



# Q2

**Quarterly report for  
the period ended  
June 30, 2003**

## **KeySpan Facilities Income Fund (TSX:KEY.UN) Announces Second Quarter Results and August Distribution**

### ***Message to Unitholders***

We are pleased to provide you with our 2003 second quarter report on KeySpan Facilities Income Fund's activities as well as announce a cash distribution for August, 2003 of 9.08 cents per unit. The distribution will be payable on September 15, 2003 to unitholders of record on August 29, 2003. The ex-distribution date is August 27, 2003.

This is our first report to Unitholders since the Fund became a publicly traded entity on May 30, 2003. On May 30, 2003 the Fund closed its Initial Public Offering, raising total proceeds of \$170 million, including the underwriter's over-allotment option exercised on June 10, 2003. The trust units were priced at \$10.00 per unit, with an initial cash on cash yield of 10.9%. The Fund used the proceeds from the IPO to acquire a 39.1% interest in KeySpan Energy Canada Partnership.

**This report includes separate financial statements for the Partnership, which encompasses all of the business of KeySpan, and for the Fund, which represents a 39.1% ownership interest in the Partnership. Except where noted, the Highlights and the Business Review sections describe the business of KeySpan Energy Canada Partnership.**

Results for the quarter and year to date are significantly better than 2002. We continue to see considerable exploration and development activity within the capture areas around our plants. Drilling activity is on track to exceed 2001 and 2002 levels, indicating that producers are continuing to drill the deeper multi-zone geology in western Alberta around many of our facilities. We continue to work with producers on a variety of business initiatives to leverage our assets and create additional value. Our marketing business has delivered strong financial performance this year driven by our strategic NGL infrastructure and stronger market conditions.

We have declared distributions to date that are consistent with our expectations and are on track to deliver continued strong cash flow from operations. Standard and Poors has assigned an SR-3 stability rating, indicating the expectation of a high level of stability in distributions.

On behalf of the Fund's trustees, directors and management team, I look forward to your continued support.

Jim V. Bertram  
President and CEO  
KeySpan Facilities Income Fund

## Unit Trading Summary to June 30th

	TSX:KEY.UN - Cdn\$
High	\$11.50
Low	\$10.40
Close	\$11.15
Volume	5,817,713

## Highlights

- Successful completion of Initial Public Offering of 17,000,000 units at \$10.00 to raise gross proceeds of \$170 million.
- Net Income of \$9.5 million in the second quarter (\$2.3 million in 2002) was significantly higher than 2002 with strong contribution from both facilities and marketing.
- June Distributions to Unitholders of \$0.0908 per unit on track with expectations.
- Significant exploration and production activity around strategic plants.
- Gathering and processing activities focused on continued connection of natural gas production, completion of new projects and scheduled maintenance at certain processing facilities.
- Arranged \$125 million of long term debt in July 2003 to repay short term debt, reduce refinancing risk and take advantage of low interest levels.

## Business Review

In the second quarter KeySpan posted strong results, with net income of \$9.5 million for the second quarter compared to \$2.3 million in 2002. Year to date net income of \$22.2 million was \$10.7 million higher than for the same period last year. The following table shows the contribution to net income from the facilities and marketing businesses.

\$ millions	Three months ended		Six months ended	
	June 30, 2003	June 30, 2002	June 30, 2003	June 30, 2002
Facilities contribution <sup>1</sup>	12.3	10.2	25.6	22.0
Marketing contribution <sup>2</sup>	3.7	(1.1)	11.7	3.3
<b>Total contribution</b>	<b>16.0</b>	<b>9.1</b>	<b>37.3</b>	<b>25.3</b>
Depreciation and amortization	(5.0)	(4.5)	(10.1)	(8.8)
Corporate general, administrative and other <sup>3</sup>	(0.6)	(2.2)	(4.1)	(4.7)
Site restoration and abandonment	(0.1)	(0.1)	(0.2)	(0.2)
Interest	(0.6)	-	(0.6)	-
Income tax	(0.2)	-	(0.2)	-
<b>Net Income</b>	<b>9.5</b>	<b>2.3</b>	<b>22.2</b>	<b>11.5</b>

Notes to the table:

Facilities contribution and Marketing contribution, as defined below, are used by the Partnership to evaluate operating performance and are not standard measures under Canadian generally accepted accounting principles. Therefore, these measures may not be comparable with the calculation of similar measures for other companies.

1. Facilities contribution includes revenues for processing and storage services provided to KeySpan's marketing business
2. Marketing contribution includes expenses for processing and storage services provided by KeySpan's facilities and direct marketing general and administrative costs.
3. Corporate general, administrative and other costs exclude the direct marketing general and administrative costs.

## **Facilities**

Facilities contribution was \$12.3 million for the second quarter of 2003, compared to \$10.2 million in 2002. Included in the facilities contribution is an electricity hedge, the proceeds/(loss) of which accrue to KeySpan Energy Development Co. Excluding the electricity hedge losses (\$0.6 and \$0.8 million for the second quarters of 2003 and 2002 respectively), facilities contribution was \$12.9 million for the second quarter, compared to \$11.0 million in 2002, an increase of 17%. Year to date, facilities contribution excluding the electricity hedge losses (\$0.7 million - 2003 and \$2.1 million – 2002) was \$26.3 million compared to \$24.1 million in 2002, 9% higher than 2002.

The primary reason for this increase was an increase in gross plant throughput. Plant throughput volumes increased 4% in the quarter and 2% year to date compared to 2002.

### ***Gathering and Processing***

In keeping with KeySpan's objectives of expanding its value chain and leveraging its existing asset base, a number of small capital projects were undertaken in the second quarter. Natural gas liquids (NGL) truck loading facilities were commissioned at both the Strachan and Paddle River gas plants. NGLs from these facilities are now being trucked to KeySpan's Rimbey gas plant and Fort Saskatchewan facilities for NGL processing into spec products. An NGL truck offloading facility was constructed at the Rimbey plant to receive these NGL volumes. A letter of intent was completed in May to acquire a pipeline to gather gas for processing at the Strachan gas plant. Closing is expected to be in August. This line will allow KeySpan to access gas produced from a new area where significant drilling has occurred over the past six months. Construction of facilities began in June at Easyford, providing capacity for processing shut-in sour solution gas volumes at the Bigoray gas plant. Active drilling in this area will provide additional gas volumes by year end.

Work is underway to construct a CO<sub>2</sub> liquification facility at the Rimbey gas plant. This \$9 million project (KeySpan 49.9%) is expected to be completed by the end of the first quarter, 2004 and will utilize Rimbey's existing infrastructure to supply liquid CO<sub>2</sub> to industrial markets in Alberta. A propane condenser was installed at the Nordegg gas plant to increase propane and butane recoveries, particularly in the summer months.

Minor maintenance was done at the Nordegg plant in April to change catalyst and overhaul a compressor. The Brazeau plant completed a full plant turnaround in May. Processing interruption was minimized during the Brazeau turnaround by diverting gas to other KeySpan plants through KeySpan pipelines, benefiting both KeySpan and its customers.

### ***NGL Facilities***

NGL processing volumes increased in the second quarter at both KeySpan operated and partner operated facilities as both KeySpan and third party processing demand increased. The Rimbey plant benefited from volumes being trucked in from the Strachan gas plant. Offsetting the higher revenues at these facilities was higher natural gas fuel costs.

Pipeline volumes on Rimbey Pipe Line Co. Ltd. achieved a record high in the second quarter, driven by higher NGL volumes from the Rimbey plant as well as other plants in the area, which resulted in increased equity earnings in the period.

## **Marketing**

Marketing posted strong second quarter and year to date results. Second quarter marketing contribution was \$3.7 million for the second quarter, compared to a \$1.1 million loss in 2002. Included in the marketing contribution are proceeds from a terminated gas marketing services contract, the proceeds of which accrue to KeySpan Energy Development Co. Excluding these proceeds (\$1.2 and \$0.3 million for the second quarters of 2003 and 2002 respectively), marketing contribution was \$2.5 million compared to a \$1.4 million loss in 2002,

an increase of \$3.9 million. Year to date marketing contribution, excluding these proceeds (\$2.1 million - 2003 and \$0.5 million – 2002), was \$9.6 million compared to \$2.8 million in 2002, an increase of \$6.8 million.

