



interim statement

For the three months ended June 30, 2005

July 27, 2005

Pacific Northern Gas Ltd.
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Pacific Northern Gas Ltd.

MANAGEMENT'S DISCUSSION AND ANALYSIS for the Three Months Ended June 30, 2005

FORWARD-LOOKING STATEMENTS

Management's discussion and analysis contains certain forward-looking statements that are subject to risks and uncertainties that may cause the results or events predicted in this discussion to differ materially from actual results or events. Factors which could cause the results or events to differ include, but are not limited to: general economic conditions; gas commodity price volatility; decisions by regulators; seasonal weather patterns; the cost and availability of capital; and the ability of the Company to attract and retain quality employees. No assurance can be given that results, performance or achievement expressed in, or implied by, forward-looking statements within this disclosure will occur, or if they do, that any benefits may be derived from them. The Company undertakes no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

Business Environment

The Company continues to monitor the competitiveness of its natural gas retail sales relative to alternative heating sources in its service areas. Substantial increases in gas supply commodity prices over the last few years, combined with increases in the Company's delivery margins for residential, commercial and small industrial customers located in the west-central region of northern British Columbia continue to be a factor in reducing the quantity of gas sold and delivered to the Company's customers in this area of the province. In contrast, a more vibrant economy in northeastern British Columbia as a result of activity in the oil and gas exploration and coal sectors is helping to maintain gas deliveries closer to historical levels on a system-wide basis.

Income Trust Application

In December 2004, the Company reapplied to the British Columbia Utilities Commission (the "Commission") to recapitalize under an income trust ownership structure. The Commission had denied a previous application in a decision released on July 29, 2004, citing concerns over the requirement to deem a common equity component higher than the proposed income trust's level of equity, as well as requirements to deem income tax expenses for rate making purposes. The Company believes its new application addresses the concerns raised by the Commission in its denial of the first application. In particular, the new application requests that the Commission set customer rates using the actual capital structure of the proposed income trust rather than a deemed capital structure. An oral public hearing on the application concluded on July 7, 2005 and a decision by the Commission is expected late in the third quarter of 2005.

Public Offering

On March 11, 2005, the Company filed a preliminary prospectus for the public offering of 1,338,477 common shares of the Company owned by Tricor Acquisition (STP) Inc. ("Tricor"), at a price of \$19.40 per common share, for gross proceeds of approximately \$26 million. The common shares offered by Tricor represented 37 percent of the Company's outstanding common shares and 100 percent of Tricor's interest in the Company. The transaction was subsequently completed on April 12, 2005. The Company did not sell any newly issued common shares as part of this offering and did not receive any of the proceeds from the sale of the common shares by the selling shareholder.

Overall Performance

Net income for the three months ended June 30, 2005 was \$0.1 million, compared with \$0.3 million for the corresponding period in 2004. After providing for preferred share dividends, earnings per common share in the three months ended June 30, 2005 were \$0.02 compared with \$0.06 for the same period in 2004. The decrease in net income is primarily the result of higher gas processing and distribution maintenance expenses, offset by reductions in administrative expenses.

Net income for the six months ended June 30, 2005 was \$4.1 million, compared with \$4.2 million for the corresponding period in 2004. After providing for preferred share dividends, earnings per common share in the six months ended June 30, 2005 were \$1.09 compared with \$1.11 for the same period in 2004. The decrease in net income is primarily the result of a 12 basis point reduction in the average allowed return on equity, from 9.75 percent in 2004 to 9.63 percent in 2005, offset by lower administrative and other interest expenses.

The rate stabilization adjustment mechanism approved by the Commission continues to contribute to the stability of the Company's earnings. This mechanism allows the Company to record the after-tax revenue variances arising from differences between actual and forecast sales volumes for residential and small commercial customers in a deferral account for collection or refund in future rates. Net income was \$0.6 million higher for the three months ended June 30, 2005, and \$0.4 million higher for the six months ended June 30, 2005 as a result of this account.

