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Shell Canada Limited
Annual Report
1985

Seventy-five years of growth with Canada

The graphic cutaway of the spiralling shell of the chambered nautilus, a perfect example in nature of systematic growth and development, is featured on the cover to symbolize Shell Canada's expansion in the first 75 years of the Corporation's existence.

Shell Canada in 1986 celebrates 75 years of growth as a major energy resources company. This report is dedicated to the anniversary of past achievements in serving Canadians, on which the Corporation builds for the future.

With assets of $5.8 billion, Shell Canada is one of the largest integrated petroleum companies in Canada. It is a major producer of crude oil and natural gas liquids, the largest natural gas and sulphur producer and a significant producer of thermal and metallurgical coal. The Corporation is also a leading manufacturer, distributor and marketer of refined petroleum products and petrochemicals.

In adapting to changing economic and political environments, Shell Canada moves into the future with an established operating and financial base, leadership in research and technology and a highly-skilled workforce and management team of about 7200 Canadians.

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Unless the context indicates otherwise, the terms 'Shell', 'Shell Canada', 'Shell Canada Limited', 'Corporation', 'Company', 'we', 'our' and 'its' are used interchangeably in this report to refer to Shell Canada Limited and consolidated subsidiaries.

On peut obtenir ce rapport en français sur demande.

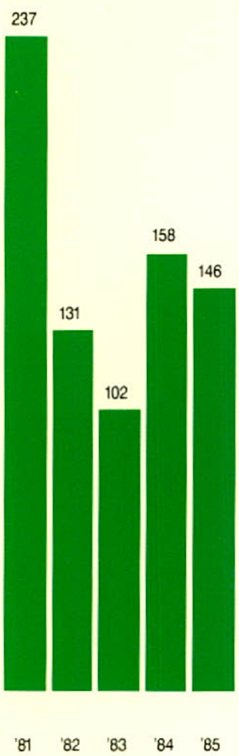
Shell Canada Limited – Financial and Operating Highlights

Financial

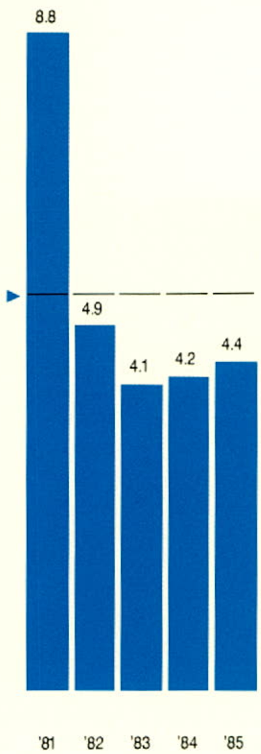
($ millions, except per share amounts)	**1985**	1984
Earnings – before extraordinary item	**146**	158
– after extraordinary item	**146**	123
Return on average capital employed (%)	**4.4**	4.2
Return on average common equity (%)	**5.8**	4.8
Earnings per Class "A" Common Share		
– before extraordinary item	**1.17**	1.27
– after extraordinary item	**1.17**	0.96
Dividends paid per Class "A" Common Share	**0.60**	0.60
Earnings (loss) adjusted for inflation	**32**	(39)

Operating

	1985	1984
Crude oil and natural gas liquids produced – gross (m^3/d)	**10 700**	11 400
Natural gas produced and sold – gross (thousands of m^3/d)	**16 700**	14 500
Sulphur sales – gross (tonnes/d)	**3 928**	3 960
Coal sales – gross (tonnes/d)	**6 360**	5 749
Crude oil processed by Shell refineries (m^3/d)	**37 500**	33 600
Petroleum product sales (m^3/d)	**34 400**	32 900
Chemical sales (tonnes/d)	**2 062**	1 667

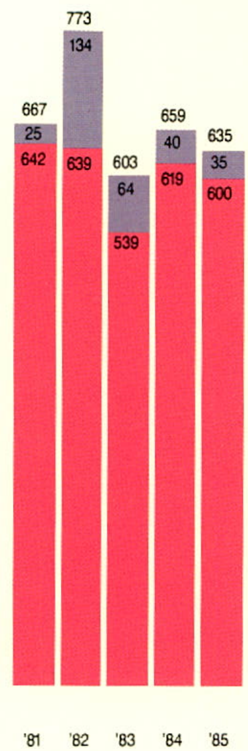


Earnings
($ millions)



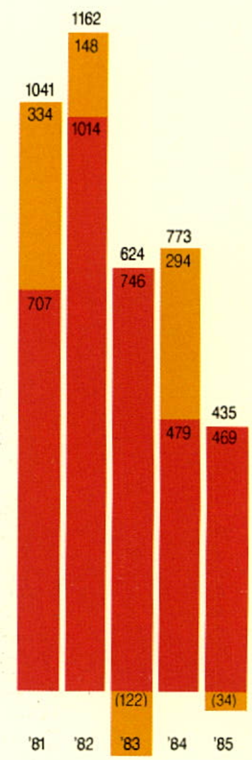
Return on average capital employed (%)

► Five-year average 5.3%



Cash internally generated
($ millions)

■ Other
■ Cash from operations



Investment during the year
($ millions)

■ Working capital (excluding cash) and other investments
■ Capital and exploration expenditures

President's Message

Shell Canada's objective is to achieve consistent, robust financial performance in whatever market conditions prevail. The key to this is flexibility in our investment plans. We have been putting technology and people to work to serve Canadians for 75 years. We will continue to do so.

Shell is marking its 75th year in Canada in 1986. We have grown with Canada. We will grow with Canada in the future.

The year 1985 was one of notable events and achievements, both for the Canadian energy industry and for your Company.

Actions taken by governments created a constructive, market-oriented environment for the oil industry. This is a turnaround from a policy regime in which we were beleaguered by government intervention and burdened by excessive taxation. Governments implemented these actions through the Western and Atlantic Accords, new oil and gas incentive programs in Alberta and other producing provinces, the Natural Gas Agreement, and through new operating rules applying to Canada Lands.

However, as we passed through the last weeks of 1985 into January, the investment stimulus provided by these positive events was dampened by the sudden downward spiral of international oil prices.

The objective that we have set, as we move through our 75th year and into the future, is to achieve consistent, robust financial performance in whatever market conditions prevail. The key to achievement of this objective is flexibility to adapt our short-term plans while pursuing our long-term strategies. We have this flexibility.

Significant achievements

The achievements across the total scope of Shell Canada's operations during 1985 are outlined throughout this report. The following were of particular note:

- The profit ($192 million) and cash contribution ($431 million) of the Resources segment.
- The cash contributions of the Oil Products ($152 million) and Chemicals ($64 million) segments.
- Investment of $469 million to support future growth.
- The achievement of consistent, reliable performance of the new Scotford refinery at 90 per cent of capacity and of the new Scotford styrene plant.
- The success of Project EnGulf in attracting thousands of former Gulf credit card accounts to Shell as well as new dealers and commercial/industrial accounts.
- New initiatives in natural gas and sulphur marketing, including progress toward penetrating a new natural gas market for Shell in the United States northeast.
- Implementation of a strengthened safety program through all Company operations.

Financial results

Consolidated corporate financial results for 1985 reflect some negative influences in the business environment.

Earnings of $146 million were lower than the $158 million achieved in 1984. Resources showed a substantial year-over-year gain of $28 million. However, this was offset by a loss in Chemicals directly related to the styrene business, lower earnings in Oil Products and a

$20 million inventory profit adjustment related to crude oil deregulation.

We are not satisfied with the 1985 earnings performance. Furthermore, the return on capital employed in the business at 4.4 per cent remains unacceptably low. We are determined to improve the earnings and profitability performance of the Corporation.

Corporate objectives

It is fundamental to the long-term stewardship of our shareholders' investment that we manage all of the resources of the Company – people, financial and technological – more effectively than any of our competitors. This applies to the continuing process of adjustment to short-term market conditions and to the pursuit of long-term strategic objectives.

Stated simply, these long-term strategic objectives to which we are committed are:

- Growth in net income and return on investment;
- Leadership in technology;
- Demonstration to our customers of the best product and service performance in the industry;
- Provision of a safe and productive work environment in which our people will be able to realize their full personal potential.

Investment plans

Turning to the role of investment in the achievement of these objectives, we have established a 1986 budget of some $675 million. Our principal focus is on the Resources segment. To the full extent that short-term business conditions permit, we plan aggressive investment programs in Western Canada. These include the oil sands of northern Alberta, enhanced conventional oil recovery programs and conventional oil and gas exploration and development. As well, we plan continued selective exploration investments in Canada's frontier regions.

We will also make substantial investments in the Oil Products segment, principally to upgrade our Montreal East refinery and our retail gasoline network.

Our investment targets to the early 1990s amount to $6 billion. We will adjust specific short- and long-term investments consistent with our financial capability.

The people factor

Goals and strategies are essential. Equally critical are the attitudes of Shell people toward achieving them. We believe that we will realize the success we seek through the capability, the determination and the commitment of our people. We are grateful for their immense contribution in the recently difficult times. We are confident of it in the future.

From their efforts, substantial benefits will flow to the Canadian economy. Shell, for example, contributed about $1.2 billion to Canada's balance of payments in 1985 through the exports of coal, sulphur, natural gas and petroleum and chemical products. The Corporation added value to the economy by creating products from natural resources amounting to $1.9 billion.

Your Company will continue on a path of growth. We are a Company with a proud history in Canada. We came in 1911. We developed new technologies, new ways of serving our customers, new ways of doing business. We have been putting technology and people to work to serve Canadians for 75 years. We will continue to do so.

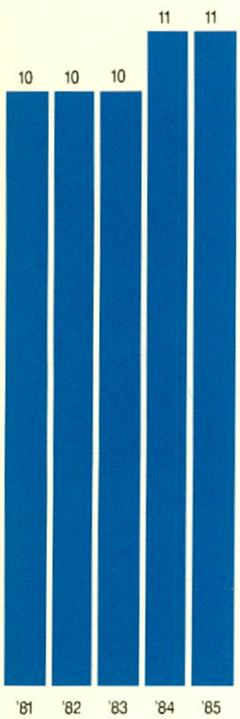
J.M. MacLeod
President and
Chief Executive Officer

On behalf of the Board,

J.M. MacLeod

J.M. MacLeod
President and Chief Executive Officer
Calgary, Alberta, March, 1986

Resources Group



Gross production of crude oil and natural gas liquids was virtually unchanged from 1984
(thousands of cubic metres daily)

Continued major emphasis is on programs to increase crude oil production and reserves in Western Canada. Successful expansion of the Peace River in-situ oil sands project and enhanced conventional oil recovery schemes are under way. In natural gas and sulphur, aggressive steps are being taken to develop and secure new market opportunities.

In a rapidly changing business environment, Shell Canada is pursuing exploration and development programs aimed at increasing crude oil production and reserves in Western Canada as well as maximizing opportunities resulting from its strong position in natural gas.

As it did at other times in its history in Canada, the Corporation has managed its way through a difficult period marked by the government-imposed National Energy Program and a worldwide recession during which oil and gas demand declined and prices were eroded. Investment flexibility was maintained and Shell is able to participate in profitable growth opportunities in a supportive investment climate created by new government policies, federal and provincial.

Those policy changes allow the industry, and Shell, to plan in a more rational business environment. The marketplace is becoming paramount and companies are facing the challenge of negotiating market-sensitive oil and gas prices and contractual arrangements.

Resources' 1985 oil and gas investments were made in anticipation of the improvements that evolved throughout the year in government policies.

A total of 107 conventional exploration and development wells were drilled, resulting in 60 successful oil wells and 15 successful gas wells.

In Western Canada, volumes of natural gas produced and sold increased 15 per cent in 1985, returning Shell to the rank of Canada's largest gas producer. This partly reflected the federal government's incentive pricing policy on exports which made Canadian gas more attractive in the United States. The Corporation's first interruptible short-term sale to the export market began in December, 1985.

Reserves situation improves

In 1985, net proved developed plus undeveloped crude oil and condensate reserves increased five per cent and natural gas reserves were up 3.5 per cent. Crude oil additions in excess of production were gained by positive revisions due to improved performance in a number of mature fields, aggressive infill drilling programs, field extension following recent exploration successes and net reserve benefits resulting from royalty reduction. Natural gas additions were also due in part to positive revisions based on improved performance of old fields, plus extensions and new field additions and royalty reduction benefits. Natural gas liquids and sulphur also showed increases in net reserves. Additional reserves data are shown on page 42 of this report.

Enhanced oil recovery schemes are under way in a number of Shell's oil fields and have the potential of adding significantly to reserves. Exploration activity, infill drilling in new and existing fields, and artificial lift and well workovers in mature fields are also adding to reserves and productive capacity.

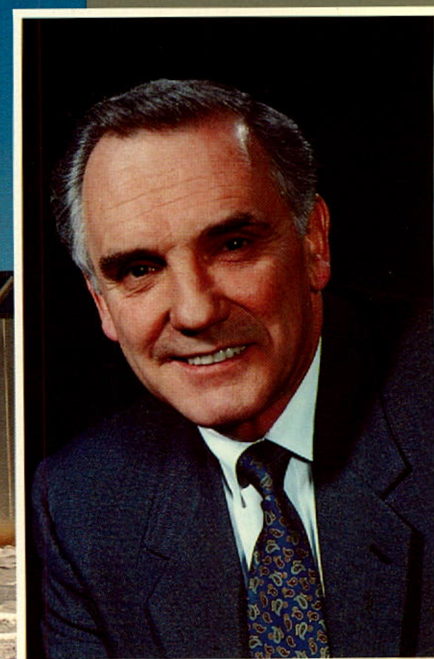
Progress continues at the Peace River in-situ oil sands project in Alberta. With the current expansion phase scheduled for completion in late 1986, planning has started for an additional expansion by the early 1990s. Consideration is also being given to installation of an upgrader to process Peace River bitumen into synthetic crude oil. As well, Shell has prime oil sands mining leases in Alberta's Athabasca region and a laboratory pilot to test a new mining extraction technology may be conducted in 1986.

In natural gas sales, Shell is firmly positioned to take advantage of opportunities resulting from deregulation in both domestic and export markets. Sales in 1986 are expected to show modest growth as new processing plants come on stream. Regulatory approval is being sought for an innovative plan to export gas to customers in the United States northeast by converting an idle oil pipe-

Resources financial profile

($ millions)	**1985**	1984	1983
Revenues	**1 454**	1 345	1 250
Earnings	**192**	164	154
Capital employed	**1 745**	1 617	1 599
Capital and exploration expenditures	**367**	246	204
Return on average capital employed (%)	**11.5**	10.2	9.8

Successful expansion is being carried out at the Peace River in-situ oil sands project in Alberta. This first-phase expansion will quadruple production capability to 1600 cubic metres a day by the end of 1986.



J.E. Czaja
Executive Vice President (Resources)

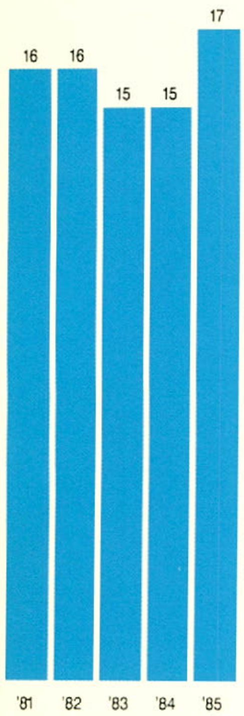
line running between Montreal and Portland, Maine. This is a potential new market for Shell Canada, with first sales scheduled in 1987. Over the next two years it is anticipated that the current surplus of U.S. gas will be worked off and export markets for Canadian gas will improve even further.

As part of a restructuring to reflect a more logical alignment of the Corporation's business activities, Shell Canada Resources Limited, a wholly-owned subsidiary, was amalgamated with its parent, Shell Canada Limited, effective January 1, 1986.

Crude oil activities

Most of Shell's exploration in the oil-prone areas of Western Canada in 1985 continued to be concentrated in Alberta, with limited exploratory work in Saskatchewan and northeastern British Columbia. Seismic surveys were conducted in selected areas of the plains and light oil was discovered in tests at Sakwatamau, Dimsdale, Little Smoky Lake, Gordondale and Sousa in central and northwestern Alberta.

Development drilling activities were at a high level in 1985 and wells were drilled in 11 different Shell-operated oil fields. Extensive infill drilling programs



Gross natural gas volumes produced and sold rose 15 per cent (millions of cubic metres daily)

were continued in the Midale and Benson fields in Saskatchewan where 63 wells were completed, and in the Virginia Hills field in Alberta where 12 wells were drilled. Five infill wells were drilled in Alberta's Garrington and Pembina fields. Outstep development drilling in Alberta continued, with six wells in Wembley and three in each of Manyberries, Sakwatamau and the Pouce Coupe/Progress area. Centralized facilities are being constructed in Wembley and Sakwatamau.

Drilling was also at a high level in outside-operated fields. Two of the most active programs were in Weyburn, Saskatchewan, where 21 infill wells were drilled, and in Wembley, Alberta, where nine wells were drilled.

Extensive and improved artificial lift and well recompletion programs were conducted in Virginia Hills, Innisfail, Fenn/Big Valley and Harmattan East during 1985 to increase oil production from mature wells.

Peace River oil sands progress

The single most significant investment in Shell Canada's strategy to increase crude oil reserves and production potential involves the Peace River in-situ oil sands project in northern Alberta. A pilot plant at Peace River, operating since 1979, has effectively demonstrated Shell's pressure-cycle steam-drive recovery process, which is expected to recover more than 50 per cent of the bitumen in place at the site.

