 2016	January 16, 2017	0.04
Total		0.54

Dividends declared in 2016 totaled \$59.5 million (\$0.54 per share). From inception of Freehold Royalty Trust in 1996 to December 31, 2016, Freehold distributed \$1.5 billion (\$30.47 per share) to our shareholders.

ACCUMULATED DIVIDENDS ⁽¹⁾

	2016	2015	Change
Dividends declared (\$000s)	59,502	90,139	-34%
Accumulated, beginning of year	1,425,971	1,335,832	7%
Accumulated, end of year	1,485,473	1,425,971	4%
Dividends per share (\$) ⁽²⁾	0.54	1.00	-46%
Accumulated, beginning of year	29.93	28.93	3%
Accumulated, end of year	30.47	29.93	2%

(1) Accumulated dividends reflect distributions paid on trust units of Freehold Royalty Trust (the predecessor of Freehold) from 1996 through 2010 and dividends paid on common shares of Freehold from 2011 onwards.

(2) Based on the number of shares issued and outstanding at each record date.

The amended and restated DRIP allows for the issuance of shares from treasury at a 5% discount to market (i.e. 95% of the weighted average closing price for the 10 trading days preceding each payment date). Effective with the August 31, 2016 dividend the Board approved the suspension of the DRIP pending further notice.

The tables below and on the following page show reconciliations of funds from operations and dividends. In 2016 Freehold's basic payout ratio was 63% and its adjusted payout ratio was 66%, exhibiting that dividend payments are being made within our means, with excess free cash flow being used to repay debt (see Non-GAAP Financial Measures).

DIVIDENDS ANALYSIS

(\$000s)	2016	2015	Change
Dividends paid in cash	56,582	76,478	-26%
Dividends paid in shares (DRIP)	4,997	17,225	-71%
Total dividends paid ⁽¹⁾	61,579	93,703	-34%
Dividends declared	59,502	90,139	-34%
Funds from operations	94,211	103,820	-9%
Capital expenditures	5,218	22,295	-77%
Basic payout ratio ⁽²⁾	63%	87%	-28%
Adjusted payout ratio ⁽³⁾	66%	95%	-31%

(1) Based on the dividend payment date which is generally on the 15th day of the month following the month it was declared.

(2) Dividends declared as a percentage of funds from operations (see Non-GAAP Financial Measures).

(3) Dividends paid in cash plus capital expenditures as a percentage of funds from operations (see Non-GAAP Financial Measures).

RECONCILIATION OF DIVIDENDS DECLARED

(\$000s)	2016	2015	Change
Funds from operations	94,211	103,820	-9%
Proceeds from the DRIP	4,997	17,225	-71%
Issuance of shares, net of issue costs	201,747	390,236	-48%
Debt additions (repayment)	(68,000)	13,000	-623%
Acquisition advance	-	949	-100%
Acquisitions	(162,590)	(411,352)	-60%
Capital expenditures	(5,218)	(22,295)	-77%
Working capital change	(5,645)	(1,444)	291%
Dividends declared	59,502	90,139	-34%

Investing Activities**Acquisitions**

We pursue opportunities to augment our production and reserves, primarily targeting royalty interests. Freehold's acquisition strategy targets individual properties or groups of properties with a focus on royalty interests. The key criteria are:

- quality assets;
- attractive returns;
- acceptable risk profile; and
- long economic life.

Freehold expended \$163 million on acquisitions in 2016, of which \$162 million, including adjustments, resulted from the Husky Transaction where an extensive suite of royalty production and fee lands were acquired. The effective date of the Husky Transaction was January 1, 2016 with the closing occurring on May 25, 2016.

Capital Expenditures

In 2016, development expenditures of \$5.2 million amounted to 6% of funds from operations, a 77% reduction from 2015 levels, as there were reduced capital commitments on our largely non-operated properties.

In the upstream oil and gas sector, because of the nature of reserve reporting, natural reservoir depletion, and the risks involved in capital investment, it is not possible to distinguish between capital spent on maintaining productive capacity and capital spent on growth opportunities. Therefore, maintenance capital is not disclosed separately from development capital spending.

(\$000s, except as noted)	2016	2015	Change
Development drilling and other	2,990	12,179	-75%
Plant and facilities	2,228	10,116	-78%
Total capital expenditures	5,218	22,295	-77%

Decommissioning Liability

We have no decommissioning liability on our royalty interest properties. Our decommissioning liability results from our responsibility to abandon and reclaim our net share of all working interest properties. The undiscounted value of our total decommissioning liability is estimated to be \$36.3 million (2015 - \$40.6 million). Payments to settle the obligations are expected to

occur continuously over the next 57 years, with the majority being settled within 7 to 17 years. At December 31, 2016, a risk-free rate of 2.3% (2015 - 2.2%) and an inflation rate of 2.0% (2015 - 1.5%) were used to calculate the fair value. The value of the decommissioning liability at December 31, 2016 was \$23.7 million (2015 - \$27.6 million).

Business Risks and Mitigating Strategies

Our operations are subject to the same industry risks and conditions faced by all oil and gas companies. The most significant of these include the following:

- fluctuations in commodity prices and quality differentials as a result of weather patterns, world and North American market forces or shifts in the balance between supply and demand for crude oil and gas;
- access to pipelines or other transportation methods for bringing oil and natural gas to market;
- variations in currency exchange rates;
- imprecision of reserve estimates and uncertainty of depletion and recoverability of reserves. Our reserves will deplete over time through continued production and we and our industry partners and royalty payors may not be able to replace these reserves on an economic basis;
- reliance on royalty payors to drill and produce on our lands and their ability to pay their obligations;
- industry activity levels and intense competition for land, goods and services, and qualified personnel;
- stock market volatility and the ability to access sufficient capital from internal and external sources;
- risk associated with volatility in global financial markets;
- risk associated with the renegotiation of our credit facility;
- operational or marketing risks resulting in delivery interruptions, delays or unanticipated production declines;
- changes in government regulations, taxation, and royalties; and
- safety and environmental risks.

For a more detailed description of risk factors, please see our Annual Information Form, filed on SEDAR.

We employ the following strategies to mitigate these risks:

- Our diversified revenue stream limits the size of any one property with respect to our total assets.
- We are not liable for abandonment and reclamation costs on our royalty lands.
- Due to our high percentage of royalty lands, we have one of the lowest all-in cost structures of our peer group. In addition, we maintain a focus on controlling direct costs to maximize profitability.
- We negotiate agreements that provide mechanisms to ensure that our interests are protected.
- Systems and processes are in place to identify any unpaid or incorrect revenues.
- We maintain a dedicated compliance function, with a comprehensive auditing program, to ensure that the terms of the various agreements are followed. During 2016, our audit staff issued audit exception queries amounting to \$6.1 million, bringing the total amount of audit exception queries since 1997 to \$76.4 million, of which we have successfully recovered \$61.5 million.

- We adhere to strict investment criteria for acquisitions, seeking quality royalty properties that have attractive returns, acceptable risk profiles and long economic lives.
- We market our products to a diverse range of buyers or with our diverse range of royalty payors. Currently, we do not have any commodity price, exchange rate, or interest rate hedging programs in place.
- We employ a qualified Manager that has many years of experience and knowledge in managing our assets.
- We maintain levels of liability insurance that meet or exceed industry standards.
- We employ a conservative approach to debt management. As circumstances warrant, we allocate a portion of funds from operations to debt repayment.

Environmental Regulation and Risk

The oil and gas industry is currently subject to environmental regulations pursuant to provincial and federal legislation. Such legislation provides for restrictions and prohibitions on the release or emission of various substances produced in association with certain oil and gas industry operations. In addition, such legislation requires that well and facility sites be abandoned and reclaimed to the satisfaction of provincial authorities. Compliance with such legislation can require significant expenditures and a breach of such requirements may result in suspension or revocation of necessary licenses and authorizations, civil liability for pollution damage, and the imposition of material fines and penalties. It is reasonably likely that the trend towards stricter standards in environmental legislation and regulation will continue. Given the evolving nature of the debate related to climate change and the control of greenhouse gases and resulting requirements, it is not possible to predict the impact of those requirements on our operations and financial condition. For information about climate change and other environmental regulations, see “Industry Conditions” in our Annual Information Form.

Controls and Accounting Matters

In compliance with National Instrument 52-109 *Certification of Disclosure in Issuers' Annual and Interim Filings* (NI 52-109), Freehold has filed certificates signed by our Chief Executive Officer (CEO) and Chief Financial Officer (CFO) that, among other things, deal with the matter of disclosure controls and procedures and internal control over financial reporting. While we believe that our disclosure controls and procedures and internal control over financial reporting provide a reasonable level of assurance, we do not expect that the controls will prevent all errors and fraud. A control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objective of the control system is met.

Disclosure Controls

As of December 31, 2016, an internal evaluation was carried out of the effectiveness of Freehold's disclosure controls and procedures. This evaluation was performed under the supervision of, and with the participation of the CEO and the CFO. It took into consideration Freehold's Disclosure, Insider Trading, Code of Business Conduct and Conflict of Interest, and Whistleblower policies, as well as the functioning of the Manager, the officers, the Board and Board Committees. In addition, the evaluation covered the processes, systems and capabilities relating to regulatory filings, public disclosures, and the identification and communication of material information. Based on this evaluation, management has concluded that Freehold's disclosure controls and procedures were effective as at December 31, 2016, in ensuring that material information is made known to management in a timely manner, particularly during the period in which the annual filings were being prepared, and information required to be disclosed by Freehold in its annual filings, interim filings or other reports filed or submitted by Freehold

under securities legislation is recorded, processed, summarized and reported within the time periods specified in securities legislation.

Internal Control Over Financial Reporting

Our CEO and CFO are responsible for establishing and maintaining internal control over financial reporting (ICFR). They have caused ICFR to be designed under their supervision to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with Canadian GAAP. The control framework used to design ICFR is the Internal Control – Integrated Framework (2013 COSO Framework) published by The Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Under the supervision of the CEO and CFO, Freehold conducted an evaluation of the effectiveness of its ICFR as at December 31, 2016, as structured within the 2013 COSO Framework. Based on this evaluation, the CEO and CFO concluded that, as of December 31, 2016, our ICFR provides reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP. There were no changes in our ICFR during 2016 that materially affected Freehold's ICFR.

