Cenovus Energy Inc.

Consolidated Financial Statements

For the Year Ended December 31, 2011

(Canadian Dollars)

Report of Management

Management's Responsibility for the Consolidated Financial Statements

The accompanying Consolidated Financial Statements of Cenovus Energy Inc. ("Cenovus") are the responsibility of Management. The Consolidated Financial Statements have been prepared by Management in Canadian dollars in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board and include certain estimates that reflect Management's best judgments.

The Board of Directors has approved the information contained in the Consolidated Financial Statements. The Board of Directors fulfills its responsibility regarding the financial statements mainly through its Audit Committee which is made up of three independent directors. The Audit Committee has a written mandate that complies with the current requirements of Canadian securities legislation and the United States *Sarbanes-Oxley Act of 2002* and voluntarily complies, in principle, with the Audit Committee guidelines of the New York Stock Exchange. The Audit Committee meets with Management and the independent auditors on at least a quarterly basis to review and approve interim Consolidated Financial Statements and Management's Discussion and Analysis prior to their public release as well as annually to review the annual Consolidated Financial Statements and Management's Discussion and Analysis and recommend their approval to the Board of Directors.

Management's Assessment of Internal Control over Financial Reporting

Management is also responsible for establishing and maintaining adequate internal control over financial reporting. The internal control system was designed to provide reasonable assurance to Management regarding the preparation and presentation of the Consolidated Financial Statements.

Internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management has assessed the design and effectiveness of internal control over financial reporting as at December 31, 2011. In making its assessment, Management has used the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") framework in Internal Control–Integrated Framework to evaluate the design and effectiveness of internal control over financial reporting. Based on our evaluation, Management has concluded that internal control over financial reporting was effective as at December 31, 2011.

PricewaterhouseCoopers LLP, an independent firm of Chartered Accountants, was appointed to audit and provide independent opinions on both the Consolidated Financial Statements and internal control over financial reporting as at December 31, 2011 as stated in their Auditor's Report dated February 15, 2012. PricewaterhouseCoopers LLP has provided such opinions.

(signed)

Brian C. Ferguson
President &
Chief Executive Officer
Cenovus Energy Inc.

(signed)

Ivor M. Ruste
Executive Vice-President &
Chief Financial Officer
Cenovus Energy Inc.

February 15, 2012

Independent Auditor’s Report

To the Shareholders of Cenovus Energy Inc.

We have completed an integrated audit of Cenovus Energy Inc.’s 2011 consolidated financial statements and its internal control over financial reporting as at December 31, 2011 and an audit of its 2010 consolidated financial statements. Our opinions, based on our audits, are presented below.

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Cenovus Energy Inc., which comprise the consolidated balance sheets as at December 31, 2011, December 31, 2010 and January 1, 2010 and the consolidated statements of earnings and comprehensive income, shareholders’ equity and cash flows for the years ended December 31, 2011 and 2010, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

Management’s Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor’s Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards and the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform an audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement. Canadian generally accepted auditing standards require that we comply with ethical requirements.

An audit involves performing procedures to obtain audit evidence, on a test basis, about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor’s judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the company’s preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances. An audit also includes evaluating the appropriateness of accounting principles and policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion on the consolidated financial statements.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Cenovus Energy Inc. as at December 31, 2011, December 31, 2010 and January 1, 2010 and its financial performance and cash flows for the years ended December 31, 2011 and 2010 in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board.

Report on Internal Control over Financial Reporting

We have also audited Cenovus Energy Inc.’s internal control over financial reporting as at December 31, 2011, based on criteria established in Internal Control–Integrated Framework, issued by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”).

Management’s Responsibility for Internal Control over Financial Reporting

Management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management’s Assessment of Internal Controls over Financial Reporting.

Auditor's Responsibility

Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit. We conducted our audit of internal control over financial reporting in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects.

An audit of internal control over financial reporting includes obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control, based on the assessed risk, and performing such other procedures as we consider necessary in the circumstances.

We believe that our audit provides a reasonable basis for our audit opinion on the company's internal control over financial reporting.

Definition of Internal Control over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that: (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Inherent Limitations

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate.

Opinion

In our opinion, Cenovus Energy Inc. maintained, in all material respects, effective internal control over financial reporting as at December 31, 2011 based on criteria established in Internal Control–Integrated Framework, issued by COSO.

(signed)

PricewaterhouseCoopers LLP
Chartered Accountants
Calgary, Alberta, Canada

February 15, 2012

CONSOLIDATED STATEMENTS OF EARNINGS AND COMPREHENSIVE INCOME

For the years ended December 31,
($ millions, except per share amounts)

	Notes	2011	2010*
Revenues	1		
Gross Sales		**16,185**	13,090
Less: Royalties		**489**	449
		15,696	12,641
Expenses	1		
Purchased product		**9,090**	7,551
Transportation and blending		**1,369**	1,065
Operating		**1,406**	1,286
Production and mineral taxes		**36**	34
(Gain) loss on risk management	31	**(248)**	(324)
Depreciation, depletion and amortization		**1,295**	1,302
Exploration expense		**-**	3
General and administrative		**295**	246
Finance costs	5	**447**	498
Interest income	6	**(124)**	(144)
Foreign exchange (gain) loss, net	7	**26**	(51)
(Gain) loss on divestiture of assets	17	**(107)**	(116)
Other (income) loss, net		**4**	(13)
Earnings Before Income Tax		**2,207**	1,304
Income tax expense	8	**729**	223
Net Earnings		**1,478**	1,081
Other Comprehensive Income (Loss), Net of Tax			
Foreign currency translation adjustment		**48**	71
Comprehensive Income		**1,526**	1,152
Net Earnings per Common Share	9		
Basic		**1.96**	1.44
Diluted		**1.95**	1.43

* Refer to Note 34 for the impact of adopting IFRS effective January 1, 2010.

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED BALANCE SHEETS

As at
($ millions)

	Notes	**December 31, 2011**	December 31, 2010*	January 1, 2010*
Assets				
Current Assets				
Cash and cash equivalents	10	**495**	300	155
Accounts receivable and accrued revenues	11	**1,405**	1,059	982
Income tax receivable		**-**	31	40
Current portion of Partnership Contribution Receivable	12	**372**	346	345
Inventories	13	**1,291**	880	875
Risk management	31	**232**	163	60
Assets held for sale	14	**116**	65	-
Current Assets		**3,911**	2,844	2,457
Exploration and Evaluation Assets	1,15	**880**	713	580
Property, Plant and Equipment, net	1,16	**14,324**	12,627	12,049
Partnership Contribution Receivable	12	**1,822**	2,145	2,621
Risk Management	31	**52**	43	1
Income Tax Receivable		**29**	-	-
Other Assets	18	**44**	281	192
Deferred Income Taxes	8	**-**	55	3
Goodwill	1,19	**1,132**	1,132	1,146
Total Assets		**22,194**	19,840	19,049
Liabilities and Shareholders' Equity				
Current Liabilities				
Accounts payable and accrued liabilities	20	**2,579**	1,843	1,605
Income tax payable		**329**	154	-
Current portion of Partnership Contribution Payable	12	**372**	343	340
Risk management	31	**54**	163	70
Liabilities related to assets held for sale	14	**54**	7	-
Current Liabilities		**3,388**	2,510	2,015
Long-Term Debt	21	**3,527**	3,432	3,656
Partnership Contribution Payable	12	**1,853**	2,176	2,650
Risk Management	31	**14**	10	4
Decommissioning Liabilities	22	**1,777**	1,399	1,185
Other Liabilities	23	**128**	346	246
Deferred Income Taxes	8	**2,101**	1,572	1,484
Total Liabilities		**12,788**	11,445	11,240
Commitments and Contingencies	33			
Shareholders' Equity		**9,406**	8,395	7,809
Total Liabilities and Shareholders' Equity		**22,194**	19,840	19,049

* Refer to Note 34 for the impact of adopting IFRS effective January 1, 2010.

See accompanying Notes to Consolidated Financial Statements.

Approved by the Board

(signed)

Michael A. Grandin
Director
Cenovus Energy Inc.

(signed)

Colin Taylor
Director
Cenovus Energy Inc.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
($ millions)

	Share Capital (Note 25)	Paid in Surplus (Note 25)	Retained Earnings	AOCI**	Total
Balance as at January 1, 2010*	3,681	4,083	45	-	7,809
Net earnings	-	-	1,081	-	1,081
Other comprehensive income (loss)	-	-	-	71	71
Total comprehensive income for the year	-	-	1,081	71	1,152
Common shares issued under option plans	35	-	-	-	35
Dividends on common shares	-	-	(601)	-	(601)
Balance as at December 31, 2010*	3,716	4,083	525	71	8,395
Net earnings	-	-	1,478	-	1,478
Other comprehensive income (loss)	-	-	-	48	48
Total comprehensive income for the year	-	-	1,478	48	1,526
Common shares issued under option plans	64	-	-	-	64
Stock-based compensation expense	-	24	-	-	24
Dividends on common shares	-	-	(603)	-	(603)
Balance as at December 31, 2011	**3,780**	**4,107**	**1,400**	**119**	**9,406**

* Refer to Note 34 for the impact of adopting IFRS effective January 1, 2010.
** Accumulated Other Comprehensive Income.

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the years ended December 31,
($ millions)

	Notes	2011	2010*
Operating Activities			
Net earnings		**1,478**	1,081
Depreciation, depletion and amortization		**1,295**	1,302
Deferred income taxes	8	**575**	141
Cash tax on divestiture of assets		**13**	-
Unrealized (gain) loss on risk management	31	**(180)**	(46)
Unrealized foreign exchange (gain) loss	7	**(42)**	(69)
(Gain) loss on divestiture of assets	17	**(107)**	(116)
Unwinding of discount on decommissioning liabilities	5,22	**75**	75
Other		**169**	44
		3,276	2,412
Net change in other assets and liabilities		**(82)**	(55)
Net change in non-cash working capital		**79**	234
Cash From Operating Activities		**3,273**	2,591
Investing Activities			
Capital expenditures – exploration and evaluation assets	15	**(527)**	(350)
Capital expenditures – property, plant and equipment	16	**(2,265)**	(1,851)
Proceeds from divestiture of assets		**173**	309
Cash tax on divestiture of assets		**(13)**	-
Net change in investments and other		**(28)**	4
Net change in non-cash working capital		**130**	95
Cash (Used in) Investing Activities		**(2,530)**	(1,793)
Net Cash Provided (Used) before Financing Activities		**743**	798
Financing Activities			
Net issuance (repayment) of short-term borrowings		**(9)**	-
Net issuance (repayment) of revolving long-term debt		**-**	(58)
Proceeds on issuance of common shares		**48**	28
Dividends paid on common shares	9	**(603)**	(601)
Other		**6**	-
Cash From (Used in) Financing Activities		**(558)**	(631)
Foreign Exchange Gain (Loss) on Cash and Cash Equivalents Held in Foreign Currency		**10**	(22)
Increase (Decrease) in Cash and Cash Equivalents		**195**	145
Cash and Cash Equivalents, Beginning of Year		**300**	155
Cash and Cash Equivalents, End of Year		**495**	300

* Refer to Note 34 for the impact of adopting IFRS effective January 1, 2010.

See accompanying Notes to Consolidated Financial Statements.

1. DESCRIPTION OF BUSINESS AND SEGMENTED DISCLOSURES

Cenovus Energy Inc. and its subsidiaries (together "Cenovus" or the "Company") are in the business of the development, production and marketing of crude oil, natural gas and natural gas liquids ("NGLs") in Canada with refining operations in the United States ("U.S.").

Cenovus began independent operations on December 1, 2009, as a result of the plan of arrangement ("Arrangement") involving Encana Corporation ("Encana") whereby Encana was split into two independent energy companies, one a natural gas company, Encana, and the other an oil company, Cenovus. In connection with the Arrangement, Encana common shareholders received one share in each of the new Encana and Cenovus in exchange for each Encana share held.

Cenovus was incorporated under the *Canada Business Corporations Act* and its shares are publicly traded on the Toronto ("TSX") and New York ("NYSE") stock exchanges. The executive and registered office is located at #4000, 421 - 7th Avenue S.W., Calgary, Alberta, Canada, T2P 4K9. Information on the Company's basis of presentation for these financial statements is found in Note 2.

The Company's reportable segments are as follows:

- **Oil Sands,** which consists of Cenovus's producing bitumen assets at Foster Creek and Christina Lake, heavy oil assets at Pelican Lake, new resource play assets such as Narrows Lake, Grand Rapids and Telephone Lake, and the Athabasca natural gas assets. Certain of the Company's operated oil sands properties, notably Foster Creek, Christina Lake and Narrows Lake, are jointly owned with ConocoPhillips, an unrelated U.S. public company.

- **Conventional,** which includes the development and production of conventional crude oil, natural gas and NGLs in Alberta and Saskatchewan, notably the carbon dioxide enhanced oil recovery project at Weyburn, and the Bakken and Lower Shaunavon crude oil properties.

- **Refining and Marketing,** which is focused on the refining of crude oil products into petroleum and chemical products at two refineries located in the U.S. The refineries are jointly owned with and operated by ConocoPhillips. This segment also markets Cenovus's crude oil and natural gas, as well as third-party purchases and sales of product that provide operational flexibility for transportation commitments, product type, delivery points and customer diversification.

- **Corporate and Eliminations,** which primarily includes unrealized gains and losses recorded on derivative financial instruments, gains and losses on divestiture of assets, as well as other Cenovus-wide costs for general and administrative, and financing activities. As financial instruments are settled, the realized gains and losses are recorded in the operating segment to which the derivative instrument relates. Eliminations relate to sales and operating revenues and purchased product between segments recorded at transfer prices based on current market prices and to unrealized intersegment profits in inventory.

The tabular financial information which follows presents the segmented information first by segment, then by product and geographic location.

A) Results of Operations - Segment and Operational Information

For the years ended December 31,	Oil Sands 2011	Oil Sands 2010	Conventional 2011	Conventional 2010	Refining and Marketing 2011	Refining and Marketing 2010
Revenues						
Gross Sales	**3,291**	2,702	**2,328**	2,284	**10,625**	8,228
Less: Royalties	**284**	279	**205**	170	**-**	-
	3,007	2,423	**2,123**	2,114	**10,625**	8,228
Expenses						
Purchased product	**-**	-	**-**	-	**9,149**	7,674
Transportation and blending	**1,231**	935	**138**	130	**-**	-
Operating	**438**	367	**488**	434	**481**	488
Production and mineral taxes	**-**	-	**36**	34	**-**	-
(Gain) loss on risk management	**70**	(10)	**(152)**	(258)	**14**	(10)
Operating Cash Flow	**1,268**	1,131	**1,613**	1,774	**981**	76
Depreciation, depletion and amortization	**347**	375	**778**	799	**130**	96
Exploration expense	**-**	3	**-**	-	**-**	-
Segment Income (Loss)	**921**	753	**835**	975	**851**	(20)

For the years ended December 31,	Corporate and Eliminations 2011	Corporate and Eliminations 2010	Consolidated 2011	Consolidated 2010
Revenues				
Gross Sales	**(59)**	(124)	**16,185**	13,090
Less: Royalties	**-**	-	**489**	449
	(59)	(124)	**15,696**	12,641
Expenses				
Purchased product	**(59)**	(123)	**9,090**	7,551
Transportation and blending	**-**	-	**1,369**	1,065
Operating	**(1)**	(3)	**1,406**	1,286
Production and mineral taxes	**-**	-	**36**	34
(Gain) loss on risk management	**(180)**	(46)	**(248)**	(324)
	181	48	**4,043**	3,029
Depreciation, depletion and amortization	**40**	32	**1,295**	1,302
Exploration expense	**-**	-	**-**	3
Segment Income (Loss)	**141**	16	**2,748**	1,724
General and administrative	**295**	246	**295**	246
Finance costs	**447**	498	**447**	498
Interest income	**(124)**	(144)	**(124)**	(144)
Foreign exchange (gain) loss, net	**26**	(51)	**26**	(51)
(Gain) loss on divestiture of assets	**(107)**	(116)	**(107)**	(116)
Other (income) loss, net	**4**	(13)	**4**	(13)
	541	420	**541**	420
Earnings Before Income Tax			**2,207**	1,304
Income tax expense			**729**	223
Net Earnings			**1,478**	1,081

Exploration and Evaluation Assets, Property, Plant and Equipment, Goodwill and Total Assets

	Exploration and Evaluation Assets			Property, Plant and Equipment		
As at	**December 31, 2011**	December 31, 2010	January 1, 2010	**December 31, 2011**	December 31, 2010	January 1, 2010
Oil Sands	**741**	570	452	**6,224**	5,219	4,870
Conventional	**139**	143	128	**4,668**	4,409	4,645
Refining and Marketing	**-**	-	-	**3,200**	2,853	2,418
Corporate and Eliminations	**-**	-	-	**232**	146	116
Consolidated	**880**	713	580	**14,324**	12,627	12,049

	Goodwill			Total Assets		
As at	**December 31, 2011**	December 31, 2010	January 1, 2010	**December 31, 2011**	December 31, 2010	January 1, 2010
Oil Sands	**739**	739	739	**10,524**	9,487	9,426
Conventional	**393**	393	407	**5,566**	5,186	5,453
Refining and Marketing	**-**	-	-	**4,927**	4,282	3,669
Corporate and Eliminations	**-**	-	-	**1,177**	885	501
Consolidated	**1,132**	1,132	1,146	**22,194**	19,840	19,049

Capital Expenditures

For the years ended December 31,	**2011**	2010
Capital		
Oil Sands	**1,415**	857
Conventional	**788**	526
Refining and Marketing	**393**	656
Corporate	**127**	76
	2,723	2,115
Acquisition Capital		
Oil Sands	**44**	23
Conventional	**25**	25
Refining and Marketing	**-**	38
Corporate	**2**	-
Total	**2,794**	2,201

Major Customers

In connection with the marketing and sale of Cenovus's own and purchased crude oil, natural gas and refined products for the year ended December 31, 2011, Cenovus had two customers (2010 – two) which individually accounted for more than 10 percent of its consolidated gross revenues. Sales to these customers, major international integrated energy companies with an investment grade credit rating, were approximately $7,324 million and $2,683 million respectively (2010 – $5,376 million and $2,295 million).

