



PRIMARY ENERGY RECYCLING CORPORATION

**Unaudited Interim Consolidated Financial Statements
(In US Dollars)**

Three Months Ended March 31, 2006

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Primary Energy Recycling Corporation
CONSOLIDATED BALANCE SHEETS

(In thousands of U.S. dollars)

	March 31, 2006 (Unaudited)	December 31, 2005
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 15,751	\$ 12,090
Accounts receivable	13,770	14,847
Spare parts inventory	1,033	1,033
Current future tax asset (Note 7)	1,502	1,622
Other current assets	829	802
Total current assets	32,885	30,394
Non-current assets:		
Property, plant and equipment, net	257,612	260,241
Intangible assets, net	202,190	209,711
Foreign currency exchange contracts	3,373	3,492
Interest rate swap contract	1,325	639
Deferred finance fees, net	7,707	8,019
Other non-current assets	233	247
Total assets	\$ 505,325	\$ 512,743
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 1,086	\$ 162
Due to affiliates (Note 9)	1,184	1,534
Accrued property taxes	5,496	5,255
Accrued interest payable	1,935	1,888
Distributions payable	2,508	2,508
Accrued expenses	1,953	2,096
Total current liabilities	14,162	13,443
Long term debt (Note 3)	217,255	217,340
Future tax liability (Note 7)	60,416	59,534
Asset retirement obligation	2,800	2,749
Total liabilities	294,633	293,066
Commitments and contingencies (Note 4)		
Non-controlling preferred interest (Note 5)	13,225	13,225
Non-controlling common interest (Note 5)	34,084	36,418
Shareholders' equity:		
Common stock (Note 6)	178,571	178,571
Shareholders' deficit	(15,188)	(8,537)
Total shareholders' equity	163,383	170,034
Total liabilities, non-controlling interests and shareholders' equity	\$ 505,325	\$ 512,743

The accompanying notes are an integral part of these unaudited interim consolidated financial statements.

Primary Energy Recycling Corporation
CONSOLIDATED STATEMENT OF OPERATIONS AND SHAREHOLDERS' DEFICIT
(In thousands of U.S. dollars, except share and per share amounts)
(Unaudited)

	Three Months Ended March 31, 2006
Revenue:	
Capacity	\$ 9,018
Energy Service	16,700
	25,718
Expenses:	
Operations and maintenance	8,727
General and administrative	3,711
Depreciation and amortization	10,150
	3,130
Operating income	
Other Income (Expense):	
Interest income (expense), net	(5,058)
Unrealized gain on derivative hedge contracts (Note 8)	655
Gain on foreign currency translation	85
	(4,318)
Loss before income taxes	
Income tax expense (Note 7)	(989)
	(1,188)
Loss before non-controlling interest	
Non-controlling interest in class B Preferred	(382)
Non-controlling interest in class B Common	1,243
	(1,177)
Net Loss	
	\$ (1,316)
Shareholders' deficit - beginning of period	(8,537)
Distributions	(5,335)
Shareholders' deficit - end of period	\$ (15,188)
Weighted average number of shares outstanding	
	31,000,000
Basic and Diluted net loss per share (Note 10)	
	\$ (0.04)

The accompanying notes are an integral part of these unaudited interim consolidated financial statements.

Primary Energy Recycling Corporation
CONSOLIDATED STATEMENT OF CASH FLOWS

(In thousands of U.S. dollars, unless specified)

(Unaudited)

		Three Months Ended March 31, 2006
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	\$	(1,316)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization		10,150
Unrealized gain on foreign currency translation		(85)
Unrealized gain on foreign currency exchange contracts and interest rate swaps		(655)
Non-controlling interest		(1,243)
Amortization of deferred finance costs		312
Income taxes		989
Accretion of asset retirement obligations		51
Changes in operating assets and liabilities:		
Accounts receivable		1,077
Other assets		117
Accounts payable		924
Accrued property tax		241
Accrued interest payable		47
Accrued expenses		(143)
Increase in amounts owed to affiliates		(379)
Net cash provided by operating activities		<u>10,087</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Distributions on non-controlling Class B common interest		(1,091)
Distributions on Common Shares		(5,335)
Net cash used in financing activities		<u>(6,426)</u>
Net increase in cash		3,661
Cash - beginning of period		<u>12,090</u>
Cash - end of period	\$	<u><u>15,751</u></u>
 Supplemental disclosure of cash flow information:		
Cash paid during the period for interest	\$	4,842

The accompanying notes are an integral part of these unaudited interim consolidated financial statements.

