ATCO Ltd.
1985 Annual Report

The Corporation's business segments (utilities, resources, manufacturing and real estate) recorded an improved performance in the past year.

Our strong financial, technological and human resources will support continued growth in the future.

Financial Highlights

Years ended March 31

(Thousands except share data)	1985	1984	Change
Revenues	$1,644,663	$1,610,339	+2%
Earnings for the year	$ 44,685	$ 18,533	+141%
Earnings (loss) attributable to Class I and Class II shares	$ 11,342	$ (3,171)	—
Earnings (loss) per Class I and Class II share	$ .51	$ (.16)	—
Dividends paid per Class I and Class II share	$ .20	$ .20	—
Cash provided by operating activities	$ 248,548	$ 202,028	+23%
Working capital	$ 16,043	$ 50,816	−68%
Additions to property, plant and equipment	$ 239,623	$ 305,722	−22%
Total assets	$3,036,379	$2,882,057	+5%
Class I and Class II shareholders' equity	$ 204,148	$ 201,998	+1%
Class I and Class II shares outstanding	22,166,800	22,156,900	—
Weighted average Class I and Class II shares outstanding	22,164,344	19,304,544	—

From its beginnings as a supplier of innovative transportable shelter to the resource industries, ATCO's pursuit of excellence has taken it into energy services, resource development, real estate activity and electric and natural gas utilities.

In manufacturing, ATCO is the world leader in sales and leasing of industrial housing. Other products include community and commercial structures, metal buildings and metal components.

In resource development, ATCO's interests embrace petroleum exploration and production and natural gas processing and marketing, while energy services include contract drilling, well servicing and the supply of oilfield equipment.

ATCO's real estate activities range from property development and management to commercial and industrial construction.

In utilities, ATCO is a major participant in the generation and distribution of electricity and the production and distribution of natural gas.

This broad base of activities provides the financial stability vital to further progress. Through the commitment of more than 6,500 employees worldwide, ATCO challenges the future with imagination and expertise.

From left to right: C.S. Richardson, Senior Vice President, Finance, ATCO Ltd.; N.W. Robertson, President and Chief Operating Officer, ATCO Ltd.; R.D. Southern, Deputy Chairman and Chief Executive Officer, ATCO Ltd.; and J.D. Wood, President and Chief Operating Officer, Canadian Utilities Limited.

Executive Report to Shareholders

Improving business conditions and innovative management programs combined to produce substantially better results for the ATCO Group of Companies for the year ended March 31, 1985.

Earnings before preferred share dividends increased to $44,685,000 on total revenue of $1,644,663,000 compared with the previous year's earnings before preferred share dividends of $18,533,000 on total revenue of $1,610,339,000. After payment of preferred share dividends of $33,343,000, net earnings attributable to Class I and Class II shares were $11,342,000, or 51 cents per share, compared with a loss of $3,171,000 or 16 cents loss per share in 1984. The weighted average number of shares outstanding for 1985 was 22,164,344 compared with 19,304,544 last year.

A new management initiative, the monthly performance review meeting, which involved the setting of goals and the monitoring of performance by management from around the world, helped produce these results. Concurrent with the adoption of this approach, the traditional ATCO activities were organized into three areas of endeavor, each with its own president.

The three areas are: Manufacturing/Leasing worldwide, K.B. Purdie president; Energy Services worldwide, J. Hlavka president; and Real Estate Development worldwide, O. Steiner president. Prior to these changes there were several upper management changes in Canadian Utilities. All of these moves combine to shorten the decision-making process substantially.

Cash decreased by $35.4 million during 1985. The majority of the decline resulted from the repayment of long term debt with the cash proceeds of 1984 financing. Lines of credit are available to more than replace this cash, if necessary.

As the year progressed, most Canadian activities benefited from the general optimism resulting from the election of a new Federal Government, the announced phase-out of the National Energy Policy and the Alberta Provincial Government's proposal to reduce royalties on gas and oil production and increase royalty tax credits.

In manufacturing, ATCO increased its share of the industrial housing leasing market through the purchase of the lease fleet assets of two major western Canadian competitors. With new manufacturing sales slow during most of the year, the Corporation adopted a strategy of emphasizing the leasing of its large inventory of transportable structures. Custom orders, such as the supply of modular panels for exhibitors' pavilions at Expo '86 in Vancouver, did produce modest levels of manufacturing activity during this period.

Although the United States energy industry remained depressed because of softening prices for gas and oil, ATCO's United States industrial housing leasing activities grew substantially because of a series of contracts received for a major project in Wyoming.

In the southern hemisphere, ATCO Australia had a good year with widespread acceptance of its new solid-core laminated panels used in the manufacture of industrial housing products.

ATCO Saudi Arabia Ltd. had another excellent year dominated by a fast delivery of housing for 19 missile bases. This housing was successfully installed in just four weeks.

Canadian Utilities' earnings increased as a result of improved efficiency and higher returns from non-utility operations. Restraint programs limiting capital expenditures and personnel levels remained in effect throughout the corporation.

In the resource service sector, redeployment of capital equipment to more favorable locations continued, with a drilling rig and two service rigs being moved from the United States to Australia, where ATCO-APM Drilling Pty. Ltd. had a most successful year. In

New management techniques, reorganization and a better business environment increased profits.

addition, a United States rig was moved to Canada and converted to the first self-propelled rig designed specifically for pad drilling on heavy oil developments.

ATCO's real estate portfolio, which is located entirely in Alberta, maintained its remarkable record for high occupancy. The Construction Division has been working on the development of a large building on a strategically-located site in downtown Calgary. The project will proceed as tenant commitments are received. The Construction Management Division of ATCO Development was responsible for one of the city's largest building projects of 1984-85, an extensive hangar expansion at the Calgary International Airport.

During the year, a number of floating rate loans were converted to fixed rates of interest thereby reducing the Corporation's exposure to higher costs from increasing interest rates.

Also completed, through a wholly owned subsidiary, was the private placement of $150 million in floating-rate preferred shares. The proceeds of this issue were used to repay debt incurred for acquisition of the controlling interest in Canadian Utilities. As a result of this financing, this investment is now self-sustaining on a cash basis. In November, the Corporation sold privately $50 million of 9.3% cumulative redeemable preferred shares.

The Board continued the payment of dividends of five cents per share per quarter on Class I and Class II shares during 1985.

A number of senior executives undertook new or additional duties during the past year. At its meeting of August 14, 1984, the Board of Directors appointed R.D. Southern as Deputy Chairman of the Board and Chief Executive Officer and N.W. Robertson as President and Chief Operating Officer of ATCO Ltd. G.P. Kiefer, who has filled many key roles in the Corporation has been appointed Senior Vice President, Special Projects for ATCO Ltd.; C.A. Whiteside as President, U.S. Manufacturing/Leasing; and A.J. Pullman as Vice President, Controller, ATCO Ltd. J. Todd recently assumed the position of Managing Director of the Australian group of companies.

Canadian Utilities recently appointed C.S. Richardson as Chief Financial Officer, a role he undertakes in addition to his position as Deputy Chairman of the Board of Directors of Canadian Utilities and Senior Vice President, Finance for ATCO Ltd. C.O. Twa was appointed Senior Vice President and General Manager of Alberta Power Limited.

It is with deep regret that we report the sudden death of George W. Hull, President of ATCO Saudi Arabia Ltd., in a fire on February 13th at his home in Dammam, Kingdom of Saudi Arabia. Mr. Hull had been a valued employee of ATCO since 1973 and served as a director of ATCO Saudi Arabia Ltd. and InterATCO B.V.

In reviewing the past year, it is evident that the Group has established considerable upward momentum in its performance. Most encouraging is the broad-based nature of this momentum with no individual business segment dominating the improvement. Indications are that this trend will continue during 1986.

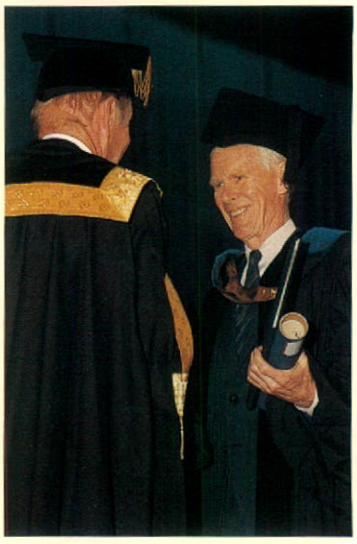
Our thanks to the many dedicated employees of the Corporation worldwide who have been instrumental in effecting the considerable improvement in this year's performance. Our customers and suppliers also continue to make an important contribution to the Corporation's success, for which we are grateful. Further, the wise counsel and service of our Board of Directors has been invaluable throughout the year. Special appreciation is extended to our shareholders whose support during the economic downturn was so vital.

On behalf of the Board of Directors,

R.D. Southern
Deputy Chairman and
Chief Executive Officer

Monthly meetings of senior ATCO executives from around the world, photo far left, were held throughout the year. Management programs and strategies developed and monitored at these meetings brought substantially improved results.

Dr. C.N. Simpson, a member of ATCO Ltd.'s Board of Directors and President of C. Norman Simpson Consultants Limited of Vancouver, received an honorary doctorate, photo on right, at the recent convocation of the Technical University of Nova Scotia. Presenting the degree is Dr. J. Joudrey, chancellor.



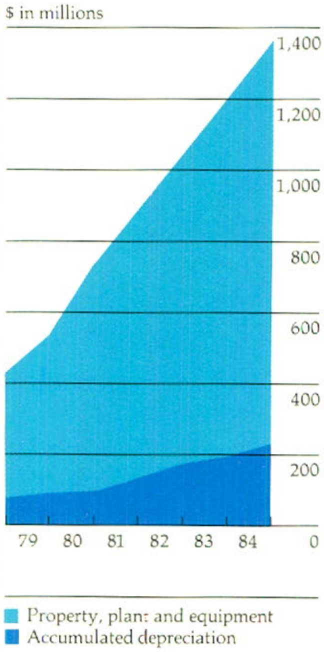
Alberta Power prepared for future customer needs through capital investment of $147.7 million.

1. Utilities

Increased efficiency, resulting from the ongoing review of operational methods and staffing, proved a significant factor in the growth of Canadian Utilities Limited. Earnings for CU, in which ATCO Ltd. holds the controlling interest, were $101.4 million ($1.87 per share) in calendar 1984 compared with $87.1 million ($1.62 per share) for the previous year.

Since Canadian Utilities' fiscal year corresponds with the calendar year, where 'this year' and 'last year' are mentioned in the following report, these references are to calendar years 1984 and 1983, respectively.