Residential deliveries were lower by seven percent in the three months ended June 30, 2005 and were lower by one percent in the six months ended June 30, 2005 relative to deliveries over the same periods in 2004. Weather was a prime contributor to reduced residential sales, as it was 8.7 percent warmer in the three months ended June 30, 2005, and 4.5 percent warmer in the six months ended June 30, 2005, compared to the same periods in 2004. Commercial deliveries were higher by twelve percent in the second quarter of 2005 and were higher by four percent in the first six months of 2005 relative to deliveries over the same periods in 2004. Deliveries to commercial customers tend to be less temperature sensitive and a large commercial customer was added in the northeastern region during the third quarter of 2004. Industrial deliveries for the three month and six month periods ended June 30, 2005 were lower by three percent and one percent, respectively, compared to the same periods in 2004. The reduction in industrial deliveries is primarily attributable to lower deliveries to three large industrial customers. A deferral account is in place that recovers or refunds margin differences resulting from large industrial customers' demand varying from the forecast approved for ratemaking purposes.

Results of Operations

Operating revenues in the three months ended June 30, 2005 increased to \$30.3 million as compared with \$28.2 million in the corresponding period in 2004. The increase in operating revenues was primarily due to an increase of \$1.6 million in revenues from the sale of gas surplus to the needs of the Company's sales customers ("off system gas sales"), as well as higher gas supply costs embedded in sales customers' rates compared with the corresponding period in 2004. Natural gas commodity prices, which are passed through to the Company's sales customers without mark-up, are very volatile and result in significant variability of the Company reported operating revenues, but do not affect net income. Any profit or loss realized on off system gas sales is deferred for future recovery from, or refund to, the Company's sales customers.

Operating revenues in the first six months of 2005 increased to \$78.1 million as compared with \$71.8 million in the first six months of 2004. The increase in operating revenues was primarily due to higher gas supply costs embedded in sales customers' rates compared with the corresponding period in 2004, as well as an increase of \$1.2 million in off system gas sales.

Operating margin in the three months ended June 30, 2005 declined to \$9.8 million, as compared with \$10.4 million in the same period in 2004. Operating margin in the first six months of 2005 declined to \$25.9 million, as compared with \$26.9 million in the first six months of 2004. The

decreases in operating margin are largely a result of lower company use gas costs included in customer rates, compared to the same periods in 2004, as well as a 12 basis point reduction in allowed return on equity.

The Company filed a report with the Commission in June 2005 on past and projected gas supply costs compared to gas cost recoveries from customers. On the basis of the report, and at the Company's request, the Commission issued an order, effective July 1, 2005, to increase the gas supply commodity and rate rider components of rates for customers in the PNG-West division by \$0.50 per gigajoule and in the Fort St. John/Dawson Creek division by \$0.40 per gigajoule and to decrease the corresponding Tumbler Ridge division gas supply rates by \$0.75 per gigajoule..

On May 5, 2005, the Commission released its decision on the 2005 revenue requirements application for the Fort St. John/Dawson Creek and Tumbler Ridge divisions. The decision resulted in the allowed cost of service for 2005 being slightly less than what the interim rates were based on effective January 1, 2005. The lower permanent rates were implemented as of July 1, 2005. The interim to permanent rate reductions on gas deliveries from January 1 to June 30, 2005, amounting to \$0.2 million, have been recorded as a liability at June 30, 2005 and are being refunded by the application of interim rate refund riders on deliveries over the third and fourth quarters of 2005.

Summary of Quarterly Results for Eight Quarters Ending June 30, 2005

<i>Thousands of dollars except per share amounts</i>	June 30, 2005	Mar 31, 2005	Dec 31, 2004	Sept 30, 2004	June 30, 2004	Mar. 31, 2004	Dec 31, 2003 ³	Sept 30, 2003 ³
Operating Revenues	\$30,293	\$47,798	\$40,757	\$25,169	\$28,245	\$43,584	\$39,448	\$24,025
Net Income (loss) ¹	137	3,984	2,670	(1,427)	317	3,848	2,665	(723)
- per share ²	0.02	1.08	0.72	(0.42)	0.06	1.05	0.72	(0.22)
- per share diluted ²	0.01	1.06	0.71	(0.42)	0.06	1.03	0.70	(0.22)

¹ The Company did not have any extraordinary items which impacted net income over the most recently completed eight quarters.