Primary Energy Recycling Corporation
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(In thousands of U.S. dollars, unless specified)

(Unaudited)

1. Description of Business

Primary Energy Recycling Corporation (the “Company”) was incorporated on June 10, 2005 under the laws of the Province of Ontario and continued under the laws of British Columbia. For the period from June 10, 2005 to August 23, 2005, the Company was inactive. The Company initiated business activity on August 24, 2005 upon completion of an initial public offering (the “Offering”). In conjunction with the Offering, the Company acquired a majority interest in Primary Energy Recycling Holdings, LLC (“PERH”). The non-controlling interests of PERH is held by Primary Energy Holdings, LLC (“PEH”) a wholly-owned subsidiary of Primary Energy Ventures, LLC (the “Manager”). PERH, headquartered in Oak Brook, Illinois, indirectly owns and operates four recycled energy projects and a 50% interest in a pulverized coal facility all located in the United States (collectively, the “Projects”). The Projects have a combined electrical generating capacity of 283 megawatts and a combined steam generating capacity of 1,851 Mlbs/hour. PERH creates value for its customers by capturing and recycling waste energy from industrial processes and converting it into reliable and economical electricity and thermal energy for its customers’ use. For additional information with respect to the business, please see the Company’s public filings including its Annual Information Form dated March 30, 2006 available on SEDAR at www.sedar.com.

2. Basis of Presentation

The accompanying interim consolidated financial statements have been prepared in accordance with accounting principles generally accepted in Canada (“Canadian GAAP”) for interim financial information and do not contain all of the disclosures required for annual financial statements. Accordingly, the interim consolidated financial statements and related notes included herein are unaudited and should be read in conjunction with the annual consolidated financial statements and related notes for the year ended December 31, 2005, included in the Company’s 2005 Annual Report. These statements have been prepared following the same accounting policies and methods of computation as the annual consolidated financial statements of the Company for the year ended December 31, 2005 and include all normal recurring adjustments which management considers necessary for fair presentations. Certain amounts in the prior period financial statements and related notes have been reclassified to conform to the 2006 presentation.

3. Long Term Debt

Credit Facility

The Company’s Credit Facility is comprised of a \$135.0 million four-year term loan facility and a three-year \$15.0 million revolving credit facility, of

Primary Energy Recycling Corporation
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(In thousands of U.S. dollars, unless specified)

(Unaudited)

which \$0 of the revolving credit facility has been drawn as of March 31, 2006. The Credit Facility bears interest at a rate equal to LIBOR or U.S. Base Rate, plus an applicable margin. The borrower may elect from time to time to convert Eurodollar rate loans to base rate loans or base rate loans to Eurodollar rate loans by providing appropriate notice to the Administrative Agent of the Credit Facility. For the period ended March 31, 2006 the interest rate was defined using an average LIBOR rate of 4.5% plus 2.75%. The Credit Facility has a standby fee of 0.5% of the undrawn availability associated with the revolving credit facility. The Credit Facility requires the Company to meet certain financial covenants that among other things, requires the Company to maintain certain defined leverage and coverage ratios. The Credit Facility is collateralized by the Company's interests in, and the assets of, all subsidiaries and Projects. The Company has the ability to prepay the outstanding borrowings at anytime in whole or in part without penalty.

Subordinated and Separate Subordinated Notes

The Company has issued Subordinated Notes (forming part of EISs) of US\$59.3 million or Cdn\$71.25 million (as denominated in Canadian dollars using an exchange rate of Cdn\$1.20235 per US\$1.00. In connection with the Offering, the Company also issued the equivalent of US\$15.4 million or Cdn\$18.5 million (denominated in Canadian dollars using an exchange rate of Cdn\$1.20235 per US\$1.00) of Separate Subordinated Notes with a stated annual interest rate of 11.75% and a term of 12 years. Upon exercise of the Over-Allotment Option, an additional \$5.3 million or Cdn\$6.3 million (as denominated in Canadian dollars using an exchange rate of Cdn\$1.17050 per US\$1.00) of Subordinated Notes were also issued. The Subordinated Notes have a stated annual interest rate of 11.75% and a term of 12 years. For the period ended March 31, 2006, the Company recorded a gain on foreign currency translation of \$0.1 million related to these notes denominated in Canadian dollars. Amounts payable under these notes in U.S. dollars at March 31, 2006, have been adjusted to reflect the change in foreign exchange rates. The Subordinated and Separate Subordinated Notes are collateralized by unsecured guarantees of PERC's subsidiaries.