Electric power operations – property, plant and equipment



Electric Operations

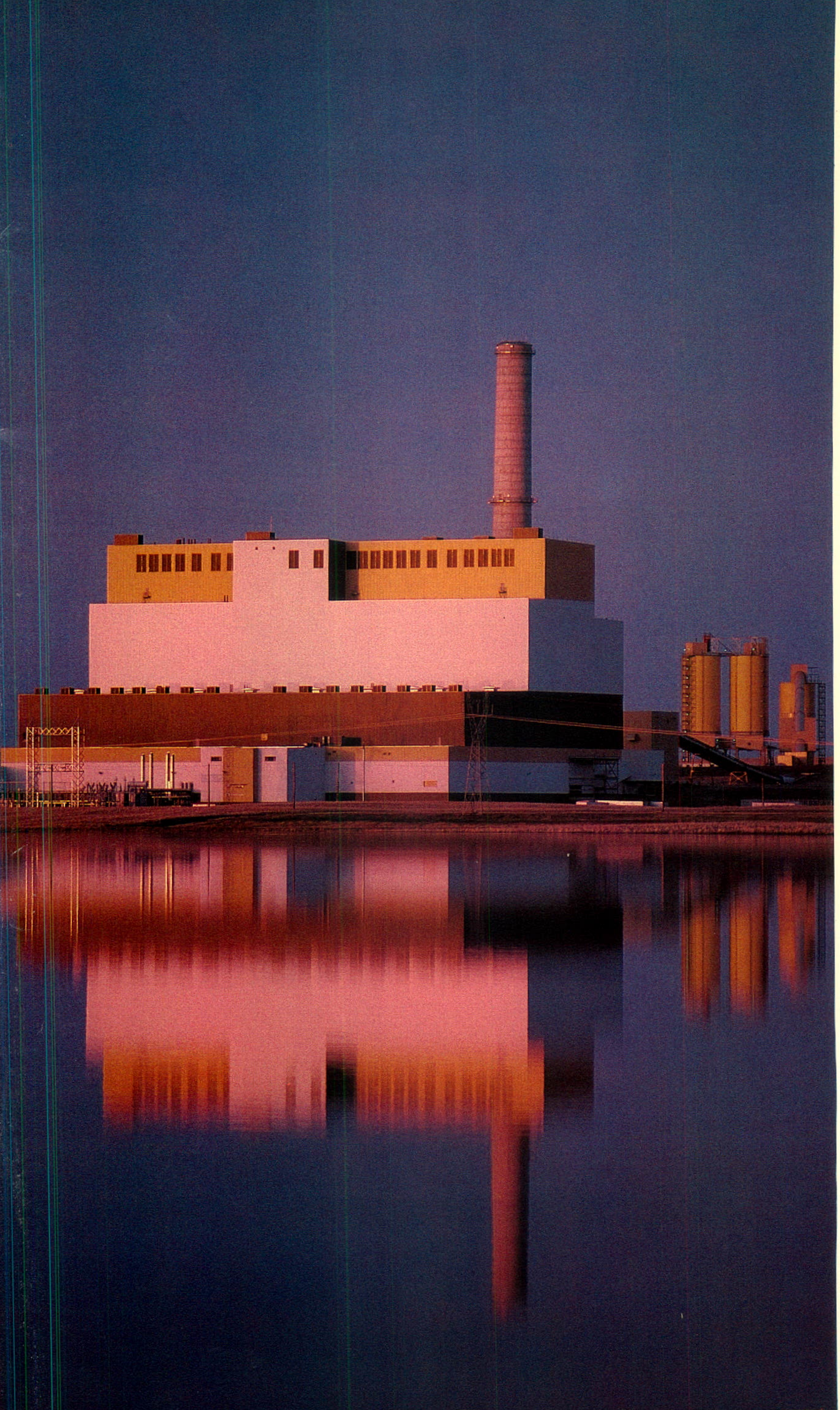
Responding to forecasts by the Alberta Electric Utilities Planning Council of slower growth in provincial electrical demand, the Energy Resources Conservation Board has ordered a further delay in commissioning the second unit of the Sheerness Generating Station. Alberta Power Limited, Canadian Utilities' largest subsidiary, and TransAlta Utilities Corporation, are partners in this $1 billion project, the first unit of which is to be commissioned in January 1986.

The past year saw a significant increase in energy generated. Energy sales to retail customers climbed 7.3% to 3,882 million kilowatt hours while the peak load increased to 741 megawatts in 1984 from 720 megawatts in the previous year. Substantial bulk sales were made to the City of Edmonton under a unit power agreement and to TransAlta Utilities under the province-wide system of economic dispatch.

Alberta Power earnings improved modestly, growing from $61.3 million to $62.9 million, while the company continued operating on a rate of return approved in 1983. Contributing to the increase in earnings was Alberta Power's stringent control of operational and capital expenditures. As a result, employment remained virtually unchanged despite the addition of 3,511 new retail customers.

Capital expenditures totalled $147.7 million during the year, with the largest amount, $91.6 million, being for the Sheerness Generating Station and related facilities.

An investment of $25.5 million was made in transmission projects including a 103-kilometre, 240-kilovolt line from Louise Creek to Mitsue; and a 46-kilometre, 144-kilovolt line from Flyingshot to Beaverlodge.



Commissioning of the first unit of the Sheerness Thermal Generating Station in central Alberta, photo left, is planned for January 1986. The project, owned jointly by Alberta Power and TransAlta Utilities, was delayed because of lower projections of growth in the demand for electricity.

Electrical transmission lines, photo far left, were extended in several areas of Alberta, involving a capital expenditure of $25.5 million.

The transmission of natural gas to industrial plants, photo right, is a growing part of the activities of Canadian Western Natural Gas and Northwestern Utilities. Transportation of gas for industrial customers increased by 6.1 petajoules during the year.

The efficiency of natural gas as a fuel for large motor fleets has resulted in further conversions during the past year. Among the advantages are lower cost than alternative fuels, pollution-free burning, longer engine life and relative safety. Bob Opelt refuels a Northwestern Utilities' fleet vehicle, photo far right. The company pioneered fleet conversion programs in Canada and has made important technological advances.

Natural Gas Operations

Canadian Utilities supplies Alberta with natural gas through two subsidiaries: Canadian Western Natural Gas Company Limited, which serves the southern part of the province, and Northwestern Utilities Limited, which serves the northern half of the province.

These operations recorded a significant increase in profits in the past year, improving from $26.2 million in the previous year to $34.2 million. Contributing to increased earnings was the reduced price for gas purchased.

The total number of natural gas customers increased by 2.2% to 593,558. Part of this growth resulted from the purchase of Lloydminster Gas Company Limited which was subsequently amalgamated with Northwestern Utilities.

After taking into account the effects of weather and rate changes, earnings from gas operations were consistent with the rate of asset growth and changes in the cost of capital.

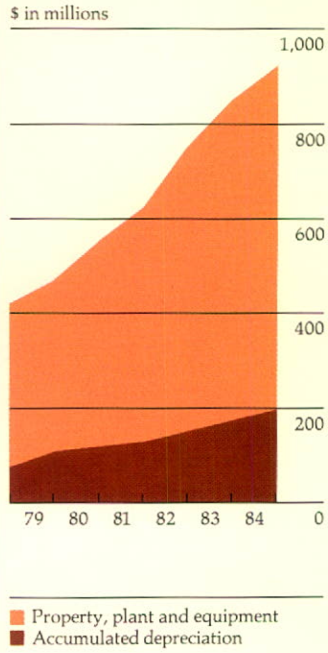
Both Canadian Western and Northwestern transport gas within Alberta for industrial users and other companies. The total natural gas sold and transported increased to 470.5 petajoules (PJ), from 450.9 PJ in 1983. Sales to residential and commercial customers increased by 7.9 PJ due to colder temperatures than in 1983. However, average temperatures within Northwestern's service area during both 1983 and 1984 were 4% warmer than normal while temperatures in Canadian Western's service area were 5% warmer than normal in 1984 and 6% above normal in 1983.

Because of reductions in the Federal Natural Gas Liquids Tax and lower sales to power plants and industrial users, revenue from natural gas operations declined by $67.2 million to $861.2 million. This decline was more than offset by a reduction of $83.9 million in operating expenses, down to $791.6 million. Also declining were taxes paid to all levels of government. These decreased by $97.2 million to $134.3 million, or 15.6% of total revenue compared with 24.9% in 1983.

Capital additions totalled $72.9 million, a major expenditure being the development of salt cavern storage facilities near Fort Saskatchewan, Alberta. Two caverns were commissioned during 1984 and three more are under development.

Although moderate growth in the gas utilities is forecast for the short term, significant future expansion is anticipated as a result of energy developments at Cold Lake, Lloydminster, Fort McMurray and Peace River.

Natural gas operations – property, plant and equipment



Successful cost control programs and increased productivity resulted in higher earnings for the Utilities Group.

Cash flow generated by production activities contributed to an improvement in ATCOR's net earnings.

2. Resources

A subsidiary of Canadian Utilities Limited, ATCOR Resources, is involved in gas and oil exploration and production, natural gas processing and gas marketing to large-volume industrial users. Both ATCO Ltd. and ATCOR hold an equity interest in AT&S Exploration Ltd., which is engaged in exploration on Canada Lands.

Because ATCOR's fiscal year corresponds with the calendar year, references to 'this year' and 'last year' in the Exploration and Production and Gas Processing and Marketing sections refer to calendar 1984 and 1983, respectively.

Wholly owned ATCO subsidiaries are involved in contract drilling and well servicing in Canada, the United States and Australia, and a Canadian subsidiary sells and rents oilfield equipment.

Exploration and Production

ATCOR participated in the drilling of 102 wells during the past year with 48 being completed as oil wells and 22 as gas producers. Total investment in exploration and production was $22.3 million. Because of this good success ratio, the company plans to take a larger net working interest in future drilling programs.

Oil production averaged 260 cubic metres per day, while average daily production of natural gas was 125,128 cubic metres. A strategy to accelerate the growth of gas reserves has been adopted, with 60% of the exploration and development budget for the next two years devoted to the search for natural gas.

AT&S Exploration Ltd. was formed in September 1983 with the objective of exploring for gas and oil on lands under federal government jurisdiction. The joint exploration company is owned 30% by ATCOR Resources Limited, 7½% by ATCO Ltd., 25% by Texaco Canada Resources Ltd. and 37½% by Sun Life Assurance Company of Canada.

By year end, AT&S had participated in the drilling of two oil discoveries and one dry hole while six additional wells were in various stages of drilling and testing. AT&S has earned an approximate 3% interest in the Gulf-operated East Amauligak J-44 gas and oil discovery in the Beaufort Sea. This well is considered the most significant discovery in the Canadian Beaufort Sea to date. Delineation drilling will be necessary to ascertain the magnitude of the reserves related to this discovery.