The strong performance was due to strong butane and condensate prices in the first half of the year, the benefit of the acquisition of the Dow operated fractionation facilities at Fort Saskatchewan in April 2003 and slightly higher sales volumes compared to year to date 2002.

### **Distributions to Unitholders**

Distributions to Unitholders of \$0.0908 per unit for June, 2003 were consistent with expectations and the subsequent announcements of the July and August distributions continue that trend. The Fund is focused on ensuring stable long term distributions that grow over time. Although there is a certain seasonality to the business that will cause some variability in the financial results over the year, the Fund expects to use its working capital and bank facilities to stabilize monthly distributions.

### **Taxability of 2003 Distributions**

The Fund expects that the 2003 distributions will be fully tax deferred. Unitholders should seek independent tax advice in respect of the consequences to them of acquiring, holding and disposing of Units.

### **Debt Refinancing**

In late July, KeySpan agreed to terms for the issue of \$125 million of long term notes, through a private placement to investors in the U.S. and Canada. The transaction is expected to close in late August and proceeds will be used to repay short term debt. Refinancing of the current short term bank facilities will better match the term of the debt with the longevity of KeySpan's asset portfolio and reduce refinancing risk. Of the total amount, \$20 million will have a five year term, \$52.5 million will have a seven year term and \$52.5 million will have a ten year term. The weighted average interest rate will be 5.9%, payable monthly. By structuring the debt in three terms, KeySpan has mitigated the refinancing risk.

### **Corporate Governance**

KeySpan's Board of Directors is committed to strong corporate governance. The Board has established subcommittees with responsibilities for Health, Safety and Environment, Compensation and Governance and Audit. Each sub committee chairperson is an independent director and terms of reference of each committee have been established.

## ***Management Discussion and Analysis***

The following discussion and analysis as provided by Management should be read in conjunction with the accompanying unaudited consolidated financial statements of KeySpan Facilities Income Fund (the "Fund") and KeySpan Energy Canada Partnership (the "Partnership" or "KeySpan") for the quarter ended June 30, 2003 and the notes thereto as well as the audited financial statements of the Fund and the Partnership and the related management discussion and analysis contained in the Fund's May 22, 2003 Prospectus.

The Fund began operations on May 30, 2003 acquiring a 34.5% indirect interest in the Partnership, and later an additional 4.6% indirect interest. The Partnership acquired KeySpan Energy Facilities Limited and KeySpan Energy Canada Inc. on May 30, 2003. Accordingly, the Statement of Operations contained in the Consolidated Financial Statements of the Partnership presents the results of operations of the Partnership for the full second quarter, April 1, 2003 to June 30, 2003 and the results of operations of these subsidiaries from the time of acquisition, May 30, 2003, to June 30, 2003. The information presented by the Partnership for the comparative periods of 2002 represents only the results of operations for the Partnership. Accordingly, some of the variances described in this report include the effect of these acquisitions.

Distributable Cash Flow as defined in the Partnership Agreement and described in Note 3 of the June 30, 2003 Partnership Interim Consolidated Financial Statements is not a standard measure under Canadian generally accepted accounting principles and therefore may not be comparable with the calculation of similar measures for other companies.

## **KEYSPAN FACILITIES INCOME FUND**

### **Results of Operations**

The Fund reported net earnings of \$1.4 million or 7.97¢ per Trust Unit for the quarter ended June 30, 2003 based upon 17,000,000 units outstanding at that date. The earnings were attributable to the Fund's 39.1% interest in the consolidated earnings of KeySpan Energy Canada Partnership from May 30, 2003 to June 30, 2003.

### **Liquidity and Capital Resources**

The Fund was established on April 3, 2003 and commenced operations on May 30, 2003. Subsequently, the Fund issued 17,000,000 Trust Units for net proceeds of \$158,225,000 after transaction fees. The proceeds were used to acquire a 39.1% interest in KeySpan Energy Canada Partnership and its managing partner, KeySpan Canada Management Ltd.

The Fund does not actively operate a business and is dependent upon distributions from its subsidiaries for earnings. Since commencing operation, the Fund has recorded \$1.5 million of distributions receivable and declared a distribution payable to Unitholders of \$1.5 million.

At June 30, 2003, the Fund has no cash from operations, no cash on hand and no external debt.

## **KEYSPAN ENERGY CANADA PARTNERSHIP**

### **Results of Operations**

For the three months ended June 30, 2003, the Partnership reported net income of \$9.5 million compared to \$2.3 million during the same period last year. On a year to date basis, net income for 2003 is \$22.2 million compared to \$11.5 million in 2002. The increase in Net Income earned during the quarter and on a year to date basis was due primarily to the stronger performance of the NGL marketing business during 2003.

For the three months ended June 30, 2003, operating margin<sup>1</sup>, which is defined as operating revenues minus operating expenses, was comprised of \$11.5 million related to the operation of plants and pipelines and \$5.0 million related to the marketing of natural gas and natural gas products compared to \$10.1 and a loss of \$0.4 million respectively for the same period last year. The operating margin from plant and pipeline activities represents approximately 69% of the operating margin for the second quarter of 2003.

Year to date, the operating margin was comprised of \$24.5 million related to the operation of plants and pipelines and \$14.0 million related to the marketing of natural gas and natural gas products compared to \$21.4 and \$5.1 million respectively for the same period last year. The operating margin from plant and pipeline activities represents approximately 63% of the operating margin for the year. The proportion of plant and pipeline operating margin is less than historical norms due to the strong performance of the NGL marketing business during the first half of the year.

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<sup>1</sup> Operating margin is not a standard measure under Canadian generally accepted accounting principles and therefore may not be comparable with the calculation of similar measures for other companies.

## Facilities

The operating margin generated from gathering, processing and pipeline activities is not significantly exposed to changes in operating costs as much of the revenue stream is generated on a cost of service basis. This fee arrangement provides a mechanism for the recovery of operating costs plus a return on capital.

For the three months ended June 30, 2003, operating margin generated from plant and pipeline facilities was \$11.5 million, up \$1.5 million from the same period last year. This increase was primarily attributable to the Foothills Region. Higher throughput volumes at the Strachan plant and higher fees for acid gas injection services at the Brazeau plant contributed to the increase. Operating margin from the other regions showed modest growth.

Year to date, operating margin generated from plant and pipeline facilities was \$24.5 million compared to \$21.4 million last year, due to lower payments on electricity hedge contracts as well as higher throughput volumes and higher fees for acid gas injection services in the Foothills Region.

In order to fix the price of electricity consumed at its plants and facilities until December 31, 2003, KeySpan entered into financial price swap contracts to purchase electricity at an average price of \$88.06 per Megawatt hour. As electricity commodity prices fluctuate this hedge can post gains or losses. The combination of the potential volatility of the hedge and its short remaining life resulted in a decision, at the time the Fund was created, to not include its proceeds(losses) in distributions to the Fund. Accordingly, subsequent to May 30, 2003, Keyspan Energy Development Co. ("KEDCO"), a subsidiary of KeySpan Corporation, assumed responsibility for all payments by and to the Partnership under these hedging agreements. As a result, distributions to KEDCO for the month of June 2003 were reduced by \$0.2 million.

During the second quarter of 2003, Keyspan paid \$639,000 pursuant to these contracts, compared to \$763,000 in the second quarter of 2002. Year to date in 2003, KeySpan paid \$702,000 pursuant to these contracts compared to \$1.7 million in the first six months of 2002.

At June 30, 2003, the fair value of the contacts was a loss of \$0.9 million and the notional volume remaining was 35,328 Megawatt hours. The fair value of these contracts represents an estimate of the amount that KeySpan would pay or receive if those contracts were closed on June 30, 2003.