B) Financial Results by Upstream Product

Crude Oil and NGLs

	Oil Sands		Conventional		Total	
For the years ended December 31,	**2011**	2010	**2011**	2010	**2011**	2010
Revenues						
Gross Sales	**3,217**	2,610	**1,492**	1,229	**4,709**	3,839
Less: Royalties	**282**	276	**193**	153	**475**	429
	2,935	2,334	**1,299**	1,076	**4,234**	3,410
Expenses						
Transportation and blending	**1,229**	934	**104**	86	**1,333**	1,020
Operating	**409**	339	**244**	199	**653**	538
Production and mineral taxes	**-**	-	**27**	28	**27**	28
(Gain) loss on risk management	**87**	14	**43**	5	**130**	19
Operating Cash Flow	**1,210**	1,047	**881**	758	**2,091**	1,805

Natural Gas

	Oil Sands		Conventional		Total	
For the years ended December 31,	**2011**	2010	**2011**	2010	**2011**	2010
Revenues						
Gross Sales	**63**	78	**825**	1,042	**888**	1,120
Less: Royalties	**2**	1	**12**	17	**14**	18
	61	77	**813**	1,025	**874**	1,102
Expenses						
Transportation and blending	**2**	1	**34**	44	**36**	45
Operating	**24**	23	**240**	231	**264**	254
Production and mineral taxes	**-**	-	**9**	6	**9**	6
(Gain) loss on risk management	**(17)**	(24)	**(195)**	(263)	**(212)**	(287)
Operating Cash Flow	**52**	77	**725**	1,007	**777**	1,084

Other

	Oil Sands		Conventional		Total	
For the years ended December 31,	**2011**	2010	**2011**	2010	**2011**	2010
Revenues						
Gross Sales	**11**	14	**11**	13	**22**	27
Less: Royalties	**-**	2	**-**	-	**-**	2
	11	12	**11**	13	**22**	25
Expenses						
Transportation and blending	**-**	-	**-**	-	**-**	-
Operating	**5**	5	**4**	4	**9**	9
Production and mineral taxes	**-**	-	**-**	-	**-**	-
(Gain) loss on risk management	**-**	-	**-**	-	**-**	-
Operating Cash Flow	**6**	7	**7**	9	**13**	16

Total

	Oil Sands		Conventional		Total	
For the years ended December 31,	**2011**	2010	**2011**	2010	**2011**	2010
Revenues						
Gross Sales	**3,291**	2,702	**2,328**	2,284	**5,619**	4,986
Less: Royalties	**284**	279	**205**	170	**489**	449
	3,007	2,423	**2,123**	2,114	**5,130**	4,537
Expenses						
Transportation and blending	**1,231**	935	**138**	130	**1,369**	1,065
Operating	**438**	367	**488**	434	**926**	801
Production and mineral taxes	**-**	-	**36**	34	**36**	34
(Gain) loss on risk management	**70**	(10)	**(152)**	(258)	**(82)**	(268)
Operating Cash Flow	**1,268**	1,131	**1,613**	1,774	**2,881**	2,905

C) Geographic Information

	Canada		United States		Consolidated	
For the years ended December 31,	**2011**	2010	**2011**	2010	**2011**	2010
Revenues						
Gross Sales	**7,513**	6,466	**8,672**	6,624	**16,185**	13,090
Less: Royalties	**489**	449	**-**	-	**489**	449
	7,024	6,017	**8,672**	6,624	**15,696**	12,641
Expenses						
Purchased product	**1,867**	1,456	**7,223**	6,095	**9,090**	7,551
Transportation and blending	**1,369**	1,065	**-**	-	**1,369**	1,065
Operating	**947**	814	**459**	472	**1,406**	1,286
Production and mineral taxes	**36**	34	**-**	-	**36**	34
(Gain) loss on risk management	**(255)**	(322)	**7**	(2)	**(248)**	(324)
	3,060	2,970	**983**	59	**4,043**	3,029
Depreciation, depletion and amortization	**1,165**	1,216	**130**	86	**1,295**	1,302
Exploration expense	**-**	3	**-**	-	**-**	3
Segment Income (Loss)	**1,895**	1,751	**853**	(27)	**2,748**	1,724

The Oil Sands and Conventional segments operate in Canada. Both of Cenovus's refining facilities are located and carry on business in the U.S. The marketing of Cenovus's crude oil and natural gas produced in Canada, as well as the third party purchases and sales of product, is undertaken in Canada. Physical product sales that settle in the U.S. are considered to be export sales undertaken by a Canadian business. The Corporate and Eliminations segment is attributed to Canada with the exception of the unrealized risk management gains and losses which have been attributed to the country in which the transacting entity resides.

Export Sales

Sales of crude oil, natural gas and NGLs produced or purchased in Canada that have been delivered to customers outside of Canada were $700 million (2010 – $646 million).

Exploration and Evaluation Assets, Property, Plant and Equipment, Goodwill and Total Assets

	Exploration and Evaluation Assets			Property, Plant and Equipment		
As at	**December 31, 2011**	December 31, 2010	January 1, 2010	**December 31, 2011**	December 31, 2010	January 1, 2010
Canada	**880**	713	580	**11,124**	9,774	9,645
United States	**-**	-	-	**3,200**	2,853	2,404
Consolidated	**880**	713	580	**14,324**	12,627	12,049

	Goodwill			Total Assets		
As at	**December 31, 2011**	December 31, 2010	January 1, 2010	**December 31, 2011**	December 31, 2010	January 1, 2010
Canada	**1,132**	1,132	1,146	**17,536**	15,906	15,669
United States	**-**	-	-	**4,658**	3,934	3,380
Consolidated	**1,132**	1,132	1,146	**22,194**	19,840	19,049

2. BASIS OF PREPARATION AND STATEMENT OF COMPLIANCE

In these Consolidated Financial Statements, unless otherwise indicated, all dollars are expressed in Canadian dollars. All references to C$ or $ are to Canadian dollars and references to US$ are to U.S. dollars.

These Consolidated Financial Statements represent the Company's first annual financial statements prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and interpretations of the International Financial Reporting Interpretations Committee ("IFRIC"). These Consolidated Financial Statements have been prepared in compliance with IFRS. The Company's accounting policies have been applied consistently to all years presented with the exception of certain IFRS 1, "*First-time Adoption of International Financial Reporting Standards*" ("IFRS 1") transition elections and exemptions

the Company applied in its transition from Canadian generally accepted accounting principles ("previous GAAP") as discussed in Note 34. The impact of the transition to IFRS on the Company's financial position, results of operation and cash flows from the Consolidated Financial Statements for the year ended December 31, 2010 prepared under previous GAAP is included in Note 34.

After applying the transition exemptions of IFRS 1, these Consolidated Financial Statements have been prepared on a historical cost basis, except as detailed in the Company's accounting policies disclosed in Note 3.

The Consolidated Financial Statements of Cenovus were authorized for issuance in accordance with a resolution of the Board of Directors on February 14, 2012.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A) Principles of Consolidation

The Consolidated Financial Statements include the accounts of Cenovus and its subsidiaries. Subsidiaries are entities over which the Company has the power to govern the financial and operating policies. Subsidiaries are consolidated from the date of acquisition of control and continue to be consolidated until the date that there is a loss of control. All intercompany transactions, balances and unrealized gains and losses from intercompany transactions are eliminated on consolidation.

Investments in jointly controlled partnerships and unincorporated joint operations carry on certain of Cenovus's development, production and crude oil refining businesses and are accounted for using the proportionate consolidation method, whereby Cenovus's proportionate share of revenues, expenses, assets and liabilities are included in the consolidated accounts.

B) Segment Reporting

Management has determined the operating segments based on information regularly reviewed for the purposes of decision making, allocating resources and assessing performance by Cenovus's chief operating decision makers. The Company evaluates the financial performance of its operating segments primarily based on operating cash flow.

C) Foreign Currency Translation

Functional and Presentation Currency

The Company's presentation currency is Canadian dollars. The accounts of the Company's foreign operations that have a functional currency different from the Company's presentation currency are translated into the Company's presentation currency at period end exchange rates for assets and liabilities and at the average rate over the period for revenues and expenses. Translation gains and losses relating to the foreign operations are recognized in Other Comprehensive Income ("OCI") as cumulative translation adjustments.

When the Company disposes of an entire interest in a foreign operation or loses control, joint control, or significant influence over a foreign operation, the foreign currency gains or losses accumulated in OCI related to the foreign operation are recognized in net earnings. When the Company disposes of part of an interest in a foreign operation which continues to be a subsidiary, a proportionate amount of gains and losses accumulated in OCI is allocated between controlling and non-controlling interests.

Transactions and Balances

Transactions in foreign currencies are translated to the respective functional currencies at exchange rates in effect at the dates of the transactions. Monetary assets and liabilities of Cenovus that are denominated in foreign currencies are translated into its functional currency at the rates of exchange in effect at the period end date. Any gains or losses are recorded in the Consolidated Statements of Earnings and Comprehensive Income.

D) Revenue and Interest Income Recognition

Sales of Product

Revenues associated with the sales of Cenovus's crude oil, natural gas, NGLs and petroleum and refined products are recognized when the significant risks and rewards of ownership have been transferred to the customer, the sales price and costs can be measured reliably, and it is probable that the economic benefits will flow to the Company. This is generally met when title passes from the Company to its customer. Revenues from crude oil and natural gas production represent the Company's share, net of royalty payments to governments and other mineral interest owners.

Purchases and sales of products that are entered into in contemplation of each other with the same counterparty are recorded on a net basis. Revenues associated with the services provided as agent are recorded as the services are provided.

Interest Income

Interest income is recognized as the interest accrues using the effective interest method.

E) Transportation and Blending

The costs associated with the transportation of crude oil, natural gas and NGLs, including the cost of diluent used in blending, are recognized when the product is delivered and the services provided.

F) Production and Mineral Taxes

Costs paid to non-mineral interest owners based on production of crude oil, natural gas and NGLs are recognized when the product is sold.

G) Exploration Costs

Costs incurred prior to obtaining the legal right to explore (pre-exploration costs) are expensed in the period in which they are incurred as exploration expense.

Costs incurred after the legal right to explore is obtained, are initially capitalized. If it is determined that the field/project/area is not technically feasible or commercially viable or if the Company decides not to continue the exploration and evaluation activity, the accumulated costs are expensed as exploration expense.

H) Employee Benefit Plans

Accruals for obligations under the employee defined benefit plans and the related costs are recorded net of plan assets.

The cost of pensions and other post-employment benefits is actuarially determined using the projected credit method based on length of service, and reflects Management's best estimate of expected plan investment performance, salary escalation, retirement ages of employees and expected future health care costs. The expected return on plan assets is based on the fair value of those assets. The accrued benefit obligation is discounted using the market interest rate on high quality corporate debt instruments as at the measurement date.

Pension expense for the defined benefit pension plan includes the cost of pension benefits earned during the current year, the interest cost on pension obligations, the expected return on pension plan assets, the amortization of adjustments arising from pension plan amendments and the amortization of the excess of the net actuarial gain or loss over ten percent of the greater of the benefit obligation and the fair value of plan assets. Amortization is calculated on a straight-line basis over a period covering the non-vested expected average remaining service lives of employees and recognized immediately for vested benefits covered by the plans.

Pension expense for the defined contribution pension plans is recorded as the benefits are earned by the employees covered by the plans.

I) Income Taxes

Income taxes comprise current and deferred tax. Current and deferred income taxes are provided for on a non-discounted basis at amounts expected to be paid using the tax rates and laws that have been enacted or substantively enacted at the Balance Sheet date.

Cenovus follows the liability method of accounting for income taxes, where deferred income taxes are recorded for the effect of any temporary difference between the accounting and income tax basis of an asset or liability, using the substantively enacted income tax rates expected to apply when the assets are realized or liabilities are settled. Deferred income tax balances are adjusted to reflect changes in income tax rates that are substantively enacted with the adjustment being recognized in net earnings in the period that the change occurs except when it relates to items charged or credited directly to equity, in which case the deferred income tax is also recorded in equity.

Deferred income tax is provided on temporary differences arising from investments in subsidiaries except in the case where the timing of the reversal of the temporary difference is controlled by the Company and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets are recognized only to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized.

Deferred income tax assets and liabilities are only offset where they arise within the same entity and tax jurisdiction.

Deferred income tax assets and liabilities are presented as non-current.

J) Net Earnings per Share Amounts

Basic net earnings per common share is computed by dividing the net earnings by the weighted average number of common shares outstanding during the period. Diluted net earnings per share amounts are calculated giving effect to the potential dilution that would occur if stock options or other contracts to issue common shares were exercised or converted to common shares. The treasury stock method is used to determine the dilutive effect of stock options and other dilutive instruments. The treasury stock method assumes that proceeds received from the exercise of in-the-money stock options are used to repurchase common shares at the average market price. For those contracts that may be settled in cash or in shares at the holder's option, the more dilutive of cash settlement and share settlement is used in calculating diluted earnings per share.

K) Cash and Cash Equivalents

Cash and cash equivalents include short-term investments, such as money market deposits or similar type instruments, with a maturity of three months or less.

L) Inventories

Product inventories are valued at the lower of cost and net realizable value on a first-in, first-out or weighted average cost basis. The cost of inventory includes all costs incurred in the normal course of business to bring each product to its present location and condition. Net realizable value is the estimated selling price in the ordinary course of business less any expected selling costs. If the carrying amount exceeds net realizable value, a write-down is recognized. The write-down may be reversed in a subsequent period if the circumstances which caused it no longer exist.

M) Assets (Disposal Group) Held for Sale

Non-current assets or disposal groups are classified as held for sale when their carrying amount will principally be recovered through a sales transaction rather than through continued use and a sales transaction is highly probable. Assets held for sale are recorded at the lower of carrying value and fair value less cost to sell.

N) Exploration and Evaluation ("E&E") Assets

Costs incurred after the legal right to explore an area has been obtained and before technical feasibility and commercial viability of the area have been established are capitalized as E&E assets. These costs include license acquisition, geological and geophysical, drilling, sampling, decommissioning and other directly attributable internal costs. E&E assets are not depreciated and are carried forward until technical feasibility and commercial viability of the field/area/project is determined or the assets are determined to be impaired.

Once technical feasibility and commercial viability have been established for a field/area/project the carrying value of the E&E assets associated with that field/area/project is tested for impairment. The carrying value, net of any impairment loss, is then reclassified as property, plant and equipment.

E&E costs are subject to regular technical, commercial and management review to confirm the continued intent to develop the resources. If a field/area/project is determined to no longer be technically feasible or commercially viable and Management decides not to continue the exploration and evaluation activity, the unrecoverable costs are charged to exploration expense in the period in which the determination occurs.

Any gains or losses from the divestiture of E&E assets are recognized in net earnings.

O) Property, Plant and Equipment

Development and Production Assets

Development and production assets are stated at cost less accumulated depreciation, depletion, amortization and net impairment losses. Development and production assets are capitalized on an area-by-area basis and include all costs associated with the development and production of the crude oil and natural gas properties as well as any E&E expenditures incurred in finding commercial reserves of crude oil or natural gas transferred from E&E assets. Capitalized costs include internal costs, decommissioning liabilities, and, for qualifying assets, borrowing costs, directly associated with the acquisition of, the exploration for, and the development of crude oil and natural gas reserves.

Costs accumulated within each area are depleted using the unit-of-production method based on estimated proved reserves determined using estimated future prices and costs. For the purpose of this calculation, natural gas is converted to oil on an energy equivalent basis. Costs subject to depletion include estimated future costs to be incurred in developing proved reserves.

Exchanges of development and production assets are measured at fair value unless the transaction lacks commercial substance or the fair value of neither the asset received nor the asset given up can be reliably measured. When fair value is not used, the carrying amount of the asset given up is used as the cost of the asset acquired.

Expenditures related to renewals or betterments that improve the productive capacity or extend the life of an asset are capitalized. Maintenance and repairs are expensed as incurred. Land is not depreciated.

Any gains or losses from the divestiture of development and production assets are recognized in net earnings.

Other Upstream Assets

Other upstream assets include pipelines and information technology assets used to support the upstream business. These assets are depreciated on a straight-line basis over their useful lives of three to 35 years.

Refining Assets

The refining assets are stated at cost less accumulated depreciation and net impairment losses.

The initial acquisition costs of refining property, plant and equipment are capitalized when incurred. Costs include the cost of constructing or otherwise acquiring the equipment or facilities, the cost of installing the asset and making it ready for its intended use, the associated decommissioning costs, and for qualifying assets, borrowing costs. Routine maintenance and repair costs are expensed in the period in which they are incurred.

Capitalized costs are not subject to depreciation until the asset is available for use, after which they are depreciated on a straight-line basis over the estimated service lives of each component of the refineries. The major components are depreciated as follows:

Land Improvements and Buildings	25 to 40 years
Office Equipment and Vehicles	3 to 20 years
Refining Equipment	5 to 35 years

The residual value, method of amortization and the useful lives of each component are reviewed annually and adjusted, if appropriate.

Other Assets

Costs associated with office furniture, fixtures, leasehold improvements, information technology, marine terminal facilities and aircraft are carried at cost and depreciated on a straight-line basis over the estimated service lives of the assets, which range from three to 25 years. The residual value, method of amortization and the useful lives of the assets are reviewed annually and adjusted, if appropriate. Assets under construction are not subject to depreciation until they are available for use. Expenditures related to renewals or betterments that improve the productive capacity or extend the life of an asset are capitalized. Maintenance and repairs are expensed as incurred. Land is not depreciated.

P) Impairment

Non-Financial Assets

Property, plant and equipment and E&E assets are assessed for impairment at least annually or when facts and circumstances suggest that the carrying amount may exceed its recoverable amount. Recoverable amount is determined as the greater of an asset's or cash-generating unit's ("CGU") value-in-use ("VIU") and fair value less costs to sell ("FVLCTS"). VIU is estimated as the discounted present value of the future cash flows expected to arise from the continuing use of a CGU or asset.

The impairment test is performed at the CGU for development and production assets and other upstream assets. E&E assets are allocated to a related CGU containing development and production assets. Corporate assets are allocated to the CGUs to which they contribute to the future cash flows for the purposes of testing for impairment. For refining assets, the impairment test is performed at each refinery independently.

Impairment losses are recognized in the Consolidated Statements of Earnings and Comprehensive Income as additional depreciation, depletion and amortization and are separately disclosed. An impairment of E&E assets is recognized as exploration expense in the Consolidated Statement of Earnings and Comprehensive Income.