New Accounting Standards

Recent Pronouncements

In May 2014, the IASB issued IFRS 15 Revenue from Contracts with Customers, which replaces IAS 11 Construction Contracts, IAS 18 Revenue, and other revenue related interpretations. The standard establishes a single revenue recognition framework that applies to contracts with customers. The effective date for adopting IFRS 15 in its entirety is January 1, 2018. Freehold is in the process of reviewing its royalty and other revenue streams along with underlying contracts to determine the impact on the consolidated financial statements and additional disclosures requirements.

In July 2014, the IASB completed a three-phase project to replace IAS 39 Financial Instruments: Recognition and Measurement with IFRS 9 Financial Instruments. The first two completed phases replaced the current multiple classification and measurement models for financial assets and liabilities with a single model that has only two classification categories: amortized cost and fair value. The third phase describes a new hedge accounting model. Presently and historically, Freehold has not entered into any transactions in which hedge accounting could be applied and don't anticipate changing the practice. The effective date for adopting IFRS 9 in its entirety is January 1, 2018.

In January, 2016, the IASB issued IFRS 16 Leases, which replaces IAS 17 Leases. The standard establishes a single lessee accounting model and requires a lessee to recognize assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee is required to recognize a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. Other areas of the lease accounting model have been impacted, including the definition of a lease. Transitional provisions have been provided. The effective date for adopting IFRS 16 in its entirety is January 1, 2019.

Freehold's assessment of these recent pronouncements is ongoing and the impact, if any, on the consolidated financial statements and additional disclosure requirements are yet to be determined.

Critical Accounting Estimates

Our financial statements are prepared within a framework of Canadian GAAP (being IFRS) selected by management and approved by our Board. The assets, liabilities, revenues, and expenses reported in our financial statements depend to varying degrees on estimates made by management. These estimates are based on historical experience and reflect certain assumptions about the future that are believed to be both reasonable and conservative. The more significant reporting areas are crude oil and gas reserve estimation, depletion, impairment of assets, oil and gas revenue accruals, oil and gas royalty interests, decommissioning obligations, income taxes, and share based compensation. Management's judgments and estimates in these areas are based on information available from both internal and external sources, including engineers, geologists, and historical experience in similar matters. Actual results could differ from the estimates, as additional information becomes known.

An estimate is considered a critical accounting estimate if it requires management to make assumptions about matters that are highly uncertain, and if different estimates that could have been used would have a material impact. We continually evaluate the estimates and assumptions. In the normal course, changes are made to assumptions underlying all critical accounting estimates to reflect current economic conditions, and updating of historical information is used to develop the assumptions. Except as discussed in this MD&A, we are not aware of trends, commitments, events, or uncertainties that are expected to materially affect the methodology or assumptions associated with the critical accounting estimates.

Reserve Estimates, Depletion and Impairment Testing

The current estimates of oil and gas reserves and our future capital expenditures are based on an independent evaluation conducted as of December 31, 2016. Reserve estimates are updated once a year (as at December 31) and when a significant acquisition or development is completed. At each interim reporting date, reserves are also adjusted for production. The reserve and recovery information provided are only estimates. The actual production and ultimate reserves may be greater than or less than the estimates and the differences may be material.

Petroleum and natural gas interests, including the cost of production equipment, future capital costs, estimated decommissioning costs and directly attributable general and administrative costs are depleted on the unit-of-production method based on estimated proved plus probable oil and gas reserves. Reserves are converted to equivalent units on the basis of relative energy content. An increase in estimated proved plus probable oil and gas reserves would result in a corresponding reduction in the depletion rate.

At each reporting date, Freehold assesses groups of assets for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable. If any such indication of impairment exists, Freehold makes an estimate of its recoverable amount. Where the carrying amount of a group of assets exceeds its recoverable amount, the assets are considered impaired and written down. Impairments can be reversed if the impairment indicators have been reversed. Indicators and recoverable amounts are primarily estimates from independent sources. The determination of CGUs is subject to management judgment.

Oil and Gas Revenue Accruals and Royalty Interests

Freehold follows the accrual method of accounting, making estimates in its financial and operating results. This may include estimates of revenues, royalties, production and other expenses and capital items related to the period being reported, for which actual results have not yet been received. We expect that these accrual estimates will be revised, upwards or downwards, based on the receipt of actual results. We have no operational control over our

royalty lands, and we primarily hold small interests in several thousand wells. Thus, obtaining timely production data from the well operators is extremely difficult. As a result, we use government reporting databases and past production receipts to estimate revenue accruals.

Significant judgment is required to determine the interests of royalty properties in areas where mineral rights are shared with Canpar (see Related Party Transactions). We use publicly available information on geological formations to apportion revenues between the entities in accordance with the respective party's interests. As new geological information becomes available and as part of our ongoing internal audit activities, we periodically revise these allocations and consideration is transferred to reflect the changes.

Decommissioning Liability

Freehold measures decommissioning liability as the present value of management's best estimate of the expenditure required to settle the obligation at the reporting date using a risk-free discount rate. This estimate is recognized when a legal or constructive obligation arises and is recorded as a long-term liability, with a corresponding increase in the carrying value of the petroleum and natural gas working interest asset. The capitalized amount is depleted on a unit-of-production method over the life of the reserves. At each reporting date, the passage of time and changes to estimates results in liability changes and the amount of accretion is charged against current period income.

In determining our decommissioning liability, we are required to make a significant number of estimates with respect to activities that will occur in many years to come. In arriving at the recorded amount of the decommissioning liability, numerous assumptions are made with respect to ultimate settlement amounts, inflation factors, risk-free discount rates, timing of settlement and expected changes in legal, regulatory, environmental and political environments. The decommissioning liability also results in an increase to the carrying cost of capital assets. The obligation accretes to a higher amount with the passage of time as it is determined using discounted present values. A change in any one of the assumptions could affect the estimated future obligation and in return, net income. It is difficult to determine the impact of a change in any one of our assumptions. As a result, a reasonable sensitivity analysis cannot be performed.

Income Taxes

We follow the asset and liability method of accounting for income taxes. Under this method, income tax liabilities and assets are recognized for the estimated tax consequences attributable to differences between the amounts reported in the financial statements and their respective tax bases, using enacted or substantially enacted income tax rates. The effect of a change in income tax rates on deferred income tax liabilities and assets is recognized in income in the period that the change occurs. The actual amount of income tax may be greater than or less than the estimates and the differences may be material.

Share Based Compensation

Freehold funds its proportionate share of the costs associated with a long-term incentive compensation plan (LTIP) for employees of Rife Resources Ltd. (Rife) through the Manager of Freehold, Rife Resources Management Ltd. The LTIP uses a combination of the value of phantom Rife shares and Freehold shares as the basis for rights, which are granted annually at the discretion of the directors of Rife and vest at the end of a three-year period. Dividends to shareholders paid by Freehold during the vesting period are assumed to be reinvested in notional rights on the dividend payment date. Since participants in the LTIP receive a cash payment on a fixed vesting date, a liability is determined and recognized as services are rendered based on the fair value of the rights at each period end. The valuation incorporates

the consideration of share price, the number of rights outstanding at each period end, an estimated performance multiplier, and an estimated forfeiture rate. Compensation expense is recognized over the vesting period. If factors change actual payments resulting from the LTIP can vary significantly from amounts expensed in prior periods.

Forward-Looking Statements

Certain statements contained in this MD&A constitute forward-looking statements. These statements relate to future events or our expectations of future performance. All statements other than statements of historical fact may be forward-looking statements. Forward-looking statements are often, but not always, identified by the use of words such as “seek”, “anticipate”, “plan”, “continue”, “estimate”, “expect”, “may”, “will”, “forecast”, “project”, “predict”, “potential”, “targeting”, “intend”, “could”, “might”, “should”, “believe” and similar expressions (including the negatives thereof). These statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking statements. We believe the expectations reflected in those forward-looking statements are reasonable but no assurance can be given that these expectations will prove to be correct and, as such, forward-looking statements included in this MD&A should not be unduly relied upon. These forward-looking statements are provided to allow readers to better understand our business and prospects.

In particular, this MD&A contains forward-looking statements pertaining to the following:

- our outlook for commodity prices including supply and demand factors relating to crude oil, heavy oil, and natural gas;
- light/heavy oil price differentials;
- changing economic conditions;
- our strategies and the expectation that those strategies will sustain production and reserves life;
- our acquisition criteria and the intent that such criteria will result in acquisitions being accretive to shareholders;
- foreign exchange rates;
- industry drilling and development activity on our royalty lands;
- the expected low decline and value added from the Husky Transaction or any of the more recent transactions;
- development of our working interest properties;
- estimated capital budget and expenditures and the timing thereof;
- expectation to continue to position ourselves as a low risk entity, able to maintain sustainability through all commodity price cycles;
- current estimated production and development expected from the February 2017 acquisition;
- Freehold’s decommissioning liability and timing of payment thereof;
- forecast 2017 production, including product mix and percentage from royalties;
- forecast 2017 percentage of operating income from royalties;
- forecast 2017 basic payout ratio and adjusted payout ratio;
- forecast 2017 year end net debt to funds from operations;
- average production and contribution from royalty lands;
- key operating assumptions;

- amounts and rates of income taxes and timing of payment thereof;
- expected production additions from our strong audit function;
- our tax pools and the expected tax horizon;
- our dividend policy and expectations for future dividends;
- treatment under governmental regulatory regimes and tax laws; and
- our assessment of litigation risk.

Our actual results could differ materially from those anticipated in these forward-looking statements because of many factors, the most significant of which are as follows:

- volatility in market prices for crude oil and natural gas;
- lack of pipeline capacity;
- currency fluctuations;
- changes in income tax laws or changes in tax laws, regulations, royalties, or incentive programs relating to the oil and gas industry;
- reliance on royalty payors to drill and produce on our lands and their ability to pay their obligations;
- uncertainties or imprecision associated with estimating oil and gas reserves;
- stock market volatility and our ability to access sufficient capital from internal and external sources;
- a significant or prolonged downturn in general economic conditions or industry activity;
- incorrect assessments of the value of acquisitions;
- competition for, among other things, capital, acquisitions of reserves, undeveloped lands and skilled personnel;
- geological, technical, drilling, and processing problems;
- environmental risks and liabilities inherent in oil and gas operations; and
- other factors discussed under Business Risks and Mitigating Strategies in this MD&A, and under Risk Factors and elsewhere in our Annual Information Form.

