PRIMARY ENERGY RECYCLING CORPORATION

Management's Discussion and
Analysis of Financial Condition and Results of Operations
(In US Dollars)

Three Months and Six Months Ended June 30, 2007 and 2006

Primary Energy Recycling Corporation
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following management's discussion and analysis of the financial condition and results of operations ("MD&A") of Primary Energy Recycling Corporation (the "Company") dated July 24, 2007 should be read in conjunction with the unaudited interim consolidated financial statements of the Company for the three months and six months ended June 30, 2007 and 2006. The Company's financial statements are prepared in accordance with accounting principles generally accepted in Canada ("Canadian GAAP"). All amounts described in this MD&A are in thousands of U.S. dollars, unless otherwise stated.

Forward-Looking Statements

Certain statements in this MD&A may constitute ''forward-looking statements'', which reflect the expectations of management regarding future growth, results of operations, performance and business prospects and opportunities of the Company. Such forward-looking statements reflect current expectations regarding future events and operating performance and speak only as of June 30, 2007. These forward-looking statements involve significant risks and uncertainties, and should not be read as guarantees of future performance or results, and will not necessarily be accurate indications of whether or not or the times at or by which such performance or results will be achieved.

A number of factors could cause actual results to differ materially from the results discussed in the forward-looking statements, including, but not limited to, the factors discussed under ''Risk Factors'' in this MD&A and in the Company's Annual Information Form dated March 8, 2007. Additional information relating to the Company, including its Annual Information Form, is available on SEDAR at www.sedar.com. Although the forward-looking statements contained in this MD&A are based upon what are believed to be reasonable assumptions, investors cannot be assured that actual results will be consistent with these forward-looking statements, and the differences may be material. These forward-looking statements are made as of the date of this MD&A and the Company assumes no obligation to update or revise them to reflect new events or circumstances.

Overview

General

The Company owns a majority interest in Primary Energy Recycling Holdings LLC ("PERH") which is headquartered in Oak Brook, Illinois. PERH indirectly owns and operates four recycling energy projects and a 50% interest in a pulverized coal facility (collectively, the ''Projects''). The Projects have a combined electrical generating capacity of 283 megawatts and a combined steam generating capacity of 1.8 MMlbs/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.

On August 24, 2005, the Company completed an initial public offering (the "Offering") through the issuance of 28.5 million enhanced income securities ("EISs") at a price of Cdn$10.00 per EIS, each representing one common share of the Company ("Common Share") and Cdn$2.50 principal amount of 11.75% subordinated notes ("Subordinated Notes"). In addition, the Company issued Cdn$18.5 million separate Subordinated Notes (not forming part of EISs) ("Separate Subordinated Notes") with the same terms as the EIS Subordinated Notes. A new credit facility was also entered into contemporaneously with the Offering consisting of a term loan facility of $135.0 million and a $15.0 million revolving credit facility (the "Credit Facility"). On September 27, 2005, the underwriters of the Offering exercised their over-allotment option to purchase 2.5 million additional EISs.

The Company used the proceeds of the Offering, and the proceeds of the over-allotment, to acquire an ownership interest in PERH. On completion of the Offering and closing of the over-allotment, the Company owned 85.8% of the preferred interests and 83.0% of the common interests in PERH, through its ownership of all of the issued and outstanding Class A preferred membership interests and all of the issued and outstanding Class A common membership interests of PERH. Primary Energy Ventures LLC (the "Manager"), indirectly holds the remaining 14.2% of the preferred interests and 17.0% of the common interests in PERH, through its ownership of all of the issued and outstanding Class B preferred membership interests and all of the issued and outstanding Class B common membership interests in PERH.

Definitions of Distributable Cash

References to ''EBITDA'' are to earnings before interest, taxes, depreciation, amortization and certain other adjustments listed in the reconciliation table provided herein. References to "Distributable Cash" are to EBITDA, as adjusted for: interest on the Credit Facility and interest on the Separate Subordinated Notes. EBITDA and Distributable Cash are not recognized measures under Canadian GAAP and do not have standardized meanings prescribed by Canadian GAAP. Therefore, EBITDA and Distributable Cash may not be comparable to similar measures presented by other issuers. The Company intends to distribute substantially all of its cash excluding those amounts required for operation of the business on an ongoing basis. Accordingly, management believes that EBITDA and Distributable Cash are important measures in evaluating the Company's performance. However, EBITDA and Distributable Cash should not be construed as an alternative to net earnings or loss determined in accordance with Canadian GAAP as an indicator of the Company's performance or to cash flows from operating, investing and financing activities, as a measure of liquidity and cash flows.

Primary Energy Recycling Corporation
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Results of Operations
(in 000's of US$, except per share data)

	Three Months Ended June 30, 2007	Three Months Ended June 30, 2006
Revenue:		
Capacity	$ 9,018	$ 9,018
Energy Service	8,888	12,884
	17,906	21,902
Expenses:		
Operations and maintenance	8,244	8,726
General and administrative	2,517	1,107
Depreciation and amortization	10,131	9,852
Total Operating Expenses	20,892	19,685
Operating income (loss)	$ (2,986)	$ 2,217
Other income (expense):		
Interest income (expense), net	(5,546)	(5,126)
Realized and unrealized gain on derivative hedge contracts	10,467	7,772
Unrealized loss on foreign currency translation	(7,337)	(3,844)
Income (loss) before income taxes	(5,402)	1,019
Income tax benefit (expense)	2,349	33
Income (loss) before non-controlling interest	(3,053)	1,052
Non-controlling interest in class B Preferred	(410)	(380)
Non-controlling interest in class B Common	(178)	1,202
Net Income (Loss)	$ (3,641)	$ 1,874
Weighted average number of shares outstanding	31,000,000	31,000,000
Basic and Diluted net income (loss) per share (Note 1)	$ (0.12)	$ 0.06

Note 1: Basic and Diluted net loss per share has been calculated using the weighted average number of Common Shares outstanding of 31,000,000 for the three months ended June 30, 2007 and June 30, 2006.