A first-phase expansion started in 1985 is ahead of schedule and under the initial total budget of $200 million. Drilling of 213 wells during the year was completed four months ahead of schedule. Construction of processing, steam generation, oil dehydration and additional water treatment facilities is expected to be completed in the third quarter of 1986.

This expansion will quadruple production capability to 1600 cubic metres a day and first sales are anticipated by the end of 1986. Engineering design has started for a second expansion phase which will raise total production to 4800 cubic metres a day, with Shell Canada having a 50-per-cent share. Resulting reserve additions could amount to 13 million cubic metres.

Increased enhanced recovery

Shell moved aggressively in 1985 on enhanced oil recovery projects. A small-scale commercial hydrocarbon flood in the Simonette field is scheduled to start up in late 1986. At year end, regulatory approval was pending for a hydrocarbon flood in the Virginia Hills/Beaverhill Lake field and for an experimental carbon dioxide flood in the Manyberries field. Shell's share of the estimated incremental oil recovery from these three Alberta projects is forecast to total 1.9 million cubic metres.

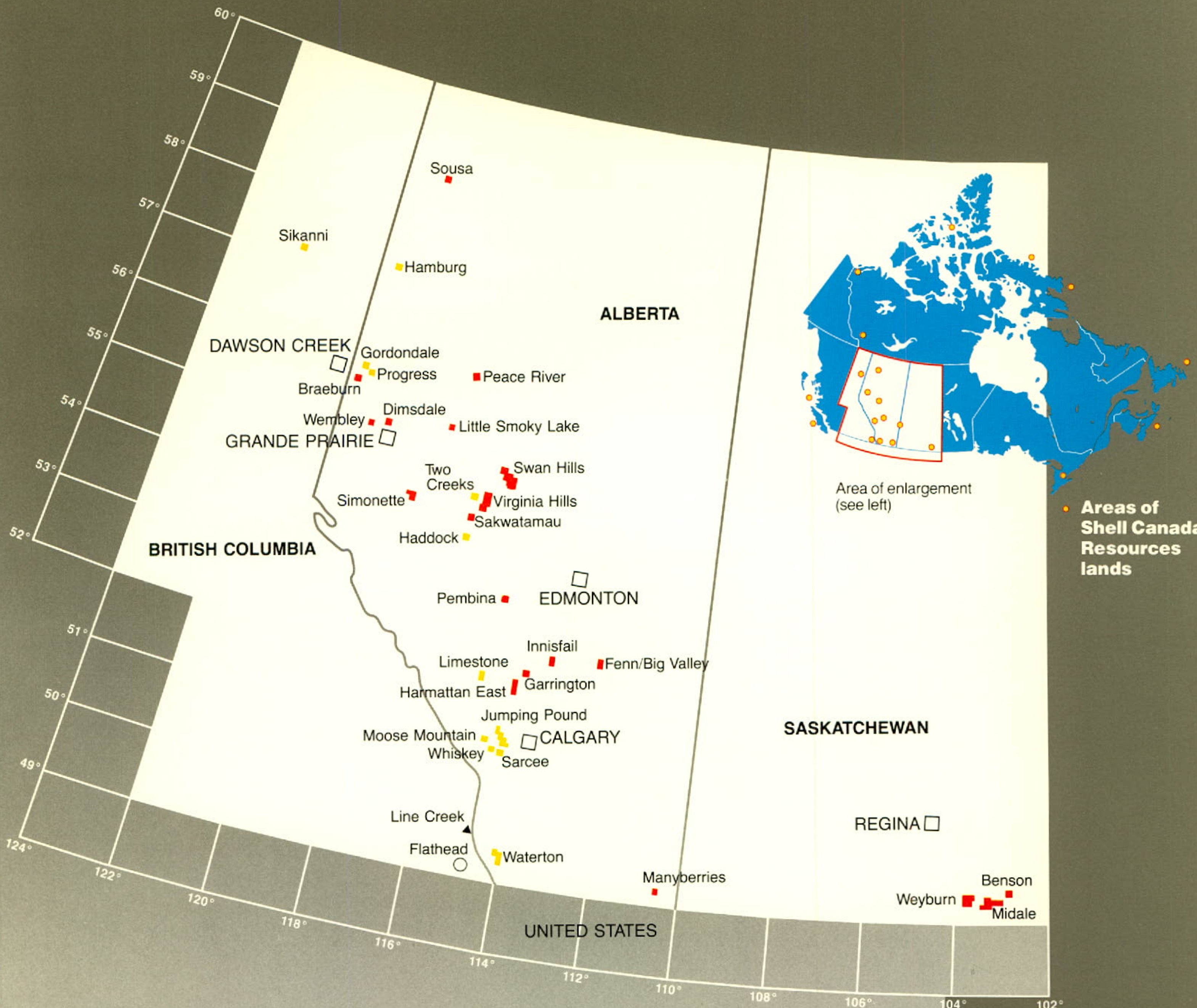
The Midale carbon dioxide pilot flood in Saskatchewan began operation in September with a preliminary water flood. This will be followed up by carbon dioxide injection in 1986. Results from this pilot will determine whether commercial-scale carbon dioxide recovery projects in this and other southeast Saskatchewan fields are technically viable.

Shell's efforts to delineate a natural carbon dioxide source in the Flathead Valley of southeastern British Columbia continued in 1985. One additional well was drilled and two were spudded late in the year in following up an encouraging three-well program in 1984. Development potential of the area will be evaluated on completion of the current drilling program.

Natural gas activities

Shell conducted seismic surveys and drilling programs during 1985 exploring for gas in the Alberta and British Columbia foothills and plains. Gas was discovered in tests at Hamburg, Two Creeks, Gordondale and Haddock in central and west-central Alberta and at Sikanni in northeastern B.C.

The Corporation initially encountered gas in 1981 at Hamburg, 250 kilometres northwest of Grande Prairie. The hole was redrilled in 1983 and completed as a gas well. A successful outstep well was completed in 1984. Now a $17 million plant to process the north Hamburg gas is under construction and is expected to be in operation by the second quarter of 1986. Owned 100 per cent by Shell, it has a planned capacity of about 1.2 million cubic metres daily. The 1985 Hamburg new pool discovery is located approximately 10 kilometres to the southwest



Gas Oil

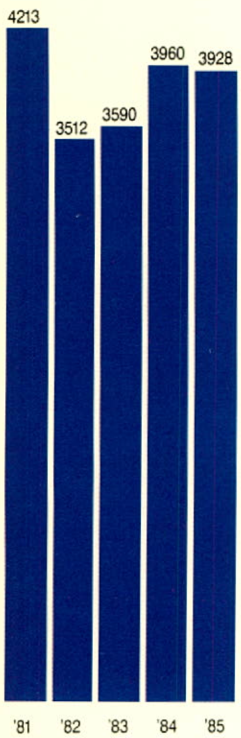
Western Canadian exploration and development activities

and additional exploratory and development drilling is under way.

Development work continued in producing gas fields to maximize deliverabilities under existing gas sales contracts. This included drilling three wells in the Jumping Pound West field and one in Waterton, beginning construction to reactivate wells in the north end of Waterton by mid-1986, and starting up compression facilities in the Sarcee field. At year end, outstep drilling was under way to delineate new reserve potential in the Limestone, Waterton and Jumping Pound West areas. An aggressive delineation program for new reserves is also planned for 1986.

The Progress gas plant and gathering system, 65 kilometres northwest of Grande Prairie, began operating in October to process natural gas from four area fields. Shell's initial share of production has averaged 450 000 cubic metres a day of sales gas. Three new gas wells were also drilled in the Progress area during 1985.

The Moose Mountain and Whiskey Creek gathering, compression, pipeline and processing system, 50 kilometres southwest of Calgary, went into operation late in the year. Shell's initial share of production is 350 000 cubic metres a day of sales gas, 100 cubic metres daily of liquid petroleum products and 75 tonnes a day of sulphur.



Sulphur sales remained at a high level in 1985
(tonnes daily)

Sulphur sales continue high

Export demand for sulphur during the year continued at the high level established in 1984. Shell is Canada's largest producer and independent marketer.

Shell's 1985 sales volumes, which hit an all-time high in the first half, averaged 3928 tonnes daily through the year, a level about the same as in the previous year and forecast to continue in 1986.

In responding to the sustained high demand, the Corporation significantly expanded its sulphur pellet-forming capability. More than 80 per cent of Shell's sales are directed to markets outside North America and sulphur must be formed into pellets for shipment through Vancouver. A new $11 million pellet-forming unit was added to the Jumping Pound gas plant near Calgary and utilization of facilities was maximized at the Waterton plant in southwest Alberta. Capacity of the Jumping Pound unit, completed in the third quarter of 1985, is 400 000 tonnes a year.

To enhance marketing opportunities, Shell terminated the single agency approach to making sulphur sales and will manage this activity with its own staff.

Frontier region developments

On the East Coast, Shell and partners in 1985 continued the evaluation of Nova Scotia offshore oil and gas prospects by exploration drilling and seismic surveys. The oil potential was downgraded by the results of two exploratory wells, Peskowesk A-99 and Kegeshook G-67, both abandoned without encountering any hydrocarbons.

A natural gas appraisal well, Alma K-85, was drilled five kilometres southwest of the 1984 Alma discovery. Five zones tested gas at rates varying from 270 000 to 850 000 cubic metres a day. An exploratory well, Merigomish C-52, was then drilled 10 kilometres south of Alma with the objective of proving more gas in the greater Alma area. The well was unsuccessful and Alma, at this time, is considered a modest-sized gas accumulation.

Another exploration well, North Triumph G-43, discovered natural gas on a prospect 23 kilometres east-northeast of the 1983 gas discovery made by Shell and partners at Glenelg. Two zones were tested at North Triumph G-43 and gas flowed at rates of 990 000 cubic metres and 1.04 million cubic metres a day from intervals 3835 to 3846 metres and 3795 to 3809 metres respectively. Condensate rates were 25 and 32 cubic metres daily. A delineation well, North Triumph B-52, is being drilled approximately three kilometres southwest of North Triumph G-43.

A three-dimensional seismic survey was completed at Glenelg in 1984-85 and further appraisal drilling is planned.

The gas accumulations discovered to date on Shell-operated acreage offshore Nova Scotia would require additional volumes to support commercial development. For the longer term, the prospects off Nova Scotia remain of interest.

In the Arctic Islands, the Corporation participated in drilling an oil and gas discovery, Cape Allison C-47, about five kilometres from Ellef Ringnes Island. The well, operated by Panarctic Oils Limited, was drilled to a depth of 2100 metres from an ice platform. It flowed light oil at rates up to 400 cubic metres daily and gas at 740 000 cubic metres a day on production tests. Shell has a 25-per-cent interest in acreage covering the Cape Allison prospect.

The Corporation is participating in a second Arctic Islands exploratory well, North Buckingham L-71 four kilometres west of Buckingham Island, and drilling commenced in early 1986.

In the Mackenzie River Delta of the Northwest Territories, Shell resumed exploration in 1984 after an absence of seven years. Seismic surveys were conducted on Shell lands in 1985 and a two-well drilling program is scheduled to start in 1986 and continue in 1987. The Corporation's Delta exploration in earlier years resulted in the discovery of Niglintgak and Kumak gas and oil accumulations in 1973 and 1974 respectively and the Kugpik oil discovery in 1973.

Intense coal competition

Competition in world coal markets remains intense. In these very difficult conditions, Crows Nest Resources achieved significant productivity improvements at its Line Creek mine in southeastern British Columbia. In a

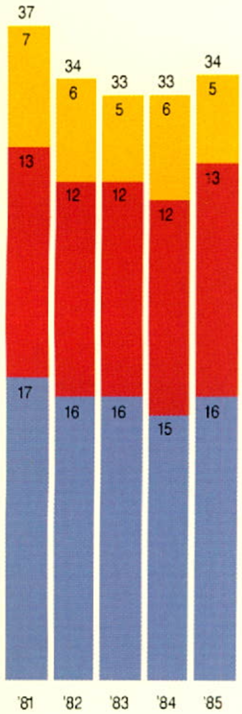
To meet continuing high export demand for sulphur, Shell Canada installed a new pellet-forming unit at its Jumping Pound plant near Calgary. Tim Tivendale monitors the sulphur pellets being produced at the $11 million unit.

phased approach to maintain production for current contracts as well as expand Line Creek's total utilization as new sales are developed, a new road to access additional coal reserves was constructed in 1985 at a cost of $4 million.

The Line Creek mine continued to provide metallurgical coal to customers in Japan and Korea and thermal coal to customers in Korea under long-term contracts. These contracts are subject to periodic review in light of market conditions. During the year, Crows Nest Resources shipped 1 069 000 tonnes of metallurgical coal and 1 252 000 tonnes of thermal coal from Line Creek compared with 1 038 000 and 1 072 000 tonnes respectively in 1984.

Approval in principle from the B.C. government is expected in early 1986 on an application related to the proposed Telkwa thermal coal project near Smithers, B.C. While no commitment by Crows Nest Resources to proceed is likely in the near term because of reduced growth in export demand, the approval was sought to enable the project to move ahead when markets improve.

Products Group



Petroleum product sales increased four per cent over 1984
(thousands of cubic metres daily)

- Other products
- Middle distillates
- Gasolines

Gains were recorded by Oil Products in 1985 sales volumes, market share and revenues, although earnings were disappointing. Shell's refineries operated at high average utilization rates. In Chemicals, robust polypropylene markets kept the Sarnia plant operating at full capability and demand for industrial chemicals remained stable, but international over-supply severely depressed margins for styrene.

OIL PRODUCTS

Shell's Oil Products division achieved significant gains from initiatives to be highly competitive and offer quality products and services that meet the needs of Shell customers. A variety of programs were launched in 1985 to reinforce and communicate the Corporation's commitment to remain a leading marketer of oil products.

There was continuing investment in both the manufacturing and retailing sectors, new emphasis on dealer and agent training and incentives and bold new marketing programs and promotions. Comprehensive employee communications sessions were held, each tied to the theme of customer focus, and more extensive use was made of consumer surveys.

Although pricing instability continued, particularly in Eastern Canada, and some early operational difficulties were encountered at the Scotford refinery in Alberta, overall results were positive in terms of volumes, market share, revenues, cost control, cash flow and refinery utilizations. Oil Products is strongly positioned to maintain its forward thrust during 1986.

Effective January 1, 1986, refinery, marketing and chemical businesses were transferred to Shell Canada Products Limited, a wholly-owned subsidiary of Shell Canada Limited. Shell Canada Chemical Company will operate as a division of Shell Canada Products Limited.

During 1985, Shell's refineries operated at about 90 per cent of capacity. A fire in a hydrocracker unit at Scotford in the first quarter reduced refinery production to 40 per cent, but repairs by mid-year and the start-up of a second hydrocracker restored crude processing runs to close to 95 per cent of design capacity. Quality control and yields at Scotford improved through the year and other minor start-up problems were satisfactorily resolved.

A major addition to the Montreal East refinery was approved late in 1985. An $80 million residue catalytic cracker, scheduled to be completed by the third quarter of 1987, will increase the refinery's octane generation capability while reducing the production of heavy fuel oil. This project will also improve energy utilization and propylene production.

Gains in sales volumes

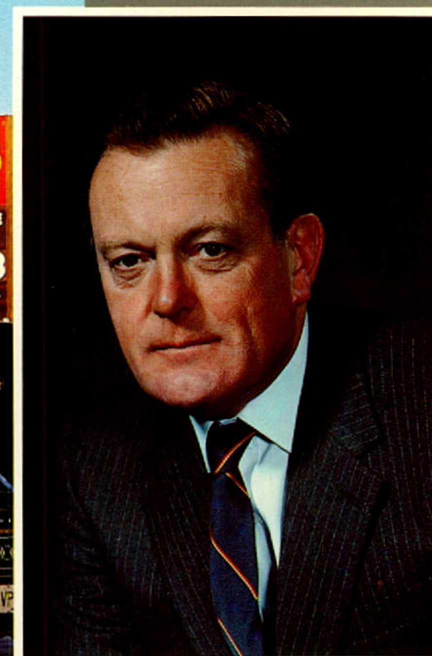
Despite a steady but moderating decline in demand across Canada for petroleum products, Shell made gains in 1985 in market share and volumes compared with overall industry performance. Light oil sales were up over 1984, increasing approximately eight per cent to 10.6 billion litres, including exports. An offsetting factor on earnings, however, was unit product cost, exacerbated by rising crude prices.

A number of programs designed to enhance Oil Products' competitiveness for the future were launched or continued during 1985. They involve a major review and implementation of marketing strategies, development and installation of information systems, upgrading of service stations and expansion of retail services and promotions. The cost of these programs detracted from the year's earnings.

Oil Products financial profile

($ millions)	**1985**	1984	1983
Revenues	**4 504**	4 127	3 869
Earnings	**54**	71	23
Capital employed	**2 029**	2 095	1 673
Capital expenditures	**40**	144	273
Return on average capital employed (%)	**2.6**	3.8	1.4

Customers service their cars at a newly-upgraded service station in Toronto. The continuing program to improve the appearance of Shell's retail outlets includes multi-grade product dispensing equipment, offering customers gasoline selection convenience through one pump.

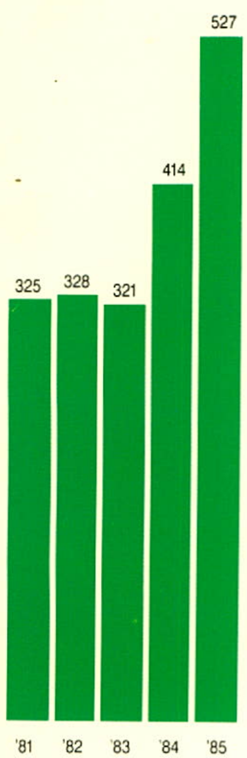


Donald J. Taylor
Executive Vice President (Products)

A program to improve the appearance of Shell's service stations in major metropolitan centres was started, with 215 sites completed by the end of the year and 160 scheduled for 1986. In some cases, this includes new signs and internally-lit canopies. Buildings at stations are being painted in neutral colours to focus attention on the pump island and Shell signs. A new canopy design, in Shell's red and yellow colours, uses translucent material lighted from behind, making it far more visible to motorists at night.

