Prairie Oil Royalties

COMPANY, LTD.

ANNUAL REPORT

1981

Prairie Oil Royalties

COMPANY, LTD.

The Company was incorporated July 13, 1951 under the laws of the Province of Saskatchewan, Canada. There are 1,961,520 Common Shares outstanding, of which 74.4% are owned by Norcen Energy Resources Limited of Toronto, Canada. The Company produces and sells crude oil, gas liquids and natural gas in Western Canada and is engaged in oil and gas exploration and development in Western Canada, the Arctic Islands, and the United States. Interests are also held in exploratory lands in the Northwest Territories and the Province of Ontario. Operations in the United States are carried out through a wholly-owned subsidiary, P.O.R. Oil & Gas Inc. The Company is not involved in refining or retail marketing.

CORPORATE PROFILE

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ANNUAL MEETING

The Annual Meeting of Shareholders of the Company will be held on Friday, April 30, 1982, at 10:30 o'clock in the forenoon, local time, in the Board Room of Norcen Energy Resources Limited, 32nd Floor, 715 Fifth Avenue Southwest, Calgary, Alberta, Canada.

Report to Shareholders

Financial

Revenue from all sources in 1981, after deducting the new Petroleum and Gas Revenue Tax, was \$7,536,000, a slight increase over revenue for the previous year. The Petroleum and Gas Revenue Tax, which came into effect on January 1, 1981, amounted to \$815,000 for the year under review and largely offset revenue increases attributable to higher average prices received for oil and gas in 1981. Net income for the year, at \$3,062,000 or \$1.56 a share, was down \$88,000 from net income of \$3,150,000 or \$1.61 a share recorded in 1980. Cash flow from operations was \$6,570,000 or \$3.35 a share compared with \$6,496,000 or \$3.31 a share in 1980.

A more detailed financial analysis of the Company's 1981 operations appears on page 5 of this Report.

Production

Average daily production for 1981 before deducting royalties was 718 barrels of oil and natural gas liquids and 8,465 Mcf of gas compared to 787 barrels and 9,169 Mcf in 1980. The decrease in oil and gas liquids is largely the result of production cutbacks in Saskatchewan due to unfavorable economic conditions following the introduction of the National Energy Program. Production cutbacks imposed by the Alberta government as a result of the National Energy Program and natural declines in older fields in Alberta were more than offset by increases in production from the West Pembina and Taber fields. The production cutbacks were discontinued following the signing of the agreements referred to later in this report and production is gradually returning to the levels that previously existed. The continuing low level of exports to the United States accounted for most of the decrease in production of natural gas.

The average prices received by the Company from the sale of its production were \$18.23 a barrel for oil and natural gas liquids and \$2.30 an Mcf for natural gas. The average prices received in 1980 were \$14.60 a barrel and \$2.13 an Mcf respectively.

Reserves

Estimated reserves at December 31, 1981 before royalties were 3.01 million barrels of crude oil and natural gas liquids and 64.4 billion cubic feet of natural gas. Comparable figures at December 31, 1980 were 2.96 million barrels of crude oil and 66.7 billion cubic feet of natural gas. These estimates have been calculated by engineers of the parent company, Norcen Energy Resources Limited, and do not include the Company's share of natural gas reserves in the Arctic Islands. Further information on the Company's reserves appears in note 8 to the Financial Statements.

Oil and Gas Prices

During 1981 the governments of Alberta, British Columbia and Saskatchewan entered into 5 year agreements with the Canadian government with respect to oil and gas pricing, taxation and revenue sharing. The new pricing structure under these agreements provides for:

- *an increase on October 1, 1981 of \$2.50 a barrel in the price of old oil and semi-annual increases commencing January 1, 1982 to bring the price to 75% of the world price by 1986;*
- *a substantial increase on January 1, 1982 in the price of new oil to establish a New Oil Reference Price which is close to the world price, and periodic adjustments to keep pace with the world price; and*
- *semi-annual increases beginning in 1982 of 25¢ an Mcf in the Alberta border price of natural gas destined for domestic markets.*

New oil includes all conventional crude oil produced from new oil pools or extensions of existing oil pools discovered after December 31, 1980 and from qualifying enhanced recovery schemes (other than waterflood) commencing after the same date. It is estimated that approximately 10% of the Company's 1982 production will qualify for the New Oil Reference Price.

Outlook

Cash flow problems resulting from substantial tax increases under the recently concluded federal-provincial energy pricing agreements and from high interest rates are having an adverse effect on exploratory activity in Western Canada and this situation is expected to continue during 1982. In an effort to assist small exploration companies the government of Alberta has doubled the benefits to oil and gas producers under the Alberta Royalties Tax Credit Program. This tax credit is now 50% of Crown royalties payable, up to a maximum credit of \$2,000,000. Because of its size, the Company will receive the maximum benefit from the enhanced program and the resulting improvement in cash flow will enable the Company to maintain a high level of exploratory activity during 1982.

Although much of the benefit from the higher oil and gas prices under the new energy agreements in 1982 and beyond will be absorbed by increased taxation, the agreements will provide a measure of stability in the industry over the next five years and the Company is expected to do relatively well under the new energy policies.

