

AUX 24 1978
McGILL UNIVERSITY



Corporate

DIRECTORS:

Mr. A. Bryce Cameron — Sorrento, B.C. Dr. A. Cree — West Sedona, Arizona, U.S.A. Mr. R. A. Hayes — Calgary, Alberta

Mr. B. A. Macdonald — Calgary, Alberta

Mr. D. C. Traxel — Calgary, Alberta

OFFICERS:

Donne C. Traxel — President Robert A. Hayes — Vice President Linda B. Morrison — Secretary

HEAD OFFICE:

#565, 808 — 4th Avenue S.W. Calgary, Alberta T2P 0K4 Phone (403) 269-6911

LEGAL COUNSEL:

Moore, Martin 8th Flr., 205 - 5th Avenue S.W. Calgary, Alberta

AUDITORS:

Peat, Marwick, Mitchell & Co. 2500 — 700 — 2nd Street S.W. Calgary, Alberta

REGISTRAR AND TRANSFER AGENT:

Canada Trust Company 239 — 8th Avenue S.W. Calgary, Alberta

STOCK EXCHANGE LISTING:

Toronto Stock Exchange Share Symbol: ULP

ANNUAL MEETING:

10:00 A.M. on June 12, 1979 Room 205, International Hotel 220 — 4th Avenue S.W. Calgary, Alberta

1978 Highlights

FINANCIAL	1978	1977
Net Earnings	\$ 212,000 04¢	\$ 182,000 04¢
Working Capital Provided From Operations	\$ 452,000 08¢	\$ 465,000 09¢
Oil and Gas Sales, Less Royalties	\$ 856,000	\$1,079,000
Working Capital End of Year	\$ 51,000	\$ 99,000
Number of Shares Outstanding	5,454,675	5,354,675
SUMMARY OF LAND HOLDINGS (1)		
CANADA: Western Canada	45,894 372,080	45,004 324,438
FOREIGN: United States	6,375 332	 332
TOTAL	424,681	369,774
(1) Net acres excluding royalty interests		
SUMMARY OF WELLS DRILLED		
Total (Gross) Oil Gas Service Dry (1) 5 of these wells were drilled by farmees at no cost to the Company	42 19 10 5 8 (1)	11 - 11 - -
SUMMARY OF PRODUCTION DATA		
Natural Gas Production Annual production — mcf	665,000 2,216	993,000 2,720
Crude Oil Production Annual production — gross barrels	5,250 15	16,730 46

ULSTER PETROLEUMS LTD.

Report To The Shareholders

The past year marked a period of unprecedented activity for Ulster Petroleums Ltd. Expenditures on exploration and development activities exceeded \$1,500,000 during the year compared to \$70,000 for 1977. Highlights of these activities include:

- Participation in the drilling of 42 wells in Canada and the United States; 34 of which were successfully completed.
- Acquisition of working interests in approximately 280,000 gross acres of additional petroleum and natural gas rights in Western Canada, the Beaufort Sea and the United States.
- Acquisition of a working interest in 18 producing shallow gas wells in Alberta.

As detailed in subsequent sections of this report, management is encouraged by these results, since the majority of the wells drilled during the year represent initial exploratory work on blocks of land which offer significant additional development potential.

Expenditures on exploration and development activities for 1979 are expected to exceed those of the previous year with continuing emphasis being placed on development drilling of the Company's oil reserves in the Wainwright area of Alberta. In addition, Ulster will aggressively pursue new exploration prospects in the United States due to the availability of higher product prices and fewer marketing restrictions.

Expenditures of this magnitude are necessary if Ulster expects to overcome the negative effects of contract cutbacks and depletion from existing reserves. Management is confident that the discoveries made during the latter part of 1978 and its current initiatives will not only reverse the trend of recent years but once again put the company into a growth pattern.

Much recent discussion and speculation has taken place with regard to the enormous indicated potential for petroleum reserves in the Beaufort Sea region of Canada. Ulster is extremely well represented in this area and during the year increased its holdings further by acquiring a $2\frac{1}{2}$ % working interest in an additional 220,287 permit acres. Ulster now has working and royalty interests in over 1,000,000 permit and lease acres within the Beaufort Sea.

