

# **PACIFIC ENERGY RESOURCES LTD.**

## **MANAGEMENT DISCUSSION AND ANALYSIS**

The following discussion and analysis is for the nine month period ending September 30, 2005 compared with the nine month period ending September 30, 2004. This information is current to November 22, 2005 and has not been reviewed by the Company's auditors.

### **Introduction**

The discussion and analysis of the operating results and financial position of the Company should be read in conjunction with the attached Financial Statements and related Notes ("the Financial Statements"), which have been prepared in accordance with Canadian generally accepted accounting principles (GAAP) (see Summary of Significant Accounting Policies and Nature of Operations). This discussion and analysis may contain forward-looking statements about the Company's future prospects, and the Company provides no assurance that actual results will meet management's expectations.

### **Significant Changes in Reporting**

Effective with the Financial Statements for the three months ended March 31, 2005, the Company changed its reporting currency from Canadian dollars to United States dollars. Additionally, the Company has effected the acquisition of the additional 75% of the California Joint Venture in March, 2005. The financial results for the current quarter and nine months reflect these changes. The comparative amounts for 2004 have been changed to United States dollars, but only the 25% of the results from the Joint Venture have been included, as originally reported.

On March 3, 2005, the Company completed the acquisition of PetroCal, Inc., a private corporation organized under the laws of the State of Delaware, U.S.A. with oil and gas operations in California. Pacific Energy issued 40,363,457 common shares to the shareholders of PetroCal, Inc. and its wholly owned subsidiary. The Company acquired the 75% interest in shared oil and gas leases in California, as well as a 100% interest in an additional oil and gas lease, also located in California.

For accounting purposes, the acquisition of Petrocal and its subsidiary have been recorded as a business combination. Earnings for the period from January 1 to March 3, 2005 for the 75% interest in California operations that was acquired became part of the acquisition price, and are not included in the current year's operating results.

This acquisition will immediately add approximately 400 BOPD in production and increase overall quarterly revenues by US\$1,600,000.00. Pacific Energy will hold a 100% interest in net proved developed producing reserves of 2.4 million barrels, proved developed non-producing reserves of 0.2 million barrels, and proved undeveloped reserves of 8.7 million barrels. This is an increase of 31.6% from the

total net proved reserves reported by DeGolyer and MacNaughton, a Houston Based Independent Engineering and Consulting Firm. The report is an evaluation of the Company's reserves as of August 1, 2004. See Note 3 to the Financial Statements for more details.

## Results of Operations

The Company had no production in 2002, and completed the acquisition of their 25% interest in the producing wells in the Los Angeles basin (the California Joint Venture) late in 2003. The Company was credited with the results of operations from January 2003, the effective date of the purchase agreement.

Pacific Energy Resources Ltd. completed the acquisition of the balance of the Joint Venture in March, 2005, by a merger with the three associated companies that each held an equal 25%. As part of the merger, the Company also received an adjacent property in the Wilmington field that was acquired in August, 2004 by Petrocal Inc, an affiliate and owner of one of the 25% interests in the Joint Venture.

Statement of Operations	2005 <u>9 Months</u>	2004 <u>12 Months</u>	2003 <u>12 Months</u>
	US\$	Cdn\$	Cdn\$
Total revenues	5,141,151	1,676,625	1,207,845
Net income (loss)	737,398	(106,696)	(1,626,241)
Gain (loss) per share	0.01	(0.01)	(0.20)
Total assets	12,242,889	3,629,275	3,005,927
Total long-term liabilities	1,674,942	1,482,684	1,363,628
Cash dividends	0	0	0

\*Loss per share is reflected on a 3:1 share consolidation basis.  
No diluted loss per share will be provided as the result will be anti-dilutive.

The Company has a net income of \$737,398 for the nine months ending September 30, 2005 (\$0.01 per share) compared with income of \$173,122 for the same period in 2004 (\$0.01 per share). During the nine months ending September 30, 2005 the gross revenue and expenses from production were \$5,141,151 and \$2,101,032 respectively. Production revenue increased by \$4,144,896 over 2004, due to revenue from the additional 75% of the Joint Venture from March 3, 2005 and the increase in the price of crude oil in the past year.