The upgrading includes installation of new multi-grade product dispensing equipment, offering customers gasoline selection convenience through one pump. In addition, a test site was developed in Toronto for state-of-the-art consumer invoicing and billing computerization at the point of sale. The process is activated by credit card at the service station site.

In an aggressive and successful response to the Petro-Canada takeover of Gulf Canada's Ontario and Western Canada marketing network, Shell invited Gulf



Chemical product sales revenues rose 27 per cent in 1985
($ millions annually)

customers to change their oil products supplier. The late summer newspaper and broadcast promotion, called Project EnGulf, resulted in thousands of new Shell credit cards being issued and a large number of former Gulf commercial and industrial accounts being supplied by Shell.

Lubricants growth continues

The lubricants segment of Oil Products continued to record significant advances in 1985. Exports of custom-manufactured lubricants were doubled, with Shell product being shipped around the world. A substantial share of the domestic and international markets for AeroShell oil, a piston engine oil for aircraft, is held by the Corporation. Sales of grease in 1985 increased four per cent over the previous year.

Sales volumes exceeded expectations following a national marketing campaign for TLO, a premium high-grade motor oil. Further gains are expected in 1986 with the support of media promotions featuring Shell's involvement with professional motorsport.

Canadian Oil, a subsidiary of Shell Canada, operated its Toronto plant at full capacity in re-refining used lubricating oil. Improvements were made in 1985 in yield and unit costs. Canadian Oil's recycling process continues to be consistently supported by government representatives and special interest groups for the environmental waste-disposal benefits as well as conservation of a valuable resource. The plant, in its second full year of operation, is making a modest contribution to profit and cash flow.

CHEMICALS

All three major business centres – industrial chemicals, polymers and styrene – contributed to increased activity for Shell Canada Chemical Company in 1985. Total tonnage increased 24 per cent over 1984, revenues rose 27 per cent and exports, as a per cent of sales, advanced to nearly 60 per cent.

Margins for most industrial chemicals were firm throughout the year, supported by stable demand and successful marketing programs. Exceptions were benzene, toluene and xylenes, which experienced wide price swings caused by trends in unleaded gasoline demand and some industry over-capacity. Close to half of the Corporation's industrial chemicals is exported to various countries around the world. The demand outlook remains positive for 1986, but declines in international oil prices could cause some instability in product pricing.

Robust polypropylene markets

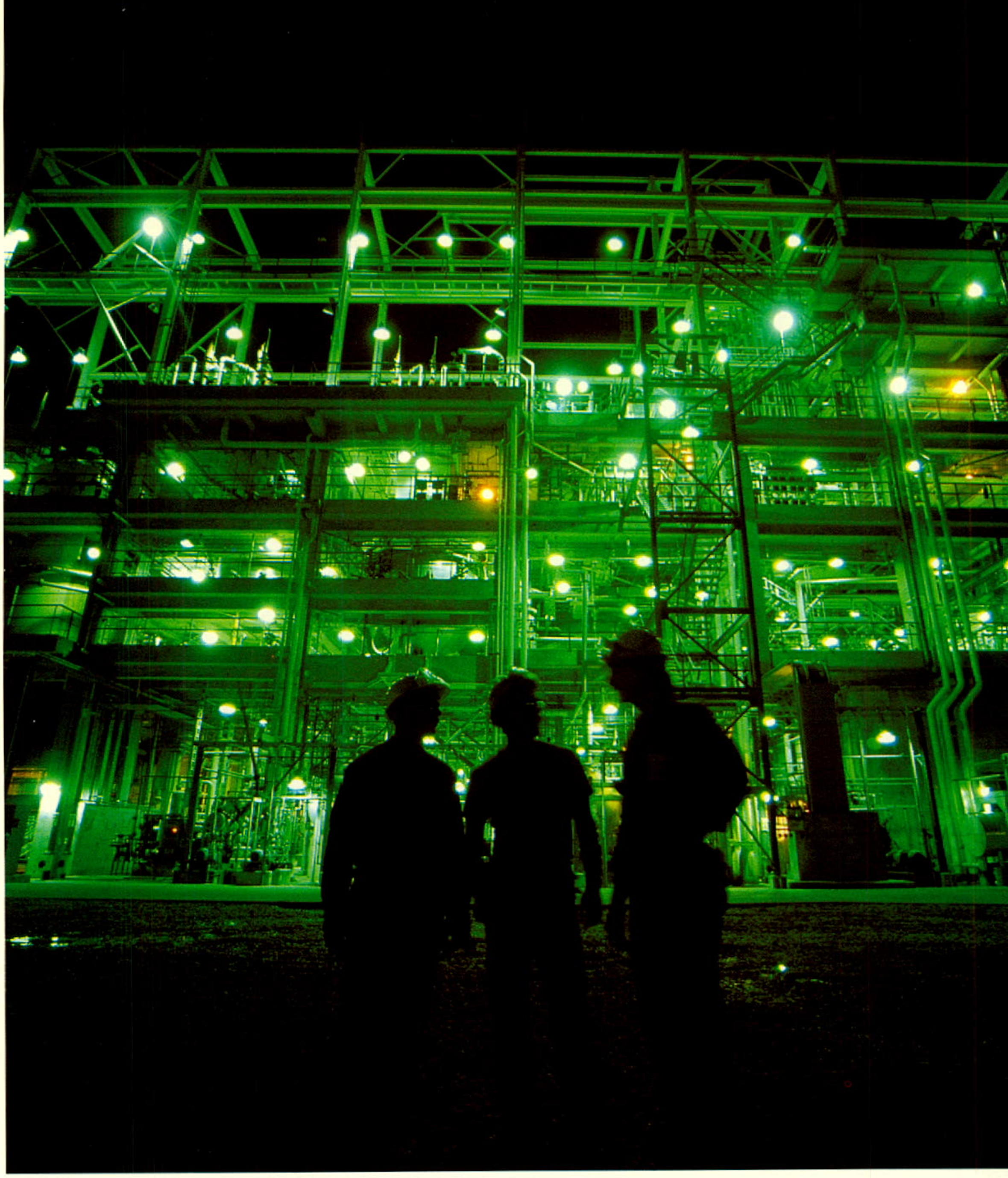
Strong demand for polypropylene, especially in international markets, kept the Sarnia plant operating at full production capability in 1985. Operating improvements and efficiencies led to record production levels in the plant which has a name-plate capacity of 80 000 tonnes a year. Substantial volumes were shipped to the Far East where China is Shell's largest polypropylene export market.

Polypropylene, a versatile plastic, is used in carpet backing, fine fibres, ropes, packaging and a variety of moulded consumer articles. In the domestic market it is replacing competing synthetic resins and natural fibres in terms of cost performance, and many new applications are being developed.

Assuming sustained world economic activity, markets for polypropylene are expected to remain robust in 1986.

Chemicals financial profile

($ millions)	**1985**	1984	1983
Revenues	**527**	414	321
Earnings (loss)	**(11)**	9	8
Capital employed	**943**	977	838
Capital expenditures	**23**	74	260
Return on average capital employed (%)	**—**	1.0	1.1



Strong demand for polypropylene, a versatile plastic, has kept Shell's Sarnia plant in Ontario operating at full production capability. Assuming sustained world economic activity, markets for polypropylene are expected to remain robust in 1986.

Scotford styrene difficulties

Despite international success in styrene marketing, the 1985 results for this business centre were adversely affected by world over-supply and by start-up production problems at the Scotford plant in Alberta.

Current surplus international capacity continued to depress prices and margins on product. Over the long term, anticipated global growth in demand for styrene and its derivatives is expected to absorb existing excess supply and prices should improve. Shell has established a strong customer base throughout Pacific Rim countries and North America and will benefit when markets recover.

Various difficulties experienced at the Scotford plant during 1985 held production levels well below capacity. Early in the year there were interruptions in benzene supply from the nearby Shell refinery, a problem that has since been corrected. Benzene is a basic feedstock used in the manufacture of styrene monomer. Mechanical and equipment failures have been overcome, including the replacement of a major process heat exchanger in the plant's styrene unit. By year end, Scotford was operating at more than 90 per cent of its styrene production capacity of 300 000 tonnes annually.

Business Services/ Research/ Corporate

The Corporation is committed to provide a safe and productive work environment in which Shell people can realize their full individual potential while achieving business goals. It strives to build on a position of leadership in technology, supported by a strong research effort. And it continues to create long-term economic and social benefits for Canadian society in general.

The Business Services group, created in Shell's 1984 reorganization, provides efficient support services for the Resources, Products, Corporate and Research groups. It covers the areas of Human Resources, Information and Computing, Health, Safety and Environment, Purchasing, Legal, Facilities and Administrative functions. The integration of these services contributes to a business and technical environment within which employees can maximize their contribution to corporate performance and achieve personal growth.

In 1985 steps were taken to create a more responsive, results-oriented work environment. A performance management process was launched that sharpens the relationship between organizational objectives, individual employee goals and work priorities, and recognition and reward systems.

In October, a Human Resources strategy review was completed which identified a number of quality and motivation factors to assist the Corporation in developing the skills base required to achieve its business strategies. Design and implementation of specific initiatives were under way at year end.

Human Resources also conducted a corporate-wide organization effectiveness survey in 1985. Its purpose was to obtain detailed employee views of the Corporation's strengths and weaknesses, providing the basis for planning future policies and programs. More than 80 per cent of employees responded to the survey questionnaire. The responses reflected a continuing strong commitment to making Shell a more successful company.

Employee communication received greater emphasis during the year as a way of building employee understanding of and commitment to corporate goals. Increased attention was given to face-to-face communication between supervisors and employees. Underlining the 1984 objective, managers at all levels initiated programs to improve employee understanding of how each individual can contribute to Shell's future success.

Health, safety and environment

A high level of concern for human health and safety as well as environmental protection continued in 1985. Particular attention was placed on enhanced safety management. Initiatives included the formalization of a Health, Safety and Environment department within Business Services and the formation of a steering group of senior managers reporting to the President as a focal point for safety. Strengthened safety programs are being implemented.

To comply with new and strict government regulations, Shell Canada emergency response teams are now in place at strategic locations across Canada. This represents a formalization of the previous practice of assisting railroads and other carriers at spills involving Shell products. An agreement was also reached to assist the Canadian coast guard in responding to major oil spills.

A major issue in 1985 continued to be the health and environmental effects of gasoline. An internal task force was formed to study octane capability following federal government moves to reduce permissible levels of lead in gasoline and introduce more stringent automotive emission standards. In addition, major evaluation of employee and customer gasoline exposure levels was undertaken.

Computerization of all Shell Canada material safety data sheets was completed in 1985, significantly increasing product health and safety information for customers.

The Corporation continued to promote programs enhancing employee health. A physical fitness centre was opened at Shell Centre in Calgary.

Workplace technologies

The successful development and management of new workplace technologies have become important aspects of today's business. Virtually every Shell Canada employee makes use of the computer in some aspect of Shell work – from the preparation of letters and messages to

The latest technology is being utilized in Shell's computer processing systems. Using an advanced computer terminal, Debbie Morton executes four concurrent on-line sessions to help in diagnosing problems anywhere on Shell's national telecommunications network.

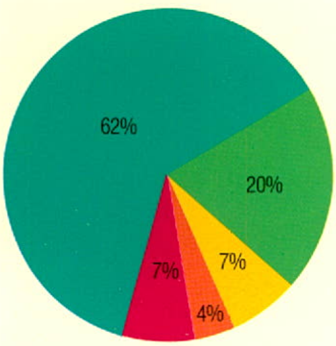
R.F. Taylor
Senior Vice President
(Business Services)

applications as complex as process control in refineries, gas plants and oil fields.

Computing has come a long way since 1957 when Shell installed its first computer in Calgary. That first machine performed an amazing 30 calculations per second. The Corporation's newest computer, the largest of many now used in Shell, performs 30 million instructions per second. In telecommunications, as well, technology has changed more in the last five years than in the previous 50.

In 1985 significant progress was made by the Information and Computing section of Business Services to renew many of the computer processing systems. These included new systems for exploration geophysical processing, financial and production accounting, and Human Resources. The new systems utilize the latest technology and significantly enhance productivity and the availability of information for decision-making.

An Information and Computing strategic review was commenced during the year as a focus for future computing plans to support business strategies. In addition, major upgrading was realized in the Corporation's voice and data telecommunications network allowing Shell people across the country to have access to, interpret and act on information essential to their work.



Shell Canada's 1985 'value added'
($1 871 million)

- Royalties and taxes to governments ($1 153)
- Employees wages and salaries ($371)
- Interest to lenders of capital ($128)
- Dividends to share-holders ($83)
- Retained in the business ($136)

A leader in research

Shell's research and development activities have kept it in the forefront of technological innovations. Hundreds of customer-focused products have emerged from such research.

Rapid growth in research – with consolidation of downstream activities in the Oakville Research Centre in 1970 and then with the opening in 1983 of upstream facilities at the Calgary Research Centre – has given the Research and Technology department a greater role in Shell Canada's business objectives.

Numerous achievements have resulted since the opening of the Oakville and Calgary centres. These include development of advanced performance lubricants and greases such as Rotella T, TLO, Extrema and microgel greases, non-leaded gasolines, the formulation of new polypropylene films and fibres, and an improved understanding of the steam-drive process for bitumen recovery from oil sands. Advances were also made in such engineering and science disciplines as material corrosion, production chemistry, well completion using foamed cements and oil-based drilling and stimulation fluids.

Shell's support of institutions and universities is also opening doors to significant research and development efforts for both the present and future.

As an active participant in Shell's international research community, Shell Canada contributes through independent research and development to a general pool of knowledge. In return, it is strengthened by access to the resources and developments of Shell laboratories around the world.

In 1985 the cost-sharing agreement with Shell Internationale Research made available to Shell Canada $570 million of technological developments from other Shell laboratories. Shell Canada paid $15 million as its share while receiving $7 million in funding for domestic research programs.

Shell Canada's research and development expenditures in 1985, including the Shell Internationale agreement, totalled $34 million compared with $28 million in 1984. Capital expenditures were about $2 million.

Partners with the community

In a variety of ways, Shell Canada contributes to the broad economic and social goals of Canadian society. The Corporation regularly carries out information exchanges with community groups interested in and affected by proposed developments. Communication between the industry, public and government agencies creates the basis for evolving regulatory and policy approaches in the energy field.

Shell Canada's activities have consistently resulted in significant benefits to the Canadian economy.

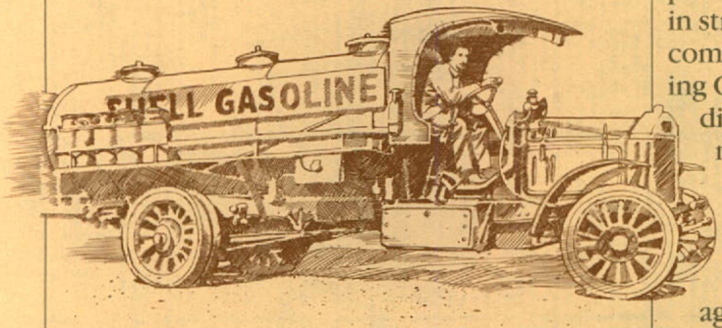
For example, the Corporation's added value to the economy – the difference between the cost of materials and services and revenues from product sales – amounted to $1.9 billion in 1985. Of this total, governments received by far the largest share, $1.2 billion, in royalties and taxes. Employees earned $371 million in salaries, wages and contributions to pensions and social insurance. Lenders of capital received $128 million in interest payments, and shareholders received $83 million in dividends. The remaining $136 million was reinvested in the business.

As well, Shell actively promotes Canada's businesses with a policy of giving preference to suppliers, consultants, contractors and service companies offering a high level of Canadian content. Purchases in 1985 of goods and services, excluding crude oil, amounted to $1 billion. Of the total, 94 per cent came from Canadian-based suppliers and 80 per cent, or about $800 million, was spent on Canadian-made goods and services.

The Corporation contributed $2 million during 1985 to more than 700 non-profit volunteer community organizations in the fields of health, social services, education, culture and sports. A large part of Shell's community support was directed to United Way campaigns in which many employees participated. The Corporation also had a major role in sponsoring the Steve Fonyo Journey for Lives program, and ultimately contributed some $200 000.

In education, the emphasis was on university disciplines of direct interest to Shell such as engineering, earth sciences, environmental research and business administration. A Shell-sponsored workshop in Calgary for high school teachers from across Canada stressed energy and environmental studies.

Building on a proud past



Seventy-five years ago, Shell came to Canada – and the beginning was indeed modest in scale.

That initial entry in 1911 by the Royal Dutch/Shell Group of Companies, a major international petroleum concern at the time, was a small bunkering plant in Montreal to serve the ocean shipping trade. There were but few signs then of the potential for Canada's development and the growth of the petroleum industry.

It was an age of ships, railways, horses and carts, a few thousand rattling autos, single-engine planes, frock coats and high-buttoned shoes. The Canadian petroleum industry consisted of some small and declining oil fields in Ontario, and a few natural gas showings in the West and the Maritimes.

But a kernel of growth was there, though the numbers seem small in retrospect. There were slightly over seven million Canadians, owning some 34,000 motor vehicles, driving on fewer than 2000 kilometres of paved roads.