On behalf of the Board

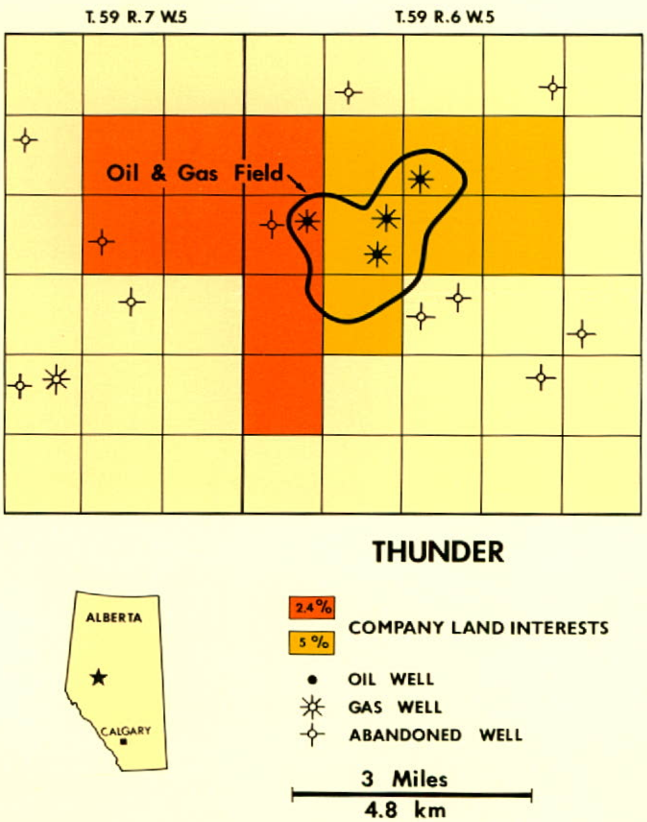
Calgary, Alberta
February 25, 1982

D. D. Barkwell
President

Exploration and Development

Taber - Chin Coulee - Manyberries

The Company participated in a twenty-three well drilling program in this area of southeast Alberta during 1981. As a result the Company now has an interest in three oil wells in North Taber and two gas wells in Manyberries. The Company's share of crude oil production from the North Taber wells was 38 barrels a day in 1981, three times the 1980 share. Another aggressive drilling program is planned for this area during 1982.



Thunder (Greencourt)

In the Thunder area of central Alberta, the Company participated in the completion of a multi-zone oil and gas well making a total of four such wells completed in the area to date. The Company's interest is 5% in three wells and 2.4% in one well. A further well is planned for 1982.

Hoadley

Further drilling in this area of central Alberta resulted in the completion of another gas well in 1981. The company has a 7⅞% interest in this latest completion and a 7⅛% interest in four gas wells completed prior to 1981.

Minnehik

Interests in acreage acquired over a year ago in the Minnehik area of central Alberta were pooled and in 1981 the Company participated to the extent of a 24½% interest in the drilling of an oil well on the pooled lands. The well has not been production tested but a potential in the range of 100 barrels a day is indicated. This is the third successful well in this area.

Pembina - Cynthia

The Company participated in the completion of a Glauconitic sandstone gas well in this area in 1981. The well is located on the northern edge of the Pembina Cardium oil field and the Company's interest is 5%. Three deep Mississippian wells are planned for 1982 to test seismic anomalies in the area.

During 1981 the Company added 29,600 gross acres to its landholdings in this general area through acquisitions in the Peco, Blackstone and West Cynthia areas. The Company also has taken a 10% interest in a deep test to be drilled on a Nisku reef seismic anomaly at West Pembina. This well is presently drilling.

Dyberg

A dual zone gas well in which the Company has a 15⅛% interest was completed in this area of central eastern Alberta during 1981.

Brewster Creek

An 11,000 foot Mississippian test well drilled as part of a joint venture program in the Brewster Creek area of western Alberta has multi-zone gas potential and is being production tested to determine reservoir potential. The Company has a 13¼% interest in this well. A further test well in this area is included in the Company's 1982 drilling program.

Arneson

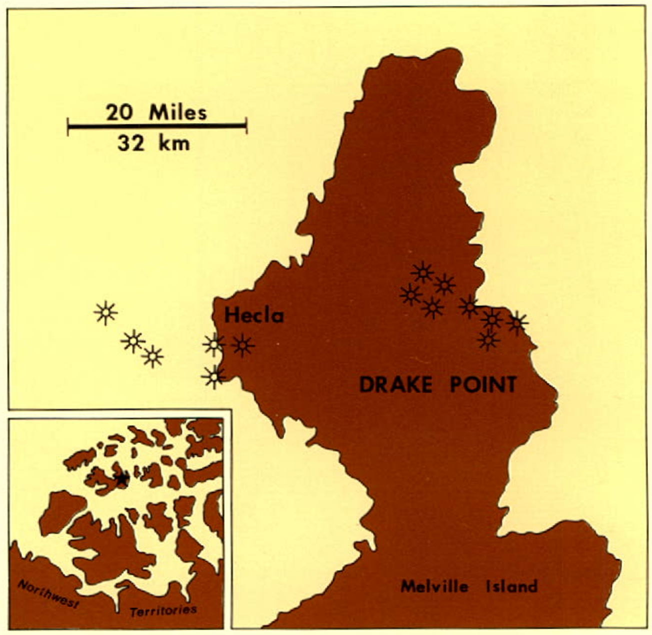
The first well to be drilled under a farmout of the Company's landholdings in the Arneson area of central eastern Alberta has resulted in a gas well completion. The Company holds an overriding royalty in production from the well until the farmees recover their costs, at which time the Company's interest will revert to a 15⅛% working interest.

West Pembina

Enhanced recovery schemes are in operation in the four Nisku pools in this field. The Company's interests are 1.75% in the one unitized pool and 5% in each of the other three pools. During 1981 the Company's share of production from the field was in excess of 300 barrels a day and this is expected to double in 1982. Slightly more than one-third of this production should qualify for the New Oil Reference Price.