Readers are cautioned that the foregoing list of factors is not exhaustive.

With respect to forward-looking statements contained in this MD&A, we have made assumptions regarding, among other things, the following:

- future crude oil and natural gas prices;
- future capital expenditure levels;
- future production levels;
- future exchange rates;
- future tax rates;
- future participation rates in the DRIP and use of cash preserved through the DRIP;
- future legislation,
- the cost of developing and expanding our assets;

- our ability and the ability of our industry partners and royalty payors to obtain equipment in a timely manner to carry out development activities;
- our ability to market our product successfully to current and new customers;
- our expectation for the consumption of crude oil and natural gas;
- our expectation for industry drilling levels on our royalty lands;
- the impact of increasing competition;
- our ability to obtain financing on acceptable terms; and
- our ability to add production and reserves through our development and acquisition activities.

Key operating assumptions with respect to the forward-looking statements contained in this MD&A are provided in the Outlook section.

You are further cautioned that the preparation of financial statements in accordance with IFRS requires management to make certain judgments and estimates that affect the reported amounts of assets, liabilities, revenues, and expenses. These estimates may change, having either a positive or negative effect on net income, as further information becomes available and as the economic environment changes.

The forward-looking statements contained in this MD&A are expressly qualified by this cautionary statement and speak only as of the date of this MD&A. Our policy for updating forward-looking statements is to update our key operating assumptions quarterly and, except as required by law, we do not undertake to update any other forward-looking statements.

Non-GAAP Financial Measures

Within this MD&A, references are made to terms commonly used as key performance indicators in the oil and gas industry. We believe that operating income, operating netback, basic payout ratio, adjusted payout ratio, free cash flow and cash costs are useful supplemental measures for management and investors to analyze operating performance, financial leverage, and liquidity, and we use these terms to facilitate the understanding and comparability of our results of operations and financial position. However, these terms do not have any standardized meanings prescribed by GAAP and therefore may not be comparable with the calculations of similar measures for other entities.

Operating income, which is calculated as royalty and other revenue less royalties and operating expenses, represents the cash margin for product sold. Operating netback, which is calculated as average unit sales price less royalties and operating expenses, represents the cash margin for product sold, calculated on a per boe basis (see Netback Analysis).

Payout ratios are often used for dividend paying companies in the oil and gas industry to identify its dividend levels in relation to the funds it receives and uses in its capital and operational activities. Basic payout ratio is calculated as dividends declared as a percentage of funds from operations. Adjusted payout ratio is calculated as dividends paid in cash plus capital expenditures as a percentage of funds from operations.

Free cash flow is calculated by subtracting capital expenditures from funds from operations. Free cash flow is a measure often used by dividend paying companies to determine cash available for payment of dividends, paying down debt or investment.

Cash costs is a total of all recurring costs in the statement of income (loss) deducted in determining funds from operations. For Freehold cash costs are identified as royalty expense, operating expense, general and administrative expense, interest expense and share based compensation expense (if paid out in the period). It is key to funds from operations, representing the ability fund capital expenditures, sustain dividends and repay debt.

We refer to various per boe figures which provide meaningful information on our operational performance. We derive per boe figures by dividing the relevant revenue or cost figure by the total volume of oil, NGL and natural gas production during the period, with natural gas converted to equivalent barrels of oil as described above.

Conversion of Natural Gas to Barrels of Oil Equivalent (boe)

To provide a single unit of production for analytical purposes, natural gas production and reserves volumes are converted mathematically to equivalent barrels of oil (boe). We use the industry-accepted standard conversion of six thousand cubic feet of natural gas to one barrel of oil (6 Mcf = 1 barrel). The 6:1 boe ratio is based on an energy equivalency conversion method primarily applicable at the burner tip. It does not represent a value equivalency at the wellhead and is not based on either energy content or current prices. While the boe ratio is useful for comparative measures, it does not accurately reflect individual product values and might be misleading, particularly if used in isolation. As well, given that the value ratio, based on the current price of crude oil to natural gas, is significantly different from the 6:1 energy equivalency ratio, using a 6:1 conversion ratio may be misleading as an indication of value.

MANAGEMENT'S REPORT

The accompanying consolidated financial statements and other financial information in this Financial Report have been prepared by management, who is responsible for their integrity, consistency, objectivity and reliability. To fulfill this responsibility, Freehold maintains policies, procedures and systems of internal control to ensure that reporting practices and accounting and administrative procedures are appropriate to provide reasonable assurance that the assets are safeguarded, transactions are properly authorized and relevant and reliable financial information is produced.


These consolidated financial statements have been prepared in conformity with International Financial Reporting Standards and, where appropriate, reflect estimates based on management's judgment. The financial information presented throughout this Financial Report is generally consistent with the information contained in the accompanying consolidated financial statements.

Independent auditors, KPMG LLP, were appointed by the shareholders to perform an examination of the corporate and accounting records so as to express an opinion on the consolidated financial statements. Their examination included tests and procedures considered necessary to provide reasonable assurance that the consolidated financial statements are presented fairly in accordance with International Financial Reporting Standards.

The consolidated financial statements have been further reviewed and approved by the Board of Directors acting through its Audit Committee, which is comprised of independent directors. The Audit Committee, which meets with the auditors and management to review the activities of each and reports to the Board of Directors, oversees management's responsibilities for the financial reporting and internal control systems. The auditors have full and direct access to the Audit Committee and meet periodically with the committee both with and without management present to discuss their audit and related findings.



THOMAS J. MULLANE
President and
Chief Executive Officer



DARREN G. GUNDERSON
Vice-President, Finance and
Chief Financial Officer

March 2, 2015

INDEPENDENT AUDITORS' REPORT

To the Shareholders of Freehold Royalties Ltd.

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

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

Opinion

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

The logo for KPMG LLP, featuring the letters 'KPMG' in a large, bold, sans-serif font, with 'LLP' in a smaller, similar font to the right.

CHARTERED PROFESSIONAL ACCOUNTANTS

March 2, 2017
Calgary, Canada

CONSOLIDATED BALANCE SHEETS

(\$000s)	December 31, 2016	December 31, 2015
Assets		
Current assets:		
Cash	\$ 892	\$ 876
Accounts receivable	24,064	21,046
Current taxes receivable	-	73
	24,956	21,995
Exploration and evaluation assets (note 4)	64,019	49,479
Petroleum and natural gas interests (note 5)	892,120	846,825
Deferred income tax asset (note 3, 11)	26,355	21,095
	\$ 1,007,450	\$ 939,394
Liabilities and Shareholders' Equity		
Current liabilities:		
Dividends payable	\$ 4,716	\$ 6,924
Accounts payable and accrued liabilities	9,219	9,826
Current portion of share based compensation payable (note 10)	182	194
	14,117	16,944
Decommissioning liability (note 7)	23,705	27,635
Share based compensation payable (note 10)	932	191
Long-term debt (note 6)	84,000	152,000
Shareholders' equity:		
Shareholders' capital (note 8)	1,263,796	1,050,494
Contributed surplus	2,717	3,282
Deficit	(381,817)	(311,152)
	884,696	742,624
	\$ 1,007,450	\$ 939,394

See accompanying notes to consolidated financial statements.

On behalf of the Board of Directors of Freehold Royalties Ltd.:



MARVIN F. ROMANOW
Director



ARTHUR N. KORPACH
Director

CONSOLIDATED STATEMENTS OF LOSS AND COMPREHENSIVE LOSS

<i>(\$000s, except per share and weighted average data)</i>	<i>Year Ended December 31</i>	
	2016	2015
Revenue:		
Royalty and other revenue (note 14)	\$ 129,968	\$ 135,664
Royalty expense	(1,317)	(2,297)
	128,651	133,367
Gain on corporate acquisition (note 3)	-	24,340
Other income (loss) (note 9, 15)	(1,066)	756
Expenses:		
Operating	17,630	18,215
General and administrative	10,184	10,643
Share based compensation (note 10)	1,208	766
Interest and financing	4,578	5,696
Depletion and depreciation (note 5)	104,159	95,703
Impairment (note 5)	-	38,800
Accretion of decommissioning liability (note 7)	543	566
Management fee (note 9)	3,543	3,693
	141,845	174,082
Loss before taxes	(14,260)	(15,619)
Income taxes (note 11):		
Current recovery	-	(5,097)
Deferred recovery	(3,097)	(6,442)
	(3,097)	(11,539)
Net loss and comprehensive loss	\$ (11,163)	\$ (4,080)
Net loss per share, basic and diluted	\$ (0.10)	\$ (0.05)
Weighted average number of shares:		
Basic	110,391,160	90,504,786
Diluted	110,391,160	90,504,786

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(\$000s)	<i>Year Ended December 31</i>	
	2016	2015
Operating:		
Net loss	\$ (11,163)	\$ (4,080)
Items not involving cash:		
Depletion and depreciation	104,159	95,703
Impairment	-	38,800
Share based compensation	1,208	766
Deferred income tax recovery	(3,097)	(6,442)
Accretion of decommissioning liability	543	566
Management fee	3,543	3,693
Gain on corporate acquisition	-	(24,340)
Expenditures on share based compensation	(490)	(619)
Decommissioning expenditures	(492)	(227)
Funds from operations	94,211	103,820
Changes in non-cash working capital (note 14)	(1,078)	6,693
	93,133	110,513
Financing:		
Issuance of shares, net of issue costs	201,747	390,236
Long-term debt	(68,000)	13,000
Dividends paid	(56,582)	(76,478)
	77,165	326,758
Investing:		
Acquisition advance	-	949
Acquisitions	(162,590)	(411,352)
Capital expenditures	(5,218)	(22,295)
Changes in non-cash working capital (note 14)	(2,474)	(4,823)
	(170,282)	(437,521)
Increase (decrease) in cash	16	(250)
Cash, beginning of year	876	1,126
Cash, end of year	\$ 892	\$ 876

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

(\$000s)	<i>Year Ended December 31</i>	
	2016	2015
Shareholders' capital:		
Balance, beginning of year	\$ 1,050,494	\$ 635,223
Shares issued for dividend reinvestment plan	4,997	17,225
Shares issued for payment of management fee	3,543	3,693
Shares issued for deferred share unit plan redemption	1,066	-
Shares cancelled	(214)	-
Shares issued for equity offering	209,759	405,600
Issue costs, net of tax effect	(5,849)	(11,247)
Balance, end of year	1,263,796	1,050,494
Contributed surplus:		
Balance, beginning of year	3,282	2,577
Share based compensation expense	614	705
Shares cancelled and return of accumulated dividends	345	-
Deferred share unit plan redemption	(1,524)	-
Balance, end of year	2,717	3,282
Deficit:		
Balance, beginning of year	(311,152)	(216,933)
Net loss and comprehensive loss	(11,163)	(4,080)
Dividends declared	(59,502)	(90,139)
Balance, end of year	(381,817)	(311,152)
	\$ 884,696	\$ 742,624

See accompanying notes to consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Years ended December 31, 2016 and 2015

1. Basis of Presentation

Freehold Royalties Ltd. (Freehold) is a dividend-paying corporation incorporated under the laws of the Province of Alberta. Freehold's primary focus is acquiring and managing oil and gas royalties.