Available seismic data on Ulster's acreage indicates the presence of a number of structures similar in size to those currently being drilled by Dome Petroleum Limited. Accordingly, Ulster is anxiously awaiting the results of the 1979 drilling season since a number of Dome's reported discoveries and proposed locations are in close proximity to the company's acreage and as such will provide valuable information concerning the potential of our holdings.

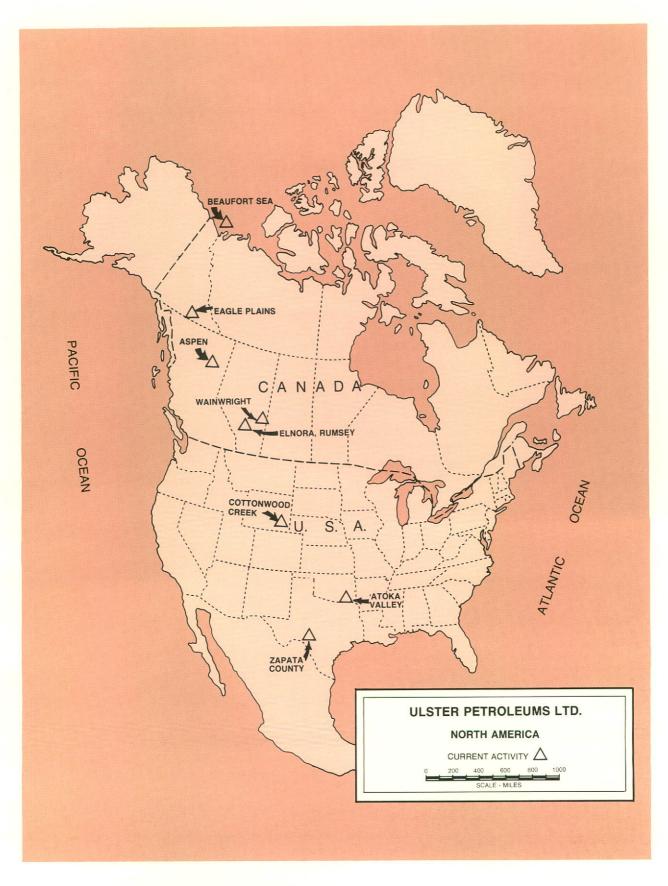
Subsequent to the year end the Company successfully completed a rights offering which resulted in the issuance of 1,818,225 shares to existing shareholders. This offering netted \$2,220,000 in additional funds which enabled the Company to retire all of its bank debts and increase its current working capital by approximately \$750,000. This infusion of new capital has put your Company into an extremely strong financial position and will allow it to continue to pursue an aggressive exploration policy. Management appreciates this vote of confidence in the direction being taken by Ulster and in its future.

Diaxel

On Behalf of the Board of Directors

Donne C. Traxel

President



Exploration and Development Activity

Ulster had an interest in 42 wells drilled during 1978. Of this total 19 were completed as oil wells; 10 were completed as gas wells; and 5 were completed as service wells.

The index map on Page three of this report highlights the principal areas of current activity described in the following narrative.

WESTERN CANADIAN ACTIVITY Wainwright Area:

In June 1978, Ulster acquired a 25% working interest in 7,500 acres which offset the Wainwright oil field in Central Alberta. This acreage contains twelve producing Viking gas wells and a compressor station.

A farmout agreement was subsequently negotiated involving development of the Sparky oil rights on a 480 acre parcel of land within this block. This program, which included the drilling of 15 oil wells, 4 injection wells and one water source well, was completed and fully operational on March 1, 1979. Ulster has retained a 5% working interest in the farmout acreage and its 25% interest in all of the offsetting lease acreage.

While much publicity has been given to the Lloydminster area "heavy oil" prospects, we believe the area at Wainwright to have two distinct advantages. Firstly, the productive sands are consolidated vs. unconsolidated at Lloydminster, and secondly the gravity of the oil is 21 - 24° A.P.I. vs. 11 - 14° A.P.I. at Lloydminster. As a result the Wainwright area offers fewer operating problems, hence a greater potential return on investment.