United States

During 1981 the Company participated in an Ordovician formation oil discovery on a block of 9,080 acres in western North Dakota. The well will be on production early in 1982 with an estimated initial potential of 290 barrels a day. A follow-up well is presently drilling. The Company's interest in these wells is 5%.



DRAKE POINT
ARCTIC ISLANDS

Arctic Islands

A joint venture known as the Arctic Pilot Project has been formed by a group of Canadian companies to deliver liquefied natural gas from the on-shore wells in the Drake Point field on Melville Island in the Canadian Arctic, to eastern Canada. The project is designed to test the feasibility of producing natural gas from wells in the Arctic Islands, transporting the gas by a 100 mile buried pipeline, transforming the gas into liquefied natural gas and shipping it by ice-breaking carrier to a regasification plant in southern Canada — all on a year-round basis. The pilot project will be one-tenth the size of a full scale plant.

The Company has a 3.15% interest in the Drake Point gas reserves and has entered into a 20 year contract for the sale of its share of these reserves to the Arctic Pilot Project. Delivery of this gas could begin as early as 1986 if regulatory approvals of the project are received in 1982. Public hearings in this regard are now underway.

Drilling Summary

During 1981 the Company participated in the drilling of 48 (5.49 net) wells resulting in 5 (1.12 net) oil wells and 11 (.95) gas wells. The following table sets forth the gross and net exploratory and development wells in which the Company participated during the five year period ended December 31, 1981.

	Exploratory Wells				Development Wells			
		Net Wells				Net Wells		
Year	Gross Wells	Oil	Gas	Dry Holes	Gross Wells	Oil	Gas	Dry Holes
1977	20	.42	1.17	3.21	31	.50	7.58	.56
1978	31	.48	1.53	4.91	6	—	.54	—
1979	31	.47	2.34	2.19	19	.05	4.03	—
1980	40	.29	2.19	2.83	14	—	2.17	—
1981	44	.62	.82	3.05	4	.50	.13	.37
	166	2.28	8.05	16.19	74	1.05	14.45	.93

As at December 31, 1981 the Company had working interests in 836 gross (59 net) producing oil and gas wells in Western Canada and royalty interests in 382 gross (10 net) producing oil and gas wells most of which are in the province of Saskatchewan.

Oil and Gas Landholdings

At December 31, 1981 the Company owned interests in 3,550,208 gross (337,689 net) acres compared to 3,525,014 gross (334,014 net) at the end of 1980. These landholdings include 290,642 gross (56,263 net) producing acres and are shown in detail in the following summary:

	Leases		Reservations & Permits		Total	
	Gross Acres	Net Acres	Gross Acres	Net Acres	Gross Acres	Net Acres
British Columbia	124,759	6,832	—	—	124,759	6,832
Alberta	915,408	174,475	169,120	13,884	1,084,528	188,359
Saskatchewan	90,423	34,186	—	—	90,423	34,186
Manitoba	78,649	23,270	3,200	800	81,849	24,070
Ontario	3,543	876	—	—	3,543	876
Arctic Islands	103,381	3,256	2,013,305	77,529	2,116,686	80,785
Northwest Territories	39,340	1,673	—	—	39,340	1,673
United States	9,080	908	—	—	9,080	908
	1,364,583	245,476	2,185,625	92,213	3,550,208	337,689

In addition to the above, royalty interests are held in 217,101 acres.

Management's Discussion and Financial Review

Revenue and Expenses

Net income decreased in 1981 to $1.56 per share from $1.61 per share in 1980 and $1.15 per share in 1979. Return on average common share equity was 13.0% in 1981 compared with 14.8% in 1980 and 12.1% in 1979. Funds from operations increased 1% over 1980. Comparatively 1980 was 25% over 1979.

1981 Compared to 1980

Sales and other revenues increased by less than 1% over the 1980 level. In 1981, there were price increases on crude oil and natural gas liquids of $1.00 per barrel on January 1 and July 1, and $2.50 per barrel October 1 compared to price increases in 1980 of $1.00 per barrel on January 1 and $2.00 per barrel on August 1. The increased revenue from oil and oil and gas liquids was offset by lower production levels and the Petroleum and Gas Revenue Tax which became effective January 1, 1981. Natural gas production revenues were unchanged from 1980 despite an 8% decline in volumetric sales, due to the annual impact of the 30¢ per Mcf increase on September 1, 1980.

Expenses, exclusive of income taxes, decreased $120,000 or 3%. Production expenses continued to rise due to inflationary pressures and higher costs to maintain producibility in existing fields. Depletion expense is lower due to a change to the production revenue method from the unit of production method described in note 2 of the financial statements. The increase in depreciation results from capital expenditures incurred in 1980. General and administrative expenses are up due to higher management fees paid to Norcen Energy Resources Limited under the terms of the management contract. Interest expense decreased by 7% due to lower short-term borrowings.

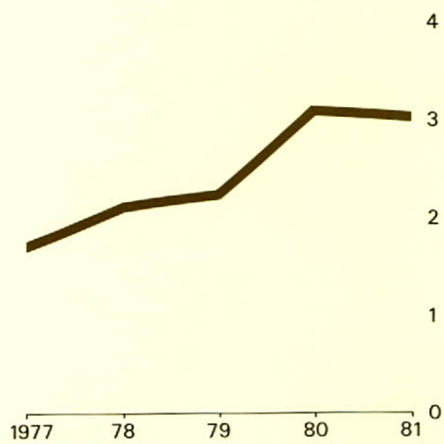
Income taxes increased as explained in note 6 to the Financial Statements.

1980 Compared to 1979

Sales and other revenues increased 22% above the 1979 level. The increase in oil and gas revenues primarily reflects price increases of $1 per barrel of crude oil on January 1 and $2 per barrel on August 1, 1980 and related increases of 15¢ per Mcf on natural gas on February 1 and 30¢ per Mcf on September 1, 1980.