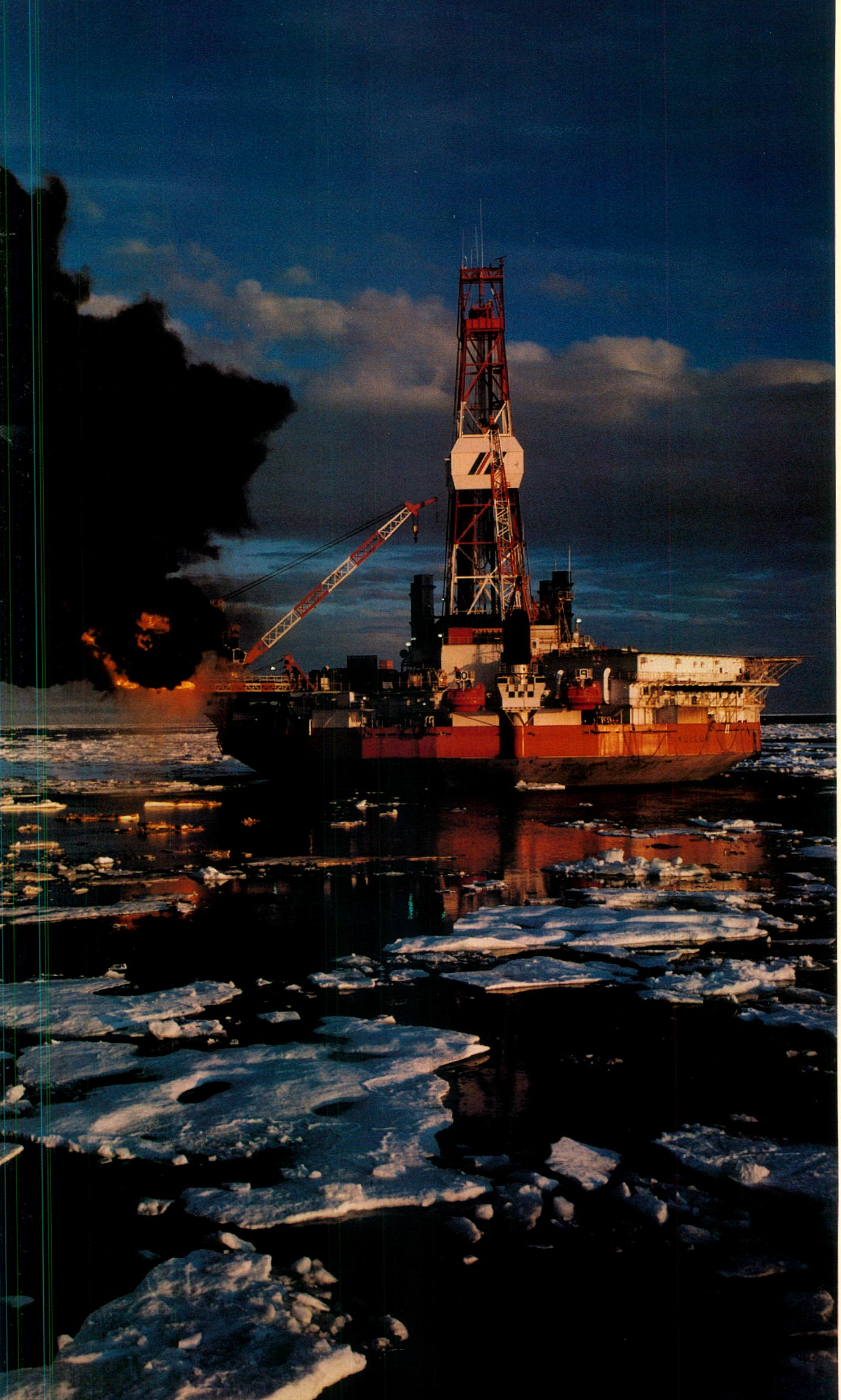
The second oil discovery was the Beaufort Sea Tarsiut P-45 well drilled by Gulf in which AT&S earned a 6.5% interest. The well, a delineation follow-up of earlier Gulf discoveries in the area, extended the known productive areas.

AT&S Exploration has earned, or has the right to earn, interests in more than 5.6 million gross hectares of land. Exploration plans for these lands are being re-evaluated in light of recently announced changes in federal energy policy.

Gas Processing and Marketing

ATCOR distributed record volumes of natural gas during 1984 to both the fuel and feedstock industries and to resource companies for enhanced oil recovery. 76 petajoules of natural gas were marketed to 16 clients during the year, a significant increase over the 52 petajoules sold to 14 customers in 1983. The gas was purchased from 42 producers.

The Edmonton extraction plant, in which ATCOR has a 50% interest, processed a daily average of 5.9 million



This ethane extraction plant in Edmonton, photo far left, is 50% owned by ATCOR Resources Limited. Two additional natural gas liquids recovery plants are planned by ATCOR for the Carbon and Joffre areas of east-central Alberta.

AT&S Exploration Ltd., a joint exploration company involving ATCOR Resources Limited and ATCO Ltd., is a participant in a Beaufort Sea discovery well, photo left, capable of producing 2,160 cubic metres of light crude a day. The well, Amauligak J-44, is the largest find in the Beaufort.

Demand for well servicing, photo far right, has increased in Canada with the revitalization of western Canada's gas and oil industry.

ATCO Drilling's newly developed self-propelled rig, photo right, for heavy oil pad drilling is the first of its kind in Canada. Its efficiency gives the company a competitive edge in obtaining contracts for major heavy oil developments.

cubic metres of natural gas during 1984. While this is below the plant's capacity of 8.9 million cubic metres per day, agreement has been reached with a third party to process, on a fee basis, additional volumes of natural gas over the next ten years. This contract will increase processing activities to near capacity.

During 1984, the plant recovered a daily average of 651 cubic metres of ethane and 200 cubic metres of LPG's (propane, butanes and pentanes-plus) for ATCOR's account. Ethane is sold to the petrochemical industry on a cost-of-service basis, and LPG's are marketed in Canada and the United States at prevailing prices.

ATCOR is developing plans for the possible construction of two natural gas liquids recovery plants in the Carbon and Joffre areas of east-central Alberta. Capital costs are projected at $35 million.

Contract Drilling

In order to maximize asset utilization and respond to operational needs in each country, drilling and well servicing subsidiaries in Canada, the United States and Australia are now managed by ATCO Energy Services.

At year end, 31 drilling rigs were located in Canada, 24 in the United States and 4 in Australia. In addition, ATCO/Equtak Drilling Ltd., a joint venture with the Inuvialuit, operated a rig in northern Canada.

In Canada, drilling and exploration activity increased significantly because of the improved financial health of the petroleum industry and optimism based on changes in government energy and taxation policy. ATCO's rig utilization averaged over 50%, a considerable improvement from the 40% of the previous year. As a result of the improved utilization, operating rates began to firm as the year progressed.

A self-propelled pad drilling rig has been developed, giving ATCO Drilling a competitive edge in obtaining contracts for major heavy oil developments in western Canada. The rig, originally of conventional design, was transferred from the United States and modified with innovative features that reduce down-time and operating costs.

Activity in the United States gas and oil industry remained slow because of depressed world oil prices and excess natural gas production; however, ATCO's rig utilization compared favorably with industry levels.

A strong market helped ATCO-APM Drilling Pty. Ltd. to record its best performance since inception. Projections that Australian self-sufficiency in oil production may be jeopardized in the next decade are expected to spur greater exploration activity. To capitalize on this potential, another drilling rig was moved to Australia from the United States and further transfers are being contemplated.

Well Servicing

Two well servicing rigs were moved to Australia from the United States during the year, bringing the total to 3 in that country, 15 in Canada and 15 in the United States. The Well Servicing Division improved its market share in all three countries. Utilization in Canada and the United States was comparable to industry-wide levels, while in Australia, ATCO-APM achieved above average utilization and established itself as the industry leader.

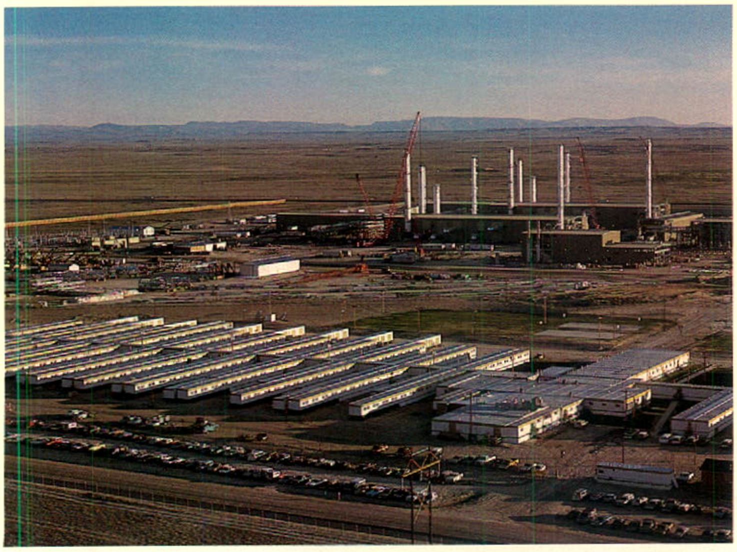
Oilfield Equipment Rentals and Sales

Increased oilfield activity resulted in improved levels of business for the Canadian-based sales and rental operation. Favorable asset utilization rates, good service and low overhead combined to generate satisfactory earnings.

Utilization of ATCO's rigs in Canada increased substantially, while in Australia, ATCO-APM had a record year.

Protection of the environment was a major priority in the design of three camps for crews double tracking CP Rail's main line in the Rogers Pass area. Two of the camps, including that pictured on the right, are located in Glacier National Park within a short distance of the Trans-Canada Highway.

A major lease contract involved the provision of housing for 2,800 workers on Exxon's gas processing project in Wyoming. The largest camp, at Shute Creek, photo far right, includes dormitories, kitchens and support facilities.



Internationally, ATCO maintained its position as the world leader in the supply of industrial housing.

3. Manufacturing

The Corporation first achieved international prominence as a manufacturer of modular transportable shelter for the energy and resource industries. Today, ATCO remains the world leader in the supply of industrial housing, providing accommodation for personnel and equipment around the globe.

Metal fabrication products include metal buildings and various metal components for a wide array of applications in the agricultural, resource development, commercial and industrial fields.

Industrial Housing

In response to market demand, ATCO is increasing its emphasis on the leasing of shelter products. To further strengthen its presence in Canadian leasing, ATCO, during 1985, acquired the lease assets of competitors in Edmonton, Vancouver and Sarnia.

The past year's largest lease contract involved the provision of housing for 2,800 workers on Exxon's gas processing project in Wyoming. The scope of work included housing, engineering, site preparation and installation. Another major lease contract called for the supply of camp facilities for 1,200 workers employed on CP Rail's double tracking project at Rogers Pass in the Canadian Rockies. Further orders were received from contractors working on the railway's main line through the Selkirk Mountains.

