Scurry-Rainbow Oil Limited

Annual Report 1976

Scurry-Rainbow Oil Limited

Head Office: 709 - 8th Avenue S.W., Calgary, Alberta T2P 1H5
Administrative Office: 304 - 6th Avenue S.W., Calgary, Alberta T2P 0R4

Board of Directors

ROBERT G. BLACK, Q.C., *Calgary, Alberta*
Partner in the law firm of Jones, Black & Company
Director: Calgary Power Ltd.

* RONALD B. COLEMAN, *Calgary, Alberta*
Senior Vice-President and General Counsel of Home Oil Company Limited; President and Director of Cygnus Corporation Limited

GEORGE E. CREBER, Q.C., *Toronto, Ontario*
President and Chief Executive Officer and Director of The Consumers' Gas Company;
Director: Home Oil Company Limited, Cygnus Corporation Limited, Canadian Trustco Mortgage Company, The Canada Trust Company, Rothmans of Pall Mall Canada Limited

* J. HOWARD GEDDES, *Calgary, Alberta*
Executive Vice-President and General Manager of the Company; Vice-President, Corporate Development of Home Oil Company Limited

* ANTHONY G.S. GRIFFIN, *Toronto, Ontario*
Chairman of the Boards of the Company, Home Oil Company Limited, The Commercial Life Assurance Company of Canada, The Halifax Insurance Company
Director: The Consumers' Gas Company, Canadian Corporate Management Company Limited, Canadian Industries Limited, ICI Americas Inc., Raymond International Inc., Triarch Corporation Limited, United Dominions Corporation (Canada) Limited, Victoria & Grey Trust Company, National Film Board

+* J. GORDON HUTCHISON, F.C.A., *Calgary, Alberta*
Financial Consultant
Director: Siebens Oil & Gas Ltd., Cavalier Energy Inc.

\+ HENRY E. LANGFORD, Q.C., *Toronto, Ontario*
Corporate Director
Director: Home Oil Company Limited, The Consumers' Gas Company, The Dominion of Canada General Insurance Company, Victoria & Grey Trust Company, The Empire Life Insurance Company, E.L. Financial Corporation

\+ JOHN F. LANGSTON, *Calgary, Alberta*
Petroleum Engineer

MAURICE P. PAULSON, *Calgary, Alberta*
Executive Vice-President and General Manager and Director of Home Oil Company Limited

* ROSS F. PHILLIPS, *Calgary, Alberta*
President and Chief Executive Officer and Director of Home Oil Company Limited and the Company
Director: The Consumers' Gas Company, Calgary Power Ltd., Crown Trust Company

* Member of Executive Committee
\+ Member of Audit Committee

Executive Officers

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Chairman of the Board

R. F. PHILLIPS,
President

J. H. GEDDES,
Executive Vice-President and General Manager

R. B. COLEMAN,
Vice-President

F.C. FINN,
Vice-President, Mining Division

R.I. SMITH,
Vice-President, Petroleum Division

C. B. CLARK,
Secretary

D. E. DEAKIN,
Treasurer

E. JORGENSEN,
Comptroller

F. G. MITCHELL,
Assistant-Secretary

J.A. PETTY,
Assistant-Treasurer

Registrar & Transfer Agents

Guaranty Trust Company of Canada, Calgary, Alberta; Toronto, Ontario; Montreal, P.Q.; Vancouver, B.C.
The Canadian Bank of Commerce Trust Company, New York, N.Y.

Stock Listings

Toronto Stock Exchange
Vancouver Stock Exchange
American Stock Exchange

Annual Meeting

The Annual Meeting of shareholders will be held on Tuesday, February 8, 1977 at 11:00 a.m. at the head office of the Company in Calgary, Alberta. Formal notice of this meeting and proxy material has been mailed to all registered shareholders with this report.

The Company files annually with the United States Securities and Exchange Commission, a report on its operations known as the Annual Report on Form 10-K. Copies of this SEC Form 10-K are available free of charge upon written request to: E. Jorgensen, Comptroller, Scurry-Rainbow Oil Limited, 304 - 6th Avenue S.W., Calgary, Alberta T2P 0R4.

TO THE SHAREHOLDERS

During the fiscal year ended September 30, 1976, the Company achieved substantial improvements in revenues, cash flow and earnings. Expenditures on exploration and development for both petroleum and mining projects, aggregating in excess of $12 million, were the highest in the Company's history, and were incurred in conducting activities not only in Canada but also in the United States and the North Sea.

The Company's mining activities were broadened through the acquisition of the partially developed Gooseberry gold-silver mine in Nevada, which should commence production in the spring of 1977. Subsequent to year end, the Company reduced its interest in the Elk River Valley coal properties in British Columbia to a level more in keeping with its financial capabilities by selling a 40% interest out of its 50% interest. The Company retained a 10% working interest in these coal properties and a royalty on coal produced from the interest sold. In Mexico construction delays, start-up problems and flooding of the Santa Rita silver mine delayed the achievement of full-scale production. With resolution of these problems, full-scale production should commence early in 1977.

A new Alberta Coal Policy was issued in June, 1976. This policy governs all coal mining activities within the Province, including the Company's Blairmore coal properties. The regulations through which this policy will be administered are still being reviewed and further development work on our Alberta coal properties is being curtailed until this review is completed. Under the policy, royalties on coal produced will increase substantially. In addition, the policy divides the Province into areas according to permitted levels of exploration and development. The policy imposes a complete ban on activity in environmentally sensitive areas while permitting commercial development in historical coal mining areas and on the Plains. The Company's major coal properties in Alberta fall within areas where commercial development is permitted but some of its smaller coal properties are situated in the areas designated for no exploration and/or development. No plans have been developed as yet with respect to these restricted properties.

During the year the Company participated in a significant oil discovery on Block 3/7, in which we have a 20% interest, in the U.K. sector of the North Sea. A second successful well was drilled on the same block after the fiscal year end. Additional exploratory and delineation drilling will be required to evaluate these discoveries and to plan potential commercial development on the Block.