As of March 31, 2006, the Company is in compliance with all debt covenant requirements.

4. Commitments and Contingencies

Environmental Matters

The Company's operations are subject to a number of federal, state and local laws and regulations relating to the protection of the environment and the safety and health of personnel and the public. Some of the Company's operations require environmental permits and controls to prevent and reduce air and water

Primary Energy Recycling Corporation
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(In thousands of U.S. dollars, unless specified)

(Unaudited)

pollution, and these permits are subject to modification, renewal and revocation by issuing authorities. These requirements relate to a broad range of activities, including:

- Discharge of pollutants into the air, water and soil
- Identification, generation, storage, handling, transportation, disposal, record keeping, labeling and reporting of, and the emergency response in connection with, hazardous and toxic materials and wastes including asbestos
- Safety and health standards, practices and procedures that apply to the workplace and the operation of facilities

5. Non-controlling interest

Non-controlling interest at March 31, 2006 is comprised of the Class B preferred and common shares of PERH retained by the original investors in PERH and represents a 16.8% financial interest. Each Class B common is entitled to receive pro rata distributions as and when declared by the board of managers after payment in full of Class A preferred return and Class B preferred return.

6. Common stock

The Company issued 28.5 million EISs for cash proceeds of \$237.0 million on closing of the Offering on August 24, 2005. An additional 2.5 million EISs were issued on the closing of the Over-Allotment Option on September 27, 2005 generating additional proceeds of \$21.4 million. Each EIS was issued for Cdn\$10. Each EIS consists of one Common Share and Cdn\$2.50 of aggregate principal amount of 11.75% Subordinated Notes (Note 3). Net proceeds of \$178.6 million were allocated to Common Shares. Certain expenses of the Offering were specifically allocated and shared expenses were allocated based on the relative fair value of the Common Shares and the Subordinated Notes.

7. Income Taxes

Income tax expense (benefit) consists of the following for the three months ended March 31, 2006:

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(In thousands of U.S. dollars, unless specified)

(Unaudited)

Current tax provision:

Federal	\$	(10)
State		(3)
Total current tax		<u>(13)</u>

Future tax provision:

Federal		792
State		210
Total future tax		<u>1,002</u>
Total tax expense	\$	<u>989</u>

The Company recorded a net future tax liability at the date of acquisition representing the net tax effects of temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Future income tax expense relates to the increase in the future tax liability as reflected on the December 31, 2005 balance sheet as compared to the future tax liability at March 31, 2006. At inception, substantially all of the net future tax liability was the result of the differences in the basis of those assets and liabilities contributed by the non-controlling shareholders and is being amortized. This amount does not create a liability for EIS and Common share holders and will not impact the Company's future cash flow.

Significant components of the future tax assets and liabilities are as follows:

	<u>As at March 31, 2006</u>	<u>As at December 31, 2005</u>
	Future Tax Asset / (Liability)	Future Tax Asset / (Liability)
Accrued Expenses	\$ 708	\$ 708
Foreign Currency Translation	902	936
Current Future Tax Assets	<u>1,610</u>	<u>1,644</u>
Contract Termination Fee	18,469	19,085
Asset Retirement Obligation	1,134	1,113
Net Operating Loss	3,479	2,009
Valuation Allowance	<u>(3,479)</u>	<u>(2,009)</u>
Long-Term Future Tax Assets	<u>19,603</u>	<u>20,198</u>
Interest Rate Swap	<u>(108)</u>	<u>(22)</u>
Current Future Tax Liability	<u>(108)</u>	<u>(22)</u>
Other	(28)	(46)
Fixed Assets	(17,686)	(17,616)
Intangible Assets	(30,352)	(31,947)
Interest Rate Swap	(536)	(259)
Investment in PCI	<u>(31,417)</u>	<u>(29,864)</u>
Long-Term Future Tax Liability	<u>(80,019)</u>	<u>(79,732)</u>
Net Future Tax Liability	<u>\$ (58,914)</u>	<u>\$ (57,912)</u>

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The Company has U.S. and Canadian net operating loss carryforwards that will start to expire in 2025 and 2015, respectively. The Company has recorded a full valuation allowance on the net operating loss as it is more likely than not that the future asset will not be realized during the carryforward period.