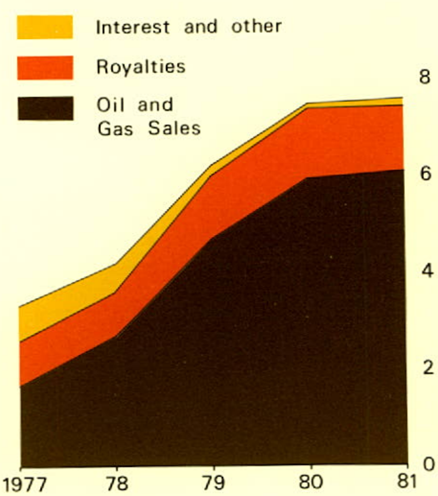
Net Income

Millions of Dollars



Revenues

Millions of Dollars

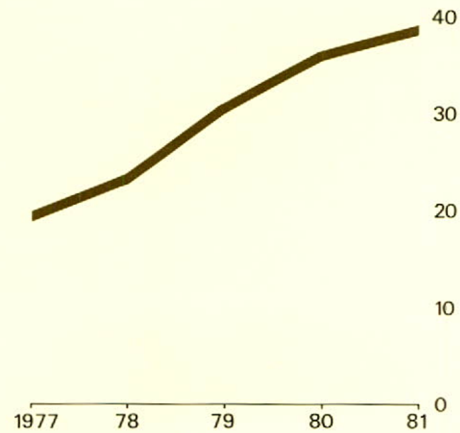


Expenses, exclusive of income taxes, increased \$513,000 or 16%. Production expenses continued to rise due to inflationary pressures and higher costs to maintain producibility in existing fields. The increase in depreciation and depletion results from increased capital expenditures in the last few years and the full year effect of the Shenandoah acquisition of 1979. The depletion rate per equivalent barrel increased to \$1.95 from \$1.69. General and administrative expenses are up due to higher management fees paid to Norcen Energy Resources Limited under the terms of the management contract. Interest expense decreased by 15% as a result of lower short-term borrowings which was partially offset by higher average interest rates.

Income taxes decreased as explained in detail in note 6 to the Financial Statements.

Total Assets

Millions of Dollars



Balance Sheet

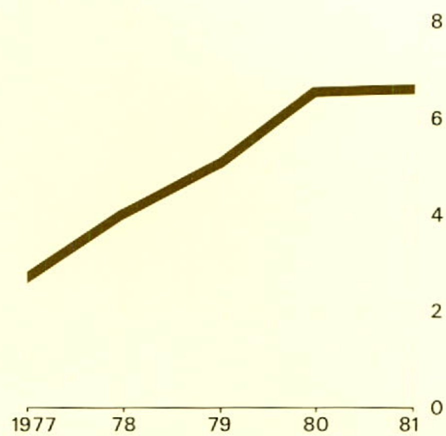
The total assets of the Company have continued to grow to \$38.8 million from \$35.6 million in 1980 and \$30.4 million in 1979. This growth is attributable to the significant capital expenditures program amounting to \$4.3 million, \$7.5 million and \$13.4 million in the last three years.

Short-term Debt

Short-term debt outstanding has declined during the past year from \$3.0 million in 1980 to \$1.7 million in 1981 arising mostly from internally generated funds, but partially contributed to by an increase of \$0.4 million from deferred gas revenues. In 1981, the Company under the terms of a joint venture exploration agreement also sold some oil and gas properties for \$2.5 million, although this amount will be recovered in equal instalments over the next three years.

Funds from Operations

Millions of Dollars



Financial Position

The funds position of the Company increased \$3.9 million in 1981 and \$0.3 million in 1980 compared to an \$8.1 million decrease in 1979. While annual generation of funds from operations has increased consistently over the period, the increase has been more than offset by greatly increased annual capital expenditures.

Financial Statements

years ended December 31, 1981, 1980 and 1979

Accounting Policies

The Annual Report and the accompanying financial statements have been prepared by Management and approved by the Board of Directors. The financial statements have been prepared in accordance with generally accepted accounting principles applied, except for the change in the method of depletion described in note 2, on a consistent basis and comply with United States' disclosure requirements. The principles used were those judged by Management to be the most appropriate in the circumstances. Management acknowledges responsibility for the fairness, integrity and objectivity of all financial information contained in the Annual Report including the financial statements.

Principles of consolidation

The consolidated financial statements include the accounts of Prairie Oil Royalties Company, Ltd. and its wholly-owned subsidiary, P.O.R. Oil & Gas Inc.

Foreign currency translation

Amounts in foreign currency have been translated to Canadian dollars on the following bases: current assets and current liabilities, at the rate of exchange as at the balance sheet date; properties, plant and equipment and related depreciation and depletion, at the rate of exchange at the date of acquisition; revenue and expenses, at the average rate of exchange for the respective year.

Properties, plant and equipment

Oil and gas properties, in accordance with the full cost method of accounting, include all expenditures related to the exploration and development of oil and gas reserves, whether or not potentially productive. As set out in note 2, commencing January 1, 1981 these costs are depleted on the production revenue method based on total estimated future production revenues from proven recoverable reserves. Prior thereto these costs were depleted on the composite unit of production method based on total estimated proven recoverable reserves.

Oil and gas production equipment and related facilities are depreciated over their estimated useful service life on the straight-line method at various rates, the application of which is equivalent to a composite rate of approximately 7.9% (8.3% in 1980, 7.8% in 1979).

