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# Discovery



DISCOVERY WEST CORP.

ANNUAL REPORT 1987

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## **CORPORATE PROFILE**

*Discovery West Corp. is a Canadian independent oil and gas company with offices in Toronto, Ontario and Calgary, Alberta. The Company was formed on March 1, 1987 through the merger of Discovery Mines Limited, Midcon Oil & Gas Limited and Yellowknife Bear Resources Inc.*

*Discovery's petroleum exploration and development program in Alberta concentrates on medium to large reserve prospects with acceptable risk levels. In addition, the Company will be exploiting a high potential heavy oil property containing 700 million barrels of oil in place at Cold Lake, Alberta. Discovery West has recently acquired a 65% working interest in this property from Rayrock Yellowknife Resources Inc. On completion of a pilot steam flood project scheduled for 1989, Discovery and Norcen Energy Resources will each have a 50% interest in this property.*

*Discovery West Corp. also holds the voting control block of Rayrock Yellowknife Resources Inc. In a transaction to be approved by shareholders, Discovery's equity interest in Rayrock will increase to 23%. This holding will consist of 2,637,560 Subordinate Voting shares. In addition, Discovery owns 550,000 preferred shares of Rayrock, each carrying six votes. Rayrock is a rapidly growing gold mining and minerals producing company with activities throughout North and South America.*

*As at December 31, 1987, there were 19,421,312 common and non voting shares of Discovery West Corp. outstanding. These shares are listed for trading on The Toronto Stock Exchange under the symbol DSW and DSW.A, respectively.*





- March 1, 1987, formation of Discovery West Corp.
- Establishment of a full time management team in Calgary with a mandate to maintain future Company growth through participation in high quality exploration programs and the acquisition of producing properties.
- Sale of \$8,000,000, 8% Convertible Subordinated Debentures with proceeds used to purchase \$4,970,000 of Rayrock 7.5% Convertible Subordinated Debentures and the balance added to the Company's cash reserve.
- 1987 production of 203,000 working interest Bbls of crude oil (556 Bbls per day) and 933,000 working interest Mcf of gas (2,560 Mcf per day).
- Working Interest Reserves (Before Royalties) December 31, 1987

*Crude Oil & Natural Gas Liquids (Mbbbls)*

<i>Proven</i>	2,788.3
<i>Probable</i>	<u>323.6</u>
<i>Total</i>	<u>3,111.9</u>

*Natural Gas (Mmcf)*

<i>Proven</i>	12,246.4
<i>Probable</i>	<u>570.0</u>
<i>Total</i>	<u>12,816.4</u>

*Value of Oil and Gas Reserves (December 31, 1987)*

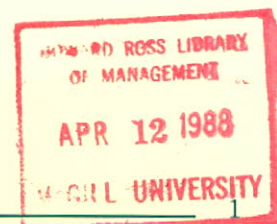
*Discounted @ 15% before Tax*

<i>Proven</i>	\$32,872,000
<i>Probable</i>	<u>3,153,000</u>
<i>Total</i>	<u>\$36,025,000</u>

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To Our Shareholders:

Discovery West Corp. is now a fully independent oil and gas company with operating management located in Calgary. In addition to developing its extensive oil and gas properties, the Company is generating its own exploration prospects and acquiring land in several areas of Alberta selected for their high potential.

Subsequent to the end of 1987, Discovery entered into formal agreements to acquire additional Subordinate Voting shares of Rayrock Yellowknife Resources Inc., completing the planned rationalization between the companies. As a result, Discovery will increase its equity interest in Rayrock from 14% to 23% and Discovery will now equity account for Rayrock. This is expected to have a significant positive effect on Discovery's future financial results.

The Company has acquired all of Rayrock's 65% interest in Cold Lake Oil Sands Lease No. 80 and will be participating with its partner, Norcen Energy Resources, in constructing a huff and puff steam pilot plant on the property. Discovery is the only junior company with a major position in the heart of the high quality Cold Lake Oil Sands development.

The market value of Discovery's investment in Rayrock is \$0.85 per Discovery share and the discounted value of Discovery's oil and gas reserves (explained in detail on page 5 of the report) is \$1.85 per Discovery share as at December 31, 1987.

#### **Exploration and Operations Capability**

Discovery West has a new Calgary based management group that is committed to growth. Mr. O. Mike Isaac has joined Discovery West as Executive Vice-President responsible for oil and gas. Mr. Isaac has also been nominated for election as a Director of your Company.

Discovery's senior management have many years of experience in finding and developing oil and gas reserves. The Company has a solid asset base with interests in high quality, long life, income producing properties. The Company's policy is to reinvest the cash flow from these properties in new oil and gas projects in order to build up reserves.

Western Canada is considered one of the most favourable areas in the world for oil industry growth and investment. In 1988, Discovery West will be conducting a

\$4,200,000 capital program for conventional oil and gas exploration and development projects in Alberta.

#### **Cold Lake Oil Sands Lease No. 80**

Discovery agreed to acquire all of Rayrock's 65% interest in this lease adjoining Esso Resources' leases to the northwest. Esso has developed a large scale operation at Cold Lake, now producing about 95,000 barrels per day of heavy oil. Oil Sands Lease No. 80 contains a high quality reservoir with about 700 million barrels of oil in place. Permit applications have been filed and engineering work is underway on a 700 barrel per day steam flood pilot plant. Norcen Energy Resources, Discovery's partner, has a 35% interest and may increase its interest to 50% by paying for 65% of the \$15,000,000 estimated cost for a pilot huff and puff steam plant.

On completion of the pilot plant construction program, each party will own a 50% interest in the project. When a pattern of higher average oil prices is established, this project will become economically attractive for commercial scale development and is expected to become a major source of growth and revenue for the Company.

Discovery's share of the cost to participate in the pilot plant construction is expected to be approximately \$5,000,000 or 25 cents per share.

#### **Rayrock Yellowknife Resources Inc.**

Rayrock and Discovery West are associated companies. Discovery West holds the voting control block of Rayrock. During 1987, a rationalization of the two companies' assets was undertaken. The purpose was to clearly define Rayrock as the mining company and Discovery West as the oil and gas company. These transactions were completed with the agreement early in 1988 to transfer Discovery's mining property interests to Rayrock in exchange for treasury shares. In turn, Rayrock sold its Cold Lake and Seal area heavy oil properties to Discovery for cash. In addition, Discovery will purchase, by means of a private placement, 518,807 Subordinate Voting shares of Rayrock. As a result of all of these transactions, Discovery will own 23% of the equity of Rayrock. The private placement, notice of which has been accepted for filing by The Toronto Stock Exchange, is subject to



confirmation by the Rayrock shareholders at the next Annual Meeting.

Rayrock has established itself as a highly successful mineral exploration and development company concentrating on the precious metals business. Rayrock currently operates three gold mines in Nevada as well as a profitable long-term langbeinite (specialty fertilizer mineral) mine in Carlsbad, New Mexico. Rayrock has ongoing exploration programs in Canada, the United States, Costa Rica, Chile and Ecuador.

Rayrock's gold reserves have increased significantly during 1987 and gold production is expected to increase at least 30% when the new Marigold mine begins operation in 1989. Rayrock has a strong financial position and has additional projects that are expected to contribute to future growth. Net earnings in 1987 were \$6,922,000 (\$.69 per share).

#### **Financial**

Discovery earned \$906,000 or \$.04 per share in 1987, compared to a loss of \$2,048,000 or \$.11 per share the prior year. The loss resulted from unusual charges of \$2,785,000 relating to the write down of certain mineral and oil and gas properties in 1986. Revenues were \$7,072,000 on the sale of 203,000 Bbls of oil at an average price of \$23.91 per Bbl and 933,000 Mcf of natural gas at an average price of \$1.64 per Mcf in 1987.

Cash flow from operations provided \$4,003,000 or \$.18 per share in 1987 compared to \$2,692,000 or \$.12 per share in 1986. These funds, together with the proceeds of an \$8,000,000, 8% Convertible Subordinated Debenture issue, maturing in 1997, were used to invest approximately \$2,064,000 in oil and gas properties and to increase the Companies' long term investments by \$4,970,000. Cash and short term deposits increased by \$3,726,000 during 1987. Each \$100 debenture is convertible into 50 common shares of the Company.

As a result of the completion of the corporate rationalization program undertaken with Rayrock, Discovery West has emerged as the oil and gas operating entity for the Rayrock-Discovery Group of companies. Discovery will also benefit from its significant investment in Rayrock, indirectly participating in that company's future growth and earnings. Discovery believes it has an excellent financial

base upon which its future expansion in oil and gas can be undertaken.

We would like to thank the staff of both Discovery West and Rayrock as well as the Board of Directors of the Company for their hard work, support and guidance during 1987 when Discovery West Corp. was being established as a new entity. We would also like to thank our shareholders for their continued interest in the Company.

On behalf of the Board of Directors,



M. A. Upham  
Chairman of the Board



D. R. Crombie  
President and  
Chief Executive Officer





As 1987 was a transition year in the Company's operations, emphasis shifted from the previous policy of participating for small working interests in programs and joint ventures initiated by other operators.

