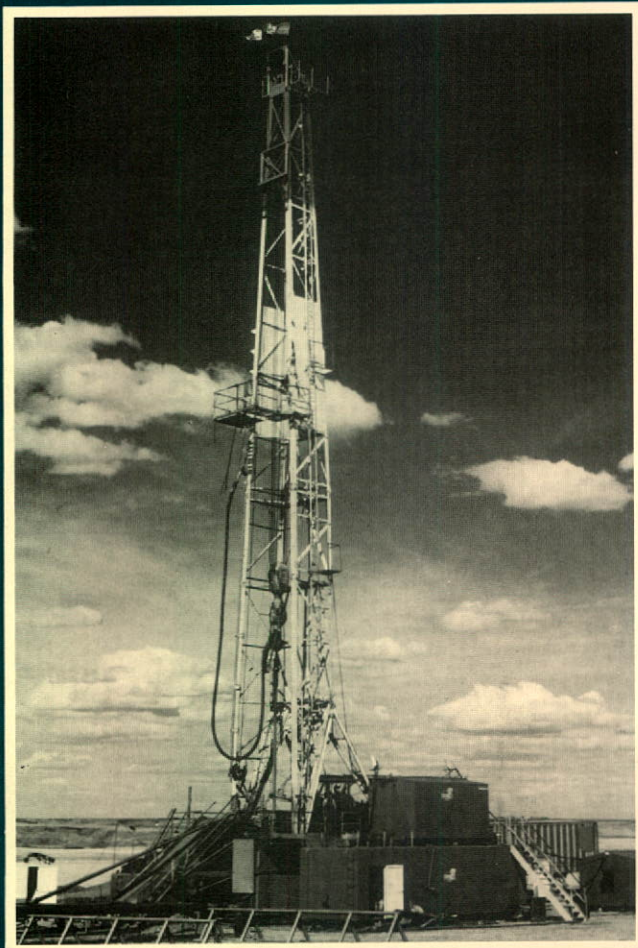


1977 annual report



 **OMEGA**
hydrocarbons ltd.

DIRECTORS

T. Jack Hall, Calgary
Henry Higgins, Calgary
Ernest M. Braithwaite, Calgary

OFFICERS

President — T. Jack Hall
Vice President — Arthur L. Evans
Secretary — Ernest M. Braithwaite
Treasurer — Henry Higgins
Assistant Secretary — Bonnie Foote

HEAD OFFICE

Suite 630, 330 - 5th Avenue S.W.
Calgary, Alberta T2P 0L4

AUDITORS

Thorne Riddell & Co.
Chartered Accountants
1400 Bow Valley Square 2
205 - 5th Avenue S.W.
Calgary, Alberta T2P 2W4

REGISTRAR

The Canada Trust Company
239 - 8th Avenue S.W.
Calgary, Alberta T2P 1B9

TRANSFER AGENTS

The Canada Trust Company
239 - 8th Avenue S.W.
Calgary, Alberta T2P 1B9

SOLICITORS

Macleod Dixon
1500 Home Oil Tower,
Toronto Dominion Square
Calgary, Alberta T2P 2Z2

BANKERS

Bank of Montreal
604 - 8th Avenue S.W.
Calgary, Alberta T2P 1G4

Annual General Meeting

The Annual General Meeting of the shareholders of Omega Hydrocarbons Ltd. will be held at the Head Office of the Company at Suite 630, 330 - 5th Avenue S.W., Calgary, Alberta on Friday, the 26th day of May, 1978 at 3:00 p.m. (local time).

1

1. Service rig used during completion of Omega's Provost 11 - 11 - 36 - 8 W4M (pumping oil well).

2

3

2. Bodor Rig No. 2 drilling Omega et al Bow Island 6 - 20 - 11 - 11 - W4M (capped gas well).

3. Omega's Provost 10 - 4 - 36 - 8 - W4M (pumping oil well).



President, T. Jack Hall



*Left to Right:
Receptionist-typist, Linda Stewart
V.P. Exploration, Art Evan
Accountant-Land, Bonnie Foote*

DIRECTORS' REPORT

To the Shareholders of
Omega Hydrocarbons Ltd.

While the 1977 operating results are gratifying to your directors, it must be recognized that the highlight of the year's activity was in the area of financing. The Company was successful in raising a substantial amount of money through its sponsorship of two drilling funds.