## Marketing

Due to the seasonality of demand for NGLs, the second quarter marketing results can have variability from year to year. For the three months ended June 30, 2003, operating margin from marketing activities was \$5.0 million compared to a loss of \$0.4 million during the same period last year. The increase was primarily attributable to the NGL marketing business where strong prices on term butane contracts contributed to improved margins. NGL sales volumes for the quarter averaged approximately 30,000 barrels per day compared to 31,900 barrels per day during the same period last year.

The marketing results for the second quarter of 2003 also contained \$1.2 million of fees related to the termination of a gas marketing services contract compared to \$0.3 million during the same period last year. Proceeds from this contract expire on November 30, 2003 and, given the short remaining life, a decision was made, at the time the Fund was created, to not include its proceeds in distributions to the Fund. Accordingly, subsequent to May 30, 2003, KEDCO assumed responsibility for all fees to the Partnership under this contract. As a result, distributions to KEDCO for the month of June 2003 were increased by \$0.3 million.

On a year to date basis, operating margin of \$14.0 million was up significantly from the \$5.1 million generated during the first six months of last year. In addition to the favourable second quarter variance discussed above, strong North American demand for propane in the first quarter contributed to sound margins on sales from inventory. NGL sales volumes for 2003 are approximately 35,400 barrels per day compared to 34,300 barrels per day in 2002. The marketing results for the first six months of 2003 also contain \$2.1 million of fees related

to the termination of the gas marketing services contract described above, compared to \$0.5 million during the same period last year.

### **Non-Operating Expenses**

Non-operating expenses during the second quarter of 2003 were \$7.2 million, a decrease of \$0.3 million over the second quarter of 2002. Year to date, non-operating expenses were \$16.4, up \$1.3 million from 2002.

For the three months ended June 30, 2003, depreciation and amortization expense of \$5.0 million increased \$0.5 million compared to the same period last year. Year to date depreciation and amortization expense of \$10.1 million increased \$1.2 million compared to last year. These increases were due primarily to the acquisition of the interest in the Paddle River plant that was previously held by an affiliated company.

For the three months ended June 30, 2003 general and administrative expenses of \$1.6 million decreased \$1.2 million compared to the same period last year, due primarily to the timing of overhead recoveries and lower incentive compensation accruals. Year to date, general and administrative expenses of \$5.7 million are down \$0.3 million.

### **Liquidity and Capital Resources**

During the three months ended June 30, 2003, cash provided by operating activities was \$45.6 million compared to the use of \$5.2 million in the same period last year. Year to date, cash provided by operating activities was \$77.3 million compared to the use of \$10.5 million in the same period last year. These increases were due primarily to the increase in earnings for each period and the receipt of funds due from related parties. Working capital at the end of the quarter was a deficit of \$79.3 million, compared to a surplus of \$88.3 million at December 31, 2002. Cash on hand was \$5.6 million at June 30, 2003 compared to \$4.8 million at December 31, 2002.

The working capital deficit was a result of the establishment of temporary revolving and short term bank credit facilities that provide for borrowings up to CAD\$100 million and US\$50 million. The Partnership also entered into a short term borrowing agreement with KEDCO. Borrowings under these facilities at June 30, 2003 were \$68 million from the short term bank credit facility and \$57 million from KEDCO.

Cash of \$4.8 million was required during the three months ended June 30, 2003 for additions to property, plant and equipment, compared to \$2.9 million in the same period last year. Year to date expenditures on additions to property, plant and equipment in 2003 were \$5.4 million, primarily for the acquisition of an interest in fractionation facilities, leasehold improvements and maintenance capital projects, compared to \$4.2 million during the same period last year.

During the quarter ended June 30, 2003 the Partnership received \$125.0 million of proceeds from the short term credit facilities described above, repaid \$31.4 million of loans to a related party, paid \$164.4 million in distributions pursuant to the structuring transactions that preceded the sale of 39.1% of the Partnership to the Fund, and declared \$4.0 million of distributions to partners subsequent to the sale.

The Partnership expects to complete a long term debt issue in the third quarter of 2003. The proceeds of the issue, approximately \$125 million, will be used to repay the outstanding short term borrowings.

### **Commitments**

The Partnership has lease commitments relating to railway tank cars, vehicles, computer hardware, office space and transportation agreements. At June 30, 2003 the estimated future cash payments total \$18.4 million. They are described in Note 9 of the Notes to the June 30, 2003 Interim Consolidated Financial Statements of the Partnership.

## **Distributable Cash Flow**

The Partnership pays distributions to Partners on a monthly basis from its Distributable Cash Flow, as defined in the Partnership Agreement. Distributable Cash Flow for each month will generally be all of its cash flow from operations for such month, including dividends received from subsidiaries, after satisfaction of its debt service obligations (principal and interest), reclamation expenditures, maintenance capital expenditures, other expense obligations and reasonable reserves for working capital and capital expenditures as may be considered appropriate by the board of directors of the Managing Partner.

The share of Distributable Cash Flow paid to KEDCO is adjusted to include 100% of the net receipts (or payments) of certain contracts. For the month of June 2003, the Partnership's Distribution to Partners was \$4.0 million, including the \$60,000 distribution to KEDCO for the net receipts of the specified contracts.

## **Forward Looking Statements**

This disclosure contains certain forward looking statements that involve significant known and unknown risks and uncertainties. A number of factors could cause actual results to differ materially from the results discussed in the forward looking statements, including risks associated with the general economic, market and business conditions, competition, environmental and other regulatory change, interest rates, the results of exploration and development drilling and related activity, actions by governmental authorities including decisions or approvals of administrative tribunals, the availability of capital markets, reliance on key personnel, uninsured or underinsured losses and activity in the natural gas industry and other factors, many of which are beyond the control of the Fund and KeySpan. No assurances can be given that actual results will be consistent with these forward looking statements.

## **Second Quarter Results Conference Call and Webcast**

KeySpan will be conducting a conference call and webcast for investors, analysts, brokers and media representatives to discuss the second quarter 2003 results at 8:00 am MDT (10 am EDT) on Thursday, August 21, 2003. Callers may participate by either dialling 800-814-4853 or 416-640-4127. A recording of the call will be available for replay until midnight, August 28, 2003 by dialling 877-289-8525 or 416-640-1917 and entering passcode 21014996 followed by the pound key.

Internet users can listen to the call live on KeySpan's website at [www.keyspancanada.com](http://www.keyspancanada.com) under Investor Information, Webcasts. Shortly after the call, a recording of the webcast will be placed on the website for replay.

## **Questions**

KeySpan welcomes questions from interested parties. Calls should be directed to Investor Relations at 403-205-7670, or toll free at 888-699-4853. Information on KeySpan can also be found on our website at [www.keyspancanada.com](http://www.keyspancanada.com).

## KeySpan Facilities Income Fund

### INTERIM CONSOLIDATED STATEMENT OF FINANCIAL POSITION

(all amounts expressed in Canadian dollars)

As at

	June 30, 2003 \$ (unaudited)	April 3, 2003 \$
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and cash equivalents	—	10
Distributions receivable	1,543,600	—
	1,543,600	10
Investment in KeySpan Energy Canada Partnership [note 3]	158,028,662	—
Investment in KeySpan Canada Management Ltd. [note 3]	7,957	—
	159,580,219	10
<b>LIABILITIES AND UNITHOLDERS' EQUITY</b>		
<b>Current liabilities</b>		
Distributions payable	1,543,600	—
	1,543,600	—
Unitholders' equity [note 4]	158,036,619	10
	159,036,619	10
	159,580,219	10

See accompanying notes to the interim consolidated financial statements

## Keyspan Facilities Income Fund

### INTERIM CONSOLIDATED STATEMENT OF NET EARNINGS AND UNITHOLDERS' EQUITY

(all amounts expressed Canadian dollars)  
(unaudited)

April 3, 2003 to  
June 30, 2003  
\$

<b>Revenues</b>	
Equity earnings from KeySpan Energy Canada Partnership and KeySpan Canada Management Ltd. <i>[note 2(d)]</i>	1,355,219
	<u>1,355,219</u>
<b>Expenses</b>	
Management and administrative	—
	<u>—</u>
<b>Net earnings</b>	<u>1,355,219</u>
<hr/>	
Number of Trust Units outstanding at the end of the period	17,000,000
Net earnings per Trust Unit outstanding at the end of the period	0.0797
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Weighted average number of Trust Units outstanding	5,738,636
Net earnings per weighed average Trust Unit	<u>0.2362</u>