Goodwill is assessed for impairment at least annually. To assess impairment, the recoverable amount of the CGU to which the goodwill relates is compared to the carrying amount. If the recoverable amount of the CGU is less than the carrying amount, an impairment loss is recognized. An impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the CGU and then to reduce the carrying amounts of the other assets in the CGU. Goodwill impairments are not reversed.

Impairment losses recognized in prior periods, other than goodwill impairments, are assessed at each reporting date for any indicators that the impairment losses may no longer exist or may have decreased. In the event that an impairment loss reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but only to the extent that the carrying amount does not exceed the amount that would have been determined had no impairment loss been recognized on the asset in prior periods. The amount of the reversal is recognized in net earnings.

Financial Assets

At each reporting date, the Company assesses whether there are any indicators that its financial assets are impaired. An impairment loss is only recognized if there is objective evidence of impairment and the loss event has an impact on future cash flow and can be reliably estimated.

Evidence of impairment may include default or delinquency by a debtor or indicators that the debtor may enter bankruptcy. For equity securities a significant or prolonged decline in the fair value of the security below cost is evidence that the assets are impaired.

An impairment loss is recognized on a financial asset carried at amortized cost as the difference between the amortized cost and the present value of the future cash flows discounted at the asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account. Impairment losses on financial assets carried at amortized cost are reversed through net earnings in subsequent periods if the amount of the loss decreases.

Q) Borrowing Costs

Borrowing costs are recognized as an expense in the period in which they are incurred unless there is a qualifying asset. Borrowing costs directly associated with the acquisition, construction or production of a qualifying asset are capitalized when a substantial period of time is required to make the asset ready for its intended use. Capitalization of borrowing costs ceases when the asset is in the location and condition necessary for its intended use.

R) Government Grants

Government grants are recognized at fair value when there is reasonable assurance that the grants will be received and the Company will comply with the conditions of the grant. Grants related to assets are recorded as a reduction of the asset's carrying value and are depreciated over the useful life of the asset. Grants related to income are treated as a reduction of the related expense in the Consolidated Statement of Earnings and Comprehensive Income.

S) Leases

Leases in which substantially all the risks and rewards of ownership are retained by the lessor are classified as operating leases. Operating lease payments are recognized as an expense on a straight-line basis over the lease term.

Leases where the Company assumes substantially all the risks and rewards of ownership are classified as finance leases within property, plant and equipment.

T) Business Combinations and Goodwill

Business combinations are accounted for using the acquisition method of accounting in which the identifiable assets acquired, liabilities assumed and any non-controlling interest are recognized and measured at their fair value at the date of acquisition. Any excess of the purchase price plus any non-controlling interest over the fair value of the net assets acquired is recognized as goodwill. Any deficiency of the purchase price over the fair value of the net assets acquired is credited to net earnings.

At acquisition, goodwill is allocated to each of the CGUs to which it relates. Subsequent measurement of goodwill is at cost less any accumulated impairment losses.

U) Provisions

General

A provision is recognized if, as a result of a past event, the Company has a present obligation, legal or constructive, that can be estimated reliably, and it is more likely than not that an outflow of economic benefits will be required to settle the obligation. Where applicable, provisions are determined by discounting the expected future cash flows at a pre-tax credit-adjusted rate that reflects current market assessments of the time value of money and the risks specific to the liability. The increase in the provision due to the passage of time is recognized as a finance cost in the Consolidated Statements of Earnings and Comprehensive Income.

Decommissioning Liabilities

Decommissioning liabilities include those legal or constructive obligations where the Company will be required to retire tangible long-lived assets such as producing well sites, crude oil and natural gas processing facilities and refining facilities. The amount recognized is the present value of estimated future expenditures required to settle the obligation using a credit-adjusted risk-free rate. A corresponding asset equal to the initial estimated liability is capitalized as part of the cost of the related long-lived asset. Changes in the estimated liability resulting from revisions to estimated timing or future decommissioning cost estimates are recognized as a change in the decommissioning liability and the related long-lived asset. The amount capitalized in property, plant and equipment is depreciated over the useful life of the related asset. Increases in the decommissioning liabilities resulting from the passage of time are recognized as a finance cost in the Consolidated Statements of Earnings and Comprehensive Income.

Actual expenditures incurred are charged against the accumulated liability.

V) Share Capital

Common shares are classified as equity. Transaction costs directly attributable to the issue of common shares are recognized as a deduction from equity, net of any income tax.

W) Dividends

Dividends are accrued when declared by the Board of Directors.

X) Stock-Based Compensation

Cenovus has a number of cash and stock-based compensation plans which include stock options with associated tandem stock appreciation rights, stock options with associated net settlement rights, performance share units and deferred share units.

Tandem Stock Appreciation Rights

Stock options with associated tandem stock appreciation rights ("TSARs") are accounted for as liability instruments which are measured at the fair value at each period end using the Black-Scholes-Merton valuation model. The fair value is recognized as compensation costs over the vesting period. When options are settled for cash, the liability is reduced by the cash settlement paid. When options are settled for common shares, the cash consideration received by the Company and the previously recorded liability associated with the option are recorded as share capital.

Net Settlement Rights

Stock options with associated net settlement rights ("NSRs") are accounted for as equity instruments which are measured at fair value on the grant date using the Black-Scholes-Merton valuation model and are not revalued at each reporting date. The fair value is recognized as compensation costs over the vesting period of the options, with a corresponding increase recorded as paid in surplus in Shareholders' Equity. On exercise, the consideration received by the Company and the associated paid in surplus are recorded as share capital.

Performance and Deferred Share Units

Performance share units ("PSUs") and deferred share units ("DSUs") are accounted for as liability instruments and are measured at fair value based on the market value of the Cenovus common shares at each period end. The fair value is recognized as compensation costs over the vesting period. Fluctuations in the fair values are recognized as compensation costs in the period they occur.

Y) Financial Instruments

Financial instruments are recognized when the Company becomes a party to the contractual provisions of the instrument. Financial assets and liabilities are not offset unless the Company has the legal right to offset and intends to settle on a net basis or settle the asset and liability simultaneously. A financial asset is derecognized when the rights to receive cash flows from the asset have expired or have been transferred and the Company has transferred substantially all the risks and rewards of ownership. A financial liability is derecognized when the obligation is discharged, cancelled or expired. When an existing financial liability is replaced by another from the same counterparty with substantially different terms, or the terms of an existing liability are substantially modified, this exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability. The difference in the carrying amounts of the liabilities is recognized in the Consolidated Statement of Earnings and Comprehensive Income.

Financial instruments are classified as either "fair value through profit and loss", "loans and receivables", "held-to-maturity investments", "available for sale financial assets" or "financial liabilities measured at amortized cost". The Company determines the classification of its financial assets at initial recognition. Financial instruments are initially measured at fair value except in the case of "financial liabilities measured at amortized cost" which are initially measured at fair value net of directly attributable transaction costs.

The Company's financial assets include cash and cash equivalents, accounts receivable and accrued revenues, partner loans receivable, the Partnership Contribution Receivable, risk management assets and long-term receivables. The Company's financial liabilities include accounts payable and accrued liabilities, partner loans payable, the Partnership Contribution Payable, derivative financial instruments, short-term borrowings and long-term debt.

Fair Value through Profit or Loss

Financial assets and financial liabilities at "fair value through profit or loss" are either "held-for-trading" or have been "designated at fair value through profit or loss". In both cases the financial assets and financial liabilities are measured at fair value with changes in fair value recognized in net earnings.

Risk management assets and liabilities are derivative financial instruments classified as "held-for-trading" unless designated for hedge accounting. Derivative instruments that do not qualify as hedges, or are not designated as hedges, are recorded using mark-to-market accounting whereby instruments are recorded in the Consolidated Balance Sheets as either an asset or liability with changes in fair value recognized in net earnings as a (gain) loss on risk management. The estimated fair value of all derivative instruments is based on quoted market prices or, in their absence, third-party market indications and forecasts.

Derivative financial instruments are used to manage economic exposure to market risks relating to commodity prices, foreign currency exchange rates and interest rates. Derivative financial instruments are not used for speculative purposes. Policies and procedures are in place with respect to the required documentation and approvals for the use of derivative financial instruments. Where specific financial instruments are executed, the Company assesses, both at the time of purchase and on an ongoing basis, whether the financial instrument used in the particular transaction is effective in offsetting changes in fair values or cash flows of the transaction.

Loans and Receivables

"Loans and receivables" are financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement, these assets are measured at amortized cost at the settlement date using the effective interest method of amortization. "Loans and receivables" comprise cash and cash equivalents, accounts receivable and accrued revenue, partner loans receivable, the Partnership Contribution Receivable and long-term receivables. Gains and losses on "loans and receivables" are recognized in net earnings when the "loans and receivables" are derecognized or impaired.

Held to Maturity Investments

"Held-to-maturity investments" are measured at amortized cost at the settlement date using the effective interest method of amortization.

Available for Sale Financial Assets

"Available for sale financial assets" are measured at fair value at the settlement date, with changes in the fair value recognized in other comprehensive income. When an active market is non-existent, fair value is determined using valuation techniques. When fair value cannot be reliably measured, such assets are carried at cost.

Financial Liabilities Measured at Amortized Cost

These financial liabilities are measured at amortized cost at the settlement date using the effective interest method of amortization. Financial liabilities measured at amortized cost comprise accounts payable and accrued liabilities, partner loans payable, the Partnership Contribution Payable, short-term borrowings and long-term debt. Long-term debt transaction costs, premiums and discounts are capitalized within long-term debt or as a prepayment and amortized using the effective interest method.

Z) Reclassification

Certain information provided for prior years has been reclassified to conform to the presentation adopted in 2011.

AA) Recent Accounting Pronouncements

Joint Arrangements and Off Balance Sheet Activities

In May 2011, the IASB issued the following new and amended standards:

- IFRS 10, "*Consolidated Financial Statements*" ("IFRS 10") replaces IAS 27, "*Consolidated and Separate Financial Statements*" ("IAS 27") and Standing Interpretations Committee ("SIC") 12, "*Consolidation – Special Purpose Entities*". IFRS 10 revises the definition of control and focuses on the need to have power and variable returns for control to be present. IFRS 10 provides guidance on participating and protective rights and also addresses the notion of "de facto" control. It also includes guidance related to an investor with decision making rights to determine if it is acting as a principal or agent.

- IFRS 11, "*Joint Arrangements*" ("IFRS 11") replaces IAS 31, "*Interest in Joint Ventures*" ("IAS 31") and SIC 13, "*Jointly Controlled Entities – Non-Monetary Contributions by Venturers*". IFRS 11 defines a joint arrangement as an arrangement where two or more parties have joint control. A joint arrangement is classified as either a "joint operation" or a "joint venture" depending on the facts and circumstances. A joint operation is a joint arrangement where the parties that have joint control have rights to the assets and obligations for the

liabilities, related to the arrangement. A joint operator accounts for its share of the assets, liabilities, revenues and expenses of the joint arrangement. A joint venturer has the rights to the net assets of the arrangement and accounts for the arrangement as an investment using the equity method.

- IFRS 12, "*Disclosure of Interest in Other Entities*" ("IFRS 12") replaces the disclosure requirements previously included in IAS 27, IAS 31, and IAS 28, "*Investments in Associates*". It sets out the extensive disclosure requirements relating to an entity's interests in subsidiaries, joint arrangements, associates and unconsolidated structured entities. An entity is required to disclose information that helps users of its financial statements evaluate the nature of and risks associated with its interests in other entities and the effects of those interests on its financial statements.

- IAS 27, "*Separate Financial Statements*" has been amended to conform to the changes made in IFRS 10 but retains the current guidance for separate financial statements.

- IAS 28, "*Investments in Associates and Joint Ventures*" has been amended to conform to the changes made in IFRS 10 and IFRS 11.

The above standards are effective for annual periods beginning on or after January 1, 2013. Early adoption is permitted, providing the five standards are adopted concurrently. The Company is currently evaluating the impact of adopting these standards on its Consolidated Financial Statements.

Employee Benefits

In June 2011, the IASB amended IAS 19, "*Employee Benefits*" ("IAS 19"). The amendment eliminates the option to defer the recognition of actuarial gains and losses, commonly known as the corridor approach, rather it requires an entity to recognize actuarial gains and losses in Other Comprehensive Income ("OCI") immediately. In addition, the net change in the defined benefit liability or asset must be disaggregated into three components: service cost, net interest and remeasurements. Service cost and net interest will continue to be recognized in net earnings while remeasurements, which include changes in estimates or the valuation of plan assets, will be recognized in OCI. Furthermore, entities will be required to calculate net interest on the net defined benefit liability or asset using the same discount rate used to measure the defined benefit obligation. The amendment also enhances financial statement disclosures. This amended standard is effective for annual periods beginning on or after January 1, 2013, with modified retrospective application. Earlier adoption is permitted. The Company is currently evaluating the impact of adopting these amendments on its Consolidated Financial Statements.

Fair Value Measurement

In May 2011, the IASB issued IFRS 13, "*Fair Value Measurement*" ("IFRS 13") which provides a consistent and less complex definition of fair value, establishes a single source for determining fair value and introduces consistent requirements for disclosures related to fair value measurement. IFRS 13 is effective for annual periods beginning on or after January 1, 2013 and applies prospectively from the beginning of the annual period in which the standard is adopted. Early adoption is permitted. The Company is currently evaluating the impact of adopting IFRS 13 on its Consolidated Financial Statements.

Financial Instruments

The IASB intends to replace IAS 39, "*Financial Instruments: Recognition and Measurement*" ("IAS 39") with IFRS 9, "*Financial Instruments*" ("IFRS 9"). IFRS 9 will be published in three phases, of which the first phase has been published.

The first phase addresses the accounting for financial assets and financial liabilities. The second phase will address the impairment of financial instruments, and the third phase will address hedge accounting.

For financial assets, IFRS 9 uses a single approach to determine whether a financial asset is measured at amortized cost or fair value, and replaces the multiple rules in IAS 39. The approach in IFRS 9 is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. The new standard also requires a single impairment method to be used, replacing the multiple impairment methods in IAS 39. For financial liabilities, although the classification criteria for financial liabilities will not change under IFRS 9, the approach to the fair value option for financial liabilities may require different accounting for changes to the fair value of a financial liability as a result of changes to an entity's own credit risk.

IFRS 9 is effective for annual periods beginning on or after January 1, 2015 with different transitional arrangements depending on the date of initial application. The Company is currently evaluating the impact of adopting IFRS 9 on its Consolidated Financial Statements.

Presentation of Items of Other Comprehensive Income

In June 2011, the IASB issued an amendment to IAS 1, "*Presentation of Financial Statements*" ("IAS 1") requiring companies to group items presented within Other Comprehensive Income based on whether they may be subsequently reclassified to profit or loss. This amendment to IAS 1 is effective for annual periods beginning on or after July 1, 2012 with full retrospective application. Early adoption is permitted. The Company is currently evaluating the impact of adopting this amendment on its Consolidated Financial Statements.

Offsetting Financial Assets and Financial Liabilities

In December 2011, the IASB issued the following amended standards:

- IFRS 7, *"Financial Instruments: Disclosures"* ("IFRS 7"), has been amended to provide more extensive quantitative disclosures for financial instruments that are offset in the statement of financial position or that are subject to enforceable master netting or similar arrangements.

- IAS 32, *"Financial Instruments: Presentation"* ("IAS 32"), has been amended to clarify the requirements for offsetting financial assets and liabilities. The amendments clarify that the right to offset must be available on the current date and cannot be contingent on a future event.

The amendments to IFRS 7 are effective for annual periods beginning on or after January 1, 2013 and the amendments to IAS 32 are effective for annual periods beginning on or after January 1, 2014, both requiring retrospective application. The Company is currently evaluating the impact of adopting the amendments to IFRS 7 and IAS 32 on its Consolidated Financial Statements.

4. SIGNIFICANT ACCOUNTING JUDGEMENTS, ESTIMATES AND ASSUMPTIONS

The timely preparation of the Consolidated Financial Statements in accordance with IFRS requires that Management make estimates and assumptions and use judgment regarding the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the Consolidated Financial Statements and the reported amounts of revenues and expenses during the period. Such estimates primarily relate to unsettled transactions and events as of the date of the Consolidated Financial Statements. The estimated fair value of financial assets and liabilities, by their very nature, are subject to measurement uncertainty. Accordingly, actual results may differ from estimated amounts as future confirming events occur. Significant judgments, estimates and assumptions made by Management in the preparation of these Consolidated Financial Statements are outlined below.

Carrying Value of Property, Plant and Equipment

Development and production assets within property, plant and equipment are depreciated, depleted and amortized using the unit-of-production method based on estimated proved reserves determined using estimated future prices and costs. There are a number of inherent uncertainties associated with estimating reserves. By their nature, these estimates of reserves, including the estimates of future prices and costs, and related future cash flows are subject to measurement uncertainty, and the impact on the Consolidated Financial Statements of future periods could be material.

Refining, marketing, other upstream and corporate assets are depreciated on a straight-line basis and are subject to Management's estimate of useful life and salvage value. Changes to the estimated useful life and salvage value could have a material impact on the Consolidated Financial Statements of future periods.

Carrying Value of Exploration and Evaluation Assets

The application of the Company's accounting policy for exploration and evaluation expenditures requires judgment in determining whether it is likely that future economic benefit exists when activities have not reached a stage where technical feasibility and commercial viability can be reasonably determined and when technical feasibility and commercial viability have been reached. Estimates and assumptions may change as new information becomes available.

Decommissioning Costs

Provisions are recognized for the future decommissioning and restoration of the Company's upstream oil and gas assets and refining assets at the end of their economic lives. Assumptions have been made to estimate the future liability based on past experience and current economic factors which Management believes are reasonable. However, the actual cost of decommissioning is uncertain and cost estimates may change in response to numerous factors including changes in legal requirements, technological advances, inflation and the timing of expected decommissioning and restoration. The impact to net earnings over the remaining economic life of the assets could be significant due to the changes in cost estimates as new information becomes available. In addition, Management determines the appropriate discount rate at the end of each reporting period. This discount rate, which is credit adjusted, is used to determine the present value of the estimated future cash outflows required to settle the obligation and may change in response to numerous market factors.

Impairment of Assets

The recoverable amounts of CGUs and individual assets have been determined as the greater of an asset's or CGU's value-in-use and fair value less costs to sell. These calculations require the use of estimates and assumptions and are subject to changes as new information becomes available including information on future commodity prices, expected production volumes, quantity of reserves and discount rates as well as future development and operating costs. Changes in assumptions used in determining the recoverable amount could affect the carrying value of the related assets and CGUs.