Upon retirement or sale of major items of producing property or equipment, the asset accounts are relieved of the cost of such property together with the applicable accumulated depletion or depreciation. The difference between net book value of such items and the proceeds, if any, is charged or credited to income. Proceeds on sale of non-producing properties are credited to asset costs.

Maintenance and repairs are charged to income when incurred and betterments which extend the serviceable life of properties are capitalized.

National Energy Program

As part of the National Energy Program, the Federal Government instituted the Petroleum Incentive Program which provided for certain companies to qualify for incentive grants on exploration and development expenditures. The amounts of the grants vary with the degree of Canadian ownership. As legislation providing for determination of the degree of Canadian ownership has not been issued, it is uncertain the extent to which the Company will qualify for these incentives. Consequently, no provision has been made for recovery of such grants in the current year.

Income taxes

The Company follows the tax allocation method of accounting whereby provisions for income taxes are based on the income reported in the accounts. This method results in the provision of deferred income taxes to the extent that taxes currently payable have been reduced by claiming depletion and depreciation for income tax purposes in amounts differing from those reported in the accounts.

Deferred gas revenues

Amounts received for annual contracted gas volumes not taken by pipeline purchasers are deferred and will be recognized as revenue when deliveries are made or upon expiry of the period allowed for such deliveries.

CONSOLIDATED BALANCE SHEET

as at December 31, 1981 and 1980

(thousands of dollars)

Assets

	1981	1980
CURRENT ASSETS		
Accounts receivable	$ 2,237	$ 1,946
Income taxes recoverable	916	26
Drilling and other deposits	57	43
Portion of note receivable due within one year	622	—
	3,832	2,015
NOTE RECEIVABLE (note 3)	1,245	—
PROPERTIES, PLANT AND EQUIPMENT (note 4)	33,769	33,620
	$38,846	$35,635

Liabilities

	1981	1980
CURRENT LIABILITIES		
Bank indebtedness	$ 1,528	$ 2,612
Accounts payable and accrued liabilities	1,223	2,094
Due to parent company	233	405
	2,984	5,111
DEFERRED GAS REVENUES	1,962	1,541
DEFERRED INCOME TAXES	8,826	6,971

Shareholders' Equity

	1981	1980
CAPITAL STOCK		
Issued 1,961,520 Common Shares	1,962	1,962
CONTRIBUTED SURPLUS	574	574
RETAINED EARNINGS	22,538	19,476
	25,074	22,012
	$38,846	$35,635

Approved by the Board

Director

Director

CONSOLIDATED STATEMENT OF INCOME

years ended December 31, 1981, 1980 and 1979

(thousands of dollars except per share amounts)

	1981	1980	1979
SALES AND OTHER REVENUES			
Oil and gas sales (net of Petroleum and Gas Revenue Tax of $693; 1980 - nil; 1979 - nil)	$ 6,116	$ 5,983	$ 4,695
Royalties (net of Petroleum and Gas Revenue Tax of $122; 1980 - nil; 1979 - nil)	1,384	1,501	1,327
Interest	36	17	144
	7,536	7,501	6,166
COSTS AND EXPENSES			
Production	889	785	592
Depletion (note 2)	1,193	1,648	1,453
Depreciation	460	343	262
General and administrative			
Charges from parent company	599	510	389
Other	96	46	62
Interest	309	334	395
	3,546	3,666	3,153
Income before income taxes	3,990	3,835	3,013
Income taxes			
Current (recovery)	(927)	(671)	(454)
Deferred	1,855	1,356	1,220
	928	685	766
NET INCOME	$ 3,062	$ 3,150	$ 2,247
EARNINGS PER SHARE	$1.56	$1.61	$1.15

CONSOLIDATED STATEMENT OF RETAINED EARNINGS

years ended December 31, 1981, 1980 and 1979

(thousands of dollars)

	1981	1980	1979
BALANCE AT BEGINNING OF YEAR			
As previously reported	$20,354	$17,204	$14,957
Adjustment of prior years' income taxes (note 5)	(878)	(878)	(878)
As restated	19,476	16,326	14,079
Net income	3,062	3,150	2,247
BALANCE AT END OF YEAR	$22,538	$19,476	$16,326

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

years ended December 31, 1981, 1980 and 1979

(thousands of dollars)

	1981	1980	1979
SOURCE OF FUNDS			
Operations	$ 6,570	$ 6,496	$ 5,183
Sale of oil and gas properties	2,489	—	—
Deferred gas revenues	421	1,296	48
	9,480	7,792	5,231
APPLICATION OF FUNDS			
Expenditures on properties, plant and equipment	4,291	7,536	13,374
Note receivable	1,245	—	—
	5,536	7,536	13,374
INCREASE (DECREASE) IN FUNDS	$ 3,944	$ 256	$(8,143)
CHANGES IN COMPONENTS OF FUNDS ARE REPRESENTED BY:			
Accounts receivable	$ 291	$ 194	$ 790
Income taxes	890	182	(245)
Drilling and other deposits	14	(15)	(12)
Portion of note receivable due within one year	622	—	—
Bank indebtedness	1,084	1,272	(8,669)
Accounts payable and accrued liabilities	871	(1,162)	68
Due to parent company	172	(215)	(75)
INCREASE (DECREASE) IN FUNDS	$ 3,944	$ 256	$(8,143)

Auditors' Report

TO THE SHAREHOLDERS OF
PRAIRIE OIL ROYALTIES COMPANY, LTD.

We have examined the consolidated balance sheet of Prairie Oil Royalties Company, Ltd. as at December 31, 1981 and 1980 and the consolidated statements of income, retained earnings and changes in financial position for each of the three years ended December 31, 1981. Our examinations were 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, 1981 and 1980 and the results of its operations and the changes in its financial position for each of the three years ended December 31, 1981 in accordance with generally accepted accounting principles applied, except for the change in the method of depletion as described in note 2, on a consistent basis.