Freehold's principal place of business is located at 400, 144 - 4 Avenue SW, Calgary, Alberta, Canada T2P 3N4.

a. Statement of compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS). A summary of Freehold's significant accounting policies under IFRS are presented in note 2.

These consolidated financial statements were approved by the Board of Directors on March 2, 2017.

b. Basis of measurement and principles of consolidation

These consolidated financial statements have been prepared on a historical cost basis, with the exception of certain share based compensation payable, and include the accounts of Freehold and its wholly-owned subsidiaries: 1872348 Alberta Ltd., Freehold Holdings Trust and Freehold Royalties Partnership. All inter-entity transactions have been eliminated.

c. Use of estimates and judgment

The preparation of financial statements in accordance with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities and the reported amounts of revenue and expenses during the reporting period. Actual results could differ as a result of using estimates.

The amounts recorded for the depletion of petroleum and natural gas properties, the provision for decommissioning liability and the amounts used in the impairment calculations are based on estimates of petroleum and natural gas reserves and future costs to develop those reserves. By their nature, these estimates of reserves, costs and related future cash flows are subject to uncertainty, and the impact on the financial statements of future periods could be material.

The decommissioning liability amounts recorded are based on estimates of inflation rates, risk-free rates, timing of abandonments and future abandonment costs, all of which are subject to uncertainty. The long-term incentive plan amounts recorded include an estimate of forfeitures and certain management assumptions. The retirement benefit amounts recorded include an estimated discount rate. Actual results could differ as a result of using estimates.

Income tax liabilities and assets are recognized for the estimated tax consequences attributable to differences between the amounts reported in the financial statements and their respective tax bases, using enacted or substantively enacted income tax rates. The effect of a change in income tax rates on deferred income tax liabilities and assets is recognized in income in the period that the change occurs. The actual amount of income tax may be greater than or less than the estimates and the differences may be material.

The determination of a cash generating unit (CGU) and whether an acquisition transaction constitutes a business combination is subject to management judgments. The recoverability of petroleum and natural gas interests and exploration and evaluation assets are assessed at the CGU level. A CGU is the lowest level at which there are identifiable cash inflows that are largely independent of the cash inflows of other CGUs. Each acquisition transaction is reviewed by management and judgment is used when determining if the transaction met the IFRS 3 inputs and processes criteria for business combinations.

Freehold follows the accrual method of accounting, making estimates in its financial and operating results. This may include estimates of revenues, royalties, production and other expenses and capital items related to the period being reported, for which actual results have not yet been received. It is expected that these accrual estimates will be revised, upwards or downwards, based on the receipt of actual results. Freehold has no operational control over its royalty lands and primarily holds small interests in several thousand wells. Thus, obtaining timely production data from the well operators is extremely difficult. As a result, Freehold uses government reporting databases and past production receipts to estimate revenue accruals.

Significant judgment is required to determine the interests of royalty properties in areas where mineral rights are shared with a related party, Canpar Holdings Ltd. (Canpar). Freehold uses publicly available information on geological formations to apportion revenues between the entities in accordance with the respective party's interests. As new geological information becomes available and as part of its ongoing internal audit activities, Freehold periodically revises these allocations and consideration is transferred to reflect the changes.

d. Functional and presentation currency

These consolidated financial statements are presented in Canadian dollars, which is the functional currency of Freehold and its subsidiaries.

2. Significant Accounting Policies

a. Jointly controlled operations and jointly controlled assets

Some of Freehold's oil and gas activities involve jointly controlled assets. These consolidated financial statements include only Freehold's share of the jointly controlled assets and a proportionate share of the relevant revenue and related costs.

b. Exploration and evaluation assets

Exploration and evaluation (E&E) costs are accounted for in accordance with IFRS 6, *Exploration for and Evaluation of Mineral Resources*. All E&E costs incurred after acquiring the "right to explore" are capitalized into a single cost pool. Upon determination of the technical feasibility and commercial viability of reserves, the associated E&E costs are assessed for impairment and the estimated recoverable amount is transferred to petroleum and natural gas interests. All costs incurred prior to acquiring the "right to explore" are expensed as incurred. At each reporting date, E&E costs are reviewed for indicators of impairment. If circumstances indicate the carrying amount exceeds its recoverable amount, the cost is written down to its recoverable amount and the difference is accounted for as an impairment expense. No depletion or depreciation is charged to E&E.

c. Petroleum and natural gas interests

Petroleum and natural gas interests

Petroleum and natural gas interests are classified under International Accounting Standard (IAS) 16 as Property, Plant and Equipment and include both working and royalty interests, stated at cost, less accumulated depletion and accumulated impairment losses. All costs incurred after determining technical feasibility and commercial viability of reserves are capitalized. Subsequent expenditures are capitalized only where they enhance the economic benefits of the asset. A gain or loss on disposal of a petroleum and natural gas interest is recognized to the extent that the net proceeds exceed or are less than the appropriate portion of the capitalized costs of the asset.

Depletion

Petroleum and natural gas interests, including the costs of production equipment, future capital costs, estimated decommissioning liability costs, and directly attributable general and administrative costs, are depleted on the unit-of-production method based on estimated proved plus probable oil and gas reserves. Reserves are converted to equivalent units on the basis of relative energy content.

Impairment

At each reporting date, Freehold assesses groups of assets or CGUs, for impairment whenever events or changes in circumstances indicate that the carrying value of the CGU may not be recoverable. If any such indication of impairment exists, Freehold makes an estimate of its recoverable amount. A CGU's recoverable amount is the higher of its fair value less costs of disposal (FVLCTD) and its value in use (VIU). Where the carrying amount of a CGU exceeds its recoverable amount, the CGU is considered impaired and is written down. In assessing VIU, the estimated future cash flows are adjusted for the risks specific to the CGU and are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money. FVLCTD is the amount obtainable from the sale of assets in an arm's length transaction less cost of disposal.

An assessment is made at each reporting date as to whether there is any indication that previously recognized impairment losses may no longer exist or have decreased. If such indication exists, the recoverable amount is estimated. A previously recognized impairment loss is reversed only if there has been a change in the estimates used to determine the CGU's recoverable amount since the last impairment loss was recognized. If that is the case, the carrying amount of the CGU is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depletion, had no impairment loss been recognized for the CGU in prior periods. Such a reversal is recognized in profit or loss. After such a reversal, the depletion charge is adjusted in future periods to allocate the CGU's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life.

d. Decommissioning liability

Freehold measures the decommissioning liability as the present value of management's best estimate of the expenditure required to settle the liability at the reporting date using a risk-free discount rate. This estimate is recognized when a legal or constructive obligation arises and is recorded as a long-term liability, with a corresponding increase in the carrying value of the petroleum and natural gas working interest asset. The capitalized amount is depleted on a unit-of-production method over the life of the reserves. At each reporting date, the passage of time and changes to estimates results in liability changes, and the amount of accretion is charged against current period income.

e. Income taxes

Freehold follows the asset and liability method of accounting for income taxes. Under this method, income tax liabilities and assets are recognized for the estimated tax consequences attributable to differences between the amounts reported in the financial statements and their respective tax bases, using enacted or substantially enacted income tax rates. The effect of a change in income tax rates on deferred income tax liabilities and assets is recognized in income in the period that the change occurs.

f. Share based compensation plans**Long-term incentive plan**

Freehold funds its proportionate share of the costs associated with a long-term incentive compensation plan (LTIP) for employees of Rife Resources Ltd. (Rife) through the Manager of Freehold, Rife Resources Management Ltd. The LTIP uses a combination of the value of phantom Rife shares and Freehold shares as the basis for rights, which are granted annually at the discretion of the directors of Rife and vest at the end of a three-year period. Dividends to shareholders paid by Freehold during the vesting period are assumed to be reinvested in notional rights on the dividend payment date. Since participants in the LTIP receive a cash payment on a fixed vesting date, a liability is determined and recognized as services are rendered based on the fair value of the rights at each period end. The valuation incorporates the consideration of the share price, the number of rights outstanding at each period end, an estimated performance multiplier (0.25 to 1.5 times the market value) and an estimated forfeiture rate. Compensation expense is recognized over the vesting period.

Deferred share unit plan

A deferred share unit (DSU) plan was established for the non-management directors of Freehold whereby fully-vested DSUs are granted annually. Under this plan, dividends to shareholders declared prior to redemption are assumed to be reinvested on behalf of the directors in notional share units on the dividend payment date. Compensation expense is recognized at the market value of Freehold's common shares at the time of grant or dividend, with a corresponding increase to contributed surplus. Upon redemption of the DSUs for Freehold's common shares, the amount previously recognized in contributed surplus is recorded as an increase to shareholders' capital.

