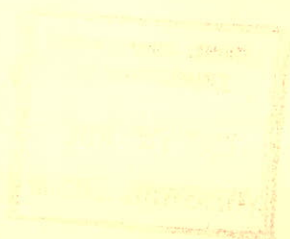




MSR Exploration Ltd.
Tenth Annual Report 1982



Directors and Officers Corporate Data

DIRECTORS:

JOSEPH V. MONTALBAN — Cut Bank, Montana
JAMES GRAY — Edmonton, Alberta
F.K. ROY GILLESPIE — Calgary, Alberta
CORA BELLE MONTALBAN — Cut Bank, Montana

OFFICERS:

JOSEPH V. MONTALBAN — President, Managing Director
EDWARD F. DURKEE — Vice-President, Exploration
CORA BELLE MONTALBAN — Secretary-Treasurer

OFFICES:

EXECUTIVE & OPERATIONS OFFICE — CBM Building,
Cut Bank, Montana 59427 • (406) 873-2235

REGISTERED OFFICE —

2500 Canadian Commercial Bank Tower
Edmonton, Alberta T5J 1V3

AUDITORS:

THORNE RIDDELL — 1200 Bow Valley Square 2,
205 Fifth Avenue S.W., Calgary, Alberta T2P 2W4

BANKERS:

TORONTO-DOMINION BANK — Centennial Building
Branch, Edmonton, Alberta T5J 2E5
FIRST NATIONAL BANK — Cut Bank, Montana 59427
FIRST INTERSTATE BANK — Cut Bank, Montana 59427

BARRISTERS AND SOLICITORS:

BISHOP & McKENZIE —
2500 Canadian Commercial Bank Tower
Edmonton, Alberta T5J 1V3
SOBOLEWSKI, ANFIELD — Stock Exchange Tower,
Vancouver, British Columbia V7Y 1C3
FRISBEE, MOORE & STUFFT — Wilkins Building,
Cut Bank, Montana 59427

CONSULTANTS:

CITIDAL ENGINEERING LTD. — Petroleum Engineers,
700, 808 4th Avenue S.W., Calgary, Alberta T2P 0K4
WORLDWIDE EXPLORATION CONSULTANTS INC. —
Petroleum Geologists, 1244 Capital Life Bldg., Denver,
Colorado 80203
CONNIE M. KRIVANEK — Petroleum Geologist
609 Meseta, Farmington, New Mexico 87401
TEAGUE GEOLOGICAL, INC. — Petroleum Geologists
147 Main Street — P.O. Drawer K
Shelby, Montana 59474

REGISTRAR AND TRANSFER AGENTS:

NATIONAL TRUST COMPANY, LIMITED —
510 Burrard Street, Vancouver, British Columbia V6C 2J7
NATIONAL TRUST COMPANY, LIMITED —
21 King St. East, Toronto, Ontario M5C 1B3
NATIONAL BANK OF NORTH AMERICA —
80 Pine St., New York, N.Y. 10005

CAPITALIZATION:

SHARE STRUCTURE —

Shares Authorized:	20,000,000
Shares Issued:	7,627,203

STOCK EXCHANGE LISTINGS:

TORONTO STOCK EXCHANGE —
Trading Symbol: MTN-T
VANCOUVER STOCK EXCHANGE —
Trading Symbol: MTN-V
NASDAQ — New York
Trading Symbol: MSREF

Share Price Range:

	Toronto Stock Exchange (Canadian dollars)		NASDAQ System (U.S. dollars)	
	High Sale	Low Sale	High Bid	Low Bid
1981:				
1st quarter	18.00	12.25	12.50	10.37
2nd quarter	16.50	12.00	13.37	10.00
3rd quarter	14.00	7.00	11.37	6.37
4th quarter	13.38	8.00	10.87	6.62
1982:				
1st quarter	8.40	4.55	6.87	3.62
2nd quarter	8.00	4.85	6.50	3.87
3rd quarter	6.20	4.60	4.75	3.75
4th quarter	8.40	4.55	6.75	4.62

ANNUAL MEETING

Friday, June 17, 1983
Westin Bayshore Inn 2 p.m.
Presidents Room
Vancouver, B.C.

FRONT COVER PHOTO:

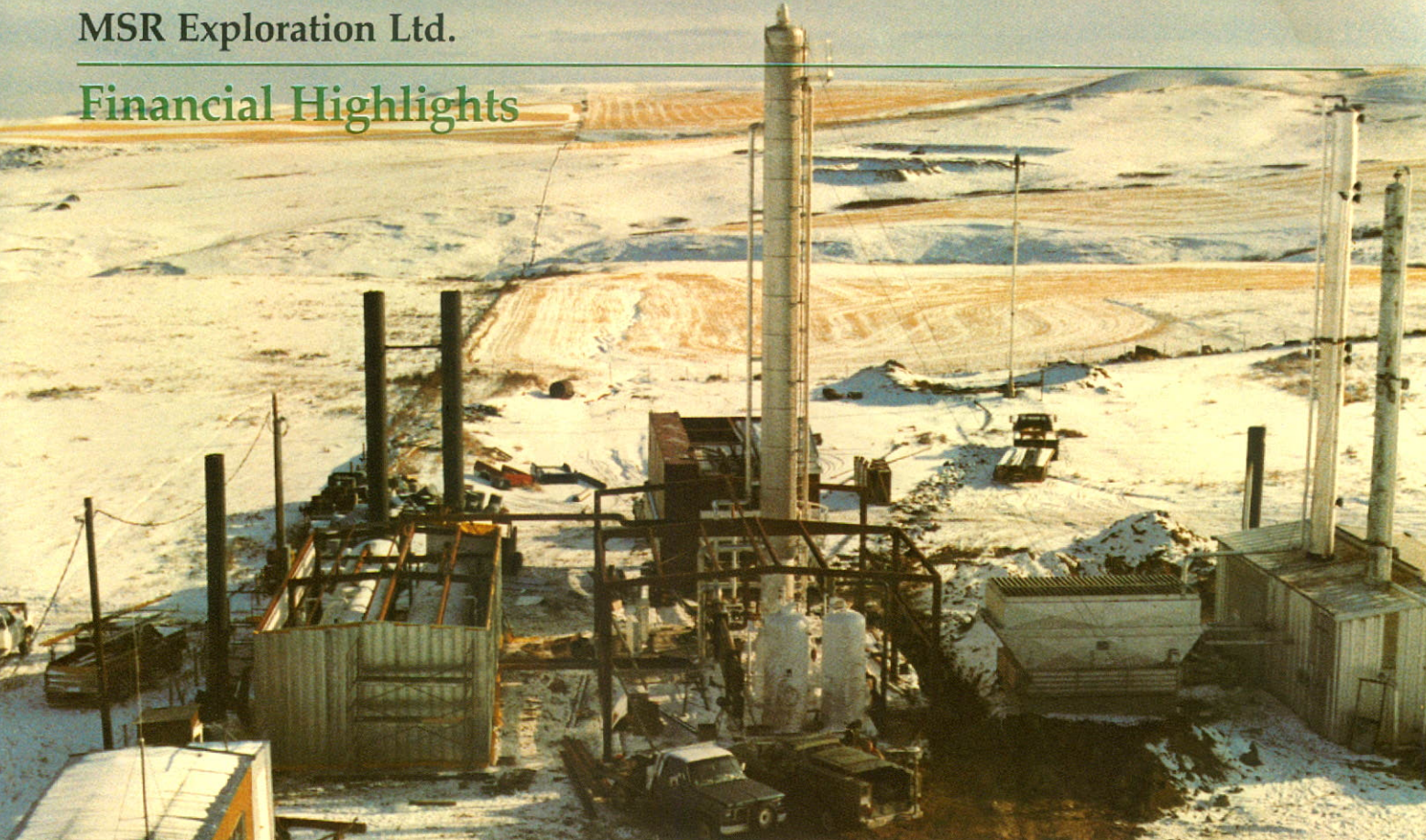
*The Montana Overthrust Belt watches over
our Gypsy Basin Field.*

NOTE: FORM 10

The Company will file its first FORM 10 with the Securities and Exchange Commission of the United States of America (S.E.C.) prior to the end of April, 1983.

Copies of this report will be available free of charge to all shareholders of record and beneficial owners of shares, by writing to the Secretary of the Company.

Financial Highlights



Plant expansion at Gypsy Highview Gathering System, November 1982.

Year Ended December 31	1982	1981	1980
Operating Revenue			
Gas Production	\$ 1,886,074	\$ 3,290,282	\$ 3,931,599
Oil Production	3,036,344	3,051,548	1,639,138
Interest and Other	459,209	1,046,165	790,916
Total	5,381,627	7,387,995	6,361,653
Operating Income	1,654,302	3,459,988	3,259,091
Net Income	1,112,868	2,217,491	2,119,112
Cash Flow from Operations	2,865,251	4,235,469	3,859,465
Financial Position			
Current Assets	5,290,510	5,601,081	8,357,328
Working Capital	3,243,204	4,330,010	6,983,631
Total Assets	26,444,540	24,600,639	20,727,883
Debt	—	—	—

President's Message



In this our tenth year of operations it would normally be cause for a spectacular and large annual report. However, with last year being an economic disaster for so many companies in the oil and gas industry, MSR Exploration Ltd. is keeping with its policy of conservatism, both in the field and in its reporting to the shareholders. Our policy of restraint has kept your company in a solvent and solid position in a year where revenues are down some 30% within the industry.

In spite of decreased revenues our operating income was \$1,654,302, and we generated \$2,865,251 cash flow from operations, or 38¢ per share. Although oil prices dropped by more than \$10.00 per barrel, our oil revenues remained almost constant, as we put new wells on production. Nevertheless, our overall revenue picture for year end December 31, 1982, was down 25% to \$5,381,627, due mainly to a 40% decline in gas revenues. With falling interest rates, our interest earned on term deposits also dropped some 40% in 1982. Last year may not have been a good year for the industry as a whole but we feel that MSR fared very well. We reduced expenses by keeping our company lean, our shareholders equity increased \$1.8 million, and retained earnings were up by \$1.1 million over 1981.

EXPLORATION 1982:

Teec Nos Pos Field, N.E. Arizona

Staying within our guidelines of restraint, we drilled sixteen 100% owned wells in 1982, compared to 42 wells in 1981. The most significant event of our 1982 exploration program was the drilling of two successful wells in the Teec Nos Pos field, located in Apache County, in Northeastern Arizona. The Navajo 'O' No. 16 well, completed in early 1983, appears to have discovered a new pool for the field, and established gas and condensate production in both the Desert Creek and lower Ismay formations, clearly defining two producing horizons not part of the main Teec Nos Pos field. On January 21, 1983, MSR petitioned the Arizona Oil & Gas commission to change the spacing in the Teec Nos Pos field from 80 acre to 40 acre spacing. The petition was granted as applied for, and management now feels that possibly 10 additional locations are available for drilling: which could add up to 1.5 million barrels of new oil reserves, and 1.8 billion cubic feet of gas reserves, based on engineering data from off-setting wells.

Northern Montana

Drilling continued all summer and fall at Gypsy Basin, Highview and Bills Coulee fields. Fourteen development wells have been drilled in all fields and all wells have been successful oil and/or gas wells, and will add to present production and reserves. One highlight to date of this program is the discovery of a new pay zone some 120 feet below the present producing gas zone at the top of the Madison. By year's end six new wells had been drilled, all indicating success in this new reservoir. Completion of these wells has continued all winter, due to exceptionally mild temperatures.