For impairment testing purposes, goodwill has been allocated to each of the CGUs to which it relates.

At December 31, 2011, the recoverable amounts of Cenovus's Upstream CGUs were determined based on fair value less costs to sell. Key assumptions in the determination of cash flows from reserves include reserves as estimated by Cenovus's independent qualified reserve evaluators, oil and natural gas prices and the discount rate.

Reserves

Reserve estimates are dependent on a number of variables including the recoverable quantities of hydrocarbons, the cost of the development of the required infrastructure to recover the hydrocarbons, production costs and estimated selling price of the hydrocarbons produced. Changes in these variables could significantly impact the reserve estimates. The Company's oil and gas reserves are evaluated and reported to the Company by independent qualified reserves evaluators.

Oil and natural gas prices

The future prices used to determine cash flows from oil and gas reserves are as follows:

	2012	2013	2014	2015	2016	Average Annual % Change to 2023
WTI (US$/barrel)	97.50	97.50	100.00	100.80	101.70	1.3%
AECO ($/Mcf)	3.50	4.20	4.70	5.10	5.55	3.5%

Discount rate

A discount rate of 10 percent has been used to determine the present value of future cash flows. Changes in the economic conditions could significantly change the estimated recoverable amount.

Employee Benefit Plans and Post-Employment Benefits

The values of pension assets and obligations and the amount of pension costs charged to net earnings depend on certain actuarial and economic assumptions which, by their nature, are subject to measurement uncertainty.

Compensation Plans

The amount of compensation expense accrued for long-term performance-based compensation arrangements is subject to Management's best estimate of whether or not the performance criteria will be met and what the ultimate payout will be. Certain obligations for payments under the Cenovus compensation plans are measured at fair value and therefore fluctuations in the fair value will affect the accrued compensation expense that is recognized. The fair value of the obligation is based on several assumptions including the risk-free interest rate, dividend yield, and the expected volatility of the share price and therefore is subject to measurement uncertainty.

Income Tax Provisions

Tax regulations and legislation and the interpretations thereof in the various jurisdictions in which Cenovus operates are subject to change. As a result there are usually a number of tax matters under review. As such, income taxes are subject to measurement uncertainty.

Deferred income tax assets are recognized to the extent that it is probable that the deductible temporary differences will be recoverable in future periods. The recoverability assessment involves a significant amount of estimation including an evaluation of when the temporary differences will reverse, an analysis of the amount of future taxable earnings, the availability of cash flow to offset the tax assets when the reversal occurs and the application of tax laws. To the extent that assumptions used in the recoverability assessment change, there may be a significant impact on the Consolidated Financial Statements of future periods.

Contingencies

Contingencies, by their nature, are subject to measurement uncertainty as the financial impact will only be confirmed by the outcome of a future event. The assessment of contingencies involves a significant amount of judgment including assessing whether a present obligation exists and providing a reliable estimate of the amount of cash outflow required to settle the obligation. The uncertainty involved with the timing and amount at which a contingency will be settled may have a material impact on the Consolidated Financial Statements of future periods to the extent that the amount provided for differs from the actual outcome.

Financial Instruments

The estimated fair values of financial assets and liabilities, by their very nature, are subject to measurement uncertainty due to their exposure to credit, liquidity and market risks. Furthermore, the Company may use derivative instruments to manage commodity price, foreign currency and interest rate exposures. The fair values of these derivatives are determined using valuation models which require assumptions concerning the amount and timing of future cash flows and discount rates. Management's assumptions rely on external observable market data including quoted commodity prices and volatility, interest rate yield curves and foreign exchange rates. The resulting fair value estimates may not be indicative of the amounts realized or settled in current market transactions and as such are subject to measurement uncertainty.

5. FINANCE COSTS

For the years ended December 31,	**2011**	2010
Interest Expense – Short-Term Borrowings and Long-Term Debt	**213**	227
Interest Expense – Partnership Contribution Payable	**138**	165
Unwinding of Discount on Decommissioning Liabilities	**75**	75
Other	**21**	31
	447	498

6. INTEREST INCOME

For the years ended December 31,	**2011**	2010
Interest Income – Partnership Contribution Receivable	**120**	144
Other	**4**	-
	124	144

7. FOREIGN EXCHANGE (GAIN) LOSS, NET

For the years ended December 31,	2011	2010
Unrealized Foreign Exchange (Gain) Loss on translation of:		
U.S. dollar debt issued from Canada	**78**	(182)
U.S. dollar Partnership Contribution Receivable issued from Canada	**(107)**	91
Other	**(13)**	22
Unrealized Foreign Exchange (Gain) Loss	**(42)**	(69)
Realized Foreign Exchange (Gain) Loss	**68**	18
	26	(51)

8. INCOME TAXES

The provision for income taxes is as follows:

For the years ended December 31,	2011	2010
Current Tax		
Canada	**150**	82
United States	**4**	-
Total Current Tax	**154**	82
Deferred Tax	**575**	141
	729	223

The following table reconciles income taxes calculated at the Canadian statutory rate with the recorded income taxes:

For the years ended December 31,	2011	2010
Earnings Before Income Tax	**2,207**	1,304
Canadian Statutory Rate	**26.7%**	28.2%
Expected Income Tax	**589**	368
Effect of Taxes Resulting from:		
Foreign tax rate differential	**78**	(22)
Non-deductible stock-based compensation	**18**	34
Multi-jurisdictional financing	**(50)**	(93)
Foreign exchange gains (losses) not included in net earnings	**(9)**	28
Non-taxable capital (gains) losses	**(9)**	(13)
Capital losses	**26**	(107)
Adjustments arising from prior year tax filings	**31**	26
Other	**55**	2
	729	223
Effective Tax Rate	**33.0%**	17.1%

The Canadian statutory tax rate decreased to 26.7 percent in 2011 from 28.2 percent in 2010 as a result of tax legislation enacted in 2007.

The analysis of deferred income tax liabilities and deferred income tax assets is as follows:

As at	**December 31, 2011**	December 31, 2010	January 1, 2010
Deferred Income Tax Liabilities			
Deferred tax liabilities (assets) to be settled (recovered) within 12 months	**117**	57	(68)
Deferred tax liabilities to be settled after more than 12 months	**1,984**	1,515	1,552
	2,101	1,572	1,484
Deferred Income Tax Assets			
Deferred tax assets to be recovered within 12 months	**-**	(3)	-
Deferred tax assets to be recovered after more than 12 months	**-**	(52)	(3)
	-	(55)	(3)
Net Deferred Income Tax Liability	**2,101**	1,517	1,481

For the purposes of the above table, deferred income tax assets are shown net of offsetting deferred income tax liabilities where these occur in the same entity and jurisdiction. The deferred income tax liabilities and assets to be settled (recovered) within 12 months represents Management's estimate of the timing of the reversal of temporary differences and does not correlate to the current income tax expense of the subsequent year.

The movement in deferred income tax liabilities and assets, without taking into consideration the offsetting of balances within the same tax jurisdiction, is as follows:

Deferred Income Tax Liabilities	**Property, Plant and Equipment**	**Timing Of Partnership Items**	**Net Foreign Exchange Gains**	**Risk Management**	**Other**	**Total**
As at January 1, 2010	1,678	9	61	17	-	1,765
Charged/(credited) to earnings	83	116	66	38	54	357
Charged/(credited) to held for sale	2	-	-	-	-	2
Charged/(credited) to other comprehensive income	(112)	-	-	-	1	(111)
As at December 31, 2010	1,651	125	127	55	55	2,013
Charged/(credited) to earnings	725	38	(15)	16	75	839
Charged/(credited) to other comprehensive income	18	-	-	-	2	20
As at December 31, 2011	**2,394**	**163**	**112**	**71**	**132**	**2,872**

Deferred Income Tax Assets	**Unused Tax Losses**	**Risk Management**	**Other**	**Total**
As at January 1, 2010	(242)	(33)	(9)	(284)
Charged/(credited) to earnings	(47)	(12)	(161)	(220)
Charged/(credited) to other comprehensive income	8	-	-	8
As at December 31, 2010	(281)	(45)	(170)	(496)
Charged/(credited) to earnings	(270)	29	(21)	(262)
Charged/(credited) to other comprehensive income	(13)	-	-	(13)
As at December 31, 2011	**(564)**	**(16)**	**(191)**	**(771)**

Net Deferred Income Tax Liabilities	**Total**
Net Deferred Income Tax Liabilities as at January 1, 2010	1,481
Charged/(credited) to earnings	137
Charged/(credited) to held for sale	2
Charged/(credited) to other comprehensive income	(103)
Net Deferred Income Tax Liabilities as at December 31, 2010	1,517
Charged/(credited) to earnings	577
Charged/(credited) to other comprehensive income	7
Net Deferred Income Tax Liabilities as at December 31, 2011	**2,101**

The allocation of deferred income tax expense is comprised of:

As at	**December 31, 2011**	December 31, 2010
Credited/(charged) to net deferred income tax liabilities	**577**	137
Credited/(charged) to liabilities related to assets held for sale	**(2)**	4
Deferred Income Tax Expense	**575**	141

No tax liability has been recognized in respect of temporary differences associated with investments in subsidiaries. As no taxes are expected to be paid in respect of these differences related to Canadian subsidiaries the amounts have not been determined. There are no taxable temporary differences associated with investments in non-Canadian subsidiaries.

The approximate amounts of tax pools available are as follows:

As at	**December 31, 2011**	December 31, 2010	January 1, 2010
Canada	**4,471**	4,239	3,754
United States	**2,740**	3,082	2,637
	7,211	7,321	6,391

At December 31, 2011, the above tax pools included $78 million (December 31, 2010 – $236 million, January 1, 2010 – $491 million) of Canadian non-capital losses and $1,479 million (December 31, 2010 – $607 million, January 1, 2010 – $232 million) of U.S. net operating losses. These losses expire no earlier than 2029.

Also included in the December 31, 2011 tax pools are Canadian net capital losses totaling $759 million (December 31, 2010 – $983 million, January 1, 2010 – $51 million) which are available for carry forward to reduce future capital gains. Of these losses, $286 million are unrecognized as a deferred income tax asset at December 31, 2011 (December 31, 2010 – $415 million). Recognition is dependent on the level of future capital gains.

9. PER SHARE AMOUNTS

A) Net Earnings per Share

For the years ended ($ millions, except earnings per share)	**December 31, 2011** Net Earnings	Shares	Earnings per Share	December 31, 2010 Net Earnings	Shares	Earnings per Share
Net earnings per share – basic	**1,478**	**754.0**	**$1.96**	1,081	751.9	$1.44
Dilutive effect of Cenovus TSARs	**-**	**3.7**		-	2.1	
Dilutive effect of NSRs	**-**	**-**		-	-	
Net earnings per share – diluted	**1,478**	**757.7**	**$1.95**	1,081	754.0	$1.43

B) Dividends per Share

The dividends paid in 2011 and 2010 were $603 million ($0.80 per share) and $601 million ($0.80 per share) respectively. The Cenovus Board of Directors declared a first quarter 2012 dividend of $0.22 per share, payable on March 30, 2012, to common shareholders of record as of March 15, 2012.

10. CASH AND CASH EQUIVALENTS

As at	**December 31, 2011**	December 31, 2010	January 1, 2010
Cash	**232**	160	76
Short-Term Investments	**263**	140	79
	495	300	155

11. ACCOUNTS RECEIVABLE AND ACCRUED REVENUES

As at	**December 31, 2011**	December 31, 2010	January 1, 2010
Accruals	**801**	606	409
Trade	**251**	242	395
Joint Operations with Partners	**30**	32	32
Prepaids and Deposits	**34**	24	20
Interest	**28**	32	38
Other	**261**	123	88
	1,405	1,059	982

12. PARTNERSHIP CONTRIBUTION RECEIVABLE AND PAYABLE

In connection with the Arrangement with Encana (Note 1), Cenovus acquired Encana's assets which are jointly controlled with ConocoPhillips. On January 2, 2007, Encana became a 50 percent partner in an integrated, North American oil business with ConocoPhillips which consisted of an upstream entity and a refining entity. The upstream entity contribution included assets from Encana, primarily the Foster Creek and Christina Lake properties, with a fair value of US$7.5 billion and a note receivable (Partnership Contribution Receivable) contributed from ConocoPhillips of an equal amount. For the refining entity, ConocoPhillips contributed its Wood River and Borger refineries, located in Illinois and Texas, respectively, for a fair value of US$7.5 billion and Encana contributed a note payable (Partnership Contribution Payable) of US$7.5 billion.

These entities are accounted for using the proportionate consolidation method with the results of operations included in the Oil Sands and Refining and Marketing segments (Note 29).

Partnership Contribution Receivable

This note receivable is denominated in US$ and bears interest at a rate of 5.3 percent per annum. Equal payments of principal and interest are payable quarterly, with final payment due January 2, 2017. The current and long-term Partnership Contribution Receivable shown in the Consolidated Balance Sheets represent Cenovus's 50 percent share of this promissory note, net of payments to date.

Mandatory Receipts – Partnership Contribution Receivable

	2012	2013	2014	2015	2016	Thereafter	**Total**
US$	366	386	407	429	452	117	**2,157**
C$ equivalent	372	393	414	436	460	119	**2,194**

Partnership Contribution Payable

This note payable is denominated in US$ and bears interest at a rate of 6.0 percent per annum. Equal payments of principal and interest are payable quarterly, with final payment due January 2, 2017. The current and long-term Partnership Contribution Payable amounts shown in the Consolidated Balance Sheets represent Cenovus's 50 percent share of this promissory note, net of payments to date.

Mandatory Payments – Partnership Contribution Payable

	2012	2013	2014	2015	2016	Thereafter	**Total**
US$	366	388	412	437	464	121	**2,188**
C$ equivalent	372	395	419	445	472	122	**2,225**

In addition to the Partnership Contribution Receivable and Payable, Other Assets and Other Liabilities include equal amounts for interest bearing partner loans, with no fixed repayment terms, related to the funding of refining operating and capital requirements. At December 31, 2011 these amounts were $nil (December 31, 2010 – $274 million, January 1, 2010 – $183 million) (Notes 18 and 23).

13. INVENTORIES

As at	**December 31, 2011**	December 31, 2010	January 1, 2010
Product			
Refining and Marketing	**1,079**	779	772
Oil Sands	**186**	80	84
Conventional	**1**	-	-
Parts and Supplies	**25**	21	19
	1,291	880	875

The total amount of inventories recognized as an expense during the year was $7,189 million (2010 – $5,997 million).

14. ASSETS AND LIABILITIES HELD FOR SALE

Assets and liabilities classified as held for sale consisted of the following:

As at	**December 31, 2011**	December 31, 2010	January 1, 2010
Assets Held for Sale			
Property, plant and equipment	**116**	65	-
Liabilities Related to Assets Held for Sale			
Decommissioning liabilities	**54**	5	-
Deferred income taxes	**-**	2	-
	54	7	-

Non-Core Natural Gas Assets

At December 31, 2011, the Company classified certain non-core natural gas assets located in Northern Alberta as assets held for sale. The assets were recorded at the lesser of fair value less costs to sell and their carrying amount, resulting in an impairment loss of approximately $2 million which has been recorded as additional depreciation, depletion and amortization in the Consolidated Statement of Earnings and Comprehensive Income. These assets and the related liabilities are reported in the Conventional segment.

In January 2012, the Company completed the sale of the natural gas assets to an unrelated third party for net proceeds of $63 million.

Marine Terminal Facilities

On November 1, 2010, under the terms of an agreement with a non-related Canadian company, Cenovus acquired certain marine terminal facilities in Kitimat, British Columbia for cash consideration of $38 million. The net assets were recorded at estimated fair value less costs to sell and classified as held for sale. These assets and liabilities were reported in the Refining and Marketing segment. Cenovus recognized a bargain purchase gain of $12 million, resulting from the excess fair value of the net assets acquired over the cash consideration paid. The gain was recorded in other income.

In October 2011, the Company completed the sale of the marine terminal facilities and recorded an after-tax gain on sale of $89 million.

15. EXPLORATION AND EVALUATION ASSETS

	E&E
COST	
As at January 1, 2010	580
Additions	350
Transfers to property, plant and equipment (Note 16)	(144)
Divestitures	(81)
Change in decommissioning liabilities	8
As at December 31, 2010	713
Additions	527
Transfers to property, plant and equipment (Note 16)	(356)
Divestitures	(3)
Change in decommissioning liabilities	(1)
As at December 31, 2011	**880**

E&E assets consist of the Company’s evaluation projects which are pending the determination of technical feasibility and commercial viability. All of the Company’s E&E assets are located within Canada.

Additions to E&E assets for the year ended December 31, 2011 include $15 million of internal costs directly related to the evaluation of these projects (year ended December 31, 2010 – $11 million).

For the year ended December 31, 2011, $356 million of E&E assets were transferred to property, plant and equipment – development and production assets following the determination of technical feasibility and commercial viability of the projects in question (year ended December 31, 2010 – $144 million).

Impairment

The impairment of E&E assets and any subsequent reversal of such impairment losses are recognized in exploration expense in the Consolidated Statement of Earnings and Comprehensive Income. There were no impairments of E&E assets in 2011 and 2010.

16. PROPERTY, PLANT AND EQUIPMENT, NET

	Upstream Assets				
	Development & Production	Other Upstream	Refining Equipment	Other [1]	Total
COST					
As at January 1, 2010	20,836	134	2,419	427	23,816
Additions	1,061	19	651	136	1,867
Transfers from E&E assets (Note 15)	144	-	-	-	144
Transfers and reclassifications	-	-	-	(92)	(92)
Change in decommissioning liabilities	237	-	22	-	259
Exchange rate movements	(2)	-	(142)	-	(144)
Divestitures	(556)	-	-	(21)	(577)
As at December 31, 2010	21,720	153	2,950	450	25,273
Additions	1,704	41	391	131	2,267
Transfers from E&E assets (Note 15)	356	-	-	-	356
Transfers and reclassifications	(326)	-	(5)	(2)	(333)
Change in decommissioning liabilities	403	-	10	1	414
Exchange rate movements	1	-	79	-	80
Divestitures	-	-	-	(4)	(4)
As at December 31, 2011	**23,858**	**194**	**3,425**	**576**	**28,053**
ACCUMULATED DEPRECIATION, DEPLETION AND IMPAIRMENT					
As at January 1, 2010	11,342	113	15	297	11,767
Depreciation and depletion expense	1,163	11	72	42	1,288
Transfers and reclassifications	-	-	-	(28)	(28)
Impairment losses	-	-	14	-	14
Exchange rate movements	(1)	-	(4)	-	(5)
Divestitures	(383)	-	-	(7)	(390)
As at December 31, 2010	12,121	124	97	304	12,646
Depreciation and depletion expense	1,108	15	85	40	1,248
Impairment losses	2	-	45	-	47
Transfers and reclassifications	(211)	-	(5)	-	(216)
Exchange rate movements	1	-	3	-	4
As at December 31, 2011	**13,021**	**139**	**225**	**344**	**13,729**
CARRYING VALUE					
As at January 1, 2010	9,494	21	2,404	130	12,049
As at December 31, 2010	9,599	29	2,853	146	12,627
As at December 31, 2011	**10,837**	**55**	**3,200**	**232**	**14,324**

1. Includes office furniture, fixtures, leasehold improvements, information technology, aircraft and marine terminal facilities.