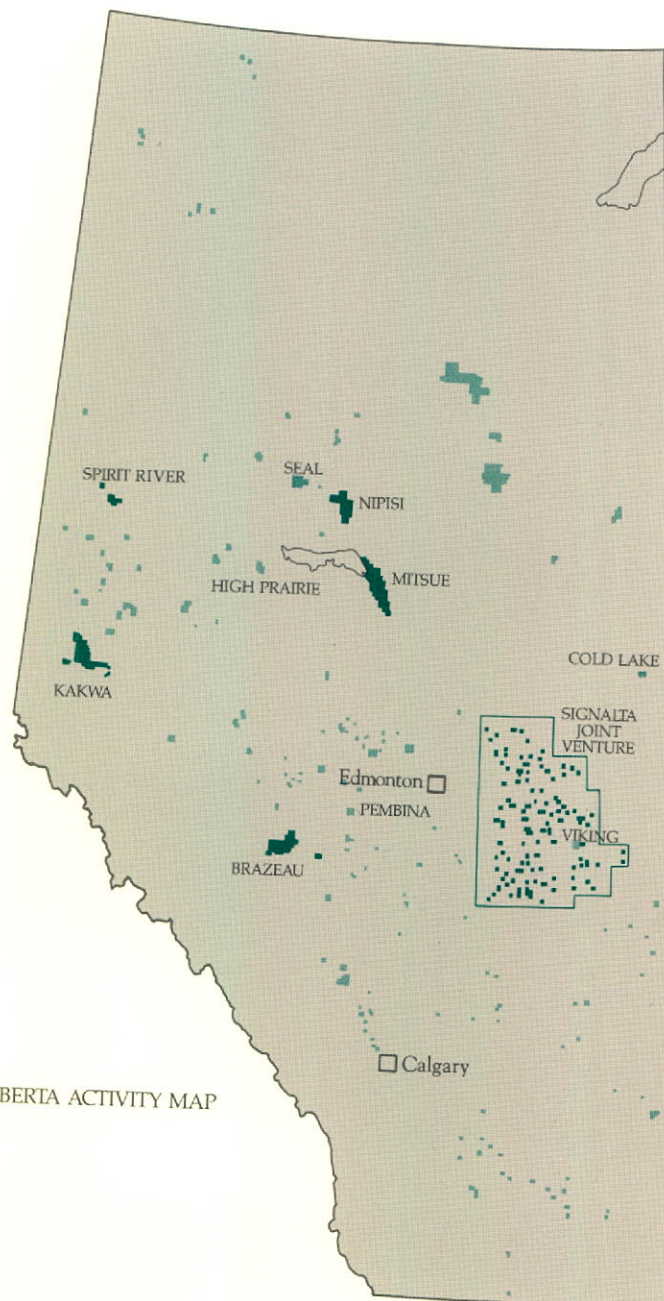
With the addition of staff and a data base in Calgary, the Company is now able to generate prospects internally and in late 1987 participated with larger working interests in several wells and a number of land acquisitions. The Company will be pursuing this policy of greater participation in all future programs.

Although the Company is no longer participating in new joint ventures, the large inventory of smaller positions continues to be important. Each year a large number of wells are drilled to further explore and develop this acreage and in 1987 several significant discoveries were made. It is expected that the Company's participation in new wells on these joint venture lands will continue for a number of years until the existing lands have been drilled up or the leases have expired. In 1988, approximately 30% of the Company's capital budget will be devoted to further activity on these lands with the remaining 70% being devoted to new ventures with larger participation interests.

Company oil and gas related exploration and development expenditures totalled \$2,064,000 in 1987 and the budget for 1988 is \$4,200,000.

**Land:**

Discovery West Corp. holds a widespread acreage position in Alberta with minor land holdings in British Columbia. Due to reporting variances by some joint venture operators, it is difficult to calculate the exact ratio of producing to non-producing acreage. The Company estimates that it holds 24,900 net non-producing acres in Alberta out of a total net acreage position of 36,300 acres. In total, Discovery West holds interests in 904,000 gross acres in Alberta. In British Columbia, Discovery West holds 66 net acres (4,811 gross acres) of non-producing lands. Under its philosophy of acquiring larger interests in new exploratory plays the Company, during 1987, acquired interests varying from 12.5% to 50% in 3,400 net acres (8,820 gross acres) situated in eight different prospect areas. Capital expenditures on land in 1987 totalled \$450,000. The value of the Company's land holdings is not included in the value of the Company's oil and gas reserves.



ALBERTA ACTIVITY MAP



	Net Undeveloped Acres	Total Net Acres	Total Gross Acres
Alberta . . . . .	24,900	36,300	904,000
British Columbia . . . . .	66	212	7,240
Total . . . . .	<u>24,966</u>	<u>36,512</u>	<u>911,240</u>

### Drilling Activity:

Discovery West participated in the drilling of 110 gross wells in 1987 with results as follows:

Gas Wells . . . . .	12
Oil Wells . . . . .	63
Injectors . . . . .	7
Unsuccessful Wells . . . . .	28

The most significant of these was an active drilling program in the Kakwa-Chicken area of Western Alberta, where the Company participated for a 2.5% interest in 15 wells in 1987 resulting in 14 oil wells and 1 dry hole.

### Production:

Production in 1987 totalled 203,000 working interest Bbls oil (556 working interest Bbls/d) and 933,000 working interest Mcf gas (2,560 Mcf/d). Year end production of oil was 654 Bbls/d while gas production was 3,469 Mcf/d.

Oil production is expected to show substantial gains in 1988 due to development and infill drilling on existing properties and follow-up to new discoveries. Natural gas production is expected to increase modestly as volumes taken under the Company's long term TransCanada gas contracts continue to improve.

The average price realized for the Company's oil production in 1987 was \$23.91 per Bbl while Company gas prices averaged \$1.64 per Mcf.

### Reserves:

The Company changed its reporting policies in 1987 to be consistent with other operators in reporting total working interest reserves of crude oil and natural gas before royalties. In 1987, 95% of Alberta Crown royalties paid were returned to the Company through the Alberta Royal Tax Credit program. In 1988, 75% of Alberta Crown royalties will be rebated. It is believed that since most of the Company's reserves are on Crown land, consideration of working interest reserves before royalties is a more accurate reflection

of the Company's success and progress.

Total working interest reserves of crude oil and natural gas liquids were 3,111.9 Mbbls at year end 1987. Of this total, 90% or 2,788.3 Mbbls are classified as proven reserves. Total working interest natural gas reserves at year end 1987 are 12,816.4 Mmcf. Of this total, 96% or 12,246.4 Mmcf are classified as proven.

The present value of Discovery West's total reserves after consideration of all operating costs, royalties and royalty rebates is \$36,025,000 discounted at 15%.

Proven reserves have a present value, discounted at 15%, of \$32,872,000.

It should be noted that much of the Company's production, particularly of oil, is located in areas that have been unitized. These areas are well understood, generally have an extensive production history and, therefore, an accurate estimate of remaining reserves can be forecast.

The following table was derived from a report by Martin Petroleum & Associates as at January 1, 1988. The report indicates Discovery West's working interest oil and gas reserves and estimated net values of future cash flows based on current pricing forecasts.

### Company Reserves Oil & NGL (Mbbls):

Proven Producing	2,467.0
Proven Non-Producing	321.3
Probable	323.6
Total	<u>3,111.9</u>

### Company Reserves of Gas (Mmcf):

Proven Producing	11,810.5
Proven Non-Producing	435.9
Probable	570.0
Total	<u>12,816.4</u>

### Discounted Value of Reserves<sup>(1)(2)(3)</sup>:

	10%	15%	20%
Proven Producing	\$40,688,500	\$31,318,900	\$25,411,600
Proven Non-Producing	2,615,000	1,553,400	896,700
Probable	4,007,300	3,152,700	2,560,100
Total	<u>\$47,310,800</u>	<u>\$36,025,000</u>	<u>\$28,868,400</u>

(1) Does not consider General and Administrative expenses or Corporate Income Taxes.

(2) After allowing for Alberta Royalty Tax Credits.

(3) For pricing forecast, see table under "Shareholder Information", page 24.





**1988 Program:**

Discovery West Corp. proposes to spend approximately \$4,200,000 in 1988 on conventional oil and gas programs in Alberta. Of this total approximately \$1,200,000 is dedicated to continuing activity on existing projects at Kakwa, Mitsue and Nipisi and through further drilling by Allaro and Signalta. The remaining \$3,000,000 will be spent on land, seismic and drilling on new exploration prospects in Alberta.

In addition to its conventional oil and gas activities, in January 1988 Discovery West acquired interests in two enhanced recovery heavy oil properties at Cold Lake and Seal from Rayrock Yellowknife Resources Inc. These projects, particularly Cold Lake, are anticipated to require significant funding in late 1988 and 1989, subject to possible regulatory delays. It is estimated that Discov-

ery West will spend \$5,000,000 by mid-1989 in developing Cold Lake.