The increases during the year in the selling prices of crude oil and natural gas, coupled with the more moderate approach taken by the various levels of Canadian governments with respect to royalties and resource taxation, have enhanced the after-tax return to companies within the industry and provided an economic climate more conducive to exploration. The Company intends to respond to improved incentives by expanding its domestic exploration program in 1977.

Effective for fiscal periods commencing after September 30, 1976 the Company has changed its fiscal year end to December 31 to simplify its reporting procedures within the industry. As a result, the next Annual Report will cover the 15 month period October 1, 1976 to December 31, 1977.

Mr. H.E. Langford, Q.C. will be retiring from the Board at this year's annual meeting. The Board has appreciated the valuable contributions he has made during his service as a Director and as a member of the Audit Committee. To replace Mr. Langford, Mr. J.D. Gibson, O.B.E. will be nominated.

The Board also wishes to commend the employees for their dedicated efforts and to thank them for their support during the past year.

On Behalf of the Board

November 30, 1976

A.G.S. Griffin
Chairman of the Board

R.F. Phillips
President

EXPLORATION AND DEVELOPMENT

During fiscal 1976 Scurry-Rainbow continued its active exploration program in Canada, the United States and in both the United Kingdom and Netherlands sectors of the North Sea. The Company participated in the drilling of 52 wells resulting in 11 oil wells and 13 natural gas wells. At year end, 10 additional wells were still drilling.

CANADA

Alberta

The Company drilled a Basal Blairmore oil discovery on 100% Scurry-Rainbow interest acreage at Arrowwood in southeastern Alberta. Three wells were drilled offsetting this discovery, one of which was successful. In the Retlaw area the Company participated in four wells, resulting in two gas wells and two oil wells. Drilling in the Marten Hills area of central Alberta was postponed pending the results of an extensive production testing program completed last winter, but further drilling is planned in 1977.

In the Coleman area of southwestern Alberta the Company is participating in a 16,000' well designed to increase the deliverability of natural gas from the Coleman pool and to evaluate the potential of a deeper Paleozoic thrust sheet. Spudded July 14, 1976, this well was drilling below 7,900' at year end. Scurry-Rainbow and Plains Petroleums Limited, a 70% owned subsidiary, have interests of 8.17% and 9.05% respectively in this project.

British Columbia

An active exploration and development program is currently in progress in the Cecil Lake-Eagle area resulting thus far in two new oil pool discoveries.

A development well to further evaluate the oil potential in the North Pine Sandstone at Cecil Lake was drilled but was dry and abandoned. Subsequently, approval in principle was received from the British Columbia regulatory authorities for concurrent production of oil and natural gas from the North Pine Sandstone "A" pool and negotiations toward unitization of this pool are currently in progress. The Company has approximately a 53% interest in this project, which is expected to have a daily production rate of approximately 5.0 MMcf of natural gas and 20 barrels of oil.

Saskatchewan

The Company has a 50% working interest in the Winnipegosis oil discovery drilled on the Tableland prospect near Estevan, which is currently producing approximately 35 barrels per day. There are no immediate plans for development as the field appears to be of limited areal extent and is producing water.

Arctic Islands

Scurry-Rainbow participated to the extent of a 10% working interest in the recently drilled Panarctic Key Point 0-51 exploratory well on Vanier Island and has earned an interest in the Key Point prospect. While the initial well was dry and abandoned, sufficient encouragement was obtained from this well to warrant further drilling on this prospect.

Recent seismic activity has confirmed the presence of a large structure on Melville Island partially located on acreage in which the Company holds an 11% interest. Panarctic has indicated an exploratory well will be drilled on this structure during the spring of 1977.

UNITED STATES

Wyoming

A seismic program has indicated the need for further exploratory work in the south Ash Creek area of the Powder River Basin where the Company holds an interest in over 70,000 acres. Farmin negotiations are currently in progress and drilling operations should commence before the end of the calendar year.

Scurry-Rainbow is being carried in a five-well exploratory drilling program in the Oedekoven area, Powder River Basin. Three exploratory wells have been drilled resulting in two Muddy Sandstone oil discoveries. Unfortunately, development drilling has been unsuccessful.

A well to evaluate the Cretaceous potential of the Packsaddle prospect, Green River Basin was abandoned at a total depth of 9,868'. The Company is continuing exploration in the Green River Basin; currently a limited in-fill seismic program and land acquisition is centered on a deep, multizone prospect which may be drilled in 1977.

North Dakota

Scurry-Rainbow is being carried in a twelve-well exploration drilling program in North Dakota. By the end of fiscal 1976 six wells had been drilled, all being abandoned. This program will be completed in 1977.

Utah

To further evaluate the Mississippian and Devonian potential of the Company's acreage in the Paradox Basin, a 9,200' exploratory well in which Scurry-Rainbow has a 12½% interest was spudded September 30, 1976 and is still drilling.

UNITED KINGDOM OFFSHORE

Scurry-Rainbow participated (20%) in the drilling of the 3/7-1 well southwest of the Ninian Field. This well flowed oil at rates up to 3,100 barrels per day from the Middle Jurassic Sandstone reservoir. Subsequently, the Company participated (10%) in a line well, 3/7-2, in which costs were shared equally with the owners of the neighbouring block to the north. This well, located to evaluate the West Ninian Fault block, flowed oil at rates up to 3,300 barrels per day from the Middle Jurassic reservoir.

Continuing exploration is currently in progress on this Block 3/7. A 1,200 mile seismic detailing program covering prospects in the northwest quarter and south half of the Block was commenced in November, 1976. Leads evaluated by the seismic data and drilling to date will probably justify further exploratory drilling in 1977.

The Company has a 16.66% interest in a group which made application for certain blocks being offered in the United Kingdom Fifth Round.