Blackleaf Canyon, Montana

MSR's greatest accomplishment in 1982, was probably the expansion of Gypsy Highview Gathering System, our pipeline and gas plant subsidiary. GHGS contracted to purchase 6 MMcf of gas per day from the consortium of Superior Oil Co., Burlington Northern Railroad (Milestone Petroleum, Inc.) and Williams Exploration Company. This group drilled and discovered gas in the Montana overthrust belt, at Blackleaf Canyon in Northwestern Montana, located some 15 miles southwest of our Gypsy Basin, Highview, and Bills Coulee fields. The Blackleaf Canyon represents the first significant overthrust belt gas discovered in Montana. Gas production from Blackleaf Canyon commenced in December of 1982 and the new plant is now running at a stabilized rate of 6.2 MMcf per day. This new project will increase gas revenues and will add some 25¢ per share to our cash flow from operations.

OUTLOOK FOR 1983

The financial strength and capable management of MSR Exploration Ltd. is the key to the company's past achievements and continued success. The company has no debt and has ample cash resources to manage its business based on its philosophy of generating funds internally, rather than borrowing these funds, or participating in fractional plays with other companies.

MSR continues to seek out a merger company; but, because of our strong cash position it has been difficult to find a suitable company. All suitor companies to date appear to be lacking operating cash, and have overleveraged debt; which is not

acceptable to MSR's management. We feel that with our healthy financial structure, we are in an excellent position to take advantage of opportunities in today's difficult industry environment, and will continue to seek a proper merger company.

As in the past, MSR will continue to operate totally in the U.S.A., where oil market conditions are far superior to those in Canada.

Consolidated operating revenues are estimated to reach \$8.0 million in fiscal 1983, with a cash flow of some \$5.0 million being generated from operations.

Although the energy stocks, as a whole, continue to be avoided by the investment community, management firmly believes that the energy market will recover, and as MSR continues to be solvent and totally debt free, our market can only improve upwards.

Notwithstanding the business and economic uncertainty that exists in the oil industry today, MSR's management believes that the energy sector, over the long-term, will provide for continued corporate expansion, and we feel that by following a prudent and shrewd operational program, we are well positioned to continue our conservative, yet aggressive, growth.

We look forward to seeing you at our annual meeting in June, at which time our activities will be reviewed and discussed.

Respectfully submitted on behalf
of the Board of Directors



J.V. Montalban
President & Managing Director

Cut Bank, Montana
April 15, 1983

Oil & Gas Land Holdings

Your Companies presently own interests in 216,832 gross (122,072 net) acres of oil and gas rights in the United States as shown in the following summary:

Lease	Acreage		No. Wells	
	Gross	Net	Oil	Gas
Graben Coulee	2522	2522	58	
Gypsy Basin	7780	7780	26	17
Highview	2340	2340	12	2
Bills Coulee	2530	2530		7
Crazy Mtns.	53,900	32,340		(7)
Bearpaw/Laredo	130,000	65,000		43
Utah-Vega	16,400	8200	2	
Turner Bluff	80	80		
Teec Nos Pos	1280	1280	1	
	216,832 acres	122,072 acres	99	69
			Net	Net
			98	45.4

Reserves and Associated Economics

The Companies' oil and gas reserves, future revenues from gas plant operations and land position as evaluated by Independent Consulting Engineers as of March 1, 1983, is as follows:

	Cash Flow in Thousands of Dollars (U.S.)						
	Net Reserves		Undisc.	Discounted			
	MMscf(1)	MSTB		10% Per Annum	12% Per Annum	15% Per Annum	20% Per Annum
U.S.A.							
Proven Producing	4,814	723	35,862	14,902	13,234	11,333	9,171
Proven Developed Nonproducing ...	1,533	221	12,474	3,307	2,841	2,339	1,799
Proven Undeveloped	6,961	609	42,384	13,747	11,536	9,044	6,282
Plant Revenue	—	—	44,088	25,721	23,797	21,371	18,227
Probable (2)	4,306	558	31,019	9,782	8,001	5,977	3,723
Plant Revenue Probable	—	—	6,738	3,006	2,607	2,127	1,550
Sub-Total	17,614	2,111	172,565	70,465	62,016	52,191	40,752
Land (Acres)	(216,832)		4,650	4,650	4,650	4,650	4,650
TOTAL (2)			177,215	75,115	66,666	56,841	45,402
TOTAL (3)			212,658	90,138	79,999	68,209	54,482