**Kakwa Area:**

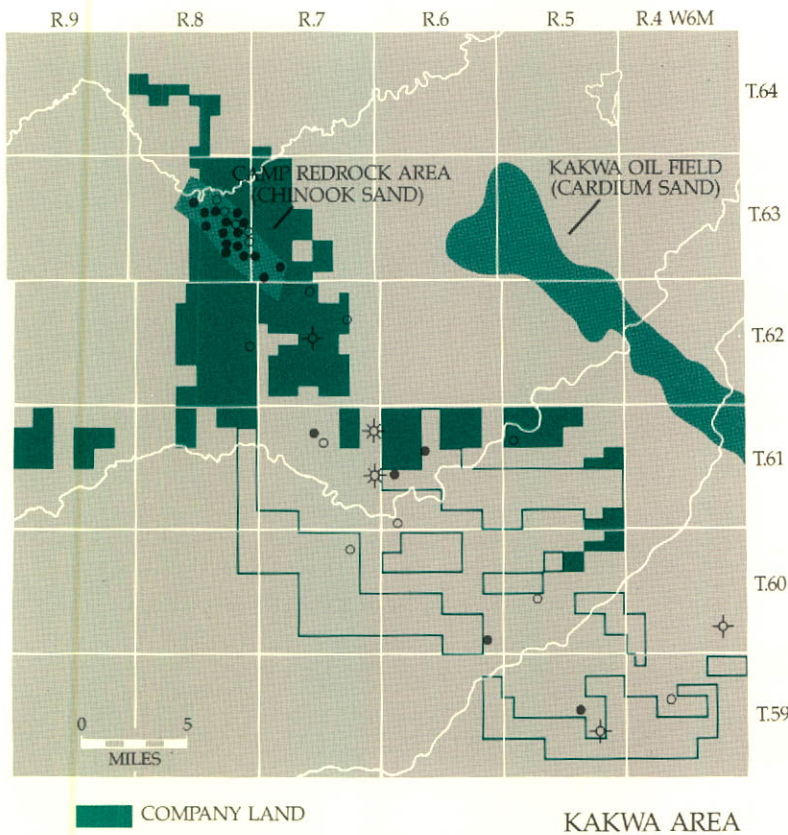
The Company holds interests varying from 2.5% to 5.0% in 76,480 acres in the deep basin area of Western Alberta. During late 1986 and in 1987, the Company participated in drilling 15 wells on these lands resulting in 14 oil wells and 1 dry hole. Production is from the Upper Cretaceous Chinook formation and this is the first significant oil production recorded from that unit. An extensive accumulation of oil has been defined and an active development drilling program is planned in 1988.

The Chinook formation is thought to most resemble the Cardium formation in its depositional history and is now thought to have the potential to contain major hydrocarbon reserves in this general area. Although limited production history is available, with moderate drilling depths (approximately 5,000 feet) and favorable producing characteristics, the Chinook is a significant new objective. As an indication of the interest generated by this new discovery, competitors paid in excess of \$28,000,000 acquiring leases and licences in a 6 township area adjoining the Discovery West acreage during July and August 1987. A number of wildcat wells have been drilled or are now drilling on this trend.

In addition to developing existing proven reserves, Discovery West will be participating in several wildcat wells designed to test the potential of the Chinook Zone as well as other potentially productive zones on this large land spread in 1988.

**Mitsue:**

This large Gilwood sand unit is one of Discovery West's major producing areas. In 1987, the Company's share of working interest production averaged 208 Bopd. Approximately 50% of this unit is currently under tertiary hydrocarbon miscible flood. The remaining 50% is under waterflood. Recent favorable response to miscible injection combined with results from a \$27,000,000 capital drilling program planned for the waterflood portion of the unit are expected to significantly increase 1988 production. Discovery West's



- COMPANY LAND
- COMPETITION LAND PURCHASES AT CROWN SALES JULY-AUGUST 1987 \$28 MILLION
- CURRENT DRILLING 1987-1988
  - OILWELL
  - ⊛ GASWELL
  - ⊙ DRY & ABANDONED
  - LOCATION



interest in this unit is 0.973735% before payout and 0.945856% after payout.

**Nipisi:**

Discovery West's working interest share of production from the Nipisi Gilwood No. 1 Unit averaged 241 Bopd in 1987. For several years a tertiary hydrocarbon miscible flood project has been operating in portions of this large unit. Results of this project have been encouraging and in 1987 the Energy Resources Conservation Board of Alberta granted approval for Stage III expansion of this project, estimated to cost \$43,000,000. Sixty percent of this work had been completed at year end 1987.

Discovery West Corp. has a 0.91627% interest before payout and a 0.87046% interest after payout in this unit.

**Spirit River:**

Discovery West has a 0.95209% interest in the Spirit River Triassic Unit No. 1 placed on waterflood production during 1986. With the completion of gas conservation facilities, the unit reached its maximum current productive capacity of approximately 4,500 Bopd in 1987. Discovery West's share of oil production was 43 Bopd at year end. This unit produces from the Triassic Halfway Formation that has excellent producing characteristics and contains high quality, long life reserves.

**Allaro Joint Venture:**

The Company participated for a number of years in a joint venture program operated by Allaro Resources Ltd. Through this joint venture the Company now has 9,240 net acres representing varying interests in a large number of properties in Alberta. Production from these properties averaged 32 Bopd and 96 Mcf/d net to Discovery in 1987. During 1987 several discoveries were made on these lands. At High Prairie, Discovery West participated for a net 1.31% interest in six new Gilwood oil wells. At Pembina the Company has a 3.3% interest in five Nordegg oil wells.

Although Discovery West will not be participating in new projects to be undertaken by this joint venture, the Company will be participating in 13 wells currently planned for existing lands in 1988.

**Signalta:**

Discovery participated for several years in a joint venture managed by Signalta Resources Limited and through this venture acquired interests in a large number of gas wells, some oil wells and associated acreage primarily located in East Central Alberta. Gas sales from this area are arranged with TransCanada Pipelines Ltd., through a contract known as the Birch-Wavy Contract. The Company's working interest production from Signalta Properties averaged 1,493 Mcf/d and 20 Bopd in 1987. Gas production is expected to rise in 1988 as TransCanada volumes taken improve in response to market conditions.

In late 1987, a one section parcel in the Viking area in which Discovery West has an 8.25% working interest was offset by several oil wells. Signalta, as operator of this lease, has plans to drill a number of wells on reduced spacing on this lease in 1988.

**Brazeau:**

Discovery West holds a 0.92% interest in the Brazeau Gas Unit No. 1 located in West Central Alberta. This is a large unit with gas sold to TransCanada Pipelines Ltd. Discovery West's share of production from this unit averaged 388 Mcf/d in 1987.



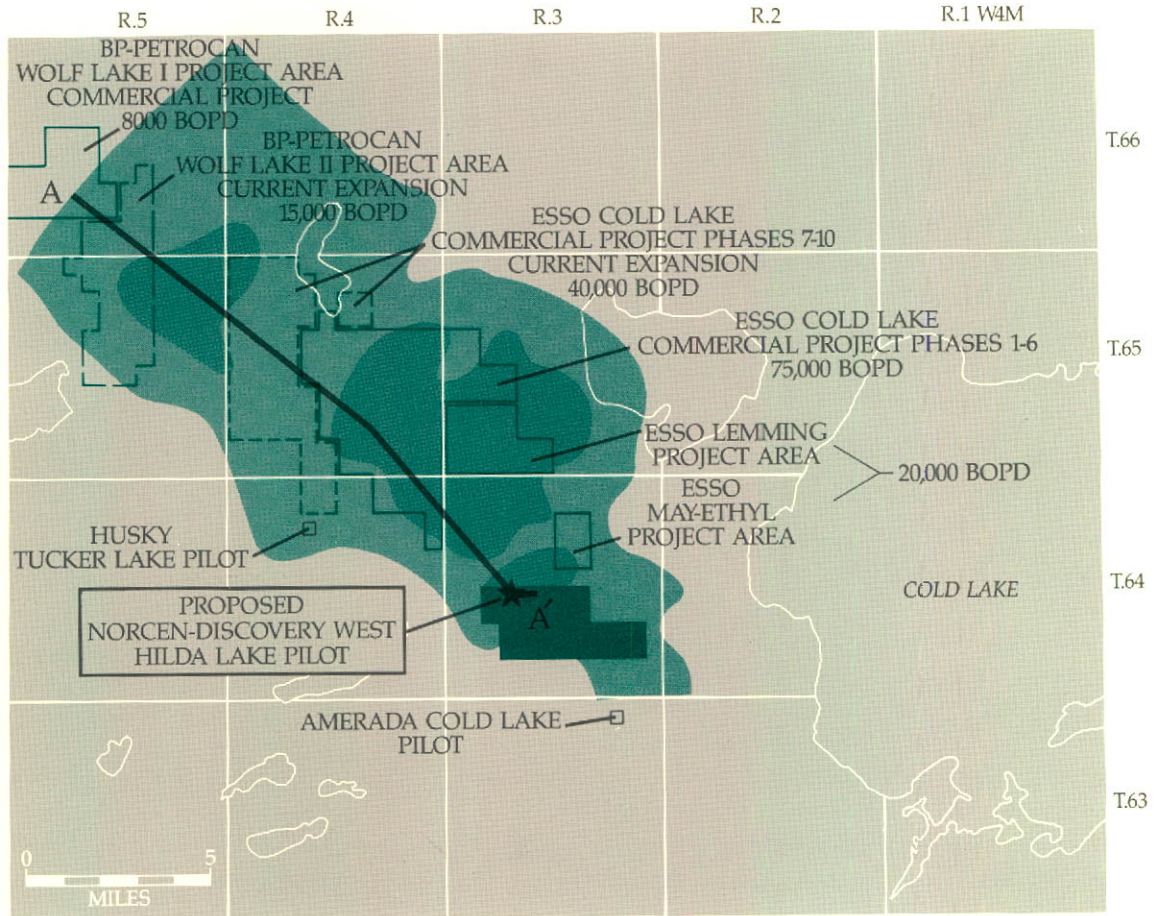


**Cold Lake Area:**

Discovery West Corp. has recently acquired a 65% interest in 4,480 acres of well situated acreage (Oil Sands Lease No. 80) in the Cold Lake area of Alberta. This lease, located in Township 64, Range 3W4, is situated near several major commercial projects constructed to extract bitumen from the Clearwater formation of Cretaceous age.

