

*PENN WEST*  
ENERGY TRUST

UNLEASHING ENERGY

Q3

QUARTERLY REPORT

For the three months and nine months ending September 30, 2007





**Quarterly Report**  
**For the three and nine months ended September 30, 2007**

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### **Proposed Merger**

- On October 31, 2007, Penn West Energy Trust ("Penn West") and Canetic Resources Trust ("Canetic") entered into a combination agreement (the "Agreement") that provides for the strategic combination of Penn West and Canetic to form Canada's largest energy trust (the "Combined Trust"). The Combined Trust will have an enterprise value of over \$15 billion and current production of over 200,000 barrels of oil equivalent per day. The combined asset portfolio will include interests in a significant number of Western Canada's highest quality conventional oil and natural gas pools and will also include a number of non-conventional growth opportunities including oil sands, coalbed methane, shale gas and enhanced oil recovery. Under the terms of the Agreement, Canetic unitholders will receive 0.515 of a Penn West unit on a tax-deferred basis for Canadian and U.S. tax purposes and a one-time special distribution of \$0.09 for each Canetic unit. The strategic merger of assets and people will operate under the Penn West name and will be led by a combined management team and Board of Directors. The combination is expected to close in January 2008.

### **Operations**

- Production averaged 125,345 boe per day in the third quarter of 2007 compared to 126,599 boe per day in the second quarter of 2007. The previously announced fire at our Wildboy tank farm reduced reported third quarter 2007 production (approximately 3,750 barrels of oil equivalent per day).
- Crude oil and NGL production averaged 72,783 barrels per day and natural gas production averaged 315 mmcf per day in the third quarter of 2007.
- Penn West invested \$230 million on capital development including, \$55 million of net acquisitions and drilled 68 net wells in the third quarter with a success rate of 97 percent.
- Production is currently approximately 131,000 boe per day, comprised of 67,700 boe per day of crude oil, 350 mmcf per day of natural gas and 5,200 boe per day of natural gas liquids.

### **Financial**

- Cash flow of \$347 million (\$1.44 per unit, basic) in the third quarter of 2007 was six percent higher than cash flow of \$326 million (\$1.37 per unit, basic) realized in the second quarter of 2007.
- Net income in the third quarter of 2007 was \$137 million (\$0.57 per unit, basic) compared to a loss of \$185 million (\$0.77 per unit, basic) in the second quarter of 2007. The second quarter loss was due to the enactment of the Specified Investment Flow-Through tax.
- In September 2007, Penn West entered into foreign exchange contracts to fix the future repayment amount in Canadian dollars on US\$250 million of its US\$475 million private notes at an exchange rate of approximately one CAD\$ equals one US\$. During the third quarter of 2007, Penn West also entered oil and natural gas collars, increased its syndicated credit facility to \$2.1 billion from \$1.9 billion while extending it to a three-year term and amended its Distribution Reinvestment Program to enable the participation of US investors.

## Distributions

- Penn West's Board of Directors recently resolved to keep our distribution level at \$0.34 per unit, per month, for the next three months subject to current forecasts of commodity prices, production and planned capital expenditures.

## Vault Energy Trust Acquisition

- On September 24, 2007, Penn West entered into an Arrangement Agreement to acquire Vault Energy Trust ("Vault") where Vault's unitholders and exchangeable shareholders will receive 0.14 of a Penn West trust unit for each equivalent Vault trust unit and Vault warrant holders will receive \$0.51 per warrant. The total acquisition cost is expected to be approximately \$380 million. The acquisition is expected to add approximately 6,500 barrels of oil equivalent per day weighted 65 percent natural gas and 35 percent oil. It is expected that the acquisition will close in December of 2007.

## The New Alberta Royalty Framework

- On October 25, 2007, the Government of Alberta announced that effective January 1, 2009, it intends to adopt a new royalty framework, incorporating some of the recommendations of the Alberta Royalty Review Panel. At our current commodity prices and asset mix, the new royalty regime is expected to have only a minimal impact on Penn West's current production and cash flow. We are reviewing our go forward strategy on a project by project basis and we have formulated a 2008 capital budget that considers the impact of the new royalty framework on project economics. It is important to note that Penn West has a large and diversified land and product base in all four western Canadian provinces.