Additions to development and production assets include internal costs directly related to the development, construction and production of oil and gas properties of $125 million (2010 – $87 million). All of the Company's development and production assets are located within Canada. Costs classified as general and administrative expenses have not been capitalized as part of capital expenditures. No borrowing costs have been capitalized in 2011 (2010 – $nil).

Property, plant and equipment include the following amounts in respect of assets under construction which are not subject to depreciation until put into use:

As at	**December 31, 2011**	December 31, 2010	January 1, 2010
Development and production	**52**	42	64
Refining equipment	**125**	1,673	1,366
Other	**112**	45	4
	289	1,760	1,434

Impairment

The impairment of property, plant and equipment and any subsequent reversal of such impairment losses are recognized in depreciation, depletion and amortization in the Consolidated Statement of Earnings and Comprehensive Income.

Depreciation, depletion and amortization expense includes impairment losses as follows:

As at	**December 31, 2011**	December 31, 2010	January 1, 2010
Development and Production	**2**	-	-
Refining Equipment	**45**	14	-
	47	14	-

The impairment losses during the year were related to a catalytic cracking unit at the Wood River Refinery, which will not be used in future operations and an impairment on non-core natural gas assets that have been reclassified as held for sale (Note 14). The natural gas assets reside in the Conventional segment. The 2010 impairment loss was related to a processing unit at the Borger Refinery which was determined to be a redundant asset.

17. DIVESTITURES

In 2011, the Company disposed of non-core oil and gas properties and marine terminal facilities recognizing an after-tax gain of $91 million in the Statement of Earnings and Comprehensive Income. In 2010, an after-tax gain of $116 million was recognized on the disposition of non-core oil and gas properties and corporate assets.

18. OTHER ASSETS

As at	**December 31, 2011**	December 31, 2010	January 1, 2010
Partner Loans	**-**	274	183
Long-term Receivables	**18**	7	7
Prepaids	**8**	-	-
Other	**18**	-	2
	44	281	192

19. GOODWILL

As at	**December 31, 2011**	December 31, 2010
Carrying Value, Beginning of Year	**1,132**	1,146
Divestitures	**-**	(14)
Impairment	**-**	-
Carrying Value, End of Year	**1,132**	1,132
Cost	**1,132**	1,132
Accumulated Impairment	**-**	-
Carrying Value, End of Year	**1,132**	1,132

There were no additions to goodwill during 2011 and 2010.

Impairment Test for Cash-Generating Units Containing Goodwill

For the purpose of impairment testing, goodwill is allocated to the CGU to which it relates. All of the Company's goodwill arose on the acquisition of exploration and production assets. The carrying amount of goodwill allocated to the Company's exploration and production CGUs was as follows:

As at	**December 31, 2011**	December 31, 2010	January 1, 2010
Suffield	**393**	393	393
Palliser	**-**	-	14
Foster Creek	**242**	242	242
Northern Alberta	**497**	497	497
	1,132	1,132	1,146

There was no impairment of goodwill in 2011 and 2010.

20. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

As at	**December 31, 2011**	December 31, 2010	January 1, 2010
Accruals	**1,193**	852	545
Trade	**789**	471	509
Employee Long-Term Incentives	**209**	267	217
Interest	**72**	74	104
Other	**316**	179	230
	2,579	1,843	1,605

21. LONG-TERM DEBT

As at	Note	**December 31, 2011**	December 31, 2010	January 1, 2010
Canadian Dollar Denominated Debt				
Revolving term debt [1]	A	**-**	-	32
U.S. Dollar Denominated Debt				
Revolving term debt [1]	A	**-**	-	26
Unsecured notes (US$ 3,500)	B	**3,559**	3,481	3,663
		3,559	3,481	3,689
Total Debt Principal		**3,559**	3,481	3,721
Debt Discounts and Transaction Costs	C	**(32)**	(49)	(65)
Current Portion of Long-Term Debt	D	**-**	-	-
		3,527	3,432	3,656

1. Revolving term debt may include bankers' acceptances, LIBOR loans, prime rate loans and U.S. base rate loans.

The weighted average interest rate on outstanding debt for the year ended December 31, 2011 was 5.5 percent (2010 – 5.8 percent).

A) Revolving Term Debt

At December 31, 2011, Cenovus had in place a committed credit facility in the amount of $3,000 million or its equivalent amount in U.S. dollars. The committed credit facility matures on November 30, 2015 and is extendable from time to time for a period of up to four years at the option of Cenovus and upon agreement from the lenders. Borrowings are available by way of Bankers Acceptances, LIBOR based loans, prime rate loans or U.S. base rate loans. At December 31, 2011, there were no amounts drawn on Cenovus's committed bank credit facility (December 31, 2010 – $nil, January 1, 2010 – $58 million).

B) Unsecured Notes

Unsecured notes are comprised of the following senior unsecured notes:

	US$ Principal Amount	**December 31, 2011**	December 31, 2010	January 1, 2010
4.50% due September 15, 2014	**800**	**814**	796	837
5.70% due October 15, 2019	**1,300**	**1,322**	1,293	1,361
6.75% due November 15, 2039	**1,400**	**1,423**	1,392	1,465
	3,500	**3,559**	3,481	3,663

Cenovus has in place a Canadian base shelf prospectus for unsecured medium term notes in the amount of $1,500 million. The Canadian shelf prospectus allows for the issuance of medium term notes in Canadian dollars or other foreign currencies from time to time in one or more offerings. The terms of the notes, including, but not limited to, interest at either fixed or floating rates and expiry dates, will be determined at the date of issue. At December 31, 2011, no medium term notes have been issued under this Canadian prospectus. The shelf prospectus expires in July 2012.

Cenovus has in place a U.S. base shelf prospectus for unsecured notes in the amount of US$1,500 million. The U.S. shelf prospectus allows for the issuance of debt securities in U.S. dollars or other foreign currencies from time to time in one or more offerings. The terms of the notes, including, but not limited to, interest at either fixed or floating rates and expiry dates, will be determined at the date of issue. At December 31, 2011, no notes have been issued under this U.S. prospectus. The shelf prospectus expires in August 2012.

At December 31, 2011, the Company is in compliance with all of the terms of its debt agreements.

C) Debt Discounts and Transaction Costs

Long-term debt transaction costs and discounts associated with the unsecured notes are recorded within long-term debt and are being amortized using the effective interest rate method. Transaction costs associated with the revolving term debt have been recorded as a prepayment and are being amortized over the remaining term of the committed credit facility. During 2011, additional transaction costs of $3 million were recorded (2010 – $nil).

D) Mandatory Debt Payments

	US$ Principal Amount	C$ Principal Amount	**Total C$ Equivalent**
2012	-	-	**-**
2013	-	-	**-**
2014	800	-	**814**
2015	-	-	**-**
2016	-	-	**-**
Thereafter	2,700	-	**2,745**
	3,500	-	**3,559**

22. DECOMMISSIONING LIABILITIES

The decommissioning provision represents the present value of the future costs associated with the retirement of upstream oil and gas assets and refining facilities. The aggregate carrying amount of the obligation is as follows:

As at	**December 31, 2011**	December 31, 2010
Decommissioning Liabilities, Beginning of Year	**1,399**	1,185
Liabilities incurred	**49**	44
Liabilities settled	**(56)**	(32)
Liabilities divested	**-**	(90)
Transfers and reclassifications	**(55)**	(5)
Change in estimated future cash flows	**146**	51
Change in discount rate	**218**	173
Unwinding of discount on decommissioning liabilities	**75**	75
Foreign currency translation	**1**	(2)
Decommissioning Liabilities, End of Year	**1,777**	1,399

The undiscounted amount of estimated cash flows required to settle the obligation is $6,541 million (December 31, 2010 – $6,093 million, January 1, 2010 – $5,683 million), which has been discounted using a credit-adjusted risk free rate of 4.8 percent (December 31, 2010 – 5.4 percent, January 1, 2010 – 6.0 percent). Most of these obligations are not expected to be paid for several years, or decades, and will be funded from general resources at that time.

Sensitivities

Changes to the credit-adjusted risk-free rate or the inflation rate would have the following impact on the decommissioning liabilities:

	2011		2010	
As at	**Credit-adjusted risk-free rate**	**Inflation rate**	Credit-adjusted risk-free rate	Inflation rate
One percent increase	**(367)**	**504**	(287)	398
One percent decrease	**494**	**(379)**	388	(278)

23. OTHER LIABILITIES

As at	**December 31, 2011**	December 31, 2010	January 1, 2010
Partner Loans	**-**	274	183
Deferred Revenue	**35**	37	40
Employee Long-Term Incentives	**55**	18	-
Pension and Other Post-Employment Benefits	**16**	13	19
Other	**22**	4	4
	128	346	246

24. PENSIONS AND OTHER POST-EMPLOYMENT BENEFITS

The Company provides employees with a pension plan that includes defined contribution and defined benefit components, and other post-employment benefit plans ("OPEB"). Most of the employees participate in the defined contribution pension; the defined benefit pension component is closed to new entrants.

The Company files an actuarial valuation of its pension plans with the provincial regulator at least every three years. The most recently filed valuation was dated December 31, 2010 and the next required actuarial valuation will be as at December 31, 2013.

Information related to defined benefit pension and OPEB plans, based on actuarial estimations is as follows:

	Pension Benefits		
As at	**December 31, 2011**	December 31, 2010	January 1, 2010
Accrued Benefit Obligation, End of Year	**84**	68	56
Fair Value of Plan Assets, End of Year	**61**	59	54
Funded Status–Plan Assets (less) than Benefit Obligation	**(23)**	(9)	(2)
Amounts Not Recognized:			
Unamortized net actuarial (gain) loss	**22**	8	-
Unamortized past service cost	**-**	-	-
Accrued Benefit Asset (Liability)	**(1)**	(1)	(2)

	OPEB		
As at	**December 31, 2011**	December 31, 2010	January 1, 2010
Accrued Benefit Obligation, End of Year	**19**	14	11
Fair Value of Plan Assets, End of Year	**-**	-	-
Funded Status–Plan Assets (less) than Benefit Obligation	**(19)**	(14)	(11)
Amounts Not Recognized:			
Unamortized net actuarial (gain) loss	**4**	2	-
Unamortized past service cost	**-**	-	-
Accrued Benefit Asset (Liability)	**(15)**	(12)	(11)

Pension and other post-employment benefit costs recognized are as follows:

	Pension Benefits		OPEB	
For the years ended December 31,	**2011**	2010	**2011**	2010
Current Service Cost	**3**	3	**2**	1
Interest Cost	**4**	3	**1**	1
Expected Return on Plan Assets	**(4)**	(3)	**-**	-
Actuarial Gains (Losses)	**1**	-	**-**	-
Past Service Cost	**-**	-	**-**	-
Effect of Curtailment/Settlement	**-**	-	**-**	-
Plan Cost	**4**	3	**3**	2
Defined Contribution Plans Cost	**22**	18	**-**	-
Net Benefit Plan Cost	**26**	21	**3**	2

The weighted average actuarial assumptions used to determine benefit obligations are as follows:

	Pension Benefits			OPEB		
As at	**December 31, 2011**	December 31, 2010	January 1, 2010	**December 31, 2011**	December 31, 2010	January 1, 2010
Discount Rate	**4.25%**	5.25%	6.00%	**4.25%**	5.25%	6.00%
Rate of Compensation Increase	**3.99%**	4.05%	4.05%	**5.77%**	5.65%	5.77%

The expected future benefits payments for the year ended December 31, 2012 is $2 million for the defined benefit plan and $nil for the OPEB.

25. SHARE CAPITAL

Authorized

Cenovus is authorized to issue an unlimited number of common shares, an unlimited number of First Preferred Shares and an unlimited number of Second Preferred Shares. The First and Second Preferred Shares may be issued in one or more series with rights and conditions to be determined by the Company's Board of Directors prior to issuance and subject to the Company's articles.

Issued and Outstanding

	2011		2010	
As at December 31,	**Number of Common Shares (thousands)**	**Amount**	Number of Common Shares (thousands)	Amount
Outstanding, Beginning of Year	**752,675**	**3,716**	751,309	3,681
Common Shares Issued under Stock Option Plans	**1,824**	**64**	1,366	35
Outstanding, End of Year	**754,499**	**3,780**	752,675	3,716

There were no Preferred Shares outstanding as at December 31, 2011 (2010 – nil).

At December 31, 2011, there were 30 million (2010 – 26 million) common shares available for future issuance under stock option plans.

The Company has a dividend reinvestment plan ("DRIP"). Under the DRIP, holders of common shares may reinvest all or a portion of the cash dividends payable on their common shares in additional common shares. At the discretion of the Company, the additional common shares may be issued from treasury or purchased on the market.

Paid in Surplus

Cenovus's paid in surplus reflects the Company's retained earnings prior to the split of Encana under the Arrangement into two independent energy companies, Encana and Cenovus. In addition, paid in surplus includes compensation expense related to the Company's NSRs discussed in Note 26 A).

	Pre-Arrangement Earnings	**Stock-based Compensation**	**Total**
As at January 1, 2010 and December 31, 2010	4,083	-	4,083
Stock-based compensation expense	-	24	24
As at December 31, 2011	**4,083**	**24**	**4,107**

26. STOCK-BASED COMPENSATION PLANS

A) Employee Stock Option Plan

Cenovus has an Employee Stock Option Plan that provides employees with the opportunity to exercise an option to purchase common shares of the Company. Option exercise prices approximate the market price for the common shares on the date the options were issued. Options granted are exercisable at 30 percent of the number granted after one year, an additional 30 percent of the number granted after two years, and are fully exercisable after three years. Options granted prior to February 17, 2010 expire after five years while options granted on or after February 17, 2010 expire after seven years.

Options issued by the Company under the Employee Stock Option Plan prior to February 24, 2011 have associated tandem stock appreciation rights. In lieu of exercising the options, the tandem stock appreciation rights give the option holder the right to receive a cash payment equal to the excess of the market price of Cenovus's common shares at the time of exercise over the exercise price of the option.

Options issued by the Company on or after February 24, 2011 have associated net settlement rights. The net settlement rights, in lieu of exercising the option, give the option holder the right to receive the number of common shares that could be acquired with the excess value of the market price of Cenovus's common shares at the time of exercise over the exercise price of the option.

The tandem stock appreciation rights and net settlement rights vest and expire under the same terms and conditions as the underlying options. For the purpose of this financial statement note, options with associated tandem stock appreciation rights are referred to as "TSARs" and options with associated net settlement rights are referred to as "NSRs".

In addition, certain of the TSARs are performance based ("Performance TSARs"). The Performance TSARs vest and expire under the same terms and service conditions as the underlying option, and have an additional vesting requirement whereby vesting is subject to achievement of prescribed performance relative to pre-determined key measures. Performance TSARs that do not vest when eligible are forfeited.

In accordance with the Arrangement described in Note 1, each Cenovus and Encana employee exchanged their original Encana TSAR for one Cenovus Replacement TSAR and one Encana Replacement TSAR. The terms and conditions of the Cenovus and Encana Replacement TSARs are similar to the terms and conditions of the original Encana TSAR. The original exercise price of the Encana TSAR was apportioned to the Cenovus and Encana Replacement TSARs based on the one day volume weighted average trading price of Cenovus's Common Share price relative to that of Encana's Common Share price on the TSX on December 2, 2009. Cenovus TSARs and Cenovus Replacement TSARs are measured against the Cenovus Common Share price while Encana Replacement TSARs are measured against the Encana Common Share price. The Cenovus Replacement TSARs have similar vesting provisions as outlined above for the Employee Stock Option Plan. The original Encana Performance TSARs were also exchanged under the same terms as the original Encana TSARs.

As at December 31, 2011	Issued	Term (Years)	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price ($)	Closing Share Price ($)	Units Outstanding
Encana Replacement TSARs held by Cenovus Employees	Prior to Arrangement	**5**	**1.35**	**31.97**	**18.89**	**10,411**
Cenovus Replacement TSARs held by Encana Employees	Prior to Arrangement	**5**	**1.38**	**28.96**	**33.83**	**9,686**
TSARs	Prior to February 17, 2010	**5**	**1.45**	**28.95**	**33.83**	**9,395**
TSARs	On or After February 17, 2010	**7**	**5.20**	**26.72**	**33.83**	**5,526**
NSRs	On or After February 24, 2011	**7**	**6.24**	**36.95**	**33.83**	**5,809**

Unless otherwise indicated, all references to TSARs collectively refer to both the Cenovus issued TSARs and Cenovus Replacement TSARs.

NSRs

The weighted average unit fair value of NSRs granted during the year ended December 31, 2011 was $8.27 before considering forfeitures. The fair value of each NSR was estimated on their grant date using the Black-Scholes-Merton valuation model with weighted average assumptions as follows:

	2011
Risk Free Interest Rate	**2.46%**
Expected Dividend Yield	**2.16%**
Expected Volatility [1]	**28.81%**
Expected Life (Years)	**4.55**

1. Expected volatility has been based on historical volatility of the Company's publicly traded shares.

The following tables summarize the information related to the NSRs as at December 31, 2011:

As at December 31, 2011 (thousands of units)	NSRs	Weighted Average Exercise Price ($)
Outstanding, Beginning of Year	-	-
Granted	5,931	36.96
Exercised as options for common shares	-	-
Forfeited	(122)	37.50
Outstanding, End of Year	5,809	36.95
Exercisable, End of Year	1	37.54

	Outstanding NSRs (thousands of units)		
Range of Exercise Price ($)	NSRs	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price ($)
30.00 to 39.99	5,809	6.24	36.95
	5,809	6.24	36.95

	Exercisable NSRs (thousands of units)	
Range of Exercise Price ($)	NSRs	Weighted Average Exercise Price ($)
30.00 to 39.99	1	37.54
	1	37.54

TSARs Held by Cenovus Employees

The Company has recorded a liability of $90 million at December 31, 2011 (December 31, 2010 – $87 million, January 1, 2010 – $43 million) in the Consolidated Balance Sheets based on the fair value of each TSAR held by Cenovus employees. Fair value was estimated at the period end date using the Black-Scholes-Merton valuation model with weighted average assumptions as follows:

	2011
Risk Free Interest Rate	1.10%
Expected Dividend Yield	2.36%
Expected Volatility [1]	31.95%
Cenovus's Common Share Price	$33.83

1. Expected volatility has been based on historical volatility of the Company's publicly traded shares.

The intrinsic value of vested TSARs held by Cenovus employees at December 31, 2011 was $43 million (December 31, 2010 – $42 million).