The horizons widen

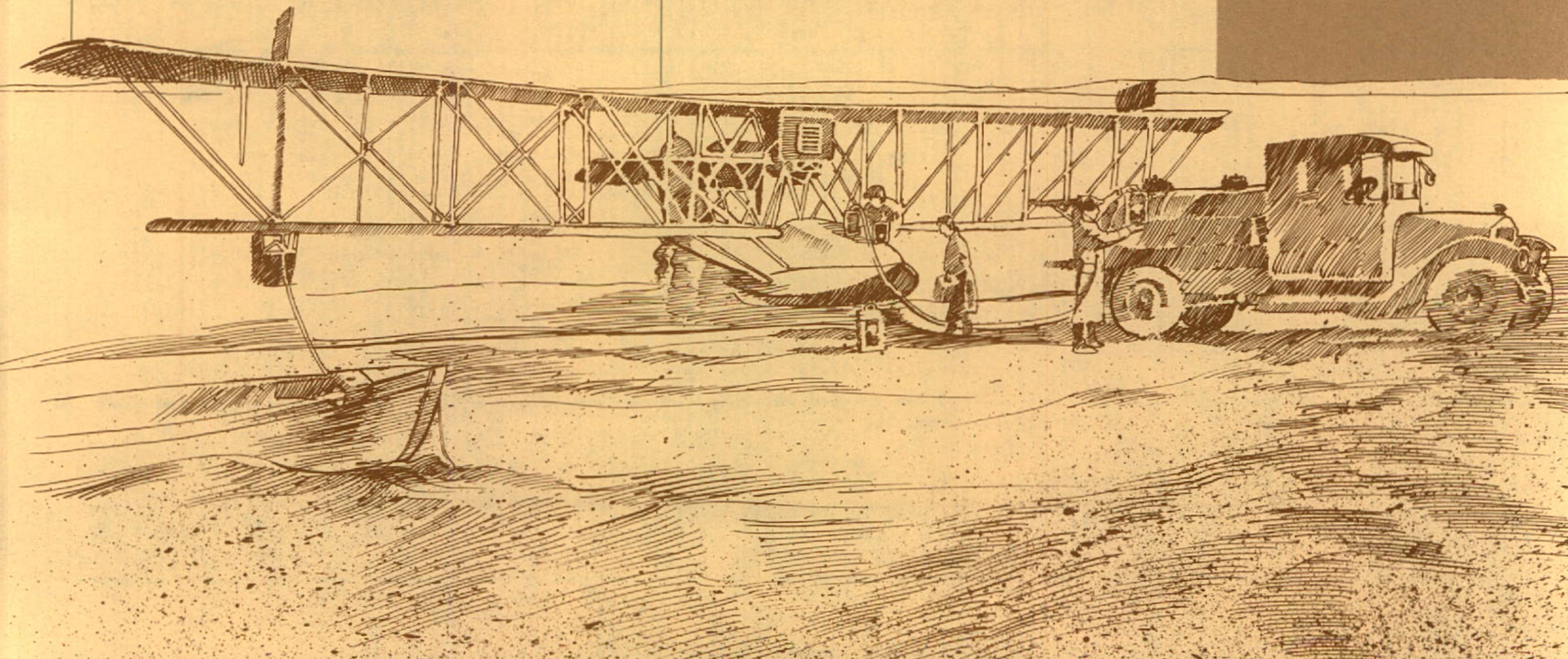
The historical record shows that those who directed early Shell operations in Canada were not deterred by this unprepossessing prospect. They took setbacks in stride and did not shy from high-risk commitments in the then new, developing Canadian petroleum industry. They did not hesitate to develop and implement a variety of innovative production and marketing techniques.

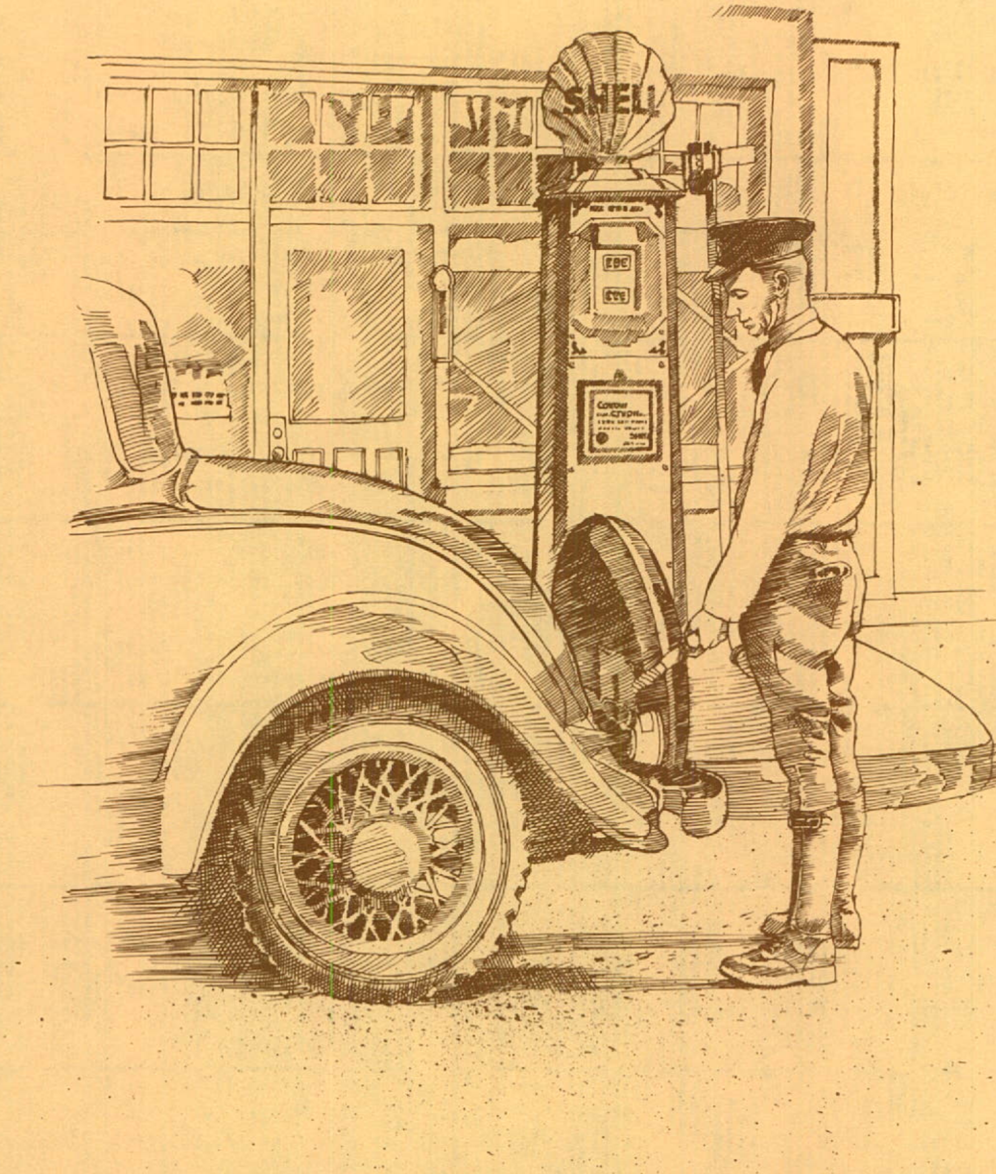
Shell was committed to a presence in Canada, and to widening its horizons. In the 1920s, it launched aggressive, market-building programs to establish its position in serving the rapidly expanding demand for gasoline and fuel oil.

The company carried this growth pattern through the Depression of the 1930s. Its market share rose to 11 per cent from six, and employment in the company grew by 50 per cent to nearly 1,000 by 1939. Refineries were opened in Montreal and on the West Coast. Shell also built more company-owned service stations and converted many of the multiple-brand dealers to Shell outlets – quite different and new marketing patterns for the time.

Marketing innovations

Other innovations in product handling were introduced to build customer trust in quality. Shell motor oil was sold in bottles, a first in the industry and popular because it prevented adulteration with low-quality oils. The company was also first in developing a new gasoline tank-sealing technique to guarantee to the customer that Shell product was not mixed with inferior brands.





1911

1930

1948

Through the 1920s and 1930s, as in later years, Shell was in the forefront as a supplier of aircraft fuel to the growing aviation industry. Until 1930 it had marketed an unleaded automotive gasoline and then in 1931 introduced a leaded premium gasoline. In the late 1930s, the company marketed propane, the first to do so from a Canadian refinery so far as is known.

After the restrictions of the Second World War, Shell initiated a highly successful program to upgrade its transportation facilities and retailing operations in Central Canada. To implement expansion plans, Shell became the first in the industry to employ the sale/leaseback principle to service station financing to assist dealers in getting established.

Exploration expansion

By the late 1940s the company had acquired major land holdings in Western Canada and had stepped up its exploration and development activities. Shell seized the opportunity to play a front-rank role in this most significant of Canadian endeavours – the discovery and development of Canada's own energy resources.

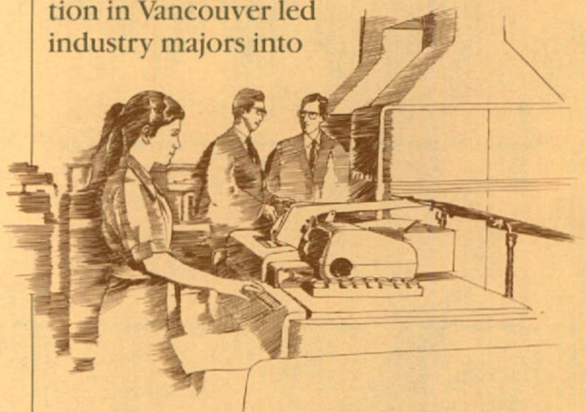
The company in those early years was in the forefront in developing and using natural gas processing technology. It was and continues to be a leader in the drilling of deep gas reservoirs in the foothills of the Rockies. And it is recognized for its technological advances in the production of gas with high sulphur content.

At Jumping Pound near Calgary, where a processing plant was opened in 1951, Shell pioneered the Canadian production of elemental sulphur from gas. At Waterton, near a major gas discovery in the southwest part of Alberta, the company's expanding technology was applied in another processing plant to separate a wide range of product, including methane, ethane, propane, butane and sulphur. Shell quickly became the largest Canadian producer and exporter of sulphur.

First in petrochemicals

It was in the early 1950s that Shell became the first Canadian oil company to manufacture chemicals from petroleum at its Montreal East refinery. The business grew rapidly and two decades later world-scale petrochemical plants to produce polypropylene and isopropyl alcohol were constructed at Sarnia, Ontario.

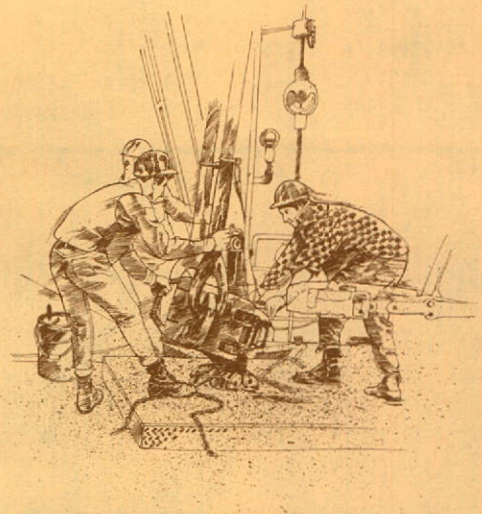
Dramatic expansion for Shell occurred in the 1960s. Two major acquisitions, of North Star Oil and Canadian Oil Companies, sharply increased the company's asset base, resource holdings, refining capacity and marketing strengths. Later in the decade, the opening of a Shell self-service station in Vancouver led industry majors into



the era of pump-your-own gasoline.

It was on November 1, 1962, that Shell became a public company in Canada. The Canadian proportion of public shareholders has climbed steadily since, from 34 per cent at the end of 1962 to more than 85 per cent in 1985.

In the 1970s, Shell acquired Crows Nest Resources to produce and market coal from a British Columbia mine.



Benefits to Canada

The story of Shell in Canada is liberally dotted with many pioneering thrusts and new ideas, with the application of advanced technologies and with the numerous spin-off benefits that have accrued to Canadian businesses and employment.

As a technologically intensive company requiring a variety of goods and services, Shell helped develop the resources and skills of many Canadian suppliers and job contractors from east to west. It aided in the initial design and development in Western Canada of mobile trailers for exploration and production requirements, equipment that became internationally renowned.

On the West Coast, it commissioned the construction at Victoria in 1964 of the first offshore drilling vessel ever built in Canada, the semi-submersible Sedco 135F. On the East Coast, too, Shell helped initiate offshore drilling rig construction in the 1970s, and used the first Halifax-built rig, the Sedco H, in offshore exploration.

1955

1961

1971

Oil recovery advances

In Western Canada, Shell pursued a policy of employing the most advanced technologies to extract greater amounts of oil from Canada's existing deposits.

In the Peace River area of Alberta, the company developed an in-situ steam-injection recovery technique for the deep oil sands accumulation discovered by Shell back in the 1950s. At Midale, Saskatchewan, Shell is pushing ahead with a plan to recover more oil from a field it discovered in the 1950s. There, a pilot project is evaluating the effectiveness of a miscible flood recovery scheme using carbon dioxide as the injected solvent. Shell is a leader in Canada in the application of carbon dioxide to enhanced recovery, although it is widely used in the United States.

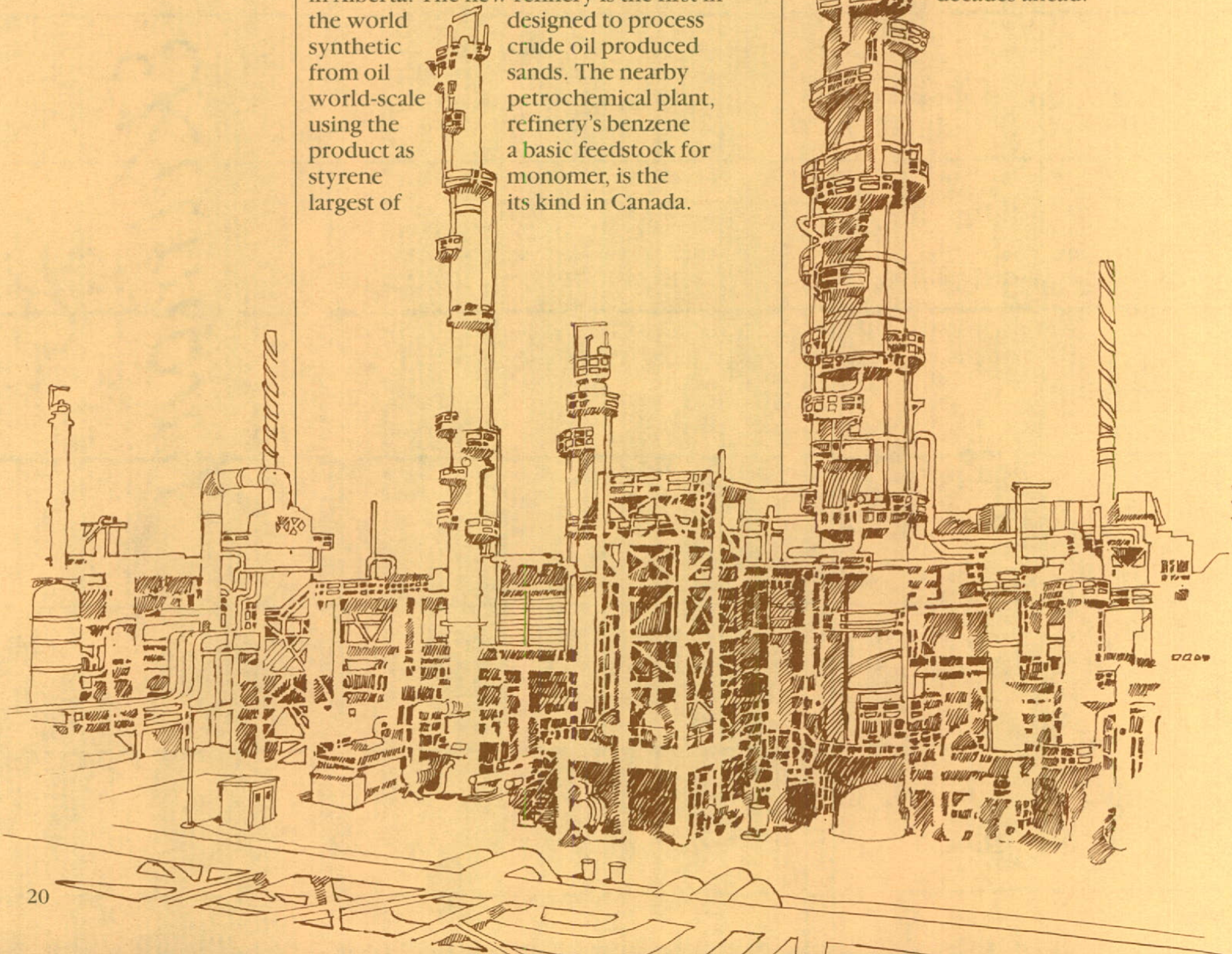
In refining and petrochemicals, Shell Canada, just prior to its 75th year in this country, realized one of its most imaginative and technologically advanced projects – the $1.4 billion Scotford complex in Alberta. The new refinery is the first in the world designed to process synthetic crude oil produced from oil sands. The nearby world-scale petrochemical plant, using the refinery's benzene product as a basic feedstock for styrene monomer, is the largest of its kind in Canada.

