



TERRAENERGY
CORP

2005 INTERIM REPORT

Q1

*Three months ended
March 31, 2005*



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Abbreviations

AIF	Annual Information Form	mcf/d	thousand cubic feet per day
Bbl	barrel	mmcf	million cubic feet
bbl/d	barrels per day	mmcf/d	million cubic feet per day
boe	barrels of oil equivalent	NGLs	natural gas liquids
boe/d	barrels of oil equivalent per day	TSX-V	TSX Venture Exchange
C\$	Canadian dollars	WCSB	Western Canadian Sedimentary Basin
mcf	thousand cubic feet		

Company Definition

Throughout the annual report, Terra Energy Corp. is referred to as "Terra Energy", the "Company" or the "Corporation".

Volume Reporting Definition

For the purposes of calculating unit costs, natural gas has been converted to a barrel of oil equivalent ("boe") using six thousand cubic feet equal to one barrel of oil unless otherwise stated. This conversion conforms to Canadian Securities Regulators National Instrument 51-101 Standards of Disclosure for Oil and Gas Activities. Barrels of oil equivalent are a very approximate comparative measure that, in some cases, could mislead particularly if used in isolation.

Forward Looking Statements

Certain information regarding the Company contained herein may constitute forward-looking statements under applicable securities laws. Such statements are subject to known or unknown risks and uncertainties that may cause actual results to differ materially from those anticipated or implied in the forward-looking statements.

Management's Discussion & Analysis

Period Ended March 31, 2005 as compared to March 31, 2004

This Management Discussion and Analysis should be read in conjunction with Terra Energy Corp.'s ("Terra Energy" or the "Corporation") unaudited consolidated financial statements and corresponding notes for the periods ended March 31, 2005 and March 31, 2004. This commentary is based on information available at May 12, 2005. Additional information relating to Terra Energy is available on SEDAR at www.sedar.com.

For the purposes of calculating unit costs, natural gas has been converted to a barrel of oil equivalent ("boe") using six thousand cubic feet equal to one barrel of oil unless otherwise stated. This conversion conforms to Canadian Securities Regulators National Instrument 51-101 – Standards of Disclosure for Oil and Gas Activities. Boe's are a very approximate comparative measure that, in some cases, could mislead particularly if used in isolation.

Management's Discussion and Analysis contains the term cash flow from operations and funds from operations, which should not be considered alternative to, or more meaningful than cash flows from operating activities as determined in accordance with Canadian generally accepted accounting principles ("GAAP") as an indicator of Terra Energy's performance. Terra Energy's determination of cash flow from operating activities may not be comparable to that reported by other companies. The reconciliation between net earnings and cash flows from operating activities can be found in the statements of cash flows from the unaudited consolidated financial statements.

CORPORATE HISTORY

Terra Energy is a publicly traded corporation, amalgamated under the Business Corporations Act of Alberta, and formed as a result of the amalgamation of Terra Energy Corp., Terrapet Energy Corp., and Rhodes Resources Corp. on January 30, 2004. This Management Discussion and Analysis along with the associated financial statements referenced above include the accounts of the Corporation and its wholly-owned subsidiary Constar Resources Ltd. and Terra Energy, a general partnership between Terra Energy Corp. and Constar Resources Ltd.

The Corporation's principal business is the exploration, development and production of petroleum and natural gas in Western Canada.

Highlights

<i>Operations for the three months ended March 31st</i>	<i>2005</i>	<i>2004</i>	<i>Percent Growth</i>
Average Daily Production	2,155	946	128%
Exit Production (boe/d)	2,591	1,180	120%
Undeveloped Land (Net Acres)	84,458	11,296	648%

Management's Discussion & Analysis

<i>Financial for the three months ended March 31st</i>	2005	2004	<i>Percent Growth</i>
Revenue	\$7,932,681	\$3,762,921	111%
Cashflow From Operations	\$3,809,611	\$1,494,740	155%
Cashflow Per Share - basic	\$0.08	\$0.06	33%
Revenue per boe	\$40.88	\$40.03	2%
Operating Netback per boe	\$25.50	\$23.17	10%
Cashflow per boe	\$19.64	\$15.90	24%

The Corporation's reserves were evaluated at December 31, 2004. Information regarding the reserves is available at www.sedar.com.