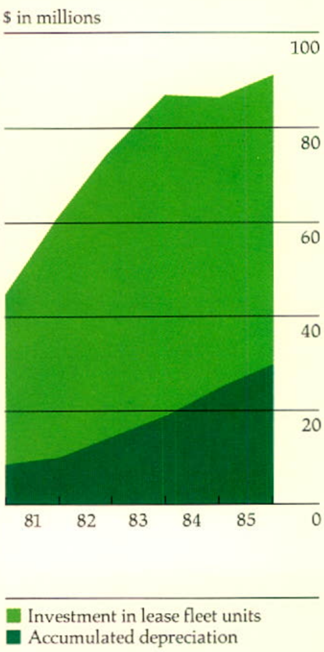
In addition, two camps were leased to house 460 workers expanding Esso Resources' Cold Lake heavy oil production facilities.

In eastern Canada, major commercial and industrial projects brought about a resurgence in site office rental activity. The Corporation also received an order to supply, on a lease basis, housing for 440 workers, together with a major office complex for a gold mine development near Hemlo, Ontario.

A unique $8 million contract for Expo '86 in Vancouver involved the manufacture of modular wall and roof panels for exhibitors' pavilions. Modular construction was necessary to facilitate relocation of the pavilions throughout British Columbia at the conclusion of the exposition.

A shortage of accommodation in North American correctional institutions has opened a new market for ATCO's transportable lease fleet. The versatility of ATCO's modular units and their availability on short notice make this form of accommodation increasingly popular with the authorities.

ATCO's transportable lease fleet provides a major contribution to corporate revenues

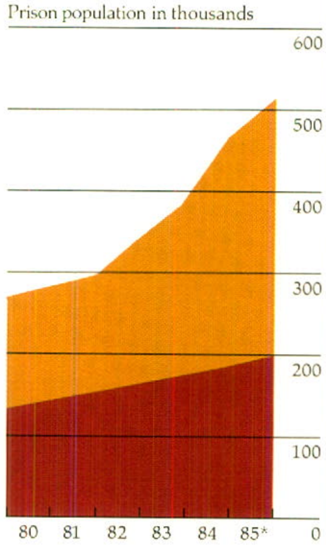


In Saudi Arabia, the highlight of the year was a sizeable order which again tested ATCO's ability to react to expedited delivery schedules. Accommodation for 1,200 workers at 19 missile bases was supplied and installed in just four weeks. The major part of the order was manufactured in ATCO's Saudi Arabia plant with some specialized units coming from the Waco, Texas facility.

Another major project involving ATCO International and ATCO Saudi Arabia was a 384-man turnkey camp for use at the Qassim refinery complex.

ATCO International's Waco factory was busy early in the year manufacturing camp facilities destined for Al Qurna, Iraq. The contract, awarded by the U.S.S.R. agency Technoexport, called for facilities to serve 2,500 men. Another major international contract was a $9 million housing order to support construction crews working on a fertilizer complex for the National Nitrogenous Fertilizer Company of Nigeria.

Prison overcrowding stimulates emerging prefabricated housing market in the U.S.



■ Prison population–State and Federal
■ Rate of incarceration

*Estimate

Sources: Report to the Nation on Crime and Justice—The Data NCJ—87068 Corrections Today, published by the American Correctional Association, June 1985.

In Australia, ATCO's factories completed the $10 million industrial housing contract for the Argyle Diamond Mine development in Western Australia.

Widespread acceptance of the solid-core laminated panel units introduced last year resulted in the Adelaide plant being totally converted to this product.

The dramatic recovery of the Australian housing industry was reflected in the doubling of production of transportable homes at ATCO's Adelaide plant.

Metal Fabrication

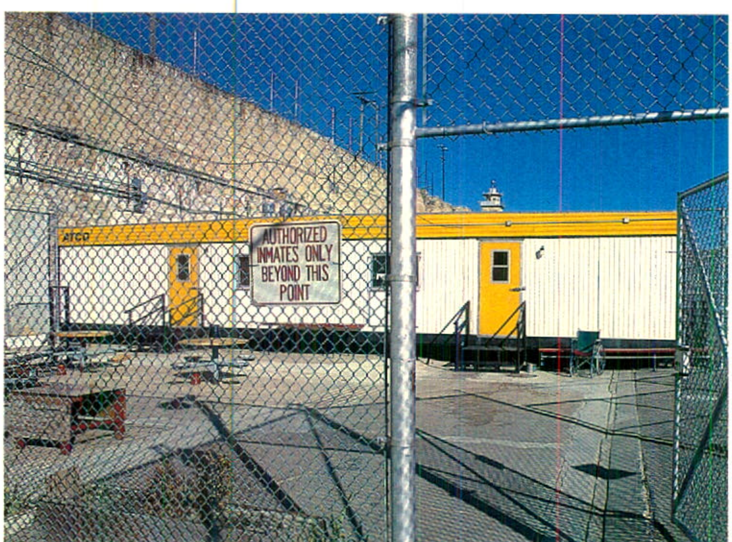
Through an expanded dealer network, ATCO Metal in Calgary is solidifying its position as western Canada's largest manufacturer of pre-engineered buildings. The major project undertaken during 1985 was the supply of a 4,100 square metre building in Calgary for Prudential Steel Ltd.

ATCO Metal entered 1986 with a large backlog of orders. Included are seven buildings for Esso Resources' Cold Lake heavy oil facility, a 5,000 square metre plant for Western Co-operative Fertilizers Limited, an 8,000 square metre building for the Container Port of Alberta Research Corporation in Edmonton and a 2,880 square metre maintenance facility for Manalta Coal Ltd.'s Montgomery mine, which supplies Alberta Power's Sheerness Generating Station.

As resource development activity expands, demand will increase for the division's unique Fold-A-Way metal buildings that can be erected in as little as 24 hours and do not require permanent foundations.

In Australia, the Salisbury metal fabrication facility was closed, but sales of Supertruss metal buildings continued with enhanced profitability through subcontracted manufacturing.

In North America, ATCO shifted its primary emphasis from manufacturing to leasing of shelter products.



All exhibitors' pavilions at Vancouver's Expo '86 site contain modular wall and roof panels manufactured by ATCO. In the foreground of this model of the Expo site is the Chinese pavilion; in the background, the 17-storey geodesic sphere, Expo Centre.

Modular units from ATCO's lease fleet are being utilized at Old Max correctional facility in Colorado, photo far left.

During the past year, a Metropolitan Store was added to ATCO's TowerLane Mall in Airdrie, photo far right. The Mall now offers comprehensive shopping to residents of Airdrie and surrounding communities.

ATCO Development's most significant project during the past year was designing and building an expansion of Pacific Western Airlines' hangar at Calgary International Airport, photo right. The project will be completed by July 1985.

Occupancy of 93% distinguishes ATCO's commercial real estate portfolio and a major building is planned for Calgary.

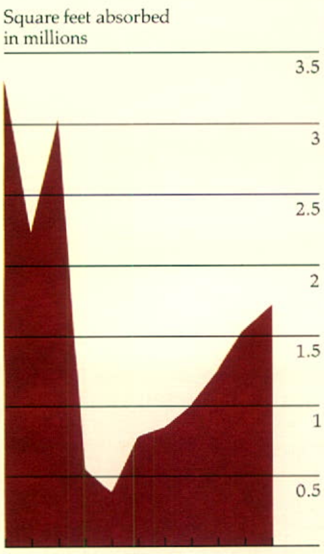
4.

Real Estate

The Corporation's real estate expertise ranges from property acquisition and design and construction management to property management, sales and leasing. These skills are applied to commercial real estate being developed for investors and partners as well as for ATCO's portfolio.

ATCO is a partner in ALDC Partnership which holds for future development an attractive inventory of commercial and residential land in Alberta.

Office space absorption in downtown Calgary continues to improve



*Estimate

Property Development

Despite an over supply in the market, the Corporation continues to enjoy a high level of occupancy in its commercial buildings. The ATCO portfolio includes Place 800 and Canadian Western Centre in Calgary, Canadian Utilities Centre and the Milner Building in Edmonton, and TowerLane Mall in Airdrie. Occupancy is 93%.

Expansion of TowerLane Mall and development of an industrial building in Airdrie are planned for next year.

Early development is planned for a strategically-located commercial site at Fourth Avenue and Second Street Southwest in downtown Calgary which is owned by a partnership headed by ATCO. Tenant commitments are being sought for a 75,000 square metre building featuring a prestigious design that will make it a landmark in the city's business district.

The 11,000 square metre second phase of Canadian Western Centre could follow closely behind the Fourth Avenue project if recent tenant interest continues.

Construction Management

General contracting, project management and interior finishing have been handled by ATCO Development's Construction Division. ATCO's most significant contract during the past year was a hangar expansion for Pacific Western Airlines at Calgary's International Airport. The project is expected to be completed in July 1985.

Property Management

In addition to the day-to-day operation of ATCO's real estate portfolio, ATCO's Property Management Division operates buildings for other investors. Efforts are underway to expand this activity through the provision of a superior service at a competitive cost.

Place 800 in downtown Calgary, part of the ATCO real estate portfolio, has been fully occupied since its completion in 1980. The ATCO portfolio of office buildings also includes Canadian Western Centre in Calgary, Canadian Utilities Centre and the Milner Building in Edmonton.

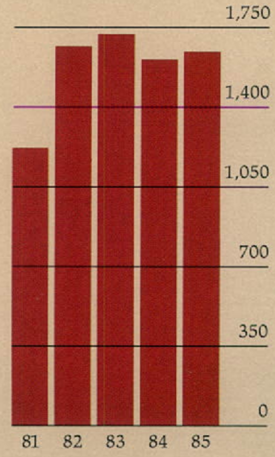
Consolidated Statement of Operations and Retained Earnings

Years ended March 31

(Thousands of Canadian dollars)	Note Reference	1985	1984
Revenues	10	$1,644,663	$1,610,339
Costs and expenses			
Natural gas supply		525,447	517,674
Taxes—other than income	11	113,136	182,955
Operating and maintenance		455,502	414,446
Selling and administrative		113,415	117,428
Depreciation, depletion and amortization		105,764	94,007
Interest	12	56,164	62,182
		1,369,428	1,388,692
		275,235	221,647
Income taxes			
Current		110,133	94,457
Deferred		(1,914)	(7,670)
	14	108,219	86,787
		167,016	134,860
Minority Interests	6	122,331	116,327
Earnings for the year		44,685	18,533
Dividends on redeemable preferred shares	8	33,343	21,704
Earnings (loss) attributable to Class I and Class II shares		11,342	(3,171)
Retained earnings at beginning of year		140,935	150,864
		152,277	147,693
Dividends on Class I and Class II shares		4,433	3,861
Share issue expenses, net of income taxes		—	1,604
Exchange adjustments on preferred shares	8	1,039	1,293
Retained earnings at end of year		$ 146,805	$ 140,935
Earnings (loss) per Class I and Class II share		$.51	$(.16)
Dividends paid per Class I and Class II share		$.20	$.20