### Consolidated Statement of Unitholders' Equity

<b>Unitholders' equity, beginning of period</b>	10
Net earnings	1,355,219
Units issued, net of transaction fees <i>[note 4]</i>	158,225,000
Units cancelled	(10)
Distributions	(1,543,600)
<b>Unitholders' equity, end of period</b>	<u>158,036,619</u>

Distributions to Unitholders and Distributions per Trust Unit – See Note 7

*See accompanying notes to the interim consolidated financial statements*

## KeySpan Facilities Income Fund

### INTERIM CONSOLIDATED STATEMENT OF CASH FLOWS

(all amounts expressed in Canadian dollars)  
(unaudited)

Inception to

	June 30, 2003 \$
<b>OPERATING ACTIVITIES</b>	
Net earnings	1,355,219
Items not requiring cash:	
Equity earnings from KeySpan Energy Canada Partnership and KeySpan Canada Management Ltd.	(1,355,219)
Distributions received from KeySpan Energy Canada Partnership	—
Changes in non-cash working capital	—
Cash provided by operating activities	—
<b>INVESTING ACTIVITIES</b>	
Acquisition of interest in KeySpan Energy Canada Partnership	(158,217,111)
Acquisition of interest in KeySpan Canada Management Ltd.	(7,889)
Cash used in investing activities	(158,225,000)
<b>FINANCING ACTIVITIES</b>	
Issuance of Trust Units, net of transaction fees <i>[note 4]</i>	158,225,000
Cancellation of Trust Unit	(10)
Distributions paid	—
Cash provided by financing activities	158,224,990
<b>Decrease in cash and cash equivalents</b>	<b>(10)</b>
<b>Cash and cash equivalents, beginning of period</b>	<b>10</b>
<b>Cash and cash equivalents, end of period</b>	<b>—</b>

*See accompanying notes to the interim consolidated financial statements*

## KeySpan Facilities Income Fund

### NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

As at June 30, 2003 and for the period from April 3, 2003 (date of inception) to June 30, 2003  
(all amounts expressed in Canadian dollars)  
(unaudited)

#### 1. STRUCTURE OF THE FUND

KeySpan Facilities Income Fund (the "Fund") is an unincorporated open-ended trust established under the laws of the Province of Alberta pursuant to the Fund Declaration of Trust dated April 3, 2003. The Fund indirectly owns a 39.1% interest in KeySpan Energy Canada Partnership ("KECP").

The Fund commenced operations on May 30, 2003, with the initial acquisition of a 34.5% interest in KECP. The acquisition of the Fund's indirect interest in KECP has been accounted for based on the Fund's cost (see note 3).

KECP is involved in the business of gathering, processing, transporting, buying and selling petroleum, natural gas, natural gas liquids and related products, electricity and thermal energy and other related businesses.

KECP is managed by KeySpan Canada Management Ltd. (the "Managing Partner" or "KCML").

The Fund makes monthly cash distributions to Unitholders of record on the last business day of each month. The amount of the distributions per Trust Unit are equal to the pro rata share of the distribution received from KECP and, in the event of the termination of the Fund, participating pro rata in the net assets remaining after satisfaction of all liabilities.

#### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

These consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles. The Partnership's significant accounting policies are as follows:

##### (a) Basis of consolidation

The consolidated financial statements include the accounts of the Fund and all controlled entities. All interfund and intercompany transactions are eliminated.

## KeySpan Facilities Income Fund

### NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

As at June 30, 2003 and for the period from April 3, 2003 (date of inception) to June 30, 2003  
(all amounts expressed in Canadian dollars)  
(unaudited)

#### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

##### (b) Measurement uncertainty

The preparation of consolidated financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. These include the recoverability of the investments, which depend on estimates of future cash flows from related investments. The recognized amounts of such items are based on management's best information and judgment.

##### (c) Cash and cash equivalents

Cash and cash equivalents presented in the consolidated financial statements include short-term investments with a maturity of three months or less when purchased.

##### (d) Investments

The Fund's 39.1% interest in KECP is accounted for using the equity basis of accounting whereby the cost of the investment is increased or decreased for net earnings or losses and reduced by cash distributions paid to the Fund.

The Fund has a 39.1% interest in KCML, the managing partner of KECP. This investment is accounted for using the equity basis of accounting whereby the cost of the investment is increased or decreased for net earnings or losses and reduced by cash distributions paid to the Fund.

The Fund reviews and evaluates the carrying value of its investments for impairment annually. More frequent reviews are conducted as conditions necessitate. In the event a decrease in the value of an investment is other than a temporary decline, the investment will be written down to recognize any impairment in the carrying value.

##### (e) Financial instruments

The carrying value of the Fund's financial instruments including its current assets and current liabilities approximate fair value due to their short-term nature.

##### (f) Revenue recognition

Revenues are primarily derived from equity earnings of KECP.

## KeySpan Facilities Income Fund

### NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

As at June 30, 2003 and for the period from April 3, 2003 (date of inception) to June 30, 2003  
(all amounts expressed in Canadian dollars)  
(unaudited)

#### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

##### (g) Income taxes

Under the terms of the Income Tax Act (Canada), the Fund, as a trust, will not be subject to income taxes to the extent that its taxable income and taxable capital gains are paid or payable to unitholders. Accordingly, no provision for current income taxes is made. In addition, the Fund is contractually committed to distribute to its unitholders all or virtually all of its taxable income and taxable capital gains that would otherwise be taxable to it, and the Fund intends to continue not to be subject to income taxes.

##### (h) Distributions to Unitholders of the Fund

The amount of the distributions to unitholders ("Distributions to Unitholders") of the Fund to be distributed monthly is, as defined in the Fund Declaration of Trust. The computation of the Distribution to Unitholders is comprised of cash amounts received or receivable as distributions or interest income and any net proceeds from the issuance of Trust Units, less any amounts that relate to the redemption of Trust Units and any expenses of the Fund.

The Fund makes distributions, in respect of each month, to the Unitholders of record on the last day of such month. Payments are made on or about the 15<sup>th</sup> day of the month after each record date.

Distributions to Unitholders, as defined above, is not a measure under Canadian generally accepted accounting principles and there is no standardized measure of Distributions to Unitholders. Distributions to Unitholders, as presented, may not be comparable to similar measures presented by other income trusts.

The Fund is dependent upon the operation of its subsidiaries for earnings. Accordingly, Distributions to Unitholders from the Fund are not assured.

##### (i) Net earnings and Distributions per weighted average Trust Unit

Net earnings and distributions accruing to Unitholders per Trust Unit are calculated by dividing net earnings and Distributions accruing to Unitholders, respectively, by the weighted average number of Trust Units outstanding during the period. For the purposes of the weighted average number of Trust Units calculation, Trust Units are determined to be outstanding from the date they are issued.

## KeySpan Facilities Income Fund

### NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

As at June 30, 2003 and for the period from April 3, 2003 (date of inception) to June 30, 2003  
(all amounts expressed in Canadian dollars)  
(unaudited)

#### 3. ACQUISITIONS

On May 30, 2003, the Fund issued 15,000,000 Trust Units as an initial public offering (the "Initial Offering") at a price of \$10.00 per unit for net proceeds of \$139,375,000 after transaction fees of \$10,625,000.

Net proceeds received for the Initial Offering were used to purchase a 34.5% indirect interest in KECP for consideration of \$139,368,031. At the same time, the Fund acquired 34,490 shares of KCML, the managing partner of KECP, representing a 34.5% interest in KCML, for consideration of \$6,969. KCML has a 0.005% interest in KECP.

On June 10, 2003, under the over-allotment option, the Fund issued an additional 2,000,000 Trust Units at a price of \$10.00 per unit for net proceeds of \$18,850,000 after transaction fees of \$1,150,000. The proceeds were used to purchase an additional 4.6% interest in KECP for \$18,849,080 and an additional 4,600 common shares of KCML for \$920.