## Long-term Project Updates

- Penn West engaged Sproule Associates Limited ("Sproule") to independently evaluate certain of its resources contained on its lands located in the Peace River Oil Sands Project as at September 30, 2007. Sproule's estimate was limited to approximately 20 percent of the total Penn West lands in the Peace River Oil Sands Project. On these evaluated lands, Sproule estimates that Penn West's share of Contingent Resources<sup>(1)</sup> of heavy oil is approximately 1.7 billion barrels. This evaluation confirms Penn West's internal evaluations on this portion of our oil sands leases based on stratigraphic tests and regional geological mapping.
- At our Peace River Oil Sands Project, in the first nine months of 2007, Penn West completed the drilling of 22 of 29 planned horizontal wells, drilled 16 stratigraphic test wells and completed the tie-in of 11 production pads in Seal Main to Penn West owned production facilities. Geological and engineering studies are ongoing and include plans to drill an additional 28 stratigraphic test wells before the end of 2008, the interpretation of 3-D seismic and core analysis, all aimed at further delineating the project's resources. The application of development technology such as multi-leg horizontal wells and re-entries utilizing various configurations are yielding early promising results in our continuing efforts to increase well productivity and reduce capital costs.
- We continue to evaluate an integrated approach to enhancing our light oil recovery rates from large, legacy oil pools using miscible flooding with CO<sub>2</sub> captured from heavy industry gasification processes while at the same time helping to sequester greenhouse gases. At our Pembina CO<sub>2</sub> pilot project, monitoring and evaluation is continuing and we plan to drill two additional vertical infill wells in the fourth quarter of 2007 to gather additional petrophysical data. The horizontal pilot expansion at Pembina is targeted to be on-stream by the first quarter of 2008. The CO<sub>2</sub> pilot at South Swan Hills is currently under construction and is likewise targeted to be on-stream in the first quarter of 2008.

## Management Team

- In the third quarter of 2007, the Penn West Board of Directors named Don Wood as Vice President, Development South and Brett Frostad as Vice President, Exploration North. Mr. Wood is a Professional Engineer and an MBA graduate who brings 29 years of domestic and international upstream oil and gas experience to the Trust, most recently as President and C.E.O. of C1 Energy Ltd. Mr. Frostad is a Professional Geologist who joined Penn West in 2002 and has since served in a number of roles of increasing responsibility within the Trust.

(1) As per the Canadian Oil and Gas Evaluation Handbook, Contingent Resources are those quantities of oil and natural gas estimated on a given date to be potentially recoverable from known accumulations but may not be currently economic. Sproule Associates Limited has categorized the potentially recoverable resources as contingent in view of ownership, regulatory applications and owner commitment issues and not as a result of current economics. Penn West believes these contingent resources will become economic to develop in the future and expects these contingent resources to be converted to reserves, in whole or part, through additional project development and financial commitments in the future.

## HIGHLIGHTS

(\$ millions, except per unit and production amounts)	Three months ended September 30			Nine months ended September 30		
	2007	2006	% change	2007	2006	% change
<b>Financial</b>						
Gross revenues <sup>(1)</sup>	\$ 627.1	\$ 636.0	(1)	\$ 1,817.8	\$ 1,522.4	19
Cash flow	346.8	365.6	(5)	984.3	873.5	13
Basic per unit	1.44	1.55	(7)	4.13	4.63	(11)
Diluted per unit	1.43	1.53	(7)	4.09	4.56	(10)
Net income	137.4	177.8	(23)	48.5	542.7	(91)
Basic per unit	0.57	0.66	(14)	0.20	2.88	(93)
Diluted per unit	0.57	0.65	(12)	0.20	2.83	(93)
Total expenditures, net	230.0	116.7	97	929.5	3,741.8	(75)
Long-term debt at period-end	1,824.7	1,152.4	58	1,824.7	1,152.4	58
Distributions paid <sup>(2)</sup>	\$ 244.4	\$ 216.2	13	\$ 729.6	\$ 540.5	35
<b>Operations</b>						
Daily production						
Natural gas (mmcf/d)	315.4	359.1	(12)	329.8	298.3	11
Light oil and NGL (bbls/d)	50,861	48,029	6	49,874	36,576	36
Conventional heavy oil (bbls/d)	21,922	21,186	3	21,937	20,166	9
Total production (boe/d)	125,345	129,059	(3)	126,785	106,457	19
Average sales price						
Natural gas (\$/mcf)	\$ 5.86	\$ 5.97	(2)	\$ 7.02	\$ 6.65	6
Light oil and NGL (\$/bbl)	72.62	70.25	3	65.91	68.40	(4)
Conventional heavy oil (\$/bbl)	48.75	52.20	(7)	44.09	45.15	(2)
Netback per boe						
Sales price	\$ 52.73	\$ 51.33	3	\$ 51.81	\$ 50.70	2
Risk management	0.98	2.23	(56)	0.43	1.68	(74)
Net sales price	53.71	53.56	-	52.24	52.38	-
Royalties	9.46	9.26	2	9.63	9.45	2
Operating expenses	11.18	10.64	5	10.94	10.30	6
Transportation	0.47	0.64	(27)	0.51	0.63	(19)
Netback	\$ 32.60	\$ 33.02	(1)	\$ 31.16	\$ 32.00	(3)