Discovery West considers the acquisition of Cold Lake Lease No. 80 a rare opportunity. It is unusual for a junior company to be able to participate for a large interest in a high quality reserve at relatively modest cost. The Cold Lake property represents a potential major source of revenue and growth in the future of the Company.

Major heavy oil deposits of the Cold Lake area have attracted large scale industry interest for the past thirty years. This activity resulted in the construction of large scale commercial projects by both Esso Resources Ltd., and BP in partnership with Petro-Canada. Esso currently has a capability to produce approximately 95,000 barrels of bitumen per day at its May-Ethyl, Lemming and Phase 1-6 commercial projects, all of which are located within 10 miles of Discovery West land. The May-Ethyl project is situated only one mile away from Discovery land. BP-Petro-Canada are producing 8,000 barrels of bitumen per day from their Wolf Lake I project located 18 miles northwest of Discovery West's acreage.



- DISCOVERY WEST ACREAGE
- LINE OF CROSS-SECTION A-A'
- CLEARWATER OIL SAND NET PAY
- GREATER THAN 80' THICKNESS
- GREATER THAN 120' THICKNESS

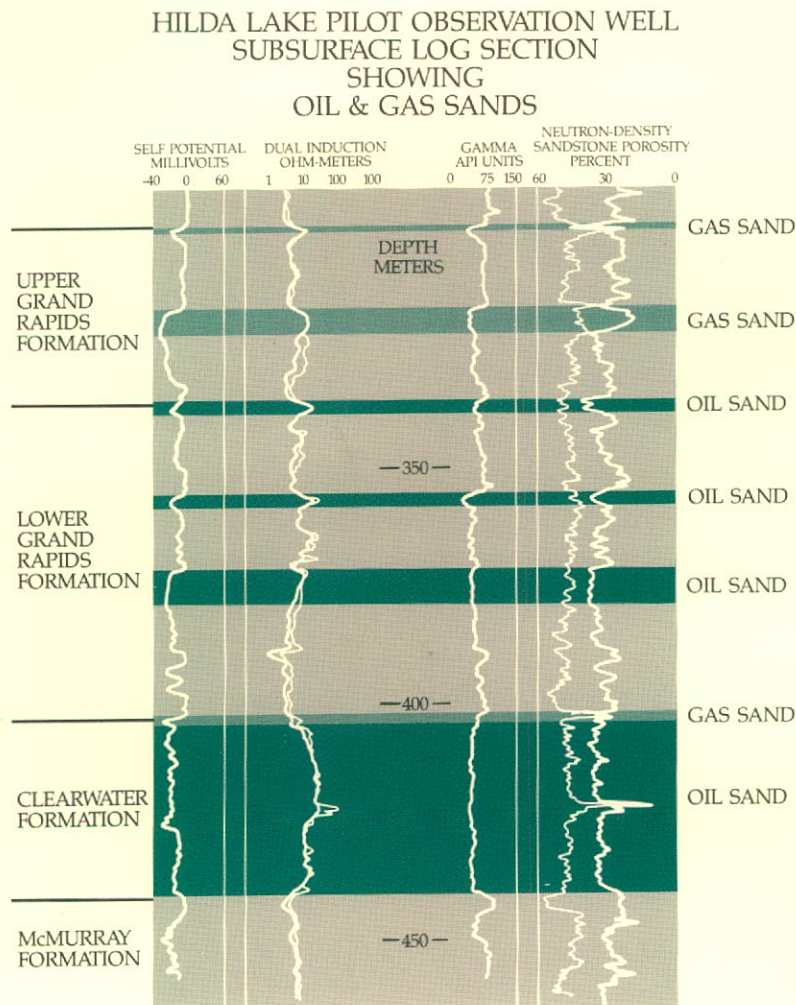
COLD LAKE AREA



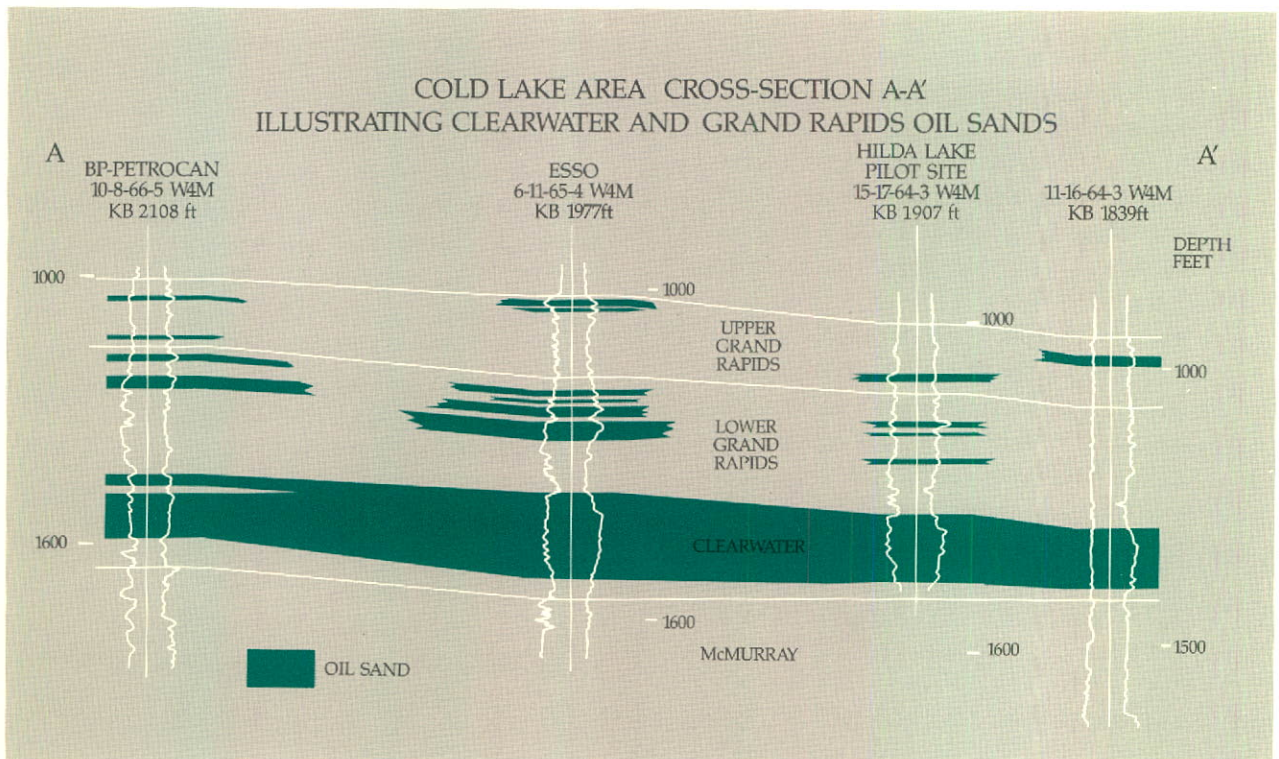
Recently Esso announced it is proceeding with plans to expand its project through four more phases. This is expected to increase output by 40,000 barrels per day. This expansion will cost \$325,000,000 with 260 wells being drilled in 1988. Production is expected to begin in mid-1989 with full production capacity to be reached in 1991 (if all four phases are completed). BP-Petro-Canada are proceeding with construction of their Wolf Lake II expansion estimated to cost \$250,000,000 with the drilling of an initial 250 wells and production of 15,000 barrels of bitumen per day.

*Oil Sands Lease No. 80:*

This lease has been explored by Rayrock Yellowknife Resources Inc., as well as Yellowknife Bear Resources Inc. Exploration was conducted with Norcen Energy Resources and included several phases of drilling and pilot operations. A number of wells drilled on the lease have defined an extensive deposit of bitumen contained within a thick high quality reservoir within the Cretaceous Clearwater formation at an approximate depth of 1,400 feet. Approximately 700 million barrels of bitumen in place have been defined on this land with net pays reaching 120 feet in the







Clearwater. An area containing 300 million barrels of bitumen in place has been selected for initial exploitation using the "huff and puff" steam recovery method. In this area, bottom water is absent or thin.

Using a conservative recovery factor it is estimated that approximately 36 million barrels of bitumen will be recovered from this portion of Lease No. 80 in a future commercial development. Under favourable conditions, other sections of the lease will be exploited.

*Pilot Project:*

Norcen Energy Resources, the 35% owner of Oil Sands Lease No. 80, has the right to increase its interest to 50% by paying 65% of the cost of a pilot steam injection and oil production project necessary to verify the feasibility of a commercial project. Discovery West will pay the other 35% of the estimated cost of the project for a net expenditure of \$5,000,000. Norcen has committed to proceed and preliminary work has been undertaken for the pilot in the NE17, Township 64, Range 3W4. Although some delays are being encountered in receiving government approvals, it is now expected that the pilot will be operational in mid-1989. A daily bitumen production of 700 barrels per day is anticipated from the 12 producing wells to be drilled. Discovery West and Norcen will be

50/50 partners from the time the pilot plant is completed.

*Commercial Project:*

If justified by oil pricing and results of the pilot, the project will be escalated to commercial status through drilling and expansion of facilities. It is currently estimated that the lease will support a commercial project of 5,500 barrels of bitumen per day through the drilling of an additional 90 wells. Initial drilling and facilities will cost approximately \$65,000,000. This production rate would be maintained for a period of 16 years with the drilling of additional wells, as needed, on four acre spacing. A total of 400 wells would be drilled over the first 16 years of the project with a total capital cost of \$150,000,000. During the subsequent eight year life of the project, production would decline to an economic limit. In total 36,000,000 barrels of bitumen would be recovered (50% Discovery West).