NETHERLANDS OFFSHORE

During 1976, the Company participated (2.5%) in one well, F/15-1, which was dry and abandoned. Plans are being made to drill a third well on the B/17 block to test the Danian potential. It is expected that one additional Danian test and a second well on the P/15 block will be drilled in 1977.

PRODUCTION

Production of crude oil and natural gas liquids in the fiscal year 1975-76 declined by a total of 367,255 bbls. to 2,281,826 bbls. or 6,234 bbls. per day. Natural gas production increased to 6,161,871 Mcf or 16,836 Mcf per day compared to 5,258,231 Mcf or 14,406 Mcf per day in fiscal 1975.

The Company's production of crude oil in western Canada decreased because of natural decline as well as from proration resulting from Government curtailment of exports.

Crude Oil and Natural Gas Liquids Production (barrels)	**1976**	**1975**
Alberta	772,420	968,151
British Columbia	517,649	537,225
Saskatchewan	920,384	1,077,768
Manitoba	64,578	61,058
United States	6,795	4,879
Barrels for the year	2,281,826	2,649,081
Average per day	6,234	7,258

Natural Gas Production (Mcf.)		
Alberta	5,454,310	5,144,919
British Columbia	672,142	113,312
Saskatchewan	26,023	—
United States	9,396	—
Mcf. for the year	6,161,871	5,258,231
Average per day	16,836	14,406

Sales Revenue		
Crude oil and natural gas liquids	$10,854,950	$10,081,540
Natural gas	4,745,627	2,718,413
Sulphur	168,063	208,509
Potash and Coal	57,714	61,617
Total sales revenue	$15,826,354	$13,070,079

PROVEN DEVELOPED RESERVES
(Before Deduction of Royalties and After Minority Interests)
As at September 30

	1976		1975	
	Working Interest	Royalty Interest	Working Interest	Royalty Interest
Crude Oil and Natural Gas Liquids — barrels	16,631,000	2,222,000	18,412,000	1,942,000
Natural Gas — Mcf	122,440,000	23,206,000	129,996,000	23,372,000
Sulphur — Long tons	829,000	19,000	800,000	12,000

MINING

Coal

The preliminary evaluation of the Elk River Valley, British Columbia property, which is located approximately 40 miles north of the Kaiser properties at Sparwood and approximately 18 miles north of the town of Elkford, was concluded. Scurry-Rainbow sold a 25% interest in the project to The Steel Company of Canada for a consideration of $2,000,000 payable $1,000,000 upon transfer and registration of the licenses, $500,000 on October 4, 1977 and $500,000 on October 4, 1978, plus a 5% overriding royalty on the F.O.R. value of Stelco's share of the coal produced. In addition, Stelco reimbursed the Company for 50% of its expenditures on the property since June, 1975. A 15% interest in the project was also sold to Home Oil Company Limited on the same proportionate terms. Participants in the project now are Elco Mining Ltd., representing a consortium of European steel and coal companies, 50%; The Steel Company of Canada, 25%; Home Oil Company Limited, 15% and Scurry-Rainbow, 10%. Elco Mining Ltd. has been designated operator of the project. The project has now moved into the preliminary planning phase which will continue through February, 1978 during which time an estimated $10.8 million will be expended. At the conclusion of this phase a decision will be made on whether or not to proceed with a commercial open pit mine capable of producing 4 million short tons per year of metallurgical coal commencing in 1982.

There was little activity on the Company's Blairmore, Alberta coal properties, jointly owned with the operator Consolidation Coal, during the year pending the issuance of the Alberta Coal Policy. In December of 1975 an application was submitted to the Energy Resources Conservation Board requesting permission to operate a small open pit mine on Grassy Mountain producing 500,000 tons of raw coal per year, to be processed through the Coleman Collieries preparation plant. Further information requested by the Board has been filed and the decision on the application is still awaited. In the meantime, the Alberta Coal Policy which was issued in June, 1976 is being studied and the economics of the development of these Alberta coal properties are being re-evaluated in the light of this new policy. Field work was conducted on other coal properties in Canada and elsewhere and this work will be evaluated early in 1977.

Potash

The Company has granted a one year extension, with a right to renew for an additional year, on the option to the Potash Corporation of Saskatchewan to acquire the Company's prospective potash land holdings and royalty interests.

Metallics

Late in the year a partially developed gold-silver property near Reno, Nevada, known as the Gooseberry Mine, was acquired. This mine had extensive underground exploration completed and a mill with a design capacity of 350 tons of ore per day and other surface installations were partially constructed. The Company has undertaken to complete this pre-production work and place the mine on full production, which is expected to take place in the fall of 1977.

At the Company's Santa-Rita silver-lead-zinc mine in the State of Zacatecas, Mexico, construction of an antimony plant was completed and the first antimony metal was produced. However, start-up problems have prevented us reaching continuous full-scale operation. Unprecedented heavy rainfalls in the area altered the quality of the water supply used in processing the ore and caused severe flooding in the mine. A delay in construction of a supplementary power line to the mine site has also delayed operations, and has necessitated further expenditure on stand-by power generation facilities. The Mexican Power Commission has indicated that the power line will be completed by the end of January, 1977. If this should come about and the flooding can be brought under control, full-scale production should re-commence shortly thereafter.

Mineral exploration programs were conducted in a number of areas in Canada, with the results to be evaluated early in 1977. Further work will be undertaken in the summer of 1977 on those properties with potential and the acquisition of new properties is contemplated.