The above information includes non-GAAP measures not defined under generally accepted accounting principles, including cash flow and netback. Cash flow is cash flow from operating activities before changes in non-cash working capital, and asset retirement expenditures. Please refer to the calculation of cash flow table on the first page of the Management's Discussion and Analysis for a reconciliation of cash flow from operating activities to cash flow. Cash flow is used to assess the ability to fund distributions and planned capital programs. Barrels of oil equivalent (boe) are based on six mcf of natural gas equalling one barrel of oil (6:1). Netback is a per unit of production measure of operating margin used in capital allocation decisions.

(1) Gross revenues include realized gains and losses on commodity contracts.

(2) Includes distributions paid in trust units under the distribution reinvestment plan.

## DRILLING PROGRAM

	Three months ended September 30				Nine months ended September 30			
	2007		2006		2007		2006	
	Gross	Net	Gross	Net	Gross	Net	Gross	Net
Natural gas	41	21	67	29	95	46	147	93
Oil	60	39	79	56	137	83	143	111
Dry	2	2	3	3	7	6	14	14
	103	62	149	88	239	135	304	218
Stratigraphic and service	8	6	11	5	27	21	20	11
Total	111	68	160	93	266	156	324	229
Success Rate <sup>(1)</sup>	97%		97%		96%		94%	

(1) Success rate is calculated excluding stratigraphic and service wells.

## UNDEVELOPED LANDS

	As at September 30		
	2007	2006	% change
Gross acres (000s)	3,914	4,519	(13)
Net acres (000s)	3,379	4,037	(16)
Average working interest	86%	89%	(3)

## FARM-OUT ACTIVITY

	Three months ended September 30		Nine months ended September 30	
	2007	2006	2007	2006
Wells drilled on farm-out lands <sup>(1)</sup>	41	58	147	112

(1) Wells drilled on Penn West lands, including re-completions and re-entries, by independent operators pursuant to farm-out agreements.

## CORE AREA ACTIVITY

Core Area	Net wells drilled for the nine months ended September 30, 2007	Undeveloped land as at
		September 30, 2007 (thousands of net acres)
Central	63	1,276
Plains	91	1,003
Northern	2	1,100
	156	3,379

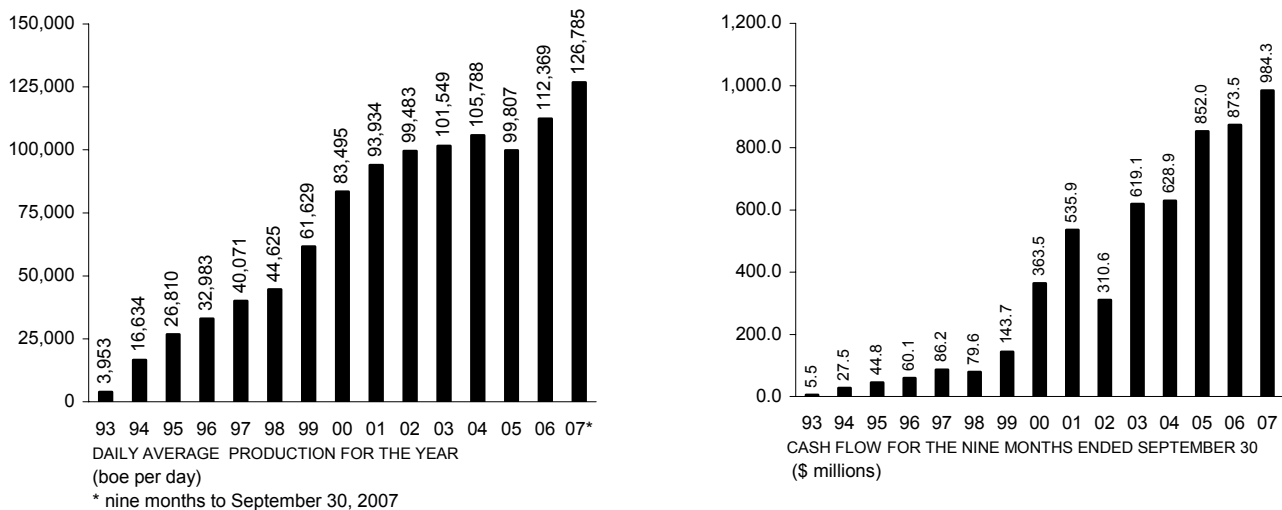
## TRUST UNIT DATA

(millions of units)	Three months ended September 30			Nine months ended September 30		
	2007	2006	% change	2007	2006	% change
Weighted average						
Basic	240.5	236.1	2	238.6	188.6	27
Diluted	242.6	239.0	2	240.9	191.5	26
Outstanding as at September 30						
Basic				240.8	236.2	2
Basic plus trust unit rights				255.2	246.8	3

