

ALVOPETRO ENERGY LTD.**INTERIM CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL POSITION**

(Unaudited, thousands of United States dollars)

	Note	June 30, 2016	December 31, 2015
ASSETS			
Current			
Cash and cash equivalents		23,779	28,733
Restricted cash	3	-	2,288
Trade and other receivables		351	247
Prepaid expenditures		238	280
Total current assets		24,368	31,548
Other assets		-	34
Exploration and evaluation assets	4	54,983	48,409
Property, plant and equipment	5	4,944	4,293
Non-current assets		59,927	52,736
Total assets		84,295	84,284
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities			
Accounts payable and accrued liabilities		1,459	2,143
Current portion of decommissioning liabilities	6	85	13
		1,544	2,156
Deferred tax liability		-	330
Decommissioning liabilities		1,304	1,066
		2,848	3,552
Shareholders' equity			
Share capital		151,937	151,937
Contributed surplus		1,512	1,444
Deficit		(54,327)	(47,812)
Accumulated other comprehensive loss		(17,675)	(24,837)
Total shareholders' equity		81,447	80,732
Total liabilities and shareholders' equity		84,295	84,284

Commitments and contingencies (Note 13)

See accompanying notes to these interim condensed consolidated financial statements.

ALVOPETRO ENERGY LTD.
INTERIM CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)

(Unaudited, thousands of United States dollars, except per share amounts)

		Three months ended June 30,		Six months ended June 30,	
	Note	2016	2015	2016	2015
Revenue					
Oil sales		126	150	279	322
Royalties and production taxes		(11)	(6)	(29)	(21)
Oil revenue		115	144	250	301
Other income		28	23	54	54
Total revenue and other income		143	167	304	355
Expenses					
Production	11	360	264	719	512
Transportation		8	5	18	21
General and administrative	11	939	1,231	1,881	2,512
Depletion and depreciation	5	127	101	225	217
Impairment	4	-	-	2,989	-
Exploration and evaluation expenses	4	152	51	152	51
Accretion of decommissioning liabilities	6	7	19	13	38
Share-based compensation		41	90	52	179
Foreign exchange loss (gain)		10	(291)	(29)	(43)
Total expenses		1,644	1,470	6,020	3,487
Loss before taxes		(1,501)	(1,303)	(5,716)	(3,132)
Income tax expense (recovery)		499	(323)	799	(589)
Net loss		(2,000)	(980)	(6,515)	(2,543)
Exchange gain (loss) on translation of foreign operations		3,954	944	7,162	(5,763)
Comprehensive income (loss)		1,954	(36)	647	(8,306)
Net loss per share					
	7				
Basic		(0.02)	(0.01)	(0.08)	(0.03)
Diluted		(0.02)	(0.01)	(0.08)	(0.03)

See accompanying notes to these interim condensed consolidated financial statements.

ALVOPETRO ENERGY LTD.**INTERIM CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY**

(Unaudited, thousands of United States dollars)

	Note	Six months ended June 30,	
		2016	2015
Common Shares			
Balance, beginning of period		151,937	151,937
Net change		-	-
Balance, end of period		151,937	151,937
Contributed surplus			
Balance, beginning of period		1,444	975
Share-based compensation expense	7	52	179
Share-based compensation capitalized	7	16	52
Balance, end of period		1,512	1,206
Deficit			
Balance, beginning of period		(47,812)	(35,388)
Net loss		(6,515)	(2,543)
Balance, end of period		(54,327)	(37,931)
Accumulated Other Comprehensive Loss			
Balance, beginning of period		(24,837)	(9,699)
Other comprehensive income (loss)		7,162	(5,763)
Balance, end of period		(17,675)	(15,462)

See accompanying notes to these interim condensed consolidated financial statements.