The principal items which cause the Company's effective tax rate in 2006 to be greater than the Canadian statutory tax rate of 36.12% are the effect of the inclusion of the U.S federal and state income taxes that are greater than the Canadian statutory tax rate and the valuation allowance on the net operating loss are as follows:

Income tax Expense at Canadian	
Statutory Rate:	\$ (429)
Additional tax from operations in	
countries with different income tax	
rates	(52)
Valuation Allowance	1,470
Total Tax Expense	<u>\$ 989</u>

8. Derivative Instruments and Hedging Activities

The Company utilizes certain derivative instruments to enhance its ability to manage risk relating to cash flow and interest rate exposure. Derivative instruments are entered into for periods consistent with the related underlying exposures and are not entered into for speculative purposes.

Foreign Currency Exchange Contracts

The Company has entered into foreign currency exchange forward contracts (the "Forward Contracts") to exchange U.S. dollars for Canadian dollars. The Canadian dollars will be used to fund interest and cash distributions to EIS holders, the non-controlling interest and interest distributions to the separate subordinate note holders. The contracts are for a series of sixty monthly payment dates through September 2010. At March 31, 2006, fifty four contracts remain open. Each month, the Company sells a fixed amount of U.S. dollars for a fixed amount of Canadian dollars at a rate of Cdn\$1.1712 to U.S. \$1.00 for distributions to EIS holders and the non-controlling interest. The forward contracts applicable to distributions for the Separate Subordinated Notes have an exchange rate of Cdn\$1.1713 to US \$1.00. The Company was not required to deposit any collateral with regard to these contracts. The Forward Contracts do not qualify as a cash flow hedge for accounting purposes, and the change in the fair value is reflected in income. Fair value of the Forward Contracts was \$3.7 million at March 31, 2006, of which \$0.3 million is recorded in other current assets. The Forward Contracts have been entered into with a major Canadian bank as the counterparty. The risk associated with the Forward Contracts is the cost of replacing these instruments in the event of default by the counterparty. Management believes that this risk is remote.

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Interest Rate Swap Agreements

The Company entered into interest rate swap agreements on August 31, 2005. The contracts were purchased to mitigate the cash flow risk associated with the impact of changing interest rates or payments due under the Credit Facility. The agreements do not qualify as a cash flow hedge for accounting purposes and the change in the fair value of the derivative is recorded in income. The fair value of these agreements was a net amount of \$1.6 million at March 31, 2006, of which \$0.3 million is recorded in other current assets.

9. Related party transactions

The Company has a Management Agreement in place with the Manager. The Management Agreement has an initial 20-year term. The Manager provides various management and administrative services to PERC and its subsidiaries under terms defined in the Management Agreement. The Manager is entitled to an incentive fee under the Management Agreement equal to 25% of the product of (a) the excess of the Company's Distributable Cash per Common Share and (b) the weighted average number of EISs, Common Shares not represented by EISs and Class B Common Interests outstanding for such fiscal year. For the three month period ended March 31, 2006, the Company generated Distributable Cash (before payment of the management incentive fee) of \$11.1 million and accrued \$0.7 million of management incentive fee. The incentive fee is paid annually based upon year end results, is designed to align the financial interests of the Manager with those of the Company and is in addition to the annual management fee. In accordance with the Management Agreement, the Company recorded management fees of \$0.8 million and management incentive fees of \$0.7 million for the period.

As of March 31, 2006, the Company had a payable due to PEH of \$0.1 million and a payable due to the Manager of \$1.1 million. The Company has the ability and intent to settle these amounts.

10. Basic and Diluted net loss per share

Basic and Diluted net loss per share has been calculated using the weighted average number of Common Shares outstanding during the period of 31,000,000. For the three months ended March 31, 2006, there were no potentially dilutive securities outstanding.

Primary Energy Recycling Corporation
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(In thousands of U.S. dollars, unless specified)
(Unaudited)

11. Comparative Figures

The Company was incorporated on June 10, 2005 and did not complete the Offering until August 24, 2005. Consequently, there are no comparative figures for previous periods.

12. Segment Reporting

The Company owns and operates facilities designed to recycle waste energy under one operating segment. The Company serves as a single source of supply for its customers' related requirements. The Company's operations are located in the United States. All sales revenue is generated from the same geographic area.