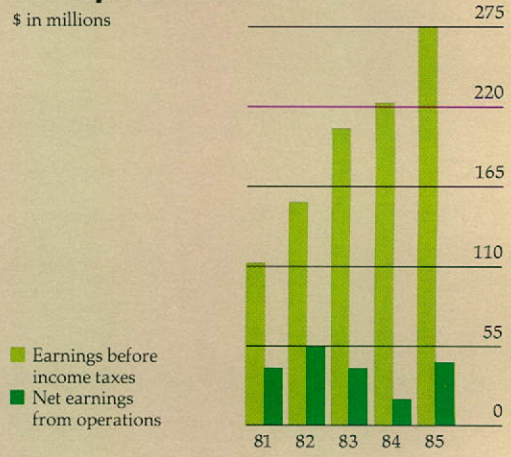
Revenue

$ in millions



Earnings from operations

$ in millions



Consolidated Balance Sheet

March 31

(Thousands of Canadian dollars)	Note Reference	1985	1984
Assets			
Current assets			
Cash and short term deposits		$ 62,893	$ 108,583
Accounts receivable		191,505	190,127
Inventories		41,312	30,975
Prepaid expenses		7,444	6,281
		303,154	335,966
Investment in real estate development	4	92,675	96,530
Investments in other companies	3	294,914	244,152
Property, plant and equipment	5	2,177,026	2,030,791
Goodwill		133,275	138,651
Deferred financing charges and other assets		35,335	35,967
		$3,036,379	$2,882,057
Liabilities and Shareholders' Equity			
Current liabilities			
Bank indebtedness		$ 2,545	$ 12,844
Accounts payable and accrued liabilities		236,282	239,960
Income taxes payable		25,571	16,825
Long term debt due within one year		22,713	15,521
		287,111	285,150
Debt on real estate development	4	87,938	83,324
Long term debt	7	683,828	780,039
Contributions for extensions to utility plant		173,329	158,180
Deferred credits		49,103	39,212
Deferred income taxes		14,877	16,378
Minority interests	6	1,078,971	1,056,356
Redeemable preferred shares	8	457,074	261,420
Class I and Class II shareholders' equity			
Class I and Class II shares	9	61,120	61,063
Retained earnings		146,805	140,935
Foreign currency translation adjustments	2	(3,777)	—
		204,148	201,998
		$3,036,379	$2,882,057

Approved by the Board:

N.W. Robertson

Director

Director

Financial Review

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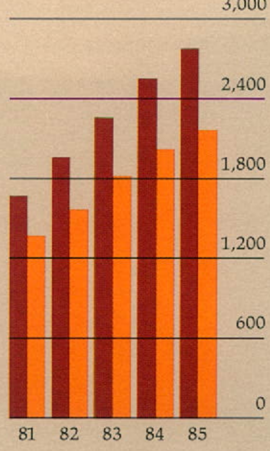
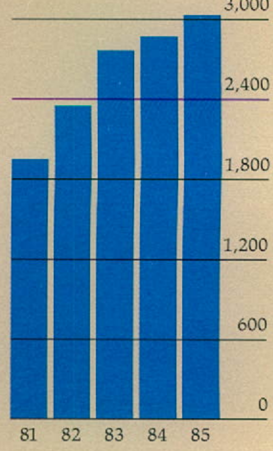
Property, plant and equipment
$ in millions



Cost
Net book value

Total assets
$ in millions



Management's Responsibility for Financial Reporting

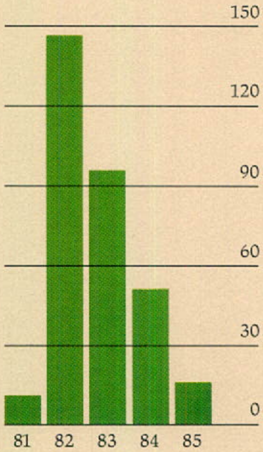
Management is responsible for the preparation of the consolidated financial statements and other financial information relating to the Corporation contained in this annual report. The consolidated financial statements have been prepared in conformity with Canadian generally accepted accounting principles and necessarily include some amounts that are based on informed judgements and best estimates of management.

Price Waterhouse, our independent auditors, are engaged to express a professional opinion on the consolidated financial statements. Their examination is conducted in accordance with generally accepted auditing standards and includes tests and other procedures which allow the auditors to report on the fairness of the consolidated financial statements prepared by management.

The Board of Directors, through an audit committee comprised of three non-management directors and one management director, oversees management's responsibilities for financial reporting. The Audit Committee meets regularly with management, the internal auditors and the independent auditors to discuss auditing and financial matters and to gain assurance that management is carrying out its responsibilities. The internal auditors and the independent auditors have full access to the Audit Committee.

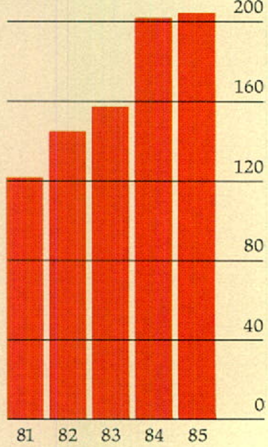
Working capital

$ in millions



Class I and Class II shareholders' equity

$ in millions



Consolidated Statement of Changes in Financial Position

Years ended March 31

(Thousands of Canadian dollars)	Note Reference	1985	1984
Cash provided by operating activities			
Earnings for the year		$ 44,685	$ 18,533
Charges (credits) not affecting cash			
Depreciation, depletion and amortization		105,764	94,007
Deferred income taxes		(1,914)	(7,670)
Minority interests		122,331	116,327
Allowance for equity funds used during construction		(16,549)	(14,560)
Other		2,041	(846)
Increase in working capital*		(7,810)	(3,763)
		248,548	202,028
Dividends			
Redeemable preferred shares	8	33,343	21,704
Class I and Class II shares		4,433	3,861
Minority interests		97,186	94,103
		134,962	119,668
Cash remaining for investment		113,586	82,360
Investment			
Property, plant and equipment		226,750	282,683
Real estate development		(285)	11,128
Other companies	3	50,762	—
Deferred credits		(8,991)	(1,109)
Other		—	(1,697)
		268,236	291,005
Cash deficiency before financing		154,650	208,645
Financing			
Issue of long term debt		122,185	62,253
Reduction in long term debt		(209,750)	(102,112)
Issue of debt on real estate development		67,897	49,533
Reduction in debt on real estate development		(64,062)	(20,990)
Issue of shares by Canadian Utilities			
Class A and Class B		—	3,816
Preferred, net of redemption		—	98,880
Issue of shares by the Corporation			
Class I and Class II	9	57	53,504
Preferred	8	200,000	—
Redemption of preferred shares		(9,194)	(36,273)
Financing and share issue expenses		(5,706)	(7,971)
Contributions for extensions to utility plant		20,353	25,578
Release of deposits		—	21,590
Other		(2,521)	—
		119,259	147,808
Decrease in cash*		$ 35,391	$ 60,837

*For the purpose of this statement, working capital does not include long term debt due within one year or cash, which is defined as cash and short term deposits less bank indebtedness.

Notes to Consolidated Financial Statements

March 31, 1985

1. Summary of Significant Accounting Policies

Consolidation

The consolidated financial statements include the accounts of ATCO Ltd. and all of its subsidiaries (collectively referred to herein as "ATCO"), which are wholly owned except for Canadian Utilities Limited ("Canadian Utilities"), which is 50.1% owned, and ATCO Saudi Arabia Ltd., which is 75% owned. The operating subsidiaries and divisions are shown on pages 38 to 40.

Investments in joint ventures and partnerships are recorded on the equity basis.

Goodwill is recorded at cost and amortized on a straight line basis generally over 40 years.

Regulation

The accounting records and policies of the utility subsidiaries reflect decisions made by regulatory bodies, principally the Public Utilities Board of Alberta, as part of the rate making process. Decisions made by these regulatory bodies which impact on operating results or accounting policies are reflected in the accounts from the date of decision.

Foreign Currency Translation

The financial statements of the foreign subsidiaries and foreign currency transactions of Canadian companies are translated as follows:

Integrated foreign subsidiaries and Canadian companies with balances and transactions denominated in foreign currency:

Monetary assets and liabilities—at year end exchange rates
Other assets and liabilities, depreciation and amortization—at historical exchange rates
Revenues and expenses, except depreciation and amortization—at exchange rates prevailing during the year

Translation adjustments are recognized in the current year's earnings, except for those arising from translation of monetary assets and liabilities that have an ascertainable life extending more than twelve months beyond the balance sheet date. These adjustments are deferred and amortized over the remaining life of the asset or liability.

Self-sustaining foreign subsidiaries:

Assets and liabilities—at year end exchange rates
Revenues and expenses—at exchange rates prevailing during the year

Translation adjustments are deferred and included in a separate component of Class I and Class II shareholders' equity.

Property, Plant and Equipment

Additions to electric and natural gas utility plant and equipment include an allowance for funds used during construction at a rate approved by the Public Utilities Board for debt and equity funds. Certain of these additions are made with the assistance of cash contributions from customers and governments where the estimated revenue is less than the cost of providing service or where special equipment is needed to supply the customers' specific requirements. These contributions are amortized on the same basis as the assets to which they relate. All other plant and equipment additions are recorded at cost.

Depreciation Methods and Rates Per Annum

	Straight Line	Declining Balance
Electric and natural gas utility plant and equipment	1.5% to 6.4%	
Industrial rental units	10%	
Drilling rigs	6% to 10%	
Replacement drill pipe	25%	
Well servicing rigs	10%	
Other buildings, furniture, fixtures and equipment		5% to 30%

On retirement of depreciable natural gas and electric utility plant and equipment, the accumulated depreciation is charged with the cost of the retired unit less net salvage value.

Included in the natural gas utility subsidiaries' property, plant and equipment are gas wells that have been drilled, tested and capped and remain unconnected to the utility system. The Public Utilities Board has directed that the costs of such wells, including an allowance for funds, be accounted for as plant held for future use. If, after a period of five years, these wells have not been added to the utility system, the costs are written off against funds received under The Natural Gas Price Administration Act. If at a future date a gas well is placed in service or is required to be used, the amount written off will be reinstated in property, plant and equipment.

In accounting for non-regulated gas and oil exploration and development activities, the full cost method is followed whereby all costs relating to the exploration for and the development of gas and oil reserves are capitalized. These costs are depleted by the unit of production method based on estimated proven gas and oil reserves.

Deferred Credits

As Alberta gas producers, the natural gas utility subsidiaries receive a pro rata share of monies available under The Natural Gas Price Administration Act. These monies, net of royalties and income taxes, are included in deferred credits. Subject to the approval of the Public Utilities Board, the costs of unsuccessful gas exploration, net of income taxes, are charged against these deferred credits.

Revenue Recognition

Utility revenues are recognized on the basis of cycle billing and are recorded when customers are billed.