Substantial additional development is currently being planned on Ulster's acreage during 1979.

Central Alberta:

Ulster participated (3.125 to 6.25% working interest) in the drilling of seven exploratory wells in the Elnora-Rumsey area of east central Alberta during 1978. Five of these wells have been completed as potential Belly River and/or Glauconite gas wells and have resulted in the Company earning an interest in 12,160 acres of petroleum and natural gas rights.

Although the majority of these lands are under gas contract, production start-up cannot be precisely forecast at this time. Limited drilling is planned in 1979 in order to delineate the extent of the reservoirs discovered, however, major development will be deferred until production has commenced from the initial wells drilled.

Aspen Area:

During 1978 Ulster acquired a 4% working interest in an 8,371 acre drilling reservation and a 697 acre petroleum and natural gas lease in the Aspen area of British Columbia. A farmee has drilled a successful Charlie Lake dolomite gas well on this reservation which flowed 2.88 mmcf/d of gas with excellent reservoir pressures. A second well drilled by the farmee was dry and abandoned, however, a third well in which Ulster participated directly, was successfully completed in the Charlie Lake formation. Additional drilling is expected once these wells have been tied into a production line.

UNITED STATES

Cottonwood Creek Area, Wyoming

Ulster participated (2.58 to 9.75% working interest) in the drilling of three 11,000 foot Phosphoria wells in Washakie County, Wyoming which have been successfully completed as oil wells. These wells recently commenced production at 200 - 300 barrels of oil per well per day. The first of a number of offsets scheduled for drilling during 1979 is currently underway.

Ulster has also acquired a 1.69% working interest in an additional 4,530 lease acres in this area and participated in the drilling of a 11,000 foot Phosphoria test. This well was suspended since it did not encounter commercial volumes of hydrocarbons. The potential for additional drilling and/or farmout is being evaluated.

Zapata County, Texas

Ulster participated (10% working interest) in the drilling and completion of a 9,500 foot test well in Zapata County, Texas. The Lobo Sands in the Upper Wilcox formation have been successfully completed and tested at flow rates in excess of 2 mmcf/d. The well was put onto production in March of 1979, however, it is currently experiencing difficulties with regard to deliverability due to surging line pressures in the purchaser's pipeline.

Atoka Valley, Oklahoma

Ulster participated (6.25% working interest) in a 9,500 foot well drilled in Atoka County, Oklahoma. This well was tested and completed in the Stanley Sands which demonstrated gas potential in over 140 feet of development. Additional drilling on the 20,000 acres in which Ulster has a 4.6% working interest will be required before this well can be economically tied into a purchaser's pipeline.

NORTHERN CANADA Beaufort Sea

The Beaufort Sea map on Page six of this report highlights the following interests which Ulster has in this area:

- a) Permits Nos. W2257 to W2261 inclusive, containing 222,288 acres — 15% working interest in 102,336 gross lease acres which were selected from these permits based upon our geophysical and geological interpretation of these lands.
- b) Permits Nos. W2262 to W2264 inclusive, W2318 and W2319, containing 220,287 acres — 2¹/₂% working interest in this block of permits.
- Permit No. 2317, containing 43,343 acres 25% working interest in this permit.
- d) Permits Nos. A2784 to A2788 inclusive, containing 400,347 acres 38% working interest in these permits which is being carried by a farmee through August 1980.
- e) Permits Nos. A2795 (E¹/₂), A2797 and A2798, containing 202,527 acres 1¹/₃% gross overriding royalty interest.
- Permits Nos. A2795 and A2796, containing 121,589 acres — 1% gross overriding royalty interest.

Although Dome was unable to complete its testing program on the Ukalerk C-50 and the Kopanoar M-13 wells during the 1978 drilling seson, indications of substantial discoveries were evident. The results of these wells, together with those of the Tarsuit well which is scheduled to reach target depth in 1979, will not only help to prove up the potential of Ulster's acreage in the immediate area of these wells but also our other acreage within this same geological setting.