Thorne Riddell

Calgary, Canada
February 2, 1982

THORNE RIDDELL
Chartered Accountants

Notes to Consolidated Financial Statements

years ended December 31, 1981, 1980 and 1979

(thousands of dollars except per share and per barrel amounts or unless otherwise stated)

1. ACCOUNTING POLICIES

The summary of accounting policies is an integral part of these financial statements.

2. CHANGE IN ACCOUNTING POLICY

The National Energy Program coupled with energy pricing and taxation agreements with the provinces signed in late 1981 has established a five year contractual pricing structure for oil and gas production in Canada. The existence of this pricing structure means that depletion of costs can be related to the value of production in relation to the total value of the reserves. The Company has concluded that, effective January 1, 1981, it is more appropriate to relate charges for depletion to production revenues than to production quantities. Estimated future production revenues are based on proven reserves as determined by Company engineers and on prices set by energy and pricing agreements limited to 75% of the 1981 world price for crude oil. As a result of this change in accounting, the provision for depletion in 1981 is $464 ($0.15 per common share after income taxes) less than it would have been had it been based on production quantities.

3. NOTE RECEIVABLE

Due in three equal instalments on April 1 each year through 1984	$1,867
Portion due within one year	622
	$1,245

4. EXPLORATION AND PRODUCTION ACTIVITIES

The Company has capitalized costs in oil and gas activities as follows:

	Year Ended December 31,	
	1981	1980
Properties	$37,135	$35,797
Production equipment	6,320	5,856
	43,455	41,653
Accumulated depreciation, depletion and amortization	9,686	8,033
Capitalized costs	$33,769	$33,620

The following table presents information on the Company's oil and gas producing activities:

	1981	1980	1979
Costs capitalized in the year			
Property acquisition	$(1,857)	$1,350	$ 9,189
Exploration	2,433	3,361	3,002
Development	1,226	2,825	1,183
Total capitalized	$ 1,802	$7,536	$13,374

Included in the above are exploration overhead costs of $246 during 1981, $292 during 1980 and $299 during 1979 charged by the parent company.

	1981	1980	1979
Depreciation and depletion expense	$1,653	$1,991	$ 1,715
Depreciation and depletion expense per equivalent barrel	$ 2.14	$ 2.36	$ 2.00
Net revenues from producing oil and gas			
Revenue	$7,500	$7,484	$ 6,022
Production expenses	889	785	592
Net revenue	$6,611	$6,699	$ 5,430

5. PRIOR PERIOD ADJUSTMENT

The opening balance for retained earnings in 1979 has been restated to reflect an income tax reassessment of $622 plus interest of $256 relating to reported capital gains in 1976. Although the Company has made provision for this liability, it is presently appealing the reassessment.

6. INCOME TAXES

Deferred income taxes result from timing differences in the recognition of income and expenses for income tax and financial statement purposes. The source of these differences and the tax effect of each are as follows:

	1981	1980	1979
Exploration and development expenditures and capital cost allowances deducted for income tax purposes in excess of depletion and depreciation	$1,908	$1,706	$1,379
Other items	(53)	(350)	(159)
	$1,855	1,356	$1,220

The provision for income taxes in the consolidated statement of income varies from the amounts that would be computed by applying the Canadian federal statutory rate of 46% to income before income taxes for the following reasons:

	1981		1980		1979	
		% of Pretax Income		% of Pretax Income		% of Pretax Income
Computed income tax expense	$1,835	46.0	$1,764	46.0	$1,386	46.0
Increase (decrease) in income taxes resulting from:						
Income tax depletion	(708)	(17.7)	(744)	(19.4)	(460)	(15.3)
Non-deductible royalties, Petroleum and Gas Revenue Tax, mineral taxes and other expense, less federal resource allowance and provincial rebates	(270)	(6.8)	(220)	(5.7)	(213)	(7.1)
Other, net	71	1.8	(115)	(3.0)	53	1.8
Actual income tax expense	$ 928	23.3	$ 685	17.9	$ 766	25.4

7. QUARTERLY AND OTHER FINANCIAL DATA (UNAUDITED)

	Quarter				
	First	Second	Third	Fourth	Year
1981					
Revenue	$2,434	$1,349	$1,698	$2,055	$7,536
Income before income taxes					
as previously reported	1,297	455	641		
as restated (i)	1,408	677	734	1,171	3,990
Net income					
as previously reported	920	324	647		
as restated (i)	999	482	727	854	3,062
Earnings per share					
as previously reported	0.47	0.17	0.33		
as restated (i)	0.50	0.25	0.37	0.44	1.56
Market price per common share (ii)					
High	16⅝	18¼	21⅜	16¼	21⅜
Low	14	14⅜	11	12⅜	11

	Quarter				
	First	Second	Third	Fourth	Year
1980					
Revenue	$2,234	$1,867	$1,510	$1,890	$7,501
Income before income taxes	1,215	1,111	783	726	3,835
Net income	867	818	742	723	3,150
Earnings per share	0.44	0.42	0.38	0.37	1.61
Market price per common share (ii)					
High	30¾	25⅜	28⅝	27	30¾
Low	15¾	17½	22	14	14¾

(i) The quarterly results have been restated to give effect to the change in the method of depletion (note 2).

(ii) The market prices are as reported by the American Stock Exchange, the primary market, in U.S. dollars.