² Per share amounts are after provision for preferred share dividends of \$84,000 per quarter.

³ Restated to reflect the fair value method of accounting for stock options in 2003

The Company's natural gas distribution business is very seasonal, with higher sales in the colder winter months and lower sales in warmer months. Given that a substantial portion of its gas sales are used for space heating purposes, the Company earns the majority of its net income in the first and fourth quarters of its fiscal year and often realizes losses in the other quarters.

Liquidity

In January 2005, the Company arranged new credit facilities, which include a \$20 million operating line and a \$15 million risk management facility. The new operating line is subject to borrowing base requirements and financial covenants which may act to restrict the amount the Company can borrow under the operating line. As of June 30, 2005, the calculated borrowing base was \$15.7 million, of which \$3.4 million had been drawn. The credit facilities are collateralized by the pledge of a \$40 million debenture and a charge on certain accounts receivables and inventories.

In addition to the borrowing base, the Company has provided certain financial covenants to its operating lender. One of these covenants is a restricted payments test which, in essence, prevents the Company from borrowing under the operating line to fund capital expenditures, make scheduled debt amortization payments, or make dividend payments. The Company continues to be in compliance with the covenants under its operating line through the end of June 2005.

The risk management facility allows the Company to hedge natural gas purchases in accordance with its annual gas contracting and gas supply price management plan and to enter into interest rate hedging transactions to the extent of a total maximum exposure of \$15 million, with exposure calculated by the facility provider using its standard methodology.

Accounts receivable at June 30, 2005 are \$7.8 million lower than at December 31, 2004 due to customer billings for the peak winter season being collected by the end of the second quarter. In addition, accounts payable at the end of the second quarter are \$6.0 million lower than at December 31, 2004, as lower gas volumes are generally purchased in the month of June compared to December.

The Company purchases gas for resale to its gas sales customers and passes through the commodity cost of gas to those customers without mark-up. The rates charged to gas sales customers are based, in part, on projected gas supply prices. The Company's liquidity requirements are affected by delays between increases or decreases in the cost of gas purchased by the Company and regulatory approval of rate adjustments to reflect the cost increases or decreases.

Capital Resources

The Company has not made any material commitments for capital expenditures at this time. It has plans for capital expenditures of \$5.8 million in the last two quarters of 2005 in order to maintain its transmission and distribution system and to provide for minor expansions of its distribution system to service new customers. The Company expects to finance these expenditures through operating cash flows.

Off-Balance Sheet Arrangements

As of June 30, 2005, the Company had no off-balance sheet arrangements, other than the natural gas hedging contracts described in Financial and Other Instruments below.

Transactions with Related Parties

The Company has not had any transactions with related parties during the first six months of 2005.

Critical Accounting Estimates

Operating revenues include natural gas sales that are recorded on the basis of regular meter readings and estimates of customer usage from the last meter reading date to the end of the reporting period for such operating revenues. These estimates are made assuming normal consumption patterns, adjusted for weather variations, which may differ from actual consumption patterns. The estimates of unbilled operating revenue comprise 2.3 percent of the Company's operating revenues for the six month period ended June 30, 2005. Through future meter readings, the usage estimates are replaced with actual delivered volumes which will be reflected in the Company's financial results at that time.

Operating revenues for the PNG West division for the six months and three months ended June 30, 2005 are based on interim rates that have been approved by the Commission. Permanent rates will be set following receipt of the Commission's decision on the Company's 2005 rate application and may result in retroactive adjustments to the interim rates. The Company has no reason to believe that the permanent rates will be materially different than its interim rates.

The Company's subsidiary Pacific Northern Gas (N.E.) Ltd. continues to be involved in a dispute with a customer over the payment for gas transported to the customer. The dispute relates to the customer's failure to offset gas delivered to the customer by PNG(NE) over an approximate two year period in 2001 and 2002. On April 22, 2003 PNG(NE) commenced an action in the Supreme Court of British Columbia against the customer, claiming damages for breach of contract and, in the alternative, restitution for unjust enrichment. On July 8, 2005 the Court heard a motion by the

customer for an order that the Company's back-billing tariff applies. If the tariff applies, the amount recoverable could be reduced. A decision on this motion is expected in early August 2005. A trial date has been set for October 2005. The Company believes its case for recovery of the amounts billed has significant merit and has recorded the related accounts receivable at management's best estimate of the amount ultimately recoverable. Approximately \$1.6 million relating to the dispute has been included in accounts receivable at June 30, 2005 and December 31, 2004. There is a risk that the amount ultimately recovered may be materially different from management's estimate.