ALVOPETRO ENERGY LTD.**INTERIM CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(Unaudited, thousands of United States dollars)

	Three months ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
Operating Activities				
Net loss	(2,000)	(980)	(6,515)	(2,543)
Adjustments for non-cash items:				
Depletion and depreciation	5	127	101	225
Impairment	4	-	-	2,989
Non-cash exploration & evaluation expenses		-	32	-
Accretion of decommissioning liability	6	7	19	13
Share-based compensation	7	41	90	52
Deferred tax		499	(323)	799
Unrealized foreign exchange loss (gain)		32	(291)	1
Settlement of decommissioning liability	6	(15)	-	(98)
		(1,309)	(1,352)	(2,534)
Changes in non-cash working capital	10	(398)	610	(273)
		(1,707)	(742)	(2,807)
Investing Activities				
Expenditures on exploration and evaluation assets	(490)	(6,135)	(3,548)	(7,162)
Expenditures on property, plant and equipment	(345)	(467)	(353)	(729)
Expenditures on other assets	-	-	-	(65)
Change in restricted cash	3	-	3,480	2,288
Changes in non-cash working capital	10	(1,122)	(1,676)	(709)
		(1,957)	(4,798)	(2,322)
Change in cash and cash equivalents	(3,664)	(5,540)	(5,129)	(9,380)
Effect of foreign exchange on cash balances	16	161	175	(261)
Cash and cash equivalents, beginning of period	27,427	36,658	28,733	40,920
Cash and cash equivalents, end of period	23,779	31,279	23,779	31,279
Cash and cash equivalents consist of:				
Cash	5,091	16,000	5,091	16,000
Cash equivalents	18,688	15,279	18,688	15,279
Supplemental information:				
Cash income taxes paid	-	11	-	16
Cash interest income received	25	29	49	40

See accompanying notes to these interim condensed consolidated financial statements.

ALVOPETRO ENERGY LTD.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

As at and for the three and six months ended June 30, 2016

All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted

NOTE 1 – CORPORATE INFORMATION AND BASIS OF PRESENTATION

Alvopetro Energy Ltd. (“Alvopetro” or “the Company”) is engaged in the exploration, development and production of hydrocarbons in Brazil. Alvopetro is a publicly traded company listed on the TSX Venture Exchange (TSX: ALV.V), was incorporated under the Business Corporations Act (Alberta) on September 25, 2013 as 1774501 Alberta Ltd., and subsequently changed its name to Alvopetro Energy Ltd. on November 19, 2013.

The Company’s head office and records are located at 1175, 332 6th Avenue S.W., Calgary, Alberta, Canada, T2P 0B2.

The interim condensed consolidated financial statements as at June 30, 2016 and December 31, 2015 and for the three and six months ended June 30, 2016 and June 30, 2015 have been prepared in accordance with International Financial Reporting Standards (“IFRS”) applicable to the presentation of interim financial statements, including International Accounting Standard (“IAS”) 34 *Interim Financial Reporting*. These interim condensed consolidated financial statements are prepared using the same accounting policies and methods of computation as disclosed in the audited consolidated financial statements as at and for the year ended December 31, 2015, except as discussed in Note 2 below with respect to the adoption of revised accounting standards. These statements do not contain all disclosures required for full annual financial statements and should be read in conjunction with the audited consolidated financial statements as at and for the year ended December 31, 2015.

These interim condensed consolidated financial statements were authorized for issuance by the Company’s Board of Directors on August 23, 2016.

The interim condensed consolidated financial statements are presented in U.S. dollars (“USD”) which is the parent Company’s functional currency.

Segmented Operations

All oil sales revenue is derived entirely from Brazilian operations. All exploration and evaluation assets and all material property, plant and equipment are located in Brazil. Any restricted cash and the majority of the cash and cash equivalents are located in Canada. The Company does not have any income in Canada other than interest earned on cash balances.

NOTE 2 – CHANGES IN ACCOUNTING STANDARDS

New and Revised Accounting Standards

The interim condensed consolidated financial statements have been prepared following the same accounting policies and methods of computation as the 2015 annual consolidated financial statements with the exception of the following standard which was amended effective January 1, 2016.

Standard and Description	Date of Adoption	Adoption Impact on Consolidated Financial Statements
IFRS 11 <i>Joint Arrangements</i> – was amended regarding the accounting for the acquisition of an interest in a joint operation that constitutes a business.	January 1, 2016	The amendment to this standard did not impact these interim condensed consolidated financial statements.