2005 OPERATIONS – YEAR TO DATE

During the current quarter, Terra Energy's efforts were primarily focused towards reviewing and assessing the recently acquired properties in the Corporation's core area of Fort St. John. In recognition of the significant potential that exists on the acquired properties, the Corporation re-evaluated its capital budget in early 2005 to ensure capital was focused on developing and exploring high-impact opportunities.

Projects in progress at year end at Sextet and Bilawchuk were completed by the quarter end. Completion of these projects was delayed due to service and equipment availability and unfavourable weather conditions. In Sextet, flow testing of suspended wells continued with the reactivation of a suspended pipeline. Three wells at Sextet are expected to stabilize during the second quarter of 2005.

In Bilawchuk, the Corporation completed a pipeline tie-in, bringing on new natural gas and liquids production. Initial operational issues are being addressed and the well is expected to stabilize with production of at least 150 barrels equivalent per day.

Continuing with the Corporation's focus to reduce operating costs on a per unit of production basis, a modification to the Red Creek facilities was undertaken to reduce trucking costs and processing fees associated with the oil production. The savings as a result of the modifications are expected to be realized in subsequent quarters.

CURRENT PRODUCTION

The average daily production rate and exit rates for the three months ended March 31, 2005 and 2004 are set out below, and expressed in barrel of oil equivalents.

Management's Discussion & Analysis

<i>Period Ended</i>	<i>Period ended March 31, 2005</i>		<i>Period ended March 31, 2004</i>		<i>Percent Growth</i>	
	<i>Average</i>	<i>Exit</i>	<i>Average</i>	<i>Exit</i>	<i>Average</i>	<i>Exit</i>
Oil (bbl/d)	532	546	244	256	118%	113%
Natural Gas (boe/d)	1,564	1,955	723	848	116%	131%
Liquids (bbl/d)	59	90	66	76	(11%)	18%
Total (boe/d)	2,155	2,591	1,033	1,180	109%	120%

The increased production for the first quarter of 2005 is higher than first quarter production for 2004 as a result of strategic acquisitions, continued drilling successes, and the tying-in of additional resources.

Results of Operations

<i>Period Ended</i>	<i>Period ended March 31, 2005</i>	<i>Period ended March 31, 2004</i>	<i>Period ended March 31, 2005</i>	<i>Period ended March 31, 2004</i>	<i>Percent Growth per boe</i>
			<i>(\$ / boe)</i>	<i>(\$ / boe)</i>	<i>(\$ / boe)</i>
Revenues	\$ 7,932,681	\$ 3,762,921	\$ 40.88	\$ 40.03	2%
Royalties	984,507	684,760	5.07	7.28	(30%)
Production Expenses	2,000,190	900,231	10.31	9.58	8%
Income from Operations	4,947,984	2,177,930	25.50	23.17	10%
General & administrative expenses	786,695	509,619	4.05	5.42	(25%)
Interest expense	351,678	72,771	1.81	0.77	135%
Non-cash expenses	5,254,890	908,000	27.09	9.66	180%
Income (loss) before income taxes	(1,445,279)	687,540	(7.45)	7.31	(202%)
Income tax expense (recovery)	(451,555)	336,000	(2.33)	3.57	(165%)
Net Income	\$ (993,724)	\$ 351,540	\$ (5.12)	\$ 3.74	(237%)

The Corporation earned higher revenues as a result of increased production activity along with continued high commodity prices. The higher commodity prices were offset by various factors. These include hedging expenses as a result of high oil prices. Approximately 30 percent of oil production is medium crude. The revenue differential between light and medium crude was approximately \$10 per boe. The differential resulted in foregone revenues during the current quarter. The primary source for the medium crude is from a property purchased during April, 2004. Therefore, the prior year's first

Management's Discussion & Analysis

quarter revenues do not include revenues from medium crude. The final factor affecting revenues is that the Corporation assumed a sales agreement in December, 2004 as part of an acquisition. The contract price is based upon a pooled price that is partially based upon resale prices that the purchaser sells to unrelated parties. This has resulted in below fair market prices as a result of this sales agreement. The Corporation has given notice that it intends to terminate the sales agreement effective November 1, 2005.

There were increased general and administrative expenses as a result of the hiring of additional technical staff.

There were increased interest charges as a result of increased indebtedness during the first quarter of 2005. The \$10 million subordinated debt outstanding at December 31, 2004 was retired on March 29, 2005.