Financial and Other Instruments

The Company utilizes natural gas commodity hedging contracts in order to manage the volatility inherent in the prices of its natural gas purchases. It also utilizes interest rate hedging contracts to reduce the volatility of the interest expense associated with its floating rate debt instruments. As of June 30, 2005 the Company had no interest rate hedging contracts outstanding.

During the first quarter of 2005 the Company completed its annual gas contracting and gas supply price management plan and filed it with the Commission. Review and acceptance of the plan by the Commission was received on June 22, 2005. The plan calls for gas price hedging, covering purchases over the period November 1, 2005 through October 31, 2006, to be completed in stages over the mid-June to mid-October 2005 period. Each hedging transaction is subject to approval by the Company's price management committee.

At June 30, 2005, the Company had outstanding fixed price contracts, natural gas swap contracts, and call options relating to natural gas supply as follows:

Financial instrument	Notional Quantity (GJ's)	Percent of Annual Gas Purchases	Delivery period	Price Range (per GJ)	Fair Value Receivable
Fixed price contracts	610,000	4.5	July 2005 to Oct. 2006	\$5.83 to \$6.87	\$312,200
Natural gas swap contracts	214,000	1.6	April 2006 to Oct. 2006	\$7.87	100
Call options	633,000	4.7	Nov. 2005 to March 2006	\$10.00	\$326,000
Total	1,457,000	10.8			\$638,300

The fair value reflects the estimated amounts that the Company would receive at June 30, 2005 to terminate the fixed price contracts, natural gas swap contracts, or call options, based on the estimated net cash flows under the terms of each contract.

Dividends

The Board of Directors declared a quarterly dividend of 20 cents per share on the Company's Common Shares, payable September 23, 2005 to shareholders of record at the close of business on September 8, 2005.

Other

The Company files an Annual Information Form on SEDAR which can be accessed at www.sedar.com.

Pacific Northern Gas Ltd. had 3,626,180 common shares and 200,000 preferred shares outstanding as of July 27, 2005. These are the only issued securities of the Company and it has no securities outstanding which may be converted into voting or equity securities.

"Roy G. Dyce"
President and Chief Executive Officer

July 27, 2005

Notice Required Under Part 4.3(3) of National Instrument 51-102

TO THE SHAREHOLDERS OF PACIFIC NORTHERN GAS LTD.

The interim financial statements of Pacific Northern Gas Ltd. for the period ended June 30, 2005 have not been reviewed by an auditor.

**PACIFIC NORTHERN GAS LTD.
CONSOLIDATED BALANCE SHEETS
AS AT JUNE 30, 2005 AND DECEMBER 31, 2004
(in thousands)**

	<u>June 30, 2005</u>	<u>December 31, 2004</u>
ASSETS		
Current assets:		
Accounts receivable	\$ 15,483	\$ 23,304
Income taxes recoverable	-	362
Inventory of supplies and natural gas	2,170	1,725
Prepaid expenses	2,208	215
	<u>19,861</u>	<u>25,606</u>
Plant, property and equipment	<u>174,979</u>	<u>176,780</u>
Deferred charges:		
Debt expense	684	754
Rate stabilization adjustment mechanism	1,934	1,788
Pipeline rehabilitation costs	1,047	1,128
Other	1,576	1,601
	<u>5,241</u>	<u>5,271</u>
	<u>\$200,081</u>	<u>\$207,657</u>
 LIABILITIES		
Current liabilities:		
Bank indebtedness	\$ 3,426	\$ 6,046
Accounts payable and accrued liabilities	10,040	16,037
Gas purchase variance payable	1,972	2,232
Income and other taxes payable	2,507	2,726
Long term debt due within one year	4,382	4,382
	<u>22,327</u>	<u>31,423</u>
Non-current liabilities	478	407
Long term debt, non-current portion	80,159	81,447
Deferred income taxes	15,430	15,430
	<u>96,067</u>	<u>97,284</u>
	<u>118,394</u>	<u>128,707</u>
 SHAREHOLDERS' EQUITY		
Preferred shares	5,000	5,000
Common shares	9,065	9,009
Contributed surplus	2,743	2,567
Retained earnings	64,879	62,374
	<u>76,687</u>	<u>73,950</u>
	<u>81,687</u>	<u>78,950</u>
	<u>\$200,081</u>	<u>\$207,657</u>