Retirement benefit

Freehold funds its proportionate share of a retirement benefit for certain former employees of the Manager, upon fulfilling certain criteria. The retirement benefit is paid in four equal installments. Freehold accrues its share of the post retirement costs over the service life of the employees.

g. Net income per share

Basic net income per share is calculated using the weighted average number of shares outstanding for each period. Diluted net income per share is calculated using the weighted average number of diluted shares outstanding for each period. Diluted shares outstanding are calculated assuming that any proceeds received from options with a market value in excess of option price would be used to buy back shares at the average market price for the period.

h. Revenue recognition

Royalty and other revenue is made up of royalty, working interest and other revenue earned during the period. Royalty and other revenue represent the sale of crude oil, natural gas, natural gas liquids and other products. Revenue is recognized when title passes from

Freehold, or the operator of Freehold's properties, to its customers. Royalty and other revenue is measured at the fair value, using estimates, per the terms of various agreements. Actual results could differ as a result of using estimates and any differences are recorded in the period in which actuals are received.

i. Financial instruments

All financial instruments, including all derivatives, are recognized on the balance sheet initially at fair value. Subsequent measurement of all financial assets and liabilities, except those measured at fair value through profit and loss and available-for-sale, are measured at amortized cost using the effective interest rate method. Available-for-sale financial assets are measured at fair value with changes in fair value recognized in comprehensive income and reclassified to earnings when derecognized or impaired.

Cash and short-term investments, if any, are financial assets measured at fair value through profit or loss, and the fair values approximate their carrying value due to their short-term nature. Accounts receivable and current taxes receivable are classified as loans and receivables and are measured at amortized cost. Dividends payable, accounts payable and accrued liabilities and long-term debt are classified as other financial liabilities and are measured at amortized cost. The fair values of accounts receivable, current taxes receivable, dividends payable, accounts payable and accrued liabilities approximate their carrying value due to the short-term nature of these instruments. Freehold has not designated any financial instruments as available-for-sale, held-to-maturity or financial liabilities at fair value through profit and loss. Freehold does not have any material embedded derivatives that required separate recognition and measurement.

A three level hierarchy that reflects the significance of the inputs used in making the fair value measurements is required. Fair values of assets and liabilities included in Level 1 are determined by reference to quoted prices in active markets for identical assets and liabilities. Assets and liabilities in Level 2 include valuations using inputs other than quoted prices for which all significant outputs are observable, either directly or indirectly. Level 3 valuations are based on inputs that are unobservable and significant to the overall fair value measurement.

j. Recent pronouncements

In May 2014, the IASB issued IFRS 15 Revenue from Contracts with Customers, which replaces IAS 11 Construction Contracts, IAS 18 Revenue, and other revenue related interpretations. The standard establishes a single revenue recognition framework that applies to contracts with customers. The effective date for adopting IFRS 15 in its entirety is January 1, 2018. Freehold is in the process of reviewing its royalty and other revenue streams along with underlying contracts to determine the impact on the consolidated financial statements and additional disclosure requirements.

In July 2014, the IASB completed a three-phase project to replace IAS 39 Financial Instruments: Recognition and Measurement with IFRS 9 Financial Instruments. The first two completed phases replaced the current multiple classification and measurement models for financial assets and liabilities with a single model that has only two classification categories: amortized cost and fair value. The third phase describes a new hedge accounting model. Presently and historically, Freehold has not entered into any transactions in which hedge accounting could be applied and don't anticipate changing this practice. The effective date for adopting IFRS 9 in its entirety is January 1, 2018.

In January, 2016, the IASB issued IFRS 16 Leases, which replaces IAS 17 Leases. The standard establishes a single lessee accounting model and requires a lessee to recognize assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee is required to recognize a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments.

Other areas of the lease accounting model have been impacted, including the definition of a lease. Transitional provisions have been provided. The effective date for adopting IFRS 16 in its entirety is January 1, 2019.

Freehold's assessment of these recent pronouncements is ongoing and the impact, if any, on the consolidated financial statements and additional disclosure requirements are yet to be determined.

3. Corporate Acquisition

On January 23, 2015 Freehold acquired all of the outstanding shares of Anderson Energy Ltd. ("Anderson") pursuant to a plan of arrangement under the Business Corporations Act (Alberta) for total consideration of \$35 million with Freehold funding the deal through its existing credit facilities. This transaction added approximately \$220 million to existing tax pools. The fair value of the petroleum and natural gas interests and decommissioning liabilities acquired was determined using internal estimates. A gain on corporate acquisition of \$24.3 million was recognized as the estimated value of income tax pools less the fair value of assets and liabilities exceeded the consideration paid.

4. Exploration and Evaluation Assets

(\$000s)	December 31, 2016	December 31, 2015
Balance, beginning of year	49,479	37,852
Acquisitions (note 5)	17,980	14,300
Transfers to petroleum and natural gas interests (note 5)	(3,440)	(2,673)
Balance, end of year	64,019	49,479

There were no indicators of impairment or impairment reversal for the year ended December 31, 2016 or December 31, 2015. As a result no impairment or impairment reversal testing was conducted.

5. Petroleum and Natural Gas Interests

(\$000s)	December 31, 2016	December 31, 2015
Cost		
Balance, beginning of year	1,271,382	874,377
Acquisitions	144,610	369,585
Capital expenditures	5,218	22,295
Capitalized portion of long term incentive plan	167	11
Transfers from exploration and evaluation assets (note 4)	3,440	2,673
Decommissioning liability additions and revisions (note 7)	(3,981)	2,441
Balance, end of year	1,420,836	1,271,382
Accumulated depletion and depreciation		
Balance, beginning of year	(424,557)	(290,054)
Impairment	-	(38,800)
Depletion and depreciation	(104,159)	(95,703)
Balance, end of year	(528,716)	(424,557)
Net book value, end of year	892,120	846,825

The depletion calculation included \$13.8 million (2015 - \$14.5 million) for estimated future development costs associated with proved plus probable undeveloped reserves.

For the year ended December 31, 2016, Freehold capitalized \$1.5 million (2015 - \$1.5 million) of administrative costs and capitalized \$167,000 (2015 - \$11,000) of LTIP costs directly related to development activities.

On May 25, 2016, Freehold acquired an extensive suite of royalty production and lands for \$161.8 million, including adjustments, which included \$17.9 million of undeveloped land classified as an exploration and evaluation asset. In addition, during the year ended December 31, 2016, Freehold had additional minor acquisition expenditures of \$0.8 million.

During the year ended December 31, 2015, including the corporate acquisition described in note 3, Freehold had several acquisition expenditures of \$411.4 million, including adjustments.

Impairment

There were no indicators of impairment or impairment reversal for the year ended December 31, 2016. As a result no impairment or impairment reversal testing was conducted.

At December 31, 2015 Freehold tested its two working interest cash generating units (CGUs) for impairment due to the continued drop in expected future commodity prices as recognized by industry reserve evaluators. Freehold estimated the recoverable amount as the value in use based on discounted future net cash flows of proved and probable reserves using forecast prices and costs, discounted at 10% (pre-tax). In determining the discount rate, Freehold considered an estimated industry weighted cost of capital and the resource composition of the assets. The estimate was based on Freehold's December 31, 2015 reserve report. Management recognizes that all assumptions and estimates affecting the value are subject to a high degree of uncertainty.

Freehold recognized a non-cash impairment charge on its Southeast Saskatchewan Working Interest CGU of \$8.0 million as the carrying value exceeded the estimated value in use. The Southeast Saskatchewan Working Interest CGU contains all of Freehold's working interest properties in southeast Saskatchewan. The estimated recoverable amount of the Southeast Saskatchewan CGU at December 31, 2015 is \$29.1 million. In addition, Freehold recognized a non-cash impairment charge on its Other Working Interest CGU of \$30.8 million as the carrying value exceeded the estimated value in use. The Other Working Interest CGU contains Freehold's diverse group of working interest properties outside of the Southeast Saskatchewan Working Interest CGU. The estimated recoverable amount of the Other Working Interest CGU at December 31, 2015 is \$54.7 million.

As future commodity prices continue to fluctuate, additional impairment charges or recoveries could be recorded in future periods. The value in use estimates are categorized as Level 3 according to the IFRS 13 fair value hierarchy. The following table summarizes key benchmarks used in the impairment estimate.

	WTI US\$/bbl	WCS Cdn\$/bbl	WCS Cdn\$/bbl	Exchange rate Cdn\$/US\$
2016	45.00	45.26	2.25	0.75
2017	60.00	57.96	2.95	0.80
2018	70.00	65.88	3.42	0.83
2019	80.00	75.11	3.91	0.85
2020	81.20	77.03	4.20	0.85
2021	82.42	78.19	4.28	0.85
Average annual increase, thereafter	1.5%	1.5%	1.5%	-

6. Long-term Debt

Freehold has a \$245 million extendible revolving term credit facility with a syndicate of four Canadian chartered banks, on which \$84 million was drawn at December 31, 2016. In addition, Freehold has available a \$15 million extendible revolving operating facility.

The facilities are secured with \$400 million demand debentures over Freehold's petroleum and natural gas assets but do not contain any financial covenants. The lenders at any time can request a redetermination of the borrowing base, which may require a repayment to the lenders within 90 days of receiving notice, of an amount that the indebtedness is in excess of the redetermined borrowing base. The facilities are extendible annually with the latest review completed in May 2016. Freehold's borrowing base is dependent on the lenders annual review and interpretation of Freehold's reserves and future commodity prices, with the next renewal to occur by May 2017. In the event that the lenders do not consent to an extension, the revolving credit facility would revert to a two-year, non-revolving term facility with equal quarterly principal repayments. The first quarterly payment would commence on January 1 of the year following the end of the revolving period.

Borrowings under the facilities bear interest at the bank's prime lending rate, bankers' acceptance or LIBOR rates plus applicable margins and standby fees. At December 31, 2016 and December 31, 2015 the fair values of the long-term debt approximated its carrying value, as the long-term debt carries interest at prevailing market rates. In 2016, the average effective interest rate on advances under Freehold's credit facilities was 2.9% (2015 - 2.9%).

7. Decommissioning Liability

Freehold has no decommissioning liability on its royalty interest properties. Freehold's decommissioning liability results from its responsibility to abandon and reclaim its net share of all working interest properties. The undiscounted value of Freehold's total decommissioning liability is estimated to be \$36.3 million (2015 - \$40.6 million). Payments to settle the obligations are expected to occur over the next 57 years, with the majority being settled within 7 to 17 years. At December 31, 2016, a risk-free rate of 2.3% (2015 - 2.2%) and an inflation rate of 2.0% (2015 - 1.5%) were used to calculate the fair value.

(\$000s)	December 31, 2016	December 31, 2015
Balance, beginning of year	27,635	21,279
Liabilities incurred	45	1,091
Liabilities settled	(492)	(227)
Revision in estimates ⁽¹⁾	(4,026)	1,350
Accretion expense	543	566
Corporate acquisition (note 3)	-	3,576
Balance, end of year	23,705	27,635

(1) For the year ended December 31, 2016 the revision in estimates decrease was primarily a result of the increase in the risk-free rate, decrease in the estimated abandonment costs and partially offset by the increase in inflation rate.