Mining Acreage	Gross	Net
Coal mining properties	108,664	99,064
Potash leases	83,238	83,238
Mining claims	94,793	69,900
	286,695	252,202
Canada		
Alberta	89,464	89,464
British Columbia	34,786	14,971
Saskatchewan	131,632	131,536
Northwest Territories	5,674	5,674
Yukon	13,980	1,398
Foreign	11,159	9,159
Total acreage at Sept. 30, 1976	286,695	252,202
Total acreage at Sept. 30, 1975	254,265	219,772

OIL AND GAS ACREAGE

	Gross Acres	Net Working Interests	Net Mineral Interests	Net Royalty Interests
Oil sands leases (Athabasca)	274,822	16,489	—	—
Petroleum and natural gas leases	2,575,638	1,051,259	—	—
Gross overriding royalties on leases	148,652	—	—	31,989
Reservations, licenses and permits	4,455,042	738,773	—	—
Oil and gas titles	1,120	—	600	—
Gross royalties in freehold land	302,779	—	—	60,656
Mineral titles and mineral leases	1,034,689	—	642,327	—
	8,792,742	1,806,521	642,927	92,645
Western Canada				
Alberta	1,740,097	466,844	11,814	86,741
British Columbia	700,480	83,907	—	4,257
Saskatchewan (1)	1,203,946	126,916	603,839	1,382
Manitoba	38,472	1,190	27,274	265
Northern Canada				
Arctic Islands	1,073,114	111,146	—	—
Northwest Territories	1,297,022	347,079	—	—
Eastern Canada				
Ontario	1,334	800	—	—
Quebec	318,750	117,938	—	—
Nova Scotia	80,640	80,640	—	—
Total Canadian acreage	6,453,855	1,336,460	642,927	92,645
United States				
Alaska	383,254	293,846	—	—
North Dakota	232,412	77,348	—	—
Utah	73,729	8,974	—	—
Wyoming	391,523	48,005	—	—
Montana	984	143	—	—
Michigan	6,959	1,740	—	—
United Kingdom				
Offshore	50,026	10,005	—	—
Netherlands				
Offshore	1,200,000	30,000	—	—
Total acreage at September 30, 1976	8,792,742	1,806,521	642,927	92,645
Total acreage at September 30, 1975	9,460,130	1,839,335	642,927	93,881

(1) Excludes 938,036 gross acres (791,058 net acres) of mineral interests which the Company has offered to surrender to the Provincial Government but which offers have not as yet been officially accepted by the Crown.

FINANCIAL REVIEW

Gross revenues after royalties amounted to $17,011,000, an increase of 24% from the $13,727,000 in 1975. Higher sales prices received for natural gas and products together with the commencement of production from the Coleman gas unit in November, 1975 were the principal reasons for the increase in gross revenues. The decline in oil production rates was more than offset by improved sales prices of this product.

Net earnings were $4,771,000 or $1.80 per share, up 60% from the $2,978,000 or $1.12 per share last year. This improvement reflects the increased revenues, partially offset by increased operating expenses, depletion charges and write-off of mining properties, and the inclusion of $363,000 in investment income related to the advances made to a Mexican company as described below. Net cash flow from operations, at $8,981,000, was up 33% from the $6,776,000 for the previous year.

The Company's capital expenditure program for 1976 totalled $12,566,000, consisting of petroleum and natural gas exploration expenditures of $4,913,000, development expenditures of $1,491,000, mining expenditures of $6,065,000 and other capital expenditures of $97,000. The major expenditure in the mining operations was the acquisition and development costs associated with the partially developed Gooseberry mine in Nevada which costs aggregated $4,168,000 at year end. It is estimated that a further $4.5 million will be required to complete the development of this mine.

During the year, the Company completed certain transactions which improved its working capital position. Property, and miscellaneous investments in marketable securities were disposed of for proceeds aggregating $537,000 resulting in a net gain of $330,000. In addition, advances aggregating $5,444,000 made to Minerales Santa Rita S.A. de C.V., a 49% owned Mexican company, to finance development of the mine in Mexico, together with interest to the date of repayment, were repaid to the Company out of the proceeds of a loan taken by the Mexican company from a Canadian chartered bank. The Company has guaranteed the repayment of this bank loan to a maximum of $6,500,000 (U.S.), which is repayable over four years.

The Company purchased for sinking fund purposes an aggregate of $1,487,000 principal amount of its 7¼% Convertible Subordinated Debentures at a cost of $1,219,000, resulting in a gain of $268,000. When these were added to the $197,000 principal amount of converted debentures on hand after the November 1, 1975 sinking fund, the Company was able to satisfy the November 1, 1976 sinking fund of $1,067,000 and the balance of $617,000 is available to apply against future sinking fund payments.

The investment in the subsidiary Plains Petroleums Limited was increased through the acquisition of 847,570 shares pursuant to an open order at 20¢ per share. In addition, the holdings of this subsidiary were consolidated when Scurry-Rainbow Oil Limited purchased the 3,979,050 shares previously held by two other subsidiary companies, also at 20¢ per share. As a result, the ownership of this subsidiary amounted to 70% at year end.

FIVE YEAR SUMMARY OF OPERATIONS

	1976	1975	1974	1973	1972
Revenue	$17,011,000	$13,727,000	$12,265,000	$ 9,917,000	$ 8,613,000
Expenses					
Operating, general, and administrative expense and minority interest...............	4,607,000	3,725,000	2,751,000	2,428,000	2,388,000
Depletion and depreciation	3,768,000	3,529,000	4,301,000	4,364,000	4,326,000
Mining properties abandoned	522,000	203,000	602,000	672,000	117,000
Interest expense ...	1,168,000	1,230,000	1,338,000	1,350,000	1,357,000
	10,065,000	8,687,000	8,992,000	8,814,000	8,188,000
Net earnings before the following	6,946,000	5,040,000	3,273,000	1,103,000	425,000
Other credits (charges)	598,000	1,219,000	(7,933,000)	228,000	(119,000)
Net earnings (loss) before provision for income taxes ..	7,544,000	6,259,000	(4,660,000)	1,331,000	306,000
Provision for income taxes	2,773,000	3,281,000	382,000	1,070,000	608,000
Net earnings (loss) ...	$ 4,771,000	$ 2,978,000	$(5,042,000)	$ 261,000	$ (302,000)

Increased revenues in 1973 and 1974 were mainly attributable to higher sales prices for crude oil and natural gas and related products, combined with a marginal increase in production volumes in 1973 and decreased production in 1974.