Three Months Ended June 30, 2007 compared to Three Months Ended June 30, 2006

The Company's revenue of $17.9 million in the second quarter of 2007 decreased $4.0 million, or 18.2% compared with revenue of $21.9 million for the second quarter of 2006. This decrease is reflective of a decline in Energy Service revenue at the Company's Harbor Coal facility totaling $3.1 million comprised of reduced revenue based on volume of $1.9 million offset by increased revenue based on pricing of $1.0 million which is due to the spread between the cost of coal supplied and the prices of the fuels that coal replaces (coke, natural gas and fuel oil) and efficiency of operations of $0.8 million. Harbor Coal also experienced a reduction in revenue of $3.0 million associated with additional consumption adjustments recorded by the facility based on ongoing physical inventory measurements conducted by Harbor Coal's joint venture host customer. The remaining decrease in Energy Service revenue of $0.9 million is primarily due to downtime associated with an unplanned turbine outage incurred at one operating facility during the second quarter of 2007.

Operating and maintenance expense for the second quarter of 2007 was $8.2 million compared to $8.7 million for the second quarter of 2006, a decrease of $0.5 million or 5.5%. The Company's Harbor Coal facility experienced reduced processing expenditures of $0.2 million and lower prices for production commodities including oxygen, nitrogen and labor resulting in decreased costs of $1.2 million. These cost reductions were offset by increased maintenance expenses of $0.9 million primarily associated with unplanned outage repair activity. As a percentage of revenue, operating and maintenance expenses increased to 46.0% for the second quarter of 2007 from 39.8% for the second quarter of 2006.

General and administrative expense for the second quarter of 2007 was $2.5 million compared to $1.1 million for the second quarter of 2006, an increase of $1.4 million or 127.2%. The increase is reflective of a second quarter of 2006 reduction in property tax expense of $1.8 million inclusive of property tax refunds and a reduction in accrued property taxes based upon completion of a successful appeal to the state taxing authorities for designation as a non-utility taxpayer, which reductions did not recur in the second quarter of 2007. The increase noted is offset by a second quarter of 2007 reduction in professional fees of $0.2 million, plant and liability insurance of $0.1 million and incentive fees of $0.1 million. As a percentage of revenue, general and administrative expenses increased to 14.1% for the second quarter of 2007 from 5.1% for the second quarter of 2006.

Depreciation expense totaled $2.6 million for the second quarter of 2007 and was essentially flat when compared to the second quarter of 2006. As a percentage of revenue, depreciation expense increased to 14.7% for the second quarter of 2007 from 12.0% for the second quarter of 2006.

Amortization expense for the second quarter of 2007 was $7.5 million compared to $7.2 million for the second quarter of 2006, an increase of $0.3 million. As a percentage of revenue, amortization expense increased to 41.9% for the second quarter of 2007 from 33.0% for the second quarter of 2006.

Operating loss for the second quarter of 2007 was $3.0 million compared to operating income of $2.2 million for the second quarter of 2006, a decrease of $5.2 million. The decrease was primarily driven by the net effect of the items discussed above.

Interest expense for the second quarter of 2007 was $5.5 million compared to $5.1 million for the second quarter of 2006. The increase in interest expense resulted primarily from an increase in the weighted average interest rate.

Realized and unrealized gain on derivative hedge contracts for the second quarter of 2007 was $10.5 million compared to $7.8 million for the second quarter of 2006. The increase reflects the change in fair value of the foreign currency exchange contracts and interest rate swap agreements held by the Company at June 30, 2007.

Unrealized loss on foreign currency translation for the second quarter of 2007 was $7.3 million compared to $3.8 million for the second quarter of 2006. The increase in the unrealized loss on foreign currency translation primarily reflects the impact of the change in foreign exchange rates used to convert the Subordinated Notes and the Separate Subordinated Notes from Canadian dollars to U.S. dollars.

The Company recorded an income tax benefit for the second quarter 2007 of $2.4 million comprised of a current tax expense of $0.3 million related to taxable income for the second quarter of 2007 and a future tax benefit of $2.7 million based on the change in value of future tax assets and liabilities. For the second quarter of 2006, the Company recorded a tax benefit of $0.03 million based on the change in value of future tax assets and liabilities.

Non-controlling interest for the second quarter of 2007 was $0.6 million compared to $0.8 million for the second quarter of 2006. These amounts represent the allocation of the non-controlling interest portion of the consolidated net loss before non-controlling interest to the Class B common interest and interest expense associated with distributions to the Class B preferred non-controlling interest.

Net loss for the second quarter of 2007 was $3.6 million compared to net income of $1.9 million for the second quarter of 2006, a decrease of $5.5 million. The decrease was primarily driven by the net effect of the items discussed above.

Primary Energy Recycling Corporation
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Results of Operations
(in 000's of US$, except per share data)

	Six Months Ended June 30, 2007	Six Months Ended June 30, 2006
Revenue:		
Capacity	$ 18,036	$ 18,036
Energy Service	16,597	29,584
	34,633	47,620
Expenses:		
Operations and maintenance	14,615	17,453
General and administrative	5,410	4,818
Depreciation and amortization	20,262	20,002
Total Operating Expenses	40,287	42,273
Operating income (loss)	$ (5,654)	$ 5,347
Other income (expense):		
Interest income (expense), net	(10,729)	(10,184)
Realized and unrealized gain on derivative hedge contracts	10,556	8,427
Unrealized loss on foreign currency translation	(8,140)	(3,759)
Loss before income taxes	(13,967)	(169)
Income tax benefit (expense)	3,101	(956)
Loss before non-controlling interest	(10,866)	(1,125)
Non-controlling interest in class B Preferred	(790)	(762)
Non-controlling interest in class B Common	735	2,445
Net Income (Loss)	$ (10,921)	$ 558
Weighted average number of shares outstanding	31,000,000	31,000,000
Basic and Diluted net income (loss) per share (Note 1)	$ (0.35)	$ 0.02

Note 1: Basic and Diluted net loss per share has been calculated using the weighted average number of Common Shares outstanding of 31,000,000 for the six months ended June 30, 2007 and June 30, 2006.