Revenues resulting from the supply of contracted products and services are recorded by the percentage of completion method, except for footage drilling contracts which are recorded when contract depths are attained. Any anticipated loss is provided for in its entirety when the estimated loss is identified.

Inventories

Inventories are carried at the lower of cost or estimated net realizable value.

Real Estate Development

Carrying costs of land held for development and properties under development are capitalized to the extent that the accumulated costs do not exceed the estimated net realizable value of the property. Carrying costs of rental properties under construction are capitalized until the earlier of one year after completion or 75% occupancy, at which time depreciation begins at 2.5% per annum on a straight line basis.

Income Taxes

The utility subsidiaries provide for current income taxes by claiming as deductions for tax purposes only amounts recorded in the accounts. This method is referred to as the "Normalization—All Taxes Paid" method of income tax accounting as approved by the Public Utilities Board.

Deferred Financing Charges

Expenses of issue of long term debt are amortized over the term of the debt and expenses of issue of preferred shares are amortized over the lesser of the expected life of the issue or 30 years.

Other deferred charges are subject to amortization over various periods not exceeding 40 years.

2. Change in Accounting Policy

Effective April 1, 1984, the Corporation prospectively changed its method of accounting for translation of foreign currency transactions and financial statements to conform to the recommendations of The Canadian Institute of Chartered Accountants. Earnings attributable to Class I and Class II shares would have been lower by approximately $1,800,000 had the Corporation continued to use its previous method.

The foreign currency translation adjustments arose as follows:

(Thousands of dollars)	
Translation of April 1, 1984 foreign currency balances of self-sustaining subsidiaries	$ (414)
Translation adjustments during the year	
Working capital	(872)
Non-current assets and liabilities	(2,491)
Balance at March 31, 1985	$(3,777)

3. Investments in Other Companies

(Thousands of dollars)	1985	1984
TransAlta Utilities Corporation	**$244,964**	$244,152
Hydro-Québec bonds	**49,950**	—
Total (detailed below)	**$294,914**	$244,152

TransAlta Utilities Corporation

On December 1, 1982, each Canadian Utilities Series H preferred shareholder was issued a warrant, for each share held, entitling the bearer to purchase one Class A common share of TransAlta owned by Canadian Utilities at a price of $22.25 per share ($24.88 market value at March 31, 1985) on or before November 1, 1987. The investment in TransAlta was acquired at an average price of $18.81 per share. Gains on disposition are recorded as warrants are exercised. During the year, 2,600 warrants were exercised (1984—2,183). As of March 31, 1985, 12,967,117 warrants were outstanding.

The investment in TransAlta consisted of the following:

(Thousands of dollars)	1985		1984	
	Shares	Amount	Shares	Amount
Common shares	**12,967,163**	**$243,889**	12,969,763	$243,938
First Preferred Shares	**352**	**26**	2,852	214
Net carrying costs		**1,049**		—
		$244,964		$244,152

Effective January 1, 1985 the net carrying cost of the TransAlta investment has been deferred and added to the cost of the investment. Included in the deferred amount of $1,049,000 are dividends on the Series H preferred shares net of dividends received from TransAlta and any related interest income. The deferral of these costs increased ATCO's earnings for the year by $525,000.

Hydro-Québec Bonds

The proceeds on the issue of the Series 3 Junior Preferred Shares were invested in $50,000,000 principal value of 12⅜% Hydro-Québec bonds maturing January 3, 1991. These securities have been hypothecated and use of the principal and interest is restricted.

4. Real Estate Development

(Thousands of dollars)	1985	1984
Investment:		
Land held for development	$ 1,392	$ 2,409
Properties under development	7,478	10,021
Canadian Western Centre and Canadian Utilities Centre net of accumulated depreciation	47,710	48,182
Equity in ALDC Partnership	15,385	15,822
Equity in joint ventures	20,710	20,096
	$92,675	$96,530

The Canadian Western Centre in Calgary is occupied principally by Canadian Western Natural Gas Company Limited and the Canadian Utilities Centre in Edmonton is occupied principally by Canadian Utilities and certain of its subsidiaries.

ATCO's share of the joint ventures' and partnership's losses amounted to $2,399,000 (1984 — earnings of $186,000) and is included in sales, rentals and service revenue.

(Thousands of dollars)	1985	1984
Debt related to:		
Properties under development	$ —	$ 762
Canadian Western Centre:		
First mortgage, at 12⅜% to July 31, 1989, at prime plus ½% thereafter, due July 31, 1991	29,943	18,000
Canadian Utilities Centre:		
First mortgage, at 12¼% to July 1, 1989, at prime minus ¼% thereafter, due July 1, 1991	35,914	44,378
ALDC Partnership:		
Bank loan, at prime plus 2¾%, due December 31, 1992, secured by assignment of partnership interest in ALDC Partnership	12,227	10,543
Joint ventures:		
Interim and long term financing on projects, at prime minus ⅛% to prime plus ½%, due at various dates to December 31, 1987, secured by charges on specific joint venture projects	9,854	9,641
	$87,938	$83,324

The minimum annual repayments of debt on real estate development over each of the next five fiscal years are as follows:

(Thousands of dollars)

1986	1987	1988	1989	1990
$251	$4,833	$5,624	$351	$434

5. Property, Plant and Equipment

(Thousands of dollars)	1985		1984	
	Cost	Accumulated Depreciation and Depletion	Cost	Accumulated Depreciation and Depletion
Electric utility plant and equipment	$1,043,197	$242,678	$ 984,184	$204,975
Natural gas utility plant and equipment	918,625	207,646	845,328	183,792
Utility plant construction work in progress	355,348	—	285,187	—
Drilling and well servicing rigs and related equipment	195,740	81,432	199,560	70,049
Rental assets	91,012	30,045	86,303	24,799
Other plant and equipment	42,314	17,442	41,042	15,889
Gas and oil properties	81,689	18,141	50,541	12,826
Deferred gas exploration	20,470	—	24,132	—
Land, buildings and improvements	40,234	14,219	40,304	13,460
	$2,788,629	$611,603	$2,556,581	$525,790
	$2,177,026		$2,030,791	

As explained in the Summary of Significant Accounting Policies, gas wells accounted for as plant held for future use in the amount of $33,093,000 are included in natural gas utility plant and equipment at March 31, 1985 (1984—$27,606,000).

During the year there were no unsuccessful gas exploration costs charged against monies received under The Natural Gas Price Administration Act (1984—$1,761,000 net of related income taxes).

6. Minority Interests

(Thousands of dollars)	1985	1984
Equity of minority interests:		
In preferred shares of Canadian Utilities and subsidiaries	$ 750,710	$ 753,240
In Class A non-voting and Class B common shares of Canadian Utilities	327,285	302,214
In common shares of ATCO Saudi Arabia Ltd.	976	902
	$1,078,971	$1,056,356
In Canadian Utilities earnings for the year	$121,872	$114,756
Resulting from issue of Class A non-voting and Class B common shares of Canadian Utilities under employee share purchase plan	—	1,187
In ATCO Saudi Arabia Ltd. earnings for the year	459	384
	$122,331	$116,327

7. Long Term Debt

(Thousands of dollars)	1985	1984
227095 Holdings Ltd.		
Term loan, at prime plus ⅝%, due April 1, 1993	$ —	$100,000
Term loan, at 11¼% to 11¾% to January 31, 1987, at prime plus ⅝% thereafter, due April 1, 1993	—	50,000
The term loans are secured by Class A non-voting and Class B common shares of Canadian Utilities owned by the corporation and its subsidiaries.		
ATCO Drilling Ltd.		
Term loan, at 11% to March 31, 1985, 12½% from April 1, 1985 to March 31, 1987 and 13% thereafter, due March 31, 1989, secured by a first charge on drilling and well servicing rigs of the corporation and its subsidiaries	30,000	30,000
Canadian Utilities and Subsidiaries		
Sinking fund debentures, at 7¼% to 17½%, due at various dates to 2002	520,914	444,988
First mortgage sinking fund bonds, at 5½% to 9¾%, due at various dates to 1994	43,227	44,958
Capitalized lease obligation	21,086	21,856
Other	15,345	15,860
Other		
Mortgage and other loans, at 8% to prime plus 1%, due at various dates to 1996, secured mainly by charges on specific operating assets	75,969	87,898
	706,541	795,560
Less: Amounts due within one year	22,713	15,521
	$683,828	$780,039

Proceeds from the issue of preferred shares by ATCO Utilities Holdings Ltd. (see Note 8) were used to repay the outstanding indebtedness of the term loans of 227095 Holdings Ltd. The lenders are irrevocably committed, except in certain limited circumstances, to re-advance up to $50,000,000 at the corporation's option. All covenants of the loan agreement remain in force.

The terms of the above debt include restrictions relating to the payment of dividends by ATCO Ltd. and certain designated subsidiaries and to new debt, intercompany loans and guarantees. Covenants also require maintenance of voting control of Canadian Utilities, specified working capital and shareholders' equity, interest coverage ratios and continued ownership, either directly or indirectly, by ATCO Utilities Holdings Ltd. of the Canadian Utilities shares currently owned by ATCO.

Canadian Utilities leases, with an option to purchase, a dragline costing $24,818,000 which is included in electric utility plant and equipment. The future minimum payments are $2,421,000 per year for the next five years and $22,276,000 thereafter to June 30, 1996. The imputed interest included in these future minimum rentals at 7.62% implicit in the lease is $13,295,000.

The minimum annual repayments of long term debt over each of the next five fiscal years are as follows:

(Thousands of dollars)

1986	1987	1988	1989	1990
$22,713	$80,671	$41,388	$59,305	$51,430

8. Redeemable Preferred Shares

(Thousands of dollars)	1985	1984
Issued by:		
ATCO Ltd.	**$105,000**	$ 55,000
ATCO Holdings (N.A.) Ltd.	**52,074**	56,420
ATCO Utilities Holdings Ltd.	**150,000**	—
474243 Ontario Ltd.	**150,000**	150,000
Total issued (detailed below)	**$457,074**	$261,420

ATCO Ltd.

1985 1984 (Thousands of dollars)	Issued Shares	 Amount	Average Prime Rate	 Dividends
Junior Preferred Shares				
Authorized 8,000,000 shares				
Series 1	**200,000**	**$ 5,000**	**12.4%**	**$ 410**
	200,000	$ 5,000	11.0%	$ 377
Series 2	**2,000,000**	**50,000**	**N/A**	**5,750**
	2,000,000	50,000	N/A	5,750
Series 3	**2,000,000**	**50,000**	**N/A**	**1,542**
	—	—	N/A	—
		$105,000		**$7,702**
		$ 55,000		$6,127

The Series 1 Junior Preferred Shares are to be redeemed June 16, 1991 (or earlier under certain circumstances). Dividends are payable quarterly, calculated daily at one-half the prime rate plus 2%.