Revenues for 1975 increased primarily as a result of increased natural gas prices. The increase in the price of crude oil did not wholly compensate for the decline in production of this product since a large portion (40%) of the crude oil production is in Saskatchewan where two-thirds of the price increases were taken by the Provincial Government.

Higher sales prices for crude oil during 1976 increased revenue despite higher Crown royalties and decreased production. Gas revenues increased significantly during the year as production from the Coleman area came on-stream in November, 1975, coupled with higher prices.

In 1972 and 1973, the Company recorded other credits (charges) relating to gains or losses realized on the sale of capital assets.

Other credits (charges) for the year 1974 relate to changes in accounting policies, the write-down of an investment in an associated company and certain remuneration costs to former employees. In 1975, the other credits (charges) represent realized gains on the disposal of capital assets, the write-down of certain of its securities and additional special compensation expenses to former employees. The Company, in 1976, recorded credits relating to gains on the sale of capital assets and the purchase of 7¼% Convertible Subordinated Debentures.

Income taxes in 1975 incorporate the effects of 1974 income tax amendments for a whole year coupled with the tax effects on other credits. The 1974 taxes include the 1974 income tax amendments which for the most part were effective on May 6, 1974.

Additional information relating to the above items is contained in the Directors' report to the shareholders, the financial and production reviews, the Five Years at a Glance and in the notes to the consolidated financial statements.

The following table shows the percentage of gross revenue contributed by the two major sources during each of the five years ended September 30, 1976:

	1976	1975	1974	1973	1972
Crude oil..................	60.78%	68.59%	77.68%	81.93%	84.28%
Natural gas and related products...............	31.90%	26.18%	15.69%	12.71%	12.56%

The Company produces crude oil, natural gas and other products principally as a result of one integrated operation. Frequently these products are produced jointly. Accordingly, it is not possible to allocate expenses to revenues generated by product in order to determine the contribution to net earnings by individual product line.

AUDITORS' REPORT

To the Shareholders of
Scurry-Rainbow Oil Limited:

We have examined the consolidated balance sheets of Scurry-Rainbow Oil Limited and subsidiary companies as at September 30, 1976 and 1975 and the consolidated statements of earnings, retained earnings and changes in financial position for the years then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion these consolidated financial statements present fairly the financial position of the companies as at September 30, 1976 and 1975 and the results of their operations and the changes in their financial position for the years then ended, in accordance with generally accepted accounting principles consistently applied.

Calgary, Alberta
November 19, 1976

PRICE WATERHOUSE & CO.
Chartered Accountants

CONSOLIDATED STATEMENTS OF EARNINGS

	Year Ended September 30 1976	1975
Sales, less royalties	$13,852,000	$11,297,000
Royalty income	1,974,000	1,773,000
Investment income	1,125,000	407,000
Other income	60,000	250,000
	17,011,000	13,727,000
Production expenses	3,171,000	2,267,000
Administrative and general expenses	1,208,000	1,282,000
Interest on long-term debt	1,168,000	1,230,000
Depletion and depreciation	3,768,000	3,529,000
Mining properties abandoned	522,000	203,000
Amortization of deferred charges	59,000	143,000
Minority interests	169,000	33,000
	10,065,000	8,687,000
Earnings before the following	6,946,000	5,040,000
Other items:		
Gain on sale of capital assets	330,000	1,619,000
Write down of non-current marketable securities	—	(105,000)
Gain on redemption of long-term debt	268,000	—
Special compensation to officers and employees	—	(295,000)
	598,000	1,219,000
Earnings before provision for income taxes	7,544,000	6,259,000
Provision for income taxes (Note 4)		
Current	2,598,000	1,885,000
Deferred	175,000	1,396,000
	2,773,000	3,281,000
Net earnings for the year	$ 4,771,000	$ 2,978,000
Net earnings per share	$ 1.80	$ 1.12

CONSOLIDATED STATEMENTS OF RETAINED EARNINGS

	Year ended September 30 1976	1975
Balance, at beginning of year	$ 2,995,000	$ 17,000
Net earnings	4,771,000	2,978,000
Balance, at end of year	$ 7,766,000	$ 2,995,000

Scurry-Rainbow Oil Limited and Subsidiary Companies

CONSOLIDATED BALANCE SHEETS

Assets

	September 30 1976	1975
Current assets:		
Cash and short-term deposits	$10,859,000	$10,179,000
Government bonds, at cost	—	96,000
Accounts receivable	2,696,000	2,867,000
Inventory of materials and supplies, at lower of cost or estimated realizable value	232,000	372,000
Prepaid expenses	123,000	220,000
	13,910,000	13,734,000
Investments and other assets:		
Investments —		
Shares of Minerals Ltd. — 50% owned	1,150,000	1,105,000
Shares of Minerales Santa Rita S.A. de C.V. — 49% owned (Note 2)	155,000	310,000
Securities of other companies at lower of cost or estimated realizable value	204,000	220,000
Advances repayable from production (Note 2)	245,000	4,064,000
Deposits and advances	249,000	227,000
	2,003,000	5,926,000
Capital assets, at cost:		
Petroleum and natural gas and other mineral interests	81,012,000	75,115,000
Less: Accumulated depletion	(37,694,000)	(34,452,000)
Production equipment, buildings and other equipment	10,948,000	10,651,000
Less: Accumulated depreciation	(6,545,000)	(6,190,000)
Mining properties, non-producing	11,004,000	5,461,000
Land	45,000	83,000
	58,770,000	50,668,000
Deferred charges:		
Debenture issue costs, less amortization	307,000	366,000
Other charges	43,000	135,000
	350,000	501,000
	$75,033,000	$70,829,000