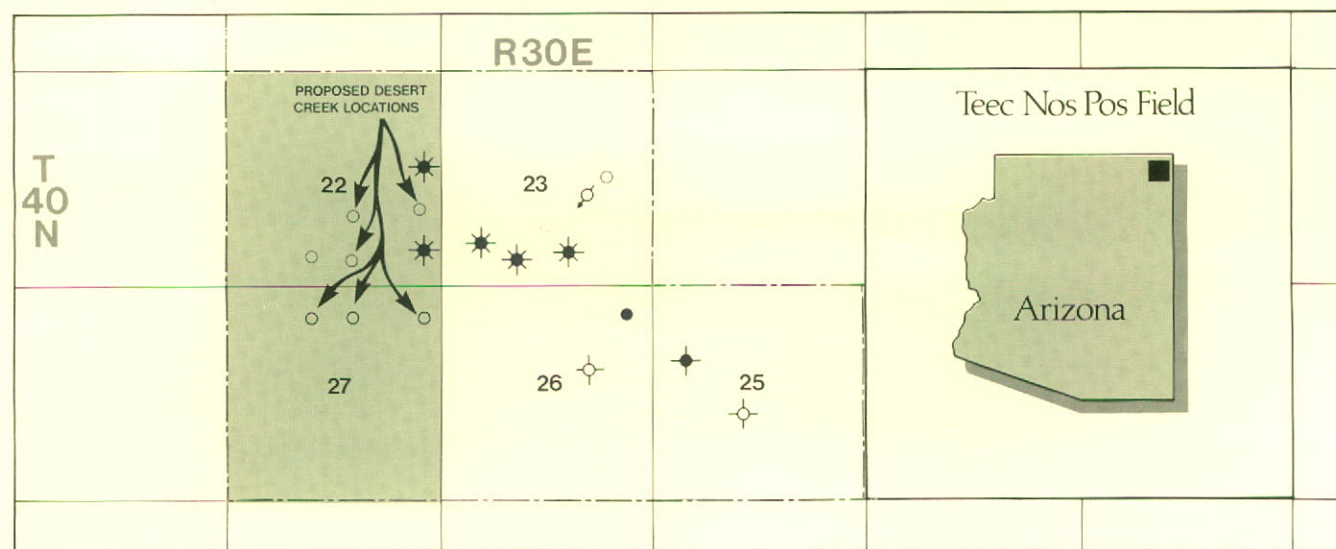
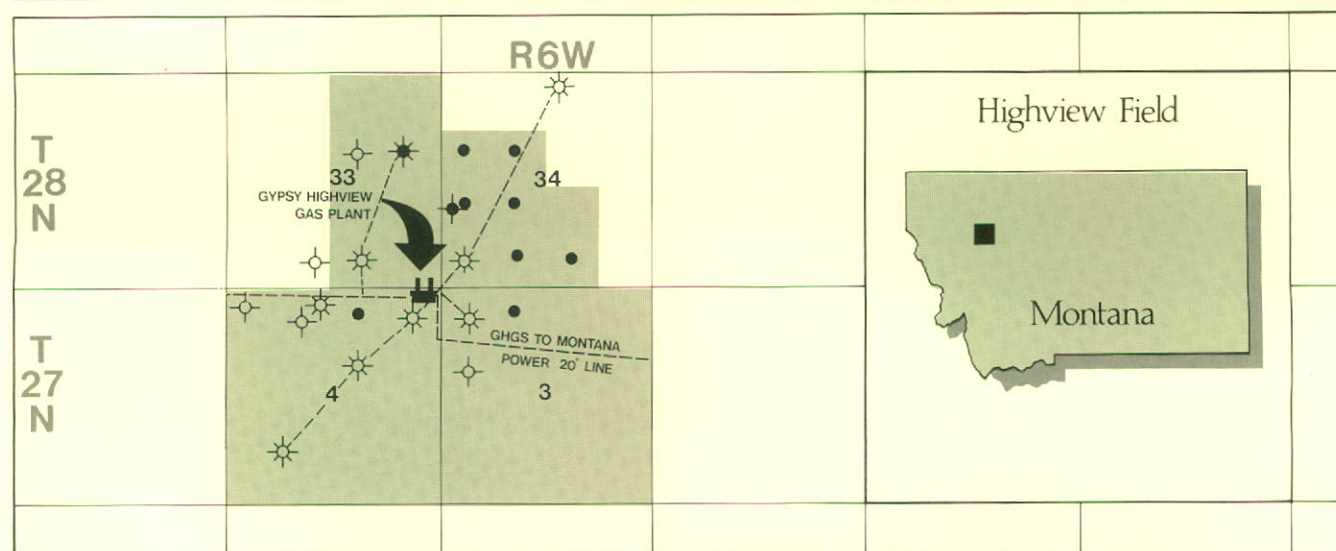
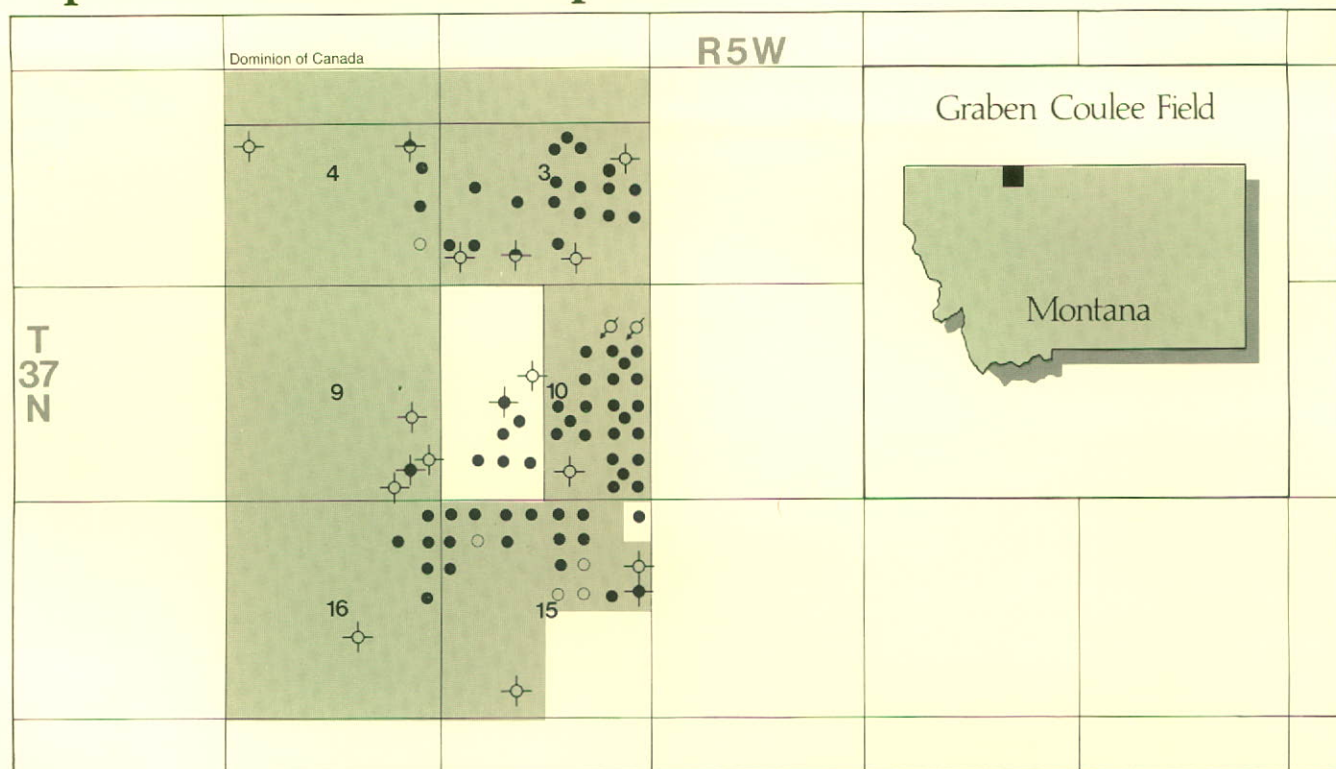
Notes:

(1) Sales gas volume measured at 14.65 psia and 60°F.

