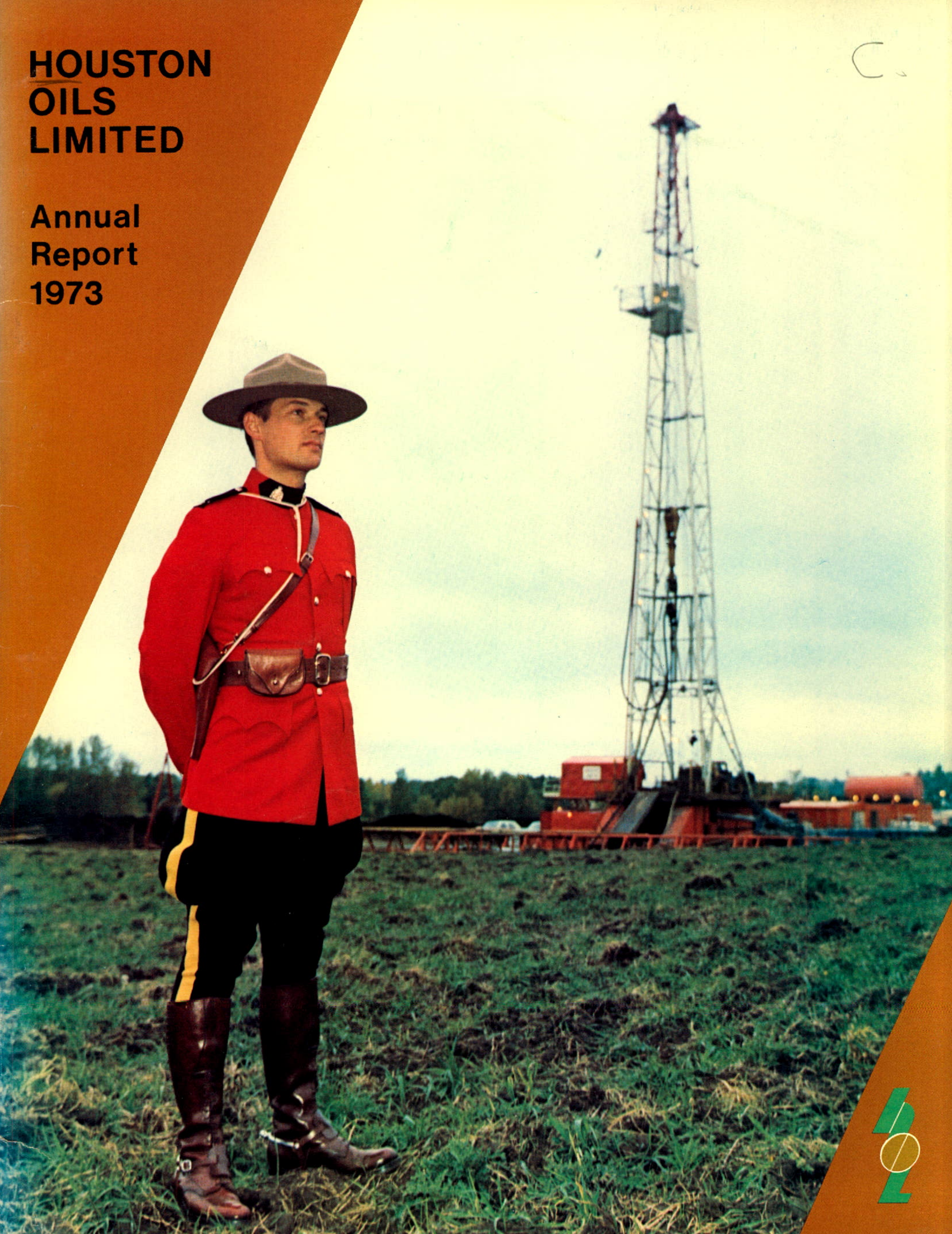
HOUSTON OILS LIMITED

Annual Report 1973



cover

During 1973 the Royal Canadian Mounted Police are celebrating their 100th anniversary. Houston Oils Limited, as a Canadian company, congratulates them on their outstanding service during this period.

We would like to thank RCMP Superintendent R. A. Vaughn, Constable M. J. Ellis and Corporal R. G. Barr for the picture on our cover.

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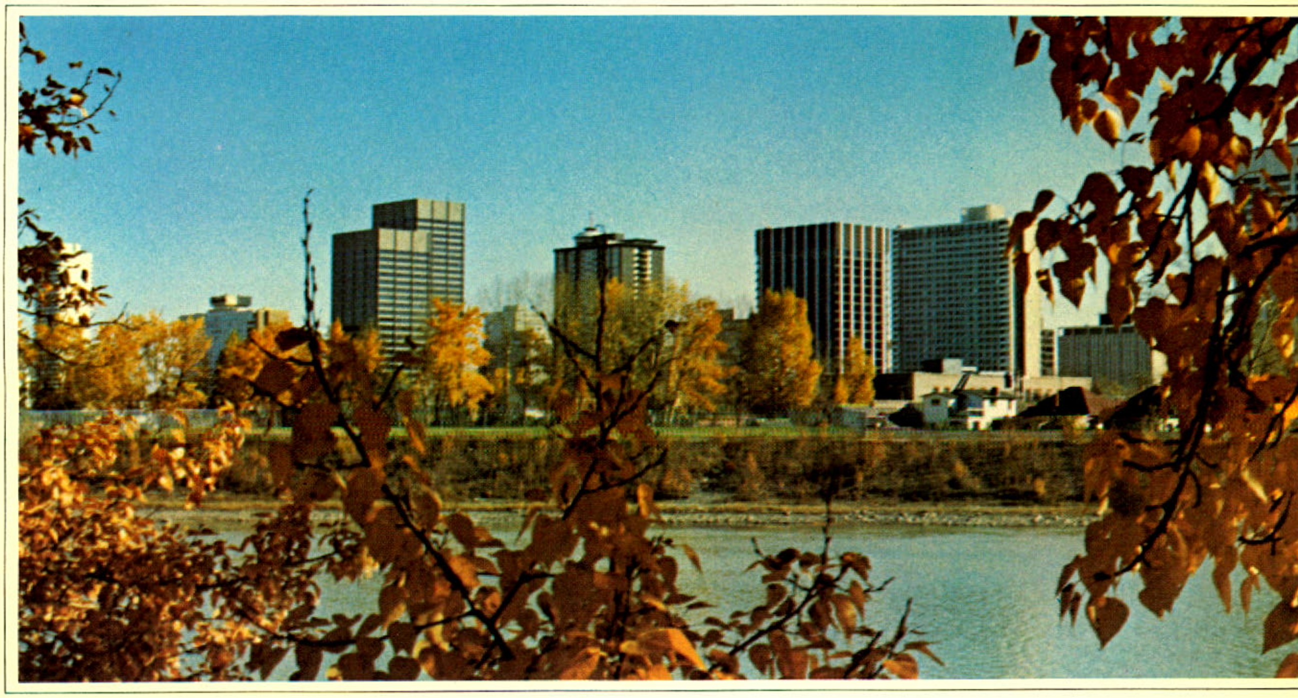
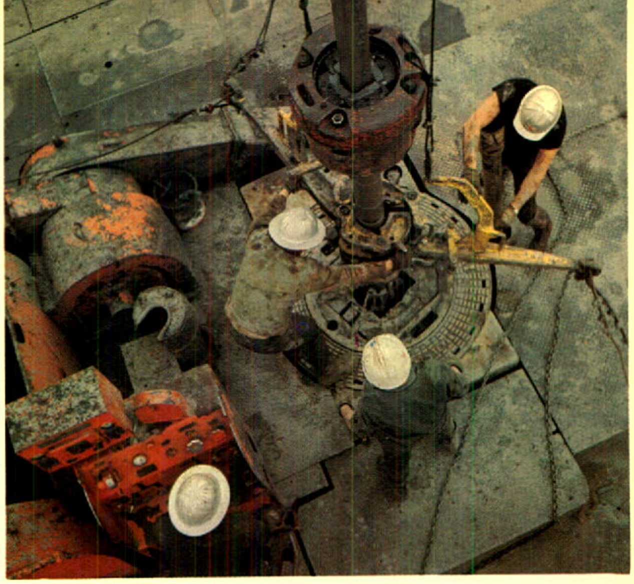
HOUSTON OILS LIMITED and Subsidiary Companies