*Outlook for Heavy Oil:*

Current forecasts suggest that production of Western Canadian light oil and conventional heavy oil will decline by approximately 500,000 barrels per day by the year 2000. Dramatic increases in bitumen production from the current 160,000 barrels per day to 325,000 barrels per day will be seen by 1995



and 450,000 to 550,000 barrels per day by the year 2000. These general forecasts assume a favorable economic climate. Although the critical factor to future development is oil pricing, other factors include improvements in steam flooding techniques. The development of new equipment, utilization of produced water and improved steam generation facilities are expected to reduce production costs. In the future the establishment of upgrading facilities will assure the marketability of new bitumen production.

**Seal:**

Discovery West also acquired a 5% working interest in 26,240 acres of leases, oil sands leases and oil sands permits in the Seal area of Northern Alberta (Townships 81 & 82, Ranges 12 & 13W5). To date, 5 wells have been drilled on this acreage, all of which have encountered heavy oil pay in isolated "reefs" within the Mississippian Pekisko formation. These reefs, although small in areal extent, have pays generally averaging about 65 feet and are readily identifiable on seismic. A number of additional untested anomalies exist on Company land. In 1985 a huff and puff stimulation test was conducted on the discovery well with favorable results. However, commercial development of this deposit will require higher crude prices. Discovery West will participate in one well in this area in 1988 in order to preserve leases.

**RAYROCK YELLOWKNIFE RESOURCES INC.**

Discovery holds the voting control block of Rayrock Yellowknife Resources Inc. In a transaction to be presented for approval at the forthcoming Rayrock shareholders' meeting, Discovery's equity interest in Rayrock will increase to 23%. For 1987, net earnings were \$6,922,000 (\$.69 per share), cash flow from operations was \$11,219,000 (\$1.12 per share), working capital as at December 31, 1987 was \$43,570,000 and shareholders' equity aggregated \$56,805,000.

Rayrock operates three joint venture gold mines in Nevada that produced a total of 129,954 ounces of gold in 1987 (Rayrock's share: 35,940 ounces). The direct cash operating cost averaged US\$164 per ounce for the year. Gold accounts for more than 60% of the total revenue and 80% of Rayrock's operating profit.

In 1988-89, Rayrock will be developing the new Marigold Mine that will increase Rayrock's gold production by approximately 30%. The total gold ore reserves for the account of Rayrock as at December 31, 1987 were 4,957,000 tons with an average grade of .068 ounces of gold per ton, the equivalent of almost 10 years production at current rates of mining.

Rayrock also owns 35% of and operates Western Ag-Minerals Company, a profitable and growing specialty fertilizer producing and marketing company with over 35 years of ore reserves in place. Rayrock is currently managing and participating in active mineral exploration programs in Canada, the United States, Costa Rica, Ecuador and Chile and has budgeted \$4,000,000 for these activities in 1988.



Discovery West Corp.  
**CONSOLIDATED BALANCE SHEET**  
As at December 31, 1987



**Assets**

	1987	1986 (note 2)
<b>Current Assets</b>		
Cash and short-term investments	\$ 7,253,000	\$ 3,527,000
Accounts receivable	989,000	991,000
Income taxes recoverable	34,000	573,000
	<b>8,276,000</b>	5,091,000
<b>Long-Term Investments</b> (note 3)	<b>10,011,000</b>	4,924,000
<b>Mining Properties</b> (notes 4, 11(b))	<b>94,000</b>	94,000
<b>Oil and Gas Properties</b>		
Petroleum and natural gas leases and equipment – at cost, less accumulated depletion and amortization of \$14,815,000 (1986 – \$11,987,000)	<b>31,349,000</b>	32,112,000
<b>Deferred Financing Costs</b>	<b>433,000</b>	–
	<b>\$50,163,000</b>	\$42,221,000

**Liabilities**

<b>Current Liabilities</b>		
Accounts payable and accrued liabilities	\$ 785,000	\$ 799,000
Current portion of bank loan	637,000	660,000
	<b>1,422,000</b>	1,459,000
<b>Long-Term Debt</b> (note 5)	<b>8,000,000</b>	637,000
<b>Deferred Revenue</b>	<b>397,000</b>	452,000
<b>Deferred Income Taxes</b>	<b>9,202,000</b>	9,349,000
<b>Minority Interest</b>	<b>121,000</b>	106,000
	<b>19,142,000</b>	12,003,000
<b>Shareholders' Equity</b>		
<b>Capital Stock</b> (note 6)	<b>20,265,000</b>	20,281,000
<b>Contributed Surplus</b>	<b>1,749,000</b>	1,749,000
<b>Retained Earnings</b>	<b>9,007,000</b>	8,188,000
	<b>31,021,000</b>	30,218,000
	<b>\$50,163,000</b>	\$42,221,000

Signed on behalf of the Board

D.R. Crombie, Director

W. Steuerman, Director



**CONSOLIDATED STATEMENT OF INCOME**

For the year ended December 31, 1987

	1987	1986 (note 2)
<b>Income</b>		
Revenue from petroleum operations	<b>\$7,072,000</b>	\$ 7,106,000
<b>Expenses</b>		
Oil and gas	<b>2,287,000</b>	2,863,000
Administrative and general	<b>1,071,000</b>	1,130,000
Depreciation, amortization and depletion	<b>2,828,000</b>	2,598,000
Current and deferred exploration expenditures written off	<b>406,000</b>	407,000
	<b>6,592,000</b>	6,998,000
<b>Income from Operations</b>	<b>480,000</b>	108,000
<b>Other Income (Expenses)</b>		
Interest expenses	<b>(592,000)</b>	(179,000)
Investment and other income	<b>912,000</b>	611,000
	<b>320,000</b>	432,000
<b>Income Before the Undernoted Items</b>	<b>800,000</b>	540,000
<b>Provision for (Recovery of) Income Taxes</b> (note 9(a))		
Current	<b>26,000</b>	411,000
Deferred	<b>(147,000)</b>	(600,000)
	<b>(121,000)</b>	(189,000)
<b>Minority Interest in Income (Loss) of Subsidiary</b>	<b>15,000</b>	(8,000)
<b>Income Before Unusual Items</b>	<b>906,000</b>	737,000
<b>Unusual Items</b>		
Write down of mining properties (net of deferred income tax recovery of \$466,000)	—	970,000
Write down of oil and gas properties (net of deferred income tax recovery of \$1,933,000)	—	1,815,000
	—	2,785,000
<b>Income (Loss) for the Year</b>	<b>\$ 906,000</b>	\$(2,048,000)
<b>Net Income per Participating Share Before Unusual Items</b>	<b>\$0.04</b>	\$ 0.03
<b>Income (Loss) per Participating Share After Unusual Items</b>	<b>\$0.04</b>	\$(0.11)



**CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION**

For the year ended December 31, 1987



	1987	1986 (note 2)
<b>Operating Activities</b>		
Income (loss) for the year	\$ 906,000	\$(2,048,000)
Non-cash charges	2,593,000	3,436,000
Decrease in working capital excluding cash	504,000	1,304,000
Cash provided by operations	4,003,000	2,692,000
<b>Investment Activities</b>		
Purchase of debentures	(4,970,000)	—
Purchase of Rayrock Series D preference shares	—	(350,000)
Increase in long-term investments	(75,000)	(64,000)
Proceeds on sale of investments	5,000	1,501,000
Expenditure on oil and gas properties	(2,064,000)	(3,097,000)
Other	—	(24,000)
Cash (used in) investment activities	(7,104,000)	(2,034,000)
<b>Financing Activities</b>		
Issue of debentures	8,000,000	—
Reduction in bank loan	(637,000)	(660,000)
(Redemption) issue of capital stock	(16,000)	36,000
Issue of flow through shares	—	350,000
Cash provided on amalgamation with Rich Group Yellowknife Mines Limited	—	1,864,000
Amalgamation expenses	—	(310,000)
Deferred financing costs	(433,000)	—
Dividends on preferred shares	(87,000)	(93,000)
Cash provided by financing activities	6,827,000	1,187,000
<b>Increase in Cash</b>	<b>3,726,000</b>	<b>1,845,000</b>
<b>Cash — Beginning of Year</b>	<b>3,527,000</b>	<b>1,682,000</b>
<b>Cash — End of Year</b>	<b>\$ 7,253,000</b>	<b>\$ 3,527,000</b>
Cash consists of cash, short-term investments including treasury bills, bankers acceptances and commercial paper.		



**CONSOLIDATED STATEMENT OF RETAINED EARNINGS**

For the year ended December 31, 1987

	1987	1986 (note 2)
<b>Retained Earnings — Beginning of Year</b>	<b>\$8,188,000</b>	\$10,741,000
Net earnings (loss) for the year	<b>906,000</b>	(2,048,000)
	<b>9,094,000</b>	8,693,000
<b>Dividends</b>		
Preferred shares	<b>87,000</b>	93,000
Assets dividend to Rayrock Yellowknife Resources Inc. (net of taxes)	—	150,000
<b>Amalgamation Expenses</b> (net of deferred income tax recovery of \$113,000)	—	262,000
	<b>87,000</b>	505,000
<b>Retained earnings — End of Year</b>	<b>\$9,007,000</b>	\$ 8,188,000

**Auditors' Report to the Shareholders**

We have examined the consolidated balance sheet of Discovery West Corp. as at December 31, 1987 and the consolidated statements of income, retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1987 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Toronto, Ontario  
February 26, 1988

Coopers & Lybrand  
Chartered Accountants





## 1. Accounting Policies

The accounting policies of the company are in accordance with generally accepted accounting principles. Those policies considered particularly significant are outlined below:

(a) Basis of consolidation

The consolidated financial statements include the accounts of the Company and its subsidiaries. Acquisitions are accounted for by the purchase method and accordingly the results of operations of subsidiaries are included from the dates of acquisition.