Liabilities

	September 30 1976	1975
Current liabilities:		
Accounts payable and accrued liabilities	$ 3,912,000	$ 3,140,000
Accrued interest	445,000	502,000
Income taxes payable	1,127,000	1,581,000
Due to parent company — Home Oil Company Limited	198,000	188,000
Long-term debt due within one year	275,000	24,000
	5,957,000	5,435,000
Long-term debt:		
Instalment purchase agreement due July 1, 1978	500,000	—
Non-interest bearing advances under exploration agreement due October 1, 1979	381,000	381,000
Non-interest bearing agreement, due July 23, 1990 repayable $25,000 U.S. per annum	337,000	362,000
7¼% convertible subordinated debentures due May 1, 1988 (Note 3)	15,115,000	16,602,000
	16,333,000	17,345,000
Less: Amounts due within one year	275,000	24,000
	16,058,000	17,321,000
Accumulated tax reduction applicable to future years (Note 4)	11,822,000	11,646,000
Minority interests in subsidiary companies	1,736,000	1,738,000
Shareholders' equity (Note 5):		
Share capital		
Authorized — 7,500,000 shares par value $3.50 each		
Issued — 2,647,921 shares	9,268,000	9,268,000
Contributed surplus	22,426,000	22,426,000
Retained earnings	7,766,000	2,995,000
	39,460,000	34,689,000
Contingent liabilities (Note 7)		
	$75,033,000	$70,829,000

APPROVED BY THE BOARD:

[signature] Director

[signature] Director

CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION

	Year Ended September 30 1976	1975
Funds were obtained from:		
Net earnings	$ 4,771,000	$ 2,978,000
Adjustments for non-cash items not requiring an outlay of funds	4,210,000	3,798,000
Funds derived from operations	8,981,000	6,776,000
Sale of capital assets	474,000	3,926,000
Repayment of advances by Minerales Santa Rita S.A. de C.V.	5,444,000	—
Dividend received from Minerals Ltd.	—	500,000
Other	63,000	—
	14,962,000	11,202,000
Funds were used for:		
Expenditures for capital assets	12,566,000	5,199,000
Investment in and advances to Minerales Santa Rita S.A. de C.V.	1,470,000	2,246,000
Retirement of long-term debt - net	995,000	444,000
Acquisition of additional shares in subsidiary companies	175,000	645,000
Other	102,000	185,000
	15,308,000	8,719,000
Increase (decrease) in working capital	(346,000)	2,483,000
Working capital at beginning of year	8,299,000	5,816,000
Working capital at end of year	$ 7,953,000	$ 8,299,000
Changes in components of working capital:		
Increase (decrease) in current assets:		
Cash	$ 680,000	$ 4,600,000
Government bonds	(96,000)	—
Accounts receivable	(171,000)	(200,000)
Inventories	(140,000)	(106,000)
Prepaid expenses	(97,000)	204,000
Net increase in current assets	176,000	4,498,000
Increase (decrease) in current liabilities:		
Accounts payable and accrued liabilities	772,000	23,000
Accrued interest	(57,000)	—
Income taxes payable	(454,000)	1,885,000
Due to parent company	10,000	188,000
Long-term debt due within one year	251,000	(81,000)
Net increase in current liabilities	522,000	2,015,000
Increase (decrease) in working capital	$ (346,000)	$ 2,483,000

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

September 30, 1976

1. Accounting policies —

The accounting policies presently followed by the companies are outlined hereunder.

(a) Principles of consolidation —

(i) The consolidated financial statements include the accounts of all subsidiaries. The Company's principal subsidiaries are Scurry-Rainbow Oil (Sask) Ltd. which is 95.4% owned and Plains Petroleums Limited which is 70.0% owned. The other subsidiaries are Williams Creek Exploration Ltd., The Winnipeg Western Land Corporation Limited, Scurry-Rainbow (International) Limited, Scurry-Rainbow (Bolivia) Limited. Scurry-Rainbow (U.K.) Limited and Westcoast Oil & Gas Corp.

The excess of the cost of shares in subsidiaries over their underlying book value at dates of acquisition has been applied to petroleum and natural gas and other mineral interests and depletion is provided thereon.

(ii) The investments in Minerals Ltd. and Minerales Santa Rita S.A. de C.V. are accounted for by the equity method. Under this method the investments are carried on the balance sheet at cost adjusted for the Company's share of undistributed earnings since acquisition less depletion of the related excess of the investments over the underlying book values at dates of acquisition. The Company's share of the net income, after deduction of a yearly provision for depletion of excess cost, is included in "Investment Income" in the Consolidated Statement of Earnings.

(iii) Current assets and liabilities of foreign subsidiaries are converted to Canadian dollars using the exchange rate at the date of the balance sheet. Other assets and liabilities are converted at historic rates. Revenue and expense items are converted using the average rates of exchange throughout the period except for items such as depletion and depreciation for which historic rates are applicable.

(b) Petroleum and natural gas and other mineral interests —

The companies follow the full cost method of accounting for petroleum, natural gas and other mineral interests whereby all costs of exploring for and developing oil, natural gas and other mineral reserves within the same properties, including exploration overhead, are capitalized whether productive or unproductive. Proceeds on disposal of properties are ordinarily deducted from costs without recognition of profit or loss. The costs are accumulated in two cost centres — North America and Northwestern Europe.

Costs accumulated in the North America cost centre are depleted by the unit of production method based on the total estimated proven reserves of oil, gas and gas by-products and indicated potash royalty reserves within the cost centre.

Costs accumulated in the Northwestern Europe cost centre are amortized by the straight-line method over a ten-year period. Under this policy, should exploration in the area prove successful the unamortized balance in the cost centre will be depleted by the unit of production method. Should production not be obtained in the area the unamortized balance in the cost centre will be written off to income (included in depletion).