1973 highlights

- Oil and Gas production revenues after royalties were increased 45.6% to $967,041.
- Proven Oil reserves were increased 37.7% and probable reserves by 20.4%.
- Proven Gas reserves were increased by 37.1% and probable reserves by 1.5%.
- $5,000,000 was added to working capital through the placement of a convertible note.
- A $6,000,000 two year exploration agreement was entered into with Marline Oil Corporation.
- The Company's worldwide net acreage holdings were increased 146% to 3,804,422 acres.
- Transalta Minerals Ltd. was acquired as a wholly owned subsidiary. Its main asset is the ownership of 36,016 acres of oil and gas mineral titles located primarily in gas areas of Eastern and Southern Alberta.
- Bridger Petroleum Corporation and Ensign Oils, Inc., both U.S. subsidiaries, were merged into one company with Bridger being the surviving company.



report to the shareholders



Cash flow for the year was $880,904 or 12.7¢ per share. Net income was $506,533 or 7¢ per share. These figures were calculated using the weighted average number of shares outstanding during the year and by using the "full cost" method of accounting. Company management made the decision to change its system of accounting to the "full cost" method in order to present corporate results to the shareholders on the basis most comparable to the industry. The full cost accounting method is used by most oil and gas companies of approximately the same size as Houston. A complete discussion of this method of accounting has been added to the note section of this report by company auditors.

Drilling operations continued at an accelerated pace by virtue of the Company's excellent working capital and a $6,000,000, two year exploration agreement with Marline Oil Corporation. Under the terms of the Marline-Houston exploration agreement Houston, as consideration for managing the Marline funds, will receive a management fee, an overriding royalty and the right to convert the overriding royalty to 40% of Marline's working interest after Marline has recovered its original investment.

The Company participated in the drilling of 155 wells, of which 106 were exploratory tests and 49 were development wells. The exploratory tests resulted in 26 gas wells and 3 oil wells. The development program resulted in 30 gas wells and 2 oil wells. Our overall success ratio for the year was 39.3%, as compared to 43.4% last year.

Financially, the Company was further strengthened by the addition of $5,000,000 to working capital through the sale of a fifteen year convertible subordinated note, which is convertible into Houston shares at $4.25 per share. This note was placed with Neil A. McConnell, a Director and substantial shareholder.

During the year the Company continued to grow through the development and acquisition of additional oil and gas reserves and increased production revenues. Substantial increases were made in our land holdings on promising plays throughout the world. Our exploration program continued to emphasize an economically sound balance between low to medium risk - near term cash flow prospects, and high

ACKNOWLEDGMENT

During the year Mr. William A. Clarke resigned as a Director of the Company. Mr. Clarke was a valued member of the Board of Directors and on behalf of the shareholders we wish to extend our sincere thanks for his service to the Company and to wish him every success.

risk - long term prospects which could result in substantial petroleum and natural gas reserves. In this latter case your Company will be participating in several prospects during the ensuing year which have large reserve potential.

We reported in our last Annual Report that the oil and gas industry was in a state of optimism; however, considerable confusion now prevails due to the worldwide supply difficulties created by the recent Middle East war and the resulting oil embargo by several Arab Nations. Here in Canada serious problems have arisen between the Province of Alberta and the Federal Government over the Federal Government's imposition of an export tax on oil. Our industry is watching these developments with a considerable amount of anxiety.

World authorities on energy matters are now convinced the days of cheap energy sources are over. The oil and natural gas reserves we have already discovered will be marketed at steadily rising prices. The improved price levels will provide a powerful new incentive for exploration in politically stable countries.

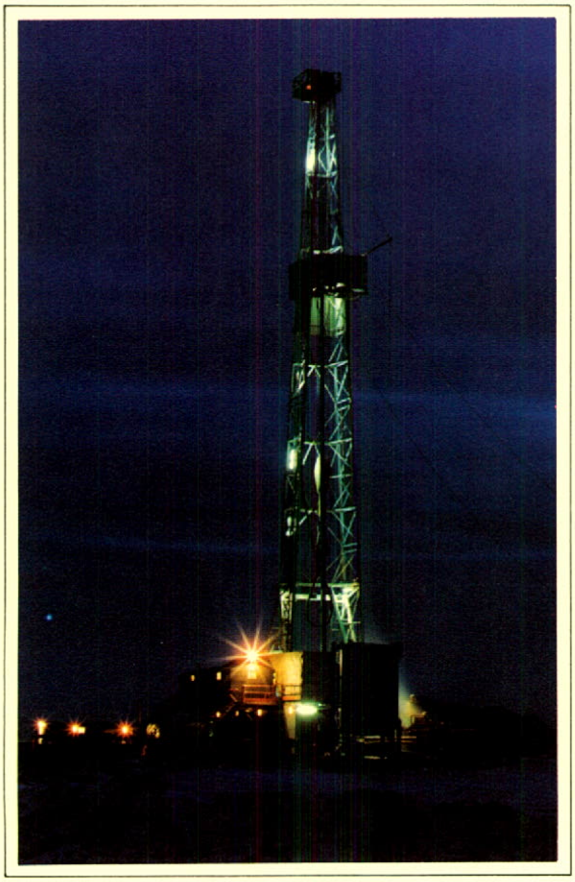
Higher prices for oil and gas will help to offset accelerating exploration costs and to create an improved financial climate which will allow the oil and gas industry to attract the tremendous amount of capital it will require to help solve the energy shortage which presently plagues much of the world.

ON BEHALF OF THE BOARD

A.E. Whitehead

A.E. Whitehead
President

exploration and development



Petroleum and Mineral exploration and development of properties in Canada, the U.S. and several overseas areas was significantly increased. This is particularly evident in the number of wells in which we participated during the year (155 gross and 63.9 net wells). From these totals Houston successfully completed 61 gross gas and oil wells or 23.9 net gas and oil wells. Of these wells 8 were indicated to be new pool discoveries and additional follow-up drilling will take place during 1974. Our concentrated efforts in building our land inventory throughout the world are reflected in the large increase in our net acreage holdings. Extensive seismic and/or drilling programs will be completed on several of the new prospect areas during the forthcoming year.