(b) Long-term investments

Long-term investments, including the investment in Rayrock Yellowknife Resources Inc., are carried at cost and are written down when there is evidence that their inherent worth has declined below their carried value.

(c) Exploration expenditures (note 11(b))

Costs incurred in exploring for minerals, including participation in partnerships and joint ventures, are charged to expense in the year incurred, unless, in the opinion of management, the expenditure is likely to result in the establishment of a viable income-producing property.

After this determination, all costs related to further development are capitalized and amortized over the productive life of the property on a unit-of-production method based on the estimated tons of ore to be recovered. Mine development costs incurred to maintain current production are included in operating costs and expenses.

Costs incurred in exploring for oil and gas, including participation in joint ventures, are capitalized until completion of the particular exploration and drilling programme, at which time the costs of unsuccessful programmes are written-off. Acquisition costs of oil and gas properties and the costs of drilling and equipping successful wells are capitalized.

Alberta Petroleum Incentive Program grants are credited to the oil and gas properties and depleted over the life of the properties.

(d) Depreciation, depletion and amortization

Depreciation and depletion of oil and gas properties, including equipment, is determined on a straight line basis over the estimated life of each oil and gas property. Such depreciation and depletion charges approximate charges determined on a unit-of-production basis. The estimated useful life is based on commercially recoverable reserves estimated by management and revised as data becomes available.

The Company carries its oil and gas properties at the lower of capitalized cost or net recoverable value. Net recoverable value is the aggregate of future net revenues from proven reserves plus unproved properties at cost or fair value where value has been determined. Net revenues are determined using year-end prices and costs, including operating, general and administrative, and interest costs, on an after-tax basis.

The costs incurred on the issuance of debentures, is deferred and amortized over the life of the debenture.

(e) Income taxes

The Company follows the deferral method of tax allocation whereby the provision for income taxes is based on the income reported in the accounts. Principal timing differences result from exploration and development expenditures claimed for tax purposes in excess of amounts written-off for accounting purposes.

## 2. Business Combination

The Company was formed by the amalgamation of Discovery Mines Limited ("Discovery"), Midcon Oil & Gas Limited ("Midcon") and Yellowknife Bear Resources Inc. ("Yellowknife") which became effective on March 1, 1987.

Under the terms of the Arrangement Agreement, the shares of the Company were issued as follows:

- (1) To the shareholders of Discovery, other than the shares held by Yellowknife:
  - One common share for each subordinate voting share held.
  - One preferred share for each preferred share held.
- (2) To the shareholders of Midcon, other than the shares held by Yellowknife:
  - Nine common shares for each five common shares held.
- (3) To the shareholders of Yellowknife (wholly-owned by Rayrock Yellowknife Resources Inc.):
  - 5,603,749 common shares
  - 3,798,544 non-voting shares

Inasmuch as an acquirer could not be identified, the combination has been accounted for as a pooling of interests. Accordingly, the assets and liabilities of the combining companies are recorded at original book values and results of operations are presented as if the companies had always been combined. Details of the net assets at December 31, 1986, brought into the combination by each of the companies are as follows:

	Discovery	Midcon	Yellowknife	Total
	(thousands)			
Total assets . . . . .	\$15,807	\$16,755	\$ 9,659	\$42,221
Total liabilities . . . . .	2,895	5,793	3,315	12,003
	\$12,912	\$10,962	\$ 6,344	\$30,218
Capital stock . . . . .	\$13,677	\$ 3,390	\$ 3,214	\$20,281
Contributed surplus . . . . .	588	1,161	—	1,749
Retained earnings . . . . .	(1,353)	6,411	3,130	8,188
	\$12,912	\$10,962	\$ 6,344	\$30,218

Details of the revenues and net earnings of each of the combining companies for the year ended December 31, 1986 are as follows:

	Discovery	Midcon	Yellowknife	Total
	(thousands)			
Revenues . . . . .	\$ 2,435	\$ 3,664	\$ 1,663	\$ 7,762
Net earnings before unusual items . . . . .	\$ 76	\$ 531	\$ 130	\$ 737
After-tax write-down of oil and gas properties	(213)	—	(1,602)	(1,815)
After-tax write-down of mining properties	(804)	—	(166)	(970)
Net earnings (loss) . . . . .	\$ (941)	\$ 531	\$(1,638)	\$(2,048)
Minority interest in net earnings . . . . .	—	\$ 8	—	\$ 8



### 3. Long-term Investments

	1987	1986
Investment in shares and debentures of Rayrock Yellowknife Resources Inc. —		
Subordinate voting shares — (quoted market value \$11,050,000; 1986 — \$8,764,000) .....	\$ 4,104,000	\$4,101,000
Preferred shares .....	550,000	550,000
\$5,000,000 — 7.5% convertible subordinated debentures .....	4,970,000	—
	<b>9,624,000</b>	4,651,000
Investments in other companies — (quoted market value \$701,000; 1986 — \$23,000) .....	259,000	145,000
Non-interest bearing advances to officers and employees under a stock purchase plan, due on or before December 31, 1989 .....	128,000	128,000
	<b>\$10,011,000</b>	<b>\$4,924,000</b>

The quoted market values referred to above do not necessarily represent the realizable value of these holdings which may be more or less than that indicated by market quotations.

### 4. Mining Properties (note 11 (b))

- (a) Mining claims were acquired for cash and shares of capital stock as valued by the directors of the applicable company and are carried at cost, less amounts written-off.
- (b) The recoverability of the amount shown for mineral properties is dependent upon the existence of economically recoverable reserves, the ability of the Company to obtain necessary financing to complete the developments, and future profitable operations.

### 5. Long-term Debt

	1987	1986
8% convertible subordinated debentures .....	\$8,000,000	\$ —
Bank loan .....	637,000	1,297,000
	<b>8,637,000</b>	1,297,000
Current portion .....	637,000	660,000
	<b>\$8,000,000</b>	<b>\$ 637,000</b>

- (a) During the year the Company issued \$8,000,000 8% convertible subordinated debentures, convertible into 4,000,000 common shares at a conversion price of \$2.00 per share. The debentures mature on March 31, 1997 and are redeemable, at par, after March 31, 1990 under certain circumstances. The holder has a retraction right exercisable on March 31, 1993. Certain employees of the Company have purchased \$1,000,000 of these debentures (see note 7(b)).
- (b) The Company has pledged as security for the bank loan certain of its petroleum and natural gas leases and equipment. The loan bears interest at prime plus ½% per annum. The loan is repayable in monthly instalments of \$55,000 with the Company having the right to repay the loan at any time.

## 6. Capital Stock

### (a) Authorized and issued

	Authorized	Issued and fully paid at December 31			
		1987		1986	
		Number of shares	Stated value	Number of shares	Stated value
Participating . . . . .	Unlimited				
Non-voting shares . . . . .		5,611,299		5,603,749	
Common shares . . . . .		13,810,013		13,827,011	
		19,421,312	\$18,825,000	19,430,760	\$18,841,000
Preferred shares . . . . .	Unlimited				
\$0.06 cumulative redeemable Series A carrying one vote per share . . . . .		500,000	\$ 500,000	500,000	\$ 500,000
Floating rate cumulative, redeemable convertible, retractable non-voting Series B . . . . .		412,500	660,000	412,500	660,000
\$0.03 non-cumulative redeemable convertible non-voting Series C . . . . .		140,000	280,000	140,000	280,000
			\$20,265,000		\$20,281,000

- i) The common and non-voting shares rank equally with each other and are interchangeable.
  - ii) The Series B and C preferred shares are convertible into common shares on a one-for-one basis.
  - iii) The Series A preferred shares are redeemable at a price of \$1.00 per share. The Series B preferred shares are redeemable at a price of \$1.60 per share, the original issue price. The Series C preferred shares are redeemable at any time after January 1, 1991 at a price of \$2.50 per share, the original issue price.
  - iv) Monthly dividends payable on the Series B preferred shares are calculated at a rate of one percentage point below the prime rate.
  - v) The Company has provided collateral and has agreed to retain sufficient funds on hand to ensure funding of the future potential retraction of the Series B preferred shares.
- (b) Changes in the year
- i) Payments of \$24,000 were made to dissenters of the Discovery West Corp. business combination holding 14,448 shares which were cancelled.
  - ii) 5,000 common shares were issued for a cash consideration of \$7,500 under the stock option plan.
- (c) Stock options
- Stock options on 494,000 common shares are outstanding and exercisable at prices from \$1.40 to \$2.13.
- (d) The Company has reserved 100,000 shares for a stock option plan for non-executive employees of which options for 7,000 shares have been granted.
- (e) Earnings per participating share are calculated on the basis of the weighted average number of participating shares outstanding during the year. The stock options, convertible preferred shares and convertible debentures have no dilutive effect for any of the years included.