The Series 2 Junior Preferred Shares are redeemable, at the Corporation's option, from October 1, 1987 (or earlier under certain circumstances) and may be converted, at the holder's option, into 2.86 Class I non-voting shares for each convertible preferred share prior to September 30, 1989. 5,720,000 Class I non-voting shares have been reserved for this purpose. The redemption price is $26.25 from October 1, 1987 to September 30, 1988 and declines $.25 per share per year to $25.00 on October 1, 1992, and thereafter. Dividends are payable quarterly at a fixed rate of $.71875 per share.

The Series 3 Junior Preferred Shares are redeemable, at the Corporation's option, from December 31, 1989 to December 14, 1990 at $26.00 per share and at $25.00 thereafter. Dividends are payable quarterly at a fixed rate of $.58125 per share.

ATCO Holdings (N.A.) Ltd.

1985 1984 (Thousands of dollars)	Issued Shares	 Amount	Average Prime Rate	 Dividends
First Preferred Shares				
Par value $100 each				
Authorized 800,000 shares				
Series A, issued in U.S. dollars	**220,000**	**$30,074**	**12.4%**	**$2,408**
	260,000	$30,420	11.3%	$2,461
Series B	**220,000**	**22,000**	**12.2%**	**1,804**
	260,000	26,000	11.0%	1,962
		$52,074		**$4,212**
		$56,420		$4,423

The Series A and B First Preferred Shares, which may be redeemed earlier subject to certain restrictions and penalties, are to be redeemed, at par, in equal semi-annual installments of U.S. $2,000,000 and Canadian $2,000,000 to April 1, 1990.

The Series A First Preferred Shares are translated at the year-end exchange rate. Exchange adjustments arising on translation are deferred and amortized to retained earnings over the remaining life of the preferred shares.

Dividends are payable monthly, calculated daily at 52% of prime plus 1½%.

The subsidiary has indemnified holders of the preferred shares to the extent of any reduction in the holders' net after tax return from the preferred shares, caused by changes in law.

The preferred shares are the subject of a sale agreement wherein ATCO Ltd. agrees upon certain events occurring to purchase the preferred shares. This sale agreement is secured by a floating charge debenture of U.S. $90,000,000 issued and pledged by ATCO Ltd. and by hypothecation of the ATCO Drilling Holdings Ltd. shares. The sale agreement is also secured by guarantees and pledge of a U.S. $90,000,000 floating charge debenture of certain subsidiaries.

Terms relating to the preferred shares include restrictions on capital expenditures, new debt, intercompany loans and guarantees and performance bonds. Covenants also require maintenance of specified working capital and debt to equity ratios.

Failure to pay dividends, redeem shares or comply with covenants constitutes default and may result in the holders of the preferred shares demanding payment under the terms of the Sale Agreement.

ATCO Utilities Holdings Ltd.

1985 1984 (Thousands of dollars)	Issued Shares	 Amount	Average Prime Rate	Dividends
Preferred Shares				
Authorized 150,000 shares	**150,000**	**$150,000**	**12.2%**	**$9,477**
	—	—	N/A	—

The preferred shares may be redeemed, at the corporation's option, at a price of $1,040 per share from July 7, 1987 through July 6, 1988 or at a price of $1,020 per share from July 7, 1988 through July 6, 1989. The preferred shares outstanding at July 7, 1989 must be redeemed at a price of $1,000 per share.

Dividends are payable quarterly at a rate of one quarter of 70% of the average prime rate for the quarter.

474243 Ontario Ltd.

1985 1984 (Thousands of dollars)	Issued Shares	 Amount	Average Prime Rate	Dividends
Preference Shares				
Par value $1,000 each				
Authorized 150,000 shares				
Classes A-G	**150,000**	**$150,000**	**12.2%**	**$11,952**
	150,000	$150,000	11.0%	$11,137

Commencing May 1, 1985, the issued preference shares are to be redeemed, at par, at 1.25% per quarter to February 1, 1992, with the balance to be redeemed, at par, on May 1, 1992. The preference shares may be redeemed earlier subject to certain restrictions and penalties.

Dividends are payable quarterly at the following rates, calculated daily:

Classes A-D ($75,000,000)	50% of prime plus 2%
Classes E-F ($25,000,000)	50% of prime plus 1⅞%
Class G ($50,000,000)	52% of prime plus 1½%

The subsidiary has indemnified holders of the preference shares to the extent of any reduction in the holders' net after tax return from the preference shares, caused by changes in law.

9. Class I and Class II Shares

(Thousands of dollars)	Class I Non-Voting		Class II Voting		Total	
	Shares	Consider-ation	Shares	Consider-ation	Shares	Consider-ation
Authorized	100,000,000		50,000,000		150,000,000	
Issued:						
March 31, 1983	11,326,102	$ 5,247	4,991,403	$2,312	16,317,505	$ 7,559
Public issue	5,700,000	52,913	—	—	5,700,000	52,913
Employee share option plans	90,930	387	48,465	204	139,395	591
Conversions	264,399	132	(264,399)	(132)	—	—
March 31, 1984	17,381,431	58,679	4,775,469	2,384	22,156,900	61,063
Employee share option plans	6,600	38	3,300	19	9,900	57
Conversions	202,241	101	(202,241)	(101)	—	—
March 31, 1985	17,590,272	$58,818	4,576,528	$2,302	22,166,800	$61,120

Each Class II voting share may be converted to one Class I non-voting share at the shareholder's option. The two classes of shares rank equally in all other respects.

Share Options and Equivalents

ATCO has share option plans under which options to purchase 994,740 Class I non-voting and 217,260 Class II voting shares may be granted to selected directors, officers and key employees. The options are exercisable cumulatively over periods up to ten years from the date of grant.

Options to purchase 722,820 Class I non-voting and 216,660 Class II voting shares have been granted under the plan, of which 287,800 and 5,400, respectively, were outstanding at March 31, 1985 at prices ranging from $5.77 to $8.75 per share.

In conjunction with the above plan, ATCO has a long term incentive compensation plan under which 747,870 share equivalents have been granted to selected officers, directors and key employees. The equivalents generally are deemed to be received (at prices ranging from $4.05 to $8.22 per share) when a stock option is exercised and are redeemable five years later. Future payments under the plan are based on the increase in the price of ATCO's Class I and Class II shares plus deemed dividends. In 1985, $1,209,000 was charged to earnings in connection with this plan (1984—credit of $712,000).

Warrants

In conjunction with the October 6, 1983 issue of Class I non-voting shares, the Corporation issued 3,000,000 warrants to purchase one Class I non-voting share each at a price of $10.50 per share. The warrants are exercisable at any time prior to April 25, 1987. At March 31, 1985 no warrants had been exercised.

10. Revenues

(Thousands of dollars)	1985	1984
Sales, rentals and service	$1,610,827	$1,571,347
Interest income	13,988	17,900
Dividends from TransAlta Utilities Corporation	14,803	18,244
Loss on disposal of property, plant and equipment	(415)	(208)
Gain on purchase of long term debt	2,085	1,131
Exchange gains (losses)		
Operating	1,424	(284)
Translation	(610)	201
Other	2,561	2,008
	$1,644,663	$1,610,339

11. Taxes—Other Than Income

(Thousands of dollars)	1985	1984
Federal natural gas and gas liquids taxes	$ 5,453	$ 66,515
Federal petroleum and natural gas revenue taxes	7,753	7,131
Federal Canadian ownership taxes	28,580	41,686
	41,786	115,332
Franchise taxes	57,084	51,331
Other	14,266	16,292
	$113,136	$182,955

12. Interest

(Thousands of dollars)	1985	1984
Incurred	$98,407	$105,207
Capitalized		
Allowance for debt funds used during construction	14,746	13,486
Real estate development	726	5,713
Allowance for equity funds used during construction	26,771	23,826
	42,243	43,025
Expensed	$56,164	$ 62,182
Expensed on non-current liabilities	$53,481	$ 58,504

13. Segmented Information

(Thousands of dollars)

By Industry 1985 1984	Electric Utility Operations	Gas Utility Operations	Drilling and Well Servicing	Other Energy	Manu-facturing	Real Estate & Property Development	Other[1]	Consoli-dated[2]
Revenues:								
Trade	**$ 345,246**	**$879,696**	**$ 77,157**	**$163,417**	**$141,652**	**$ 6,395**	**$ 31,100**	**$1,644,663**
	$ 332,364	$900,567	$ 62,986	$136,952	$130,869	$10,488	$ 36,113	$1,610,339
Inter-segment	**146**	**20,055**	**1,909**	**8,612**	**886**	**14,239**	**9,187**	**—**
	141	22,771	1,689	7,850	2,114	20,671	6,100	—
Total segment revenues	**345,392**	**899,751**	**79,066**	**172,029**	**142,538**	**20,634**	**40,287**	**1,644,663**
	332,505	923,338	64,675	144,802	132,983	31,159	42,213	1,610,339
Expenses:								
Operating costs	**146,158**	**752,516**	**71,350**	**143,900**	**120,509**	**16,386**	**11,566**	**1,207,501**
	134,733	816,072	64,111	121,110	125,945	24,357	7,551	1,232,503
Depreciation, depletion and amortization	**36,624**	**26,279**	**14,464**	**6,902**	**10,817**	**1,227**	**5,932**	**105,764**
	35,160	19,252	15,404	5,034	11,716	772	3,528	94,007
Total segment expenses	**182,782**	**778,795**	**85,814**	**150,802**	**131,326**	**17,613**	**17,498**	**1,313,265**
	169,893	835,324	79,515	126,144	137,661	25,129	11,079	1,326,510
Segment operating profit (loss)	**$ 162,610**	**$120,956**	**$ (6,748)**	**$ 21,227**	**$ 11,212**	**$ 3,021**	**$ 22,789**	**$ 331,398**
	$ 162,612	$ 88,014	$(14,840)	$ 18,658	$ (4,678)	$ 6,030	$ 31,134	$ 283,829
Identifiable assets	**$1,191,909**	**$871,970**	**$138,611**	**$114,376**	**$121,454**	**$95,757**	**$381,639**	**$3,036,379**
	$1,083,391	$838,866	$148,542	$102,324	$126,935	$98,060	$361,582	$2,882,057
Capital expenditures	**$ 129,992**	**$ 56,437**	**$ 4,008**	**$ 32,224**	**$ 16,195**	**$ 17**	**$ 750**	**$ 239,623**
	$ 171,031	$103,839	$ 3,034	$ 4,842	$ 11,751	$11,186	$ 39	$ 305,722

[1] Holding companies including dividends on TransAlta shares.
[2] Inter-segment transactions have been eliminated in the consolidated column.