At June 30, 2003 the equity investment in KECP was comprised of the following:

	\$
<i>Acquisition cost</i>	158,217,111
<i>Net earnings for the period</i>	1,355,151
<i>Distributions from KECP</i>	(1,543,600)
<b><i>Investment in KECP at June 30, 2003</i></b>	<b>158,028,662</b>

At June 30, 2003 the equity investment in KCML was comprised as follows:

	\$
<i>Acquisition cost</i>	7,889
<i>Net earnings for the period</i>	68
<b><i>Investment in KCML at June 30, 2003</i></b>	<b>7,957</b>

#### 4. UNITHOLDERS' EQUITY

The Fund Declaration of Trust provides that an unlimited number of Trust Units may be authorized and issued. Each Trust Unit is transferable, and represents an equal undivided beneficial interest in any distribution from the Fund and in the net assets of the Fund in the event of termination or winding-up of the Fund. All Trust Units are of the same class with equal rights and privileges.

## KeySpan Facilities Income Fund

### NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

As at June 30, 2003 and for the period from April 3, 2003 (date of inception) to June 30, 2003  
(all amounts expressed in Canadian dollars)  
(unaudited)

#### 4. UNITHOLDERS' EQUITY (continued)

The Declaration of Trust also provides for the issuance of an unlimited number of special trust units that will be used solely for providing voting rights to persons holding securities that are directly or indirectly exchangeable for Units and that, by their terms, have voting rights in the Fund.

The Trust Units are redeemable at the holder's option at an amount equal to the lesser of: (i) 90% of the weighted average price per Unit at which the Units during the period of the last 10 days during which the Trust Units were traded on the Toronto Stock Exchange; and (ii) an amount equal to (a) the closing market price of the Units; (b) an amount equal to the average of the highest and lowest prices of Units if there was trading on the date on which the Units were tendered for redemption; or (c) the average of the last bid and ask prices if there was no trading on the date on which the Units were tendered for redemption. Redemptions are subject to a maximum of \$50,000 cash redemptions in any particular month. Redemptions in excess of this amount will be paid by way of a distribution in specie of assets of the Fund which may include CT Series 2 notes.

#### TRUST UNITS ISSUED AND UNITHOLDERS' EQUITY

	<b>Number of Units</b>	<b>Amount \$</b>
<i>Initial Public Offering, net of transaction fees of \$11,775,000</i>	<b>17,000,000</b>	<b>158,225,000</b>
<i>Net earnings</i>		<b>1,355,219</b>
<i>Distributions declared</i>		<b>(1,543,600)</b>
<b><i>As at June 30, 2003</i></b>	<b>17,000,000</b>	<b>158,036,619</b>

The weighted average number of Trust Units outstanding for the period from inception to June 30, 2003 was 5,738,636.

Transaction costs of \$11,775,000 were incurred by the Fund in issuing Trust Units. These costs are deductible for income tax purposes on a straight-line basis over a five-year period. Each Unitholder will be required to include in computing income for tax purposes for a particular taxation year their pro rata share of the Fund's income that was paid or payable in that year to the Unitholder and that was deducted by the Fund in computing its income.

## KeySpan Facilities Income Fund

### NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

As at June 30, 2003 and for the period from April 3, 2003 (date of inception) to June 30, 2003  
(all amounts expressed in Canadian dollars)  
(unaudited)

#### 5. RELATED PARTY TRANSACTIONS

KCML is a 39.1% owned subsidiary of the Fund and is the managing partner of KECP. KeySpan Energy Development Co. owns the remaining 60.9% interest in KCML. KCML provides management and administrative services to the Fund and KECP on a cost recovery basis.

As at June 30, 2003, the Fund had the following balances receivable from related parties in the normal course of business:

	<b>Amount</b>
Distributions Receivable from KECP	<b>\$1,543,600</b>

#### 6. ECONOMIC DEPENDENCE

For the purposes of declaring distributions, the Fund is entirely dependent on cash distributions received from KECP.

#### 7. RECONCILIATION OF DISTRIBUTIONS ACCRUING TO UNITHOLDERS

April 3 to June 30

2003

NET EARNINGS	1,355,219
Add:	
Distributions receivable from KECP	1,543,600
Less:	
Equity earnings from KECP and the Managing Partner	(1,355,219)
<b>DISTRIBUTIONS ACCRUING TO UNITHOLDERS DURING THE PERIOD</b>	<b>1,543,600</b>
Number of Trust Unit outstanding at the end of the period	17,000,000
Distribution accruing to Unitholders per Trust Unit outstanding at the end of the period	0.0908
Weighted average number of Trust Units outstanding	5,738,636
Distributions accruing to Unitholders per weighted average Trust Unit	0.2690

**KeySpan Energy Canada Partnership**

**INTERIM CONSOLIDATED STATEMENT  
OF FINANCIAL POSITION**

(all amounts expressed in thousands of Canadian dollars)

As at

	June 30, 2003 \$ (unaudited)	December 31, 2002 \$
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and cash equivalents	5,627	4,760
Margin deposit	1	229
Accounts receivable	103,418	135,821
Inventory	26,276	19,034
Due from related parties <i>[note 7]</i>	2,847	40,470
Prepaid expenses	1,778	642
	<b>139,947</b>	<b>200,956</b>
Intangible assets	6,942	7,276
Property, plant and equipment	555,708	529,838
Long-term investments <i>[note 4]</i>	12,192	1,218
Future tax asset	3,614	—
Other assets	13,716	13,728
	<b>732,119</b>	<b>753,016</b>
<b>LIABILITIES AND PARTNERS' EQUITY</b>		
<b>Current liabilities</b>		
Accounts payable and accrued liabilities	81,832	106,865
Distribution payable	4,011	—
Deposits payable	1,465	1,445
Debt <i>[note 6]</i>	125,000	—
Due to related parties <i>[note 7]</i>	6,973	4,362
	<b>219,281</b>	<b>112,672</b>
Future site restoration	6,077	5,870
	<b>225,358</b>	<b>118,542</b>
Commitments and contingencies <i>[note 9]</i>		
<b>Partners' equity</b>		
Comprehensive revaluation	(98,433)	(98,433)
Related party transaction adjustment	15,418	4,196
Partners' equity	589,776	728,711
	<b>506,761</b>	<b>634,474</b>
	<b>732,119</b>	<b>753,016</b>

*See accompanying notes to the interim consolidated financial statements*

## KeySpan Energy Canada Partnership

### INTERIM CONSOLIDATED STATEMENT OF NET INCOME, RETAINED EARNINGS AND PARTNERS' EQUITY

(all amounts expressed in thousands of Canadian dollars)

	Three months ended		Six months ended	
	June 30, 2003 \$ (unaudited)	June 30, 2002 \$ (unaudited)	June 30, 2003 \$ (unaudited)	June 30, 2002 \$ (unaudited)
<b>Operating revenues</b>				
Marketing sales	136,627	119,299	363,532	240,980
Facilities – gathering, processing and pipelines	24,391	19,992	47,603	38,737
Marketing service fees	1,648	974	3,117	2,124
Other revenue	282	96	371	176
	<b>162,948</b>	140,361	<b>414,623</b>	282,017
<b>Operating expenses</b>				
Marketing cost of goods sold	133,255	120,695	352,688	237,982
Facilities – gathering, processing and pipelines	12,859	9,931	23,148	17,370
	<b>146,114</b>	130,626	<b>375,836</b>	255,352
	<b>16,834</b>	9,735	<b>38,787</b>	26,665
Depreciation and amortization	5,028	4,496	10,080	8,841
General and administrative	1,640	2,848	5,678	6,037
Site restoration and abandonment	125	116	248	233
Interest	563	7	586	12
Equity earnings from investment [note 4]	(166)	18	(166)	18
	<b>7,190</b>	7,485	<b>16,426</b>	15,141
<b>Income before income tax</b>	<b>9,644</b>	2,250	<b>22,361</b>	11,524
Income tax [note 8]	184	—	184	—
<b>Net income</b>	<b>9,460</b>	2,250	<b>22,177</b>	11,524
<b>Partners' equity, beginning of period</b>	<b>741,428</b>	677,258	<b>728,711</b>	667,984
Partners' capital contribution [notes 3 and 4]	7,306	—	7,306	—
Partners' distributions [notes 1 and 3]	(168,418)	—	(168,418)	—
<b>Partners' equity, end of period</b>	<b>589,776</b>	679,508	<b>589,776</b>	679,508