**7. Related Party Transactions** (See note 11)

- (a) Rayrock Yellowknife Resources Inc., which has a significant voting interest in the Company as a result of its share ownership, pays a portion of the remuneration of senior officers together with the rent and other joint costs of associated companies and is reimbursed by those companies for their proportionate share thereof. The amount paid during the year by the Company in respect of such charges was \$262,000 (1986 – \$162,000).
- (b) As a condition of certain employees of the Company purchasing \$1,000,000 of its 8% convertible subordinated debentures, the Company has entered into an agreement with these employees and a financial institution to redeem the debentures at par if called upon to do so by the financial institution.

**8. Segmented Information**

The Company operates substantially in Canada in one industry – the development of and participation in the operation of oil and gas properties.

While the identifiable assets related to the investment activities exceed 10% of the total assets, these activities are purely incidental to the oil and gas activities. The revenues, operating earnings, depreciation and depletion, identifiable assets and capital expenditures are self-evident in the balance sheet, statement of earnings and statement of changes in financial position.

**9. Income Tax**

- (a) The variations from the basic statutory income tax rate and the Company's effective income tax rate on the income before writedowns are as follows:

	1987	1986
Income tax at statutory rates . . . . .	\$ 412,000	\$ 270,000
Resource allowance . . . . .	(559,000)	(638,000)
Crown royalties not allowed net of Alberta Royalty tax credit . . . . .	141,000	227,000
Non taxable portion of capital gain . . . . .	—	(112,000)
Other . . . . .	(115,000)	64,000
	<u>\$ (121,000)</u>	<u>\$ (189,000)</u>

- (b) At December 31, 1987 the Company has available \$213,000 of capital loss carry-forwards to reduce future taxable capital gains. The corresponding capital losses available for accounting purposes are \$1,300,000. The potential tax benefits arising from these accounting loss carry-forwards have not been reflected in these financial statements, and will be recognized in future periods as the Company realizes capital gains for accounting purposes.

**10. Commitments and Contingencies**

- (a) The Company entered into a long-term agreement with a senior officer of the Company which provides for an annual retirement allowance, on a joint survivorship basis with his wife, in amounts ranging from \$47,500 to \$75,000.
- (b) The Company has entered into an agreement with associated companies whereby certain Canadian current account cash balances are pooled in a concentration account. Each of the companies guarantees the overdrafts (if any) of the other companies in this arrangement.

## 11. Subsequent Events

- (a) The Board of Directors of the Company has approved the purchase, for cash, of the Cold Lake and Seal area heavy oil leases from Rayrock Yellowknife Resources Inc. (Rayrock) effective January 1, 1988 for Rayrock's 1986 year-end book value of \$311,680 plus its 1987 expenditure on these leases estimated to be \$288,000.
- (b) The Board of Directors of the Company has approved the sale of all of the Company's mining properties to Rayrock effective January 1, 1988 for subordinate voting shares of Rayrock. 781,453 shares are to be received upon completion of the transaction with up to an additional 162,127 shares to be received on completion of an evaluation of an exploration programme being conducted on two properties. The Directors of Rayrock have set the value of the shares to be issued at \$7.71 per share.
- (c) The Board of Directors of the Company has approved a purchase, by way of private placement, of 518,807 subordinate voting shares of Rayrock at a price of \$7.71 per share for a total cost of \$4,000,000 cash. This transaction is subject to confirmation by the shareholders of Rayrock.





**DIRECTORS**

**\*David R. Crombie**  
Toronto, Ontario

**Earl E. Curry**  
Christina Lake, B.C.

**\*Hugh Mogensen**  
Vancouver, British Columbia

**\*John W. Sabine**  
Toronto, Ontario

**Walter Steuerman**  
Toronto, Ontario

**\*J. Douglas Streit**  
Toronto, Ontario

**Mervyn A. Upham**  
Toronto, Ontario

\*Member of Audit Committee

**OFFICERS**

**Mervyn A. Upham**  
Chairman of the Board

**David R. Crombie**  
President and Chief Executive Officer

**O. Mike Isaac**  
Executive Vice-President

**Walter Steuerman**  
Vice-President and Secretary

**C. Bruce Burton**  
Vice-President, Finance

**David A. Hutton**  
Vice-President

**Joan I. Conway**  
Treasurer

**Glen F. Lonsdale**  
Controller and Assistant Treasurer

## SHAREHOLDER INFORMATION

### **Transfer Agents and Registrars**

Central Trust Company  
88 University Avenue  
Toronto, Ontario  
M5J 1T8  
Telephone: (416) 975-5245

### **Bankers**

Canadian Imperial Bank of Commerce  
Toronto, Ontario

Lloyds Bank  
Toronto, Ontario

Royal Bank of Canada  
Calgary, Alberta

### **Auditors**

Coopers & Lybrand  
Toronto, Ontario

### **Solicitors**

Campbell, Godfrey & Lewtas  
Toronto, Ontario

**Listed:** The Toronto Stock Exchange

**Ticker Symbol:** DSW

### **For more information please contact:**

Joyce E. Davies  
Investor Relations Officer  
(416) 977-6644

### **Executive Office**

65 Granby Street  
Toronto, Ontario  
M5B 1H8  
Telephone: (416) 977-6644  
Telecopier: (416) 977-5475  
Telex: 065-24314

### **Western Canada Oil and Gas Operations**

#800, 555-4th Avenue S.W.  
Calgary, Alberta  
T2P 3E7  
Telephone: (403) 263-1441  
Telecopier: (403) 266-3799

O. Mike Isaac  
Executive Vice-President

J. C. Mawdsley  
Exploration Manager



**Shares:**

Number of participating shares outstanding at December 31, 1987 — 19,421,312.

<b>Market Price:</b>	<b>1987</b>	<b>1986</b>	<b>1985</b>
High	<b>\$2.70</b>	\$2.25	\$2.50
Low	<b>\$1.00</b>	\$1.10	\$1.35

**Metric Conversion Table:**

To assist readers of our annual report, we provide the following:

To convert from:	To:	Multiply by:
Thousand cubic feet (Mcf gas)	Thousand cubic metres (10 <sup>3</sup> m <sup>3</sup> )	0.028169
Barrels (Bbls) oil	Cubic metres (m <sup>3</sup> )	0.159000
Feet (well depths)	Metres (m)	0.305000
Miles (distance)	Kilometres (km)	1.609000
Acres (land)	Hectares (ha)	0.405000
Tons	Tonnes	0.907000

**Abbreviations:**

Bbls	barrels
Bopd	barrels oil per day
Mbbls	thousands of barrels
Mmbbls	millions of barrels
Mcf	thousands of cubic feet
Mcf/d	thousands of cubic feet per day
Mmcf	millions of cubic feet

**Pricing Forecast Table**

Martin Petroleum & Associates' current estimate of future prices are as follows:

	<b>OIL</b> (\$ Cdn./bbl)	<b>GAS (\$ Cdn./mcf)</b> WGM D <sub>1</sub> /D <sub>2</sub> Average Field Price
1988	\$22.40	\$1.88
1989	\$24.20	\$2.04
1990	\$26.05	\$2.20
1991	\$27.85	\$2.37
1992	\$29.65	\$2.65
1993	\$31.50	\$2.90
Thereafter	+6%/year	+6%/year

The foregoing prices are benchmark prices only. The Company's future net revenues are calculated according to the quality of oil and gas reserves and the terms of any gas sales contracts in place.

C

## DISCOVERY WEST CORP.

65 Granby Street  
Toronto, Ontario  
M5B 1H8

### NOTICE OF ANNUAL AND SPECIAL MEETING

NOTICE is hereby given that the Annual and a Special Meeting of the shareholders of Discovery West Corp. (the "Corporation") will be held in Confederation Room No. 4, Royal York Hotel, 100 Front Street West, Toronto, Ontario, Canada, at 10:00 a.m. on April 29, 1988 for the purposes of:

- (1) receiving the annual report of the Corporation including the financial statements for the year ended December 31, 1987 and the auditors' report thereon;
- (2) electing directors;
- (3) appointing auditors and authorizing the directors to fix their remuneration;
- (4) considering and, if thought fit, passing a resolution approving the granting of share purchase options to executive officers of the Corporation; and
- (5) transacting such other business as may properly come before the meeting.

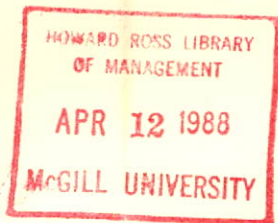
Information with respect to the foregoing matters is contained in the Management Proxy Circular which accompanies this Notice.

If you are not able to attend the meeting, would you kindly date, sign and return the enclosed Form of Proxy in the envelope provided for that purpose.

DATED at Toronto this 3rd day of March, 1988.

By Order of the Board,

W. STEUERMAN,  
Secretary





# DISCOVERY WEST CORP.

## MANAGEMENT PROXY CIRCULAR

### SOLICITATION OF PROXIES

THIS MANAGEMENT PROXY CIRCULAR IS FURNISHED IN CONNECTION WITH THE SOLICITATION OF PROXIES BY THE MANAGEMENT OF DISCOVERY WEST CORP. (THE "CORPORATION") FOR USE AT THE ANNUAL AND SPECIAL MEETING OF SHAREHOLDERS OF THE CORPORATION TO BE HELD ON APRIL 29, 1988 IN CONFEDERATION ROOM NO. 4, ROYAL YORK HOTEL, 100 FRONT STREET WEST, TORONTO, ONTARIO AT 10:00 O'CLOCK A.M. (TORONTO TIME) FOR THE PURPOSES SET FORTH IN THE ACCOMPANYING NOTICE OF MEETING. It is expected that the solicitation will be primarily by mail. Proxies may also be solicited personally or by telephone by regular employees of the Corporation at nominal cost. The costs of solicitation by management will be borne by the Corporation. In addition, proxies from unregistered shareholders whose shares are held by Canadian intermediaries may be solicited by these intermediaries who will be compensated therefor by the Corporation.