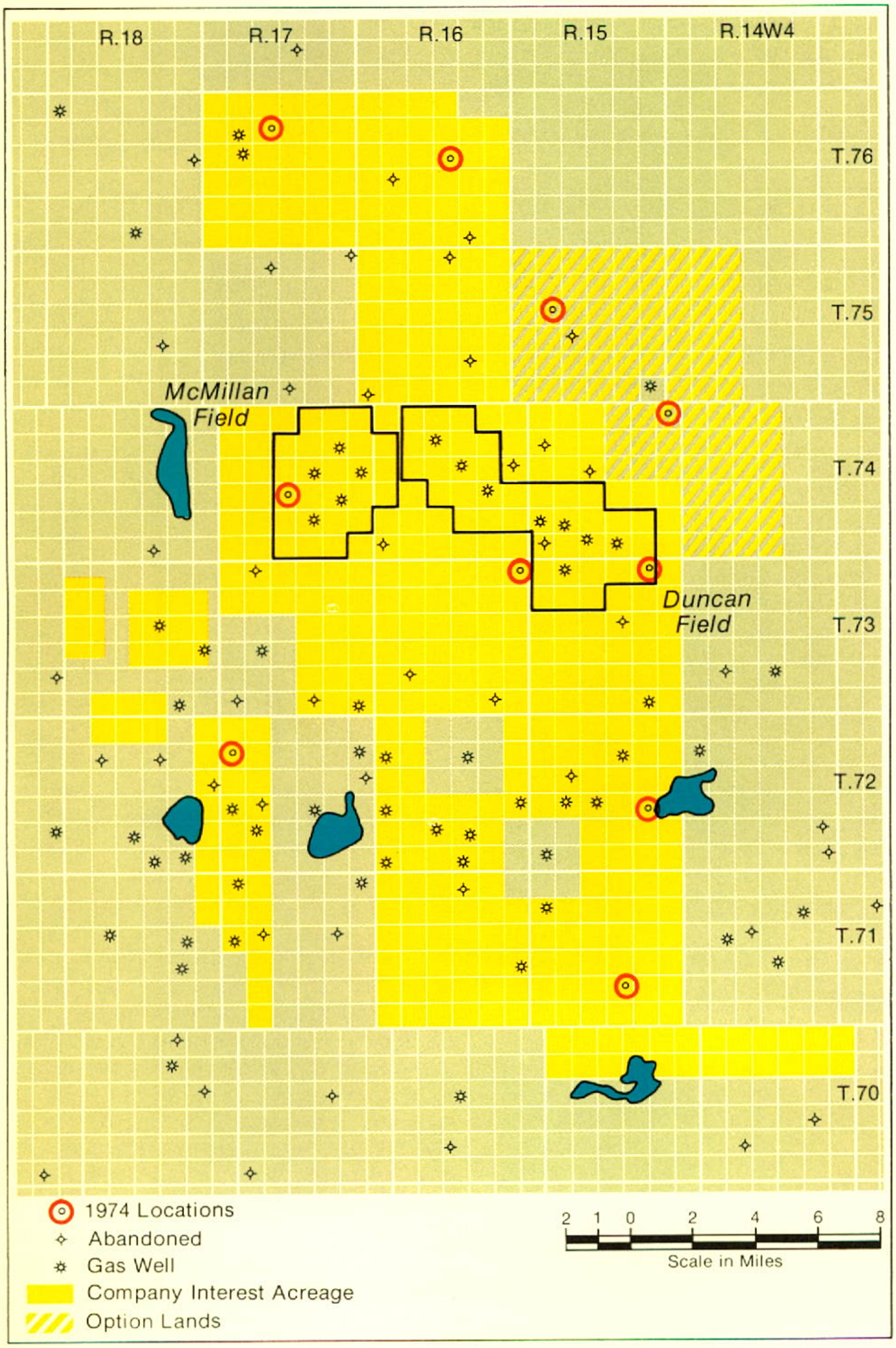
CANADA

Alberta - A total of 18 exploratory and development tests were drilled in the Wandering River Area of northeastern Alberta, of which 14 were indicated gas wells. This brings the number of Houston working interest gas wells in this project to 33. Fifteen exploratory and development test wells are scheduled to be drilled on this prospect during the coming winter season; two rigs are under contract to drill these test wells. The first ten locations are shown on the accompanying map. After this winter's drilling is completed the Company should have increased its proven gas reserves to the point where it can expect to market gas in 1975.

Expansion of land holdings has been made in several potential shallow gas areas of Central Alberta. To date four gas wells have been completed and an active drilling program is planned for the ensuing fiscal year. One of the larger acquisitions is a 98,080 acre farm-in block on which the Company committed to drill seven test wells. As of the Company's year-end, two of these tests have been drilled which resulted in dry holes. Subsequent to year-end, the drilling of three additional tests resulted in one excellent dual zone gas discovery, for which follow-up drilling is planned. The Company and Marline each have interests ranging between 25% to 50% in lands earned in this project.

Northeast British Columbia - Negotiations are well advanced to market gas from three 1972/73 successful Cretaceous wells at Buick Creek; start up of gas sales on this prospect at greatly improved prices is anticipated in early 1974. At the Grizzly - Monkman Pass prospect, one additional deep test was completed on a 6,588 acre block of leases on which the Company has a 3% gross overriding royalty. The operator of the Grizzly project has signed a gas contract with Alberta and Southern, and estimates that several trillion cubic feet of gas could be proven with additional drilling and that gas sales should commence in 1976.

WANDERING RIVER Alberta



Arctic - Magnorth Petroleum Ltd. lands in the Northwest Passage area of the Arctic Islands were extensively shot this past summer by Norlands Petroleum Ltd., a wholly owned subsidiary of Northern Natural Gas Company. Norlands completed a 3,305 mile marine seismic program on both new areas and existing structures and data is now being processed. Houston has a 10.5% equity position in Magnorth which controls 14,197,690 acres of oil and gas permits in attractive geologic basins between the Arctic Islands. Under terms of the Magnorth-Norlands agreement Norlands can earn up to 50% of Magnorth's acreage by spending approximately $36,000,000. Should the necessary sophisticated drilling equipment be available Norlands is hopeful it will drill a test well on the Magnorth acreage in 1975.

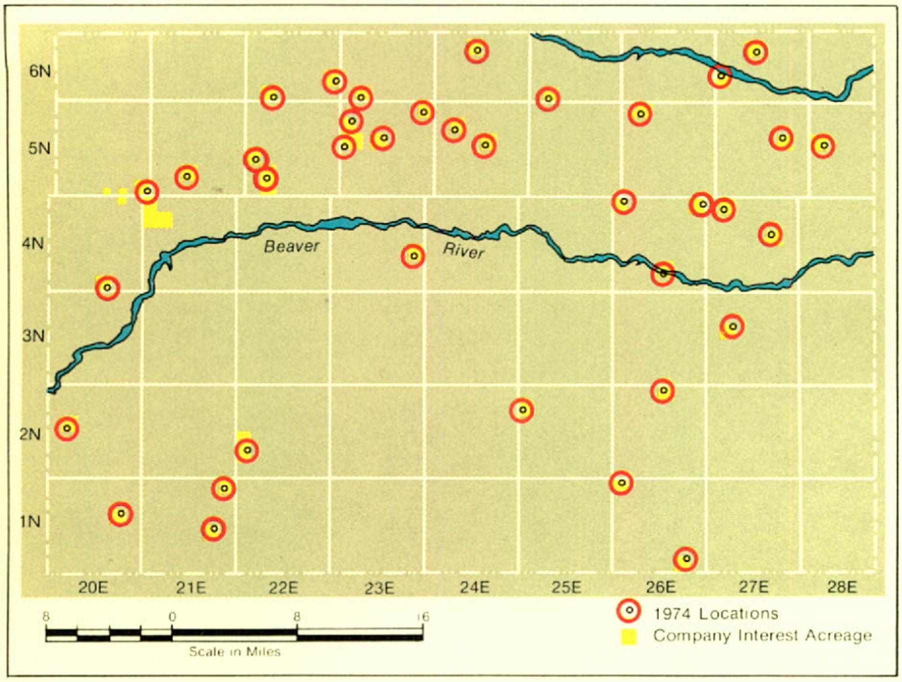
UNITED STATES

Western Oklahoma - Two major gas projects in the Anadarko Basin were undertaken by the Company, through its U.S. subsidiary, Bridger Petroleum Corporation. Basically, the prospects are of a semi-proven nature which involves drilling near producing gas fields and have become financially attractive due to the dramatic increase in U. S. natural gas prices. The Marline drilling funds were committed to a 20 well program in northwestern Oklahoma where there are a number of gas fields. At year-end Marline had drilled 9.38 net wells of the 20 well commitment with 4.25 being completed as net gas wells for a 45% success ratio. The balance of this program will be completed during the next six to eight months. Bridger undertook for its own account, an aggressive lease acquisition program in Beaver County of the Oklahoma Panhandle and acquired some 18,995 net acres of leases which for the most part offset producing gas wells. We are presently negotiating with several U.S. gas purchasers to advance the funds to drill approximately 30 net wells on these leases during the next eighteen months. It is anticipated that gas prices after BTU adjustment will be greater than 70¢/MCF with sales to commence in mid 1974.

Western Utah - Bridger and Marline, together with another company, have acquired 522,000 acres of leases which we feel have major oil and gas reserves potential. Objectives are Tertiary sandstones and Devonian reefs. Bridger has a 43.75% working interest and Marline a 12.5% working interest. A gravity survey has been completed on the project and prospects defined. We are now attempting to interest other companies in drilling two deep exploratory tests during 1974.

Montana - In late November, 1972, the large Tiger Ridge Gas Field located in Northern Montana went on production which resulted in a substantial increase in Company gas revenues. Amendments to the purchase contract with Northern Natural on this gas have recently been signed whereby the price was increased from 23.5¢ per thousand cubic feet to 40¢ per thousand cubic feet. This increase is subject to the approval of the Federal Power Commission; however it is anticipated that such approval will be received early in 1974. At Sherard, some 20 miles south of Tiger Ridge, gas sales are expected to commence in December, 1973. The contract on this gas has also been amended to provide for the 40¢ per MCF price. Development drilling plans in both Tiger Ridge and Sherard call for approximately 30 wells this coming year. In other areas of Montana the Company expanded its land holdings and plans additional acquisitions during the next year. Two excellent Montana geological consultants are under contract which gives the Company prior right to any geological prospects which they originate.