(2) Cash flow values quoted in U.S. dollars.

(3) Cash flow values quoted in equivalent Canadian dollars, increased by 20.0%.

Exploration and Development



Consolidated Balance Sheet

(Canadian dollars)

	As at December 31,	1982	1981
Assets			
Current Assets			
Cash and term deposits		\$ 3,381,672	\$ 3,953,457
Marketable securities (quoted market value, \$852,000; 1981 – \$649,000)		851,718	648,679
Accounts receivable		888,755	843,185
Inventories		168,365	155,760
		<u>5,290,510</u>	<u>5,601,081</u>
Investment in Bearpaw Gathering System, Inc. (note 3)		460,203	563,010
Properties, Plant and Equipment ("full cost" basis – note 4) ...		20,693,827	18,436,548
		<u>\$26,444,540</u>	<u>\$24,600,639</u>
Liabilities			
Current Liabilities			
Accounts payable and accrued liabilities		\$ 1,193,306	\$ 1,206,976
Notes payable		854,000	—
Income taxes payable		—	64,095
		<u>2,047,306</u>	<u>1,271,071</u>
Deferred Income Taxes		<u>4,014,042</u>	<u>3,493,042</u>
Shareholders' Equity			
Capital Stock (note 5)			
Authorized 20,000,000 Shares without nominal or par value			
Issued 7,627,203 Shares		13,204,679	13,156,679
Retained Earnings		<u>7,792,715</u>	<u>6,679,847</u>
		20,997,394	19,836,526
Investment in Company's Own Shares (note 5[c])		(614,202)	—
		<u>20,383,192</u>	<u>19,836,526</u>
		<u>\$26,444,540</u>	<u>\$24,600,639</u>

Consolidated Statement of Income and Retained Earnings

(Canadian dollars)

Year Ended December 31,	1982	1981	1980
Revenue			
Gas Production	\$1,886,074	\$3,290,282	\$3,931,599
Oil Production	3,036,344	3,051,548	1,639,138
Interest and other	459,209	1,046,165	790,916
	<u>5,381,627</u>	<u>7,387,995</u>	<u>6,361,653</u>
Expenses			
Production taxes and royalties	854,401	1,003,221	833,797
Administrative salaries	119,187	123,180	105,463
Production costs	985,522	1,082,060	1,170,606
Windfall profits tax	180,645	332,116	235,475
Shareholders information	127,372	111,791	81,525
Office	68,659	49,381	46,120
Stock exchange fees	5,214	27,360	20,452
Registrar and trust company fees	29,577	65,254	2,920
Accounting and auditing	50,658	39,134	28,824
Depleting and depreciation	1,183,785	1,010,087	545,952
Travel	93,239	66,093	18,143
Legal	25,059	13,206	11,075
Sundry	4,007	5,124	2,210
	<u>3,727,325</u>	<u>3,928,007</u>	<u>3,102,562</u>
Operating Income	<u>1,654,302</u>	<u>3,459,988</u>	<u>3,259,091</u>
Other Income (Expense)			
Share in earnings (loss) of			
50%-owned company	(47,664)	2,244	—
Gain (loss) on marketable securities	(15,047)	102,240	152,456
Provision for decline in			
marketable securities	(1,469)	(226,963)	—
Foreign exchange gain (loss)	71,031	(11,845)	84,777
	<u>6,851</u>	<u>(134,324)</u>	<u>237,233</u>
Income before income taxes and			
extraordinary item	1,661,153	3,325,664	3,496,324
Income taxes (note 8)	548,285	1,108,173	1,481,212
Income before extraordinary item ...	<u>1,112,868</u>	<u>2,217,491</u>	<u>2,015,112</u>
Extraordinary Item			
Reduction of income taxes by			
application of prior years' losses	—	—	104,000
Net Income	<u>1,112,868</u>	<u>2,217,491</u>	<u>2,119,112</u>
Retained Earnings at Beginning of Year	<u>6,679,847</u>	<u>4,462,356</u>	<u>2,343,244</u>
Retained Earnings at End of Year	<u>\$7,792,715</u>	<u>\$6,679,847</u>	<u>\$4,462,356</u>
Per Share			
Income before extraordinary item ...	<u>\$0.148</u>	<u>\$0.293</u>	<u>\$0.268</u>
Net income	<u>\$0.148</u>	<u>\$0.293</u>	<u>\$0.282</u>
Working capital generated from			
operations	<u>\$0.382</u>	<u>\$0.559</u>	<u>\$0.540</u>

Consolidated Statement of Changes in Financial Position

(Canadian dollars)

Years Ended December 31,	1982	1981	1980
Working Capital Derived From			
Operations	\$2,865,251	\$4,235,469	\$3,859,465
Issue of shares	48,000	750,000	577,000
Reduction of advances to 50%-owned company	55,143	—	—
Reduction of income taxes by application of prior years, losses	—	—	104,000
	<u>2,968,394</u>	<u>4,985,469</u>	<u>4,540,465</u>
Working Capital Applied to			
Properties, plant and equipment	3,440,998	7,076,080	5,070,816
Investment in company's own shares	614,202	—	—
Investment in 50%-owned company	—	563,010	—
	<u>4,055,200</u>	<u>7,639,090</u>	<u>5,070,816</u>
Decrease in Working Capital	(1,086,806)	(2,653,621)	(530,351)
Working Capital at Beginning of Year	4,330,010	6,983,631	7,513,982
Working Capital at End of Year	<u>\$3,243,204</u>	<u>\$4,330,010</u>	<u>\$6,983,631</u>

Auditors' Report

To the Shareholders of
MSR Exploration Ltd.