8. Shareholders' Capital

Freehold has authorized an unlimited number of common shares, without stated par value. Freehold has authorized 10,000,000 preferred shares, without stated par value, of which none have been issued.

SHARES ISSUED AND OUTSTANDING

	December 31, 2016		December 31, 2015	
	Shares	Amount (\$000s)	Shares	Amount (\$000s)
Balance, beginning of year	98,940,152	1,050,494	74,918,711	635,223
Issued for dividend reinvestment plan	488,060	4,997	1,218,129	17,225
Issued for payment of management fee	287,648	3,543	269,978	3,693
Issued for deferred share unit plan redemption	59,198	1,066	-	-
Cancelled	(17,684)	(214)	-	-
Issued for equity offering	18,160,900	209,759	22,533,334	405,600
Issue costs, net of tax effect	-	(5,849)	-	(11,247)
Balance, end of year	117,918,274	1,263,796	98,940,152	1,050,494

On May 25, 2016 Freehold closed a bought deal equity offering, issuing 16,428,900 common shares and a private equity offering with CN Pension Trust Funds (see note 9) issuing 1,732,000 common shares, both at a price of \$11.55 per share for gross proceeds of \$209.8 million. The issue costs including the underwriter fees were \$8.0 million (\$5.8 million net of a tax effect).

On May 6, 2015, Freehold closed a bought deal equity offering, issuing 20,700,000 common shares and a private equity offering to CN Pension Trust Funds issuing 1,833,334 common shares, both at a price of \$18.00 per share for gross proceeds of \$405.6 million. The issue costs including the underwriter fees were \$15.4 million (\$11.2 million net of a tax effect).

On November 30, 2016, the rights of holders of trust units of Freehold Royalty Trust not deposited on or prior to this date have been terminated. Therefore, for the year ended December 31, 2016, Freehold cancelled 17,684 common shares and received \$0.1 million for the return of related unclaimed accumulated dividends.

At December 31, 2016, a balance of 1,987,307 shares was reserved for the dividend reinvestment plan (DRIP), 678,467 shares for the management fee (note 9) and 511,737 shares for the deferred share unit plan (note 10).

For the year ended December 31, 2016 and 2015, deferred share units were excluded from the calculation of diluted net loss per share as their effect was anti-dilutive.

9. Related Party Transactions

Freehold does not have any employees. Rife Resources Management Ltd. (the Manager) is the manager of Freehold. The Manager is a wholly-owned subsidiary of Rife Resources Ltd. (Rife), and two of Rife's directors are also directors of Freehold. Rife is 100% owned by the CN Pension Trust Funds (the pension funds for the employees of the Canadian National Railway Company), which in turn is a shareholder of Freehold. The Manager recovers its general and administrative costs and a portion of its long-term incentive plan costs and retirement benefit costs, and receives a quarterly management fee paid in shares. Canpar Holdings Ltd. (Canpar) is also managed by Rife and owned 100% by the CN Pension Trust Funds, and two of Canpar's directors are also directors of Freehold.

(a) Rife Resources Management Ltd.

The Manager provides certain services for a fee based on a specified number of shares per quarter, pursuant to the amended and restated management agreement. The amended and restated management agreement caps the management fee at 71,912 shares per quarter for 2016 and the number of shares to be issued per quarter as payment of the management fee decreases to a level of 5,500 shares per quarter by 2023. For the year ended December 31, 2016, Freehold issued 287,648 shares (2015 - 269,978) as payment of the management fee to the Manager pursuant to the management agreement. For the year ended December 31, 2016, the ascribed value of \$3.5 million (2015 - \$3.7 million) was based on the closing price of the shares on the last trading day of each quarter.

For the year ended December 31, 2016, the Manager charged \$9.0 million in general and administrative costs (2015 - \$9.0 million). At December 31, 2016, there was \$0.9 million (2015 - \$0.7 million) in accounts payable and accrued liabilities relating to these costs.

(b) Rife Resources Ltd.

Freehold maintains ownership interests in certain oil and gas properties operated by Rife. A portion of net operating revenues and capital expenditures represent joint operations amounts from Rife. At December 31, 2016, there was \$0.1 million (2015 - \$nil) in accounts receivable related to these transactions. At December 31, 2016, there was \$nil (2015 - \$nil) in accounts payable and accrued liabilities relating to these transactions.

In addition, Freehold receives royalties from Rife pursuant to various royalty agreements. For the year ended December 31, 2016, Freehold received royalties of approximately \$0.9 million (2015 - \$1.5 million). At December 31, 2016, there was \$0.1 million (2015 - \$0.1 million) in accounts receivable relating to these transactions.

(c) Canpar Holdings Ltd.

Freehold and Canpar share mineral title ownership rights in a substantial land base in western Canada. Generally, Canpar owns mineral rights that were below the deepest producing formation at the time that Freehold was created, and Freehold holds the balance of the mineral rights. Given the nature of the mineral rights, which are dependent upon hydrocarbon pool formation classification as well as third party drilling data which is subject to change and revision, significant uncertainty can exist with respect to the royalty ownership of wells drilled and completed on lands where both Freehold and Canpar hold the mineral rights.

During 2015, Freehold and Canpar evaluated certain of these royalty interests where, among other factors, the identification of the reservoir formation was not straight forward and therefore ultimate ownership of the royalty interest wells was uncertain between Freehold and Canpar. The project relating to the evaluation of these interests resulted in a settlement of \$0.8 million recognized in other income in 2015.

At December 31, 2016, there was \$nil (2015 - \$nil) in accounts receivable and accounts payable and accrued liabilities relating to transactions with Canpar.

(d) CN Pension Trust Funds

Concurrent with the closing of the bought deal public equity offering completed by Freehold on May 25, 2016, CN Pension Trust Funds invested approximately \$20 million through the purchase of 1,732,000 common shares on a non-brokered private placement basis. The price paid per common share by CN Pension Trust Funds pursuant to the private placement was the same price paid per common share by purchasers pursuant to the bought deal public equity offering.

Concurrent with the closing of the bought deal public equity offering completed by Freehold on May 6, 2015, CN Pension Trust Funds invested approximately \$33 million in Freehold

through the purchase of 1,833,334 common shares on a non-brokered private placement basis. The price paid per common share by CN Pension Trust Funds pursuant to the private placement was the same price paid per common share by purchasers pursuant to the bought deal public equity offering.

All amounts owing to/from the Manager, Rife, and Canpar are unsecured, non-interest bearing and due on demand. All transactions were in the normal course of operations and were measured at the amount of consideration established and agreed to by both parties.

Expenses relating to compensation for key management personnel, considered to be Freehold's Board of Directors and Senior Management, are as follows:

(\$000s)	December 31, 2016	December 31, 2015
Short-term benefits (including employee wages and directors fees)	966	1,346
Share based compensation (note 10a and 10b)	640	723
Total	1,606	2,069

10. Share Based Compensation

a. Long-term incentive plan

Freehold funds its proportionate share of the costs associated with the LTIP for employees of Rife through the Manager, as described in note 2f. The share based compensation expense was based on the consideration of the share price, the number of rights outstanding at each period end, an estimated performance multiplier and an estimated forfeiture rate. The 2013 LTIP grants valued at \$0.1 million were paid out in 2016. The total expensed for the year ended December 31, 2016 was \$0.8 million (2015 – \$0.1 million). For the year ended December 31, 2016, Freehold capitalized \$167,000 (2015 – \$11,000) of LTIP costs directly related to development activities.

The following table reconciles the change in total accrued share based incentive compensation:

(\$000s)	December 31, 2016	December 31, 2015
Balance, beginning of year	257	741
Increase in liability	928	61
Cash payout	(120)	(545)
Balance, end of year	1,065	257
Current portion of liability	133	120
Long-term portion of liability	932	137

The following table reconciles the incentive plan activity for the period:

PHANTOM COMMON SHARES

	December 31, 2016	December 31, 2015
Balance, beginning of year ⁽¹⁾	142,108	118,482
Issued	105,735	57,019
Dividends reinvested ⁽¹⁾	11,170	10,677
Cash payout	(44,150)	(44,070)
Balance, end of year	214,863	142,108

(1) Balance as at December 31, 2015 has been adjusted for revised estimates.

b. Deferred share unit plan

Freehold has a deferred share unit (DSU) plan for non-management directors as described in note 2f. As at December 31, 2016, there were 148,499 DSUs outstanding (2015 - 177,012), which are redeemable for an equal number of shares any time after the director's retirement. For the year-end December 31, 2016, 84,567 DSUs were redeemed, resulting in the issuance of 59,198 shares from treasury. In payment of withholding tax, 25,369 DSUs were cancelled and the cash value of \$0.3 million was remitted to Canada Revenue Agency. For the year ended December 31, 2015 no DSUs were redeemed.

DEFERRED SHARE UNITS

	December 31, 2016	December 31, 2015
Balance, beginning of year	177,012	136,455
Annual grants	46,663	28,007
Additional resulting from dividends	9,391	12,550
Redeemed	(84,567)	-
Balance, end of year	148,499	177,012

For the year ended December 31, 2016, Freehold expensed \$0.4 million (2015 - \$0.7 million) of share based compensation with a corresponding offset to contributed surplus.

c. Retirement benefit

Freehold participates in its proportionate share of a retirement benefit plan for certain former employees of the Manager as described in note 2f. For the year ended December 31, 2016, Freehold expensed \$5,000 (2015 - \$11,000).

(\$000s)	December 31, 2016	December 31, 2015
Accrued benefit obligation, beginning of year	128	191
Current service cost	5	11
Payments	(84)	(74)
Accrued benefit obligation, end of year	49	128
Current portion of liability	49	74
Long-term portion of liability	-	54

11. Income Taxes

Freehold uses the asset and liability method of accounting for income taxes, as described in note 2e.

The provision for taxes in the financial statements differs from the result which would have been obtained by applying the combined federal and provincial effective tax rate to Freehold's income before taxes.