(c) Mining properties —

The costs of mining properties, consisting of coal properties, potash leases and other mining claims (none of which is yet in production), include acquisition and carrying costs, exploration costs, preliminary development expenditures and exploration overhead. Costs applicable to any particular area are written off when there is little prospect of further work being carried out by the Company or its partners; costs applicable to areas which prove to be productive will be depleted on the unit of production basis. Proceeds on partial disposal of properties are ordinarily deducted from the related costs without recognition of profit or loss.

(d) Depreciation —

Depreciation is based on the estimated service life of assets, calculated by the straight-line method.

(e) Income Taxes —

The companies follow the tax allocation method of accounting for all timing differences between taxable income and recorded income including differences relative to exploration and development expenditures. Under this method, provisions for deferred income taxes are made currently on the excess of deductions claimed for tax purposes over the related depletion, depreciation and other charges recorded in the accounts.

(f) Earnings per share —

Earnings per share are calculated on the weighted average number of shares of the Company outstanding during the year. The conversion of outstanding convertible debentures would not be dilutive.

2. Investments and advances —

The investment in Minerales Santa Rita S.A. de C.V. represents the cost of a 49% equity interest in a Mexican company incorporated to explore and develop a silver-lead-zinc-antimony property in Mexico. The property is in the preproduction stage and all exploration and development expenditures are being capitalized. Liabilities, consisting primarily of a bank loan, total $6,725,000 (See Note 7).

Advances repayable from production represent $245,000 advanced to certain Mexican nationals to enable them to purchase the remaining 51% equity interest in the Mexican company. The $245,000 is recoverable, with interest, out of any dividends attaching to the shares representing the 51% equity interest. No such dividends may be declared by Minerales Santa Rita S.A. de C.V. until a bank loan, which was taken out by the Mexican company for the purpose of repaying the amounts advanced by Scurry-Rainbow Oil Limited, has been repaid.

It is anticipated that substantially all of the sales contracts will be in U.S. dollars. Therefore the recent devaluation of the Mexican peso should have no material adverse effect on the operations of the Company.

3. Long-term debt —

The 7¼% convertible subordinated debentures are convertible into shares of the Company at any time before May 1, 1978 at $33⅓ per share and are subject to sinking fund requirements of $1,067,000 annually on November 1 until 1987 inclusive. Debentures converted or repurchased may be applied by the Company against its sinking fund obligations. The aggregate of debentures converted or repurchased to September 30, 1976 satisfy the November 1, 1976 instalment, leaving a balance of $617,000 to apply against future sinking fund payments.

The estimated amount of long-term debt maturities and remaining sinking fund requirements for the five fiscal years subsequent to 1976 are as follows: 1977 - $275,000; 1978 - $724,000; 1979 - $1,091,000; 1980 - $1,472,000; 1981 - $1,091,000.

4. Income taxes —

Total income tax expense amounted to $2,773,000 in 1976 and $3,281,000 in 1975. These amounts differ from the expected tax of $3,546,000 in 1976 and $3,192,000 in 1975 which would result from applying the Canadian income tax rate of 47% in 1976 and 51% in 1975 to pretax earnings of $7,544,000 in 1976 and $6,259,000 in 1975. These differences result from the following items:

	1976		1975	
	Amount	Percentage of Pretax Income	Amount	Percentage of Pretax Income
Computed "expected" tax expense	$3,546,000	47.0%	$3,192,000	51.0%
Increases (reductions) in taxes resulting from:				
Non-deductible acquisition costs of mining and oil and gas properties	507,000	6.7	359,000	5.7
Non-deductible government royalties and similar payments	2,982,000	39.5	2,345,000	37.4
Non-taxable portion of gains on disposal of capital assets	(218,000)	(2.9)	(114,000)	(1.8)
Other	(3,000)	—	532,000	8.5
Refund of taxes under provincial incentive plans	(1,163,000)	(15.4)	(1,396,000)	(22.3)
Statutory depletion allowances	(1,365,000)	(18.1)	(899,000)	(14.4)
Resource allowance	(1,513,000)	(20.1)	—	—
Resource profits abatement	—	—	(738,000)	(11.7)
	$2,773,000	36.7%	$3,281,000	52.4%

5. Shareholders' equity —

As of September 30, 1976, the Company had 453,450 shares reserved for issuance upon conversion of the 7¼% convertible subordinated debentures. The Trust Indenture under which the 7¼% convertible subordinated debentures have been issued contains certain dividend restrictions providing essentially that dividends may be paid only to the extent of the aggregate of the consolidated earnings accumulated subsequent to January 31, 1968 and the net consideration received from the issue of the Company's shares after January 31, 1968. Under these restrictions the amount available for distribution as dividends is in excess of the retained earnings at September 30, 1976.

6. Remuneration of directors and senior officers —

During 1976 the Company and its subsidiaries paid as direct remuneration to the Company's directors and senior officers the following:

	1976	1975
Remuneration of directors in their capacity as directors	$ 39,000	$ 42,000
Remuneration of senior officers in their capacity as officers	218,000	216,000
Consideration to senior officers under terms of employment contract	—	121,000

7. Contingent liabilities —

The Company and certain of its subsidiaries are contingently liable at September 30, 1976 for $980,000 (excluding any penalties which may be assessed thereon) relating to mineral taxes on acreage which the company has offered to surrender to the Crown in the Province of Saskatchewan, which offers have not as yet been officially accepted by the Crown.

The Company has guaranteed the bank indebtedness of Minerales Santa Rita S.A. de C.V. (a Mexican Company) which at September 30, 1976 amounted to approximately $6,500,000 (U.S.).

8. Anti-Inflation legislation —

Certain of the provisions contained in the Federal Anti-Inflation Act which was enacted with effect from October 14, 1975 apply to the Company. Included in these provisions are restrictions that place restraints on the amounts of employee compensation and dividends which may be paid.

With the exception of the above, substantially all of the Company's operations are exempt from the provisions of the Act. No provision has been made in the accounts to September 30, 1976 for the effects of the Anti-Inflation Act since those effects, if any, would not materially change the financial information reported herein.