Production expenses increased to \$2,101,302 in 2005, more than three times the expenses for the same period in 2004. This was due to the expansion of the Company's operations and increases in the price of consumables and well services due to increased demand. These higher costs are expected to continue for the rest of the current year, although the Company is attempting to use in-house staff and supplies wherever possible.

The net return from oil and gas operations for their California properties for the nine months was \$2,688,518, an increase of \$2,401,854 over 2004. The increase in the overall net income of \$564,276 over the \$173,122 earned in the first nine months of 2004 is primarily due to the acquisitions mentioned above. These increases were more than would normally be expected, even taking the merger into consideration, due to the increase in the price of crude oil in 2005.

The Company also had a temporary increase in overhead expenses in 2005, as a result of the added legal and accounting costs associated with the acquisition by the Company of the remaining 75% of the California Joint Venture. These expenditures are not expected to continue after 2005, while production revenue should increase as redevelopment plans progress and crude oil prices remain at historical highs.

The Company's total oil production for the nine months was 133,517 barrels, compared to 28,103 for the prior year. As a result of the above mentioned merger, the Company also acquired another producing property in the Wilmington field, which produced 20,192 barrels of oil in the nine months ending September 30, 2005. This property was purchased August 31, 2004 by an affiliated company prior to its merger into the Company. The company also sells natural gas to customers in Southern California. Some of this gas is purchased from other producers, and small amounts come from Company owned properties. The revenue and volume of sales are insignificant in the overall operation, and have not been shown separately.

**Quarterly Production Volumes (Bbls.):**

	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Total</u>	<u>Increase</u>	
<b>2005</b>	43,801	44,868	44,849		133,518	96,087	473%
<b>2004</b>	9,283	9,480	9,340	9,329	37,431	(2,624)	-7%
<b>2003</b>	9,891	9,843	10,253	10,068	40,056		

The Company has developed a business plan focused on the acquisition and enhancement of mature oil and gas fields that would realize increased production utilizing current engineering and production technology. The following is a summary of the key exploration and development projects the Company is currently working on:

The Company is the lessee and operator of onshore fields located in the Los Angeles Basin in southern California that currently produce over 510 barrels of oil and gas equivalent per day ("BOPD"). The majority of Pacific Energy's productive acreage is contained within the giant Wilmington Oil Field located in the city of Long Beach, California. The full development plan calls for the drilling of an additional 65

wells (52 Producers and 13 injectors) in a "Five Spot" pattern. When completed, each injector well is surrounded by four producers.

The next "5 spot" (4 producers and 1 injector) is expected to be started in early 2006. Plans to start drilling in the second quarter were delayed when the company was unable to obtain a contract for a drilling rig. These wells are estimated to cost \$3.0 million and should raise the production of oil by 250 barrels per day. Pacific Energy plans on drilling a total of 15 wells in the Wilmington Oil Field during the next year, subject to rig availability. With the current high oil prices, the Company feels that current cash flow and debt capacity should be adequate to fund this development program.

The Company continues to evaluate acquisition targets within its key area of operation, Long Beach primarily within the Wilmington field. The main objective of the Company is to be in excess of 1000 barrels oil per day production by the end of 2006, and to accomplish this through both the continued development of current assets, and additional acquisitions.

### **California Offshore Project**

AERA Energy LLC operates a three platform complex in the San Pedro Bay area, in Federal waters nine miles offshore Huntington Beach and Long Beach, California. The complex produces oil and gas from the Beta Field and consists of producing Platforms Eureka and Ellen, and facilities Platform Elly.

Pacific Energy is in discussions with AERA Energy regarding a possible Joint Venture for the return to production of Platform Eureka. While a framework for the Joint Venture has been agreed upon, the final agreement has not been completed. The Company is currently in the process of completing its due diligence and negotiating the structure of the Joint Venture. We anticipate releasing more detailed information in the next month.