Standards issued but not yet effective

The Company continues to assess the impact of adopting the new and revised accounting pronouncements that have been issued but are not yet effective as described in the 2015 annual consolidated financial statements.

ALVOPETRO ENERGY LTD.**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

As at and for the three and six months ended June 30, 2016

*All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted***NOTE 3 – RESTRICTED CASH AND CREDIT FACILITY**

	As at	
	June 30, 2016	December 31, 2015
Restricted cash – current	-	2,288
Restricted cash – non-current	-	-
Restricted cash - total	-	2,288

The Company has a credit support facility (the “Facility”) with a Canadian bank for up to \$45.0 million Canadian dollars (“CAD”). This Facility allows for the issuance of letters of credit (“LC’s”) and letters of guarantee in support of the financial guarantees required by the National Agency of Petroleum, Natural Gas and Biofuels (the “ANP”) for Alvo Petro’s work commitments under the terms of its concession contracts as discussed further in Note 13. Letters of credit and letters of guarantee issued under the Facility are supported by either cash collateral posted by Alvo Petro or through an Account Performance Security Guarantee from Export Development Canada (“EDC”). EDC supports up to \$15.5 million of Alvo Petro’s LC’s issued under the Facility.

As at June 30, 2016, the total amount of LC’s issued under the Facility was \$15.3 million (December 31, 2015 - \$17.6 million), the full balance of which was satisfied by EDC (December 31, 2015 - \$15.3 million). LC’s supported by restricted cash as at December 31, 2015 were released during the three months ended March 31, 2016 and the Company held no restricted cash as at June 30, 2016.

LC’s supported by EDC at June 30, 2016 include \$1.2 million with respect to Block 170. This work commitment was satisfied with the 170(B1) well which was drilled in the three months ended March 31, 2016. Subsequent to June 30, 2016, the ANP approved this work and released the associated LC.

NOTE 4 – EXPLORATION AND EVALUATION (“E&E”) ASSETS

	As at	
	June 30, 2016	December 31, 2015
Balance, beginning of period	48,409	62,204
Capital expenditures	3,548	11,221
Capitalized share-based compensation	14	95
Transfer from other assets	-	272
Transfer to PP&E	(98)	-
Change in decommissioning liabilities	145	104
Impairment	(2,989)	(11,514)
Foreign currency translation	5,954	(13,973)
Balance, end of period	54,983	48,409

General and administrative costs totaling \$0.4 million (December 31, 2015 - \$1.0 million) that were directly related to exploration and evaluation activities have been capitalized as exploration and evaluation assets.

Impairment

The Company recorded an impairment of \$3.0 million in the three months ended March 31, 2016 with respect to costs incurred on the 170(B1) well which was drilled during the period. No commercial quantities of oil or gas were discovered in the 170(B1) well and, on March 29, 2016, the Company notified the ANP of its intention to relinquish this block. All costs incurred up to December 31, 2015 had been impaired in the 2015 financial statements and the 2016 impairment charge of \$3.0 million reduced the carrying value of the block to \$nil at March 31, 2016 (December 31, 2015 - \$nil). Any costs incurred on this block subsequent to March 31, 2016 have been recorded in exploration and evaluation expenditures and included in net loss.

ALVOPETRO ENERGY LTD.**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

As at and for the three and six months ended June 30, 2016

*All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted***NOTE 5 – PROPERTY, PLANT AND EQUIPMENT (“PP&E”)**

	As at	
	June 30, 2016	December 31, 2015
Cost, beginning of period	8,696	10,717
Capital expenditures	353	886
Transferred from other assets	-	6
Transferred from E&E	98	-
Capitalized share-based compensation	2	7
Change in decommissioning liabilities	-	(1,043)
Foreign currency translation	2,042	(1,877)
Cost, end of period	11,191	8,696
Accumulated depletion, depreciation and impairment, beginning of period	(4,403)	(3,228)
Depletion and depreciation for the period	(225)	(429)
Impairment	-	(1,524)
Foreign currency translation	(1,619)	778
Accumulated depletion, depreciation and impairment, end of period	(6,247)	(4,403)
Net book value, end of period	4,944	4,293

General and administrative costs that were directly related to property, plant, and equipment activities have been capitalized.