See accompanying notes to the interim consolidated financial statements

## KeySpan Energy Canada Partnership

### INTERIM CONSOLIDATED STATEMENT OF CASH FLOWS

(all amounts expressed in thousands of Canadian dollars)

	Three months ended		Six months ended	
	June 30, 2003 \$	June 30, 2002 \$	June 30, 2003 \$	June 30, 2002 \$
	(unaudited)	(unaudited)	(unaudited)	(unaudited)
<b>OPERATING ACTIVITIES</b>				
Net income	9,460	2,250	22,177	11,524
Items not requiring cash:				
Depreciation and amortization	5,028	4,496	10,080	8,841
Site restoration and abandonment provision	125	116	248	233
Equity (earnings)/loss from investment	(166)	18	(166)	18
Future income tax	136	—	136	—
Loss on sale of asset	6	—	6	—
Foreign exchange loss	136	452	136	452
	14,725	7,332	32,617	21,068
Changes in non-cash working capital	30,864	(12,542)	44,702	(31,547)
Cash provided by (used in) operating activities	45,589	(5,210)	77,319	(10,479)
<b>INVESTING ACTIVITIES</b>				
Additions to property, plant and equipment	(4,750)	(2,948)	(5,402)	(4,146)
Site restoration expenditures	(143)	(58)	(193)	(66)
Proceeds on sale of asset	748	—	748	—
Increase in other assets	—	9	—	(1,358)
Cash used in investing activities	(4,145)	(2,997)	(4,847)	(5,570)
<b>FINANCING ACTIVITIES</b>				
Issuance of debt (note 6)	125,000	—	125,000	—
Repayment of promissory notes	(31,442)	—	(31,442)	—
Distributions paid	(164,407)	—	(164,407)	—
Changes in non-cash working capital	—	(589)	(756)	(995)
Cash used in financing activities	(70,849)	(589)	(71,605)	(995)
<b>(Decrease) increase in cash</b>	<b>(29,405)</b>	<b>(8,796)</b>	<b>867</b>	<b>(17,044)</b>
<b>Cash and cash equivalents, beginning of period</b>	<b>35,032</b>	<b>20,158</b>	<b>4,760</b>	<b>28,407</b>
<b>Cash and cash equivalents, end of period</b>	<b>5,627</b>	<b>11,362</b>	<b>5,627</b>	<b>11,363</b>

See accompanying notes to the interim consolidated financial statements

## KeySpan Energy Canada Partnership

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(all amounts expressed in thousands of Canadian dollars,  
except where otherwise noted)

June 30, 2003

#### 1. REORGANIZATION

On May 30, 2003 (the "Closing"), the ownership of KeySpan Energy Canada Partnership (the "Partnership" or "KECP") was restructured in accordance with the terms of an Initial Public Offering of KeySpan Facilities Income Fund (the "Fund").

The Fund is an unincorporated open-ended trust established under the laws of the Province of Alberta that has been created to acquire an indirect interest in the Partnership from KeySpan Energy Development Co. ("KEDCO"). On Closing, the Fund acquired approximately a 34.5% interest in the Partnership for cash consideration of \$139,368. On June 10, 2003, an additional 4.6% interest was acquired for cash consideration of \$18,849. As at June 30, 2003, KEDCO and the Fund have an interest of approximately 60.9% (December 31, 2002 – 100%) and 39.1% (December 31, 2002 – nil), respectively.

On May 29, 2003, before the Closing, the following transactions were completed:

(a) The Partnership acquired 100% of the outstanding common shares of KeySpan Energy Facilities Limited ("KEFL"), a wholly owned subsidiary of KEDCO, in exchange for a \$7,287 capital contribution in the Partnership. The transaction has been recorded in these financial statements at the carrying amount of KEFL's assets and liabilities as shown on the following table. The difference between the capital contribution and the carrying values, of \$8,068 has been credited to related transaction adjustment. The results of KEFL's operations have been included in the consolidated financial statements since that date. KEFL provides gas processing and fractionation services and holds a 40.6% beneficial interest in Rimbey Pipe Line Co. Ltd.

The carrying values of KEFL's assets and liabilities as at May 29, 2003 are:

	\$
<i>Current assets</i>	8,355
<i>Investment in Rimbey Pipe Line Co. Ltd.</i>	12,027
<i>Property, plant and equipment</i>	30,967
<i>Future income taxes</i>	580
<i>Current liabilities</i>	(4,979)
<i>Notes payable</i>	(31,442)
<i>Future site restoration provision</i>	(153)
	<b>15,355</b>

(b) The Partnership also acquired 100% of the outstanding common shares of KeySpan Energy Canada Company ("KECC") (formerly KeySpan Energy Canada Inc.), a wholly owned subsidiary of KEDCO in exchange for a \$20 capital contribution in the Partnership. The transaction has been recorded in these financial statements at the carrying value of KECC's assets and liabilities. The difference between the capital contribution and the carrying value has been charged to related party transaction adjustment.

(b) The Partnership distributed \$164,407 to KEDCO and its subsidiaries.

## KeySpan Energy Canada Partnership

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(all amounts expressed in thousands of Canadian dollars,  
except where otherwise noted)

June 30, 2003

#### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements of the Partnership have been prepared in accordance with Canadian generally accepted accounting principles. The accounting policies applied are consistent with those outlined in the Partnership's annual financial statements for the year ended December 31, 2002. These consolidated financial statements for the six months ended June 30, 2003, do not include all disclosures required in the annual financial statements and should be read in conjunction with the audited financial statements included on page F-30 of the KeySpan Facilities Income Fund's Initial Public Offering document dated May 22, 2003.

Interim periods may not be representative of the results expected for the full year of operations due to seasonality.

Certain amounts in these financial statements have been reclassified to reflect current year financial statement presentation.

#### 3. DISTRIBUTABLE CASH FLOW

The amount of distributable cash ("Distributable Cash Flow"), as defined in the Partnership Agreement, will generally be, on a monthly basis, the Partnership's cash flow from operations for such month after (i) satisfaction of its debt service obligations and income tax and large corporations tax expenses; (ii) satisfaction of funding requirements in respect of any reclamation fund; (iii) providing for maintenance capital expenditures; (iv) satisfaction of its other expense obligations including general and administrative expenses and those relating to incentive compensation; and (v) retaining reasonable reserves for administrative and other expense obligations and reasonable reserves for working capital and capital expenditures as may be considered appropriate by the board of directors of the Managing Partner. KEDCO's share of Distributable Cash Flow shall also include 100% of the net receipts (or payments) for contracts entered into regarding the termination of certain natural gas services and an electricity hedge.

Distributable Cash Flow, as defined above, is not a measure under Canadian generally accepted accounting principles and there is no standard measure of distributable cash flow. Distributable Cash Flow, as presented, may not be comparable to similar measures presented by other entities.

The Partnership makes monthly distributions to holders of record on the last day of each month. Payments are made on or about the 15<sup>th</sup> day of the following month.

## KeySpan Energy Canada Partnership

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(all amounts expressed in thousands of Canadian dollars,  
except where otherwise noted)

June 30, 2003

The following table calculates the Distributable Cash Flow under the terms of the Partnership agreement for the period from May 30, 2003 to June 30, 2003.