We have examined the consolidated balance sheet of MSR Exploration Ltd. as at December 31, 1982 and 1981 and the consolidated statements of income and retained earnings and changes in financial position for each of the three years ended December 31, 1982. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1982 and 1981 and the results of its operations and the changes in its financial position for each of the three years ended December 31, 1982 in accordance with generally accepted accounting principles applied on a consistent basis.

Calgary, Alberta
March 25, 1983

Therese Riddell
Chartered Accountants

Notes to Consolidated Financial Statements

Years Ended December 31, 1982, 1981 and 1980

(Canadian dollars)

1. Amalgamation

These consolidated financial statements give effect to the amalgamation on April 29, 1981, of Mountain States Resources Ltd. ("Mountain States") and Monte Grande Exploration Limited ("Monte Grande"), both publicly-traded companies engaged in oil and gas exploration and development activities, into a new company, MSR Exploration Ltd. ("MSR" or the "Company").

Under the terms of the amalgamation the shareholders of the amalgamating companies received shares of MSR in exchange for all of their former shareholdings as follows:

	Shares of MSR
Mountain States	4,926,330
Monte Grande	2,593,467
Total	<u>7,519,797</u>

The amalgamation has been accounted for on the "pooling of interests" basis and has thus been given retroactive effect in these consolidated financial statements.

2. Accounting Policies**(a) Principles of Consolidation**

These consolidated financial statements include, with retroactive effect, the accounts of the Company, the amalgamating companies as described in note 1 and the Company's three United States subsidiary companies.

(b) Conversion of Foreign Currencies

The financial statements of the United States subsidiary companies have been translated into Canadian dollars on the following basis:

- (i) current assets and current liabilities at exchange rates prevailing at the balance sheet date;
- (ii) other assets at exchange rates in effect at dates of acquisition;
- (iii) revenue and expenses at the average rate of exchange for the year, except depletion and depreciation which are translated on the same basis as the related assets.

Net gains and losses resulting from foreign exchange translation and transactions are reflected in net income.

(c) Marketable Securities

Marketable securities are recorded at the lower of cost and quoted market value.

(d) Inventories

Inventories are recorded at the lower of cost and net realizable value.

(e) Investment in 50%-Owned Company

The investment in the 50%-owned United States company, Bearpaw Gathering System, Inc., is carried on the equity basis.

(f) Properties, Plant and Equipment

The Company follows the "full cost" method of accounting for costs related to the exploration and development of oil and gas properties. Such costs are accumulated on an area of interest basis and are depleted on the unit-of-production method, based on estimated recoverable oil and gas reserves in each area, as determined by management (with reference to independent evaluations to the extent practicable), or are written off to income if exploration activities in any area are determined to be unsuccessful. Proceeds received on disposal of properties are credited against such accumulated costs.

Notes to Consolidated Financial Statements *Continued*

Other plant and equipment are depreciated on the straight-line basis as follows:

Gas processing plants and gathering systems over five years

Other equipment over eight years

(g) Joint Venture Operations

Certain of the Company's exploration and development activities relating to oil and gas are conducted jointly with others. The accounts reflect only the Company's proportionate interest in such activities.

(h) Income Taxes

The Company reflects earnings income taxes currently payable and also income taxes deferred by claiming depletion and depreciation for income tax purposes in amounts differing from those reflected in the accounts.

(i) Per Share Amounts

Per share amounts have been calculated based on the weighted average number of common shares outstanding during each year, after giving retroactive effect to the shares issued on amalgamation. The Company's investment in 97,700 shares of its own capital stock has been excluded from the number of shares outstanding for purposes of computing per share amounts for the year ended December 31, 1982.

(j) Segmented Information

All of the Company's activities are in one business segment, oil and gas exploration, development, production and processing, and substantially all of the Company's operations are conducted in one geographical segment, the United States. Accordingly, no separate disclosure has been made of financial data by segment.

3. Investment in Bearpaw Gathering System, Inc.

	1982	1981
Shares at cost	\$120,000	\$120,000
Share in earnings (losses) since acquisition	(45,420)	2,244
	74,580	122,244
Advances	385,623	440,766
	<u>\$460,203</u>	<u>\$563,010</u>

4. Properties, Plant and Equipment

	1982	1981
Oil and gas properties		
Producing		
Gypsy Basin	\$ 5,567,549	\$ 5,170,185
Graben Coulee	3,624,834	3,373,063
Highview	1,751,113	1,410,252
Tuma Coulee	1,416,083	1,368,026
Bills Coulee	878,542	663,379
Laredo Field	416,926	401,575
West Graben Coulee	570,722	525,239
Vega Prospect, Utah	1,502,027	1,330,805
Teec Nos Pos Field, Arizona	667,727	—
	<u>16,395,523</u>	<u>14,242,524</u>

Non-producing		
Crazy Mountain	2,117,211	2,115,021
Doris Creek	856,554	856,554
Rat Creek	149,974	165,713
Galveston	91,592	91,592
	<u>3,215,331</u>	<u>3,228,880</u>
	19,610,854	17,471,404
Gas processing plants and gathering systems	3,537,999	2,236,451
Other equipment	972,000	972,000
	<u>24,120,853</u>	<u>20,679,855</u>
Less accumulated depletion and depreciation	<u>3,427,026</u>	<u>2,243,307</u>
	<u>\$20,693,827</u>	<u>\$18,436,548</u>

5. Capital Stock

- (a) The authorized capital of the Company is 20,000,000 shares without nominal or par value.
- (b) Changes in issued share capital during the two years ended December 31, 1982, are summarized below, giving retro-active effect to the amalgamation as outlined in note 1:

	Number of Shares	Amount
Balance at December 31, 1980, and April 29, 1981	7,519,797	\$12,406,679
Shares issued for cash on exercise of stock options	83,333	750,000
Balance at December 31, 1981	7,603,130	13,156,679
Shares issued		
For cash on exercise of stock options	24,000	48,000
To settle fractional share holdings resulting from amalgamation	73	—
Balance at December 31, 1982	<u>7,627,203</u>	<u>\$13,204,679</u>

- (c) During the year, the Company purchased on the open market 97,700 shares of its own capital stock for an aggregate cash consideration of \$614,202. This amount is shown as a reduction of shareholders' equity.