NOTE 6 – DECOMMISSIONING LIABILITIES

The decommissioning liabilities were estimated based on the net ownership interest of wells and facilities and management’s estimates of costs to abandon and reclaim those wells and facilities, and the potential future timing of the costs to be incurred.

	As at	
	June 30, 2016	December 31, 2015
Balance, beginning of period	1,079	3,454
Liabilities incurred	145	113
Revisions to obligations	-	(1,052)
Obligations settled	(98)	-
Disposition	-	(363)
Accretion	13	72
Foreign currency translation	250	(1,145)
Balance, end of period	1,389	1,079

Total undiscounted cash flows, escalated at 6.5% (December 31, 2015 - 6.5%) for inflation, required to settle the Company’s decommissioning provision are estimated to be \$2.3 million (December 31, 2015 - \$1.9 million) and have been discounted using an average risk free rate of 2.2% (December 31, 2015 – 2.5%), which represents an estimated U.S. Treasury bill rate for a period of 20 years, the weighted-average remaining years to abandonment.

Of the total \$1.4 million in decommissioning liabilities as at June 30, 2016, \$0.09 million relates to costs expected to be incurred within one year and accordingly, is classified as current at June 30, 2016 (December 31, 2015 – \$0.01 million).

ALVOPETRO ENERGY LTD.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

As at and for the three and six months ended June 30, 2016

All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted

NOTE 7 – SHARE CAPITAL

a) Authorized

Alvopetro has an unlimited number of common shares authorized for issuance. The Company is also authorized to issue preferred shares in one or more series.

b) Issued and Outstanding Common Shares

	Number of Shares	Amount (\$000s)
Balance as at June 30, 2016 and December 31, 2015	85,166,871	\$ 151,937

c) Options to Purchase Common Shares

Alvopetro has a stock option plan whereby the Company may grant stock options to its directors, officers, employees and consultants. The plan allows for the issuance of up to ten percent of the outstanding common shares of the Company. The exercise price of each option is not less than the volume weighted five-day average price of the Company's common shares on the TSX Venture Exchange prior to the date of grant. Stock option terms are determined by the Company's Board of Directors but typically, options granted vest over a period of three years from the date of grant and expire five years from the date of grant. The options outstanding at June 30, 2016 are as follows:

	Number of Options	Weighted Average Exercise Price (CAD\$)
Balance as at December 31, 2014	4,567,436	0.82
Granted	2,303,500	0.34
Expired	(10,000)	1.02
Forfeited	(17,500)	0.75
Balance as at December 31, 2015	6,843,436	0.66
Granted	883,000	0.29
Expired	(797,498)	0.83
Forfeited	(747,502)	0.42
Balance as at June 30, 2016	6,181,436	0.62

Options Outstanding at June 30, 2016				Options Exercisable at June 30, 2016		
Exercise Price	Number of Options	Weighted Average Exercise Price (CAD\$)	Weighted Average Remaining Contractual Life (years)	Number of Options	Weighted Average Exercise Price (CAD\$)	Weighted Average Remaining Contractual Life (years)
CAD\$0.28 - \$0.50	3,714,000	0.35	4.04	1,006,329	0.43	3.60
CAD\$0.51 - \$1.00	40,000	0.57	3.31	20,000	0.57	3.31
CAD\$1.01 - \$1.24	2,427,436	1.03	2.48	2,012,841	1.02	2.48
CAD\$0.28 - \$1.24	6,181,436	0.62	3.43	3,039,170	0.82	2.86

ALVOPETRO ENERGY LTD.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

As at and for the three and six months ended June 30, 2016

All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted

d) Share-Based Compensation

The fair value of the stock options granted under the Alvopectro stock option plan for the three and six months ended June 30, 2016 and June 30, 2015 has been estimated on the grant date using the Black-Scholes option pricing model. Weighted average assumptions and resultant fair values for stock options granted are as follows:

	Three months ended		Six months ended	
	June 30,		June 30,	
	2016	2015	2016	2015
Risk free interest rate (%)	0.67	0.76	0.45	0.48
Expected term (years)	4.0	4.0	2.1	2.2
Expected volatility (%)	47.0	50.0	49.8	50.0
Dividend per share (%)	-	-	-	-
Forfeiture rate (%)	5.0	5.0	5.0	5.0
Weighted average fair value (CAD\$)	0.11	0.19	0.10	0.13

Total share-based compensation of \$0.05 million and \$0.07 million, respectively was computed for the three and six months ended June 30, 2016 (June 30, 2015 – \$0.1 million and \$0.2 million) related to the Alvopectro stock option plan. Share based compensation that was directly related to exploration and evaluation assets and property, plant and equipment has been capitalized with the remainder recognized as share-based compensation expense on the consolidated statements of operations and comprehensive income (loss).

e) Net Loss Per Share Attributable to Common Shareholders

Net loss per share is calculated by dividing net loss by the weighted average number of common shares outstanding during the applicable period. The following table provides the number of shares used in the basic and diluted per share computations:

	Three and six months ended	
	June 30,	
	2016	2015
Weighted average common shares outstanding, basic and diluted	85,166,871	85,166,871

In determination of the weighted average number of diluted common shares outstanding for the three and six months ended June 30, 2016 and 2015, all stock options were excluded because the effect would be anti-dilutive.

NOTE 8 – CAPITAL MANAGEMENT

The Company's capital consists of the following:

	As at	
	June 30, 2016	December 31, 2015
Working capital, including current restricted cash	22,909	29,405
Shareholders' equity	81,447	80,732

Alvopectro manages its capital to support the Company's strategic growth objectives and maintain financial capacity and flexibility for the purpose of funding the Company's exploration and development activities.

ALVOPETRO ENERGY LTD.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

As at and for the three and six months ended June 30, 2016

All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted

The Company considers its capital structure to include working capital (including current restricted cash), non-current restricted cash, and shareholders' equity. At June 30, 2016, the Company's net working capital surplus of \$22.9 million (December 31, 2015 - \$29.4 million), included \$23.8 million (December 31, 2015 - \$28.7 million) of cash and \$nil (December 31, 2015 - \$2.3 million) current restricted cash.

As at June 30, 2016, the Company held no current or non-current restricted cash. The Company's restricted cash of \$2.3 million at December 31, 2015 was released on March 31, 2016.

The Company has performance security guarantees with EDC which support up to \$15.5 million of LC's provided in respect of work commitments in Brazil. As at June 30, 2016 and December 31, 2015, a total of \$15.3 million of LC's were satisfied by EDC and the Company had \$0.2 million in available capacity for new LC's. Additional capacity may become available as work commitments are met and the related LC's are released.

Alvopetro has the ability to adjust its capital structure by issuing new equity or debt and making adjustments to its capital expenditure program, other than with respect to work commitments. The Company considers its capital structure at this time to include shareholders' equity of \$81.4 million (December 31, 2015 - \$80.7 million). In the event that adjustments to the capital structure are necessary, the Company may consider issuing additional equity, raising debt or revising its capital investment programs.

The Company has not paid or declared any dividends since the date of incorporation.

NOTE 9 – FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT

The Company's financial instruments consist of cash and cash equivalents, restricted cash when applicable, trade and other receivables and accounts payable and accrued liabilities. The nature of Alvopetro's operations exposes the Company to credit risk, liquidity risk, and market risk. Alvopetro's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and to monitor market conditions and the Company's activities. The Board of Directors has overall responsibility for establishment and oversight of the Company's risk management policies.

Fair Value of Financial Instruments

The Company classifies the fair value of financial instruments according to the following hierarchy based on the amount of observable inputs used to value the instrument:

Level 1 – Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions occur in sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2 – Pricing inputs are other than quoted prices in active markets included in Level 1. Prices in Level 2 are either directly or indirectly observable as of the reporting date. Level 2 valuations are based on inputs, including quoted forward prices for commodities, time value and volatility factors, which can be substantially observed or corroborated in the marketplace.

Level 3 – Valuations in this level are those with inputs for the asset or liability that are not based on observable market data.