	1985	1984
Segment operating profit	**$331,398**	$283,829
Interest	**56,164**	62,182
Income taxes	**108,218**	86,787
Minority interests	**122,331**	116,327
	286,713	265,296
Earnings for the year	**$ 44,685**	$ 18,533

14. Income Taxes

The income tax provision differs from that computed using the statutory tax rate for the following reasons:

(Thousands of dollars)	1985	1984
Earnings before income taxes and minority interests	**$275,235**	$221,647
Income taxes at statutory rate of 47% (1984—47.6%)	**$129,360**	$105,504
Effect of utility subsidiaries claiming tax deductions in respect of property, plant and equipment less than book depreciation and depletion	**—**	3,406
Allowance for funds used during construction	**(12,532)**	(11,809)
Crown royalties and other non-deductible government payments	**10,935**	8,577
Earned depletion and resource allowance	**(12,836)**	(11,638)
Unrecorded benefits of loss carryforwards	**5,108**	8,248
Taxes related to amounts allocated to assets in excess of tax values on share acquisitions	**1,506**	1,790
Foreign tax rate differences	**(3,932)**	(3,976)
Provincial rebates	**(2,193)**	(2,954)
Non-taxable dividends	**(6,838)**	(8,697)
Other	**(359)**	(1,664)
	$108,219	$ 86,787
Effective rate	**39.3%**	39.2%

Prior to adoption of the "Normalization—All Taxes Paid" method of income tax accounting, the utility subsidiaries followed the "Flow-Through" method whereby deductions claimed in calculating taxable income exceeded the expenses recorded in the accounts, thereby reducing income taxes otherwise payable. Since the income tax component of rates recovers only income taxes currently payable, the deferred tax provision for these reductions was not recorded by the utility subsidiaries. Unrecorded deferred taxes of the utility subsidiaries decreased during the year by $1,960,000 (1984—$2,666,000) to an accumulated amount of $129,171,000.

Certain United States subsidiaries have operating loss carryforwards of approximately $27,722,000 for which the tax benefits have not been recognized in the accounts. The operating loss carryforwards are available to reduce future years' taxable income and expire in 1999 and 2000.

15. Rate Applications

One of the natural gas subsidiaries received an interim rate decision effective October, 1984. The application was for an additional $23,000,000 of revenue in calendar 1984. The Public Utilities Board approved interim rates which were estimated to allow the natural gas subsidiary to recover $10,000,000 in the period November 1, 1984 to June 30, 1985, of which approximately $8,000,000 was recorded in the current year.

The Public Utilities Board, by an order dated January 17, 1985, directed the electric subsidiary to file a submission for a general rate proceeding covering the test calendar years 1984 and 1985. After reviewing the rates allowed for calendar 1984, the Public Utilities Board may or may not amend the rates the electric subsidiary charged to its customers. It is not possible, at this time, to forecast the outcome or effect of this proceeding.

16. Commitments and Contingencies

ATCO has contractual obligations in respect of long term operating leases for manufacturing facilities, office premises and equipment. The rentals amounted to $6,282,000 for 1985 (1984 — $7,354,000). Future minimum lease payments are as follows:

(Thousands of dollars)

1986	1987	1988	1989	1990	Total of All Subsequent Years
$6,139	$5,015	$3,949	$2,916	$2,126	$1,942

United States treasury officials are investigating the basis followed by ATCO in determining certain United States customs and duty payments since 1969. These investigations are still in progress. In the opinion of counsel, claims will probably be asserted. Management is of the opinion that no material amount above those amounts already provided in the accounts will ultimately be payable.

Alberta Power Limited has a 50% joint ownership in the Sheerness Generating Station which is under construction. The project is forecast to cost the corporation approximately $585,656,000 of which $313,347,000 has been expended to date. Unit I is planned to be completed in January, 1986. The electric subsidiary has applied to the Energy Resources Conservation Board to defer commissioning of Unit II from 1987 to 1990. A hearing was held in January, 1985 and a decision is pending.

ATCO has pension plans covering substantially all of its employees. The aggregate unfunded past service liability, all of which is attributable to Canadian Utilities, amounted to approximately $30,832,000 at March 31, 1985 (1984 — $26,258,000) and is being funded over a period not exceeding 14 years.

As part of the financing of the June 19, 1980 acquisition of shares of Canadian Utilities, ATCO has agreed to pay the lenders 7% of the increase in value of the Canadian Utilities shares from acquisition to date of demand, to a maximum amount of $21,000,000. The amount is payable on demand if ATCO sells or transfers any of the shares of Canadian Utilities, or at any time from December 31, 1985 to December 15, 1992. Payments may be made in cash or, at ATCO's option, by the issue of an appropriate number of Class I shares of ATCO Ltd. based on their then quoted market price. Based on the March 31, 1985 market price of the Canadian Utilities shares, the liability to the lenders would be approximately $5,000,000. The estimated amount payable arising as a result of this agreement will be deferred and charged to earnings from 1986 to 1993.

17. Comparative Figures

Certain of the comparative figures have been reclassified to conform with the financial statement presentation adopted for 1985.

Consolidated Summary of Operations

Years ended March 31

(Thousands of Canadian dollars)	1985	1984	1983	1982	1981
Revenues	$1,644,663	$1,610,339	$1,723,129	$1,668,979	$1,220,926
Costs and expenses	1,369,428	1,388,692	1,518,591	1,514,088	1,107,778
	275,235	221,647	204,538	154,891	113,148
Income taxes	108,219	86,787	68,328	43,041	36,569
	167,016	134,860	136,210	111,850	76,579
Minority interests	122,331	116,327	95,519	57,291	33,171
	44,685	18,533	40,691	54,559	43,408
Extraordinary item	—	—	—	—	2,776
Earnings for the year	44,685	18,533	40,691	54,559	40,632
Dividends on redeemable preferred shares	33,343	21,704	26,001	28,547	11,241
Earnings (loss) attributable to Class I and Class II shares	$ 11,342	$ (3,171)	$ 14,690	$ 26,012	$ 29,391
Earnings (loss) per Class I and Class II share					
—before extraordinary item	$.51	$(.16)	$.90	$1.60	$2.01
—after extraordinary item	$.51	$(.16)	$.90	$1.60	$1.83
Dividends per Class I and Class II share	$.20	$.20	$.20	$.20	$.18
Equity per Class I and Class II share	$9.21	$9.12	$9.71	$9.05	$7.68

Market price of shares					
Class I High	9⅜	10¾	11½	11¼	10 (1)
Low	5¼	6½	5	6½	7¾ (1)
Class II High	9¼	10⅝	11¼	11⅛	10½ (1)
Low	5½	6⅜	5	6½	7¾ (1)

(1) Prices from February 5, 1981, the date of reorganization of shares into Class I and Class II shares.

Auditors' Report

To the Shareholders of ATCO Ltd.

We have examined the consolidated balance sheet of ATCO Ltd. as at March 31, 1985 and the consolidated statements of operations and 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 March 31, 1985 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. Except for the change in method of accounting for foreign currency translation as explained in Note 2 to the financial statements, these principles have been applied on a basis consistent with that of the preceding year.

Price Waterhouse

Chartered Accountants

Calgary, Alberta
May 21, 1985

Directors, Officers and Operating Units

Directors

W. L. Britton, Q.C.
Partner, Bennett Jones
Calgary

B. P. Drummond ★
Vice Chairman, Richardson Greenshields of Canada Limited
Montreal

B. K. French ★
President,
Karusel Management Ltd.
Calgary

G. P. Kiefer ★☆
Senior Vice President,
Special Projects
ATCO Ltd.

E. W. King
Corporate Director
Edmonton

K. B. Purdie ☆
President, Manufacturing & Leasing
ATCO Ltd.

R. Rice ★
Consultant
Greenwich, Conn., U.S.A.

C. S. Richardson ☆
Senior Vice President,
Finance
ATCO Ltd.

N. W. Robertson ☆
President and Chief
Operating Officer
ATCO Ltd.

C. N. Simpson
President, C. Norman Simpson
Consultants Limited
Vancouver

R. D. Southern ☆
Deputy Chairman and
Chief Executive Officer
ATCO Ltd.

S. D. Southern
Chairman of the Board
ATCO Ltd.

O. Steiner ☆
President
ATCO Development Ltd.

J. D. Wood
President and Chief
Operating Officer
Canadian Utilities Limited

Officers

S. D. Southern
Chairman of the Board

R. D. Southern
Deputy Chairman and
Chief Executive Officer

N. W. Robertson
President and
Chief Operating Officer

C. S. Richardson
Senior Vice President,
Finance

G. P. Kiefer
Senior Vice President,
Special Projects

A.J. Pullman
Vice President,
Controller

D. P. Wood
Vice President, Corporate
Services and Corporate
Secretary

M. Durdle
Assistant Secretary

★ Member—Audit Committee
☆ Member—Executive Committee

Utilities Group

Alberta Power Limited
Generation and Distribution
of Electricity
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Utilities and Energy-related
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Canadian Western Natural Gas
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Production and Distribution
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The Yukon Electrical Company
Limited
Generation and Distribution
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Resources Group

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Contract Drilling
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ATCO Drilling Ltd.
Contract Drilling, Well Servicing and Oilfield Equipment Rentals and Sales
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ATCO Marine Exploration Ltd.
Exploration and Development of Frontier Lands
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ATCO Oilfield Equipment
Oilfield Equipment Rentals and Sales
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ATCO Well Servicing
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ATCO Well Servicing
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ATCO-APM Drilling Pty. Ltd.
Joint Venture with Australian Paper Manufacturers Ltd. in Contract Drilling and Well Servicing
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AT&S Exploration Ltd.
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Manufacturing Group

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ATCO Homes
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Other

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(403) 230-2911
Business Reservations
(403) 276-9991

InterATCO B.V.
InterATCO Drilling B.V.
Financial Holding Companies
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The Netherlands
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Shareholders' Information

Shareholder and security analyst inquiries should be directed to:
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ATCO Ltd.
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Calgary, Alberta T2R 1N6
Telephone (403) 229-4554

Dividend information and other inquiries concerning your shares should be directed to:
STOCK TRANSFER DEPARTMENT
National Trust Company
1008 The Home Oil Tower
324-8th Avenue S.W.
Calgary, Alberta T2P 2Z2

The shares of ATCO Ltd. are listed under the ticket symbols:
ACO.X (Class I Non-Voting Shares)
ACO.Y (Class II Voting Shares)
ACO.Pr.A (11½% Cumulative Redeemable Convertible Junior Preferred Shares, Series 2)
ACO.WT (Warrants to purchase Class I Non-Voting Shares)
on The Toronto Stock Exchange and the Montreal Exchange

ATCO's fiscal year ends on March 31. Dividends are mailed approximately the end of September, December, March and June

ATCO Ltd. is incorporated under the laws of the Province of Alberta

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AUDITORS
Price Waterhouse
Calgary, Alberta

COUNSEL
Bennett Jones
Calgary, Alberta

The annual shareholders' meeting will be held at 10 a.m. M.D.T. on Wednesday, August 14, 1985 in the Calgary Convention Centre, Calgary, Alberta

ATCO

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PRINTED IN CANADA