Platform Eureka was shut down in 1999 due to a leak in the product shipment pipeline, at which time it was producing over 4,400 barrels of oil per day. Platform Ellen is currently producing 2,100 barrels of oil per day. The estimated original oil in place for the Beta Field is 590,000,000 barrels of oil. Cumulative production through 2004 for the Beta Field is estimated at 95,000,000 barrels of oil or approximately 16% of the original oil in place.

The Beta Field was discovered in 1976. Aera Energy and its predecessor companies have operated and maintained Platforms Eureka, Ellen and Elly since production started in 1981 from Platform Ellen. Production began on Platform Eureka in 1985, and peak production from the Beta Field of 20,800 barrels of oil per day was reached in 1986. Platform Edith, a third producing platform also in the Beta Field, is neither owned nor operated by Aera and is not included in the proposed Joint Venture.

## **Other Opportunities**

The Company continues to be active in Russia, and is currently evaluating and negotiating on a number of opportunities. The Company is also investigating a potential exploration project in the Green River Basin in Wyoming.

## **Capital Resources and Liquidity**

During the first quarter of 2005 the Company issued convertible debentures for an aggregate of USD \$581,208.38. The convertible debentures have a three year term, carrying interest at a rate of 7% per annum, compounded semi-annually. The debt may be converted into common shares of the Company at a conversion rate of CDN \$0.75/share. In accordance with TSX Venture Exchange requirements, any securities issued upon conversion of the debentures were subject to a hold period that has now expired.

During 2004, Pacific Energy raised an aggregate of \$800,000 from the issue of 2,666,667 common shares pursuant to private placement agreements.

On October 19, 2004, the Company closed issuing 666,667 units at a price of \$0.60 per unit. Each unit is comprised of one common share and one share purchase warrant exercisable to acquire an additional common share at \$0.60 for a period of two years, expiring October 19, 2006. In addition to this transaction, the Company issued 66,667 units as a finder's fee.

On May 12, 2004 the Company announced that it had arranged a non-brokered private placement of 2,000,000 shares at a price of \$0.20 per unit. Each unit consists of one common share and one share purchase warrant with each entitling the holder to acquire a further common share for a period of two years at a price of \$0.20 per share. In addition to this transaction the Company issued 40,000 units as a finder's fee. The proceeds will be used to fund the pilot redevelopment program and general working capital.

At September 30, 2005 the Company had cash of \$1,171,194, compared to \$154,209 at September 30, 2004. The working capital deficit was \$1,037,952 at September 30, 2005 compared to a deficit of \$241,228 at September 30, 2004. The notes payable that make up the majority of the Company's liabilities were issued to acquire the oil and gas leases in the Los Angeles basin.

Pacific Energy continues to raise capital to fund its acquisition and development program in California. There is however, no assurance that any future funding can be accomplished as it would be wholly dependent on the state of the capital markets for junior exploration companies. Given the current high prices being paid for crude oil, the market has been able to fulfil industry needs to date. The Company does not anticipate the payment of dividends in the future.

### **Off-Balance Sheet Arrangements**

The Company has no off-balance sheet arrangements.

### **Related Party Transactions**

None in the periods disclosed.

### **Changes in Accounting Policy**

None in the periods disclosed.

### **Financial and Other Instruments**

The Company's financial assets and liabilities consist of cash, short-term investments, and receivables, accounts payable and accrued liabilities, which have in the past been denominated in Canadian dollars. Assets and liabilities that originated in United States dollars have been converted back to their original values. Assets and liabilities of Canadian origin have now been converted to U.S. dollars. These accounts were all recorded at their fair market value.

The Company has placed its cash and cash equivalents in liquid bank deposits which provide a variable rate of interest.

### **Outstanding Share Data**

The Company has one class of common shares. At September 30, 2005, there were 55,704,669 common shares outstanding. The increase during 2005 reflected the issue of 40,363,457 shares for the acquisition of PetroCal, and 1,555,556 shares issued as a result of the exercise of warrants.

The Company has a stock option plan; subsequent to September 30, 2005, the Company granted stock options for 3,350,000 shares at \$0.84 per share to key employees and directors.