Six Months Ended June 30, 2007 compared to Six Months Ended June 30, 2006

The Company's revenue of $34.6 million in the first six months of 2007 decreased $13.0 million, or 27.3% compared with revenue of $47.6 million for the first six months of 2006. This decrease is reflective of a decline in Energy Service revenue at the Company's Harbor Coal facility totaling $11.5 million comprised of reduced revenue based on volume of $4.1 million, pricing of $2.5 million which is due to the spread between the cost of coal supplied and the prices of the fuels that coal replaces (coke, natural gas and fuel oil) offset by increased efficiency of operations of $0.4 million. Additionally, Harbor Coal has experienced reductions in revenue of $5.3 million during the period as a result of consumption adjustments recorded by the facility based on ongoing physical inventory measurements conducted by Harbor Coal's joint venture host customer. The remaining decrease in Energy Service revenue of $1.5 million is due primarily to an unplanned turbine outage incurred at one operating facility during the first six months of 2007 and reduced generation at another operating facility compared to the same period in the prior year.

Operating and maintenance expense for the first six months of 2007 was $14.6 million compared to $17.5 million for the first six months of 2006, a decrease of $2.9 million or 16.3%. The Company's Harbor Coal facility experienced reduced processing expenditures of $0.2 million and lower prices for production commodities including oxygen, nitrogen and labor resulting in decreased costs of $2.7 million. Additional maintenance expenses of $0.8 million were recorded in the first six months of 2007 associated primarily with the unplanned outage. Additionally, operating and maintenance expense for the first six months of 2006 included $0.8 million of planned overhaul expenses that were not recurring in the first six months of 2007. As a percentage of revenue, operating and maintenance expenses increased to 42.2% for the first six months of 2007 from 36.7% for the first six months of 2006.

General and administrative expense for the first six months of 2007 was $5.4 million compared to $4.8 million for the first six months of 2006, an increase of $0.6 million or 12.3%. The increase is reflective of a second quarter of 2006 reduction in property tax expense of $1.8 million inclusive of property tax refunds and a reduction in accrued property taxes based upon completion of a successful appeal to the state taxing authorities for designation as a non-utility taxpayer, which reductions did not recur in the second quarter of 2007. The increase noted is offset by a second quarter of 2007 reduction in incentive fees of $0.8 million, professional fees of $0.3 million and plant liability and insurance of $0.1 million. As a percentage of revenue, general and administrative expenses increased to 15.6% for the first six months of 2007 from 10.1% for the first six months of 2006.

Depreciation expense totaled $5.3 million for the first six months of 2007 and was essentially flat when compared to the first six months of 2006. As a percentage of revenue, depreciation expense increased to 15.2% for the first six months of 2007 from 11.0% for the first six months of 2006.

Amortization expense for the first six months of 2007 was $15.0 million compared to $14.7 million for the first six months of 2006, an increase of $0.3 million. As a percentage of revenue, amortization expense increased to 43.3% for the first six months of 2007 from 31.0% for the first six months of 2006.

Operating loss for the first six months of 2007 was $5.7 million compared to operating income of $5.3 million for the first six months of 2006, a decrease of $11.0 million. The decrease was primarily driven by the net effect of the items discussed above.

Interest expense for the first six months of 2007 was $10.7 million compared to $10.2 million for the first six months of 2006. The increase in interest expense resulted primarily from an increase in the weighted average interest rate.

Realized and unrealized gain on derivative hedge contracts for the first six months of 2007 was $10.5 million compared to $8.4 million for the first six months of 2006. The increase reflects the change in fair value of the foreign currency exchange contracts and interest rate swap agreements held by the Company at June 30, 2007.

Unrealized loss on foreign currency translation for the first six months of 2007 was $8.1 million compared to $3.8 million for the first six months of 2006. The increase in the unrealized loss on foreign currency translation primarily reflects the impact of the change in foreign exchange rates used to convert the Subordinated Notes and Separate Subordinated Notes from Canadian dollars to U.S. dollars.

The Company recorded an income tax benefit for the first six months 2007 of $3.1 million comprised of a current tax expense of $0.03 million related to taxable income for the first six months of 2007 and a future tax benefit of $3.1 million based on the change in value of future tax assets and liabilities. For the first six months of 2006, the Company recorded a tax expense of $1.0 million based on the change in value of future tax assets and liabilities.

Non-controlling interest for the first six months of 2007 was $0.06 million compared to $1.7 million for the first six months of 2006. These amounts represent the allocation of the non-controlling interest portion of the consolidated net loss before non-controlling interest to the Class B common interest and interest expense associated with distributions on the Class B preferred non-controlling interest.

Net loss for the first six months of 2007 was $10.9 million compared to net income of $0.6 million for the first six months of 2006, a decrease of $11.5 million. The decrease was primarily driven by the net effect of the items discussed above.

Summary of Quarterly Results
(In 000's of US$, except per share data)

	Period from 8/24 - 9/30 2005	4th Quarter 2005	1st Quarter 2006	2nd Quarter 2006	3rd Quarter 2006	4th Quarter 2006	1st Quarter 2007	2nd Quarter 2007
Revenues	$ 9,165	$ 23,234	$ 25,718	$ 21,902	$ 21,177	$ 18,275	$ 16,727	$ 17,906
Net income (loss)	$ 510	$ (1,474)	$ (1,316)	$ 1,874	$ (4,175)	$ (14,840)	$ (7,280)	$ (3,641)
Net income (loss) per share	$ 0.02	$ (0.05)	$ (0.04)	$ 0.06	$ (0.14)	$ (0.48)	$ (0.24)	$ (0.12)

Outstanding Share Data

At June 30, 2007, the Company had 31,000,000 Common Shares outstanding, of which 257,900 Common Shares were held separately and the remaining 30,742,100 Common Shares were held as a component of EISs. Each EIS consists of one Common Share and Cdn$2.50 principal amount of 11.75% Subordinated Notes.

Income (Loss) Per Share

Basic income (loss) per share is computed based on the weighted average number of Common Shares outstanding. For the three months and six months ended June 30, 2007 and 2006, there were no potentially dilutive securities issued and outstanding. Accordingly, diluted income (loss) per share is equivalent to basic income (loss) per share.