Assessment of the significance of a particular input to the fair value measurement requires judgment that may affect the placement within the fair value hierarchy level. Due to the short-term nature of accounts receivable and accounts payable and accrued liabilities, their carrying value approximates their fair value. The carrying values and respective fair values of Alvopetro's financial instruments at June 30, 2016 and December 31, 2015 is set forth in the table below. The Company does not currently have any financial instruments classified as Level 2 or Level 3.

ALVOPETRO ENERGY LTD.**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

As at and for the three and six months ended June 30, 2016

All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted

	As at			
	June 30, 2016		December 31, 2015	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Carried at fair value through profit or loss				
Cash and cash equivalents ⁽¹⁾	23,779	23,779	28,733	28,733
Restricted cash – current ⁽¹⁾⁽²⁾	-	-	2,288	2,288
	23,779	23,779	31,021	31,021
Carried at cost or amortized cost				
Trade and other receivables	351	351	247	247
Accounts payable and accrued liabilities	(1,459)	(1,459)	(2,143)	(2,143)
	(1,108)	(1,108)	(1,896)	(1,896)

(1) Level 1

(2) Restricted cash balances include amounts pledged as collateral for work commitments (Note 3).

Risks Associated with Financial Assets and Liabilities

The nature of AlvoPetro's operations exposes the Company to credit risk, foreign currency risk, commodity price risk, interest rate risk, and liquidity risk. The Company has several practices and policies in place to help mitigate these risks. A description of the nature and extent of risks arising from the Company's financial instruments can be found in the notes to the audited consolidated financial statements for the year ended December 31, 2015 and there has been no significant change to the Company's exposure to these risks.

The following financial instruments were denominated in currencies other than U.S. dollars as at June 30, 2016:

	As at			
	June 30, 2016		December 31, 2015	
	CAD (000's)	BRL (000's)	CAD (000's)	BRL (000's)
Cash and cash equivalents	161	566	197	1,482
Trade and other receivables	13	1,096	10	933
Accounts payable and accrued liabilities	(94)	(3,798)	(54)	(7,315)
Net exposure in foreign currency	80	(2,136)	153	(4,900)
Net exposure in USD (\$000s)	62	(665)	111	(1,255)

The Company had no forward exchange rate contracts in place as at or during the periods ended June 30, 2016 or December 31, 2015.

ALVOPETRO ENERGY LTD.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

As at and for the three and six months ended June 30, 2016

All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted

NOTE 10 – CHANGES IN NON-CASH WORKING CAPITAL

Change in:	Three months ended		Six months ended	
	June 30, 2016	2015	June 30, 2016	2015
Trade and other receivables	9	3	(42)	(10)
Prepaid expenditures	70	(3)	107	(6)
Accounts payable and accrued liabilities	(1,599)	(1,066)	(1,047)	(2,179)
	(1,520)	(1,066)	(982)	(2,195)
Changes relating to:				
Operating activities	(398)	610	(273)	85
Investing activities	(1,122)	(1,676)	(709)	(2,280)
	(1,520)	(1,066)	(982)	(2,195)

NOTE 11 – NATURE OF EXPENSES

Production expenses by nature were as follows:

Production expenses:	Three months ended		Six months ended	
	June 30, 2016	2015	June 30, 2016	2015
Personnel	114	127	207	263
Production facilities rental	138	-	277	-
Other fixed	63	42	130	86
Variable	45	95	105	162
Workover	-	-	-	1
Total production expenses	360	264	719	512

The majority of the Company's production expenses relate to personnel costs and production facilities rental costs for the 182(B1) well which was brought on production late in 2015. This rental contract was cancelled during the three months ended June 30, 2016.

General and administrative expenses ("G&A") by nature were as follows:

G&A expenses:	Three months ended		Six months ended	
	June 30, 2016	2015	June 30, 2016	2015
Personnel	737	989	1,491	1,909
Travel	29	146	83	259
Office and IT	130	159	245	321
Professional fees	151	191	283	378
General corporate	123	168	283	331
Gross G&A expenses	1,170	1,653	2,385	3,198
Capitalized to E&E and PP&E	(231)	(422)	(504)	(686)
Net G&A expenses	939	1,231	1,881	2,512

The majority of the Company's G&A relates to personnel costs. General corporate expenses include public company costs, corporate insurance, directors' fees, rental vehicle costs, cell phones and other miscellaneous expenses. G&A expenses that are directly attributable to exploration and development projects are capitalized. The majority of capitalized costs relate to personnel.