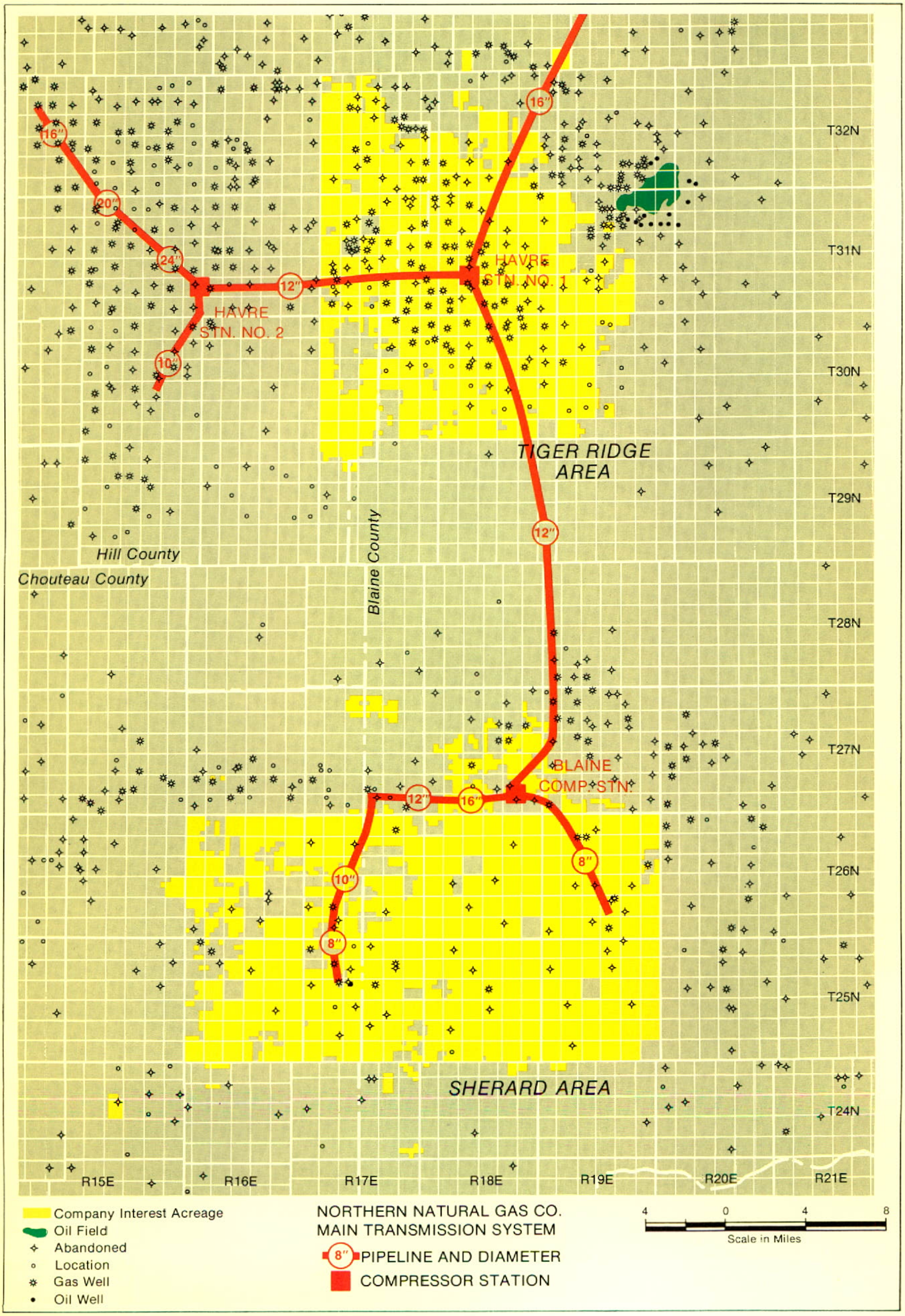
BEAVER COUNTY Oklahoma



Texas - A 21,000' test will be drilled in mid 1974 on a deep onshore gas prospect in the Gulf Coast area of Texas. A seismic program conducted on this prospect is very encouraging. Bridger and Marline each have a 6.25% interest in the prospect. We now have about 5,000 acres under lease, and by the time drilling is commenced the lease block should comprise 6,000 to 8,000 acres.

Colorado - A 9,000' wildcat was drilled on an 8,700 acre block covering a large structure in Big Horn County. While the test well was an apparent oil discovery, it had to be abandoned prior to full evaluation due to a series of serious mechanical problems. All participants in this project have indicated their willingness to drill another test as soon as weather permits next spring. Bridger has a 12½% interest.

SHERARD - TIGER RIDGE Montana



FOREIGN

Dutch North Sea - An extensive seismic survey has just been completed on Block E/7 in which the Company has a 10% working interest. This program was carried out in an attempt to further delineate a large structure underlying the block as disclosed by previous seismic. Notomas Company, as project operator, is currently evaluating this data. On Block Q-11, we have agreed to participate in a seismic program in the Spring of 1974; the Company has a 4.5% interest. An apparent gas discovery was made recently by another operator on Block Q-7, which corners our block to the northwest.

British North Sea - Houston Oils (U.K.) Limited has a 33 1/3% interest in Blocks 43/13b, 43/17b and 43/18b in the British sector, consisting of approximately 91,000 acres. A seismic program was carried out during the year with encouraging results. A large northwest trending structure is indicated with a significant portion underlying our acreage. In late November the Zapata-Clinton group will drill a test on diagonally offsetting Block 43/11. Their location is on the structural trend approximately eight miles northwest of our Block 43/17b and the results of this test will materially help determine our future drilling plans.

Norwegian North Sea - On September 17th the Company participated in the ODIN Group that submitted applications on a total of 10 blocks offered for bid in the Norwegian sector of the North Sea. Our interest in this substantial group headed by Notomas, as operator, is 11%. Applications were based on extensive geological and geophysical data acquired and interpreted prior to submission. It is anticipated that the Norwegian Government will make awards in the spring of 1974.

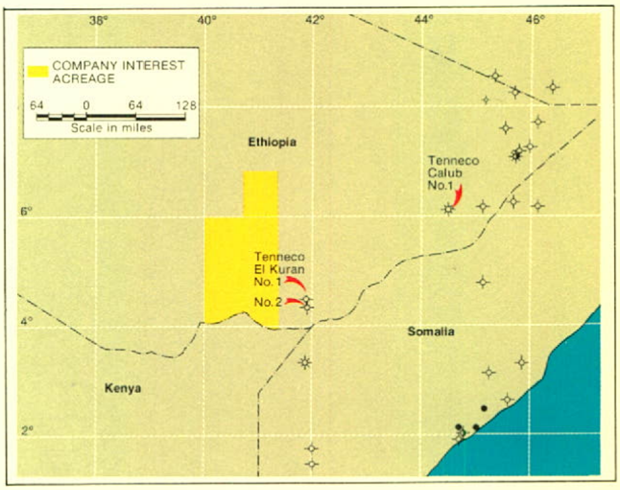
Spain - Subsequent to year-end, Houston Oils of Spain, Limited was awarded a 33 1/3% interest in four exploratory blocks located offshore in the Gulf of Cadiz. The blocks consist of a total of 376,224 acres. Exploration requirements call for a seismic program to be conducted during the first two years with a well to be drilled during the next four year period if justified by the seismic interpretation.

Ethiopia - The Imperial Ethiopian Government awarded an 8,303,200 acre petroleum concession in which the Company has a 25% interest. Located in Southern Ethiopia, the block is adjacent to a concession where drilling carried out by Tenneco, Texaco and Chevron has resulted in one important gas discovery. A photogeological study is presently being carried out, which will then be followed by a reconnaissance seismic program.