Liquidity and Capital Resources

For the three months ended June 30, 2007, the Company recorded a decrease in cash and cash equivalents of $2.3 million resulting in a balance of $11.3 million as of June 30, 2007. The Company's primary source of liquidity has historically been cash flow from operations. During the second quarter of 2007 the Company experienced the impact of additional inventory adjustments at its Harbor Coal facility, an unplanned turbine outage at one facility as well as a planned outage at another facility. These factors significantly impacted cash flow in the current quarter resulting in distributions in excess of cash generated through operating activities. To address the cash requirements impacting liquidity, as of May 2007, management reduced its annual rate distribution per EIS to Cdn$0.80 from Cdn$1.15. The monthly cash impact of the distribution reduction is $1.0 million. In the near term, management believes that the reduced distribution requirement and available cash funds will allow the Company to meet its liquidity needs. Over the long term, management believes available cash funds, in addition to cash flow to be generated from future operations and available credit facilities of $15.0 million will be sufficient to finance the Company's known or foreseeable liquidity and capital needs as well as anticipated maintenance requirements associated with the Company's facilities.

Cash Flows for the Three Months and Six Months Ended June 30, 2007

Net cash provided by operating activities for the three months ended June 30, 2007 was $4.3 million, which resulted from a net loss of $3.6 million, plus $5.5 million of net non-cash items charged to the Consolidated Statement of Operations, plus $2.4 million representing the net change in the Company's operating assets and liabilities. The net non-cash items consisted primarily of depreciation of property, plant and equipment and amortization of intangible assets. The net change in operating assets and liabilities resulted primarily from a decrease in accounts receivable and increases in accounts payable and accrued property taxes. These sources of cash were offset by decreases in accrued expenses and amounts owed to affiliates. Net cash provided by investing activities for the three months ended June 30, 2007 was $0.9 from cash settlements of foreign currency exchange contracts and interest rate swaps. Net cash used in financing activities for the three months ended June 30, 2007 was $7.5 million resulting from financing costs of $0.2 million, distribution payments of $5.3 million to holders of Common Shares and interest and distribution payments of $2.0 million to holders of Class B common and preferred membership interests in PERH.

Net cash provided by operating activities for the six months ended June 30, 2007 was $9.5 million, which resulted from a net loss of $10.9 million, plus $15.4 million of net non-cash items charged to the Consolidated Statement of Operations, plus $5.0 million representing the net change in the Company's operating assets and liabilities. The net non-cash items consisted primarily of depreciation of property, plant and equipment and amortization of intangible assets. The net change in operating assets and liabilities resulted primarily from a decrease in accounts receivable, inventory and other assets and increases in accounts payable, accrued property taxes and accrued expenses. These sources of cash were offset by increases in amounts owed to affiliates. Net cash provided by investing activities for the six months ended June 30, 2007 was $0.9 from cash settlements of foreign currency exchange contracts and interest rate swaps. Net cash used in financing activities for the six months ended June 30, 2007 was $14.8 million resulting from financing costs of $0.2 million, distribution payments of $11.0 million to holders of Common Shares and interest and distribution payments of $3.6 million to holders of Class B common and preferred membership interests in PERH.

Cash Flows for the Three Months and Six Months Ended June 30, 2006
Net cash provided by operating activities for the three months ended June 30, 2006 was $12.4 million, which resulted from net income of $1.9 million, plus $5.4 million of net non-cash items charged to the Consolidated Statement of Operations, plus $5.1 million representing the net change in the Company's operating assets and liabilities. The net non-cash items consisted primarily of depreciation of property, plant and equipment and amortization of intangible assets. The net change in operating assets and liabilities resulted primarily from a decrease in accounts receivable, increases in accounts payable and accrued property taxes, offset by reductions in accrued expenses and amounts owed to affiliates. Net cash used in financing activities for the three months ended June 30, 2006 was $6.9 million resulting from distribution payments of $5.5 million to holders of Common Shares and interest and distribution payments of $1.4 million to holders of Class B common and preferred membership interests in PERH.

Net cash provided by operating activities for the six months ended June 30, 2006 was $22.9 million, which resulted from net income of $0.6 million, plus $15.3 million of net non-cash items charged to the Consolidated Statement of Operations, plus $7.0 million representing the net change in the Company's operating assets and liabilities. The net non-cash items consisted primarily of depreciation of property, plant and equipment and amortization of intangible assets. The net change in operating assets and liabilities resulted primarily from a decrease in accounts receivable and increases in accrued property taxes, offset by reductions in accounts payable, accrued expenses and amounts owed to affiliates. Net cash used in financing activities for the six months ended June 30, 2006 was $13.7 million resulting from distribution payments of $10.8 million to holders of Common Shares and interest and distribution payments of $2.9 million to holders of Class B common and preferred membership interests in PERH.

Outstanding Debt

At June 30, 2007, the amount of outstanding debt under the Credit Facility was $135.0 million, with $15.0 million in additional borrowing capacity available under the revolving credit facility for working capital purposes. Also included in outstanding debt is $90.1 million in Subordinated Notes and Separate Subordinated Notes. The Credit Facility has a maturity date of August 24, 2009. The Subordinated Notes and Separate Subordinated Notes have a 12-year term and are due and payable on August 24, 2017. The Credit Facility, as well as the terms of the Subordinated Notes and Separate Subordinated Notes, requires the Company to meet certain financial covenants including, among other things, maintaining certain defined leverage and coverage ratios. During the second quarter of 2007, the Company's Credit Facility was amended to modify specified covenant levels for the remainder of 2007 and the first quarter of 2008. As of June 30, 2007, the Company was in compliance with all such debt covenant requirements. Subsequent to June 30, 2007, the Company drew $3 million from its Credit Facility revolver.

