



interim statement

For the three months ended March 31, 2005

April 28, 2005

Pacific Northern Gas Ltd.
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Pacific Northern Gas Ltd.
MANAGEMENT'S DISCUSSION AND ANALYSIS
for the Three Months Ended March 31, 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 area. 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 reduce 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.

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 is scheduled to commence on May 10, 2005.

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 represent 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 first three months of 2005 was \$4.0 million, compared with \$3.8 million for the corresponding period in 2004. After providing for preferred share dividends, earnings per common share in the first three months of 2005 were \$1.08 compared with \$1.05 for the first three months of

2004. The increase in net income is primarily the result of reduced operating and administrative 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 \$0.1 million lower for the three months ended March 31, 2005 as a result of this account.

Residential deliveries were lower by 2 percent in the first three months of 2005 relative to deliveries over the same period in 2004. Weather was a prime contributor to reduced residential sales, as it was 2.7 percent warmer in the three months ended March 31, 2005 compared to the same period in 2004. Commercial deliveries were higher by 5 percent in the first three months of 2005 as deliveries to commercial customers tend to be less temperature sensitive and a large commercial customer was added in the Northeast region during the third quarter of 2004. Industrial deliveries for the three months ended March 31 did not vary significantly from 2004 to 2005.

There were no significant unaccounted for gas losses in the three month period ended March 31, 2005, compared to \$0.1 million for the same period in 2004. A consultant was hired in 2004 to identify and investigate possible causes contributing to a \$0.7 million unaccounted for gas loss, net of income taxes, that was incurred in the twelve month period ended 2004. Further investigation of the 2004 gas losses is being conducted in 2005, including field audits of major gas receipt and delivery points.

Results of Operations

Operating revenues in the first three months of 2005 increased to \$47.8 million as compared with \$43.6 million in the first three 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. This was offset by a \$0.4 million decrease in revenues from the sale of gas surplus to the needs of the Company's sales customers ("off system gas sales"). 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.

Operating margin in the first three months of 2005 declined to \$16.1 million, as compared with \$16.5 million in the first three months of 2004. The decrease in operating margin is largely a result of lower company use gas costs included in customer rates, compared to the same period in 2004.

The Company filed a report with the Commission in March 2005 on forecast gas supply prices. On the basis of the report, and at the Company's request, the Commission issued an order to reduce the gas supply commodity and rate rider components of rates for customers in the Tumbler Ridge division by \$1.00 per gigajoule, effective April 1, 2005.

The Company's most recent collective agreement with the International Brotherhood of Electrical Workers (the "Union") expired on October 31, 2004. A memorandum of agreement regarding a new three year collective agreement was signed in March 2005. On April 1, 2005, the Company was advised by the Union that the memorandum of agreement had been ratified by the unionized employees.

Summary of Quarterly Results for Eight Quarters Ending March 31, 2005

<i>Thousands of dollars except per share amounts</i>	Mar 31, 2005	Dec 31, 2004	Sept 30, 2004	Jun 30, 2004	Mar 31, 2004	Dec 31, 2003 ³	Sept 30, 2003 ³	Jun 30, 2003 ³
Operating Revenues	\$47,798	\$40,757	\$25,169	\$28,245	\$43,584	\$39,448	\$24,025	\$28,571
Net Income (loss) ¹	3,984	2,670	(1,427)	317	3,848	2,665	(723)	47
- per share ²	1.08	0.72	(0.42)	0.06	1.05	0.72	(0.22)	(0.01)
- per share diluted ²	1.06	0.71	(0.42)	0.06	1.03	0.70	(0.22)	(0.01)

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

Throughout 2004, the Company had a bank demand operating and hedge line of credit of \$25 million, with interest based on the prime rate and bankers' acceptance rates. This line of credit provided funds for general corporate and working capital requirements. The amount available under this facility was subject to borrowing base requirements.