9. Subsequent events —

On October 4, 1976, the Company reduced its equity interest in the Elk River coal properties from 50% to 10%. As consideration, the Company will be reimbursed for certain of its previously incurred exploration costs in the amount of $924,000, will receive cash payments of $3,200,000 ($1,600,000 upon registration of the assignment of the coal licenses and $800,000 on both October 4, 1977 and October 4, 1978), and will eventually receive a 5% royalty on 40% of the coal produced. The proceeds of $3,200,000 will be applied against mining properties to the extent of costs incurred. The balance will be deferred to cover Scurry's share of future exploration and development costs.

On November 1, 1976, the Company and Scurry-Rainbow Oil (Sask) Ltd. purchased $5,850,000 of petroleum and natural gas leases for cash, of which $2,700,000 was provided by a bank loan.

On November 7, 1975, the Company and Potash Corporation of Saskatchewan entered into an option agreement covering the Saskatchewan potash properties of the Company and certain of its subsidiaries. Under the option, Potash Corporation could, on or before November 1, 1976, purchase all of such potash properties located in the Province of Saskatchewan for $2,300,000 (subject to adjustment in certain circumstances). Until November 1, 1976, Potash Corporation was to reimburse all maintenance charges and obligations except for such charges relating to certain revenue producing tracts. The Company has granted the Potash Corporation of Saskatchewan a one year extension on this option to November 1, 1977, with a further right to extend for one additional year. If the option is exercised mining properties will be reduced by $1,900,000 being the costs thereof and petroleum and natural gas interests by the balance of $400,000.

CORPORATE PROFILE

Scurry-Rainbow Oil Limited, incorporated in Alberta in 1954, is engaged in the exploration for, development and production of petroleum and natural gas and in the exploration for various minerals. The Company is approximately 86% owned by Home Oil Company Limited, a Canadian corporation. Its headquarters are in Calgary, Alberta. Subsidiary offices are located in Tulsa, Oklahoma, Reno, Nevada and London, England. Exploration activities are conducted in Canada, the United States and in the North Sea. Production of petroleum and natural gas is primarily located in the four western Provinces in Canada, with limited production in the United States. The Company does not engage in refining or retail marketing. The Company has substantial undeveloped coal reserves in southwestern Alberta and southeastern British Columbia, a partially developed gold-silver mine in Nevada and an investment in a silver-lead-zinc-antimony mining property in Mexico.

TWO YEAR PRICE RANGE OF SHARES

Fiscal Years Ended September 30

	Toronto Stock Exchange		American Stock Exchange	
	1976	**1975**	**1976**	**1975**
			(U.S. funds)	
First Quarter	\$14¾ - 12⅛	\$18½ - 11½	\$14¼ - 12	\$19¼ - 11
Second Quarter	17¼ - 12⅜	15¼ - 12¾	17 - 12⅜	15 - 12
Third Quarter	20½ - 15⅜	14½ - 13⅜	20⅞ - 16⅛	15 - 13
Fourth Quarter	18 - 14⅞	16 - 14	19 - 15⅝	15½ - 14⅛

The Company has not declared or paid any dividends on its outstanding shares.

FIVE YEARS AT A GLANCE

		1976	1975	1974	1973	1972
EARNINGS	Gross revenue	$17,011,000	$ 13,727,000	$12,265,000	$ 9,917,000	$ 8,613,000
	Net earnings (loss)	4,771,000	2,978,000	(5,042,000)	261,000	(302,000)
	Per share	1.80	1.12	(1.92)	.10	(.12)
BALANCE SHEET	Working capital	$ 7,953,000	$ 8,299,000	$ 5,816,000	$ 7,569,000	$ 7,816,000
	Investments and advances	2,003,000	5,926,000	4,245,000	3,338,000	3,265,000
	Capital assets — net	58,770,000	50,668,000	51,435,000	54,033,000	52,609,000
	Deferred charges	350,000	501,000	509,000	862,000	786,000
	Long-term debt — net	16,058,000	17,321,000	17,765,000	17,792,000	17,873,000
	Deferred income taxes	11,822,000	11,646,000	10,251,000	9,565,000	8,494,000
	Minority interests	1,736,000	1,738,000	2,278,000	2,409,000	2,495,000
	Shareholders' equity	39,460,000	34,689,000	31,711,000	36,036,000	35,614,000
CAPITAL EXPENDITURES	Acquisition of property	$ 2,114,000	$ 782,000	$ 3,358,000	$ 1,130,000	$ 620,000
	Exploration and Development expenditures	9,821,000	4,127,000	5,817,000	5,859,000	3,639,000
	Production equipment	534,000	232,000	375,000	250,000	592,000
	Other capital assets	97,000	58,000	63,000	10,000	97,000
	Total capital expenditures	12,566,000	5,199,000	9,613,000	7,249,000	4,948,000
LAND HOLDINGS	Gross acreage	9,079,000	9,714,000	14,610,000	14,538,000	12,868,000
	Net acreage					
	— Working interest	1,807,000	1,839,000	2,954,000	3,505,000	2,911,000
	— Minerals	643,000	643,000	1,812,000	1,812,000	1,812,000
	— Royalty interest	93,000	94,000	94,000	97,000	96,000
	— Mining	252,000	220,000	164,000	217,000	221,000
DRILLING ACTIVITY	Gross wells drilled	52	38	64	77	72
	Net oil and gas wells — working interest	5	3	4	4	4
	— royalty interest	1	4	3	9	11
PRODUCTION	Crude oil and natural gas liquids					
	— barrels per day	6,234	7,258	8,540	8,960	8,890
	Natural gas — thousand cubic feet per day	16,836	14,406	13,385	14,545	14,225
SHARES	Shares outstanding					
	— end of year	2,647,921	2,647,921	2,647,921	2,611,761	2,601,761
	— average for the year	2,647,921	2,647,921	2,627,638	2,602,829	2,601,761

The above data incorporates retroactive adjustments.