ALVOPETRO ENERGY LTD.**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

As at and for the three and six months ended June 30, 2016

*All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted***NOTE 12 – RELATED PARTY TRANSACTIONS**

Alvopetro is party to non-material office-related administrative transactions with Touchstone Exploration Inc. (“Touchstone”), a related party of the Company due to common directors, summarized as follows:

	Three months ended		Six months ended	
	June 30,		June 30,	
	2016	2015	2016	2015
Office rent and related costs	24	51	47	101

As at June 30, 2016 and December 31, 2015 the amount owed by the Company to Touchstone was \$nil.

NOTE 13 – COMMITMENTS AND CONTINGENCIES

The following is a summary of contractual commitments as at June 30, 2016:

Commitments	< 1 Year	1-3 Years	Thereafter	Total
Minimum work commitments ⁽¹⁾				
Block 183	1,039	-	-	1,039
Block 170 ⁽²⁾	935	-	-	935
Block 106	355	-	-	355
Block 107	2,368	-	-	2,368
Block 177	2,240	-	-	2,240
Block 169	1,184	-	-	1,184
Block 198	1,184	-	-	1,184
Block 255	1,417	-	-	1,417
Block 256	315	-	-	315
Block 57 ⁽³⁾	-	276	-	276
Block 62 ⁽³⁾	-	276	-	276
Block 71 ⁽³⁾	-	189	-	189
Block 145 ⁽³⁾	-	276	-	276
Bom Lugar	-	-	109	109
Jiribatuba	-	-	109	109
Total minimum work commitments	11,037	1,017	218	12,272
Office leases ⁽⁴⁾	159	134	-	293
Total commitments	11,196	1,151	218	12,565

Notes:

- (1) Under the terms of the ANP concession contracts for each of our exploration blocks, the Company has commitments which must be completed prior to the applicable phase expiry date. The Company is required to post a performance guarantee with the ANP for all commitments in the table above.
- (2) During the three months ended March 31, 2016, the Company completed drilling the 170(B1) well on Block 170 and the Company relinquished this block. Subsequent to June 30, 2016, the ANP approved the work performed in satisfaction of the above work commitment and released the associated LC.
- (3) Alvopetro holds a 65% interest in each of these blocks and the amounts provided in the table above represent Alvopetro’s share of the related commitments.
- (4) The Company is committed to future minimum payments for office space in Canada and Brazil. In Brazil, the Company is required to provide a guarantee for certain office rental payments.

As is customary in the oil and gas industry, we may at times have work plans in place to reserve or earn certain acreage positions or wells. If we do not complete such work plans in a timely manner, the acreage positions or wells may be lost, or penalties may be applied.

ALVOPETRO ENERGY LTD.**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

As at and for the three and six months ended June 30, 2016

All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted

The Company currently has no contingent liabilities recorded; however, in the normal course of operations, we may have disputes with industry participants for which we currently cannot determine the ultimate results. The Company has a policy to record contingent liabilities as they become determinable and the probability of loss is more likely than not.

Alvopetro's activities in Brazil are subject to minimum local content requirements with respect to materials and supplies utilized. The specific local content requirements for the exploration phase were determined during the bidding process for each particular block and are assessed at the phase expiry date. Management undertakes considerable effort to adhere to these requirements; however, there may be circumstances when it is not advantageous, cost-effective or reasonably possible for the Company to do so. If the Company does not meet the local content requirements for a particular phase as specified according to the respective concession contract, a fine, which varies by concession depending on exploration phase and type of cost, will be incurred. The Company is continually monitoring its local content compliance and actual or potential fines and, as of June 30, 2016, the potential estimated fine was \$0.1 million (December 31, 2015 - \$0.1 million), which is included in accounts payable and accrued liabilities in the respective consolidated statements of financial position.