In the latter part of 1977, the Company organized Omega Oil & Gas Fund No. 1 and sold sixty drilling fund units amounting to 1.5 million dollars, while at the same time negotiated arrangements with a German Drilling Fund, which resulted in the availability of 2 million dollars to Omega for approved drilling prospects during the 1978 year and an additional 1.5 million dollars in each of the next two succeeding years. These two new sources of funds are intended to cover two areas of exploration. The Omega Oil & Gas Fund No. 1 will cover the area of close-in drilling prospects whereas the German Fund is intended for exploring the large reserve areas of Canada and the United States. Omega's objectives in raising drilling funds are to accelerate exploration and development of its newly acquired lands and the acquisition of potentially available prospects. With this planning, Omega should, with a reasonable degree of success, be in a position to enhance its reserves of oil and gas, which will ultimately result in improved cash flow. Your directors are confident that these newly acquired resources will allow the Company to accomplish its objectives.

Management has been especially active in purchasing Crown lands and freehold lands during 1977. This program has resulted in the acquisition of 51,763 net acres in Alberta, Saskatchewan and Manitoba.

Omega continues to receive encouraging results from its waterflood program in Waskada, Manitoba, from its Willmar, Saskatchewan production and from the Sedalia, Alberta gas producing area. New compression facilities were installed at Sedalia, thus providing more deliverability while offsetting declining field pressure. All of these properties will experience additional expenditure during 1978, with the view of increasing sales.

Drilling activity in 1977 amounted to drilling two wells in the Bow Island area of Alberta. Although one well tested oil and water in the Sunburst sand, it was considered to be uneconomic and, subsequently, abandoned. The other well was cased to the base of the Second White Specs sand and is awaiting completion.

In November of 1977, the Company entered into an agreement to earn a 50% interest by completing and equipping two wells in the Provost area of Alberta at their cost, both of which were successful oil producers, adding substantially to the Company's reserves. This area will receive considerable attention during the 1978 drilling season.

Although your directors have great expectations of the future, they cannot ignore the surplus of gas in Alberta, rig availability and the restriction on crude oil exports to the United States, all of which are inhibiting factors in the expansion of the industry and of your Company. Let us hope that the Federal and Provincial Governments will develop policies which will, at least, maintain the present level of crude oil exports and, possibly, take steps toward increasing gas exports.

Your directors, management and staff, all of whom have contributed generously during the year, look forward to a very active and exciting year in 1978.

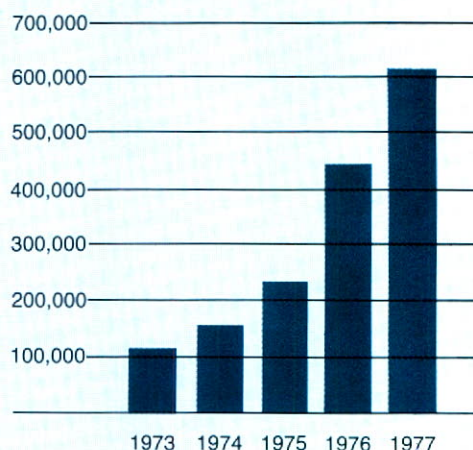
ON BEHALF OF THE BOARD



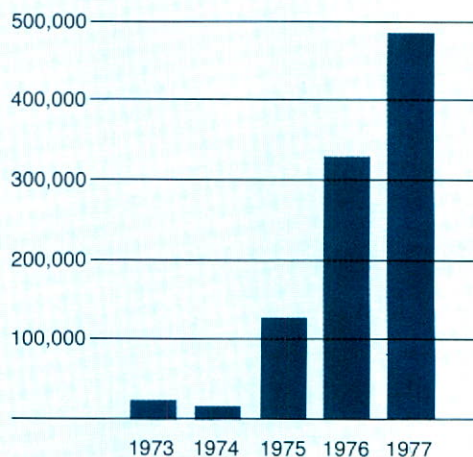
T. Jack Hall
President

Calgary, Alberta
April 21, 1978

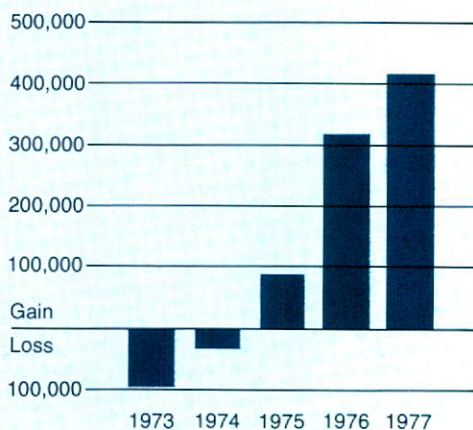
Revenue Sales



Cash Flow



Net Earnings



OMEGA HYDROCARBONS LTD.