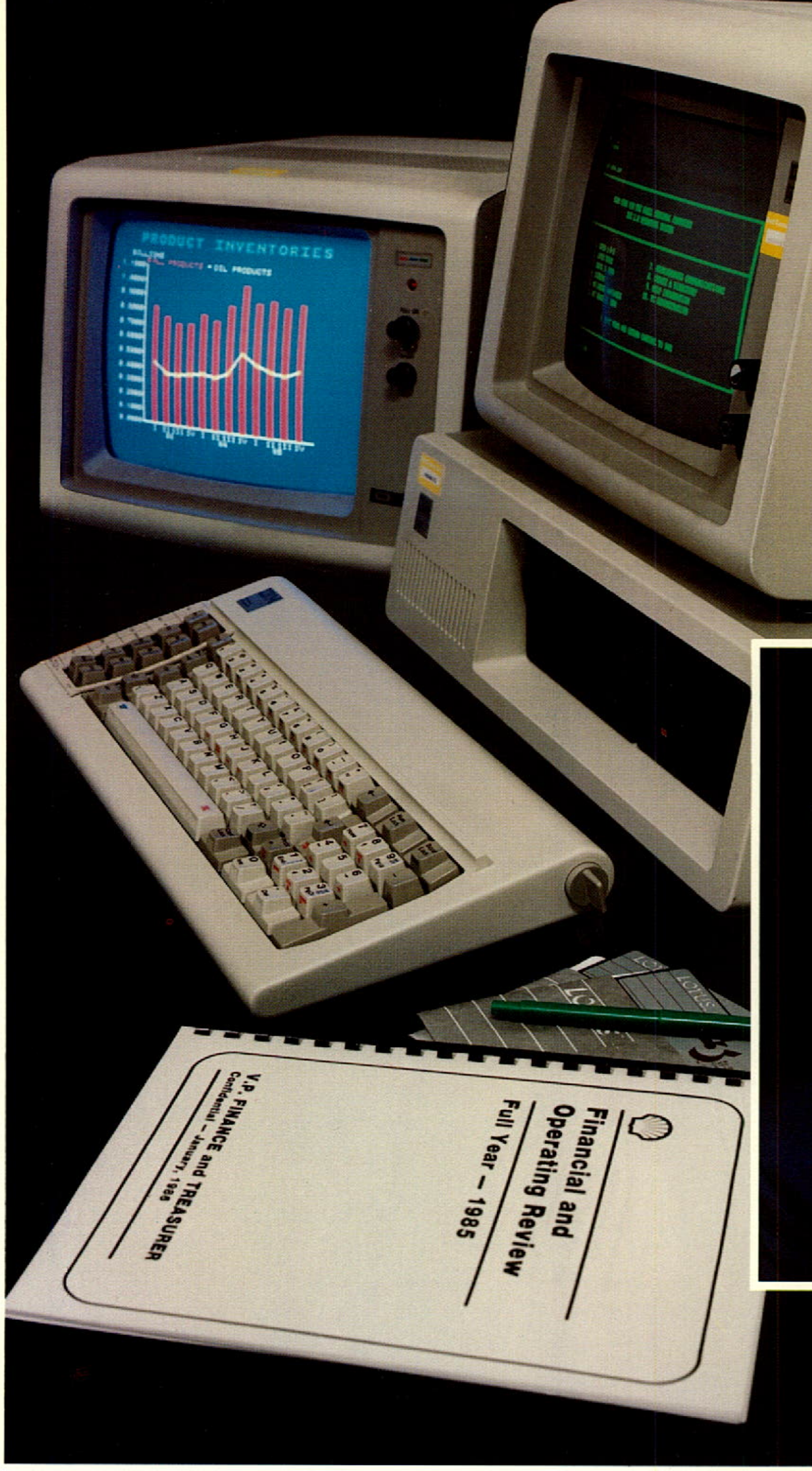
Technology and people

In retrospect, a distinctive feature of Shell Canada's participation in the petroleum industry has been its commitment to technology and innovative techniques as an essential element in enhancing its strategy of growth. Notable achievements have flowed from modern Shell research laboratories existing in Ontario and Alberta.

The Shell people who set the company on its growth course would undoubtedly feel that their efforts have been rewarded. Through the years to today's company of about 7,200 Canadians, it has been people, operating in a responsive and rewarding work environment, who have been the vital element to the many achievements.

The use of research and technology, the readiness to innovate, and committed Shell people . . . that is how the company grew with Canada and how it will continue to be a leading, major petroleum company in the decades ahead.





Financial Review

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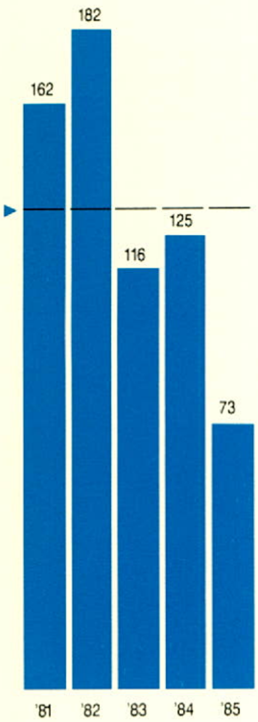
G.B. Darou
Vice President (Finance)
and Treasurer

Financial Performance and Outlook



Reinvestment ratio (%)

► Five-year average 132%

Earnings declined eight per cent from 1984. Significant improvements in Resources resulted from higher sulphur prices and higher natural gas sales volumes. These were offset by the impact of lower petroleum product margins in Oil Products and continuing depressed prices for styrene in Chemicals.

Consolidated earnings for 1985 were $146 million or $1.17 per Class "A" Common Share compared with $158 million or $1.27 in 1984 and $102 million or 83 cents in 1983. Earnings for 1984 after an extraordinary item were $123 million or 96 cents a share. The extraordinary item of $35 million after taxes represented a portion of the cost to restructure the organization, relocate corporate offices to Calgary and reduce staff.

Earnings from operations, excluding unusual items, were $156 million, essentially unchanged from the 1984 amount of $158 million. This reflected a significant upturn for Resources offset by a loss in the Chemicals segment and lower earnings in Oil Products.

Compared with 1983, the current year's performance was significantly better due to higher earnings in both the Resources and Oil Products segments.

Shell's return on average capital employed continued to be unacceptably low at 4.4 per cent, up only slightly from 4.2 per cent in 1984 (based on earnings after the extraordinary item) and 4.1 per cent in 1983. Poor performances from the Chemicals and Oil Products segments relative to their sizable investment levels continued to outweigh the modestly favourable returns in the Resources segment.

The Corporation maintained its dividend rate at the 60-cents-per-share level, consistent with 1984 and 1983.

Business segment earnings

Resources earnings increased to $192 million in 1985 from $164 million and $154 million in 1984 and 1983 respectively. The gain over 1984 resulted primarily from a significant contribution from sulphur and natural gas. World sulphur prices increased more than 60 per cent during the year while sales volumes were maintained. Gas sales increased significantly as a result of the federal government's market-related pricing policies implemented in late 1984 and in November, 1985, which stimulated export sales. These were partially offset by lower prices for natural gas volumes exported to the United States, and higher costs and write-offs. Crude oil prices also improved, but the benefits were offset by lower volumes produced due to declines in field production capabilities and pipeline transmission constraints. The Coal operation, despite adverse conditions in the industry worldwide, was able to increase its cash contribution in 1985 and, through highly-effective cost containment, ended the year in a breakeven earnings position.

Earnings for Oil Products were $54 million, down from $71 million in 1984 but considerably up from the 1983 amount of $23 million. Impairments in petroleum product margins and higher expenses in 1985 more than offset gains associated with higher sales volumes. Overall sales volumes rose four per cent while the light oils category increased eight per cent in the year. The margin impairments were caused by intense price competition in the marketplace coupled with higher costs, in part due to the start-up of the Scotford refinery. Depreciation and amortization for Scotford were higher, reflecting its first full year of operation.

Chemicals lost $11 million in 1985 compared with earnings of $9 million in 1984 and $8 million in 1983. Contributions in 1985 from both Industrial Chemicals and Polymers were more than offset by a loss in Styrene. The Styrene loss was attributable to depressed prices in international markets and operational difficulties related to the new Scotford plant. Depreciation and amortization increased for the year due to this new facility. The increase in Chemicals sales volumes of 24 per cent over the 1984 level reflected styrene sales for a full year in 1985 versus only part of 1984.

Within the Corporate segment, two unusual items reduced the overall earnings from operations of $156 million to the $146 million reported. Sale of the Corporation's investment in Interprovincial Pipe Line Limited shares gave rise to a gain of $10 million. Offsetting this gain, a downward adjustment of $20 million after taxes reflected the elimination of unrealized profit in inventories. This was necessitated by oil deregulation and changes in the operation of the Alberta Petroleum Marketing Commission which followed the signing of the Western Accord. Excluding the above two items, Corporate expenses and financing costs were lower in 1985.

Cash generation high

The Corporation continued to benefit from its strong cash generation capability in 1985. Internally generated cash of $635 million for the year was slightly lower than the 1984 amount of $659 million but higher than the 1983 amount of $603 million. Cash from operations comprised $600 million of the total internally generated cash compared with $619 million in 1984 and $539 million in 1983.

In May, 1985, the Corporation issued $75 million of 11.25 per cent debentures in international capital markets. The proceeds served to strengthen the cash position and reduce financing costs.

Resources expenditures emphasized

Consolidated capital and exploration expenditures remained high in 1985, amounting to $469 million compared with $479 million in 1984. But they were substantially down from the high level in 1983 of $746 million.

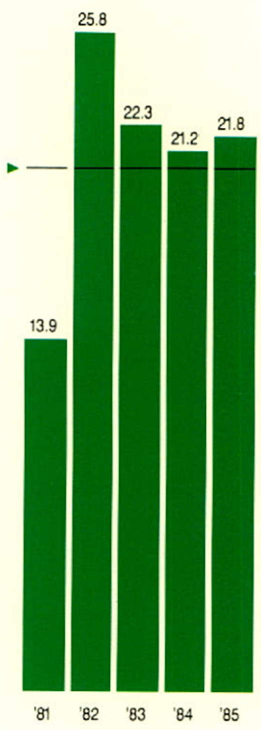
Capital and exploration expenditures for the Resources segment rose 50 per cent to $367 million in 1985 from $246 million in 1984 and $204 million in 1983. The increase primarily reflected expenditures for the first phase of the Peace River in-situ oil sands expansion and heightened activity for enhanced oil recovery in Western Canada.

Capital investment in Oil Products amounted to $40 million in 1985 compared with $144 million and $273 million in 1984 and 1983 respectively. Chemicals capital expenditures were $23 million, down from $74 million in 1984 and $260 million in 1983. The decline for both Oil Products and Chemicals resulted from the completion of construction of the Scotford refinery and chemical complex in 1984.

Capital and exploration expenditures in Resources represented a reinvestment of its funds from operations of 86 per cent, up from 64 per cent in 1984. The Corporation's total investment of cash for the year was $435 million, compared with $773 million in 1984 and $624 million in 1983, and represented a reinvestment of 73 per cent of funds from operations, down from the abnormally high levels of 125 per cent in 1984 and 116 per cent in 1983 when the Scotford complex was under construction.

Outlook for 1986

While Shell's long-term prospects are quite favourable, the outlook for 1986 has a wide range of uncertainty. Changes in attitudes of governments toward a less regulated business environment and positive steps made to provide tax and royalty relief to the energy industry signal longer-term opportunity for growth. However, in the more immediate future, concerns over crude oil price volatility counter the optimism generated by initial phase-in of the tax relief benefits. Fluctuations in foreign currency exchange rates, primarily the U.S. dollar, cause far less



Long-term debt as a percentage of total capital employed

► Five-year average 21%

concern since the Corporation's U.S. dollar inflows and outflows are effectively balanced and no significant benefit or cost is experienced from rate changes.

For the coming year, Shell intends to continue its efforts to capture new markets for natural gas exports under the more deregulated environment. Work will continue to increase the Corporation's crude oil capability in anticipation of better long-term market conditions. In the manufacturing and marketing areas, activity will be centred around maximizing refinery utilization and focusing sales strategies to improve product margins.

Capital and exploration expenditures anticipated for 1986, at approximately $675 million, are more than 40 per cent higher than for 1985. The program maintains the emphasis placed on Resources activity and includes significant expenditures for the expansion of the Peace River in-situ project, for ongoing evaluation of frontier lands, investment in conventional oil and gas exploration and for enhanced oil recovery schemes in Western Canada. This Resources program represents more than 75 per cent of the Corporation's total expanded capital budget and is $150 million higher than 1985. Oil Products' portion of the capital program includes sizable expenditures for the installation of a residue catalytic cracker at the Montreal East refinery and on customer-focused, retail network improvements. However, as indicated previously, a high degree of uncertainty exists with respect to the stability of world crude prices for the industry and the 1986 capital programs may require modification if cash flows decline significantly. Shell has incorporated a great deal of flexibility in its 1986 investment plans and is able to respond effectively to changing conditions.

Quarterly financial and stock-trading information

	1985					1984				
	Quarter				**Total**	Quarter				Total
	1st	**2nd**	**3rd**	**4th**	**Year**	1st	2nd	3rd	4th	Year
Sales and other operating revenues ($ millions)	**1 560**	**1 590**	**1 388**	**1 532**	**6 070**	1 398	1 383	1 404	1 549	5 734
Earnings before income taxes ($ millions)	**171**	**80**	**27**	**104**	**382**	131	113	108	100	452
Earnings (loss) before extraordinary item ($ millions)	**73**	**21**	**(6)**	**58**	**146**	51	35	33	39	158
Earnings (loss) after extraordinary item ($ millions)	**73**	**21**	**(6)**	**58**	**146**	51	—	33	39	123
Earnings (loss) per share before extraordinary item (dollars)	**0.62**	**0.15**	**(0.09)**	**0.49**	**1.17**	0.42	0.28	0.25	0.32	1.27
Earnings (loss) per share after extraordinary item (dollars)	**0.62**	**0.15**	**(0.09)**	**0.49**	**1.17**	0.42	(0.03)	0.25	0.32	0.96
Cash dividends (dollars)										
Per Class "A" Common Share	**—**	**0.30**	**—**	**0.30**	**0.60**	—	0.30	—	0.30	0.60
Per Class "B" Common Share	**—**	**1.20**	**—**	**1.20**	**2.40**	—	1.20	—	1.20	2.40
Share prices* (dollars)										
High	**28½**	**29⅞**	**28**	**24¾**	**29⅞**	27	26⅝	26½	26¼	27
Low	**21¼**	**25⅜**	**22⅜**	**22⅜**	**21¼**	23⅝	23⅜	19½	21⅛	19½
Close (end of period)	**28**	**27¼**	**24⅜**	**23**	**23**	26½	23⅞	26⅛	22¼	22¼
Shares traded** (thousands)	**3 639**	**4 716**	**2 646**	**3 627**	**14 628**	3 525	2 151	2 533	2 127	10 336

*Toronto Stock Exchange quotations

**Volume traded on the Montreal, Toronto, Alberta and Vancouver stock exchanges

Shell Canada Limited

Accounting policies

Shell Canada's consolidated financial statements are prepared in accordance with generally accepted accounting principles in Canada. The Corporation's major accounting policies are summarized as follows:

Audited financial information

Principles of consolidation

The accounts of Shell Canada Limited and its subsidiary companies are included in the consolidated financial statements. Interests in oil and gas joint ventures are accounted for using the proportionate consolidation method.

Investments

Investments in companies in which Shell Canada exercises significant influence are accounted for using the equity method. Other long-term investments are recorded at cost with provision made where a permanent decline in the value of such investments has occurred.

Inventories

Inventories of crude oil, products and merchandise are stated at the lower of cost, applied on a "first-in, first-out" basis, and net realizable value. Materials and supplies are stated at the lower of cost and estimated useful value.

Exploration and development costs

The Corporation follows the successful efforts method of accounting for exploration and development activities. Under this method, acquisition costs of resource properties are capitalized. Exploratory drilling costs are initially capitalized and wells subsequently determined to be unsuccessful are charged to earnings. Other exploration and predevelopment costs, including geological and geophysical costs, are charged to earnings currently. All development costs are capitalized.

Depreciation and amortization

Depreciation and amortization on resource assets are provided on the unit of production basis. Costs of producing properties are depleted and gas plants depreciated over remaining proved reserves. The costs of non-producing properties are amortized in accordance with experience. Resource development expenditures are amortized over remaining proved developed reserves. Other plant and equipment are depreciated on a straight-line basis over their estimated useful lives.

Deferred gas production revenue

Amounts received under take-or-pay contracts for future delivery of natural gas are recorded as deferred gas production revenue. The amounts are included in sales revenue when the related gas is delivered.

Retirement programs

The Corporation has retirement programs which cover virtually all employees. The annual cost of the programs includes current service costs, actuarial valuation adjustments and amortization of prior service costs over varying periods which approximate the remaining service lives of employees. These costs are charged to earnings and funded in accordance with actuarial recommendations.

Royalties and mineral taxes

Alberta royalties on crude oil obtained from its Crown leases are required to be delivered in kind, and accordingly are not reflected in these financial statements. All other royalty entitlements, which are not delivered in kind, and mineral taxes are reflected in the cost of purchased crude oil, petroleum products and other merchandise.

Government incentives and investment tax credits

Petroleum Incentive Program grants, investment tax credits and other government incentives, other than tax rate reductions, are accounted for as deductions from the related qualifying expenditures. Such government assistance is reflected in earnings immediately if the related qualifying expenditures are expensed, or through future depreciation and amortization provisions if the related qualifying expenditures are capitalized.

Interest

Interest costs are expensed as incurred.

Foreign currency translation

Long-term monetary liabilities are translated to Canadian dollars at rates of exchange in effect at the end of the period. Unrealized exchange gains and losses arising on translation are deferred and amortized over the remaining terms of these liabilities.