The following tables summarize the information related to the TSARs held by Cenovus employees as at December 31, 2011:

As at December 31, 2011 (thousands of units)	TSARs	Performance TSARs	Total	Weighted Average Exercise Price ($)
Outstanding, Beginning of Year	12,044	7,073	**19,117**	**27.75**
Granted	138	-	**138**	**33.40**
Exercised for cash payment	(1,274)	(641)	**(1,915)**	**26.31**
Exercised as options for common shares	(1,202)	(564)	**(1,766)**	**26.38**
Forfeited	(315)	(338)	**(653)**	**28.37**
Outstanding, End of Year	**9,391**	**5,530**	**14,921**	**28.12**
Exercisable, End of Year	**4,618**	**4,256**	**8,874**	**29.15**

The weighted average market price of Cenovus's common shares at the date of exercise during the year ended December 31, 2011 was $35.71.

	Outstanding TSARs (thousands of units)				
Range of Exercise Price ($)	TSARs	Performance TSARs	Total	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price ($)
20.00 to 29.99	7,617	3,578	**11,195**	**3.32**	**26.43**
30.00 to 39.99	1,711	1,952	**3,663**	**1.40**	**33.03**
40.00 to 49.99	63	-	**63**	**1.45**	**43.30**
	9,391	**5,530**	**14,921**	**2.84**	**28.12**

	Exercisable TSARs (thousands of units)			
Range of Exercise Price ($)	TSARs	Performance TSARs	Total	Weighted Average Exercise Price ($)
20.00 to 29.99	3,029	2,304	**5,333**	**26.45**
30.00 to 39.99	1,526	1,952	**3,478**	**33.04**
40.00 to 49.99	63	-	**63**	**43.30**
	4,618	**4,256**	**8,874**	**29.15**

The market price of Cenovus common shares at December 31, 2011 was $33.83.

Encana Replacement TSARs Held by Cenovus Employees

Cenovus is required to reimburse Encana in respect of cash payments made by Encana to Cenovus employees when a Cenovus employee exercises an Encana Replacement TSAR for cash. No further Encana Replacement TSARs will be granted to Cenovus employees.

The Company has recorded a liability of $1 million at December 31, 2011 (December 31, 2010 – $24 million, January 1, 2010 – $70 million) in the Consolidated Balance Sheets based on the fair value of each Encana Replacement TSAR held by Cenovus employees. Fair value was estimated at the period end date using the Black-Scholes-Merton valuation model with weighted average assumptions as follows:

	2011
Risk Free Interest Rate	**0.99%**
Expected Dividend Yield	**4.31%**
Expected Volatility [1]	**28.04%**
Encana's Common Share Price	**$18.89**

1. Expected volatility has been based on the historical volatility of Encana's publicly traded shares.

The intrinsic value of vested Encana Replacement TSARs held by Cenovus employees at December 31, 2011 was $nil (December 31, 2010 – $6 million).

The following tables summarize the information related to the Encana Replacement TSARs held by Cenovus employees as at December 31, 2011:

As at December 31, 2011 (thousands of units)	TSARs	Performance TSARs	Total	Weighted Average Exercise Price ($)
Outstanding, Beginning of Year	6,429	7,098	**13,527**	**31.17**
Exercised for cash payment	(1,824)	(451)	**(2,275)**	**26.97**
Exercised as options for Encana common shares	(16)	-	**(16)**	**25.71**
Forfeited	(308)	(517)	**(825)**	**32.72**
Outstanding, End of Year	**4,281**	**6,130**	**10,411**	**31.97**
Exercisable, End of Year	**3,605**	**4,856**	**8,461**	**32.64**

The weighted average market price of Encana's common shares at the date of exercise during the year ended December 31, 2011 was $31.95.

	Outstanding TSARs (thousands of units)				
Range of Exercise Price ($)	TSARs	Performance TSARs	Total	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price ($)
20.00 to 29.99	2,437	4,014	**6,451**	**1.48**	**29.15**
30.00 to 39.99	1,711	2,116	**3,827**	**1.12**	**36.26**
40.00 to 49.99	131	-	**131**	**1.48**	**44.86**
50.00 to 59.99	2	-	**2**	**1.39**	**50.39**
	4,281	**6,130**	**10,411**	**1.35**	**31.97**

	Exercisable TSARs (thousands of units)			
Range of Exercise Price ($)	TSARs	Performance TSARs	Total	Weighted Average Exercise Price ($)
20.00 to 29.99	1,778	2,740	**4,518**	**29.20**
30.00 to 39.99	1,694	2,116	**3,810**	**36.28**
40.00 to 49.99	131	-	**131**	**44.86**
50.00 to 59.99	2	-	**2**	**50.39**
	3,605	**4,856**	**8,461**	**32.64**

The market price of Encana common shares at December 31, 2011 was $18.89.

Cenovus Replacement TSARs Held by Encana Employees

Encana is required to reimburse Cenovus in respect of cash payments made by Cenovus to Encana's employees when these employees exercise a Cenovus Replacement TSAR for cash. No compensation expense is recognized and no further Cenovus Replacement TSARs will be granted to Encana employees.

The Company has recorded a liability of $83 million at December 31, 2011 (December 31, 2010 – $123 million, January 1, 2010 – $84 million) in the Consolidated Balance Sheets based on the fair value of each Cenovus Replacement TSAR held by Encana employees, with an offsetting account receivable from Encana. Fair value was estimated at the period end date using the Black-Scholes-Merton valuation model with weighted average assumptions as follows:

	2011
Risk Free Interest Rate	0.99%
Expected Dividend Yield	2.36%
Expected Volatility [1]	31.95%
Cenovus's Common Share Price	$33.83

1. Expected volatility has been based on historical volatility of the Company's publicly traded shares.

The intrinsic value of vested Cenovus Replacement TSARs held by Encana employees at December 31, 2011 was $32 million (December 31, 2010 – $60 million).

The following tables summarize the information related to the Cenovus Replacement TSARs held by Encana employees as at December 31, 2011:

As at December 31, 2011 (thousands of units)	TSARs	Performance TSARs	Total	Weighted Average Exercise Price ($)
Outstanding, Beginning of Year	8,214	8,940	17,154	28.16
Exercised for cash payment	(4,082)	(2,758)	(6,840)	27.00
Exercised as options for common shares	(55)	(3)	(58)	23.29
Forfeited	(142)	(428)	(570)	29.14
Outstanding, End of Year	3,935	5,751	9,686	28.96
Exercisable, End of Year	3,203	4,319	7,522	29.73

The weighted average market price of Cenovus's common shares at the date of exercise during the year ended December 31, 2011 was $35.80.

	Outstanding TSARs (thousands of units)				
Range of Exercise Price ($)	TSARs	Performance TSARs	Total	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price ($)
20.00 to 29.99	2,197	3,807	6,004	1.55	26.41
30.00 to 39.99	1,671	1,944	3,615	1.11	32.95
40.00 to 49.99	67	-	67	1.44	42.88
	3,935	5,751	9,686	1.38	28.96

	Exercisable TSARs (thousands of units)			
Range of Exercise Price ($)	TSARs	Performance TSARs	Total	Weighted Average Exercise Price ($)
20.00 to 29.99	1,465	2,375	**3,840**	**26.48**
30.00 to 39.99	1,671	1,944	**3,615**	**32.95**
40.00 to 49.99	67	-	**67**	**42.88**
	3,203	**4,319**	**7,522**	**29.73**

The market price of Cenovus common shares at December 31, 2011 was $33.83.

B) Performance Share Units

Cenovus has granted Performance Share Units ("PSUs") to certain employees under its Performance Share Unit Plan for Employees. PSUs are whole share units and entitle employees to receive, upon vesting, either a Common Share of Cenovus or a cash payment equal to the value of a Cenovus Common Share. The number of PSUs eligible for payment is determined over three years based on the units granted multiplied by 30 percent after year one, 30 percent after year two and 40 percent after year three, multiplied by a performance multiplier for each year. The multiplier is based on the Company achieving key pre-determined performance measures. PSUs vest after three years.

The Company has recorded a liability of $55 million at December 31, 2011 (December 31, 2010 – $18 million, January 1, 2010 – $nil) in the Consolidated Balance Sheets for PSUs based on the market value of the Cenovus common shares at December 31, 2011. The intrinsic value of vested PSUs was $nil at December 31, 2011 and 2010 as PSUs are paid out upon vesting.

The following table summarizes the information related to the PSUs held by Cenovus employees as at December 31, 2011:

(thousands of units)	PSUs
Outstanding, Beginning of Year	**1,252**
Granted	**1,409**
Cancelled	**(98)**
Units in Lieu of Dividends	**60**
Outstanding, End of Year	**2,623**

C) Deferred Share Units

Under two Deferred Share Unit Plans, Cenovus directors, officers and employees may receive Deferred Share Units ("DSUs"), which are equivalent in value to a Common Share of the Company. Employees have the option to convert either zero, 25 or 50 percent of their annual bonus award into DSUs. DSUs vest immediately, are redeemed in accordance with the terms of the agreement and expire on December 15 of the calendar year following the year of cessation of directorship or employment.

The Company has recorded a liability of $35 million at December 31, 2011 (December 31, 2010 – $31 million, January 1, 2010 – $20 million) in the Consolidated Balance Sheets for DSUs based on the market value of the Cenovus common shares at December 31, 2011. The intrinsic value of vested DSUs equals the carrying value as DSUs vest at the time of grant.

The following table summarizes the information related to the DSUs held by Cenovus directors, officers and employees as at December 31, 2011:

(thousands of units)	DSUs
Outstanding, Beginning of Year	**940**
Granted to Directors	**65**
Granted from Annual Bonus Awards	**17**
Units in Lieu of Dividends	**23**
Exercised	**(3)**
Outstanding, End of Year	**1,042**

D) Total Stock-Based Compensation Expense (Recovery)

The following table summarizes the stock-based compensation expense (recovery) recorded for all plans within operating and general and administrative expenses on the Consolidated Statements of Earnings and Comprehensive Income:

For the years ended December 31,	2011	2010
NSRs	**16**	-
TSARs held by Cenovus employees	**24**	45
Encana Replacement TSARs held by Cenovus employees	**(8)**	(20)
PSUs	**27**	13
DSUs	**4**	9
Total stock-based compensation expense (recovery)	**63**	47

27. EMPLOYEE SALARIES AND BENEFIT EXPENSES

For the years ended December 31,	2011	2010
Salaries, Bonuses and Other Short-Term Employee Benefits	**399**	348
Defined Contribution Pension Plan	**13**	11
Defined Benefit Pension Plan and OPEB	**4**	(1)
Stock-Based Compensation (Note 26)	**63**	47
	479	405

28. RELATED PARTY TRANSACTIONS

Key Management Compensation

Key management includes Directors (executive and non-executive), the Executive Officers, Senior Vice-Presidents and Vice-Presidents. The compensation paid or payable to key management is as follows:

For the years ended December 31,	2011	2010
Salaries, Director Fees and Short-Term Benefits	**25**	22
Post-Employment Benefits	**3**	2
Other Long-Term Benefits	**-**	-
Stock-Based Compensation	**35**	37
Total	**63**	61

Post-employment benefits represent the present value of future pension benefits earned during the year. Stock-based compensation includes the costs associated with stock options, NSRs, TSARs, PSUs and DSUs recognized during the year.

29. INTEREST IN JOINT OPERATIONS

Cenovus has a 50 percent interest in FCCL Partnership, a jointly controlled entity which is involved in the development and production of crude oil. In addition, through its interest in the general partner and a limited partner, Cenovus has a 50 percent interest in WRB Refining LP, a jointly controlled entity, which owns two refineries in the U.S. and focuses on the refining of crude oil into petroleum and chemical products.

These entities have been accounted for using the proportionate consolidation method with the results of operations included in the Oil Sands and Refining and Marketing segments, respectively. Summarized financial statement information for these jointly controlled entities is as follows:

Consolidated Statements of Earnings For the years ended December 31,	FCCL Partnership [1] **2011**	 2010	WRB Refining LP [1] **2011**	 2010
Revenues	**2,364**	1,829	**8,672**	6,624
Expenses				
Purchased product	**-**	-	**7,223**	6,095
Operating, transportation and blending and realized gain/loss on risk management	**1,397**	1,074	**473**	462
Operating Cash Flow	**967**	755	**976**	67
Depreciation, depletion and amortization	**205**	210	**130**	86
Other expenses (income)	**(136)**	20	**(4)**	13
Net Earnings (Loss)	**898**	525	**850**	(32)

1. FCCL Partnership and WRB Refining LP are not separate tax paying entities. Income taxes related to the Partnerships' income are the responsibility of their respective Partners.

Consolidated Balance Sheets as at	FCCL Partnership **December 31, 2011**	 December 31, 2010	 January 1, 2010	WRB Refining LP **December 31, 2011**	 December 31, 2010	 January 1, 2010
Current Assets	**937**	703	800	**1,402**	951	812
Long-term Assets	**6,864**	6,419	6,374	**3,188**	2,840	2,391
Current Liabilities	**317**	229	147	**759**	559	515
Long-term Liabilities	**83**	40	29	**73**	327	407

Capital commitments through jointly controlled entities are as follows:

2011	1 Year	2 Years	3 Years	4 Years	5 Years	Thereafter	**Total**
Capital Commitments	179	58	11	2	3	-	**253**

2010	1 Year	2 Years	3 Years	4 Years	5 Years	Thereafter	**Total**
Capital Commitments	147	10	3	3	-	-	**163**

There are no contingent liabilities related to the Company's interest in jointly controlled entities, nor contingent liabilities of the jointly controlled entities themselves.

30. CAPITAL STRUCTURE

Cenovus's capital structure objectives and targets have remained unchanged from previous periods. Cenovus's capital structure consists of Shareholders' Equity plus Debt. Debt includes the Company's short-term borrowings plus long-term debt, including the current portion. Cenovus's objectives when managing its capital structure are to maintain financial flexibility, preserve access to capital markets, ensure its ability to finance internally generated growth and to fund potential acquisitions while maintaining the ability to meet the Company's financial obligations as they come due.

Cenovus monitors its capital structure financing requirements using, among other things, non-GAAP financial metrics consisting of Debt to Capitalization and Debt to Adjusted Earnings Before Interest, Taxes, Depreciation and Amortization ("EBITDA"). These metrics are used to steward Cenovus's overall debt position as measures of

Cenovus's overall financial strength. Debt is defined as short-term borrowings and the current and long-term portions of long-term debt excluding any amounts with respect to the Partnership Contribution Payable or Receivable. Cenovus continues to target a Debt to Capitalization ratio of between 30 and 40 percent.

As at	**December 31, 2011**	December 31, 2010	January 1, 2010
Short-Term Borrowings	**-**	-	-
Long-Term Debt	**3,527**	3,432	3,656
Debt	**3,527**	3,432	3,656
Shareholders' Equity	**9,406**	8,395	7,809
Total Capitalization	**12,933**	11,827	11,465
Debt to Capitalization	**27%**	29%	32%

Cenovus continues to target a Debt to Adjusted EBITDA of between 1.0 and 2.0 times.

As at	**December 31, 2011**	December 31, 2010
Debt	**3,527**	3,432
Net Earnings	**1,478**	1,081
Add (deduct):		
Finance costs	**447**	498
Interest income	**(124)**	(144)
Income tax expense	**729**	223
Depreciation, depletion and amortization	**1,295**	1,302
Exploration expense	**-**	-
Unrealized (gain) loss on risk management	**(180)**	(46)
Foreign exchange (gain) loss, net	**26**	(51)
(Gain) loss on divestiture of assets	**(107)**	(116)
Other (income) loss, net	**4**	(13)
Adjusted EBITDA	**3,568**	2,734
Debt to Adjusted EBITDA	**1.0x**	1.3x

It is Cenovus's intention to maintain investment grade credit ratings to help ensure it has continuous access to capital and the financial flexibility to fund its capital programs, meet its financial obligations and finance potential acquisitions. Cenovus will maintain a high level of capital discipline and manage its capital structure to ensure sufficient liquidity through all stages of the economic cycle. To manage the capital structure, Cenovus may adjust capital and operating spending, adjust dividends paid to shareholders, purchase shares for cancellation pursuant to normal course issuer bids, issue new shares, issue new debt, draw down on its credit facilities or repay existing debt.

In order to increase comparability of Debt to Adjusted EBITDA between periods and remove the non-cash component of risk management, Cenovus changed its definition of Adjusted EBITDA to exclude unrealized gains and losses on risk management activities. The Adjusted EBITDA and the ratio of Debt to Adjusted EBITDA for prior periods have been re-presented in a consistent manner. As noted above, Cenovus's capital structure objectives and targets remain unchanged from previous periods. At December 31, 2011, Cenovus is in compliance with all of the terms of its debt agreements.

31. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Cenovus's consolidated financial assets and financial liabilities consist of cash and cash equivalents, accounts receivable and accrued revenues, accounts payable and accrued liabilities, Partnership Contribution Receivable and Payable, partner loans, risk management assets and liabilities, long-term receivables, short-term borrowings, long-term debt and obligations for stock-based compensation carried at fair value. Risk management assets and liabilities arise from the use of derivative financial instruments. Fair values of financial assets and liabilities, summarized information related to risk management positions, and discussion of risks associated with financial assets and liabilities are presented as follows.

A) Fair Value of Financial Assets and Liabilities

The fair values of cash and cash equivalents, accounts receivable and accrued revenues, and accounts payable and accrued liabilities approximate their carrying amount due to the short-term maturity of those instruments.