## Important Additional Information will be Filed with the SEC

In connection with the proposed business combination with Canetic, Penn West intends to, if required, file relevant materials with the Securities and Exchange Commission (the “SEC”) on a Registration Statement on Form F-10 (the “Registration Statement”) to register the Penn West Units (the “Units”) to be issued in connection with the proposed transaction. Investors and unitholders are urged to read the Registration Statement and any other relevant documents to be filed with the SEC when available because they will contain important information about Penn West and Canetic, the transaction and related matters. Investors and unitholders will be able to obtain free copies of the Registration Statement and other documents filed with the SEC by Penn West through the website maintained by the SEC at [www.sec.gov](http://www.sec.gov). In addition, investors and unitholders will be able to obtain free copies of the Registration Statement and such other documents when they become available from Penn West by contacting Penn West Investor Relations at [investor\\_relations@pennwest.com](mailto:investor_relations@pennwest.com) or by telephone at 1-888-770-2633.

### Charting our Performance



### Letter to our Unitholders

The third quarter of 2007 was characterized by near-record high US dollar oil prices, lower natural gas prices, which have shown some signs of recovering since quarter end, and highs in the Canadian dollar not seen for over thirty years. Penn West Energy Trust (“Penn West”) generated cash flow in the third quarter of 2007 of \$347 million (\$1.44 per unit, basic), \$21 million higher (\$0.07 per unit, basic) than the second quarter of 2007 and \$19 million lower (\$0.11 per unit basic) than the third quarter of 2006. Our average production in the quarter was negatively affected by approximately 23 mmcf per day due to the continuing fire-related outage at our Wildboy natural gas plant (the financial impact of which we expect will be largely offset by our business interruption insurance) and by approximately 1,200 barrels of oil equivalent per day due to scheduled downtime for turnarounds and other facility maintenance. Production has now been restored at Wildboy where we are currently producing in excess of 50 mmcf per day.

On October 31, 2007, Penn West Energy Trust (“Penn West”) and Canetic Resources Trust (“Canetic”) entered into a combination agreement (the “Combination Agreement”) that provides for the strategic combination of Penn West and Canetic to form Canada’s largest energy trust (the “Combined Trust”). The Combined Trust will have an enterprise value of over \$15 billion and current production of over 200,000 barrels of oil equivalent per day. Key highlights of the Combined Trust include; becoming the dominant independent light oil producer in Western Canada with conventional proven plus probable reserves in excess of 800 million boe, a large inventory of unconventional opportunities including a multi-billion barrel (discovered heavy oil resources in place) <sup>(1)</sup> Peace River Oil Sands Project and increased liquidity and enhanced financial flexibility allowing expansion both domestically and internationally. The combining entities exhibit a compelling overlap of assets and similarities in operating philosophies, which should improve operating efficiencies, field optimization and cost reductions availed

by economies of scale. The Combined Trust will operate approximately 80 percent of its production and the initial distribution will be \$0.34 per unit per month. Under the terms of the Combination Agreement, Canetic unitholders will receive 0.515 of a Penn West unit for each Canetic unit on a tax-deferred basis for Canadian and U.S. tax purposes plus a one-time special distribution of \$0.09 per unit. It is expected that the Canetic unitholder meeting to vote on the combination and closing will occur in January 2008.

The merger with Canetic will permit Penn West to remain as an income trust with approximately \$15 billion of expansion capabilities under the SIFT tax rules. We will continue to evaluate the best corporate structure for Penn West after the SIFT tax becomes effective in 2011. Subsequent to 2011, the current alternatives available to Penn West include any combination of:

- maintaining the trust structure;
- converting to a high yield, low growth corporate model;
- converting to a low yield, high growth corporate model.

We want to emphasize that there is no current plan to convert the combined corporate structure to a conventional corporation on or prior to the effective date of the SIFT tax. No change will be made until it is clear that the change is the best alternative for unitholders.