CONSOLIDATED STATEMENT OF EARNINGS AND DEFICIT YEAR ENDED DECEMBER 31, 1977

	1977	1976
REVENUE		
Oil and gas sales, net of royalties	\$ 612,860	\$ 443,281
EXPENSES		
Production	98,137	88,756
General and administrative	52,186	43,982
Interest and expense on long-term debt	9,542	23,315
Depletion	50,000	20,953
Depreciation	21,000	13,116
	<u>230,865</u>	<u>190,122</u>
Earnings before income taxes and extraordinary items	<u>381,995</u>	<u>253,159</u>
INCOME TAXES		
Deferred	175,000	118,400
Alberta Royalty Tax Credit	(34,900)	(33,260)
	<u>140,100</u>	<u>85,140</u>
Earnings before extraordinary items	<u>241,895</u>	<u>168,019</u>
EXTRAORDINARY ITEMS		
Gain on repurchase of 9% debentures	500	24,525
Recovery of deferred income taxes	175,000	126,000
	<u>175,500</u>	<u>150,525</u>
NET EARNINGS	417,395	318,544
Deficit at beginning of year	(1,430,134)	(1,748,678)
DEFICIT AT END OF YEAR	<u><u>\$(1,012,739)</u></u>	<u><u>\$(1,430,134)</u></u>
EARNINGS PER SHARE, based on weighted average number of shares outstanding		
Earnings before extraordinary items	<u>\$0.08</u>	<u>\$0.06</u>
Net earnings	<u><u>\$0.14</u></u>	<u><u>\$0.12</u></u>

OMEGA HYDROCARBONS LTD.

CONSOLIDATED BALANCE SHEET AS AT DECEMBER 31, 1977

ASSETS

	<u>1977</u>	<u>1976</u>
CURRENT ASSETS		
Cash and short-term deposits	\$ 80,000	\$ 108,063
Accounts receivable	140,573	110,416
Income taxes recoverable	34,900	33,260
Current portion of notes receivable (note 4)	28,333	—
	<u>283,806</u>	<u>251,739</u>
NOTES RECEIVABLE (note 4)	<u>56,667</u>	<u>—</u>
 FIXED ASSETS		
Petroleum and natural gas leases and rights together with exploration, development and equipment thereon, at cost	1,386,468	865,765
Accumulated depletion and depreciation	(683,518)	(612,518)
	<u>702,950</u>	<u>253,247</u>
 OTHER ASSETS		
Debenture issue expenses, at cost less amounts amortized	3,552	4,567
Drilling and other deposits	24,512	19,512
Investment in limited partnership, at cost	25,000	—
	<u>53,064</u>	<u>24,079</u>
	<u>\$1,096,487</u>	<u>\$ 529,065</u>

OMEGA HYDROCARBONS LTD.

CONSOLIDATED BALANCE SHEET AS AT DECEMBER 31, 1977

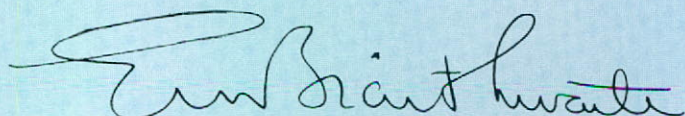
LIABILITIES

	<u>1977</u>	<u>1976</u>
CURRENT LIABILITIES		
Bank indebtedness, secured	\$ 41,242	\$
Accounts payable	<u>76,023</u>	<u>50,238</u>
	<u>117,265</u>	<u>50,238</u>
LONG-TERM DEBT (note 3)		
9% Series "A" convertible sinking fund debentures, due December 1, 1980	<u>93,000</u>	<u>95,000</u>

SHAREHOLDERS' EQUITY

CAPITAL STOCK (note 4)		
Authorized		
5,000,000 common shares of no par value		
Issued		
3,032,156 (1976 — 2,862,156) shares	1,898,961	1,813,961
DEFICIT	<u>(1,012,739)</u>	<u>(1,430,134)</u>
	<u>886,222</u>	<u>383,827</u>