6. Related Party Transactions

During the year ended December 31, 1982, \$80,000 (\$115,000 in 1981, \$161,000 in 1980) was paid for engineering and geological services and rent to consulting firms controlled by directors or officers at rates commensurate with normal industry terms.

7. Remuneration of Directors and Senior Officers

Remuneration to directors and senior officers (including the five highest paid employees) of the Company for the year ended December 31, 1982, amounted to \$252,500.

Notes to Consolidated Financial Statements *Continued*

8. Income Tax Expense

The components of income tax expense are as follows:

	1982	1981	1980
Currently payable	\$ 27,285	\$ 100,282	\$ 182,813
Deferred as a result of the following timing differences:			
Exploration and development expenditures deducted for income tax purposes in excess of depletion and depreciation	521,000	1,111,891	1,298,399
Losses of Canadian companies	—	(104,000)	—
	521,000	1,007,891	1,298,399
	<u>\$548,285</u>	<u>\$1,108,173</u>	<u>\$1,481,212</u>

Substantially all of the Company's income before income taxes and extraordinary item arises in the Company's United States subsidiary companies.

Income tax expense differs from that which would result from applying the United States Federal income tax rate to income before income taxes and extraordinary item as follows:

	1982	1981	1980
United States Federal income tax rate	46.0%	46.0%	46.0%
State income tax rate	3.6	3.6	3.6
Investment credits	(14.8)	(18.8)	(4.6)
Gain on sale of marketable securities	—	(1.5)	(4.4)
Provision for decline in marketable securities	—	3.4	—
Other	(1.8)	0.6	1.8
Actual income tax expense as a percentage of income before income taxes and extraordinary items	<u>33.0%</u>	<u>33.3%</u>	<u>42.4%</u>

9. United States Accounting Principles

The accounting principles described in note 2 differ from those prescribed by the United States' Securities and Exchange Commission in that the Commission requires that the "full cost" method of accounting for costs related to the exploration and development of oil and gas properties be applied on a "country-by-country" basis.

The effects of the foregoing are summarized as follows:

(a) Consolidated Statement of Income and Retained Earnings

	1982	1981	1980
Net income as reported	\$1,112,868	\$2,217,491	\$2,119,112
Application of prescribed "full cost" method, net of related deferred income taxes	15,617	5,542	8,712
Net income under United States accounting principles	<u>\$1,128,485</u>	<u>\$2,223,033</u>	<u>\$2,127,824</u>

(b) Consolidated Balance Sheet

	As Reported	Decrease	Under United States Accounting Principles
December 31, 1982			
Property, plant and equipment	\$20,693,827	\$(870,490)	\$19,823,337
Deferred income taxes	\$ 4,014,042	\$(326,264)	\$ 3,687,778
Retained earnings	\$ 7,792,715	\$(544,226)	\$ 7,248,489
December 31, 1981			
Property, plant and equipment	\$18,436,548	\$(899,409)	\$17,537,139
Deferred income taxes	\$ 3,493,042	\$(339,566)	\$ 3,153,476
Retained earnings	\$ 6,679,847	\$(559,843)	\$ 6,120,004

10. Oil and Gas Producing Activities

(a) Capitalized Costs

	December 31,	
	1982	1981
Oil and gas properties including related gas processing plants and gathering systems		
United States	\$22,142,325	\$18,685,588
Canada	1,006,528	1,022,267
	<u>23,148,853</u>	<u>19,707,855</u>
Accumulated depletion and depreciation		
United States	3,111,937	2,075,607
Canada	108,776	79,857
	<u>3,220,713</u>	<u>2,155,464</u>
Net book value as reported	<u>19,928,140</u>	<u>17,552,391</u>
Write-off of Canadian properties in accordance with United States prescribed "full cost" method	<u>870,490</u>	<u>899,409</u>
Net book value under United States accounting principles	<u>\$19,057,650</u>	<u>\$16,652,982</u>

(b) Costs Incurred

	Year ended December 31,		
	1982	1981	1980
Property acquisition costs			
United States			
Proven	\$ 31,488	\$ 401,575	\$ 103,958
Unproven	8,356	1,544	932
Canada, unproven	<u>—</u>	<u>—</u>	<u>—</u>
	<u>\$ 39,844</u>	<u>\$403,119</u>	<u>\$104,890</u>
Exploration costs			
United States	\$808,912	\$977,136	\$702,201
Canada	(15,739)	16,209	338
	<u>\$793,173</u>	<u>\$993,345</u>	<u>\$702,539</u>

Notes to Consolidated Financial Statements *Continued*

Development costs			
United States	\$2,607,981	\$4,704,856	\$4,251,900
Canada	—	—	—
	<u>\$2,607,981</u>	<u>\$4,704,856</u>	<u>\$4,251,900</u>
Production costs			
United States	\$ 985,522	\$1,072,766	\$1,170,606
Canada	—	9,294	—
	<u>\$ 985,522</u>	<u>\$1,082,060</u>	<u>\$1,170,606</u>
Depreciation and depletion as reported			
United States	\$1,036,330	\$ 904,045	\$ 521,634
Canada	28,919	25,119	20,858
	<u>1,065,249</u>	<u>929,164</u>	<u>542,492</u>
Effect of write-off of Canadian properties in accordance with United States prescribed "full cost" method	(28,919)	(25,119)	(20,858)
Depletion, depreciation and write-offs under United States accounting principles	<u>\$1,036,330</u>	<u>\$ 904,045</u>	<u>\$ 521,634</u>