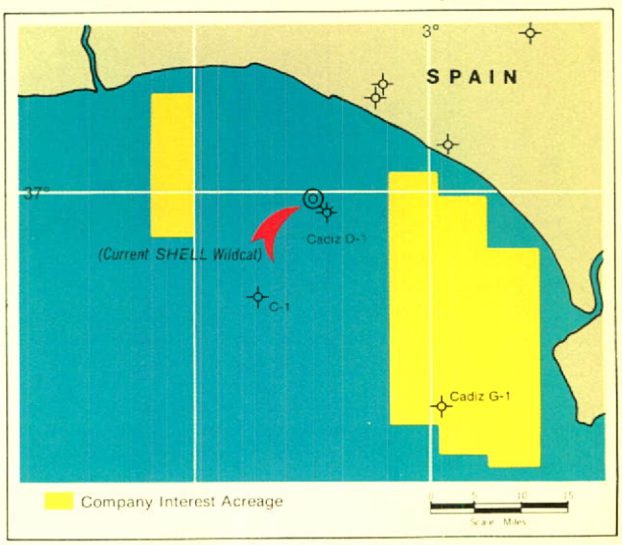
Indonesia - Three offshore test wells were drilled and additional marine seismic completed in the Strait of Malacca. Although all three tests were abandoned, one had a significant, but non commercial, oil recovery. Also, adjacent to our concession, Caltex completed a discovery for 3,000 bbls oil per day and a trade of seismic data has been made to determine if their structure extends to our block. Results to date have therefore given sufficient encouragement to merit continued exploration. During mid 1974 we will drill at least four more wildcats on seismically well defined structures. Bridger has a 4.33% interest in this 8,000,000 acre concession.

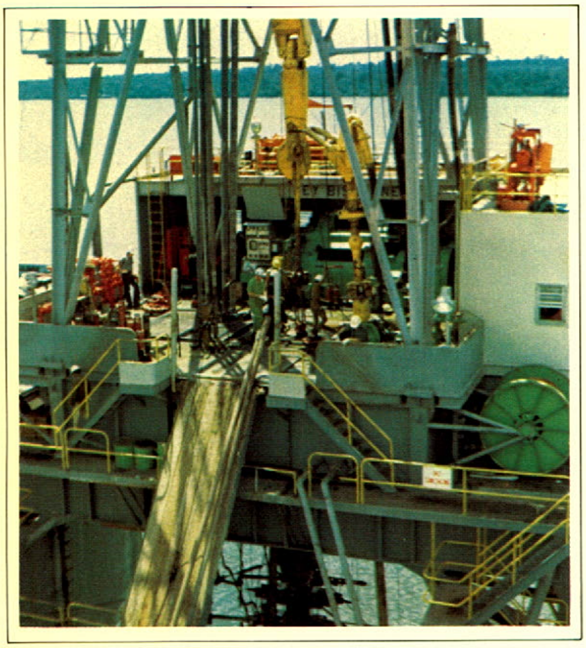
Abu Dhabi - Amerada Hess Corporation commenced drilling operations on the offshore Abu Dhabi concession on August 4, 1973, in which Bridger holds a 5% carried interest. Subsequent to our year-end, production casing was run in this well in order to conduct a testing program on prospective formations.

ETHIOPIA East Africa



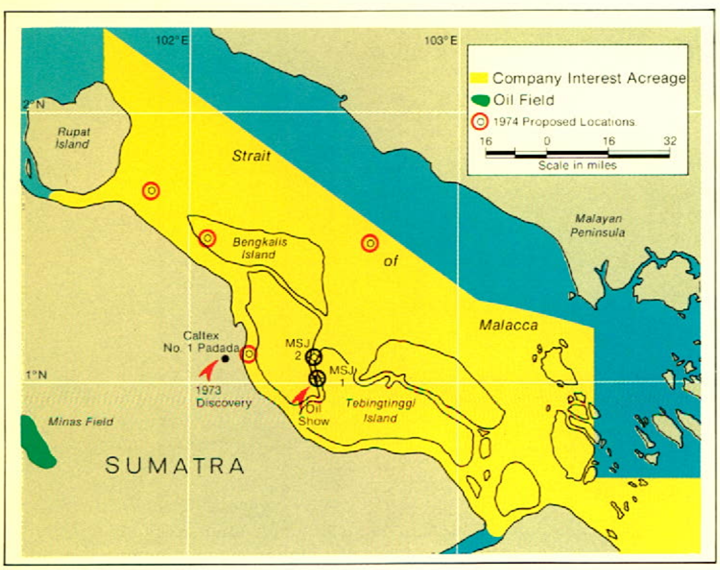
GULF OF CADIZ Southwest Spain



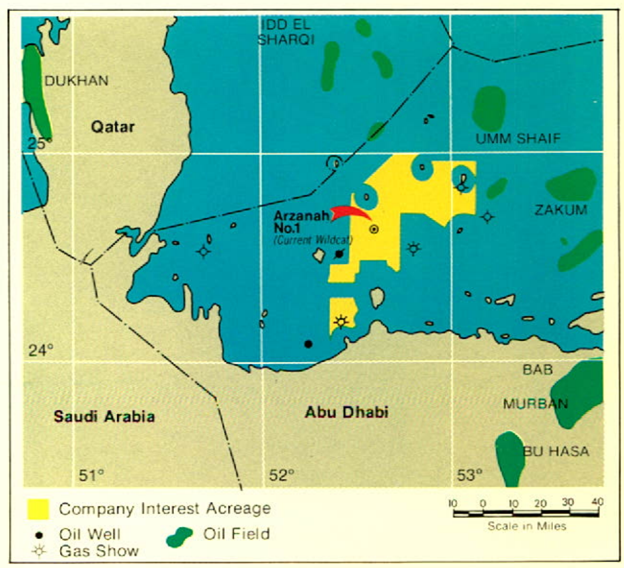


Rig floor closeup of Key Biscayne drilling Operation Strait of Malacca, Indonesia.

INDONESIA



ARABIAN GULF Abu Dhabi



MINERAL EXPLORATION

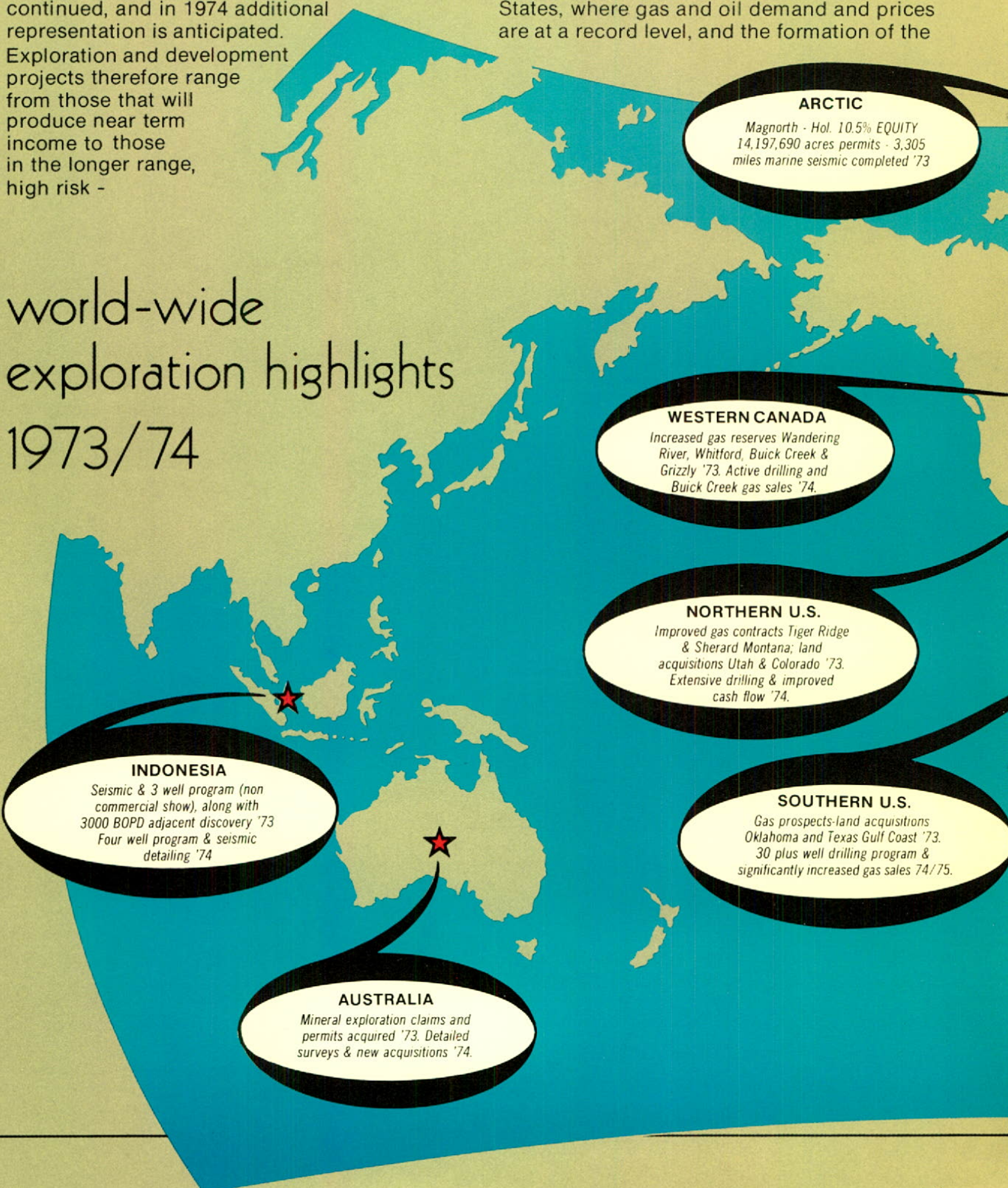
The Company continued its exploration for hard rock minerals primarily through third parties experienced in this field. In Canada our mineral exploration is carried out through Aquarius Mines Ltd. Houston and other companies provide financial support to Aquarius in return for an equity position. Aquarius then obtains other companies to perform additional exploratory and evaluation work on its properties.