### REVOCABILITY OF PROXY

In addition to revocation in any other manner permitted by law, a proxy may be revoked by instrument in writing executed by the shareholder or by his attorney authorized in writing or, if the shareholder is a body corporate, under its corporate seal or by an officer or attorney thereof duly authorized, and deposited either at the head office of the Corporation at any time up to and including the last business day preceding the day of the meeting, or any adjournment thereof, at which the proxy is to be used or with the Chairman of the meeting on the day of the meeting, or any adjournment thereof. The address of the head office of the Corporation is 65 Granby Street, Toronto, Ontario M5B 1H8.

### VOTING SHARES AND PRINCIPAL HOLDERS THEREOF

As at the close of business on March 3, 1988, 13,800,313 common shares and 500,000 Series A Preferred shares were outstanding. Each shareholder of record on March 25, 1988 is entitled to cast one vote for each common share then held of record and one vote for each Series A Preferred share then outstanding, unless pursuant to subsection 132(3) of the Canada Business Corporations Act, a transferee of shares establishes that he owns shares recorded in the name of a shareholder otherwise entitled to vote and demands not later than 10 days before the meeting that his name be substituted for that of the transferor of shares to him (with respect only to the shares transferred), in which case he is entitled to vote the shares transferred to him instead of the transferor.

To the knowledge of the directors and officers of the Corporation as at March 3, 1988 no person beneficially owns, directly or indirectly, or exercises control or direction over shares carrying more than 10% of the voting rights attached to any class of shares of the Corporation, except:

Owner	Shares Held	Voting Percentage
Rayrock Yellowknife Resources Inc. 65 Granby Street Toronto, Ontario M5B 1H8	Common: 6,588,056	46.1
	Series A Preferred: 500,000	3.5
		<u>49.6</u>

\$1.50 per share, this price being in excess of the closing price of the common shares on The Toronto Stock Exchange on that date. The options are not transferable and expire on the dates indicated. During the 30 days prior to the granting of the options, the common shares traded on The Toronto Stock Exchange at a high of \$1.37 per share and a low of \$1.18 per share.

<u>Name and Office of Optionee</u>	<u>Number of Shares</u>	<u>Expiry Date</u>
O. M. Isaac Executive Vice President	180,000	August 17, 1995
D. A. Hutton Vice President	20,000	August 17, 1995
C. B. Burton Vice President, Finance	75,000	January 25, 1996

The options are subject to acceptance of a notice filed with The Toronto Stock Exchange and approval by shareholders. To be approved, the resolution must be passed by the affirmative vote of a majority of the votes cast at the meeting.

#### **OTHER BUSINESS**

The management knows of no matters to come before the Annual and Special Meeting other than the matters referred to in the Notice of Meeting. However, if any other matters which are not now known to the management should properly come before the meeting or if amendments or variations to the matters identified in the Notice of Meeting are presented for action at the meeting, the accompanying Proxy will be voted on such other matters, amendments or variations, in accordance with the best judgment of the person voting the Proxy, which Proxy confers such discretionary authority.

The contents and the sending of this Management Proxy Circular have been approved by the directors.

W. Steerman  
Vice President and Secretary

Toronto, Ontario  
March 3, 1988



In addition to the remuneration described above, the Corporation makes contributions to Rayrock Yellowknife Resources Inc., an associated corporation, which pays remuneration to common executive officers of both corporations.

3. In addition to the cash compensation described in paragraph 2 above, the Corporation provides certain taxable benefits to its executive officers. However, such benefits do not exceed the lesser of \$10,000 times the number of executive officers or ten percent of the cash compensation in paragraph 2 above.

4. The Corporation entered into an employment contract with its President which provides for annual remuneration to be determined by the directors from time to time and, upon termination of employment, a minimum pension escalating to an annual amount of \$75,000 in 1999 subject to a review by the board of directors. To fund the Corporation's liability, the Corporation has purchased for its sole benefit a total of \$750,000 whole life insurance policies on the President's life requiring an annual premium of \$9,568 until the year 2003.

5. Directors, other than directors who are also salaried employees of the Corporation, receive an annual fee of \$5,000 and an additional fee of \$500 for each meeting attended.

### **INDEBTEDNESS OF DIRECTORS AND SENIOR OFFICERS**

During the period since January 1, 1987, the only director or senior executive indebted to the Corporation was Mr. D. R. Crombie, President, pursuant to an interest free loan of \$50,000 made for the purpose of acquiring shares of the Corporation.

### **DIRECTORS' AND OFFICERS' INSURANCE**

The Corporation, in conjunction with its associate Rayrock Yellowknife Resources Inc., purchased standard liability insurance for its directors and officers in the amount of \$3,000,000. The insurance is applicable only for lawsuits brought in Canada. The annual combined premium in respect of this insurance is \$55,060. The policy provides for a \$5,000 deductible for a claim against any director or officer and a \$20,000 deductible for claims against all directors and officers. If the Corporation reimburses its directors or officers with respect to a claim, the Corporation is subject to a \$100,000 deductible. In addition, the Corporation has agreed to indemnify each director for any legal liability which the director incurred in his capacity as a director of the Corporation and solely because of his acting in such capacity.

### **APPOINTMENT OF AUDITORS**

Unless otherwise instructed, proxies in favour of management nominees will be voted to appoint Coopers & Lybrand, the present auditors, as auditors of the Corporation and to authorize the directors to fix the remuneration of the auditors.

### **TRANSACTIONS WITH INSIDERS**

The Corporation's President, on behalf of himself and other officers and employees, purchased a total of \$1,000,000 principal amount of the Corporation's 8% subordinated convertible debentures pursuant to a private placement of a total of \$8,000,000 debentures through First Marathon Capital Corp. as agent.

### **APPROVAL OF SHARE PURCHASE OPTIONS**

The item of special business at the meeting is to consider and, if thought fit, to pass a resolution approving the granting of options to purchase 275,000 common shares to certain executive officers of the Corporation.

On January 25, 1988, the Corporation granted options to purchase common shares of the Corporation to the undermentioned executive officers for the number of shares set against their names at an exercise price of

## ELECTION OF DIRECTORS

The Articles of the Corporation provide that the board of directors shall consist of a minimum of five directors and a maximum of eleven. The board of directors has determined that there will be eight directors. Unless otherwise instructed proxies received in favour of management nominees will be voted for the election of nominees for directors set forth herein (or for substitute nominees in the event of contingencies not known at present) who will, subject to the By-laws of the Corporation, serve until the next annual meeting of shareholders or until their successors are elected or appointed in accordance with the By-laws.

The following table and notes thereto state the names of the persons proposed to be nominated for election as directors, all other positions and offices with the Corporation now held by them, their principal occupations or employment and the years in which they first became directors of the Corporation or a predecessor corporation. Each of the nominees listed below has advised the Corporation that on March 3, 1988 he beneficially owned or exercised control or direction over the indicated number of shares.

Name and Principal Occupations	Major Positions and Offices with the Corporation and its Significant Affiliates	Director Since	Number of Shares	
			Common	Non-Voting Series B Preferred
David R. Crombie <sup>(1)(2)</sup> Professional Engineer	President and Chief Executive Officer of the Corporation and of Rayrock Yellowknife Resources Inc.	1976	342,990	281,250
Earl E. Curry <sup>(2)</sup> Corporate Director	Director	1980	Nil	Nil
O. Michael Isaac <sup>(3)</sup> Professional Geologist	Executive Vice President of the Corporation	—	Nil	Nil
Hugh Mogensen Professional Geologist	Director	1985	Nil	Nil
John W. Sabine <sup>(1)</sup> Partner of the law firm of Campbell, Godfrey & Lewtas	Director	1985	2,000	Nil
Walter Steuerman Chartered Accountant	Director, Vice-President and Secretary of the Corporation and of Rayrock Yellowknife Resources Inc.	1979	24,462	37,500
J. Douglas Streit <sup>(1)</sup> Professional Engineer	Director, Chairman of the Board of Rayrock Yellowknife Resources Inc.	1956	50,000	Nil
Mervyn A. Upham Mining Engineer	Chairman of the Board	1986	Nil	Nil

(1) Member of Audit Committee.

(2) Messrs. Crombie and Curry own, respectively, \$750,000 and \$100,000 subordinated convertible debentures of the Corporation which are ultimately convertible into 375,000 and 50,000 common shares respectively of the Corporation.

(3) Mr. Isaac has occupied his present position as Executive Vice President of the Corporation since August 17, 1987. Prior to that time he was Executive Vice President of Carlyle Energy Ltd. for more than 5 years.

## STATEMENT OF EXECUTIVE REMUNERATION

1. Number of executive officers — 6.

2. Aggregate cash compensation paid to executive officers for the year ended December 31, 1987 by the Corporation and its subsidiary companies amounted to \$178,566.





**Notice of Annual and Special Meeting**

The Annual and a Special Meeting of the shareholders of Discovery West Corp., will be held on Friday, April 29, 1988 at 10:00 a.m. at Confederation Room No. 4, The Royal York Hotel, 100 Front Street West, Toronto, Ontario. All shareholders are encouraged to attend.