This difference is reconciled as follows:

<i>(\$000s, except as noted)</i>	December 31, 2016	December 31, 2015
Loss before taxes	(14,260)	(15,619)
Combined federal and provincial tax rate	27.0%	26.2%
Computed expected income tax recovery	(3,850)	(4,092)
Increase (decrease) in income tax resulting from:		
True up of tax pools	460	-
Deferred share unit plan redemption	288	-
Gain on corporate acquisition	-	(6,377)
Effect of rate change	-	(958)
Miscellaneous items	5	(112)
Total income taxes	(3,097)	(11,539)

The components of deferred income taxes are as follows:

<i>(\$000s)</i>	December 31, 2016	December 31, 2015
Deferred income tax assets:		
Non-capital losses	47,250	44,645
Decommissioning liability	6,400	7,461
Share issue expense	4,838	4,415
Deferred income tax liabilities:		
Petroleum and natural gas interests	(33,074)	(30,213)
Deferred tax on partnership income	-	(6,203)
Other	941	990
Net deferred income tax asset	26,355	21,095

The continuity of deferred income taxes is as follows:

(\$000s)	Balance December 31, 2015	Recognized in Profit or Loss	Recognized in Equity	Balance December 31, 2016
Non-capital losses	44,645	2,605	-	47,250
Decommissioning liability	7,461	(1,061)	-	6,400
Share issue expense	4,415	(1,740)	2,163	4,838
Petroleum and natural gas interests	(30,213)	(2,861)	-	(33,074)
Deferred tax on partnership income	(6,203)	6,203	-	-
Other	990	(49)	-	941
Total	21,095	3,097	2,163	26,355

Freehold's deferred tax liability relates to its assets having a higher carrying value relative to the associated tax value. Freehold's deferred tax asset primarily relates to the non-capital losses due to a corporate acquisition (note 3). When combined there is an overall net deferred tax asset.

12. Capital Management

Freehold is a publicly traded dividend-paying corporation incorporated under the laws of the Province of Alberta. Its primary focus is acquiring and managing oil and gas royalties. Freehold receives revenue from oil and gas properties as reserves are produced, which is paid to shareholders on a regular basis over the economic life of the properties. Freehold's objective for managing capital is to maximize long-term shareholder value by distributing to shareholders any cash that is not required for financing operations or capital investment growth opportunities that may offer shareholders better value.

Freehold defines capital as long-term debt, shareholders' equity and working capital based on the consolidated financial statements. Freehold's capital structure is managed by taking into account operating activities, debt levels, debt covenants, capital expenditures, DRIP participation, dividend levels and taxes, among others. In addition, changes in economic conditions, commodity prices and the risk characteristics of Freehold's assets are considered. Freehold has a declining asset base, therefore ongoing development activities and acquisitions are necessary to replace production and add additional reserves. From time to time, Freehold may issue shares or adjust capital spending to manage current and projected debt levels.

Freehold retains working capital primarily to fund capital expenditures or acquisitions, pay dividends and reduce bank indebtedness. Historically, Freehold has chosen to issue its DRIP out of treasury, which increases its flexibility with the use of working capital. DRIP participation levels can fluctuate significantly on a monthly basis depending on shareholder requirements. Effective with the August 31, 2016 dividend the Board approved the suspension of the DRIP pending further notice.

Management of Freehold's capital structure is facilitated through its financial and operating forecasting processes. The forecast of Freehold's future cash flows is based on estimates of production, commodity prices, forecast capital, royalty expenses, operating expenditures, taxes and other investing and financing activities. The forecast is regularly updated based on new commodity prices and other changes that Freehold views as critical in the current environment. Selected forecast information is frequently provided to and approved by the Board of Directors.

Freehold is bound by non-financial covenants on its credit facilities. The covenants are monitored as part of management's internal review to ensure compliance with requirements. Under the credit facilities, Freehold is restricted from paying dividends if it is or would be in default under the credit facilities or if borrowings thereunder exceed the borrowing base. As at December 31, 2016, Freehold was in compliance with all such covenants.

CAPITALIZATION

	December 31, 2016	December 31, 2015
Shareholders' equity	884,696	742,624
Long-term debt	84,000	152,000
Working capital	(10,839)	(5,051)
Net debt ⁽¹⁾	73,161	146,949
Cash provided by operating activities for last 12 months	93,133	110,513
Change in non-cash operating working capital	1,078	(6,693)
Trailing 12 months funds from operations	94,211	103,820
Net debt to trailing 12 month funds from operations (times)	0.8	1.4

(1) Net debt as presented does not have any standardized meaning prescribed by IFRS; and therefore may not be comparable to a similar measure of other entities.

13. Financial Instrument Risk Management

Freehold has exposure to credit, liquidity and market risks from its use of financial instruments. Management employs the following strategies to mitigate these risks.

a. Credit risk

Credit risk is the risk of financial loss to Freehold if a customer or counterparty to a financial instrument fails to meet its contractual obligations and arises principally from Freehold's receivables. A large part of accounts receivable is with oil and gas industry operators, either as joint venture partners or as payors of various royalty agreements. These agreements provide mechanisms to ensure that Freehold's interests are protected. There are also systems and processes in place to identify any unpaid or incorrect revenues. Freehold's diversified revenue stream limits the size of any one property or industry operator with respect to total receivables.

Freehold maintains a dedicated compliance function, with a comprehensive auditing program, to ensure that the terms of the various agreements are followed, including that royalties are paid correctly on production from Freehold's lands in accordance with the prices obtained by the royalty payor and that unwarranted or excessive deductions are not being taken. Freehold also audits its working interest properties to ensure that capital costs, operating expenses and production volumes are properly allocated.

The carrying amounts of accounts receivable and cash represent Freehold's maximum credit exposure. Freehold did not have an allowance for doubtful accounts as at December 31, 2016 or 2015, and did not provide for any doubtful accounts and was not required to write off any significant receivables during the years ended December 31, 2016 or 2015. Freehold considers all material amounts greater than three months to be past due. Due to the nature of Freehold's royalty income assets, there are amounts over three months which require significant time and effort to collect.

Estimates of amounts owed for various time periods are as follows:

(\$000s)	Less than 3 months	4-12 months	Over 1 year	Total
Accounts receivable	21,472	1,970	622	24,064

Freehold markets approximately 75% of its production along with the operator or royalty payor under the terms of a diverse number of agreements. Freehold takes a portion of its production in kind (approximately 25%) and sells to two primary purchasers.

b. Liquidity risk

Liquidity risk is the risk that Freehold will not be able to meet financial obligations as they come due. Management maintains a conservative approach to debt management that aims to provide maximum financial flexibility with respect to acquisitions and development expenditures, while maintaining stable dividend payments. At December 31, 2016, there was \$176 million of available capacity under the credit facilities. As circumstances warrant, management allocates a portion of funds from operations to debt repayment. Management prepares annual capital expenditure and operating budgets, which are regularly monitored and updated. In addition, dividend levels are monitored and adjusted as necessary to levels that are supported by our funds from operations.

Freehold's non-derivative financial liabilities include its dividends payable, accounts payable and accrued liabilities, share based compensation payable and long-term debt. Freehold has no derivative financial liabilities. The following table outlines cash flows associated with the contractual maturities of Freehold's non-derivative financial liabilities as at December 31, 2016:

(\$000s)	Less than 1 Year	2-3 Years	Total
Dividends payable	4,716	-	4,716
Accounts payable and accrued liabilities	9,219	-	9,219
Share based compensation payable	182	932	1,114
Long-term debt	-	84,000	84,000
Total	14,117	84,932	99,049

c. Market risk

Market risk is the risk that changes in market prices, such as foreign currency exchange rates, commodity prices and interest rates, will affect net income or the value of financial instruments. The Board reviews the potential use of derivative contracts on a quarterly basis. For short-term investments, if any, Freehold selects counterparties based on strong credit ratings and monitors all investments to ensure a stable return.

Foreign currency exchange rate risk

Freehold does not sell or transact in any foreign currency; however, the underlying market prices in Canada for oil and natural gas are influenced by changes in the exchange rate between the Canadian and U.S. dollar. During the years ended December 31, 2016 and 2015, Freehold had no foreign exchange related derivative contracts in place. Assuming all other variables held constant, a \$0.01 change (plus or minus) in the U.S./Canadian dollar exchange rate for the year ended December 31, 2016, would have resulted in a corresponding change to income before taxes of approximately \$1.4 million (2015 - \$1.4 million).

Commodity price risk

Commodity price risk is the risk that the fair value of future cash flows will fluctuate with changes in commodity prices. Commodity prices for oil and natural gas are influenced by the relationship between the Canadian and U.S. dollar as well as macroeconomic events that dictate the levels of supply and demand. During the years ended December 31, 2016 and 2015, Freehold had no commodity price related derivative contracts in place. Assuming all other variables held constant, a US\$1.00 change (plus or minus) in the WTI crude oil price for the year ended December 31, 2016, would have resulted in a corresponding change to income before taxes of approximately \$2.4 million (2015 - \$2.2 million). A \$0.25 change (plus or minus) in the AECO natural gas price would have resulted in a corresponding change to income before taxes of approximately \$2.4 million (2015 - \$1.9 million).

Interest rate risk

Freehold is exposed to interest rate risk on outstanding bank debt, which has a floating interest rate, and fluctuations in interest rates would impact future cash flows. Assuming all other variables held constant, a 1% change (plus or minus) in the interest rate for the year ended December 31, 2016 would have resulted in a corresponding change to income before taxes of approximately \$1.2 million (2015 - \$1.7 million).

14. Supplemental Disclosure

a. Statements of income and comprehensive income presentation

Freehold's consolidated statements of income and comprehensive income are prepared by nature of expense.

b. Supplemental cash flow disclosure

CHANGES IN NON-CASH WORKING CAPITAL BALANCE

(\$000s)	December 31, 2016	December 31, 2015
Accounts receivable	(3,018)	5,384
Current taxes receivable	73	2,524
Accounts payable and accrued liabilities	(607)	(6,038)
	(3,552)	1,870
Operating	(1,078)	6,693
Investing	(2,474)	(4,823)
	(3,552)	1,870

CASH EXPENSES

(\$000s)	December 31, 2016	December 31, 2015
Interest	4,343	5,757
Taxes paid (received)	(73)	(7,621)

c. Royalty and other revenue

<i>(\$000s)</i>	December 31, 2016	December 31, 2015
Royalty interest revenue ⁽¹⁾	103,464	99,935
Working interest and other revenue ⁽²⁾	26,504	35,729
	129,968	135,664

(1) Royalty interest revenue includes potash, sulphur, and lease rentals.