The Australian mining exploration syndicate in which the Company became a participant last year, has acquired several uranium prospects on which exploration is being carried out by third parties.

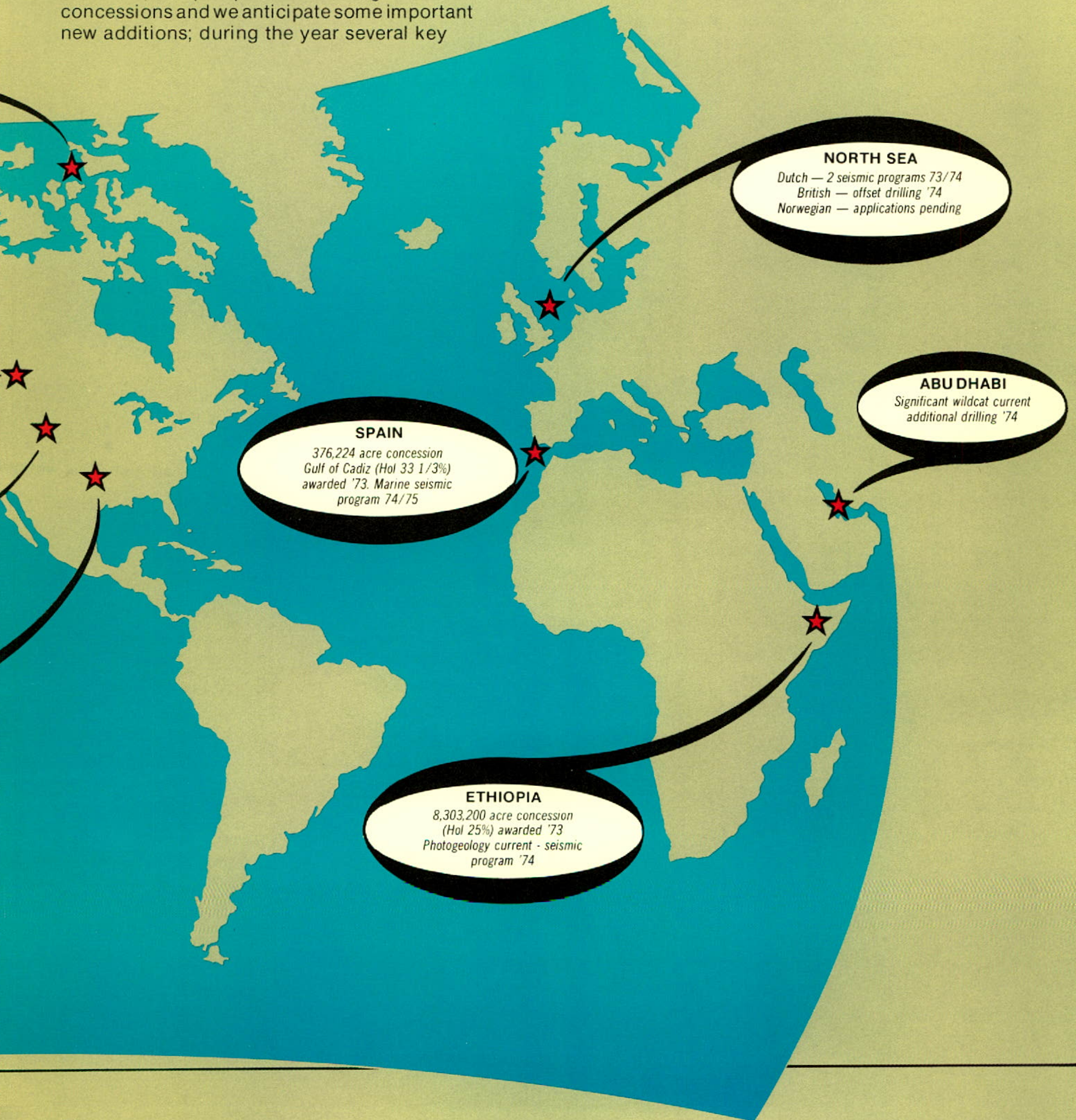
During this past year Bridger entered into a limited partnership agreement with the Nokota Company and Charles Bruce. Bridger and Nokota provide financial support to the "BNB Partnership" which will be managed by Charles Bruce. Mr. Bruce has 20 years experience in the exploration and mining of gold, silver, copper, lead, zinc, antimony, tin, wolfram and coal. He resigned as Vice President - Mining Department of DeGolyer and MacNaughton to join with Bridger and Nokota. To date, the partnership has acquired mining properties in Costa Rica and Colorado and is working on projects in Scotland, Brazil, New Mexico, California and Mexico.

Houston's participation in petroleum prospects and mining ventures around the world is best illustrated on a global basis. Particular emphasis is being placed on expanding and diversifying our interests to those areas of high potential and those of excellent reserve marketability. This policy will be aggressively continued, and in 1974 additional representation is anticipated. Exploration and development projects therefore range from those that will produce near term income to those in the longer range, high risk - high return category. During 1973 gas and oil reserves were increased in Canada and the United States, important land acquisitions were made on both domestic and foreign prospects, and mineral exploration was accelerated. Of particular note are our most recent acquisitions in the southern United States, where gas and oil demand and prices are at a record level, and the formation of the

world-wide exploration highlights 1973/74



new wide ranging mineral exploration venture of the Bridger-Nokota-Bruce partnership. In 1974 petroleum and mineral exploration and development will continue at a stepped up pace and several significant new prospects will be tested. Negotiations are underway on new domestic prospects and foreign concessions and we anticipate some important new additions; during the year several key wildcats will probably be drilled by other companies on concessions adjacent to Company prospects. These factors all add to a promising year for Houston in 1974. Summaries of some of the more important highlights are shown below.



land holdings summary

SEPTEMBER 30, 1973

WORKING INTEREST IN OIL & GAS RIGHTS

	Gross Acres	Net Acres
CANADA		
Alberta	615,728	240,730
British Columbia	30,541	11,879
East Coast (Offshore)	2,762,749	661,715
Manitoba	1,320	858
Ontario	3,511	1,509
Saskatchewan	15,623	6,520
Canadian Total	3,429,472	923,211
U.S.A.		
Alaska	5,112	5,112
Colorado	14,760	2,899
Montana	500,598	63,704
Nebraska	1,524	572
New Mexico	957	437
North Dakota	153,621	38,806
Oklahoma	25,966	19,759
Utah	249,729	234,037
Texas	5,394	449
Wyoming	2,604	868
U.S. Total	960,265	366,643
INTERNATIONAL		
Abu Dhabi	583,786	29,120
British North Sea	91,602	30,534
Dutch North Sea	138,000	11,635
#Ethiopia	8,302,200	2,075,550
Indonesia	8,000,000	344,000
Italy	133,287	23,729
International Total	17,248,875	2,514,568

 # Includes all mining rights

	Gross Acres	Net Acres
Total Working Interest in Oil & Gas Properties	21,638,612	3,804,422

NET CARRIED INTEREST IN OIL & GAS RIGHTS

	Gross Acres	Net Acres
Arctic Islands	737,286	11,059
Northwest Territories	55,167	2,067
Yukon	138,642	25,996
	931,095	39,122

Royalty Interests

Arctic Islands	6,455,637	.25% overriding royalty
Turkey	494,200	1.523% overriding royalty
Various Canadian and U.S. Lands	320,470	Overriding royalty varies 1 to 15%
	7,270,307	