The fair values of the Partnership Contribution Receivable and Partnership Contribution Payable, partner loans and long-term receivables approximate their carrying amount due to the specific non-tradeable nature of these instruments.

Risk management assets and liabilities are recorded at their estimated fair value based on mark-to-market accounting, using quoted market prices or, in their absence, third-party market indications and forecasts.

Long-term debt is carried at amortized cost. The estimated fair values of long-term borrowings have been determined based on prices sourced from market data.

	December 31, 2011		December 31, 2010		January 1, 2010	
As at	**Carrying Amount**	**Fair Value**	Carrying Amount	Fair Value	Carrying Amount	Fair Value
FINANCIAL ASSETS						
Held-For-Trading:						
Risk management assets	**284**	**284**	206	206	61	61
Loans and Receivables:						
Cash and cash equivalents	**495**	**495**	300	300	155	155
Accounts receivable and accrued liabilities	**1,405**	**1,405**	1,059	1,059	982	982
Partnership contribution receivable	**2,194**	**2,194**	2,491	2,491	2,966	2,966
Other	**29**	**29**	-	-	-	-
FINANCIAL LIABILITIES						
Held-For-Trading:						
Risk management liabilities	**68**	**68**	173	173	74	74
Financial Liabilities Measured at Amortized Cost:						
Accounts payable and accrued liabilities	**2,579**	**2,579**	1,843	1,843	1,605	1,605
Short-term borrowings	**-**	**-**	-	-	-	-
Long-term debt	**3,527**	**4,316**	3,432	3,940	3,656	3,964
Partnership contribution payable	**2,225**	**2,225**	2,519	2,519	2,990	2,990
Other	**17**	**17**	-	-	-	-

B) Risk Management Assets and Liabilities

Under the terms of the Arrangement, the risk management positions at November 30, 2009 were allocated to Cenovus based upon Cenovus's proportion of the related volumes covered by the contracts. To effect the allocation, Cenovus entered into a contract with Encana with the same terms and conditions as between Encana and the third parties to the existing contracts. All positions entered into after the Arrangement have been negotiated between Cenovus and third parties.

Net Risk Management Position

As at	**December 31, 2011**	December 31, 2010	January 1, 2010
Risk Management Assets			
Current asset	**232**	163	60
Long-term asset	**52**	43	1
	284	206	61
Risk Management Liabilities			
Current liability	**54**	163	70
Long-term liability	**14**	10	4
	68	173	74
Net Risk Management Asset (Liability) [1]	**216**	33	(13)

1. Of the $216 million net risk management asset balance at December 31, 2011, a liability of $3 million relates to the contract with Encana (2010 – net asset of $41 million).

Summary of Unrealized Risk Management Positions

	December 31, 2011			December 31, 2010			January 1, 2010		
	Risk Management			Risk Management			Risk Management		
As at	**Asset**	**Liability**	**Net**	Asset	Liability	Net	Asset	Liability	Net
Commodity Prices									
Crude Oil	**22**	**65**	**(43)**	4	159	(155)	8	66	(58)
Natural Gas	**247**	**3**	**244**	202	-	202	53	-	53
Power	**15**	**-**	**15**	-	14	(14)	-	8	(8)
Total Fair Value	**284**	**68**	**216**	206	173	33	61	74	(13)

Net Fair Value Methodologies Used to Calculate Unrealized Risk Management Positions

As at	**December 31, 2011**	December 31, 2010	January 1, 2010
Prices actively quoted	**226**	40	6
Prices sourced from observable data or market corroboration	**(10)**	(7)	(19)
Total Fair Value	**216**	33	(13)

Prices actively quoted refers to the fair value of contracts valued using quoted prices in an active market. Prices sourced from observable data or market corroboration refers to the fair value of contracts valued in part using active quotes and in part using observable, market-corroborated data.

Net Fair Value of Commodity Price Positions at December 31, 2011

As at December 31, 2011	**Notional Volumes**	**Term**	**Average Price**	**Fair Value**
Crude Oil Contracts				
Fixed Price Contracts				
WTI NYMEX Fixed Price	24,800 bbls/d	2012	US$98.72/bbl	**(1)**
WTI NYMEX Fixed Price	24,500 bbls/d	2012	$99.47/bbl	**(12)**
Other Fixed Price Contracts [1]		2012-2013		**(22)**
Other Financial Positions [2]				**(8)**
Crude Oil Fair Value Position				**(43)**
Natural Gas Contracts				
Fixed Price Contracts				
NYMEX Fixed Price	130 MMcf/d	2012	US$5.96/Mcf	**131**
AECO Fixed Price [1]	127 MMcf/d	2012	$4.50/Mcf	**73**
NYMEX Fixed Price	166 MMcf/d	2013	US$4.64/Mcf	**43**
Other Fixed Price Contracts [1]		2012-2013		**(3)**
Natural Gas Fair Value Position				**244**
Power Purchase Contracts				
Power Fair Value Position				**15**

1. Cenovus has entered into fixed price swaps to protect against widening price differentials between production areas in Canada, various sales points and quality differentials.
2. Other financial positions are part of ongoing operations to market the Company's production.

Earnings Impact of Realized and Unrealized Gains (Losses) on Risk Management Positions

For the years ended December 31,	**2011**	2010
REALIZED GAIN (LOSS) [1]		
Crude Oil	**(135)**	(17)
Natural Gas	**210**	289
Refining	**(14)**	10
Power	**7**	(4)
	68	278
UNREALIZED GAIN (LOSS) [2]		
Crude Oil	**106**	(92)
Natural Gas	**38**	152
Refining	**7**	(8)
Power	**29**	(6)
	180	46
Gain (Loss) on Risk Management	**248**	324

1. Realized gains and losses on risk management are recorded in the operating segment to which the derivative instrument relates.
2. Unrealized gains and losses on risk management are recorded in the Corporate and Eliminations segment.

Reconciliation of Unrealized Risk Management Positions from January 1 to December 31,

	2011		2010
	Fair Value	**Total Unrealized Gain (Loss)**	**Total Unrealized Gain (Loss)**
Fair Value of Contracts, Beginning of Year	**33**		
Change in fair value of contracts in place at beginning of year and contracts entered into during the year	**248**	**248**	324
Unrealized foreign exchange gain (loss) on U.S. dollar contracts	**3**	**-**	-
Fair value of contracts realized during the year	**(68)**	**(68)**	(278)
Fair Value of Contracts, End of Year	**216**	**180**	46

Commodity Price Sensitivities – Risk Management Positions

The following table summarizes the sensitivity of the fair value of Cenovus's risk management positions to fluctuations in commodity prices, with all other variables held constant. Management believes the price fluctuations identified in the table below are a reasonable measure of volatility. Fluctuations in commodity prices could have resulted in unrealized gains (losses) impacting earnings before income tax as follows:

Risk Management Positions in Place as at December 31, 2011

Commodity	Sensitivity Range	Increase	Decrease
Crude oil commodity price	± US$10 per bbl applied to WTI hedges	**(214)**	**214**
Crude oil differential price	± US$5 per bbl applied to differential hedges tied to production	**67**	**(67)**
Natural gas commodity price	± $1 per mcf applied to NYMEX and AECO natural gas hedges	**(160)**	**160**
Natural gas basis price	± $0.10 per mcf natural gas basis hedges	**2**	**(2)**
Power commodity price	± $25 per MWHr applied to power hedge	**19**	**(19)**

Risk Management Positions in Place as at December 31, 2010

Commodity	Sensitivity Range	Increase	Decrease
Crude oil commodity price	± US$10 per bbl applied to WTI hedges	(251)	251
Crude oil differential price	± US$5 per bbl applied to differential hedges tied to production	7	(7)
Natural gas commodity price	± $1 per mcf applied to NYMEX and AECO natural gas hedges	(218)	218
Natural gas basis price	± $0.10 per mcf natural gas basis hedges	2	(2)
Power commodity price	± $25 per MWHr applied to power hedge	38	(38)

C) Risks Associated with Financial Assets and Liabilities

Commodity Price Risk

Commodity price risk arises from the effect that fluctuations of future commodity prices may have on the fair value or future cash flows of financial assets and liabilities. To partially mitigate exposure to commodity price risk, the Company has entered into various financial derivative instruments. The use of these derivative instruments is governed under formal policies and is subject to limits established by the Board of Directors. The Company's policy is not to use derivative instruments for speculative purposes.

Crude Oil – The Company has used fixed price swaps to partially mitigate its exposure to the commodity price risk on its crude oil sales and condensate supply used for blending. To help protect against widening crude oil price differentials, Cenovus has entered into a limited number of swaps and futures to manage the price differentials.

Natural Gas – To partially mitigate the natural gas commodity price risk, the Company has entered into swaps, which fix the NYMEX and AECO prices. To help protect against widening natural gas price differentials in various production areas, Cenovus has entered into a limited number of swaps to manage the price differentials between these production areas and various sales points.

Power – The Company has in place a Canadian dollar denominated derivative contract, which commenced January 1, 2007 for a period of 11 years, to manage a portion of its electricity consumption costs.

Credit Risk

Credit risk arises from the potential that the Company may incur a loss if a counterparty to a financial instrument fails to meet its obligation in accordance with agreed terms. This credit risk exposure is mitigated through the use of Board-approved credit policies governing the Company's credit portfolio and with credit practices that limit transactions according to counterparties' credit quality. Agreements are entered into with major financial institutions with investment grade credit ratings or with counterparties having investment grade credit ratings. A substantial portion of Cenovus's accounts receivable are with customers in the oil and gas industry and are subject to normal industry credit risks. As at December 31, 2011, over 92 percent (2010 – 92 percent) of Cenovus's accounts receivable and financial derivative credit exposures are with investment grade counterparties.

At December 31, 2011, Cenovus had two counterparties whose net settlement position individually account for more than 10 percent (2010 – two counterparties) of the fair value of the outstanding in-the-money net financial and physical contracts by counterparty. The maximum credit risk exposure associated with accounts receivable and accrued revenues, risk management assets, Partnership Contribution Receivable, partner loans receivable, and long-term receivables is the total carrying value. The current concentration of this credit risk resides with A rated or higher counterparties. Cenovus's exposure to its counterparties is acceptable and within Credit Policy tolerances.

Liquidity Risk

Liquidity risk is the risk that Cenovus will not be able to meet all of its financial obligations as they become due. Liquidity risk also includes the risk of not being able to liquidate assets in a timely manner at a reasonable price. Cenovus manages its liquidity risk through the active management of cash and debt and by maintaining appropriate access to credit. As disclosed in Note 30, Cenovus targets a Debt to Capitalization ratio between 30 and 40 percent and a Debt to Adjusted EBITDA of between 1.0 to 2.0 times to manage the Company's overall debt position. It is Cenovus's intention to maintain investment grade credit ratings on its senior unsecured debt.

Cenovus manages its liquidity risk by ensuring that it has access to multiple sources of capital including: cash and cash equivalents, cash from operating activities, undrawn credit facilities, commercial paper and availability under its shelf prospectuses. At December 31, 2011, Cenovus's committed credit facility was fully available. In addition, Cenovus had in place a Canadian debt shelf prospectus for $1,500 million and a U.S. debt shelf prospectus for US$1,500 million, the availability of which are dependent on market conditions. No notes have been issued under either prospectus.

Undiscounted cash outflows relating to financial liabilities are outlined in the table below:

2011	Less than 1 Year	1-3 Years	4-5 Years	Thereafter	Total
Accounts Payable and Accrued Liabilities	2,579	-	-	-	**2,579**
Risk Management Liabilities	54	14	-	-	**68**
Long-Term Debt [1]	208	1,230	343	5,182	**6,963**
Partnership Contribution Payable [1]	497	994	994	125	**2,610**
Other [1]	3	10	3	4	**20**

1. Principal and interest, including current portion.

2010	Less than 1 Year	1-3 Years	4-5 Years	Thereafter	Total
Accounts Payable and Accrued Liabilities	1,843	-	-	-	1,843
Risk Management Liabilities	163	10	-	-	173
Long-Term Debt [1]	203	407	1,167	5,236	7,013
Partnership Contribution Payable [1]	486	972	972	609	3,039
Partner Loans Payable	-	274	-	-	274

1. Principal and interest, including current portion.

Foreign Exchange Risk

Foreign exchange risk arises from changes in foreign exchange rates that may affect the fair value or future cash flows of Cenovus's financial assets or liabilities. As Cenovus operates in North America, fluctuations in the exchange rate between the U.S./Canadian dollars can have a significant effect on reported results.

As disclosed in Note 7, Cenovus's foreign exchange (gain) loss primarily includes unrealized foreign exchange gains and losses on the translation of the U.S. dollar debt issued from Canada and the translation of the U.S. dollar Partnership Contribution Receivable issued from Canada. At December 31, 2011, Cenovus had US$3,500 million in U.S. dollar debt issued from Canada (US$3,500 million at December 31, 2010) and US$2,157 million related to the U.S. dollar Partnership Contribution Receivable (US$2,505 million at December 31, 2010). A $0.01 change in the U.S. to Canadian dollar exchange rate would have resulted in a $13 million change in foreign exchange (gain) loss at December 31, 2011 (2010 – $10 million).

Interest Rate Risk

Interest rate risk arises from changes in market interest rates that may affect the earnings, cash flows and valuations. Cenovus has the flexibility to partially mitigate its exposure to interest rate changes by maintaining a mix of both fixed and floating rate debt.

At December 31, 2011, the increase or decrease in net earnings for a one percentage point change in interest rates on floating rate debt amounts to $nil (2010 – $nil). This assumes the amount of fixed and floating debt remains unchanged from the respective balance sheet dates.

32. SUPPLEMENTARY INFORMATION

Supplementary Cash Flow Information

For the years ended December 31,	2011	2010
Interest Paid	**357**	423
Income Taxes Paid	**-**	62

33. COMMITMENTS AND CONTINGENCIES

A) Commitments

As part of normal operations, the Company has committed to certain amounts over the next five years and thereafter as follows:

2011	1 Year	2 Years	3 Years	4 Years	5 Years	Thereafter	**Total**
Pipeline Transportation [1]	143	137	187	311	347	2,754	**3,879**
Operating Leases (Building Leases)	71	93	85	80	80	1,491	**1,900**
Product Purchases	19	18	19	19	6	-	**81**
Capital Commitments [2]	366	98	40	23	22	20	**569**
Other Long-Term Commitments	5	4	1	1	-	1	**12**
Total Payments [3]	604	350	332	434	455	4,266	**6,441**
Product Sales	52	54	56	57	60	3	**282**

1. Certain transportation commitments included are subject to regulatory approval.
2. Includes those commitments related to jointly controlled entities.
3. Contracts undertaken by the Company on behalf of FCCL Partnership are reflected at Cenovus's 50 percent interest.

2010	1 Year	2 Years	3 Years	4 Years	5 Years	Thereafter	**Total**
Pipeline Transportation [1]	107	93	167	167	166	953	1,653
Operating Leases (Building Leases)	33	87	88	85	78	1,553	1,924
Product Purchases	23	18	18	18	18	7	102
Capital Commitments [2]	248	94	16	14	11	37	420
Other Long-Term Commitments	4	2	1	1	-	1	9
Total Payments [3]	415	294	290	285	273	2,551	4,108
Product Sales	50	52	54	56	57	63	332

1. Certain transportation commitments included are subject to regulatory approval.
2. Includes those commitments related to jointly controlled entities.
3. Contracts undertaken by the Company on behalf of FCCL Partnership are reflected at Cenovus's 50 percent interest.

At December 31, 2011, there were outstanding letters of credit aggregating $17 million issued as security for performance under certain contracts (2010 – $23 million).

In addition to the above, Cenovus's commitments related to its risk management program are disclosed in Note 31.

B) Contingencies

Legal Proceedings

Cenovus is involved in a limited number of legal claims associated with the normal course of operations. Cenovus believes it has made adequate provisions for such legal claims. There are no individually or collectively significant claims.

Decommissioning Liabilities

Cenovus is responsible for the retirement of long-lived assets related to its oil and gas properties, refining facilities and midstream facilities at the end of their useful lives. Cenovus has recognized a liability of $1,777 million based on current legislation and estimated costs. Actual costs may differ from those estimated due to changes in legislation and changes in costs.

Income Tax Matters

The tax regulations and legislation and interpretations thereof in the various jurisdictions in which Cenovus operates are continually changing. As a result, there are usually a number of tax matters under review. Management believes that the provision for taxes is adequate.

34. FIRST TIME ADOPTION OF IFRS

Transition to IFRS

These Consolidated Financial Statements for the year ended December 31, 2011 represent the Company's first annual consolidated financial statements prepared in accordance with IFRS, which are also generally accepted accounting principles for publicly accountable enterprises in Canada. The Company adopted IFRS in accordance with IFRS 1, "First-time Adoption of International Financial Reporting Standards" and has prepared its Consolidated Financial Statements with IFRS applicable for periods beginning on or after January 1, 2010, using significant accounting policies as described in Note 3. For all periods up to and including the year ended December 31, 2010, the Company prepared its Consolidated Financial Statements in accordance with Canadian generally accepted accounting principles ("previous GAAP"). As allowed by IFRS 1, the Company has chosen not to include the comparative financial information for the year ended December 31, 2009. This note explains the principal adjustments made by the Company to restate its previous GAAP Consolidated Financial Statements on transition to IFRS.

Exemptions Applied under IFRS 1

On first-time adoption of IFRS, the general principle is that an entity retrospectively restates its results for all standards in force at the first reporting date. However, IFRS 1 provides certain exemptions from the general requirements of IFRS to assist with the transition process. Cenovus has applied the following exemptions in the preparation of its opening Balance Sheet dated January 1, 2010 (the "Transition Date"):

- **Fair Value as Deemed Cost** – The Company has elected to measure its Refining assets at their fair values at the Transition Date and use those fair values as their deemed cost at that date (Note A).

- **Deemed Cost Election for Oil and Gas Assets** – Under previous GAAP, Cenovus accounted for its oil and gas properties in one cost centre using full cost accounting. The Company has elected to measure its oil and gas properties at the Transition Date on the following basis:

  a) exploration and evaluation assets at the amount determined under the Company's previous GAAP; and
  b) the remainder allocated to the underlying property, plant and equipment assets on a pro rata basis using proved reserve values discounted at 10 percent at the Transition Date (Note B).

- **Leases** – Cenovus has elected to assess lease arrangements using the facts and circumstances as of the Transition Date under International Financial Reporting Interpretations Committee Interpretation 4, *"Determining whether an Arrangement contains a Lease"* ("IFRIC 4").