On October 25, 2007, the Government of Alberta (the "Government") released its new royalty framework, which will become effective January 1, 2009. There are four important aspects of the new framework that impact Penn West. First, the new program confirmed that conventional production from oil sands leases will continue to be subject to oil sands royalty rates rather than the higher conventional oil royalty rates proposed by the Alberta Royalty Review Panel (the "ARRP"). This is positive at our Peace River Oil Sands Project as pay-out times will not be materially increased. Second, the Government decided to retain the Enhanced Oil Recovery ("EOR") and the Innovative Energy Technology incentive programs related to CO<sub>2</sub> and hydrocarbon miscible flood EOR projects. Penn West believes strongly in these projects which aim to recover a material amount of oil remaining in large light oil pools while sequestering greenhouse gases and applauds the Government for these initiatives. Penn West has a significant inventory of legacy, light oil interests amenable to EOR and has interests in CO<sub>2</sub> EOR producing properties and other CO<sub>2</sub> pilot projects. Third, the new framework will continue to encourage solution gas conservation associated with both conventional and bitumen production and thus is consistent with Penn West's long standing environmental operating and asset optimization objectives. Lastly, on conventional production, the Government confirmed that its new royalty framework will be sensitive to well productivity and commodity prices at slightly higher thresholds than the September 18, 2007 proposals of the ARRP. Penn West, as the largest energy trust in North America, has a wide diversity of play types across the Western Canada Sedimentary Basin. Approximately sixty percent of our production is from Alberta Crown leases and our historical asset strategies have favored mature assets. While we are currently assessing the impact the new royalty framework will have on our longer-term conventional capital allocations, at current commodity prices and at our current asset mix, we expect that our conventional producing oil and natural gas business will be only minimally affected.

On September 24, 2007, Penn West entered an Arrangement agreement to acquire Vault Energy Trust ("Vault") for a total acquisition cost of approximately \$380 million of which approximately \$170 million will be paid through the issue of 5.5 million Penn West trust units, with the remainder of the acquisition cost being the assumption of debt, including convertible debentures. Vault Unitholders and Exchangeable Shareholders will receive 0.14 of a Penn West trust unit for each equivalent Vault trust unit and Vault's Warrant Holders will receive \$0.51 per warrant. Our interest in Vault's assets, which currently produce about 6,500 barrels of oil equivalent per day, is due to the opportunity to add another significant legacy light oil area, Wimborne, as well as assets at Pembina, Bigoray, Crystal and Westeros which fold into some of our existing core light oil holdings. We also like the fit of Vault's natural gas assets. An Information Circular was mailed to Vault's Unitholders on October 29, 2007 and Vault's Unitholder meeting to vote on the arrangement is expected to occur in December 2007.

On September 18, 2007, we commenced the statutory acquisition of the remainder of the C1 Energy Ltd. shares and subsequently de-listed its shares from the Toronto Stock Exchange. In the third quarter, Penn West also added natural gas and oil collars, fixed the Canadian dollar repayment amount of US\$250 million of its US dollar denominated private notes at slightly better than parity, increased its syndicated credit facility to \$2.1 billion from \$1.9 billion while extending it to a three-year term and amended our Distribution Reinvestment Program to enable the participation of US investors.

Penn West is pleased to announce the Conference Board of Canada named it to the Climate Disclosure Leadership Index (the "CDLI"). The CDLI consists of the top 16 Canadian companies on the TSX that are recognized for their high level of transparency regarding climate change disclosure. The Carbon Disclosure Project (the "CDP") provides a coordinating secretariat for institutional investors with a combined \$41 trillion of assets under management. On their behalf it seeks information on the business risks and opportunities presented by climate change and greenhouse gas emissions data from the world's largest companies: 2,400 in 2007. Additional information regarding this index can be found on the Conference Board of Canada's website ([www.conferenceboard.ca](http://www.conferenceboard.ca)) or the International Carbon Disclosure Project website ([www.cdproject.net](http://www.cdproject.net)).

Penn West has shown the ability to meet challenges head-on. With guidance we receive from our Board of Directors and a focus on detail, we believe we can adjust our operations and programs to effectively address recent challenges including the tax on specified investment flow through entities in 2011, the proposals to change the royalty structure in Alberta and others. As in the past, our primary objective remains to provide superior returns to our Unitholders in a safe and environmentally-responsible manner.

Upon successful completion of the Canetic, Vault and other pending transactions, Penn West forecasts initial production between 200,000 - 210,000 boe per day generating cash flow for 2008 of \$2.0 - \$2.2 billion using budgeted prices of US\$75.00 WTI oil prices, \$7.00 per mcf AECO natural gas prices and a par exchange rate. Based on this level of cash flow and other factors, we estimate 2008 net capital expenditures of \$900 million to \$1 billion.