### **Selected Quarterly Information**

The following is summary data of the most recent completed eleven quarters. In March of 2005 the Company acquired the additional 75% of the California Joint Venture that was held by their affiliated companies. The results for 2005 reflect this increase in the investment in the Joint Venture. Income and expenses from March 3, 2005 for the additional 75% are included in operating results.

An increase in the average oil price of over 45% in the third quarter of 2005 (over the average price in the first quarter) directly contributed to the increase in revenues. Expenses also increased in the fourth quarter of 2004 as the company installed a new computer and accounting system and incurred legal and accounting fees related to the acquisition of the other 75% of the Joint Venture. This high level of expenses is expected to ease as the Company concentrates more on developing current opportunities.

<b>2005 - United States Dollars</b>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Total</u>
Total revenues	828,124	1,964,367	2,348,660		5,141,151
Net income (loss)	98,088	470,668	168,642		737,398
Earnings (loss) per share	\$ 0.00	\$ 0.01	\$ 0.01		\$ 0.01
<b>2004 - Canadian Dollars</b>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Total</u>
Total revenues	362,439	483,518	476,389	354,279	1,676,625
Net income (loss)	141,904	60,439	27,444	(336,483)	(106,696)
Earnings (loss) per share *	\$ 0.02	\$ 0.02	\$ 0.02	\$ (0.03)	\$ (0.01)
<b>2003 - Canadian Dollars</b>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Total</u>
Total revenues	-	27,179	148,148	1,032,518	1,207,845
Net loss	(75,457)	(294,931)	(63,884)	(1,191,969)	(1,626,241)
Earnings (loss) per share *	\$ (0.03)	\$ (0.09)	\$ (0.01)	\$ (0.14)	\$ (0.02)

\*Earning (loss) per share is reflected on a 3:1 share consolidation basis.  
No diluted earnings (loss) per share will be provided as there is no difference or is anti-dilutive.

### Subsequent Events

As discussed earlier, the Company has entered into a preliminary agreement with AERA Energy for a possible return of AERA's Platform Eureka to production. As of November 22, 2005 no final agreement has been completed.

### Business Risks & Risk Management

Except for historical information contained in this discussion and analysis, disclosure statements contained herein are forward-looking, which statements are subject to risks and uncertainties, which could cause actual results to differ materially from those in such forward-looking statements.

The long term commercial success of the Company depends on its ability to find, acquire, develop and commercially produce oil reserves. Pacific Energy attempts to reduce these risks through the combination of experienced personal with local knowledge and careful evaluation.

Commodity price fluctuations can pose a risk to the Company, and management monitors these on an ongoing basis. External factors beyond the company's control may affect the marketability of the oil and gas produced. The Company currently has no hedging instruments in place although it has in the past and may decide to do so in the future.

The Company has selected appropriate personnel to monitor field operations and has some automated field information where possible, so that difficulties and operational issues can be assessed and dealt with on a timely basis, and so that production can be maximized as much as possible.

Oil and gas exploration, development and production operations are subject to all the risks and hazards typically associated with such operations, including hazards such as fire, explosion, blowouts and spills, each of which could result in damage to wells, production facilities, other property and environment or in personal injury. In accordance with industry practice, the Company insures against most of these risks (although not all such risks are insurable). The Company maintains liability insurance in an amount that it considers consistent with industry practice; although the nature of these risks is such that liabilities could potentially exceed policy limits. The Company also reduces risk by operating all its current properties, as such it has control over quality of work and performance.

The Company anticipates making substantial capital expenditures in the future for exploration, development and acquisition and production of oil and gas reserves. If the Company's revenues or reserves decline, it may have limited ability to expend the capital necessary to undertake or complete future development programs. There can be no assurance that debt or equity financing will be available. The Company mitigates this risk by monitoring expenditures, operations and results of operations in order to manage capital effectively.

### **Future Prospects**

Management is optimistic about the growth potential of the Company. Pacific Energy has a large number of proven undeveloped locations to be drilled. Although there are some mechanical challenges inherent in our main area of operation, Wilmington Oil Field, our preliminary results are positive and point to an asset with much undeveloped potential. With proper risk management and careful evaluation and continued development of current assets, management believes that the Company will continue to grow.