Shell Canada Limited

Consolidated statement of earnings

($ millions, except per share amounts)

	Year ended December 31	**1985**	1984	1983
Revenues	Sales and other operating revenues	**6 070**	5 734	5 300
	Dividends, interest and other income	**32**	28	36
		6 102	5 762	5 336
Expenses	Purchased crude oil, petroleum products and other merchandise	**3 686**	3 552	3 409
	Operating expenses	**856**	741	660
	Selling and general expenses	**577**	500	467
	Exploration and predevelopment expenses	**121**	99	88
	Depreciation, amortization and retirements	**229**	169	140
	Interest on long-term debt	**128**	131	133
	Petroleum and gas revenue taxes	**123**	118	114
	Income taxes (Note 14)	**236**	294	223
		5 956	5 604	5 234
Earnings	Earnings before extraordinary item	**146**	158	102
	Extraordinary item, after income taxes (Note 2)	**—**	35	—
	Earnings for the year	**146**	123	102
	Earnings per Class "A" Common Share (dollars)			
	Before extraordinary item	**1.17**	1.27	0.83
	After extraordinary item	**1.17**	0.96	0.83

Consolidated statement of earnings retained in the business

($ millions)

	Year ended December 31	**1985**	1984	1983
Earnings retained	Balance at beginning of year	**1 427**	1 387	1 366
	Earnings for the year	**146**	123	102
		1 573	1 510	1 468
	Dividends paid (Note 12)	**83**	83	81
	Balance at end of year	**1 490**	1 427	1 387

The accompanying notes are an integral part of these statements.

Shell Canada Limited

Consolidated statement of changes in financial position

($ millions)

	Year ended December 31	1985	1984	1983
Cash internally generated	Cash from operations (Note 4)	**600**	619	539
	Sales of properties, plant and equipment and miscellaneous items	**58**	15	22
	Deferred gas production revenue	**(23)**	25	42
		635	659	603
Cash invested	Capital and exploration expenditures	**469**	479	746
	Investments, long-term receivables and other **	**(88)**	150	10
	Working capital excluding cash (Note 5)	**54**	144	(132)
		435	773	624
Dividends paid	Preferred shares	**16**	16	17
	Common shares	**67**	67	64
		518	856	705
	Cash surplus (deficiency) before external financing	**117**	(197)	(102)
External financing	Capital stock	**—**	2	291
	Long-term debt	**58**	(13)	(19)
		58	(11)	272
Net change	Increase (decrease) in cash*	**175**	(208)	170
	Cash at December 31	**202**	27	235

*Cash comprises cash and short-term investments less short-term borrowings.

**Includes $35 million in 1984, reflecting extraordinary item expense adjusted for non-cash amounts.

The accompanying notes are an integral part of these statements.

Shell Canada Limited

Consolidated statement of financial position

($ millions)

	At December 31	1985	1984
Assets	Current assets		
	Cash	**59**	107
	Short-term investments, at cost which approximates market	**143**	—
	Accounts receivable	**854**	808
	Inventories		
	Crude oil, products and merchandise	**927**	1 018
	Materials and supplies	**53**	45
	Prepaid expenses	**28**	19
		2 064	1 997
	Investments, long-term receivables and other	**173**	296
	Properties, plant and equipment (Note 6)	**3 562**	3 483
		5 799	5 776
Liabilities	Current liabilities		
	Short-term borrowings	**—**	80
	Accounts payable and accrued liabilities	**844**	762
	Income and other taxes payable	**35**	203
	Long-term debt due within one year	**18**	14
		897	1 059
	Long-term debt (Note 7)	**1 070**	998
	Deferred gas production revenue	**241**	264
	Deferred income taxes	**1 049**	976
Shareholders' investment	Shareholders' investment		
	Capital stock (Note 12)	**761**	761
	Contributed surplus	**291**	291
	Earnings retained in the business	**1 490**	1 427
	Total shareholders' investment	**2 542**	2 479
	Contingencies (Notes 9 and 10)		
		5 799	5 776

The accompanying notes are an integral part of these statements.

The consolidated financial statements have been approved by the Board.

J.M. MacLeod, Director

Peter J.G. Bentley, Director

Notes to consolidated financial statements

1. Accounting policies

A summary of major accounting policies of Shell Canada is presented on page 25.

2. Extraordinary item

The extraordinary item in 1984 represented the costs of $70 million less income taxes of $35 million associated with restructuring the Corporation's organization, relocating corporate headquarters to Calgary and reducing staff, including severance pay, relocation costs, the present value of additional pensions to those not otherwise entitled to early retirement and the gain on disposal of the Head Office building in Toronto. Additional pension benefits, having an initial present value of $55 million less related income taxes of $24 million, payable under the enhanced voluntary retirement program to those entitled to retire early, are being provided out of earnings and funded over a period not exceeding 15 years.

3. Other statement of earnings information

The following amounts were included in the determination of earnings:

($ millions)	**1985**	1984	1983
Sales revenues attributable to exports	**1 244**	870	695
Maintenance and repair expenses	**168**	130	127
Short-term interest expenses	**2**	2	7
Research and development expenses	**34**	28	29

4. Cash internally generated from operations

($ millions)	**1985**	1984	1983
Earnings before extraordinary item	**146**	158	102
Exploration and predevelopment expenses	**121**	99	88
Expenses not requiring any outlay of cash			
Depreciation, amortization and retirements	**229**	169	140
Deferred income taxes	**73**	175	209
Other items	**31**	18	—
Cash from operations	**600**	619	539

5. Analysis of working capital changes excluding cash

Details of net changes in each element of working capital excluding cash are as follows:

($ millions)	**1985**	1984	1983
Increase (decrease) in accounts receivable	**46**	75	67
Increase (decrease) in inventories	**(83)**	299	(134)
Increase (decrease) in prepaid expenses	**9**	4	(31)
(Increase) decrease in accounts payable and accrued liabilities	**(82)**	(121)	19
(Increase) decrease in income and other taxes payable	**168**	(116)	(43)
(Increase) decrease in long-term debt due within one year	**(4)**	3	(10)
Net change in working capital excluding cash	**54**	144	(132)

6. *Segmented information*

Shell Canada operates principally in three industry segments: Resources, Oil Products and Chemicals.

Resources comprises exploration and production activities for crude oil, bitumen, natural gas, gas liquids, sulphur, synthetic oils and coal.
Oil Products and *Chemicals* include the manufacture, distribution and marketing of refined products and chemical products respectively.
Other includes cash, short-term securities, pipeline investments, miscellaneous corporate ventures, long-term debt, general corporate facilities, unallocated corporate revenues and expenses, and interest on long-term debt.

Segmented financial results and property, plant and equipment data are reported as if the segments were separate entities. Inter-segment sales of products, which are accounted for at estimated market-related values, are included in revenues of the segment making the transfer. However, such inter-segment sales and the associated estimated profits are eliminated from total revenues and operating profit respectively on consolidation.

Financial results

($ millions)
Sales and other revenues
Inter-segment sales
Total revenues
Operating profit (loss)
Depreciation, amortization and retirements
Interest on long-term debt
Petroleum and gas revenue taxes
Income taxes
Earnings before extraordinary item
Extraordinary item, after income taxes
Earnings for the year
Total assets
Capital employed*

*Capital employed is total assets less current liabilities.

Properties, plant and equipment

($ millions)
Cost
Accumulated depreciation*
Net book value
Capital expenditures
Cost
Accumulated depreciation*
Net book value
Capital expenditures
Total segment
Cost
Accumulated depreciation*
Net book value
Capital expenditures

*Principal depreciation and amortization rates:
Resources segment—unit of production
Other segments—straight-line 4% to 13%

	Resources			Oil Products			Chemicals			Other			Total		
	1985	1984	1983	**1985**	1984	1983	**1985**	1984	1983	**1985**	1984	1983	**1985**	1984	1983
	1 249	1 345	1 250	**4 307**	3 975	3 728	**527**	414	321	**19**	28	37	**6 102**	5 762	5 336
	205	—	—	**197**	152	141	**—**	—	—	**—**	—	—	**—**	—	—
	1 454	1 345	1 250	**4 504**	4 127	3 869	**527**	414	321	**19**	28	37	**6 102**	5 762	5 336
	753	701	631	**128**	134	57	**20**	34	26	**(39)**	1	(2)	**862**	870	712
	118	105	85	**61**	37	30	**44**	18	12	**6**	9	13	**229**	169	140
	—	—	—	**—**	—	—	**—**	—	—	**128**	131	133	**128**	131	133
	123	118	114	**—**	—	—	**—**	—	—	**—**	—	—	**123**	118	114
	320	314	278	**13**	26	4	**(13)**	7	6	**(84)**	(53)	(65)	**236**	294	223
	192	164	154	**54**	71	23	**(11)**	9	8	**(89)**	(86)	(83)	**146**	158	102
	—	—	—	**—**	—	—	**—**	—	—	**—**	(35)	—	**—**	(35)	—
	192	164	154	**54**	71	23	**(11)**	9	8	**(89)**	(121)	(83)	**146**	123	102
	1 906	1 781	1 729	**2 612**	2 703	2 235	**966**	1 006	869	**315**	286	407	**5 799**	5 776	5 240
	1 745	1 617	1 599	**2 029**	2 095	1 673	**943**	977	838	**185**	28	385	**4 902**	4 717	4 495

	Resources			Oil Products			Chemicals			Other			Total		
	1985	1984	1983	**1985**	1984	1983	**1985**	1984	1983	**1985**	1984	1983	**1985**	1984	1983
	Conventional oil and gas			Refining											
	1 862	1 707	1 605	**1 201**	1 184	1 092									
	626	551	496	**345**	292	320									
	1 236	1 156	1 109	**856**	892	772									
	308	236	174	**4**	120	234									
	Non-conventional oil and gas, and coal			Marketing and transportation											
	441	384	375	**454**	450	453									
	56	39	22	**223**	215	196									
	385	345	353	**231**	235	257									
	59	10	30	**36**	24	39									
	2 303	2 091	1 980	**1 655**	1 634	1 545	**901**	873	800	**116**	94	91	**4 975**	4 692	4 416
	682	590	518	**568**	507	516	**124**	81	62	**39**	31	31	**1 413**	1 209	1 127
	1 621	1 501	1 462	**1 087**	1 127	1 029	**777**	792	738	**77**	63	60	**3 562**	3 483	3 289
	367	246	204	**40**	144	273	**23**	74	260	**39**	15	9	**469**	479	746

7. *Long-term debt*

($ millions)	Maturity	**1985**	1984	1983
Debentures				
15¾% (1985 – U.S. $96; 1984 – U.S. $96; 1983 – U.S. $100)	1991	**134**	127	124
14⅜% (1985 – U.S. $125; 1984 – U.S. $125; 1983 – U.S. $125)	1992	**175**	165	156
11¾%	1988	**100**	100	100
11¼%*	1992	**75**	—	—
Sinking fund debentures				
Series 1 – 7½% (1985 – U.S. $49; 1984 – U.S. $52; 1983 – U.S. $56)	1994	**68**	69	70
Series 2 – 9¼% (1985 – U.S. $64; 1984 – U.S. $69; 1983 – U.S. $75)	1996	**89**	91	93
14⅛% (1985 – U.S. $200; 1984 – U.S. $200; 1983 – U.S. $200)	1997	**280**	264	249
9⅜%	2003	**119**	119	120
Promissory notes				
Floating rate**	1992	**100**	100	100
Other long-term obligations	Varying dates	**33**	34	30
		1 173	1 069	1 042
Included in current liabilities as due within one year		**18**	14	17
Unamortized balance of exchange gains and losses		**85**	57	23
Total		**1 070**	998	1 002

*Interest is payable on a floating rate basis under an interest rate swap arrangement.

**Interest is payable monthly at three-quarters of one per cent below prime rates prevailing at Canadian chartered banks to August, 1986, subject thereafter to annual renegotiation. In the event that agreements cannot be reached with respect to a new interest rate, the principal amount may be repaid in full without penalty.

Of the $1 173 million long-term debt, the aggregate amount of payments required to meet sinking fund or retirement provisions will be:

- $ 18 million in 1986
- $ 15 million in 1987
- $116 million in 1988
- $ 16 million in 1989
- $ 30 million in 1990.

The principal amounts of the U.S. debentures included above are expressed in terms of Canadian dollars, translated at the rates of exchange prevailing on December 31, 1985, 1984 and 1983 respectively. Unrealized gains and losses arising on translation of long-term debt are deferred and amortized over the remaining term of the debt.

8. Pension costs

The Corporation's pension costs in 1985 were $26 million (1984 – $23 million; 1983 – $7 million). The pension costs in 1984 included $7 million which was provided as part of the extraordinary item. Due to favourable actuarial experience, the pension plan charge was reduced in 1985 by $9 million (1984 – $10 million; 1983 – $21 million).

The most recent actuarial valuation was prepared as at December 31, 1985. A comparison of the accumulated pension benefits and pension net assets using an actuarial rate of return of eight per cent follows:

December 31 ($ millions)	**1985**	1984	1983
Actuarial present value of accumulated pension benefits			
Vested	**518**	486	343
Non-vested	**22**	12	29
Total	**540**	498	372
Market value of pension net assets	**603**	501	417

The Corporation has an unrecorded liability, the present value of which is $48 million, reflecting additional pension benefits which arose from early retirements taken during 1984 under an enhanced voluntary retirement program. These additional benefits represented prior service pension costs and are being expensed and funded over a period not to exceed 15 years from that date.

9. Commitments and contingencies

At December 31, 1985, the Corporation had non-cancelable operating leases with an initial or remaining term of one year or more, covering service stations, offshore drilling equipment, office space and other facilities. Future minimum payments (without reduction for related rental income) under such leases are estimated to be:

$ 36 million in 1986
$ 31 million in 1987
$ 27 million in 1988
$ 23 million in 1989
$ 21 million in 1990
$120 million thereafter.

The Corporation has agreed to guarantee indebtedness, totalling $36 million, incurred by major petroleum product customers.

To assure a long-term supply of ethylene, the Corporation entered into a take-or-pay contract which started in 1984 for a duration of 20 years to purchase 107 000 tonnes per annum representing 16 per cent of the output of an ethylene plant. The price of the product is to be determined on a cost of service basis which includes fixed and variable operating expenses, debt service and a specified return on capital to the owner of the plant. In certain circumstances, a portion of the commitment under the take-or-pay contract, not exceeding $69 million, could be accelerated; such payment would have the effect of eliminating the debt service component of the take-or-pay contract.

10. Legal proceedings

Shell Canada Resources Limited was one of nine companies which, along with the Government of Alberta, were named as defendants in an action commenced by the Lubicon Lake Indian Band for a declaration for proprietary rights in certain lands and natural resources in northern Alberta, and for $900 million for damages and past royalties and revenues. Counsel has advised that the extent of the corporate defendants' liability cannot currently be determined but has expressed the opinion that it is unlikely the plaintiffs will succeed in establishing their claim to the natural resources or in their claim for damages.

11. Transactions with affiliated companies

Shell Canada, in the course of its regular business, has routine transactions at commercial rates with affiliates of the Royal Dutch/Shell Group of Companies. Such transactions are not material in relation to the Corporation's overall activities.

12. Capital stock

($ millions)	1985 Issued	1985 Dividends	1984 Issued	1984 Dividends	1983 Issued	1983 Dividends
10 000 000 Series "A" Preferred Shares	**250**	**16**	250	16	250	17
100 4% Preference Shares	**1**	**—**	1	—	1	—
75 215 511 Class "A" Common Shares (1984 – 75 201 911; 1983 – 75 116 386)	**481**	**45**	481	45	479	42
9 087 039 Class "B" Common Shares	**29**	**22**	29	22	29	22
Total	**761**	**83**	761	83	759	81

Shell Canada Limited carries on business under the Canada Business Corporations Act. All classes of shares are without nominal or par value and are authorized in unlimited number.

Series "A" Preferred Shares
The holders of Series "A" Preferred Shares are entitled to receive cumulative preferential dividends fixed at a rate of one-half of the Canadian bank prime rate plus five-eighths of one per cent. These shares are retractable at the holder's option on February 15, 1989 at the price of $25 per share plus accrued dividends. The shares are redeemable at the option of Shell Canada Limited on not less than 60 days notice, at a price equal to $25 per share plus accrued dividends to the redemption date.

4% Preference Shares
The holder of the Preference Shares receives fixed, cumulative dividends of $40 000 per annum. The Preference Shares may be redeemed at the amount paid up thereon plus accrued dividends.

Common Shares
The holder of the Class "B" Common Shares is entitled on a share-for-share basis to four times any amount paid or distributed by way of dividends or other distribution to the holders of Class "A" Common Shares.