Eagle Plains, Yukon

Aquitaine has advised that their 14,000 foot test well in the South Eagle Plains area of the Yukon has been plugged and abandoned since it did not encounter commercial hydrocarbons. This well was drilled at no cost to Ulster on Yukon permit #6448 which contains 26,152 acres and is subject to a 3% gross overriding royalty in Ulster's favour. The likelihood of continued exploratory work in the immediate area of this permit is uncertain.

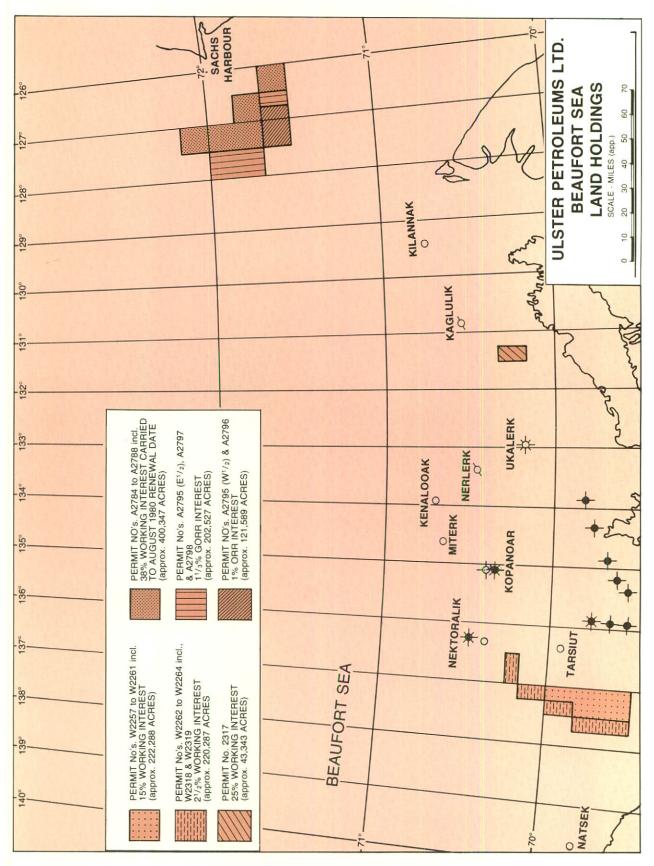
Operational and Financial Review and Analysis

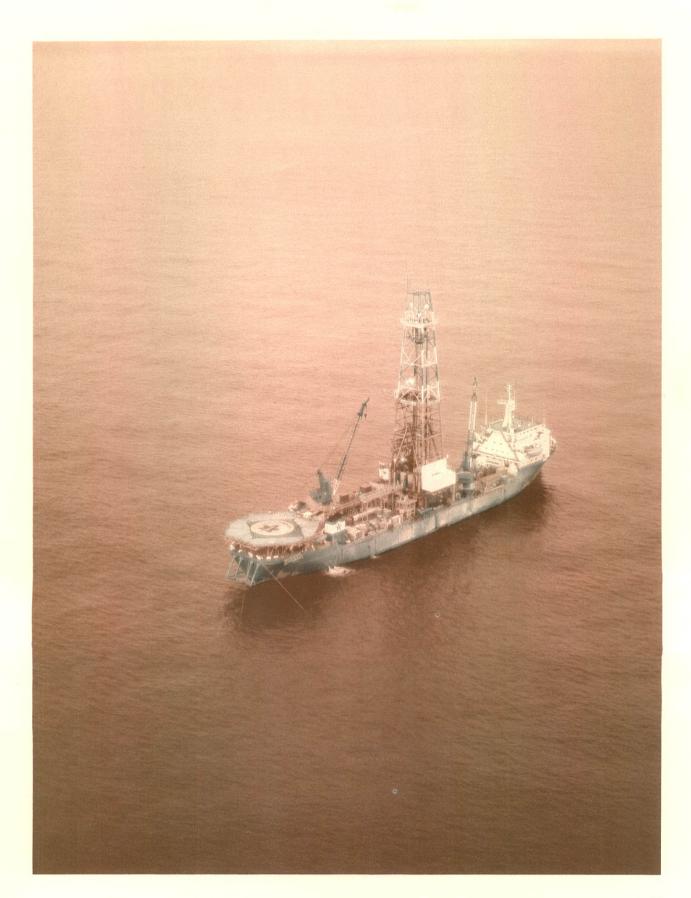
Net earnings for the year were \$212,000 (4¢ per share) in 1978 compared to \$182,000 in 1977. Although earnings increased by approximately 16% for the year, a number of significant changes have occurred in the various components which gave rise to these results.