Mineral Titles Owned

Alberta	39,382	39,382
Montana	320	160
	39,702	39,542

Working Interests in Mining Rights

Colorado	14,900	2,235
Northwest Territories	4,760	2,023
Saskatchewan	7,330	3,665
Utah	14,980	3,745
	41,970	11,668

During the past fiscal year Houston has increased its net land holdings by more than 140%. The most dramatic increases were in international areas where our net holding increased by 379% and in the United States where the increase was 167%. Canadian holdings increased by a significant 10%.

exploration and production summary

DRILLING ACTIVITY

	1973	1972
Gross Wells	155	106
Net Wells	63.9	16.1
Net Gas Wells	20.7	6.60
Net Oil Wells	3.2	.80

PRODUCTION

	1973	1972
Daily Oil (Bbls.)	576	548
Yearly Oil (Bbls.)	210,393	200,782
Daily Gas (Mcf)	4,087	740
Yearly Gas (Mcf)	1,491,931	271,100
*Take or Pay Gas:		
Daily (Mcf)	896	6,060
Yearly (Mcf)	327,000	2,200,000

**Gas for which Company is being paid even though it is not produced.*

RESERVES (NET AFTER ROYALTY)

PROVEN	1973	1972
Oil (Bbls)	2,789,496	2,026,135
Gas (Mcf)	97,954,000	70,433,385
PROBABLE		
Oil (Bbls)	3,359,000	2,789,638
Gas (Mcf)	37,995,000	37,438,667
TOTALS		
Oil (Bbls)	6,148,496	4,815,773
Gas (Mcf)	135,949,000	107,872,052

consolidated balance sheet

assets

	September 30, 1973	September 30, 1972 Restated
Current assets		
Cash	$ 1,231	$ 35,933
Deposit certificates	8,921,520	6,691,440
Accounts receivable	927,616	582,155
Marketable securities, at cost (market value $1,885,303)	1,527,132	16,105
Note receivable (note 3)	25,000	—
Joint venture drilling fund receivable (note 2)	622,519	—
Prepaid expenses	82,302	27,260
	12,107,320	7,352,893
Property and equipment, net (note 4)	10,227,569	5,501,297
Other assets, at cost		
Note receivable (note 3)	75,000	25,000
Drilling and exploration deposits	102,369	99,354
Investments (no quoted market value)	80,789	65,504
Sundry	11,623	8,548
	269,781	198,406
	$22,604,670	$13,052,596

Approved on behalf of the Board,

Director

Director

The accompanying notes are an integral part of these financial statements

liabilities

	September 30, 1973	September 30, 1972 Restated
Current liabilities		
Accounts payable	**$ 1,120,630**	$ 751,958
Unexpended joint venture drilling fund advances (note 2)	**2,232,171**	1,790,377
Current portion of long term debt	**180,000**	140,000
	3,532,801	2,682,335
Long term debt (note 5)		
Development loans	**178,447**	300,681
Prepayment of future gas deliveries	**849,644**	722,088
	1,028,091	1,022,769
Less: portion due within one year	**180,000**	140,000
	848,091	882,769
Convertible subordinated note	**5,000,000**	—
	5,848,091	882,769

shareholders' equity

Capital stock (note 6)		
Authorized		
20,000,000 shares of no par value		
Issued		
7,760,607 shares (1972 - 6,645,000 shares)	**13,014,544**	9,784,791
Retained earnings (deficit)	**209,234**	(297,299)
	13,223,778	9,487,492
	$22,604,670	$13,052,596

The accompanying notes are an integral part of these financial statements

consolidated statement of income

	Year Ended September 30, 1973	Year Ended September 30, 1972 Restated
Income		
Oil, gas and ore sales, less royalties	**$ 967,041**	$ 526,103
Interest	**296,327**	65,962
Other	**640,176**	82,436
	1,903,544	674,501
Expenses		
Production	**246,232**	233,627
Interest	**180,957**	32,020
General and administrative	**595,451**	173,013
	1,022,640	438,660
Cash flow from operations	**880,904**	235,841
Non-cash expenses		
Depletion	**287,749**	136,092
Depreciation	**86,622**	64,042
	374,371	200,134
Net income	**$ 506,533**	$ 35,707
Net income per share (note 9)	**$ .07**	$ .01

consolidated statement of retained earnings

	Year Ended September 30, 1973	Year Ended September 30, 1972
Deficit, beginning of year as previously reported	**$ (536,245)**	$(1,323,956)
Less: Adjustment of prior years (note 1)	**238,946**	990,950
As restated	**(297,299)**	(333,006)
Net income for the year	**506,533**	35,707
Retained earnings (deficit), end of year	**$ 209,234**	$ (297,299)

The accompanying notes are an integral part of these financial statements

consolidated statement of source and application of funds

	Year Ended September 30, 1973	September 30, 1972 Restated
Source of funds		
Funds provided by operations	**$ 880,904**	$ 235,841
Convertible note issued	**5,000,000**	—
Capital stock issued	**3,229,753**	5,050,000
Gas purchase prepayments received	**127,556**	—
Proceeds on disposal of property and equipment	**33,481**	1,179,208
	9,271,694	6,465,049
Application of funds		
Increase in notes receivable	**50,000**	—
Repayment of long term debt	**162,234**	393,280
Increase in drilling deposits	**3,015**	27,000
Acquisition of property and equipment	**5,134,124**	1,337,779
Other	**18,360**	16,706
	5,367,733	1,774,765
Increase in working capital	**3,903,961**	4,690,284
Working capital (deficiency), beginning of year	**4,670,558**	(19,726)
Working capital, end of year	**$8,574,519**	$4,670,558

The accompanying notes are an integral part of these financial statements

auditors' report

TO THE SHAREHOLDERS, HOUSTON OILS LIMITED

We have examined the consolidated balance sheet of Houston Oils Limited and Subsidiary Companies as at September 30, 1973 and the consolidated statements of income, retained earnings and source and application of funds for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion these consolidated financial statements present fairly the financial position of the companies as at September 30, 1973 and the results of their operations and the source and application of their funds for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year, except for the change in accounting for oil and gas operations (with which we concur) as outlined in note 1 to the consolidated financial statements.

Calgary, Alberta
December 6, 1973

Collins Love Eddis Valiquette & Barrow
CHARTERED ACCOUNTANTS

notes to financial statements

September 30, 1973

1. ACCOUNTING POLICIES

(a) BASIS OF CONSOLIDATION

The consolidated financial statements include the accounts of the company (which was formed in 1971 upon the amalgamation of two predecessor companies) and all of its subsidiaries. The amalgamation has been accounted for on a pooling of interests basis.

The acquisitions of the subsidiaries were treated as purchases. Any excess of initial cost over the underlying net book value of an acquired subsidiary has been allocated to the property and equipment account.

The accounts of the foreign subsidiaries have been converted to Canadian dollars on the following basis:

Current assets and current liabilities at the rate of exchange in effect at the year end.

Other assets and liabilities at the rate of exchange in effect at the date of the transaction.

The net exchange difference has been included in the statement of income.

(b) OIL AND GAS OPERATIONS

In prior years the companies followed the practice of capitalizing all lease acquisition costs and exploration costs. If the lease was subsequently surrendered, the accumulated costs were charged to income at the time of surrender. The costs of drilling unproductive wells were charged to income when the prospect area was abandoned. Lease acquisition costs and exploration costs of each producing area were amortized on the unit of production method based on estimated recoverable reserves of the area.

On October 1, 1972 the companies retroactively changed to the full cost method of accounting for oil and gas operations. Under this concept, all costs, including a portion of administrative expenses, relating to exploration for and development of oil and gas reserves are capitalized. Proceeds on disposal of properties are ordinarily deducted from costs without recognition of profit or loss. These capitalized costs are depleted on the unit of production method based on the estimated recoverable oil and gas reserves as determined by the companies' engineers.

The retroactive adjustment described above relates to the period from the inception of the companies to September 30, 1972 and results in an increase in the consolidated assets and a decrease in consolidated deficit of $238,946. Calculated on the previous basis there would have been a $134,662 net loss in the current year compared to net income of $787,711 in the previous year.