ON BEHALF OF THE BOARD

"Robert F. Chase"
Director

"Roy G. Dyce"
Director

PACIFIC NORTHERN GAS LTD.
CONSOLIDATED STATEMENTS OF RETAINED EARNINGS
(in thousands)

	For the six months ended June 30		For the three months ended June 30	
	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>
Balance, beginning of period	\$62,374	\$60,183	\$65,636	\$63,312
Net income for the period	4,121	4,165	137	317
	<u>66,495</u>	<u>64,348</u>	<u>65,773</u>	<u>63,629</u>
Preferred Dividends	169	168	169	169
Common dividends	1,447	1,439	725	720
	<u>1,616</u>	<u>1,608</u>	<u>894</u>	<u>889</u>
Balance, end of period	<u>\$64,879</u>	<u>\$62,740</u>	<u>\$64,879</u>	<u>\$62,740</u>

CONSOLIDATED STATEMENTS OF CASH FLOW
(in thousands)

	For the six months ended June 30		For the three months ended June 30	
	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>
Operating activities:				
Net income for the period	\$4,121	\$4,165	\$ 137	\$ 317
Add (deduct) items not involving cash				
Deferred income taxes	456	846	331	316
Depreciation and amortization	4,501	4,287	2,263	2,144
Stock option expense	47	47	24	24
Other	(386)	(858)	(297)	(322)
Operating cash flow	<u>8,739</u>	<u>8,487</u>	<u>2,458</u>	<u>2,479</u>
Non-cash working capital changes	(727)	7,503	3,112	7,246
Net cash provided by operating activities	<u>8,012</u>	<u>15,990</u>	<u>5,570</u>	<u>9,725</u>
Investing activities:				
Additions to plant, property and equipment	(2,201)	(2,953)	(1,113)	(2,250)
Increase in deferred charges	(470)	(1,469)	(323)	(541)
Net cash used in investing activities	<u>(2,671)</u>	<u>(4,422)</u>	<u>(1,436)</u>	<u>(2,791)</u>
Financing activities:				
Decrease in bank indebtedness	(2,620)	(2,900)	(2,723)	-
Repayment of long term debt	(1,290)	(1,288)	(645)	(643)
Issue of common shares	185	110	128	11
Dividends paid	(1,616)	(1,608)	(894)	(889)
Net cash used in financing activities	<u>(5,341)</u>	<u>(5,686)</u>	<u>(4,134)</u>	<u>(1,521)</u>
Increase in cash during the period	-	5,882	-	5,413
Cash, beginning of period	-	313	-	782
Cash, end of period	<u>\$ -</u>	<u>\$6,195</u>	<u>\$ -</u>	<u>\$6,195</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

These unaudited interim consolidated financial statements are prepared, from the records of the Company, in accordance with Canadian generally accepted accounting principles, except that disclosures do not conform, in all respects, to the requirements for annual consolidated financial statements. While management believes that the disclosures presented are adequate to make the information not misleading, these consolidated financial statements and notes should be read in conjunction with the Company's most recent annual consolidated financial statements.

These interim consolidated financial statements follow the same accounting policies and methods of their application as the Company's most recent annual consolidated financial statements.

Earnings for the interim periods may not be indicative of results for the fiscal year due to weather variations and other factors.

1. STOCK-BASED COMPENSATION

The Company does not have any plans which result in the direct award of stock, stock appreciation rights and awards that call for settlement in cash or other assets. The Company has one stock-based compensation plan. No options were issued in the six-month period ended June 30, 2005. The compensation cost that has been charged against income (and credited to contributed surplus) in the quarter ended June 30, 2005 is \$24,000 [2004 - \$24,000] and represents expense for options issued in previous periods which are being amortized over their vesting period.