Cash Available for Distribution
The Company pays interest on the Subordinated Notes and Separate Subordinated Notes as stipulated and distributions on the Common Shares (when declared) in equal monthly amounts. Declarations of distributions on the Common Shares are based on periodic reviews of the Company's estimated annual earnings and related estimated annual cash flows. For the three months and six months ended June 30, 2007, the Company generated Cdn$4.6 million and Cdn$9.5 million of Distributable Cash and distributed Cdn$8.5 million and Cdn$19.3 million, for a payout ratio of 187.4 % and 202.5%, respectively. For three months and six months ended June 30, 2006, the Company generated Cdn$10.5 million and Cdn$22.6 million of Distributable Cash and distributed Cdn$10.6 million and Cdn$20.8 million, for a payout ratio of 100.9% and 92.2%, respectively. The Board of Directors monitors the distribution policy of the Company with respect to excess cash, forecasted cash flows, debt levels and spending plans for the long term and may adjust distributions to retain appropriate liquidity for business operations and to meet debt covenant requirements. The Company expects to follow its distribution policy of Cdn$0.80 per EIS unit.

Distributable Cash Summary

(in 000's of US$, except per share data and as otherwise indicated)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Reconciliation of cash flows from operating activities to Distributable Cash:				
Cash provided by operating activities	$ 4,296	$ 12,394	$ 9,499	$ 22,863
Cash interest expense	5,360	4,816	10,232	9,562
Changes in operating assets and liabilities	(2,457)	(5,091)	(5,014)	(6,975)
Accretion of asset retirement obligations	(54)	(50)	(108)	(101)
EBITDA (Note 1)	7,145	12,069	14,609	25,349
Less:				
Interest on credit facility	2,786	2,645	5,544	5,126
Interest on separate subordinated notes	464	464	928	928
Distributable Cash (Note 1)	$ 3,895	$ 8,960	$ 8,137	$ 19,295
Per Common and equivalent Common Share (Note 2)	$ 0.10	$ 0.24	$ 0.22	$ 0.52
Interest on EIS Subordinated Notes	$ 1,944	$ 1,944	$ 3,888	$ 3,888
Distributions on Common Shares	4,131	5,573	9,824	10,908
Distributions on non-controlling Class B preferred interest	380	380	760	762
Distributions on non-controlling Class B common interest	844	1,139	2,008	2,230
Total distributions (Note 3)	$ 7,299	$ 9,036	$ 16,480	$ 17,788
Per Common and equivalent Common Share (Note 2)	$ 0.20	$ 0.24	$ 0.44	$ 0.48
Hedge rate (Cdn$ per US$) (Note 4)	$ 1.1712	$ 1.1684	$ 1.1689	$ 1.1699
Distributable Cash (Cdn$) (Note 1)	$ 4,562	$ 10,469	$ 9,511	$ 22,573
Per Common and equivalent Common Share (Cdn$) (Note 2)	$ 0.12	$ 0.28	$ 0.26	$ 0.61
Excess (shortfall) distributable cash (Cdn$)	$ (3,987)	$ (89)	$ (9,752)	$ 1,763
Per Common and equivalent Common Share (Cdn$) (Note 2)	$ (0.11)	$ (0.00)	$ (0.26)	$ 0.05

Note 1: EBITDA and Distributable Cash are not recognized measures under Canadian GAAP and do not have standardized meanings prescribed by Canadian GAAP. Therefore, EBITDA and Distributable Cash may not be comparable to similar measures presented by other issuers. As the Company intends to distribute substantially all of its cash on an ongoing basis, management believes that EBITDA and Distributable Cash are important measures in evaluating the Company's performance. Distributable Cash is not intended to be representative of cash flow or results of operations determined in accordance with Canadian GAAP.

Note 2: Common and equivalent Common Share computation for Distributable Cash purposes assumes 31,000,000 Common Shares are outstanding for the full period and the conversion of Class B common interests into equivalent Common Shares. For the three months and six month ended June 30, 2007 and 2006, the number of Common and equivalent Common Shares outstanding is 37,265,455.

Note 3: Includes distributions declared, but not distributed in reporting period.

Note 4: Hedge rate is based on weighted average of outstanding hedge contracts in place in each respective period.

Foreign Currency Exchange Contracts

On closing of the Offering, the Company entered into forward contracts to purchase Canadian dollars sufficient to make monthly distributions through September 2010 at the initial distribution level to all EIS holders, including non-controlling investors, as well as interest payments on the Separate Subordinated Notes. Beginning with the May 2007 distribution declaration, the Canadian dollar funding requirement for distributions per EIS was reduced to an annual rate of Cdn$0.80 from Cdn$1.15. The forward contracts for the Separate Subordinated Notes have an exchange rate of Cdn$1.1713 to U.S. $1.00. The remaining forward contracts have an exchange rate of Cdn$1.1712 to U.S. $1.00 and a rate of Cdn$1.0840 to U.S. $1.00. For the three months and six months ended June 30, 2007, the net impact of the change in the foreign exchange rate on the aggregate value of the hedges resulted in an unrealized gain of $9.0 million and $9.5 million, respectively. For the three months and six months ended June 30, 2006, the net impact of the change in the foreign exchange rate on the aggregate value of the hedges resulted in an unrealized gain of $6.9 million and $6.7 million, respectively. At June 30, 2007 and December 31, 2006, the fair value of these contracts, respectively, was a net amount of $11.9 million (of which $3.7 million is recorded in current assets) and $2.4 million (of which $0.3 million is recorded in current assets).

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 on 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. For the three months and six months ended June 30, 2007, the net impact of the exchange in the fair value of the agreements resulted in an unrealized gain of $0.6 million and $0.1 million, respectively. For the three months and six months ended June 30, 2006, the net impact of the exchange in the fair value of the agreements resulted in an unrealized gain of $0.9 million and $1.7 million, respectively. At June 30, 2007 and December 31, 2006, the fair value of these agreements, respectively, was a net amount of $1.0 million (of which $0.5 million is recorded in current assets) and $0.9 million (of which $0.4 million is recorded in current assets).

Commitments and Contractual Obligations

The following table reflects the Company's contractual obligations and commitments related to outstanding indebtedness as of June 30, 2007, including payments due for each of the next five years and thereafter.