- Production revenues declined by approximately 20% during the year. This decrease results primarily from additional shut-in periods under existing gas contracts in Alberta and normal depletion. Allowable production volumes under existing gas contracts are expected to remain at their 1978 levels during the forthcoming year. Accordingly, management is moving to bring recent exploratory successes onto stream as quickly as possible.
- Overall general and administration expenses declined significantly in 1978 as the direct result of a streamlining of operations. This reduction, however, was partially offset by a substantial increase in exploration related overhead charges which are directly attributable to the higher levels of activity during the year.
- Other income aggregated \$194,000 during the current year and is primarily related to the provision of drilling and property management services to third parties.

Working capital provided from operations was \$452,000 (8¢ per share) compared to \$465,000 in 1977. These funds, together with additional bank borrowings of \$937,000 were used to finance drilling activities and property acquisitions.

ULSTER PETROLEUMS LTD.







Balance Sheet

December 31, 1978 (with comparative figures for 1977)

Assets

	1978	1977
CURRENT ASSETS:		
	\$ 255,000	285,000
Accounts receivable	384,000 22,000	366,000
Total current assets	661,000	651,000
Notes receivable, net of current portion (Note 4)	88,000	_
Property, plant and equipment (Note 2)	4,715,000	3,377,000
Other assets, at cost	81,000	121,000
	\$5,545,000	4,149,000
Liabilities and Shareholders' Equity		
CURRENT LIABILITIES:		
Accounts payable and accrued liabilities	\$ 610,000 —	238,000 314,000
Total current liabilities	610,000	552,000
Deferred revenue	79,000	_ 1
Long-term debt (Note 3)	1,462,000	525,000
SHAREHOLDERS' EQUITY: Share capital (Notes 4 and 5): Shares without nominal or par value. Authorized 12,000,000 shares;		
Issued 5,454,675 shares (1977 — 5,354,675)	6,929,000	6,819,000
Deficit	(3,535,000)	(3,747,000)
	3,394,000	3,072,000
	\$5,545,000	4,149,000

Approved on behalf of the Board:

D. Director
Ray Director

See accompanying notes.



Statement of Changes in Financial Position Year ended December 31, 1978

(with comparative figures for 1977)

	1978	1977
Working capital was provided from:		
Operations	\$ 452,000	465,000
Increase in long-term debt	937,000	_
Proceeds from sale of property, plant and equipment	-1,-0-	210,000
Issue of shares	110,000	-
Deferred revenue	79,000	_
Other	13,000	
	1,591,000	675,000
Working capital was applied to:		
Reduction of long-term debt	_	260,000
Additions to property, plant and equipment	1,551,000	71,000
Notes receivable, net of current portion	88,000	
	1,639,000	331,000
Increase (decrease) in working capital	(48,000)	344,000
Working capital (deficiency), beginning of year	99,000	(245,000)
Working capital, end of year	\$ 51,000	99,000



Statement of Earnings and Deficit Year ended December 31, 1978

(with comparative figures for 1977)

	1978	1977
REVENUE:		
Oil and gas sales, less royalties	\$ 856,000 194,000	1,079,000
	1,050,000	1,079,000
EXPENSES:	.,,	.,,
Production	372,000	372,000
General and administrative	172,000	221,000
Interest on long-term debt	123,000	81,000
Depletion	146,000	194,000
Depreciation	82,000	89,000
	895,000	957,000
Earnings before the following	155,000	122,000
INCOME TAXES:		
Deferred	90,000	88,000
Alberta royalty tax credit	(57,000)	(60,000)
Ansona Toyarty tax ordar		
	33,000	28,000
Earnings before extraordinary item	122,000	94,000
Extraordinary item, reduction of income taxes		
resulting from application of prior years'		
drilling and exploration expenditures	90,000	88,000
Net earnings	212,000	182,000
Deficit, beginning of year	3,747,000	3,929,000
	\$3,535,000	3,747,000
	φ3,535,000	3,747,000
Earnings per share (Note 5):		
Before extraordinary item	\$ 0.02	0.02
Extraordinary item	0.02	0.02
	\$ 0.04	0.04