8. SUMMARY OF OIL AND GAS PRODUCING ACTIVITIES (UNAUDITED)

Reserves as determined by Company engineers are stated on a before royalty basis and include proven remaining reserves together with probable additional reserves reduced by a risk factor, all in accordance with Canadian practice.

The following information is provided in response to United States reporting requirements for which purpose information is to be provided on a proven reserve basis only after deducting royalty interest of others. Since all of the Company's proven reserves are developed, such information is provided only for proven developed reserves.

The following table summarizes the changes in quantities of net proven oil and gas reserves as determined by independent reservoir engineers. Such quantities vary from reserves determined by Company engineers due to judgemental and timing differences in making reserve estimates.

	Year Ended December 31,					
	1981		1980		1979	
	Oil and Gas Liquids	Gas	Oil and Gas Liquids	Gas	Oil and Gas Liquids	Gas
	(000's bbls)	(Mmcf)	(000's bbls)	(Mmcf)	(000's bbls)	(Mmcf)
Beginning of year	1,833	39,000	1,759	36,848	1,284	34,243
Revisions of previous estimates	406	(492)	273	313	339	1,826
Extensions, discoveries and other additions	—	316	—	3,984	328	3,012
Production	(203)	(2,008)	(199)	(2,145)	(192)	(2,233)
End of year	2,036	36,816	1,833	39,000	1,759	36,848

9. RESERVE RECOGNITION ACCOUNTING (UNAUDITED)

The following information summarizes the oil and gas producing activities for the years indicated on the basis of the reserve recognition method of accounting as prescribed by the United States Securities and Exchange Commission ("SEC"). The SEC requires that reserve recognition accounting ("RRA") be presented as a supplement to the cost methods historically followed by oil and gas producing companies. The Company believes that RRA statements generally do not accurately reflect the economic value of oil and gas reserves or the income to be derived therefrom.

RRA attempts to (i) assign a value to proven reserves which is more indicative of the value of the reserves than cost, (ii) reflect additions to proven reserves and changes in valuation of proven reserves in the income statement and (iii) expense all costs of finding and developing additions to proven reserves, including all costs determined to be not productive, during the current period. In order to develop the values for inclusion in the balance sheet and the additions to proven reserves on the income statement, several assumptions are made. The present value information is calculated by applying a per annum discount rate of 10% as stipulated by the SEC to the estimated net proven reserves shown above. Income taxes have been calculated on the taxes payable basis by applying rates and other statutory provisions currently in effect.

The basis for the amounts presented includes projected production schedules, forecasted development and production costs and estimates of reserve quantities. Because of the uncertainty inherent in any projections of the future, actual production volumes and development costs may vary from those utilized to calculate the present value of estimated future net revenues. Further, to the extent that the actual cost of capital is different from the prescribed discount rate of 10%, the value of the reserves, as shown below, will be different.

In calculating the estimated future net revenues before income taxes at the end of 1981, prices and costs in effect at January 1, 1982 were assumed to continue for all future periods and provision was made for estimated future development expenditures that will be required to produce the reserves.

The estimated future net revenues before income taxes as at December 31, 1981 expected to be earned in each of the three years subsequent to 1981 and in total for all future years are as follows:

1982	1983	1984	Thereafter	Total
		(millions)		
$6.3	$6.8	$6.4	$80.4	$99.9

The present value of estimated future net revenues discounted at 10% based on estimated reserves at the end of each year, calculated on the basis outlined above, is as follows:

1981	1980 (ii)	1979
	(millions)	
$48.6	$39.1	$37.5

The following table summarizes the oil and gas producing activities for the years indicated on the basis of RRA and was prepared under the assumptions stated above for proven developed reserves. RRA is based on the recognition of revenue at the time that proven reserves are determined. The summary of oil and gas producing activities on the basis of RRA sets out the present value (discounted at 10% per annum) of the future net revenues expected to be derived at current price and cost levels from the current year's exploration activities and evaluation of proven reserves.

	Year Ended December 31,		
	1981	1980 (ii)	1979
		(millions)	
Additions and revisions to estimated proven reserves, net of royalties			
Additions to estimated proven reserves	$ .2	$ 2.0	$ 4.9
Revisions to estimates of proven reserves in prior years			
Changes in prices	13.6	7.4	6.1
Other	3.8	.5	2.1
Revenue taxes	(6.3)	(5.4)	—
Accretion of discount	3.9	3.7	2.7
	15.2	8.2	15.8
Acquisition, exploration, development and production costs (i)	2.9	5.7	4.5
Additions and revisions to proven reserves over evaluated costs (ii)	12.3	2.5	11.3
Provision for income taxes (ii)	7.3	2.5	4.8
Results of oil and gas producing activities on the basis of RRA (ii)	$ 5.0	$ NIL	$ 6.5

The primary financial statements shown elsewhere herein recognize revenue upon the production and sale of the Company's reserves. For 1981 the profit contribution from the production and sale of oil and gas, before administrative expenses, interest and taxes, reflected in the primary financial statements is $5.0 million (1980 - $4.7 million, 1979 - $3.7 million).

The following table which was prepared using the assumptions stated above summarizes the changes in the present value of estimated future net revenues from proven reserves.

	Year Ended December 31,		
	1981	1980(ii)	1979
		(millions)	
Increase			
Net additions and revisions	$15.2	$ 8.2	$15.8
Previously projected development costs	.9	$ 0.1	—
	16.1	8.3	15.8
Decrease			
Sales of oil and gas and value of transfers (net of production costs of $0.9, $0.8 and $0.6 respectively)	6.6	6.7	5.4
Net increase	9.5	1.6	10.4
Beginning of year	39.1	37.5	27.1
End of year	$48.6	$39.1	$37.5

The present value of the estimated future net revenues from proven reserves as of the end of the year should not be viewed as the amount which might be realized in a sale of the reserves in place, nor as the amount which will be ultimately realized from production from the properties.