Maturities of long-term debt are as follows (in 000's):

	June 30, 2007 Balance	2007	2008	2009	2010	2011	Thereafter
Term Loan Facility	$ 135,000	$ -	$ -	$ 135,000	$ -	$ -	$ -
Subordinated debt	90,107	-	-	-	-	-	90,107
Total	$ 225,107	$ -	$ -	$ 135,000	$ -	$ -	$ 90,107

The Company pays a management fee under the Management Agreement which continues through August 2025. For a more detailed discussion, please see "Transactions with Related Parties".

The Company has no off-balance sheet debt or similar obligations.

Transactions with Related Parties

The Manager is engaged to provide management and administrative services to the Company and its subsidiaries pursuant to the terms of the Management Agreement for which it earns a fixed fee that adjusts annually based on inflation factors. The Manager is also entitled to an incentive fee under the Management Agreement. The incentive fee is designed to align the financial interests of the Manager with those of the Company. The incentive fee for each year will equal 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. The Management Agreement has an initial 20-year term which commenced August 24, 2005.

A detailed description of the principal terms of the Management Agreement is included in the Company's Annual Information Form dated March 8, 2007 and a copy of the Management Agreement is available for review on SEDAR at www.sedar.com.

On November 1, 2006, the Manager was acquired by EPCOR Power L.P. ("EPCOR Power"), a Canadian public company. As a result of the acquisition, all the employees of the Manager were transferred to EPCOR Operations (U.S.) Inc. ("EPCOR Operations"), a wholly owned subsidiary of EPCOR Utilities Inc. and an affiliate of EPCOR Power. EPCOR Operations now provides all management and administrative services to the Manager which continues to act as Manager under the Management Agreement.

In connection with the acquisition of the Manager by EPCOR Power on November 1, 2006, the Company, EPCOR Power, EPCOR Operations, the Manager and Thomas Casten (former Chair and Chief Executive Officer of the Manager) entered into an allocation agreement (the "Allocation Agreement") which allocates among the parties rights to new and certain existing development and acquisition opportunities, where such opportunities have been or will be developed or identified by any of the Manager, EPCOR Operations or Thomas Casten. The principal terms of the Allocation Agreement are summarized in the Company's Annual Information Form dated March 8, 2007 and a copy of the Allocation Agreement is available for review on SEDAR at www.sedar.com.

Critical Accounting Estimates

The preparation of financial statements in conformity with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses in the financial statements. Management bases its estimates on historical experience and other assumptions, which it believes are reasonable. If actual amounts are ultimately different from these estimates, the revisions are included in the Company's results of operations for the period in which the actual amounts become known.

Accounting policies are considered critical when they require management to make assumptions about matters that are highly uncertain at the time the estimate is made and when different estimates than those management reasonably could have made have a material impact on the presentation of the Company's financial condition, changes in financial condition or results of operations. The following is a description of the Company's accounting policies that management believes require subjective and complex judgments, and could potentially have a material effect on reported financial condition and results of operations.

Property, Plant and Equipment

Property, plant and equipment have been adjusted, giving effect to the purchase method of accounting. Depreciation for all asset classes is recorded on a straight-line basis over the estimated useful lives of the assets. Generally, the estimated useful lives are 30 years for buildings, plant and equipment. The estimated useful life of office furniture and equipment is 7 years. Leasehold improvements are amortized over the shorter of the lease term or the estimated useful lives of the assets. Expenditures for maintenance and repairs are charged to income as incurred. The carrying amount for long-lived assets is reviewed whenever events or changes in circumstances indicate that impairment may have occurred.

Intangible Assets
Identifiable intangible assets were fair valued based on valuation techniques for the purpose of applying purchase accounting to the acquisition of PERH on August 24, 2005 and represent contract rights associated with customer contracts and nitrogen oxide allowances. The respective intangible values are amortized over specified time horizons and evaluated for impairment if events or changes in circumstances indicate that the asset might be impaired. Fair value under Canadian GAAP is defined as "the amount of the consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act". Assessing the fair value of intangible assets requires management estimates on future cash flows to be generated by the assets.

Impairment of Long-Lived Assets
Management continually evaluates whether events or circumstances have occurred that indicate that the remaining estimated useful lives of property, buildings and equipment may warrant revision or that the remaining balances may not be recoverable. If this review indicates that the assets will not be recoverable, as determined based on the undiscounted future cash flows from the use of the assets, the carrying value of the assets will be reduced to their estimated fair value.

Asset Retirement Obligations
The fair value of estimated asset retirement obligations is recognized in the consolidated balance sheet when identified and a reasonable estimate of fair value can be made. The asset retirement cost, equal to the estimated fair value of the asset retirement obligation, is capitalized as part of the cost of the related long-lived asset. The fair value of asset retirement obligations depends on the total undiscounted amount of the estimated cash flows required to settle the obligations and the appropriate credit-adjusted risk-free discount rate. The asset retirement costs are amortized over the asset's estimated useful life and included in depreciation expense on the consolidated statement of operations and members' deficit. Increases in the asset retirement obligation resulting from the passage of time are recorded as accretion of asset retirement obligation, and are included in general and administrative expenses in the consolidated statement of operations and shareholders' deficit. Actual expenditures incurred are charged against the accumulated obligation.

Revenue Recognition
Revenue is recorded as services are delivered. Revenue is recorded on the accrual basis and may include estimates for services delivered. Capacity revenue represents the fixed revenue amounts established in the tolling agreements with the Company's customers and is billed on a monthly basis. Energy Service revenue represents the revenue earned based on measurements of services performed and delivered each period. Harbor Coal's Revenue determination is subject to inventory adjustments that are significant and unpredictable. The Company provides estimates for doubtful accounts it deemed necessary based on the aging category and specific knowledge of the customer's ability to pay. No such allowances were recorded at June 30, 2007 and 2006.

Future Income Taxes

The Company utilizes the liability method of accounting for income taxes under which future income tax assets and liabilities are recognized based upon the differences between the tax basis of an asset or liability and its reported amount in the financial statements. Future tax balances are determined by using estimates of future tax rates expected to be in effect when the taxes will actually be paid or refunds received.

Accounting for Derivatives

The Company evaluates derivatives in accordance with Accounting Guideline 13 "Hedging Relationships" ("AcG-13"). For those derivatives that do not qualify for hedge accounting under AcG-13 the derivative instrument is recorded on the balance sheet as either an asset or liability measured at estimated fair value, with changes in fair value recognized currently in earnings.