Approved by the Board:



Director



Director

\$1,096,487

\$ 529,065

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION
YEAR ENDED DECEMBER 31, 1977

	<u>1977</u>	<u>1976</u>
SOURCE OF FUNDS		
Operations		
Earnings before extraordinary items	\$241,895	\$168,019
Items not involving working capital		
Depletion	50,000	20,953
Depreciation	21,000	13,116
Amortization of debenture issue expense	1,015	10,417
Deferred income taxes	<u>175,000</u>	<u>118,400</u>
	488,910	330,905
Issue of common shares (note 4)	<u>85,000</u>	<u>70,000</u>
	<u>573,910</u>	<u>400,905</u>
 APPLICATION OF FUNDS		
Notes receivable (note 4)	56,667	—
Fixed assets	520,703	117,795
Drilling deposits	5,000	12,075
Investment in limited partnership	25,000	—
Reduction in long-term debt	<u>1,500</u>	<u>72,875</u>
	<u>608,870</u>	<u>202,745</u>
 INCREASE (DECREASE) IN WORKING CAPITAL	 (34,960)	 198,160
Working capital at beginning of year	<u>201,501</u>	<u>3,341</u>
WORKING CAPITAL AT END OF YEAR	<u><u>\$166,541</u></u>	<u><u>\$201,501</u></u>

OMEGA HYDROCARBONS LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS YEAR ENDED DECEMBER 31, 1977

1. ACCOUNTING POLICIES

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its recently incorporated wholly-owned subsidiary, Omega Oil & Gas Ltd.

Oil and Gas Operations

The Company follows the full cost method of accounting for costs related to the exploration and development of petroleum and natural gas properties. Such costs, including production equipment, are accumulated on an area of interest basis and are amortized on the unit of production method based on estimated recoverable oil and gas reserves in each area or are written off to income if exploration activities in any area are determined to be unsuccessful.

2. INCOME TAXES

As of December 31, 1977, the Company had approximately \$690,000 of exploration and development expenditures and undepreciated capital costs available for deduction against future taxable income (subject to final determination by taxation authorities).

3. LONG-TERM DEBT

The 9% debentures are subject to annual sinking fund payments of \$50,000. As of December 31, 1977 debentures had been repurchased sufficient to satisfy the 1978 sinking fund obligations and \$7,000 principal amount of debentures remained to be applied against the 1979 obligation.

The debentures are convertible into common shares, prior to maturity or cancellation, at \$2.00 per share to August 31, 1979. No debentures have been converted to December 31, 1977.

4. CAPITAL STOCK

a) During 1977 the Company issued 170,000 common shares to certain officers (including a director) and employees for promissory notes totalling \$85,000, on exercise of rights granted in November, 1976 under the Company's "Share Purchase Plan". The promissory notes are non-interest bearing and repayable in three equal annual instalments up to October 31, 1980.

b) As of December 31, 1977 common shares were reserved as follows:

i) 130,000 shares under the Company's "Share Purchase Plan" for issue to officers and employees from time to time as determined by the directors of the Company.

ii) 46,500 shares for issue on conversion of the outstanding 9% debentures.

iii) 500,000 shares under the terms of a share option agreement dated December 9, 1977 for issue in return for drilling funds to be made available to the Company as follows:

100,000 shares at \$1.15 per share for each \$1 million (up to a total of \$2 million) received and expended prior to December 31, 1978

150,000 shares at \$1.60 per share for an additional \$1.5 million received and expended prior to December 31, 1979

150,000 shares at \$2.40 per share for an additional \$1.5 million received and expended prior to December 31, 1980

The optionee may exercise each of the above options during a specified period (up to six months) from the date the funds are expended but no exercise may involve less than an aggregate purchase price of \$98,000.

Failure by the optionee to provide the funds or failure by the Company to have expended such funds in any of the option periods shall serve to terminate the Agreement.

5. STATUTORY INFORMATION

Remuneration paid to directors and senior officers (including all employees) of the Company during 1977 amounted to \$68,088.

AUDITORS' REPORT

To the Shareholders of
Omega Hydrocarbons Ltd.

We have examined the consolidated balance sheet of Omega Hydrocarbons Ltd. as at December 31, 1977 and the consolidated 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 consolidated financial statements present fairly the financial position of the company as at December 31, 1977 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 31, 1978

THORNE RIDDELL & CO.
Chartered Accountants