The increased non-cash expenses are primarily due to two reasons. First, there is a one-time charge for the amortization of the financing fees related to the subordinated debt. Second, the corporation owns more assets resulting in an increased depletion provision.

Production expenses per boe were as follows:

<i>Period Ended</i>	<i>Period ended March 31, 2005</i>	<i>Period ended March 31, 2004</i>	<i>Period ended March 31, 2005 (\$ / boe)</i>	<i>Period ended March 31, 2004 (\$ / boe)</i>	<i>Percent Change (\$ / boe)</i>
Production Expenses	\$ 2,000,190	\$ 900,231	\$ 10.31	\$ 9.58	8%

Net revenues per boe were as follows:

<i>Period Ended</i>	<i>Period ended March 31, 2005</i>	<i>Period ended March 31, 2004</i>	<i>Period ended March 31, 2005 (\$ / boe)</i>	<i>Period ended March 31, 2004 (\$ / boe)</i>	<i>Percent Change (\$ / boe)</i>
Gross Revenue	\$ 7,932,681	\$ 3,762,921	\$ 40.88	\$ 40.03	2%
Royalties	984,507	684,760	5.07	7.28	(30%)
Production Expenses	2,000,190	900,231	10.31	9.58	8%
Net Revenue	\$ 4,947,984	\$ 2,177,930	\$ 25.50	\$ 23.17	10%

General and Administrative Expenses

<i>Period Ended</i>	<i>Period ended March 31, 2005</i>	<i>Period ended March 31, 2004</i>	<i>Period ended March 31, 2005 (\$ / boe)</i>	<i>Year ended March 31, 2004 (\$ / boe)</i>	<i>Percent Change (\$ / boe)</i>
General & Administrative Expenses	\$ 786,695	\$ 509,619	\$ 4.05	\$ 5.42	(25%)

Management's Discussion & Analysis

General and administrative expenses have increased in the first quarter of 2005 as compared to the first quarter of 2004 as a result of the certain one time charges related to changes in the Corporation's financing arrangements and increased salary expense due to the strengthening of the Corporation's technical team. General and administrative expenses on a per boe basis have decreased by 25% attributable to increased production. The Corporation expects this trend to continue as additional production is added to the production base.

Interest Expense

<i>Period Ended</i>	<i>Period ended March 31, 2005</i>	<i>Period ended March 31, 2004</i>	<i>Period ended March 31, 2005 (\$ / boe)</i>	<i>Period ended March 31, 2004 (\$ / boe)</i>	<i>Percent Change (\$ / boe)</i>
Interest Expenses	\$ 351,678	\$ 72,771	\$ 1.81	\$ 0.77	135%

Interest expense for the period ended March 31, 2005 consists of Interest on the revolving line of credit for \$167,615, interest on the Subordinated Debt for \$161,091, and a preferred share dividend for \$22,972. The dividend is considered interest for accounting purposes. The higher interest expense for the period ended March 31, 2005 as compared to the period ended March 31, 2004 is due to higher indebtedness for 2005. On March 29, 2005 the Corporation retired its subordinated debt. The retirement is expected to result in a decreased interest expense for future periods.

Non Cash Items

<i>Period Ended</i>	<i>Period ended March 31, 2005</i>	<i>Period ended March 31, 2004</i>	<i>Period ended March 31, 2005 (\$ / boe)</i>	<i>Period ended March 31, 2004 (\$ / boe)</i>	<i>Percent Change (\$ / boe)</i>
Depletion and Amortization	\$ 2,040,000	\$ 673,000	\$ 10.52	\$ 7.16	47%
Accretion Expense	90,390	20,000	\$0.47	0.21	124%
Stock Based Compensation	155,000	215,000	\$0.80	2.29	(65%)
Financing Fee Amortization	2,969,500	-	15.31	-	N/A
Total Non Cash Items	\$ 5,254,890	\$ 908,000	\$ 27.09	\$ 9.66	180%

Depletion, amortization, and accretion expense for the first quarter of 2005 is high due to the amortization of deferred financing charges. This is a one-time charge that will not occur in future periods.

Management's Discussion & Analysis

Management performed and the external auditors reviewed a ceiling test calculation to assess the recoverability of its petroleum and natural gas assets as at March 31, 2005. The calculation supported the Corporation's carrying value.