Risk Factors

The Company's future performance and ability to generate sufficient cash flow to meet its monthly cash distributions to holders of EISs, and the Common Shares and Subordinated Notes represented thereby, involves a number of risks and uncertainties. Any of these risks and uncertainties could have a material adverse effect on results of operations, business prospects, financial condition, the cash available for distribution to holders of EISs, Common Shares, or Subordinated Notes or on the market price or value of EISs, Common Shares or Subordinated Notes. The following is a partial listing of primary risks facing the Company. Additional risks are discussed in the Company's Annual Information Form dated March 8, 2007 and are available for review on SEDAR at www.sedar.com.

The Projects Depend on their Electricity and Thermal Energy Customers

Each Project relies for its revenues on one or more tolling agreement, lease agreement, or other agreement with its host. The amount of cash available for distribution to holders of EISs, Common Shares and Subordinated Notes is highly dependent upon customers under such agreements fulfilling their contractual obligations. There is no assurance that these customers will perform their obligations or make required payments on a timely basis. Each of the Projects is dependent upon its industrial host's continuing operations at those Projects, in that the revenue producing agreements with those hosts do not preclude a complete cessation of operations, whether due to unforeseen circumstances, force majeure or the discretion of the host, which would also cease purchases of thermal or electric energy from the Projects, that would not necessarily result in an actionable breach of the Project's revenue producing contracts. Certain Projects rely on their industrial hosts for waste fuel and derive a significant portion of their revenue based on output rather than strictly on capacity payments; accordingly, these Projects rely on their industrial hosts to maintain industrial operations at a high level. Various conditions which are not within the control of the Company or the Project operators, and may not be within the control of the host industrial companies, may directly or indirectly result in significant reduction or cessation of industrial operations at any given Project, such as competitive pressures, mergers or acquisitions, adverse financial or economic conditions or events (including foreclosure, bankruptcy or liquidation of the industrial company), environmental constraints or incidents, weather conditions, labour actions, fuel shortages, equipment malfunction or refurbishment, accidents or sabotages, mismanagement, governmental action and force majeure. If any of the hosts were to materially curtail or cease manufacturing operations that require energy from a Project, a material portion of the Project's revenues could be interrupted or would cease, and there may be no contractual remedy or insurance coverage sufficient to cover such shortfalls. Moreover, substantial short or long-term changes in industrial operating levels short of material curtailment or cessation of operations can result from management decisions by the industrial hosts. These changes are not predictable, and such changes may produce material volatility in production-based revenues from any of the Projects so affected.

Projects May Not Operate as Planned

The revenue produced by the Projects is dependent, in whole or in part, on the amount of electric energy and thermal energy generated by them. The ability of the Projects to generate the maximum amount of energy to be distributed to hosts is the primary determinant in the amount of cash that will be distributed to the Company, and that will in turn be available for distribution to holders of EISs, Common Shares and Subordinated Notes. With respect to each of the Projects, there is a risk of equipment failure (of both Project equipment and equipment operated by the host) for various reasons including, without limitation, component failures, latent defect, design error, operator error, weather conditions or force majeure which could adversely affect revenues and cash available for distribution. To the extent that such equipment requires either longer than anticipated down times or unexpected capital requirements for maintenance and repair, or suffers disruptions of energy generation for other reasons, the amount of cash available for distribution may be adversely affected.

PERH through its subsidiaries does not control, nor does it have contractual rights in respect of, the operations of its customers. The host steel mills have the ability to run their plants at their discretion. Due to the fact that some of the Projects are affected by the level of production at these facilities, such Projects' performance may be impacted by the hosts' operational decisions. Such operational decisions include production levels and which blast furnaces the host steel mills choose to run.

The Company has Limited Control Over the Harbor Coal Project

The Projects are wholly-owned, indirectly, by the Company, with the exception of the Harbor Coal Project. Harbor Coal LLC, an indirect subsidiary of PERH, owns a 50% general partnership interest in PCI Associates which in turn owns the Harbor Coal Project. Harbor Coal LLC has limited control over the operation of the Harbor Coal Project. III/PCI, Inc., the other general partner of PCI Associates and an affiliate of Ispat Inland Inc., manages the operations of the Harbor Coal Project. Ispat Inland Inc. is an indirect subsidiary of Mittal Steel.

PERH's limited control results in a number of risks at the Harbor Coal Project. These include commodity costs such as coke, coal, natural gas, oil and oxygen costs, which can vary with market conditions; Mittal Steel determines which commodity mix is used on a daily basis. Furthermore, Mittal Steel determines the amount of hot metal produced per day for use in steel production. These factors determine the profitability of the Harbor Coal Project. PERH must also rely on the technical and management expertise of III/PCI, Inc. to oversee operations and maintenance of the Project. PERH is also reliant on accounting policies, procedures and financial reporting of Mittal Steel as they impact the accounting and financial reporting of PCI Associates. To the extent that III/PCI, Inc. does not fulfill its obligation to manage the operations of the Harbor Coal Project, or is not effective in doing so, the amount of cash available for distribution may be adversely affected.

Future Distributions are not Guaranteed

The Company only source of cash flow for payment of dividends on its Common Shares and interest on its Subordinated Notes, respectively, is distributions on its membership interest in PERH. While the Company is contractually obligated to make interest payments on the Subordinated Notes, the Company's board of directors or PERH board of managers may, in their respective discretion, amend or repeal the existing distribution policy relating to equity distributions. Future equity distributions from these companies, if any, will depend on, among other things, the results of operations, cash requirements, financial condition, contractual restrictions, business opportunities, provisions of applicable law and other factors that the board of directors or managers may deem relevant. Either of these boards of directors or managers may decrease the level of equity distributions provided for in their existing distribution policies or entirely discontinue such distributions. The Indenture and the Credit Facility contain significant restrictions on the ability to make distributions, including if the Company defers interest on the Subordinated Notes under the Indenture, restrictions on the payment of dividends until the Company has paid all deferred interest, together with accrued interest thereon.