On behalf of the Board of Directors,



William E. Andrew  
President and CEO

Calgary, Alberta  
November 1, 2007

(1) Represents the mid case. Using the definitions set out in the Canadian Oil and Gas Handbook, these resources are considered "Discovered Resources". As Penn West is in the early stages of the project, these resources have not been classified into more specific categories. There is no certainty that a significant portion of these resources will be recovered or that a significant portion of the resources will be economically or technically feasible to produce in the future. Discovered resources are those quantities of oil and gas estimated on a given date to be remaining in, plus those quantities already produced from, known accumulations. Discovered resources consist of economic and uneconomic resources with the estimated future recoverable portion classified as reserves or contingent resources.

**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
For the three and nine months ended September 30, 2007

This management's discussion and analysis ("MD&A") of financial conditions and results of operations should be read in conjunction with the unaudited interim consolidated financial statements of Penn West Energy Trust ("Penn West", "the Trust", "we" or "our") for the three and nine months ended September 30, 2007 and the audited consolidated financial statements and MD&A for the year ended December 31, 2006. The date of this MD&A is November 1, 2007.

All dollar amounts contained in this MD&A are expressed in millions of Canadian dollars unless noted otherwise.

Please refer to our disclaimer on forward-looking statements at the end of this MD&A. The calculations of barrels of oil equivalent ("boe") are based on a conversion ratio of six thousand cubic feet of natural gas to one barrel of crude oil. This could be misleading if used in isolation as it is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

Measures including cash flow, cash flow per unit-basic, cash flow per unit-diluted and netbacks included in this MD&A are not defined in generally accepted accounting principles ("GAAP") and do not have a standardized meaning prescribed by GAAP; accordingly, they may not be comparable to similar measures provided by other issuers. Management utilizes cash flow and netbacks to assess financial performance, to allocate its capital among alternative projects and to assess our capacity to fund distributions and future capital programs. Reconciliations of non-GAAP measures to their nearest measure prescribed by GAAP are provided below.

**Calculation of Cash Flow**

(\$ millions, except per unit amounts)	Three months ended September 30		Nine months ended September 30	
	2007	2006	2007	2006
Cash flow from operating activities	\$ 316.8	\$ 418.8	\$ 930.1	\$ 845.2
Increase (decrease) in non-cash working capital	11.8	(61.3)	17.5	10.7
Asset retirement expenditures	18.2	8.1	36.7	17.6
Cash flow	\$ 346.8	\$ 365.6	\$ 984.3	\$ 873.5
Basic per unit	\$ 1.44	\$ 1.55	\$ 4.13	\$ 4.63
Diluted per unit	\$ 1.43	\$ 1.53	\$ 4.09	\$ 4.56

**Quarterly Financial Summary**

(\$ millions, except per unit and production amounts) (unaudited)

Three months ended	Penn West Energy Trust							
	Sep 30 2007	Jun 30 2007	Mar 31 2007	Dec 31 2006	Sep 30 2006	Jun 30 2006	Mar 31 2006	Dec 31 2005
Gross revenues <sup>(1)</sup>	\$ 627.1	\$ 608.3	\$ 582.4	\$ 578.5	\$ 636.0	\$ 452.5	\$ 433.9	\$ 554.5
Cash flow	346.8	326.2	311.3	303.3	365.6	264.7	243.2	332.6
Basic per unit	1.44	1.37	1.31	1.23	1.55	1.59	1.49	2.03
Diluted per unit	1.43	1.35	1.30	1.22	1.53	1.56	1.47	2.03
Net income (loss)	137.4	(185.2)	96.3	122.9	177.8	220.5	144.4	241.1
Basic per unit	0.57	(0.77)	0.41	0.44	0.66	1.34	0.88	1.48
Diluted per unit	0.57	(0.77)	0.40	0.44	0.65	1.31	0.87	1.46
Distributions declared	245.0	243.5	242.4	241.5	240.7	167.6	162.0	151.8
Per unit	1.02	1.02	1.02	1.02	1.02	1.02	0.99	0.93
Production								
Liquids (bbls/d) <sup>(2)</sup>	72,783	70,923	71,716	70,819	69,215	48,599	52,226	51,953
Natural gas (mmcf/d)	315.4	334.1	340.6	354.6	359.1	267.9	266.9	277.5
Total (boe/d)	125,345	126,599	128,447	129,915	129,059	93,242	96,713	98,205

(1) Gross revenues include realized gains and losses on commodity contracts.

(2) Includes crude oil and natural gas liquids.

## **The New Alberta Royalty Framework**

On October 25, 2007, the Government of Alberta (the "Government") released its new royalty framework which becomes effective January 1, 2009. The new framework maintains or continues certain programs that are important to Penn West:

- conventional production from oil sands leases will maintain oil sands administrative status which benefits our Peace River Oil Sands project due to the reduced royalty rates;
- Enhanced Oil Recovery ("EOR") and Innovative Energy Technology incentive programs will continue. Penn West has significant inventories of legacy light oil interests amenable to EOR and interests in CO<sub>2</sub> EOR producing and other CO<sub>2</sub> pilot projects;
- Otherwise Flared Solution Gas Waiver Program will continue which supports our long standing environmental operating and asset optimization objectives.