The company has included in capitalized costs of oil and gas properties an amount of $128,670 representing advances made in prior years to Tur-Kan Petrol Ltd., a company in which it formerly held a 35.3% share interest. In 1971 the company disposed of its share interest in a share exchange transaction and received an overriding royalty interest in each of the licenses then owned by Tur-Kan Petrol Ltd. Repayments of the advances will be out of future profits earned by Tur-Kan and will be deducted from capitalized costs. No gain or loss has been recognized in the accounts with respect to the share exchange transaction.

(c) MINING PROPERTIES

The companies follow the practice of initially capitalizing all lease acquisitions and exploration costs relating to mining properties on a prospect area basis. If a prospect area is subsequently abandoned, all capitalized costs relating to the area are charged to income. Capitalized costs relating to producing properties are amortized in the unit of production method based on estimated recoverable reserves of the area.

(d) DEPRECIATION

Depreciation of production and other equipment is provided on a straight line basis at rates designed to amortize the costs over the estimated useful lives of the assets.

(e) INCOME TAXES

For income tax purposes, the companies claim drilling, exploration and lease acquisition costs in amounts which exceed the related charges to income. As at September 30, 1973, the companies and their predecessors have incurred drilling, exploration and lease acquisition costs of approximately $8,850,000 which had not been claimed for tax purposes and which are available for carry-forward against future taxable incomes, subject in part, to timing and certain other limitations. Of this amount $5,050,000 is available for carry-forward by Canadian companies and the balance of $3,800,000 is available for carry-forward by the United States subsidiaries. Included in the $5,050,000 carry-forward by Canadian companies is $1,700,000 of expenditures which were incurred by the predecessor companies.

The companies believe that tax allocation accounting as recommended by the Canadian Institute of Chartered Accountants is not appropriate in the oil and gas industry and accordingly, no provision has been made for deferred taxes on timing differences. If the tax allocation basis had been followed, the deferred income tax provision would have been $193,500 ($.02 per share) in the current year and $12,000 (nil per share) in the prior year and net income would have been reduced accordingly. The accumulated tax reductions amounted to $175,000 at September 30, 1973.

2. JOINT VENTURE PARTICIPATION AGREEMENTS

(a) 1972 - 1973 DRILLING PROGRAMS

During the current year the company acted as manager of certain drilling programs which had commenced in the prior year. As a result, the company expended $3,951,694 in the current year on behalf of three investors who also were shareholders of the company. Of this amount $622,519 was owing to the company at September 30, 1973, including $388,429 from Neil A. McConnell, a director of the company.

(b) 1973 - 1974 DRILLING PROGRAM

During the current year the company and Marline Oil Corporation (Marline) entered into an agreement which requires Marline to contribute $6,000,000 to a 1973 - 1974 drilling program. The company is responsible for the overall direction of the program and for its services will be entitled to receive a management fee of 12½% of Marline's $6,000,000 commitment. Marline will receive 100% of the revenues accruing to the program and the company is to receive a 2% gross overriding royalty on such revenues until such time as Marline has received its $6,000,000 contribution, whereupon the company has the option to convert such royalty into a 40% working interest. At September 30, 1973 Marline had advanced $3,000,000 toward its commitment.

3. NOTES RECEIVABLE

Notes receivable, at September 30, 1973, are comprised of the following loans to officers and employees of the company:

1. D.R. Long, for the purpose of purchasing fully-paid shares of a predecessor company in 1969	$ 25,000
2. H.S. Robinson, for the purpose of purchasing fully-paid shares of the company in 1973 (note 6)	75,000
	$100,000

The loans are evidenced by non-interest bearing promissory notes payable on or before August 1, 1974 and May 1, 1978, respectively, and are secured by certificates representing 10,000 and 25,000 shares, respectively, of Houston Oils Limited, which certificates are deposited with The Canada Trust Company, as Trustee.

4. PROPERTY AND EQUIPMENT

Property and equipment consists of the following:

	Cost	Accumulated depletion and depreciation	Net 1973	Net 1972 (as restated)
Oil and gas properties including exploration and development costs thereon	$10,048,302	$ 641,565	$ 9,406,737	$4,825,317
Mining properties including exploration and development costs thereon	453,660	101,262	352,398	312,846
Production and other equipment	789,087	320,653	468,434	363,134
	$11,291,049	$1,063,480	$10,227,569	$5,501,297

5. LONG TERM DEBT

(a) DEVELOPMENT LOANS AND PREPAYMENTS OF FUTURE GAS DELIVERIES

These liabilities are non-interest bearing and are repayable at the rate of one-third of the proceeds from the sale of production from specific properties.

(b) CONVERTIBLE SUBORDINATED NOTE

On June 13, 1973 the company issued a $5,000,000 convertible subordinated note due May 31, 1988. The note bears interest at a rate of 1½% over the best rate which Bankers Trust Company shall charge from time to time on 90 day unsecured commercial loans. The note is convertible up to May 31, 1988 into 1,176,471 shares of the common stock of the company at a price of $4.25 per share.

6. CAPITAL STOCK

Issued capital stock of the company consists of the following:

	Number of shares	Stated value
Balance, September 30, 1972	6,645,000	$ 9,784,791
Stock options exercised	75,299	125,911
Share purchase warrants exercised	292,270	859,274
Issued on acquisition of properties	723,038	2,169,568
Issued for a note receivable (note 3)	25,000	75,000
Balance, September 30, 1973	7,760,607	$13,014,544

At September 30, 1973, 1,294,172 shares of the capital stock were reserved as follows:

117,701 shares for options granted to officers and employees exercisable on various dates to July 21, 1977 at prices ranging from $1.40 to 3.285 per share,

1,176,471 shares for the conversion of the $5,000,000 convertible subordinated note (note 5).

7. COMMITMENTS AND CONTINGENCIES

(a) The company has issued non-interest bearing demand promissory notes and letters of guarantee as security for the performance of work obligations by the company and others in respect of normal exploration activities. The aggregate of such notes and guarantees amounted to $177,645 at September 30, 1973.

(b) A subsidiary is obligated to pay $67,000 in connection with certain lease applications in Alaska, if and when, the relevant leases are issued.

(c) On July 1, 1972 the company entered into a financial consulting agreement with a New York partnership, the partners of which are also directors of the company. The agreement terminates on June 30, 1974 and provides for the payment of $150,000 U.S. per annum by the company.

8. REMUNERATION OF DIRECTORS AND SENIOR OFFICERS

The aggregate direct remuneration of the directors and senior officers of the company during the year amounted to $151,825 (1972 - $96,700).

9. EARNINGS PER SHARE

The earnings per share are based on the weighted average number of shares outstanding during the year which was 6,929,807 shares in the current year (1972 - 4,770,000 shares).

corporate

directors
John A. Downing, *Calgary, Alberta*
James A. Millard, *Calgary, Alberta*
Albert E. Whitehead, *Calgary, Alberta*
Neil A. McConnell, *New York City*
Montague H. Hackett, Jr., *New York City*

officers
Albert E. Whitehead, *President*
Montague H. Hackett, Jr., *Executive Vice President*
Harvey S. Robinson, *Vice President*
Darrell R. Long, *Vice President, Exploration*
Thomas M.M. Bender, *Treasurer*
James A. Millard, *Secretary*

head office
950 Three Calgary Place
355 - 4th Avenue S.W.
Calgary, Alberta T2P 0J1
Phone: (403) 262-1135

u.s. office
One Battery Park Plaza
New York, New York 10004
Phone: (212) 344-4495

subsidiary companies
Bridger Petroleum Corporation
Houston Oils of Norway, Limited
Houston Oils of Spain, Limited
Houston Oils (U.K.) Limited
Transalta Minerals Ltd.
Bluenose Oils Limited

affiliated companies
Magnorth Petroleum Limited *(10.5% equity)*
Ensign Oils of Spain Limited *(50% equity)*

auditors
Collins, Love, Eddis, Valiquette & Barrow
Calgary, Alberta

banker
The Toronto-Dominion Bank
Calgary, Alberta

legal counsel
MacKimmie Matthews
Calgary, Alberta

transfer agent and registrar
The Canada Trust Company
Vancouver, Calgary, Toronto, Montreal

stock exchange listings
Toronto Stock Exchange, *Toronto*
Canadian Stock Exchange, *Montreal*

Ticker Tape Symbol: HCO

HOUSTON
OILS
LIMITED

950 Three Calgary Place
355 - 4th Avenue S.W.
Calgary, Alberta T2P 0J1

SMITH GRANT MANN ALBERTA
Litho'd in Canada