- **Employee Benefits** – The Company has elected not to apply IAS 19, *"Employee Benefits"* retrospectively and as such all cumulative actuarial gains and losses on the Company's defined benefit plans were recognized at the Transition Date (Note F).

- **Business Combinations** – IFRS 3, *"Business Combinations"* has not been applied to business combinations that occurred before the Transition Date.

- **Cumulative Currency Translation Differences** – Cumulative currency translation differences for all foreign operations are deemed to be zero at the Transition Date (Note J).

- **Decommissioning Liabilities** – Cenovus applied the deemed cost election for oil and gas assets under IFRS 1 and as such decommissioning liabilities at the date of transition have been measured in accordance with IAS 37, *"Provisions, Contingent Liabilities and Contingent Assets"* (Note D).

- **Borrowing Costs** – In accordance with IFRS 1, the Company has elected to apply IAS 23, *"Borrowing Costs"* to qualifying assets for which the commencement date for capitalization of borrowing costs occurred on or after the Transition Date. Borrowing costs have not been capitalized on qualifying assets under construction on or before the Transition Date.

- **Estimates** – Hindsight was not used to create or revise estimates and accordingly, the estimates made by the Company under previous GAAP are consistent with their application under IFRS.

Under IFRS 1, the opening Balance Sheet adjustments are recorded directly to retained earnings, or if appropriate, another category of equity. As Cenovus's paid in surplus reflects the Company's retained earnings prior to the split of Encana into two independent energy companies, Encana and Cenovus, all opening Balance Sheet adjustments have been recorded to paid in surplus. The impacts of applying the above noted IFRS 1 exemptions and the accounting policy differences between previous GAAP and IFRS are summarized in the following tables:

Reconciliation of Statement of Earnings and Comprehensive Income
For the year ended December 31, 2010

	Notes	Previous GAAP	Adjustments	IFRS
Revenues				
Gross Sales	K	13,422	(332)	**13,090**
Less: Royalties		449	-	**449**
		12,973	(332)	**12,641**
Expenses				
Purchased product	K	7,549	2	**7,551**
Transportation and blending		1,065	-	**1,065**
Operating	E,F,K	1,302	(16)	**1,286**
Production and mineral taxes		34	-	**34**
(Gain) loss on risk management	K	-	(324)	**(324)**
Depreciation, depletion and amortization	A,B,C	1,310	(8)	**1,302**
Exploration expense	H	-	3	**3**
General and administrative	E,F	251	(5)	**246**
Finance costs	K	-	498	**498**
Interest, net	K	279	(279)	**-**
Interest income	K	-	(144)	**(144)**
Accretion of asset retirement obligation	K	75	(75)	**-**
Foreign exchange (gain) loss, net		(51)	-	**(51)**
(Gain) loss on divestiture of assets	G	9	(125)	**(116)**
Other (income) loss, net		(13)	-	**(13)**
Earnings Before Income Tax		1,163	141	**1,304**
Income tax expense	I	170	53	**223**
Net Earnings		993	88	**1,081**
Other Comprehensive Income (Loss), Net of Tax				
Foreign currency translation adjustment	J	(13)	84	**71**
Comprehensive Income (Loss)		980	172	**1,152**
Net Earnings per Common Share				
Basic	L	1.32	0.12	**1.44**
Diluted	L	1.32	0.11	**1.43**

Reconciliation of the Balance Sheet
As at

	Notes	December 31, 2010 Previous GAAP	December 31, 2010 Adjustments	December 31, 2010 IFRS	January 1, 2010 Previous GAAP	January 1, 2010 Adjustments	January 1, 2010 IFRS
Assets							
Current Assets							
Cash and cash equivalents		300	-	**300**	155	-	**155**
Accounts receivable and accrued revenues	E	1,055	4	**1,059**	978	4	**982**
Income tax receivable		31	-	**31**	40	-	**40**
Current portion of Partnership Contribution Receivable		346	-	**346**	345	-	**345**
Inventories		880	-	**880**	875	-	**875**
Risk management		163	-	**163**	60	-	**60**
Assets held for sale	K	-	65	**65**	-	-	**-**
Current Assets		2,775	69	**2,844**	2,453	4	**2,457**
Assets Held for Sale	K	65	(65)	**-**	-	-	**-**
Exploration and Evaluation Assets	K	-	713	**713**	-	580	**580**
Property, Plant and Equipment, net	A,B,D, E,F,G, H,J,K	15,530	(2,903)	**12,627**	15,214	(3,165)	**12,049**
Partnership Contribution Receivable		2,145	-	**2,145**	2,621	-	**2,621**
Risk Management		43	-	**43**	1	-	**1**
Other Assets	C,F,J	391	(110)	**281**	320	(128)	**192**
Deferred Income Tax	K	-	55	**55**	-	3	**3**
Goodwill	G	1,146	(14)	**1,132**	1,146	-	**1,146**
Total Assets		22,095	(2,255)	**19,840**	21,755	(2,706)	**19,049**
Liabilities and Shareholders' Equity							
Current Liabilities							
Accounts payable and accrued liabilities	E	1,825	18	**1,843**	1,574	31	**1,605**
Income tax payable		154	-	**154**	-	-	**-**
Current portion of Partnership Contribution Payable		343	-	**343**	340	-	**340**
Risk management		163	-	**163**	70	-	**70**
Liabilities related to assets held for sale	K	-	7	**7**	-	-	**-**
Current Liabilities		2,485	25	**2,510**	1,984	31	**2,015**
Liabilities Related to Assets Held for Sale	K	7	(7)	**-**	-	-	**-**
Long-Term Debt		3,432	-	**3,432**	3,656	-	**3,656**
Partnership Contribution Payable		2,176	-	**2,176**	2,650	-	**2,650**
Risk Management		10	-	**10**	4	-	**4**
Decommissioning Liabilities	D,G	1,213	186	**1,399**	1,147	38	**1,185**
Other Liabilities	F	346	-	**346**	239	7	**246**
Deferred Income Tax	I,J,K	2,404	(832)	**1,572**	2,467	(983)	**1,484**
Total Liabilities		12,073	(628)	**11,445**	12,147	(907)	**11,240**
Share Capital		3,716	-	**3,716**	3,681	-	**3,681**
Paid in Surplus	A,C,D, E,F,I,J	5,896	(1,813)	**4,083**	5,896	(1,813)	**4,083**
Accumulated Other Comprehensive Income (Loss)	J	(27)	98	**71**	(14)	14	**-**
Retained Earnings		437	88	**525**	45	-	**45**
Shareholders' Equity		10,022	(1,627)	**8,395**	9,608	(1,799)	**7,809**
Total Liabilities and Shareholders' Equity		22,095	(2,255)	**19,840**	21,755	(2,706)	**19,049**

Reconciliation of the Statement of Cash Flows
For the year ended December 31, 2010

	Notes	Previous GAAP	Adjustments	IFRS
Operating Activities				
Net earnings		993	88	**1,081**
Depreciation, depletion and amortization	A,B,C	1,310	(8)	**1,302**
Deferred income taxes	I	88	53	**141**
Unrealized (gain) loss on risk management		(46)	-	**(46)**
Unrealized foreign exchange (gain) loss		(69)	-	**(69)**
(Gain) loss on divestitures of assets	G	9	(125)	**(116)**
Unwinding of discount on decommissioning liabilities		75	-	**75**
Other		55	(11)	**44**
		2,415	(3)	**2,412**
Net change in other assets and liabilities		(55)	-	**(55)**
Net change in non-cash working capital		234	-	**234**
Cash From Operating Activities		2,594	(3)	**2,591**
Investing Activities				
Capital expenditures – exploration and evaluation assets		-	(350)	**(350)**
Capital expenditures – property, plant and equipment		(2,208)	357	**(1,851)**
Proceeds from divestitures of assets		309	-	**309**
Net change in investments and other		4	-	**4**
Net change in non-cash working capital	E	99	(4)	**95**
Cash From (Used in) Investing Activities		(1,796)	3	**(1,793)**
Net Cash Provided (Used) before Financing Activities		798	-	**798**
Cash From (Used in) Financing Activities		(631)	-	**(631)**
Foreign Exchange Gain (Loss) on Cash and Cash Equivalents Held in Foreign Currency		(22)	-	**(22)**
Increase (Decrease) in Cash and Cash Equivalents		145	-	**145**
Cash and Cash Equivalents, Beginning of Year		155	-	**155**
Cash and Cash Equivalents, End of Year		300	-	**300**

Notes:

A) Refining Property, Plant and Equipment

At January 1, 2010, Cenovus elected to measure its refining assets at fair value and to use that fair value as its deemed cost on transition to IFRS. The fair value of the refining assets was determined to be US$4,543 million, US$2,272 million net to Cenovus, which resulted in the carrying value of the refining assets exceeding the fair value. Cenovus's carrying value of property, plant and equipment was reduced by C$2,585 million at the Transition Date with a corresponding reduction in paid in surplus.

In December 2010, it was determined that a processing unit at the Borger Refinery was a redundant asset and would not be used in future operations at the refinery. The fair value of the unit was determined to be negligible based on market prices for refining assets of similar age and condition. Accordingly, under previous GAAP, an impairment of $37 million was recorded. Under IFRS, the impairment was only $14 million due to the IFRS 1 election noted above to use the fair value as deemed cost. Therefore DD&A expense under IFRS was reduced by $23 million.

The lower carrying value under IFRS and the impairment adjustment noted above resulted in lower DD&A expense of $126 million for the year ended December 31, 2010.

B) Oil and Gas Property, Plant and Equipment

Under previous GAAP, costs accumulated within each cost centre for oil and gas properties were depleted using the unit-of-production method based on estimated proved reserves determined using estimated future prices and costs on a country-by-country cost centre basis (full cost accounting). Under IFRS, costs accumulated within each area are depleted using the unit-of-production method based on estimated proved reserves determined using estimated future prices and costs on an area-by-area basis. This resulted in an increase of $135 million in DD&A expense for the year ended December 31, 2010.

C) Impairment of Deferred Asset

Under previous GAAP, other assets included a deferred asset, which represented the disproportionate interest received in 2007 and 2008 (15 percent in 2007 and 35 percent in 2008) that arose from the acquisition of the Borger Refinery in 2007. On transition to IFRS, it was determined that as a result of the reduction in the carrying value of the refineries due to the fair value election, the deferred asset was impaired and therefore was written off. Paid in surplus was decreased by the carrying value of the asset under previous GAAP of $121 million. Under previous GAAP, the deferred asset was being amortized over 10 years. As such, DD&A expense under IFRS decreased by $17 million for the year ended December 31, 2010.

D) Decommissioning Liabilities

As discussed above, the Company elected to apply the exemption to measure decommissioning liabilities at the Transition Date in accordance with IAS 37. As such, the Company re-measured the decommissioning liabilities as at the Transition Date using the period end credit-adjusted risk-free discount rate and recognized an increase of $38 million to the decommissioning liability.

Consistent with IFRS, decommissioning liabilities under previous GAAP were measured based on the estimated costs of decommissioning, discounted to their net present value upon initial recognition. However, under IFRS, estimated cash flows are discounted using the credit-adjusted risk-free rate that exists at the balance sheet date. As at December 31, 2010, property, plant and equipment and the decommissioning liability increased $154 million under IFRS. There was minimal impact to the unwinding of the discount for the year ended December 31, 2010.

E) Stock-Based Compensation

Under previous GAAP, obligations for payments under Cenovus's stock option plan (with associated tandem stock appreciation rights) were accrued for using the intrinsic method. Under IFRS, these obligations are accrued for using the fair value method. As a result of the re-measurement of the liability as at January 1, 2010 a charge of $27 million was recognized in paid in surplus with an increase to accounts payable and accrued liabilities of $31 million and an increase to accounts receivable and accrued revenue of $4 million. For the year ended December 31, 2010, due to the differences in the measurement basis under IFRS, operating and general and administrative expense decreased $5 million and $4 million, respectively, property, plant and equipment decreased $4 million and accounts payable and accrued liabilities decreased $13 million.

F) Employee Benefits

Cenovus elected under IFRS 1 to recognize all unamortized actuarial gains and losses on the defined benefit pension and other post-employment benefits plans at the Transition Date resulting, in a $7 million increase to other liabilities, a $7 million decrease to other assets and a $14 million charge to paid in surplus. Under previous GAAP, the actuarial losses continued to be amortized and, as such, for the year ended December 31, 2010, both operating and general and administrative expense decreased by $1 million. In addition, due to the recognition of all unamortized actuarial gains and losses at the Transition date, it was necessary to reclassify the pension asset to a pension liability resulting in a reclassification from other assets to other liabilities of $4 million at December 31, 2010.

G) Gains/Losses on Divestiture of Assets

Under previous GAAP, proceeds on the divestiture of oil and gas properties were credited to the full cost pool and no gain or loss was recognized unless the effect of the sale would have changed the DD&A rate by 20 percent or more. Under IFRS, all gains and losses are recognized on oil and gas property divestitures and calculated as the difference between net proceeds and the carrying value of the net assets disposed. Accordingly, a gain of $125 million was recognized for the year ended December 31, 2010 under IFRS. At December 31, 2010 the carrying value of property, plant and equipment increased $133 million and goodwill and decommissioning liabilities were reduced by $14 million and $6 million, respectively.

H) Pre-Exploration Expense

Under IFRS, costs incurred prior to obtaining the legal right to explore must be expensed whereas under previous GAAP these costs were capitalized in the full cost pool. For the year ended December 31, 2010, $3 million of pre-exploration costs were expensed under IFRS. The accounting policy difference has resulted in a $3 million decrease to property, plant and equipment and a corresponding increase in exploration expense. This adjustment has decreased cash from operating activities by $3 million and increased cash from investing activities by a corresponding amount for the year ended December 31, 2010.

I) Deferred Income Taxes

The increase in paid in surplus of $986 million at the Transition Date related to deferred income taxes reflects the change in temporary differences resulting from the IFRS 1 exemptions applied. For the year ended December 31, 2010 deferred income tax increased by $53 million to reflect the changes in temporary differences resulting from the IFRS adjustments described above and a $9 million adjustment to recognize the deferred tax benefit on an intercompany transfer of oil and gas properties.

J) Currency Translation Adjustments

In accordance with IFRS 1, Cenovus elected to deem all cumulative currency translation differences for all foreign operations to be zero at the Transition Date. All foreign currency translation differences in respect of foreign operations that arose prior to the Transition Date were transferred to paid in surplus.

In addition, AOCI is affected by the revaluation of the adjustments noted above that reside in a foreign operation notably the reduction in the carrying value of the Refining property, plant and equipment, the impairment of the deferred asset and the associated deferred income tax payable. The table below identifies the cumulative balance sheet impact at December 31, 2010 and January 1, 2010:

Increase (Decrease)	December 31, 2010	January 1, 2010
Assets		
Refining property, plant and equipment	125	-
Other assets	5	-
Liabilities and Equity		
Deferred income tax liability	46	-
Accumulated other comprehensive income	98	14
Paid in surplus	(14)	(14)

K) Reclassifications

Exploration and evaluation ("E&E") assets

Under previous GAAP, E&E assets were included in property, plant and equipment, whereas under IFRS E&E assets are separately disclosed. The Company reclassified $580 million and $713 million from property, plant and equipment to E&E assets at January 1, 2010 and December 31, 2010, respectively.

Finance costs and interest income

In addition, under previous GAAP, the unwinding of the discount on decommissioning liabilities was classified as accretion expense in the Consolidated Statements of Earnings and Comprehensive Income. Under IFRS this amount has been reclassified to finance costs.

Under previous GAAP, interest was reported on a net basis. Under IFRS interest expense is included in finance costs and interest income is reported separately.

Gains/losses on risk management

Under previous GAAP, gains and losses from crude oil and natural gas commodity price risk management activities were recorded in gross revenues. Under IFRS, these activities do not meet the definition of revenue and therefore have been reclassified to (gain) loss on risk management in the Consolidated Statements of Earnings and Comprehensive Income. In addition, risk management activities related to power and the refining business have been reclassified to gain (loss) on risk management activities from operating expense and purchased product, respectively.

Assets and liabilities classified as held for sale

Under previous GAAP, assets held for sale and liabilities related to assets held for sale were included as part of non-current assets and liabilities. Under IFRS, non-current assets that meet the definition of held for sale are required to be classified as current.

Deferred income taxes

A net deferred income tax asset has arisen at January 1, 2010 and December 31, 2010 related to the U.S. foreign operations, due to the adjustments noted above. Consistent with previous GAAP, a deferred income tax asset may not be offset against a deferred income tax liability in a different tax jurisdiction. Accordingly, $55 million and $3 million were reclassified to deferred income tax asset at December 31, 2010 and January 1, 2010, respectively.

L) Net Earnings Per Share

Basic earnings per share

Basic earnings per share under IFRS was impacted by the IFRS earnings adjustments discussed above.

Diluted earnings per share

Under previous GAAP, Cenovus's TSARs, which may be cash or equity settled at the option of the holder, had no dilutive effect on diluted earnings per share because cash settlement was assumed. Under IFRS, the more dilutive of cash settlement and share settlement is required to be used in calculating diluted earnings per share. The following table identifies the differences between previous GAAP and IFRS:

For the year ended December 31, 2010 ($ millions, except earnings per share)	Previous GAAP Net Earnings	Previous GAAP Shares	Previous GAAP Earnings per Share	IFRS **Net Earnings**	IFRS **Shares**	IFRS **Earnings per Share**
Net earnings per share – basic	993	751.9	$1.32	**1,081**	**751.9**	**$1.44**
Dilutive effect of exercised Cenovus TSARs	-	0.8		**-**	**0.8**	
Dilutive effect of outstanding Cenovus TSARs	-	-		**-**	**1.3**	
Net earnings per share – diluted	993	752.7	$1.32	**1,081**	**754.0**	**$1.43**

M) Debt to Capitalization Ratio

The transition to IFRS resulted in changes to the Company's Debt to Capitalization ratio as follows:

	December 31, 2010 Previous GAAP	December 31, 2010 **IFRS**	January 1, 2010 Previous GAAP	January 1, 2010 **IFRS**
Long-Term Debt	3,432	**3,432**	3,656	**3,656**
Debt	3,432	**3,432**	3,656	**3,656**
Shareholders' Equity	10,022	**8,395**	9,608	**7,809**
Total Capitalization	13,454	**11,827**	13,264	**11,465**
Debt to Capitalization ratio	26%	**29%**	28%	**32%**