13. *Taxes and royalties*

The following amounts were charged to earnings:

($ millions)	**1985**	1984	1983
Items reported separately:			
Income taxes (excludes tax reduction of $35 million for 1984 extraordinary item)	**236**	294	223
Petroleum and gas revenue taxes	**123**	118	114
Items included in purchased crude oil, petroleum products and other merchandise:			
Crown royalties and mineral taxes	**255**	227	230
Royalties paid to private leaseholders	**49**	49	48
Petroleum compensation charges	**364**	286	317
Oil import compensation received	**(94)**	(116)	(101)
Canadian ownership charges	**55**	89	88
Federal sales taxes	**267**	220	204
Other taxes	**57**	48	47
Total	**1 312**	1 215	1 170
Items not included in revenues and expenses:			
Retail sales taxes collected for governments	**669**	580	608
Royalties paid in kind to the Alberta government	**151**	165	131

14. *Income taxes*

The income tax provision, $236 million in 1985, included in the determination of earnings is developed by applying Canadian federal and provincial statutory tax rates to pre-tax earnings, with adjustments as set out in the following table:

(% of pre-tax earnings)	**1985**	1984	1983
Statutory rate (weighted average)	**48.8**	48.1	48.5
Increases (decreases) resulting from:			
Non-deductibility of crown royalties and other payments to provinces	**43.5**	39.7	52.8
Non-deductibility of petroleum and gas revenue taxes	**15.7**	12.6	16.9
Resource allowance and other abatement measures to partially offset non-deductibility of crown royalties	**(35.3)**	(31.3)	(40.9)
Depletion earned by exploration and development expenditures	**(2.4)**	(0.7)	(6.1)
Inventory allowance	**(3.9)**	(2.3)	(3.9)
Adjustments arising from re-assessments	**(1.7)**	0.5	0.9
Other	**(2.9)**	(1.5)	0.5
Effective income tax rate reflected in the statement of earnings	**61.8**	65.1	68.7

Deferred taxes included in the income tax provision related to:

($ millions)			
Depreciation and amortization	**50**	157	199
Intangible drilling costs	**11**	7	12
Other	**12**	11	(2)
Total (excludes deferred tax reduction of $17 million for 1984 extraordinary item)	**73**	175	209

15. United States accounting principles and reporting practices

The financial statements have been prepared in accordance with accounting principles generally accepted in Canada. They differ in some respects from those generally accepted in the United States and include the following items (any other adjustments would not be material):

Foreign currency translation

Long-term debt denominated in foreign currencies was translated at the rates of exchange in effect at the end of the period. Unrealized exchange gains and losses arising on translation were deferred and amortized over the remaining terms of the debt. Generally accepted accounting principles in the United States when applied in the case of the Corporation would have required that such gains or losses be reflected in income in the period in which they arose.

Capitalization of interest

Interest costs were expensed as incurred. United States accounting principles would have required capitalization and subsequent amortization of certain interest costs incurred on capital outlays.

Pension contribution

Actuarial gains and losses were charged to earnings in the year in which they occurred. Under United States accounting principles, such gains and losses would have been spread over current and future periods.

Extraordinary item

An extraordinary provision of $35 million was charged against 1984 earnings to cover certain costs to restructure the Corporation's organization, relocate the corporate headquarters to Calgary and reduce staff. Additional pension costs net of income taxes under the enhanced retirement program, the present value of which is $28 million, are being charged against earnings in future years (1985 – $3 million). Under United States accounting principles, the extraordinary item together with the additional pension costs, totalling $66 million after income taxes, would have been included as an unusual item in earnings before extraordinary item in the 1984 consolidated statement of earnings and would not have been shown net of applicable income taxes.

If the Corporation's financial statements had been presented on the basis of United States accounting principles (including all material adjustments), earnings and earnings per share would have been:

December 31 ($ millions)	**1985**	1984	1983
Earnings before extraordinary item as reported	**146**	158	102
Adjustments, net of applicable income taxes:			
Foreign currency translation	**(22)**	(26)	(4)
Capitalization (amortization) of interest	**(7)**	49	68
Pension contribution	**(2)**	(5)	(11)
Unusual item	**3**	(66)	—
Earnings before extraordinary item as adjusted	**118**	110	155
Extraordinary item as adjusted	**—**	—	—
Earnings as adjusted	**118**	110	155
Earnings attributable to preferred shares	**(16)**	(16)	(17)
Earnings attributable to Class "A" Common Shares as adjusted	**102**	94	138
Earnings per Class "A" Common Share as adjusted (dollars)	**0.91**	0.85	1.35

Auditors' report

To the Shareholders of Shell Canada Limited:

We have examined the consolidated statements of financial position of Shell Canada Limited as at December 31, 1985 and 1984 and the consolidated statements of earnings, earnings retained in the business and changes in financial position for each of the three years in the period ended December 31, 1985. 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 Corporation as at December 31, 1985 and 1984 and the results of its operations and the changes in its financial position for each of the three years in the period ended December 31, 1985 in accordance with generally accepted accounting principles consistently applied.

Price Waterhouse

Price Waterhouse
Calgary, Alberta
February 14, 1986

Shell Canada Limited

Five-year financial data

Statement of earnings ($ millions)

		1985	1984	1983	1982	1981
Revenues	Petroleum products	**4 155**	3 820	3 594	3 531	3 336
	Natural gas	**593**	559	575	616	549
	Crude oil and natural gas liquids	**443**	646	569	465	338
	Chemicals	**527**	414	321	328	325
	Other operating revenues	**352**	295	241	209	203
	Sales and other operating revenues	**6 070**	5 734	5 300	5 149	4 751
	Dividends, interest and other income	**32**	28	36	40	51
		6 102	5 762	5 336	5 189	4 802
Expenses	Purchased crude oil, petroleum products and other merchandise	**3 686**	3 552	3 409	3 249	2 851
	Operating expenses	**856**	741	660	638	580
	Selling and general expenses	**577**	500	467	525	466
	Exploration and predevelopment expenses	**121**	99	88	157	193
	Depreciation, amortization and retirements	**229**	169	140	119	118
	Interest on long-term debt	**128**	131	133	76	34
	Petroleum and gas revenue taxes	**123**	118	114	125	69
	Income taxes – current	**163**	119	14	(47)	164
	– deferred	**73**	175	209	199	90
		5 956	5 604	5 234	5 041	4 565
Earnings	Earnings before unusual item	**146**	158	102	148	237
	Unusual item, after income taxes	**—**	—	—	17	—
	Earnings before extraordinary item	**146**	158	102	131	237
	Extraordinary item, after income taxes	**—**	35	—	—	—
	Earnings for the year	**146**	123	102	131	237

Statement of changes in financial position ($ millions)

		1985	1984	1983	1982	1981
Cash internally generated	Cash from operations	**600**	619	539	639	642
	Sales of properties, plant and equipment and miscellaneous items	**58**	15	22	35	2
	Deferred gas production revenue	**(23)**	25	42	99	23
		635	659	603	773	667
Cash invested	Capital and exploration expenditures	**469**	479	746	1 014	707
	Investments, long-term receivables and other	**(88)**	150	10	77	32
	Working capital excluding cash	**54**	144	(132)	71	302
		435	773	624	1 162	1 041
Dividends paid	Preferred shares	**16**	16	17	24	23
	Common shares	**67**	67	64	90	90
		518	856	705	1 276	1 154
	Cash surplus (deficiency) before external financing	**117**	(197)	(102)	(503)	(487)
External financing	Capital stock	**—**	2	291	—	—
	Long-term debt	**58**	(13)	(19)	593	114
		58	(11)	272	593	114
Net change	Increase (decrease) in cash	**175**	(208)	170	90	(373)
	Cash at December 31	**202**	27	235	65	(25)

Five-year financial data
(continued)

Financial position at year end ($ millions)		1985	1984	1983	1982	1981
Working capital	Cash and short-term investments	**202**	107	235	65	38
	Short-term borrowings	**—**	(80)	—	—	(63)
	Other working capital	**965**	911	767	899	828
	Total working capital	**1 167**	938	1 002	964	803
Capital employed	Investments, long-term receivables and other	**173**	296	204	180	134
	Properties, plant and equipment – net	**3 562**	3 483	3 289	2 805	2 117
	Total capital employed	**4 902**	4 717	4 495	3 949	3 054
	Less: Long-term debt	**1 070**	998	1 002	1 019	424
	Deferred gas production revenue	**241**	264	239	197	98
	Deferred income taxes	**1 049**	976	817	608	424
	Series "A" Preferred Shares	**250**	250	250	250	250
	4% Preference Shares	**1**	1	1	1	1
	Common shareholders' investment at book value	**2 291**	2 228	2 186	1 874	1 857
	Total assets	**5 799**	5 776	5 240	4 660	3 778
	Performance indicators (dollars)					
*Data per common share**	Earnings – before extraordinary item	**1.17**	1.27	0.83	1.07	2.12
	– after extraordinary item	**1.17**	0.96	0.83	1.07	2.12
	Dividends paid	**0.60**	0.60	0.60	0.90	0.90
	Cash from operations (before exploration and predevelopment expenses)	**5.23**	5.40	5.11	6.12	6.18
	Shareholders' investment	**20.53**	19.97	19.61	18.68	18.52
	Common shares outstanding at year end (millions)	**112**	112	111	100	100
	Shareholders (number at year end)	**12 594**	13 836	13 773	15 734	17 563
Ratios	Return on average capital employed (%)(1)	**4.4**	4.2	4.1	4.9	8.8
	Earnings attributable to common shares as % of average common shareholders' equity (2)	**5.8**	4.8	4.2	5.8	11.8
	as % of revenues (3)	**2.1**	1.9	1.6	2.1	4.4
	Common share dividends as % of earnings attributable to common shares (4)	**51.4**	62.6	74.6	83.7	42.4
	Current assets to current liabilities (5)	**2.3**	1.9	2.3	2.4	2.1
	Long-term debt as % of total capital employed (6)	**21.8**	21.2	22.3	25.8	13.9
	Interest coverage (7)	**4.0**	3.9	3.5	4.5	15.2
	Reinvestment ratio (%)(8)	**73**	125	116	182	162
Employee data	Salaries, wages and employee benefits ($ millions)	**371**	393	376	394	332
	Employees (number at year end)	**7 142**	7 136	7 975	8 611	8 822
	Capital employed per employee ($ thousands)	**686**	661	564	459	346

*Class "A" Common Share equivalent is calculated on the basis that the holder of a Class "B" Common Share is entitled, on a share-for-share basis, to four times any amount paid or distributed to a holder of a Class "A" Common Share. Cash from operations and earnings per common share have been calculated using monthly weighted average Class "A" equivalents.

Definitions of ratios

(1) Earnings plus after-tax interest expense on long-term debt divided by average capital employed. Capital employed is total assets less current liabilities.

(2) Earnings less dividends paid on preferred shares divided by average common shareholders' equity. Common shareholders' equity is total shareholders' investment less preferred share capital.

(3) Earnings less dividends paid on preferred shares divided by total revenues.

(4) Common share dividends paid divided by earnings less dividends paid on preferred shares.

(5) Total current assets divided by total current liabilities.

(6) Long-term debt divided by total capital employed.

(7) Pre-tax earnings plus interest on long-term debt divided by interest on long-term debt.

(8) Total cash invested divided by cash from operations.

Shell Canada Limited

Supplemental oil products and chemicals disclosure
(unaudited)

		1985	1984	1983	1982	1981
Production	Crude oil processed by Shell refineries (thousands of cubic metres daily)	**37.5**	33.6	31.9	36.2	38.6
	Rated refinery capacity at year end (thousands of cubic metres daily)	**42.9**	42.9	35.0	46.8	47.2
	Average rated refinery capacity utilization (%)	**87**	93*	76*	77	82
Sales	Petroleum product sales (thousands of cubic metres daily)					
	Gasolines	**15.9**	14.8	15.5	16.1	17.2
	Middle distillates	**13.2**	12.4	12.2	12.1	13.3
	Lubricants, asphalts, heavy fuel oils and greases	**5.3**	5.7	4.8	5.7	6.6
	Total	**34.4**	32.9	32.5	33.9	37.1
	Petroleum product sales ($ millions)					
	Gasolines	**2 087**	1 901	1 846	1 830	1 665
	Middle distillates	**1 507**	1 329	1 280	1 227	1 170
	Lubricants, asphalts, heavy fuel oils and greases	**561**	590	468	474	501
	Total	**4 155**	3 820	3 594	3 531	3 336
	Retail outlets (number at year end)	**3 473**	3 478	3 433	3 512	3 628
	Chemical sales (tonnes daily)	**2 062**	1 667	1 378	1 346	1 413
	Chemical sales ($ millions)					
	Aromatics	**236**	124	79	84	87
	Solvents and intermediates	**144**	137	118	118	122
	Polymers and resins	**146**	129	104	78	71
	Other	**1**	24	20	48	45
	Total	**527**	414	321	328	325

*Reflects closing of Oakville and St. Boniface refineries in the last half of 1983 and start-up of Scotford refinery in the fourth quarter of 1984.

Supplemental oil, gas and coal disclosure (unaudited)

		1985	1984	1983	1982	1981
Production	Crude oil and natural gas liquids (thousands of cubic metres daily)					
	Gross	**10.7**	11.4	10.1	10.0	10.0
	Net	**7.7**	7.9	7.0	6.7	6.3
	Natural gas (millions of cubic metres daily)					
	Gross	**16.7**	14.5	15.2	16.4	16.4
	Net	**11.8**	10.0	10.5	11.2	10.9
	Sulphur – gross (thousands of tonnes daily)	**3.5**	3.1	3.3	3.2	3.4
	Clean coal – gross (thousands of tonnes daily)	**5.7**	6.2	4.0	2.2	—
Sales	Sulphur – gross (thousands of tonnes daily)	**3.9**	4.0	3.6	3.5	4.2
	Coal – gross (thousands of tonnes daily)	**6.4**	5.7	3.8	2.0	—

Gross production includes all production attributable to Shell's interest before deduction of royalties; net production is determined by deducting royalties from gross production. Net production figures are not applicable to sulphur and coal as royalties are applied to sales volumes rather than production volumes.

Supplemental oil, gas and coal disclosure
(continued)

Land holdings

Oil and gas at December 31, 1985

(thousands of hectares)			Exploration rights		Leases	
			Gross	Net	Gross	Net
Onshore within the provinces	Conventional oil and gas:	Alberta	**267**	**228**	**1 332**	**921**
		Other	**489**	**361**	**584**	**379**
	Synthetic oils:	Oil sands – mining			**20**	**10**
		– in-situ			**168**	**84**
Canada Lands	East Coast offshore:	Nova Scotia	**2 788**	**1 138**		
		Newfoundland	**1 125**	**575**		
		Baffin Bay and Davis Strait	**1 350**	**1 350**		
	Northwest and Yukon Territories:	Mackenzie Delta	**469**	**210**		
		Other	**25**	**19**		
	West Coast offshore		**5 598**	**2 642**		
	Arctic Islands	Cape Allison	**18**	**4**		
	Total		**12 129**	**6 527**	**2 104**	**1 394**

Gross hectares include the interests of others; net hectares exclude the interests of others.

Exploration rights are acquired from the Canadian government or the provinces through application or competitive bidding, and confer upon the holder the right to explore for crude oil, natural gas and sulphur and to lease the crude oil, natural gas and sulphur rights under a specified percentage of the lands covered. No deduction has been made to reflect that only a portion of these areas may be converted to lease.

Leases essentially confer upon the lessee the right to remove crude oil and natural gas from the property, subject to the payment of a rental and/or a reserved royalty.

Of the total leased lands, approximately 318 000 gross hectares or 114 000 net hectares in Western Canada, primarily in Alberta, are classified as developed lands.

Coal at December 31, 1985

(thousands of hectares)	Licences and leases	
	Gross	Net
Alberta	**149**	**111**
British Columbia	**59**	**59**
Saskatchewan	**3**	**3**
Total	**211**	**173**

Exploration and development wells drilled (conventional oil and gas)

		1985		1984		1983		1982		1981	
		Gross	Net	Gross	Net	Gross	Net	Gross	Net	Gross	Net
Exploration	Oil	**5**	**4**	6	5	2	2	4	4	3	1
	Gas	**7**	**5**	3	1	2	1	2	2	10	4
	Dry	**35**	**27**	11	10	14	11	19	17	33	29
	Total	**47**	**36**	20	16	18	14	25	23	46	34
Development	Oil	**108**	**56**	43	19	32	17	15	9	10	7
	Gas	**12**	**10**	11	9	7	6	12	9	5	4
	Dry	**6**	**5**	6	4	10	4	2	1	5	4
	Total	**126**	**71**	60	32	49	27	29	19	20	15
	Total wells drilled	**173**	**107**	80	48	67	41	54	42	66	49

Definitions

Exploration wells – Wells drilled either in search of new and as yet undiscovered pools of oil or gas, or with the expectation of significantly extending the limits of established pools. All other wells are development wells.

Gross wells – The number of wells in which Shell Canada has a working interest.

Net wells – The aggregate of the numbers obtained by multiplying each gross well by the percentage working interest of Shell Canada therein, rounded to the nearest whole number.

Supplemental oil, gas and coal disclosure
(continued)

Reserve quantity information

Estimation of reserve quantities is based on sound geological and engineering principles. However, the results are estimates based on judgmental interpretation of reservoir data. They are subject to revision as additional information regarding producing fields and technology becomes available and as economic and operating conditions change.

The Canadian government and provincial government royalty rates vary depending on prices, production volumes, the timing of initial production and changes in regulations. The net reserves set forth in the table to the right have been calculated on the basis of royalty rates in force as of the dates the estimates were made.

Shell Canada's estimated proved reserves (excluding any reserves in the Mackenzie Delta, Nova Scotia coast, Arctic Islands and other frontier areas) are all located in Canada, with approximately 90 per cent in Alberta.

Crude oil and condensate production in 1985 was approximately 10 per cent of remaining reserves, similar to the utilization rate of recent years. Total reserves additions slightly exceeded this production on a gross basis and resulted in a five per cent increase in net proved developed and undeveloped reserves. Similar performance in matching gross crude oil production with additions has been achieved since 1982 after a period of reserves decline. Specific crude oil additions were gained by improved performance of the mature Fenn/Big Valley, Innisfail, Nipisi and Simonette fields. Infill drilling programs resulted in positive revisions of reserves in Virginia Hills, Garrington, Pembina, Weyburn and Snipe Lake. New reserves were added by field extensions from development drilling following recent discoveries at Wembley, Sakwatamau, Lake Alma and by ongoing development at Manyberries and Pouce Coupe/Progress. Most oil fields also gained some net reserves additions as a result of royalty reduction.