(c) Net Revenues

	Year ended December 31,		
	1982	1981	1980
Revenue, all United States	\$4,355,452	\$5,640,932	\$4,903,765
Production costs	985,522	1,082,060	1,170,606
Net revenue	<u>\$3,369,930</u>	<u>\$4,558,872</u>	<u>\$3,733,159</u>

11. Estimated Proven Oil and Gas Reserves (Unaudited)

The following information summarizes the Company's estimated quantities of proven oil and gas reserves, all of which are located in the United States, and estimated production therefrom:

(a) Estimated Proven Reserves

	Year ended December 31,					
	1982		1981		1980	
	Oil	Gas	Oil	Gas	Oil	Gas
	(000's bbls)	(MMcf)	(000's bbls)	(MMcf)	(000's bbls)	(MMcf)
Beginning of year	2,012	13,054	1,296	12,737	1,670	8,956
Revisions of previous estimates	(1,209)*	(7,646)*	—	—	(327)**	—
Purchase of reserves in place	—	—	—	1,345	—	—
Extensions, discoveries and other additions	839	8,482	784	—	—	5,112
Production	(72)	(567)	(68)	(1,028)	(47)	(1,331)
End of year	<u>1,570</u>	<u>13,323</u>	<u>2,012</u>	<u>13,054</u>	<u>1,296</u>	<u>12,737</u>

*Proven oil and gas reserves have been reduced due to early economic cut-off as a result of lower prices. Additionally, certain gas wells have had production substantially curtailed due to high line pressures.

**Due to declining reservoir pressures, necessitating secondary water flooding, 327,000 barrels of oil were transferred from proven to probable reserves.

(b) Estimated Future Net Revenues

1983	\$ 2,707,974
1984	3,743,146
1985	4,832,917
Thereafter	50,260,518
Total	<u>\$61,544,555</u>

(c) Present Value of Estimated Future Net Revenues

December 31, 1982	<u>\$30,978,307</u>
December 31, 1981	<u>\$33,571,053</u>

As prescribed by the United States Securities and Exchange Commission, future net revenues are computed by applying current prices and current costs to estimated future production, and the present value thereof is computed using a discount factor of ten percent.

12. Reserve Recognition Accounting (Unaudited)

(a) Summary of Oil and Gas Producing Activities on the Basis of "Reserve Recognition Accounting"

	Year ended December 31,		
	1982	1981	1980
Additions and revisions to estimated proven oil and gas reserves			
Additions to estimated proven reserves	\$18,411,516	\$10,945,661	\$8,779,642
Revisions to estimates of reserves proven in prior years	(16,957,879)	—	(3,499,632)
Changes in prices	(239,727)	1,387,974	(785,034)
Accretion of discount	<u>3,357,105</u>	<u>2,799,398</u>	<u>2,735,822</u>
	<u>4,571,015</u>	<u>15,133,033</u>	<u>7,230,798</u>
Acquisition, exploration and development costs			
Costs incurred	(3,236,836)*	(5,124,184)*	(4,357,128)*
Present value of estimated future development and production costs	<u>(3,793,831)</u>	<u>(4,997,093)</u>	<u>(2,861,875)</u>
	<u>(7,030,667)</u>	<u>(10,121,277)</u>	<u>(7,219,003)</u>
Additions and revisions to proven reserves over evaluated costs	(2,459,652)	5,011,756	11,795
Provision for income taxes	<u>1,285,987</u>	<u>(2,403,115)</u>	<u>27,432</u>
Results of oil and gas producing activities on the basis of "Reserve Recognition Accounting"	<u>\$ (1,173,665)</u>	<u>\$ 2,608,641</u>	<u>\$ 39,227</u>

*Costs totalling \$204,000, \$977,000 and \$702,000 in 1982, 1981 and 1980 respectively have been deferred pending evaluation of the related properties.

Notes to Consolidated Financial Statements *Continued*

(b) Changes in Present Value of Estimated Future Net Revenue From Proven Oil and Gas Reserves.

	Year ended December 31,		
	1982	1981	1980
Increases			
Additions and revisions	\$ 4,571,015	\$13,677,948	\$ 7,230,798
Less related estimated future development and production costs	(3,793,831)	(4,997,093)	(2,861,875)
Net additions and revisions	777,184	8,680,855	4,368,923
Purchase of reserves in place	—	1,455,085	—
	777,184	10,135,940	4,368,923
Decreases			
Sales of oil and gas	(3,369,930)	(4,558,872)	(3,733,159)
Net increase (decrease)	(2,592,746)	5,577,068	635,764
Beginning of year	33,571,053	27,993,985	27,358,221
End of year	\$30,978,307	\$33,571,053	\$27,993,985

13. Quarterly Financial Information (Unaudited)

The following table summarizes selected quarterly financial data for the year ended December 31, 1982:

	Three Months Ended			
	March 31	June 30	September 30	December 31
Gross revenue	\$1,514,000	\$1,369,000	\$1,313,000	\$1,186,000
Net income	\$ 396,000	\$ 228,000	\$ 471,000	\$ 18,000
Earnings per share	\$ 0.052	\$ 0.030	\$ 0.062	\$ 0.004
Working capital generated from operations per share	\$ 0.110	\$ 0.166	\$ 0.171	\$ 0.034

1. Reno Roncco, P. Eng. area superintendent Arizona and Utah.

2. Navajo "O" 12 Teec Nos Pos, Arizona.

3. Blackleaf Canyon Unit number 1-8.

BACKGROUND: Graben Coulee Field, Glacier County, Montana.