The fair value of each option grant is estimated on the date of the grant using the Black-Scholes option pricing model with the following assumptions:

	Six months ended June 30 2005	Three months ended June 30 2005
Risk free interest rate	3%	3%
Expected volatility (annualized)	44%	44%
Expected years of option life (average)	7	7
Expected annual rate of dividends	4%	4%

2. SEASONALITY

Due to the seasonal nature of natural gas sales, more than 95 percent of the Company's net income is generally reported in the first and fourth quarters of the year, representing the typical timing of the heating season.

3. PREFERRED SHARES

The 6.75 percent preferred shares are redeemable at the option of the Company at \$26 per share plus any accrued and unpaid dividends at the date of the redemption.

4. COMMON SHARES

The Company has outstanding stock options for 255,800 common shares, of which 219,720 are exercisable as at June 30, 2005. There were 64,800 stock options outstanding at June 30, 2005 that could potentially dilute basic earnings per share in the future but were not included in the computation of diluted earnings per share because the options' exercise prices were greater than the average market price of the common shares.

During the quarter ended June 30, 2005, the Company issued 15,400 common shares for cash consideration of \$128,820 upon the exercise of employee options. Of this amount, \$90,320 has been credited to contributed surplus, representing the excess of the issue price over the par value of the shares.

5. CONTINGENCY AND MEASUREMENT UNCERTAINTY

Pacific Northern Gas (N.E.) Ltd. continues to be involved in a dispute with a customer over the payment for gas transported to the customer. The dispute relates to the customer's failure to offset gas delivered to the customer by PNG(NE) over an approximate two year period in 2001 and 2002. On April 22, 2003 PNG(NE) commenced an action in the Supreme Court of British Columbia against the customer, claiming damages for breach of contract and, in the alternative, restitution for unjust enrichment. On July 8, 2005 the Court heard a motion by the customer for an order that the Company's back-billing tariff applies. If the tariff applies, the amount recoverable could be reduced. A decision on this motion is expected in early August 2005. A trial date has been set for October 2005. The Company believes its case for recovery of the amounts billed has significant merit and has recorded the related accounts receivable at management's best estimate of the amount ultimately recoverable. Approximately \$1.6 million relating to the dispute has been included in accounts receivable at June 30, 2005 and December 31, 2004. There is a risk that the amount ultimately recovered may be materially different from management's estimate.

6. COMPARATIVE FIGURES

Certain items in the consolidated financial statements have been reclassified to conform to the 2005 presentation.

I, Roy Dyce, the Chief Executive Officer of Pacific Northern Gas Ltd., certify that:

1. I have reviewed the interim filings of Pacific Northern Gas Ltd., (the issuer) for the interim period ending June 30, 2005;
2. Based on my knowledge, the interim filings do not contain any untrue statement of a material fact or omit to state a material fact required to be stated or that is necessary to make a statement not misleading in light of the circumstances under which it was made, with respect to the period covered by the interim filings; and
3. Based on my knowledge, the interim financial statements together with the other financial information included in the interim filings fairly present in all material respects the financial condition, results of operations and cash flows of the issuer, as of the date and for the periods presented in the interim filings.

"Roy G. Dyce"

Roy G. Dyce
Chief Executive Officer

Date: July 27, 2005



I, Elizabeth A. Fletcher, the Chief Financial Officer of Pacific Northern Gas Ltd., certify that:

1. I have reviewed the interim filings of Pacific Northern Gas Ltd., (the issuer) for the interim period ending June 30, 2005;
2. Based on my knowledge, the interim filings do not contain any untrue statement of a material fact or omit to state a material fact required to be stated or that is necessary to make a statement not misleading in light of the circumstances under which it was made, with respect to the period covered by the interim filings; and
3. Based on my knowledge, the interim financial statements together with the other financial information included in the interim filings fairly present in all material respects the financial condition, results of operations and cash flows of the issuer, as of the date and for the periods presented in the interim filings.

"Elizabeth A. Fletcher"

Elizabeth A. Fletcher
Chief Financial Officer

Date: July 27, 2005