Notes to Financial Statements

December 31, 1978

1. Significant accounting policies:

a) Property, plant and equipment:

The Company follows the full cost method of accounting whereby all costs related to the exploration for and development of oil and gas reserves are capitalized. Costs capitalized include land acquisition costs, geological and geophysical expenditures, rentals on undeveloped properties and costs of drilling productive and non-productive wells. The capitalized costs are being depleted on the unit of production method based on estimated proven recoverable reserves as determined by independent consultants. Production and other equipment is being depreciated on a reducing balance basis at annual rates ranging from 5% to 20%.

b) Deferred revenue:

Deferred revenue represents amounts received in respect of "take-or-pay" natural gas contracts. Such amounts have been deferred pending ultimate natural gas delivery or expiration of the contractual delivery period.

c) Joint interest operations:

Substantially all of the Company's petroleum and natural gas exploration and production activities are conducted jointly with others and accordingly these financial statements reflect only the Company's proportionate interest in such activities.

2. Property, plant and equipment:

	roperty, plant and equipment.	Assumulated		
		Accumulated Depletion and	Net Boo	k Value
	Cost	Depreciation	1978	1977
	Petroleum and natural gas properties including exploration and development			
	thereon	1,261,000	4,168,000	2,898,000
	Production equipment 1,213,000	691,000	522,000	459,000
	Other equipment	48,000	25,000	20,000
	\$ <u>6,715,000</u>	2,000,000	4,715,000	3,377,000
3.	Long-term debt:			
			1978	1977
	Bank loan with interest at 1% above bank prime rate secured by assignments of interests in			
	Agreement payable, bearing interest at the rate		\$1,462,000	810,000
	of 12% per annum			29,000
			1,462,000	839,000
	Deduct current portion of long-term debt			314,000
			\$1,462,000	525,000
				-

The bank loan was repaid in February 1979 out of the proceeds of the rights issue (Note 5). As the repayment was out of capital funds, the full amount of the bank loan outstanding at December 31, 1978 has been classified as long-term debt.

4. Share capital:

- a) During the year the authorized share capital was increased from 8,000,000 to 12,000,000 shares.
- b) Pursuant to agreements dated October 30, 1978, the Company issued 100,000 shares at a price of \$1.10 per share to two senior officers in return for promissory notes amounting to \$110,000. These promissory notes are non-interest bearing and are repayable in five equal annual instalments commencing in 1979. The shares are pledged as security for the promissory notes.

5. Subsequent event:

Subsequent to the year-end the Company made a rights offer on the basis of 1 share for every 3 shares held at a subscription price of \$1.35 per share. The offer was fully subscribed and resulted in the issue of an additional 1,818,225 shares for a net consideration of approximately \$2,220,000. The proceeds were initially used to repay the bank loan and the balance invested in working capital.

If the shares had been issued as at January 1, 1978 and the proceeds used to retire all the then outstanding bank indebtedness, the resulting pro-forma earnings per share for 1978 would have been \$0.03 before the extraordinary item and \$0.05 after the extraordinary item.

6. Remuneration of directors and officers:

The aggregate remuneration paid by the Company to directors and senior officers during the year amounted to \$141,500 (1977 — \$93,800).

7. Subsidiary companies:

Effective January 1, 1978 the Company disposed of its investment in its subsidiary companies for a nominal consideration.

Auditors' Report to the Shareholders

We have examined the balance sheet of Ulster Petroleums Ltd. as at December 31, 1978 and the statements of earnings and deficit 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 financial statements present fairly the financial position of the company as at December 31, 1978 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.

Calgary, Canada March 23, 1979 Peat, Marwick, Mitchell & Co. Chartered Accountants