(i) Property acquisition and exploration costs aggregating $2.5 million to December 31, 1981 have not been included in the summary pending the determination of proven reserves.

(ii) 1980 has been restated to give effect to the National Energy Program and to include Petroleum and Gas Revenue Tax on a comparable basis in 1980 with 1981.

SELECTED FINANCIAL DATA

FOR THE YEARS ENDED December 31

	1981	1980	1979	1978	1977
Revenue ($000)					
Oil Sales	$ 2,066	$ 1,520	$ 1,079	$ 529	$ 378
Gas Sales	4,050	4,463	3,616	2,191	1,370
Royalties	1,384	1,501	1,322	930	983
Interest and Other	36	17	149	675	710
	7,536	7,501	6,166	4,325	3,441
Expenses ($000)					
Production	$ 889	$ 785	$ 592	$ 421	$ 321
Depletion	1,193	1,648	1,453	556	364
Depreciation	460	343	262	171	188
General and Administrative	695	556	451	203	75
Interest	309	334	395	13	—
	3,546	3,666	3,153	1,364	948
Income Before Income Taxes ($000)	$ 3,990	$ 3,835	$ 3,013	$ 2,961	$ 2,493
Income Taxes ($000)					
Current (recovery)	$ (927)	$ (671)	$ (454)	$ (424)	$ 232
Deferred	1,855	1,356	1,220	1,226	509
	928	685	766	802	741
Net Income ($000)	3,062	3,150	2,247	2,159	1,752
Net Income Per Share	$ 1.56	$ 1.61	$ 1.15	$ 1.10	$ 0.89
Cash Flow ($000)	$ 6,570	$ 6,496	$ 5,183	$ 4,112	$ 2,700
Expenditures ($000)					
Exploration and Property Acquisitions	$ 1,338	$ 5,815	$12,607	$ 6,047	$ 2,099
Plant and Equipment (net after sales)	$ 464	$ 1,721	$ 767	$ 1,016	$ 1,061
Shares issued and outstanding (i)	1,961,520	1,961,520	1,961,520	1,961,520	1,961,520
Total Assets ($000)	$38,846	$35,635	$30,351	$22,943	$19,435

Market Price Range of Shares (U.S.$)		1981 High	1981 Low	1980 High	1980 Low	1979 High	1979 Low	1978 High	1978 Low	1977 High	1977 Low
American Stock Exchange	1st Quarter	16⅝	14	30¾	15¾	17⅞	13⅛	19⅛	13⅜	11½	8⅞
	2nd Quarter	18¼	14⅜	25⅜	17½	22⅝	15⅛	16⅛	12½	10⅜	8¼
	3rd Quarter	21⅜	11	28⅝	22⅝	21⅜	16⅝	17⅜	12¾	14⅞	8
	4th Quarter	16¼	12⅜	27⅝	14⅝	26¼	18⅝	17⅝	10⅞	20⅜	13½

NOTE: Long-term obligations, redeemable preferred stock and dividends are not applicable for the disclosed periods.

(i) The number of shareholders of record on February 25, 1982 was approximately 1,220.

DIRECTORS

*Donald D. Barkwell — Calgary, Alberta
Senior Vice-President, Natural Resources
Norcen Energy Resources Limited

*Edward A. Galvin — Calgary, Alberta
President
Poco Petroleums Ltd.

Wilfrid A. Loucks — Calgary, Alberta
Vice-President, Minerals
Norcen Energy Resources Limited

*Frederick A. McKinnon — Calgary, Alberta
Director of various companies

Clifford A. Rae — Calgary, Alberta
Barrister & Solicitor
Macleod Dixon,
Barristers & Solicitors

David M. Tyerman, Q.C. — Regina, Saskatchewan
Barrister & Solicitor
MacPherson, Leslie & Tyerman
Barristers & Solicitors

*Member of the Audit Committee

OFFICERS

Donald D. Barkwell — *President*
Senior Vice-President, Natural Resources
Norcen Energy Resources Limited

Peter Kaye — *Vice-President, Exploration*
Vice-President, Exploration
Norcen Energy Resources Limited

William C. Hennenfent — *Vice-President, Production*
Vice-President, Production
Norcen Energy Resources Limited

David M. Tyerman, Q.C. — *Secretary*
Barrister & Solicitor
MacPherson, Leslie & Tyerman
Barristers & Solicitors

A. Kenneth Davies — *Treasurer*
Assistant Treasurer
Norcen Energy Resources Limited

William T. Kilbourne — *Assistant Secretary*
Vice-President, Administration and Secretary
Norcen Energy Resources Limited

Russell G. Rennie — *Assistant Secretary*
Assistant Secretary
Norcen Energy Resources Limited

EXECUTIVE OFFICE

715 Fifth Avenue Southwest
Calgary, Alberta
T2P 2X7

REGISTERED OFFICE

2161 Scarth Street
Regina, Saskatchewan
S4P 2V4

AUDITORS

Thorne Riddell
Calgary, Alberta

REGISTRARS & TRANSFER AGENTS

Canada Permanent Trust Company
Regina, Saskatchewan
Toronto, Ontario

Morgan Guaranty Trust Company of New York
New York, U.S.A.

STOCK EXCHANGE LISTINGS
(Symbol - POY)

Toronto Stock Exchange
Toronto, Ontario

American Stock Exchange
New York, U.S.A.

SUBSIDIARY COMPANY
(Wholly-owned)

P.O.R. Oil & Gas Inc.

PRAIRIE OIL ROYALTIES COMPANY, LTD.
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