	<b>Period from May 30 to June 30, 2003</b>
	\$
<b>Net income</b>	<b>3,484</b>
Add (less):	
Depreciation and amortization	1,677
Site restoration provision	44
Equity earnings from investment	(166)
Future income tax	136
Loss on sale of asset	6
Foreign exchange (gain) loss	42
Site restoration expenditures	(74)
Maintenance capital	(1,094)
<b>Cash available for distribution for the period</b>	<b>4,055</b>
Distributions to partners payable:	4,011
To KEDCO	1,842
To KEDCO, electricity hedge and gas services contract	62
To other partners	563
To the Fund	1,544

#### 4. LONG-TERM INVESTMENTS

	<b>June 30, 2003</b>	<b>December 31, 2002</b>
	\$	\$
<i>Rimbey Pipe Line Co. Ltd. (i)</i>	<i>10,974</i>	—
<i>Alberta Laterals Company Ltd.</i>	<i>1,218</i>	<i>1,218</i>
	<b>12,192</b>	<b>1,218</b>

(i) The Partnership owns a 40.6% beneficial interest in Rimbey Pipe Line Co. Ltd. through its 100% ownership of KEFL. The investment is accounted for using the equity method.

	\$
<i>Acquisition</i>	<i>12,027</i>
<i>Equity in earnings</i>	<i>166</i>
<i>Dividends receivable</i>	<i>(1,219)</i>
<b>Carrying value, June 30, 2003</b>	<b>10,974</b>

## KeySpan Energy Canada Partnership

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(all amounts expressed in thousands of Canadian dollars,  
except where otherwise noted)

June 30, 2003

#### 5. FINANCIAL INSTRUMENTS

The Partnership enters into contracts to purchase and sell natural gas and natural gas liquids. These contracts are exposed to commodity price risk between the time contracted volumes are purchased and sold. The Partnership actively manages this risk by using energy-related futures, forwards, swaps and options and by balancing physical and financial contracts in terms of volumes, timing of performance and delivery obligations. Management monitors the Partnership's exposure to the above risks and regularly reviews its financial instrument activities and all outstanding positions.

#### Energy price risk management

The Partnership routinely enters into price swap and option agreements to mitigate its exposure to fluctuations in the price of natural gas, natural gas liquids and electricity. Price swap agreements require payments to (or receipts from) counterparties based on the differential between fixed and variable prices for commodities. Management monitors the Partnership's exposure to the above risks and regularly reviews its use of financial instruments and all outstanding positions. The fair values of the derivatives listed below represent an estimate of the amount that the Partnership would receive or pay if these instruments were closed out at the end of the period.

June 30, 2003	Carrying Amount	Notional Volume	Fair Value \$
<b>Natural gas liquids:</b>			
Price swaps (maturing by October, 2003)	—	85,523 Bbls	(582)
Price swaps (maturing by October, 2003)	—	362,287 Bbls	1,254
<b>Gas:</b>			
Price swaps (maturing by October, 2003)	—	123,000 GJs	(76)
<b>Gas:</b>			
Options (maturing by October, 2003)	—	997,500 GJs	(83)
Options (maturing by October, 2003)	—	997,500 GJs	163
<b>Hedge of electricity for processing plants:</b>			
Price swaps (maturing by December, 2003)	—	8,832 Mwh	267
Price swaps (maturing by December, 2003)	—	44,160 Mwh	(1,214)

The estimated fair value of all financial instruments is based on quoted market prices and, if not available, on estimates from third-party brokers or dealers. The carrying value of cash and cash equivalents, margin deposit, accounts receivable, due from/to related parties, accounts payable and accrued liabilities approximates their fair value because the instruments are near maturity or have no fixed repayment terms. The fair value of

## KeySpan Energy Canada Partnership

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(all amounts expressed in thousands of Canadian dollars,  
except where otherwise noted)

June 30, 2003

#### 5. FINANCIAL INSTRUMENTS (continued)

the bank credit facilities approximates fair value due to their floating rates of interest.

Pursuant to an agreement between the Partnership and KEDCO, KEDCO is responsible for all payments by and to the Partnership under the above electricity hedging contracts.

#### 6. DEBT

	<b>June 30, 2003</b>	December 31, 2002
	\$	\$
<i>Bank credit facilities (i)</i>	<b>68,000</b>	—
<i>Advance from KEDCO (ii)</i>	<b>57,000</b>	—
	<b>125,000</b>	—

(i) On May 30, 2003, the Partnership and certain financial institutions, led by the Royal Bank of Canada, entered into a credit agreement for CAD\$100,000 and US\$50,000 under three separate tranches. As at June 30, 2003, \$68,000 has been drawn on this line under Tranche C, which matures on November 26, 2003.

Tranche A of \$50,000 matures on May 29, 2004 but may be extended for one year beyond the term date. Tranche B of \$50,000 matures on May 30, 2005. The outstanding balance on June 30, 2003 was in the form of a prime loan, and bears interest at the related prime rate plus 57.5 basis points. Security is provided by first charge over the Partnership's assets.

(ii) On June 30, 2003 KEDCO advanced \$57,000 to the Partnership. The loan is non-interest bearing, unsecured and matures on September 30, 2003.

## KeySpan Energy Canada Partnership

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(all amounts expressed in thousands of Canadian dollars,  
except where otherwise noted)

June 30, 2003

#### 7. RELATED PARTY TRANSACTIONS

The following table summarizes the Partnership's related party transactions:

	<i>Three months ended</i>		<i>Six months ended</i>	
	<i>June 2003</i>	<i>June 2002</i>	<i>June 2003</i>	<i>June 2002</i>
	<i>\$</i>	<i>\$</i>	<i>\$</i>	<i>\$</i>
<i>Tariff expense for use of pipeline and NGL purchases:</i>				
<i>Corporation over which Partnership has significant influence</i>	<i>721</i>	<i>783</i>	<i>1,426</i>	<i>1,298</i>
<i>Operating allocation and NGL revenue:</i>				
<i>Corporation controlled by a partner with significant influence</i>	<i>1,191</i>	<i>1,008</i>	<i>2,242</i>	<i>1,841</i>
<i>Equity earnings:</i>				
<i>Corporation over which Partnership has significant influence</i>	<i>166</i>	<i>—</i>	<i>166</i>	<i>—</i>
<i>Dividends:</i>				
<i>Corporation over which Partnership has significant influence</i>	<i>1,218</i>	<i>—</i>	<i>1,218</i>	<i>—</i>
<i>Operating expense and general and administrative cost</i>	<i>2,353</i>	<i>3,037</i>	<i>7,566</i>	<i>7,552</i>

The transactions summarized in the above table were made in the normal course of operations and were measured at the exchange value or on a cost recovery basis, which represented the amount of consideration established and agreed to by the related parties.

	<i>June 30, 2003</i>	<i>December 31, 2002</i>
	<i>\$</i>	<i>\$</i>
<i>Trade accounts receivable:</i>		
<i>Partners and corporations controlled by a partner with significant influence</i>	<i>2,847</i>	<i>2,058</i>
<i>Advance to Partner</i>	<i>—</i>	<i>38,412</i>
<i>Total due from related parties</i>	<i>2,847</i>	<i>40,470</i>
<i>Trade accounts payable:</i>		
<i>Partners and corporations controlled by a partner with significant influence</i>	<i>2,962</i>	<i>4,362</i>
<i>Total due to related parties</i>	<i>2,962</i>	<i>4,362</i>

(a) The amounts due to the related parties are non-interest bearing, with no fixed terms of repayment.