On conventional production, the Government confirmed that its new royalty framework will be sensitive to well productivity and commodity prices at slightly higher thresholds than the September 18, 2007 proposals of the Alberta Royalty Review Panel. Penn West, as the largest energy trust in North America, has a wide diversity of play types across the Western Canada Sedimentary Basin. Approximately 60 percent of our production is from Alberta Crown leases and our historical asset strategies have favored mature assets. We are currently assessing the impact that the new royalty framework will have on our conventional capital allocations for 2008 and beyond. We currently expect that our conventional producing oil and natural gas strategies and business plans will only be minimally affected at current commodity prices and at our current asset mix.

## **Enactment of the Tax on Income Trusts**

On June 12, 2007, the legislation implementing the new tax on publicly traded income trusts and limited partnerships (the "SIFT tax"), referred to as "Specified investment flow-through" ("SIFT") entities (Bill C-52) received third reading in the House of Commons and on June 22, 2007, the Bill received Royal Assent.

For SIFTs in existence on October 31, 2006 including Penn West, the SIFT tax will be effective in 2011 unless certain rules related to "undue expansion" are not adhered to. Under the guidance provided, with the successful closing of the Vault Energy Trust ("Vault"), Canetic Resources Trust ("Canetic") and other pending transactions, we can increase our equity by approximately \$15 billion between now and 2011 without prematurely triggering the SIFT tax.

Under the SIFT tax, distributions from certain types of income will not be deductible for income tax purposes by SIFTs in 2011 and thereafter and any resultant trust level taxable income will be taxed at an approximate of the corporate income tax rate. The SIFT rate is currently 31.5 percent however on October 30, 2007, the Government of Canada, in its Mini-Budget, proposed changing the rate to 28.0 <sup>(1)</sup> percent. Distributions from income subject to the SIFT tax will be considered taxable dividends to unitholders, generally eligible for the dividend tax credit. As a result, the SIFT tax will not adversely affect Canadian investors who hold Penn West units in a non-tax deferred account. Distributions representing a return of capital for income tax purposes will continue to be an adjustment to a unitholder's adjusted cost base of trust units.

For accounting purposes, as the SIFT tax was enacted in the second quarter of 2007, Penn West recorded a one-time, non-cash charge to future income taxes of \$326 million to reflect the current estimate of the temporary differences between the book and tax basis of assets and liabilities expected to be remaining in the Trust in 2011. The majority of the temporary differences at the Penn West Trust level were assumed on the merger with Petrofund Energy Trust on June 30, 2006.

Our Board of Directors and Management are continuously monitoring the impact of this tax on our business strategies. We expect future technical interpretations and details will further clarify the legislation. At the present time, Penn West believes some or all of the following actions will or could result in the future due to the SIFT tax:

- If structural or other similar changes are not made, the after-tax distribution yield in 2011 to taxable Canadian investors will remain approximately the same, however, the distribution yield in 2011 to tax-deferred Canadian investors (RRSPs, RRIFs, pension plans, etc.) and foreign investors would fall by an estimated 31.5<sup>(1)</sup> percent and 26.5<sup>(1)</sup> percent, respectively;
- A portion of Penn West's cash flow could, as a result, be required for the payment of the SIFT tax, or other forms of tax, and would not be available for distribution or reinvestment;
- Penn West could convert to a corporate structure with yield in the form of dividends to facilitate investing a higher proportion or all of its cash flow in exploration and development projects. Such a conversion could result in the reduction, or the elimination, of the current distribution program in favor of higher capital investment and/or a dividend payment program;
- Penn West might determine that it is more economic to remain in the trust structure, at least for a period of time, and shelter its taxable income using tax pools and pay all or a portion of its distributions on a return of capital basis, likely at a lower payout ratio. Further, as the SIFT tax rate exceeds the corporate income tax rate that would be applicable to Penn West, the tax strategy might involve paying some corporate tax resulting in all or a portion of those distributions being paid on a return of capital basis at a lower payout ratio.

The Trust continues to review all organizational structures and alternatives to minimize the impact of the SIFT tax on our unitholders. While there can be no assurance that the negative effect of the tax can be minimized or eliminated, Penn West and its advisors will continue to work diligently on these issues.