Oil, gas and other reserves

Net proved developed and undeveloped reserves
Beginning of year
Revisions of previous estimates
Extensions, discoveries and other additions
Improved recovery methods
Production
End of year
Net proved developed reserves
Beginning of year
End of year
Gross proved developed and undeveloped reserves at end of year

While maintaining an industry leadership position in natural gas production during 1985, Shell sustained gross reserves and gained some 3.5 per cent on net proved developed plus undeveloped reserves. Specific natural gas reserves additions were achieved by positive revision due to infill drilling and improved performance in Jumping Pound West and Cranberry. Additions and extensions occurred as a result of outstep drilling in Pouce Coupe/Progress and Jumping Pound West and new pool discoveries in Hamburg and Simonette Dunvegan. New reserves were also added for the Hines Creek field where a plan for field development was defined as a result of a new gas sales opportunity. Additions to net reserves resulting from royalty reduction also benefited all gas fields to some degree.

Reserves additions in condensate, natural gas liquids and sulphur occurred in conjunction with the natural gas reserves increases in Jumping Pound West and on a net basis from royalty reduction. With the exception of gross natural gas liquids, which went down very slightly, the additions in the various reserves categories for these products more than offset production.

Supplemental oil, gas and coal disclosure
(continued)

Crude oil and condensate (million cubic metres)			Bitumen (million cubic metres)			Natural gas liquids (million cubic metres)			Natural gas (billion cubic metres)			Sulphur (million tonnes)		
1985	1984	1983	**1985**	1984	1983	**1985**	1984	1983	**1985**	1984	1983	**1985**	1984	1983
21.0	20.8	21.0	**7.2**	—	—	**8.6**	9.7	11.2	**80.0**	80.3	72.8	**18.0**	18.6	19.7
2.5	0.7	1.1	**—**	—	—	**0.6**	(0.4)	(0.8)	**5.2**	2.2	9.8	**1.2**	0.5	—
0.5	1.5	0.5	**—**	7.2	—	**0.3**	—	—	**2.0**	1.2	1.5	**0.2**	—	—
0.1	0.2	—	**—**	—	—	**—**	—	—	**—**	—	—	**—**	—	—
(2.0)	(2.2)	(1.8)	**—**	—	—	**(0.7)**	(0.7)	(0.7)	**(4.3)**	(3.7)	(3.8)	**(1.1)**	(1.1)	(1.1)
22.1	21.0	20.8	**7.2**	7.2	—	**8.8**	8.6	9.7	**82.9**	80.0	80.3	**18.3**	18.0	18.6
18.0	18.5	19.2	**0.2**	—	—	**7.3**	8.6	8.8	**61.2**	63.7	59.1	**13.9**	15.1	15.3
19.1	18.0	18.5	**0.2**	0.2	—	**7.7**	7.3	8.6	**64.7**	61.2	63.7	**14.8**	13.9	15.1
29.5	29.2	29.7	**8.4**	8.4	—	**10.8**	11.0	12.3	**110.2**	111.8	111.5	**21.0**	20.8	21.4

Other reserves

	Coal (million tonnes)			Oils sands mining (million cubic metres)			Oils sands in-situ (million cubic metres)		
At end of year	**1985**	1984	1983	**1985**	1984	1983	**1985**	1984	1983
Net proved	**46**	48	52	**—**	—	—	**—**	—	—
Net probable	**127**	127	132	**—**	—		**—**		
Net potential	**—**	—		**300**	300	300	**800**	800	800

Definitions

Proved reserves – Estimated quantities of crude oil, bitumen, natural gas liquids, natural gas and sulphur which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs. These estimates are based on existing economic and operating conditions (prices, costs, royalties and income taxes) as of the date the estimate is made and include only natural gas volumes which have been contracted.

Proved developed reserves – Reserves which can be expected to be recovered through existing wells with existing equipment and operating methods.

Proved undeveloped reserves – Reserves which are expected to be recovered from new wells on undrilled acreage adjacent to producing acreage, or from existing wells where further significant expenditure is required.

Gross proved reserves – Reserve estimates before the deduction of royalty interests owned by others.

Net proved reserves – Reserve estimates after deduction of royalties and therefore only those quantities which Shell Canada has a right to retain.

Probable reserves – Reserves which are estimated to be commercially recoverable and are less well-defined than proved reserves, but may be estimated or indicated to exist on the basis of geological, geophysical or engineering data.

Potential reserves – Reserves which are speculative quantities in addition to proved and probable reserves which geological, geophysical and engineering data together with trends in existing plays and statistical and interpretative methods, indicate may become economically proved.

Shell Canada Limited

Supplemental financial disclosure

(unaudited)

The following information has been prepared in accordance with the Canadian Institute of Chartered Accountants' requirements for supplemental oil and gas disclosure and provisions of the United States Financial Accounting Standards Board Statement #69. This latter standard has been adopted by the United States Securities and Exchange Commission as a comprehensive set of disclosure requirements for conventional oil and gas producing activities. Such activities involve only conventional equipment and methods and therefore exclude Shell's in-situ as well as its coal operations reported in the Resources segment data in Note 6.

Capitalized costs

December 31 ($ millions)	**1985**	1984	1983
Unproved oil and gas properties	**402**	383	359
Proved oil and gas properties	**1 460**	1 324	1 246
	1 862	1 707	1 605
Accumulated depreciation and amortization	**626**	551	496
Net capitalized costs	**1 236**	1 156	1 109

Costs incurred

Year ended December 31 ($ millions)	**1985**	1984	1983
Property acquisition – unproved	**40**	36	21
Exploration costs	**118**	111	96
Development costs	**150**	89	57
Total costs incurred	**308**	236	174

Results of operations from producing activities

Year ended December 31 ($ millions)	**1985**	1984	1983
Revenues	**1 060**	975	890
Less: Operating expenses	**201**	176	161
Exploration expenses	**120**	96	82
Depreciation, amortization and retirements	**102**	89	75
Petroleum and gas revenue taxes	**123**	118	114
Income taxes	**322**	327	291
Results of operations from producing activities	**192**	169	167

Amounts from in-situ and coal operations, the contributions from which were nil in 1985, $(5) million in 1984 and $(13) million in 1983, are excluded from the above revenues and expenses but are included in the Resources segment financial results reported in Note 6.

Supplemental financial disclosure
(continued)

Standardized measure of discounted future net cash flows

The following future net revenue information, in management's view, does not purport to represent an accurate estimate of the value of the Corporation's oil and gas operations, and should be interpreted with considerable caution since actual future cash flows will differ from future net cash flows presented in that:

(a) Future cash flows will be derived not only from proved reserves but also from probable and potential reserves which ultimately become proved,

(b) Future, rather than current year, costs and prices will apply,

(c) Economic, regulatory and operating conditions will change, and

(d) Cash flows from non-conventional oil and gas (in-situ) and coal activities are excluded from this computation.

Net cash flows

Year ended December 31 ($ millions)	**1985**	1984	1983
Future cash inflow*	**16 283**	15 667	15 006
Less: Future operating and development costs	**3 929**	3 581	3 197
Future petroleum and gas revenue taxes	**142**	1 794	1 816
Future income taxes	**5 889**	6 002	5 687
Future net cash flows	**6 323**	4 290	4 306
Less: 10% annual discount for estimated timing of cash flows	**3 257**	2 292	2 358
Standardized measure of discounted future net cash flows from proved oil and gas reserves	**3 066**	1 998	1 948

Changes in net cash flows

Sales, net of operating costs**	**(736)**	(681)	(615)
Net changes in prices and operating costs	**32**	208	197
Extensions, discoveries and improved recovery, less related costs**	**126**	156	92
Development costs incurred during the period	**150**	89	57
Revisions of previous quantity estimates**	**456**	112	399
Petroleum and gas revenue taxes	**640**	(100)	89
Accretion of discount	**479**	462	427
Net changes in income taxes	**(161)**	(227)	(250)
Other	**82**	31	(64)
Net increase (decrease) for the year	**1 068**	50	332

*Future net cash flows were computed using year-end prices and costs, and year-end statutory tax rates that relate to existing proved developed and undeveloped oil and gas reserves in which the Corporation has mineral interests.

**Costs include petroleum and gas revenue taxes.

Supplemental financial disclosure
(continued)

Accounting for inflation

For the last 10 years, Shell Canada has provided detailed presentations of the methodologies proposed by the Canadian Institute of Chartered Accountants and other authoritative bodies. This year, a change in presentation has been made to focus more attention on the areas most affected by inflation. Management continues to advise that the Current Cost methodology involves a number of fundamental assumptions which do not properly portray, particularly in the case of companies having natural resource reserves, replacement costs for these assets. Consequently, the methodology fails to reflect a fair determination of the effects of inflation.

Earnings on Current Cost basis

Year ended December 31 ($ millions)	**1985**	1984
Earnings as reported	**146**	123
Adjustments required to reflect higher current costs in the year		
– purchases	**14**	51
– depreciation, amortization and retirements	**100**	111
Earnings (loss) – adjusted	**32**	(39)

Other financial data

December 31 ($ millions)	Historical cost **1985**	Current cost **1985**	Current cost 1984
Inventories	**980**	**985**	1 125
Properties, plant and equipment – net	**3 562**	**5 144**	5 209
Capital employed	**4 902**	**6 489**	6 511

Current Cost amounts were estimated by applying specific industry indices to Historical Cost carrying values. No adjustment was made to current or deferred income tax expense.

Total increase during the year in inventory and property, plant and equipment was $199 million ($92 million in 1984) and the amount attributable to general inflation was $219 million ($155 million in 1984). Purchasing power gain was $81 million ($51 million in 1984). Financing adjustment to income for 1985 was $62 million ($78 million in 1984), and to inventories and property, plant and equipment for 1985 was $70 million ($30 million in 1984).

Interpretation of results

As indicated above, significantly higher Current Cost depreciation eroded Shell's 1985 Historical Cost-based earnings from $146 million to $32 million. Similar dramatic reductions have occurred over the past several years and demonstrate the effect of inflation on a corporation's cost of maintaining its present level of operating capability.

As a result of inflation, Shell's cost to replace its property, plant and equipment would be almost 50 per cent more than Historical Cost values recorded in the accounts. The cost of replacing reserves in the ground, which are unique and finite, was determined by applying inflation indices to the exploration and development costs recorded. However, these calculated values fail to approximate the current costs of finding and developing similar reserve quantities. This failing greatly reduces the usefulness of the methodology for resource assets.

In summary, the results determined above only partially demonstate the relative magnitude of the impairment to earnings and cash flow as a result of inflation.

Investor information

Shell Canada Limited

(incorporated under the laws of Canada)
Head Office: Shell Centre,
400-4th Avenue S.W.,
Calgary, Alberta T2P 0J4

Transfer agent and registrar

Shell Canada's transfer agent and registrar is National Trust Company – Toronto, Montreal, Winnipeg, Calgary and Vancouver and its agent in Halifax is Canada Permanent Trust Company.

Changes of address or inquiries about shares and dividends should be directed to the transfer agent.

Stock exchange listings

The Class "A" Common Shares of Shell Canada Limited are listed on the Montreal, Toronto, Alberta and Vancouver stock exchanges (stock symbol is SHC), and do not have an established public trading market in the United States.

Annual meeting

The annual meeting of shareholders will be held at 2:00 p.m. Wednesday, April 23, 1986, Regency Ballroom, Four Seasons Hotel, Toronto, Ontario.

Duplicate reports

Shareholders who receive more than one copy of Annual and Quarterly Reports, as a result of having their shareholdings represented by two or more share certificates, may wish to contact the transfer agent to have their holdings consolidated. It will not be necessary to forward share certificates.

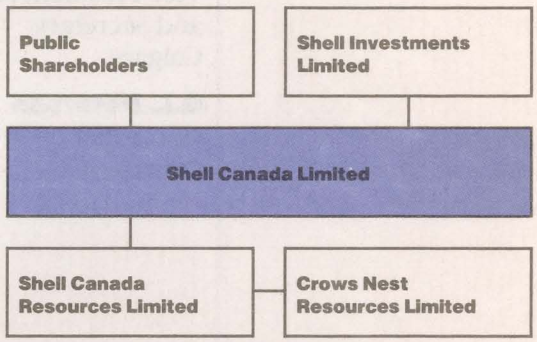
Form 10-K report

A copy of the Corporation's Form 10-K report for 1985, as filed with the Securities and Exchange Commission in the United States, is available to shareholders on request from the Corporation's Secretary at the above Head Office address.

Ownership and voting rights of Shell Canada Limited (at December 31, 1985)
Ownership of Shell Canada Limited is divided between Shell Investments Limited (SIL) and public shareholders. SIL's holdings include approximately 68 per cent of the Class "A" and 100 per cent of the Class "B" Common Shares which, when aggregated, represent a 79-per-cent ownership interest. However, while each Class "B" share has four times the value of a Class "A", it represents only one vote per share. Consequently, the SIL voting interest is approximately 72 per cent.

The publicly-held Class "A" Common Shares (approximately 23.9 million) constitute 21 per cent ownership and 28 per cent voting interest.

Shell Investments Limited is a Canadian company, wholly-owned by Shell Petroleum N.V. of the Netherlands which, in turn, is owned 40 per cent by The "Shell" Transport and Trading Company, p.l.c., an English company, and 60 per cent by Royal Dutch Petroleum Company of the Netherlands.



Effective January 1, 1986, the organization was restructured to provide a more logical alignment of Shell Canada's business activities. Shell Canada Resources Limited was amalgamated with Shell Canada Limited, its parent company, and a new wholly-owned subsidiary of Shell Canada Limited, Shell Canada Products Limited, was created to carry on its refining, marketing and chemical businesses in the future.

Approximate metric conversion factors

1 cubic metre of liquids	=	6.29 barrels
1 cubic metre of gases	=	35.3 cubic feet
1 tonne	=	2 205 pounds
	or	0.984 long ton
	or	1.102 short tons
1 kilometre	=	0.621 mile
1 hectare	=	2.47 acres
1 litre	=	0.22 gallon

Officers
at December 31, 1985

J.M. MacLeod
President and Chief Executive Officer
Calgary

J.E. Czaja
Executive Vice President (Resources)
Calgary

Donald J. Taylor
Executive Vice President (Products)
Calgary

D.G. Stoneman
Senior Vice President
(Business Development)
Calgary

R.F. Taylor
Senior Vice President
(Business Services)
Calgary

G.B. Darou
Vice President (Finance)
and Treasurer
Calgary

J.M. Killey
Vice President (General Counsel)
and Secretary
Calgary

G.L. Peterson
Controller
Calgary

Board of Directors
at December 31, 1985

Peter J.G. Bentley
Chairman and Chief Executive Officer
Canfor Corporation
Vancouver

J.E. Czaja
Executive Vice President (Resources)
Shell Canada Limited
Calgary

C. William Daniel
Corporate Director
Toronto

Dr. James M. Ham
Professor of Science,
Technology and Public Policy
University of Toronto

Peter F. Holmes
Chairman and Managing Director
The "Shell" Transport and
Trading Company, p.l.c.
London, England

Walter F. Light
Retired Chairman
Northern Telecom Limited
Toronto

Lorne K. Lodge
Chairman and Chief Executive Officer
IBM Canada Ltd.
Markham

J.M. MacLeod
President and Chief Executive Officer
Shell Canada Limited
Calgary

Margaret Southern
President
Spruce Meadows Equestrian Centre
Calgary

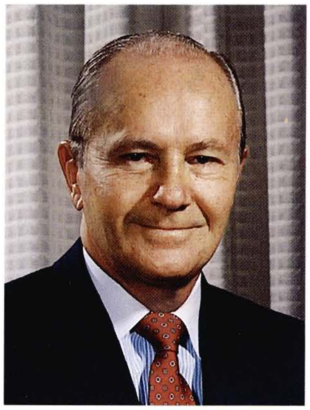
Donald J. Taylor
Executive Vice President (Products)
Shell Canada Limited
Calgary

Antoine Turmel
Corporate Director
Montreal

L.C. van Wachem
President and Managing Director
Royal Dutch Petroleum Company
The Hague, Netherlands

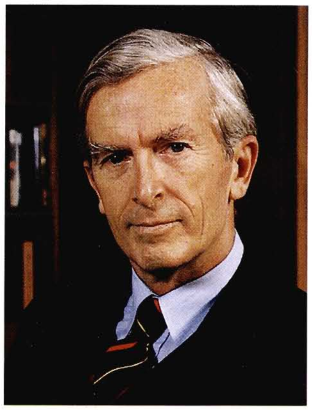
Non-employee Directors:

Peter J.G. Bentley

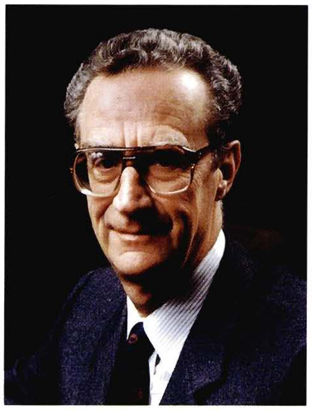


C. William Daniel

Dr. James M. Ham



Peter F. Holmes



Walter F. Light

Lorne K. Lodge

Margaret Southern

Antoine Turmel

L.C. van Wachem

Audit Committee
Composed of Messrs. Bentley, Lodge and Turmel, reviews Shell's financial statements, the scope and results of the shareholders' auditors' work, the adequacy of internal accounting controls and internal audit programs, and the compliance with accounting and reporting standards.

Management Resources and Compensation Committee
Composed of Messrs. Bentley, Light, MacLeod and Turmel, reviews and recommends to the Board succession plans for senior management and reviews and approves executive compensation.

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