In addition, the Company's after-tax cash flow available for distributions and interest payments would be reduced if the Subordinated Notes were treated as equity rather than debt for U.S. federal income tax purposes. In that event, the stated interest on the Subordinated Notes could be treated as a dividend and would not be deductible by the Issuer for U.S. federal income tax purposes. The inability to deduct interest on the Subordinated Notes could materially increase the Company's taxable income and, thus, the Company's U.S. federal and applicable state income tax liability. If this were to occur, the Company's after-tax cash flow available for distributions and interest payments may be reduced. The additional tax due to federal and state authorities in that event could adversely affect the Company's financial position, cash flows and liquidity, and could also adversely affect its ability to continue as a going concern. In addition, non-U.S. holders of the EISs could be subject to withholding taxes on the payment treated as dividends on equity, which could subject the Company to additional liability for the withholding taxes that it did not collect on such payments.

Restrictive Covenants in the Credit Facility Could Impact the Business of the Issuer and Primary Energy

The Credit Facility and the Indenture contain restrictive covenants that limit the discretion of the Company or Primary Energy Operations, LLC ("PEO"), as the case may be, to among other things,

- incur additional indebtedness;
- make distributions in respect of the EISs or membership interests, as the case may be, or to make certain other restrictive payments or investments;
- sell assets;
- consolidate, merge, sell or otherwise dispose of all or substantially all of their assets;
- enter into transactions with affiliates;
- create liens; and
- enter into new lines of businesses.

In addition, the Credit Facility includes other and more restrictive covenants and prohibits PEO and certain of its affiliates from prepaying its other indebtedness, including the Company prepaying the Subordinate Notes, while debt under the Credit Facility is outstanding. The agreement governing the Credit Facility also requires PEO to achieve specified financial and operating results and maintain compliance with specified financial ratios. PEO's ability to comply with these ratios may be affected by events beyond its control.

A breach of any of the restrictive covenants in the Credit Facility or in PEO's ability to comply with the required financial ratios could result in a default under the Credit Facility. If a default occurs, the lenders under the Credit Facility may elect to declare all borrowings outstanding under that facility together with accrued interest and other fees, to be immediately due and payable which would result in an event of default under the Indenture.

See the Company's Annual Information Form dated March 8, 2007, which can be found on SEDAR at www.sedar.com, for a full description of all of the Company's risk factors, which factors are incorporated by reference herein.

Recent Accounting Pronouncements
The Canadian Accounting Standards Board has recently issued new Handbook sections:

- 1530, Comprehensive Income;
- 3855, Financial Instruments – Recognition and Measurement; and
- 3865, Hedges.

Under these new standards, all financial assets should be measured at fair value with the exception of loans, receivables and investments that are intended to be held to maturity and certain equity investments, which should be measured at cost. Similarly, all financial liabilities should be measured at fair value when they are held for trading or they are derivatives. Gains and losses on financial instruments measured at fair value will be recognized in the income statement in the periods they arise with the exception of gains and losses arising from:

- Financial assets held for sale, for which unrealized gains and losses are deferred in other comprehensive income until sold or impaired; and
- Certain financial instruments that qualify for hedge accounting.

Sections 3855 and 3865 reference "other comprehensive income". Other comprehensive income comprises revenues, expenses, gains and losses that are excluded from net income. Unrealized gains and losses on qualifying hedging instruments, foreign currency, and unrealized gains or losses on financial instruments held for sale will be included in other comprehensive income and reclassified to net income when realized. Comprehensive income and its components will be required disclosure under the new standard.

The adoption of these standards as of January 1, 2007 did not have a material impact on the Company's consolidated financial statements.

Capital Disclosures
In December 2006, the CICA released new Handbook Section 1535, Capital Disclosures, effective for interim and annual financial statements beginning on or after October 1, 2007. Section 1535 establishes standards for disclosing information about an entity's capital and how it is managed. It requires the disclosure of information about an entity's objectives, policies and processes for managing capital. The Company does not expect adoption of Section 1535 to have a material impact on its consolidated financial statements.

Financial Instruments – Disclosures and Presentation

In December 2006, the CICA released new Handbook Section 3862, Financial Instruments – Disclosures and Handbook Section 3863, Financial Instruments – Presentations effective for interim and annual financial statements beginning on or after October 1, 2007. Section 3862 requires entities to provide disclosures in their financial statements that enable users to evaluate the significance of financial instruments on the entity's financial position and its performance and the nature and extent of risks arising from financial instruments to which the entity is exposed during the period and at the balance sheet date, and how the entity manages those risks. Section 3863 establishes standards for presentation of financial instruments and non-financial derivatives. It deals with the classification of financial instruments, from the perspective of the issuer, between liabilities and equities, the classification of related interest, dividends, losses and gains, and circumstances in which financial assets and financial liabilities are offset. The Company does not expect adoption of Section 3862 and Section 3863 to have a material impact on its consolidated financial statements.

Accounting Changes

CICA Handbook Section 1506: Accounting Changes ("CICA 1506") effective for fiscal years beginning on or after January 1, 2007 establishes standards and new disclosure requirements for the reporting of changes in accounting policies and estimates and the reporting of error corrections. CICA 1506 clarifies that a change in accounting policy can be made only if it is a requirement under Canadian GAAP or if it provides reliable and more relevant financial statement information. Voluntary changes in accounting policies require retrospective application of prior period financial statements, unless the retrospective effects of the changes are impracticable to determine, in which case the retrospective application may be limited to the assets and liabilities of the earliest period practicable, with a corresponding adjustment made to opening retained earnings. At this time, we are not aware of any pending accounting changes other than those mandated by the CICA. Adoption of this standard did not have a material impact on the Company's interim consolidated financial statements for the three months and six months ended June 30, 2007.

Internal Control over Financial Reporting

Internal control over financial reporting, designed by management, has the objective to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP. No changes to the Company's internal control over financial reporting have occurred during the six months ended June 30, 2007, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Additional Information

Additional information relating to the Company, including the unaudited interim consolidated financial statements for the three months and six months ended June 30, 2007 and 2006 and the Company's Annual Information Form dated March 8, 2007, is available on SEDAR at www.sedar.com.