- (1) On October 30, 2007, the Government of Canada delivered its Mini-Budget outlining a number of corporate tax reductions over the next five years. The general corporate tax rate will fall to a proposed rate of 15 percent in 2012, a reduction of 3.5 percent. Any reduction eventually enacted will reduce the SIFT tax rate as it becomes effective in 2011, and lower the rate at which any corporate income taxes will be paid in Penn West's operating entities.

## RESULTS OF OPERATIONS

### Production

	Three months ended September 30			Nine months ended September 30		
	2007	2006	% change	2007	2006	% change
Daily production						
Natural gas (mmcf/d)	<b>315.4</b>	359.1	(12)	<b>329.8</b>	298.3	11
Light oil and NGL (bbls/d)	<b>50,861</b>	48,029	6	<b>49,874</b>	36,576	36
Conventional heavy oil (bbls/d)	<b>21,922</b>	21,186	3	<b>21,937</b>	20,166	9
Total production (boe/d) <sup>(1)</sup>	<b>125,345</b>	129,059	(3)	<b>126,785</b>	106,457	19

- (1) Barrels of oil equivalent (boe) are based on six mcf of natural gas being equal to one barrel of oil (6:1)

Production in the third quarter of 2007 was slightly below the 126,599 boe per day produced in the second quarter of 2007 due primarily to the loss of approximately 22.5 mmcf per day of natural gas production at our 100% owned Wildboy natural gas plant which was shut down, then partially re-started after a fire at the adjoining tank farm in mid-May. We expect that our business interruption insurance will cover the lost cash flow, excluding the deductible portion. Production at Wildboy is currently in excess of 50 mmcf per day. In addition, production in the third quarter of 2007 was reduced by 1,200 barrels of oil equivalent per day due to scheduled turnarounds.

We strive to maintain an approximately balanced portfolio of liquids and natural gas production provided it is economic to do so. We believe a balance by product helps to reduce exposure to price volatility that can affect a single commodity. In the third quarter of 2007, crude oil and NGL production averaged 72,783 barrels per day (58 percent of production) and natural gas production averaged 315.4 mmcf per day (42 percent of production).

We drilled 68 net wells in the third quarter of 2007, mainly in the Central and Plains areas, compared to 93 in the same period of 2006.

## Commodity Markets

### Natural Gas

North American natural gas prices continued to weaken through the summer. With little or no interruptions to supply and record liquefied natural gas ("LNG") imports in the third quarter, storage filled quickly which eased supply concerns. Spot natural gas prices at AECO in the third quarter decreased by \$1.76 per mcf, or 24 percent, from the prior quarter to average \$5.61 per mcf. Penn West's average natural gas price in the third quarter of 2007 exceeded AECO spot prices due to the use of fixed price, short term, physical natural gas contracts. Penn West averaged \$6.18 per mcf at the plant gate, including gains from financial hedges.

### Crude Oil

WTI oil prices strengthened in the third quarter of 2007, as world oil supply remained tightly balanced to projected demand growth. Although the Canadian dollar continued to strengthen relative to the US dollar, Edmonton par oil prices traded higher relative to WTI prices as markets reacted to disruptions in synthetic oil supply through the latter part of the quarter. Subsequent to September 30, 2007, WTI oil prices have continued to increase due to the Turkey/Iraq Kurdish Rebel geopolitical situation and continuing strong demand. Both heavy and sour Canadian oil differentials to the Edmonton par light oil price widened compared to the second quarter of 2007, with the Bow River differential averaging \$24.74 per barrel compared to \$22.31 in the previous quarter due to continuing U.S. refinery outages. Penn West's average field price, including losses from financial hedges, was \$65.22 per barrel.

### Average Sales Prices Received

	Three months ended September 30			Nine months ended September 30		
	2007	2006	% change	2007	2006	% change
Natural gas (\$/mcf)	\$ 5.86	\$ 5.97	(2)	\$ 7.02	\$ 6.65	6
Risk management (\$/mcf)	0.43	1.07	(60)	0.16	0.78	(80)
Natural gas net (\$/mcf)	6.29	7.04	(11)	7.18	7.43	(3)
Light oil and liquids (\$/bbl)	72.62	70.25	3	65.91	68.40	(4)
Risk management (\$/bbl)	(0.24)	(1.97)	(88)	0.04	(1.45)	(103)
Light oil and liquids net (\$/bbl)	72.38	68.28	6	65.95	66.95	(2)
Conventional heavy oil (\$/bbl)	48.75	52.20	(7)	44.09	45.15	(2)
Weighted average (\$/boe)	52.73	51.33	3	51.81	50.70	2
Risk management (\$/boe)	0.98	2.23	(56)	0.43	1.68	(74)
Weighted average net (\$/boe)	\$ 53.71	\$ 53.56	-	\$ 52.24	\$ 52.38	-



















