(2) Working interest revenue includes processing fees, interest and other.

15. Loss On Settlement

In May 2009, a statement of claim was filed against Freehold for \$9 million. The claim involved disputed land interests and royalty obligations. During the year ended December 31, 2016 Freehold settled the claim with a \$0.9 million payment and removed \$0.2 million of associated accounts receivable, recognizing a total loss of \$1.1 million.

16. Subsequent Event

In February 2017, Freehold closed a royalty acquisition of various gross overriding royalty and mineral title lands in the Doddsland area of Saskatchewan for \$34 million (prior to normal closing adjustments). This acquisition was financed via Freehold's credit facility.

SUPPLEMENTAL INFORMATION

The majority of our assets are royalty interests and under National Instrument 51-101 – *Standards of Disclosure for Oil and Gas Activities* (NI 51-101) royalty interests cannot be included under gross reserves. This causes our gross reserves to be lower than our net reserves and makes it difficult for investors to compare our reserves and finding and development costs to exploration and development companies. We believe the most appropriate measure of reserves and finding and development costs for Freehold is on a net basis.

These royalty interest lands are significant to Freehold. The majority of these lands are leased to third party operators. As a royalty owner, we have no operational control over the operator's future development activities. As such, the extent of drilling and development activity in future years can be difficult to predict. However, these operators have historically invested significant amounts to generate future reserve additions, and production from which Freehold receives certain royalties. Reserve values do not include potential reserve additions that may occur as a result of future drilling on most of our royalty lands.

Our oil and gas reserves were independently evaluated by Trimble Engineering Associates Ltd. (Trimble) as at December 31, 2016. The evaluation was conducted in accordance with the standards contained in the COGE Handbook and the reserve definitions contained in NI 51-101. Our Reserves Committee met with Trimble to review the findings and procedures, and the reserves report has been accepted by our Board of Directors.

Our Annual Information Form, including reserves disclosure required under NI 51-101, is available at www.sedar.com and on our website at www.freeholdroyalties.com.

LAND HOLDINGS AS OF DECEMBER 31, 2016

	Developed	Undeveloped	Total
Mineral Title Lands	389,847	310,573	700,420
Royalty Assumption Lands	71,175	19,932	91,107
Total Title Lands	461,022	330,505	791,527
Gross Overriding Royalty Lands	1,938,807	625,460	2,564,267
Total Royalty Lands	2,399,829	955,965	3,355,794
Working Interest Properties	193,577	46,924	240,501
Total	2,593,406	1,002,889	3,596,295
Additional Lands ⁽¹⁾			2,500,000
Total Land Holdings	2,593,406	1,002,889	6,096,295

(1) Approximately 2,500,000 gross acres of lands acquired from Husky have not been included in the categories as they have not been released from our integration process.

**SUMMARY OF OIL AND GAS RESERVES
AS OF DECEMBER 31, 2016
FORECAST PRICES AND COSTS ⁽¹⁾⁽²⁾**

Reserves Category	Light & Medium Crude Oil		Tight Oil		Heavy Crude Oil	
	Gross ⁽¹⁾ (Mbbls)	Net (Mbbls)	Gross ⁽¹⁾ (Mbbls)	Net (Mbbls)	Gross ⁽¹⁾ (Mbbls)	Net (Mbbls)
Proved						
Developed producing	1,173	5,401	153	744	381	3,242
Developed non-producing	61	56	78	61	-	7
Undeveloped	62	1,565	-	280	-	20
Total proved	1,296	7,021	232	1,084	381	3,269
Probable	1,072	3,929	303	576	323	1,600
Total proved plus probable	2,368	10,950	534	1,660	704	4,869

Reserves Category	Conventional Natural Gas		Coal Bed Methane		Shale Gas	
	Gross ⁽¹⁾ (MMcf)	Net (MMcf)	Gross ⁽¹⁾ (MMcf)	Net (MMcf)	Gross ⁽¹⁾ (MMcf)	Net (MMcf)
Proved						
Developed producing	3,462	53,876	1,270	1,234	-	9
Developed non-producing	1,123	1,013	1,060	961	101	92
Undeveloped	121	16,193	-	-	-	1,254
Total proved	4,706	71,082	2,330	2,195	101	1,356
Probable	2,926	33,930	1,320	1,218	63	638
Total proved plus probable	7,632	105,012	3,650	3,413	164	1,994

Reserves Category	Natural Gas Liquids		Total Oil Equivalent	
	Gross ⁽¹⁾ (Mbbls)	Net (Mbbls)	Gross ⁽¹⁾ (Mboe)	Net (Mboe)
Proved				
Developed producing			191	1,193
Developed non-producing			36	27
Undeveloped			3	354
Total proved			230	1,574
Probable			153	824
Total proved plus probable			383	2,398

- (1) Under NI 51-101, gross reserves include only working interests before the deduction of royalties payable and do not include royalties receivable. Net reserves are comprised of working interests minus royalties payable plus royalties receivable. The majority of the Corporation's assets are royalty interests. This causes our gross reserves to be lower than our net reserves and may hinder an investor's ability to compare our reserves with others in our industry.
- (2) Columns may not add due to rounding.

TEN-YEAR REVIEW

(\$000s)	2016	2015	2014	2013	2012	2011	2010	2009	2008	2007
Financial										
(\$millions, except as noted) ⁽¹⁾										
Royalty and other revenue	130.0	135.7	199.9	181.6	168.1	157.9	138.2	120.0	204.1	152.2
Net income (loss) ⁽¹⁾	(11.2)	(4.1)	66.4	57.9	46.3	55.3	49.3	31.7	110.0	(1.2)
Per share (\$) ⁽²⁾	(0.10)	(0.05)	0.94	0.86	0.71	0.92	0.85	0.63	2.23	(0.02)
Funds from operations	94.2	103.8	138.4	119.4	103.9	128.2	107.0	95.1	171.3	121.0
Per share (\$) ⁽²⁾	0.85	1.15	1.95	1.79	1.60	2.14	1.83	1.90	3.47	2.46
Dividends declared	59.5	90.1	119.8	112.5	109.6	101.0	98.1	70.5	143.7	94.5
Per share (\$) ⁽²⁾⁽³⁾	0.54	1.00	1.68	1.68	1.68	1.68	1.68	1.40	2.91	1.92
Acquisitions	162.6	411.4	248.3	10.1	60.9	7.5	38.6	9.5	7.7	90.5
Capital expenditures	5.2	22.3	33.7	29.3	36.7	25.6	18.1	15.5	13.0	12.2
Long-term debt	84.0	152.0	139.0	49.0	18.0	48.0	65.0	45.0	140.0	178.0
Operating										
Production (boe/d)	12,219	10,945	9,180	8,913	8,850	7,476	7,615	7,302	7,804	8,484
Royalty Interest (%)	81	76	74	70	71	75	73	70	71	69
Oil and NGL (%)	58	62	63	64	64	63	62	64	63	63
Land (gross acres, millions)	6.1	3.7	3.2	3.1	3.0	2.7	2.8	2.4	2.4	2.4
Net reserves (Mmboe) ⁽⁴⁾	38.3	36.1	29.7	23.1	24.4	22.2	23.6	24.1	25.4	28.0
Reserve life index (years)	10.1	9.9	9.0	8.5	8.5	9.1	9.5	9.7	9.8	9.5
Share Data										
High (\$)	15.16	20.62	28.15	24.88	22.45	23.28	21.14	17.00	24.40	15.85
Low (\$)	8.29	8.73	17.02	21.00	17.25	14.51	15.08	6.87	9.15	12.51
Close (\$)	14.17	10.86	19.12	22.11	22.40	19.41	20.49	15.09	10.49	15.60
Volume (millions)	79.6	75.3	43.6	25.8	28.6	28.1	25.8	30.0	36.5	25.1
Outstanding (millions)										
At period end	117.9	98.9	74.9	67.7	66.3	61.1	59.2	57.5	49.5	49.3
Weighted average	110.4	90.5	71.2	66.9	64.9	60.0	58.3	50.0	49.4	49.2

(1) Freehold's IFRS transition date was January 1, 2010 and reflects adjustments due to IFRS. Comparative information for 2006-2009 has not been restated.

(2) Prior to conversion to a corporation on December 31, 2010, Freehold had trust units outstanding instead of shares.

(3) Based on the number of shares issued and outstanding at each record date.

(4) Net proved plus probable reserves.

CORPORATE INFORMATION

Board of Directors

MARVIN F. ROMANOW
Chair of the Board

GARY R. BUGEAUD ^{(1) (2)}
Corporate Director

PETER T. HARRISON
Manager, Oil and Gas Investments
CN Investment Division

J. DOUGLAS KAY ⁽³⁾
Corporate Director

ARTHUR N. KORPACH ^{(1) (2)}
Corporate Director

SUSAN M. MACKENZIE ^{(2) (3)}
Corporate Director

THOMAS J. MULLANE
President and Chief Executive Officer
Rife Resources Ltd.

AIDAN M. WALSH ^{(1) (3)}
Chief Executive Officer
Baccalieu Energy Inc.

- (1) Audit Committee
- (2) Governance, Nominating
and Compensation Committee
- (3) Reserves Committee

Officers

MARVIN F. ROMANOW
Chair of the Board

THOMAS J. MULLANE
President and Chief Executive Officer

DARREN G. GUNDERSON
Vice-President, Finance
and Chief Financial Officer

DAVID M. SPYKER
Vice-President, Production

MICHAEL J. STONE
Vice-President, Land

MICHAEL J. MOGAN
Controller

KAREN C. TAYLOR
Corporate Secretary

Head Office

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Investor Relations

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Manager, Investor Relations
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Auditors

KPMG LLP

Bankers

CANADIAN IMPERIAL BANK
OF COMMERCE
BANK OF MONTREAL
ROYAL BANK OF CANADA
THE TORONTO-DOMINION BANK

Legal Counsel

BURNET, DUCKWORTH &
PALMER LLP

Reserve Evaluators

TRIMBLE ENGINEERING
ASSOCIATES LTD.

Stock Exchange and Trading Symbol

Toronto Stock Exchange (TSX)
Common Shares: FRU

Transfer Agent and Registrar

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