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. The borrowing base under the new facility is less restrictive than the previous operating line, and the amount available for borrowing by the Company has therefore increased. As of March 31, 2005, the calculated borrowing base exceeded the \$20 million available under the operating line. The new 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 March 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 March 31, 2005 are \$2.7 million higher than at December 31, 2004 due to customer billings for the peak winter season not yet collected by the end of the quarter. In addition, accounts payable at the end of the first quarter are \$2.9 million lower than at December 31, 2004, as lower gas volumes are generally purchased in the month of March 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 \$8.0 million in 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 March 31, 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 three 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 which may differ from actual consumption patterns. The estimates of unbilled operating revenue comprise 13.6 percent of the Company's operating revenues to March 31, 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 three months ended March 31, 2005 are based on interim rates that have been approved by the Commission. Permanent rates will be set following receipt of the Commission's decisions on the Company's 2005 rate applications 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 April 13, 2005 the customer served notice of its intention to seek an order that the Company's back-billing tariff applies. If the tariff applies, the amount recoverable could be reduced. 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 March 31, 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 March 31, 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 is expected in the second quarter of 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-April to mid-October 2005 period. Each hedging transaction is subject to approval by the Company's price management committee.

At March 31, 2005, the Company had outstanding fixed price contracts covering approximately 1.1 million gigajoules of natural gas to be delivered in the months from April 2005 through October 2005 (representing approximately 7.6 percent of forecast annual system gas supply) at prices ranging from \$5.83 to \$6.87 per gigajoule. The fair value receivable under the fixed price contracts at March 31, 2005 was \$1.5 million. The fair value reflects the estimated amounts that the Company would receive at March 31, 2005 to terminate the fixed price contracts, 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 June 23, 2005 to shareholders of record at the close of business on June 6, 2005.

The Board of Directors also declared a semi-annual dividend of 84.375 cents per share on the Company's 6-3/4 percent cumulative, redeemable preferred shares, payable July 1, 2005 to shareholders of record at the close of business on June 9, 2005.

Other

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

Pacific Northern Gas Ltd. had 3,612,780 common shares and 200,000 preferred shares outstanding as of April 28, 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

April 28, 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 March 31, 2005 have not been reviewed by an auditor.

PACIFIC NORTHERN GAS LTD.
CONSOLIDATED STATEMENTS OF INCOME
(in thousands)
For the three months ended March 31

	<u>2005</u>	<u>2004</u>
Operating revenues	\$47,798	\$43,584
Cost of sales	31,667	27,119
Operating margin	16,131	16,465
Operating and maintenance	2,909	3,376
Administrative and general	1,692	1,780
Amortization of deferred charges	214	172
Municipal and other taxes	1,030	985
Depreciation	1,989	1,971
	7,834	8,284
Operating income	8,297	8,181
Investment and other income	4	5
	8,301	8,186
Income deductions:		
Interest on long term debt	1,773	1,844
Other	122	197
	1,895	2,041
Income before income taxes	6,406	6,145
Income taxes		
- Currently payable	2,297	1,767
- Deferred	125	530
	2,422	2,297
Net income for the period	\$3,984	\$3,848
For common shares:		
Net income for the period	\$3,984	\$3,848
Dividends on preferred shares	84	84
Net income applicable to common shares, basic and diluted	\$3,900	\$3,764
Earnings per common share:		
Basic	\$1.08	\$1.05
Diluted	\$1.06	\$1.03
Weighted average number of common shares outstanding:		
Basic	3,608,664	3,589,143
Diluted	3,690,983	3,668,562