## KeySpan Energy Canada Partnership

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(all amounts expressed in thousands of Canadian dollars,  
except where otherwise noted)

June 30, 2003

#### 8. INCOME TAXES

Income tax expense is comprised of:

	<b>June 30, 2003</b>
	<b>\$</b>
<i>Current income tax</i>	48
<i>Future income tax</i>	136
	<b>184</b>

Income taxes differ from the amounts which would be obtained by applying statutory income tax rates as follows:

	<b>June 30, 2003</b>
	<b>\$</b>
<i>Income before tax expense</i>	22,361
<i>Non taxable income attributable to the Partnership</i>	<u>(22,240)</u>
<i>Taxable income</i>	121
<i>Income tax at statutory rate of 40.70%</i>	49
<i>Equity in earnings from investments</i>	(68)
<i>Large corporation tax</i>	48
<i>Other</i>	155
	<b>184</b>

## KeySpan Energy Canada Partnership

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(all amounts expressed in thousands of Canadian dollars,  
except where otherwise noted)

June 30, 2003

#### 8. INCOME TAXES (continued)

The temporary differences comprising the future income tax asset are as follows:

	June 30, 2003 \$
<i>Property, plant and equipment</i>	<i>(1,077)</i>
<i>Non-capital losses carry forward</i>	<i>5,060</i>
<i>Equity investment</i>	<i>(379)</i>
<i>Intangible assets</i>	<i>(27)</i>
<i>Future site restoration</i>	<i>54</i>
<i>Other</i>	<i>(17)</i>
<i>Future income tax asset</i>	<i>3,614</i>

#### 9. COMMITMENTS AND CONTINGENCIES

The Partnership is involved in various contractual agreements with ConocoPhillips. The agreements range from one to sixteen years and comprise the purchase and processing of ConocoPhillips' natural gas and NGL production in the areas specified in the agreements. The purchase prices are based on current period market prices.

KECP has lease commitments relating to railway tank cars, vehicles, computer hardware, office space and natural gas transportation agreements. The estimated annual minimum operating lease rental payments from these commitments are as follows:

	\$
<i>Remainder of 2003</i>	<i>3,283</i>
<i>2004</i>	<i>4,271</i>
<i>2005</i>	<i>1,967</i>
<i>2006</i>	<i>1,317</i>
<i>2007</i>	<i>1,031</i>
<i>Thereafter</i>	<i>6,573</i>
	<i>18,442</i>

## KeySpan Energy Canada Partnership

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(all amounts expressed in thousands of Canadian dollars,  
except where otherwise noted)

June 30, 2003

#### 9. COMMITMENTS AND CONTINGENCIES (continued)

There are legal actions involving the Partnership for which the ultimate results cannot be ascertained at this time. Management believes the resolution of these matters will not have a material adverse effect upon the financial position or results of operations of the Partnership.

#### 10. SEGMENTED INFORMATION

The Partnership has two reportable segments: Facilities and Marketing. The accounting policies of the segments are the same as those disclosed in Note 2.

	Facilities		Marketing		Corporate		Total	
	2003	2002	2003	2002	2003	2002	2003	2002
<b>Three months ended June 30</b>	<b>2003</b>	<b>2002</b>	<b>2003</b>	<b>2002</b>	<b>2003</b>	<b>2002</b>	<b>2003</b>	<b>2002</b>
Revenue	25,024	20,143	138,275	120,274	282	96	163,581	140,513
Equity earnings (loss)	166	(4)	—	—	—	—	166	(4)
Intersegment revenue	(632)	(152)	—	—	—	—	(632)	(152)
<b>External revenue</b>	<b>24,558</b>	<b>19,987</b>	<b>138,275</b>	<b>120,274</b>	<b>282</b>	<b>96</b>	<b>163,115</b>	<b>140,357</b>
Cost of sales and Operating expenses	(12,860)	(9,931)	(133,255)	(120,694)	—	—	(146,115)	(130,625)
	<b>11,698</b>	<b>10,056</b>	<b>5,020</b>	<b>(420)</b>	<b>282</b>	<b>96</b>	<b>17,000</b>	<b>9,732</b>
Depreciation and amortization	(4,506)	(3,974)	(167)	(167)	(355)	(355)	(5,028)	(4,496)
General and administrative	—	—	—	—	(2,203)	(2,869)	(2,203)	(2,869)
Site restoration	(125)	(117)	—	—	—	—	(125)	(117)
<b>Income (loss) before tax</b>	<b>7,067</b>	<b>5,965</b>	<b>4,853</b>	<b>(587)</b>	<b>(2,276)</b>	<b>(3,128)</b>	<b>9,644</b>	<b>2,250</b>

## KeySpan Energy Canada Partnership

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(all amounts expressed in thousands of Canadian dollars,  
except where otherwise noted)

June 30, 2003

#### 10. SEGMENTED INFORMATION (continued)

	Facilities		Marketing		Corporate		Total	
	2003	2002	2003	2002	2003	2002	2003	2002
<b>Six months ended June 30</b>								
Revenue	48,621	39,421	366,649	243,104	371	175	415,641	282,700
Equity earnings (loss)	166	(8)	—	—	—	—	166	(8)
Intersegment revenue	(1,018)	(684)	—	—	—	—	(1,018)	(684)
<b>External revenue</b>	<b>47,769</b>	<b>38,729</b>	<b>366,649</b>	<b>243,104</b>	<b>371</b>	<b>175</b>	<b>414,789</b>	<b>282,008</b>
Cost of sales and Operating expenses	(23,148)	(17,370)	(352,688)	(237,981)	—	—	(375,836)	(255,351)
	24,621	21,359	13,961	5,123	371	175	38,953	26,657
Depreciation and amortization	(9,032)	(7,798)	(334)	(334)	(714)	(709)	(10,080)	(8,841)
General and administrative	—	—	—	—	(6,264)	(6,059)	(6,264)	(6,059)
Site restoration	(248)	(233)	—	—	—	—	(248)	(233)
<b>Income (loss) before tax</b>	<b>15,341</b>	<b>13,328</b>	<b>13,627</b>	<b>4,789</b>	<b>(6,607)</b>	<b>(6,593)</b>	<b>22,361</b>	<b>11,524</b>

## KeySpan Energy Canada Partnership

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(all amounts expressed in thousands of Canadian dollars,  
except where otherwise noted)

June 30, 2003

#### 10. SEGMENTED INFORMATION (continued)

	Facilities		Marketing		Corporate		Total	
	June 30, 2003	December 31, 2002	June 30, 2003	December 31, 2002	June 30, 2003	December 31, 2002	June 30, 2003	December 31, 2002
Identifiable assets	618,595	582,862	97,813	121,512	15,711	48,642	732,119	753,016
Capital Expenditures	4,911	11,854	—	—	491	13	5,402	11,867

For the three months and six months ended June 30, 2003 the Partnership derived Marketing revenue of \$1,473 and \$11,309, respectively (three and six months ended June 30, 2002 - \$1,491 and \$8,784, respectively) from export sales of NGL product to the United States. Revenue is attributed to the United States based on final known destination of the product.

# Corporate Information

## Board of Directors

**E. Peter Lougheed** <sup>(1)(3)(5)</sup>  
*Partner*  
*Bennett Jones LLP*  
*Calgary, Alberta*

**James V. Bertram** <sup>(4)</sup>  
*President and CEO*  
*KeySpan Canada Management Ltd.*  
*Calgary, Alberta*

**Robert B. Catell**  
*Chairman and CEO*  
*KeySpan Corporation*  
*New York, New York*

**Michael B.C. Davies** <sup>(2)</sup>  
*Principal*  
*Davies & Co.*  
*Banff, Alberta*

**Nancy M. Laird** <sup>(1)(3)</sup>  
*Corporate Director*  
*Calgary, Alberta*

**Gerald Luterman**  
*Executive Vice President and CFO*  
*KeySpan Corporation*  
*New York, New York*

**H. Neil Nichols** <sup>(3)(4)</sup>  
*President*  
*KeySpan Energy Development Corporation*  
*Mississauga, Ontario*

**William R. Stedman** <sup>(1)(2)(4)</sup>  
*Chairman and CEO*  
*ENTx Capital Corporation*  
*Calgary, Alberta*

**Wesley R. Twiss** <sup>(2)</sup>  
*Corporate Director*  
*Calgary, Alberta*

- (1) Trustee of the Fund
- (2) Member of the Audit Committee
- (3) Member of the Compensation and Governance Committee
- (4) Member of the Health, Safety and Environment Committee
- (5) Chairman of the Board

## Officers

Jim V. Bertram  
President & CEO

David G. Smith  
Senior Vice President, CFO and Secretary

Ken W. Merritt  
Vice President, Rimbey Corridor and Marketing

David A. Sentes  
Vice President and Comptroller

K. Jamie Urquhart  
Vice President, Foothills Region

## Stock Exchange Listing

The Toronto Stock Exchange  
Trading Symbol KEY.UN

## Investor Relations

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