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

	<u>March 31,</u> <u>2005</u>	<u>December 31,</u> <u>2004</u>
ASSETS		
Current assets:		
Accounts receivable	\$ 26,047	\$ 23,304
Income taxes recoverable	—	362
Inventory of supplies and natural gas	1,939	1,725
Prepaid expenses	412	215
	28,398	25,606
Plant, property and equipment	175,879	176,780
Deferred charges:		
Debt expense	719	754
Rate stabilization adjustment mechanism	1,425	1,788
Pipeline rehabilitation costs	1,084	1,128
Other	1,475	1,601
	4,703	5,271
	\$208,980	\$207,657
 LIABILITIES		
Current liabilities:		
Bank indebtedness	\$ 6,149	\$ 6,046
Accounts payable and accrued liabilities	13,159	16,037
Gas purchase variance payable	1,766	2,232
Income and other taxes payable	4,557	2,726
Long term debt due within one year	4,382	4,382
	30,013	31,423
Non-current liabilities	443	407
Long term debt	80,802	81,447
Deferred income taxes	15,430	15,430
	96,675	97,284
	126,688	128,707
 SHAREHOLDERS' EQUITY		
Preferred shares	5,000	5,000
Common shares	9,027	9,009
Contributed surplus	2,629	2,567
Retained earnings	65,636	62,374
	77,292	73,950
	82,292	78,950
	\$208,980	\$207,657

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 three months ended March 31

	<u>2005</u>	<u>2004</u>
Balance, beginning of period	\$62,374	\$60,183
Net income (loss) for the period	3,984	3,848
	<u>66,358</u>	<u>64,031</u>
Common dividends	722	719
	<u>722</u>	<u>719</u>
Balance, end of period	<u>\$65,636</u>	<u>\$63,312</u>

CONSOLIDATED STATEMENTS OF CASH FLOW
(in thousands)
For the three months ended March 31

	<u>2005</u>	<u>2004</u>
Operating activities:		
Net income for the period	\$ 3,984	\$ 3,848
Add (deduct) items not involving cash		
Deferred income taxes	125	530
Depreciation and amortization	2,238	2,143
Stock option expense	23	23
Other	(89)	(536)
	<u>6,281</u>	<u>6,008</u>
Operating cash flow	6,281	6,008
Non-cash working capital changes	(3,839)	257
	<u>(3,839)</u>	<u>257</u>
Net cash provided by operating activities	<u>2,442</u>	<u>6,265</u>
Investing activities:		
Additions to plant, property and equipment	(1,088)	(703)
Decrease (increase) in deferred charges	(147)	(928)
	<u>(1,235)</u>	<u>(1,631)</u>
Net cash used in investing activities	<u>(1,235)</u>	<u>(1,631)</u>
Financing activities:		
Increase (decrease) in bank indebtedness	103	(2,900)
Repayment of long term debt	(645)	(645)
Issue of common shares	57	99
Dividends paid	(722)	(719)
	<u>(722)</u>	<u>(719)</u>
Net cash used in financing activities	<u>(1,207)</u>	<u>(4,165)</u>
Increase (decrease) in cash during the period	—	469
Cash, beginning of period	—	313
	<u>—</u>	<u>313</u>
Cash, end of period	<u>\$ —</u>	<u>\$ 782</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 three-month period ended March 31, 2005. The compensation cost that has been charged against income (and credited to contributed surplus) in the quarter ended March 31, 2005 is \$23,000 [2004 - \$23,000] 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:

	Three months ended March 31 2005	Three months ended March 31 2004
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 271,200 common shares, of which 212,600 are exercisable as at March 31, 2005. There were 26,200 stock options outstanding at March 31, 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 March 31, 2005, the Company issued 7,200 common shares for cash consideration of \$56,520 upon the exercise of employee options. Of this amount, \$38,520 has been credited to contributed surplus, representing the excess of the issue price over the par value of the shares.

Subsequent to the period end, on April 6, 2005, the Company issued an additional 2,000 common shares for cash consideration of \$23,630 upon the exercise of employee options. Of this amount, \$18,630 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 April 13, 2005 the customer served notice of its intention to seek an order that the Company's back-billing tariff applies. If the tariff applies, the amount recoverable could be reduced. 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 March 31, 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.