Financial Condition

	<i>March 31, 2005</i>	<i>December 31, 2004</i>
Current Assets	\$ 4,489,156	\$ 3,286,086
Current Liabilities	\$ 11,065,895	\$ 21,449,670
Oil and gas properties	\$ 65,595,240	\$ 64,308,278

The increased current assets balance is due to additional revenues as a result of increased production activity in the first quarter of 2005. The decreased current liabilities balance is due to the retirement of the subordinated debt on March 29, 2005. The working capital deficiency at March 31, 2005 is \$6,576,739 as compared to \$18,163,584 at December 31, 2004.

Capitalized resource properties as at March 31, 2005 are \$65,595,240 net of depletion, compared with \$64,308,278 as at December 31, 2004. Oil and gas properties increased as a result of continued development of oil and gas properties.

Liquidity and Capital Resources

The Corporation's share capital is as follows:

Common Shares

<i>Date</i>	<i>Shares Outstanding</i>	<i>Dollar Value</i>
March 31, 2005	52,321,172	\$ 31,877,606
December 31, 2004	42,008,611	\$ 20,780,818

During the period ended March 31, 2005 the Corporation issued 3,366,361 flow through shares for net cash proceeds of \$4,502,774. Of these net proceeds, approximately \$94,000 has been recorded as part of contributed surplus as an estimate of the fair market value of agent's options granted as part of the share issuance. The Corporation also issued 6,561,200 common shares for net cash proceeds of \$7,756,501. Of these net proceeds, approximately \$1,595,000 has been recorded as part of contributed surplus as an estimate of fair market value for agent's options and warrants granted as part of the share issuance. There were also 343,000 warrants and 42,000 options exercised during the current period for proceeds of \$388,400.

As a result of flow through shares issued during the 2004 year, the Corporation is required to incur exploration and development activities by December 31, 2005 of approximately \$13,915,600. As a result of flow through share issuance during the current quarter the Corporation is required to incur exploration and development activities by December 31, 2006 of approximately \$4,731,000.

Management's Discussion & Analysis

During the prior year the Corporation obtained permission from the TSX Venture Exchange for a Normal Course Issuer Bid to repurchase for cancellation up to 250,000 common shares to April 22, 2005. During the period ended March 31, 2005, 249,400 common shares were purchased.

Subsequent to March 31, 2005, the Corporation obtained permission from the TSX Venture Exchange for a Normal Course Issuer Bid to repurchase for cancellation up to 2,500,000 common shares to April 24, 2006.

Preferred Shares

Date	Series	Shares Outstanding	Dollar Value
March 31, 2005	Series I to V	1,148,641	\$ 1,148,641
December 31, 2004	Series I to V	1,148,641	\$ 1,148,641

Cash Flow from Operations

For the year ended March 31, 2005, the Corporation has generated cash flows from operations of \$3,809,611 (\$1,494,740 for the period ended March 31, 2004).

Cash flow from operations ("Cash Flow"), representing cash generated from operating activities before changes in non-cash working capital items, is a non-GAAP measure. Management utilizes Cash Flow as a key measure to assess the ability of the Corporation to finance operating activities and capital expenditures. Additionally, Cash Flow has been described and presented in order to provide shareholders and potential investors with information regarding the Corporation's liquidity and its ability to generate funds to finance its operations. This performance indicator may not be comparable to similar measures used by other companies.

The following table reconciles the non-GAAP financial measure "cash flow from operations".

<i>Period Ended</i>	<i>March 31, 2005</i>	<i>March 31, 2004</i>
Net income (loss) for the period	\$ (993,724)	\$ 351,540
Future tax provision (recovery)	(451,555)	235,200
Accretion expense	90,390	20,000
Stock based compensation	155,000	215,000
Depletion and amortization	5,009,500	673,000
Cash flow from operations	\$ 3,809,611	\$ 1,494,740

Off-Balance Sheet Arrangements

The Corporation has entered into a 3 way collar financial gas contract with delivery between November, 2004 and October, 2005 of 365,000 GJ with a price cap of \$8.95 per GJ and a price floor of \$6.00 per GJ. At March 31, 2005 there are 214,000 GJ remaining for delivery on this contract. The Corporation

Management's Discussion & Analysis

has also entered into various fixed-price financial oil contracts with delivery for 2005 of 73,000 barrels at prices between \$35.35 and \$36.65 per barrel. At March 31, 2005 there are 55,000 barrels remaining for delivery on this contract.

The purpose of these contracts is to ensure a minimum level of cash flow for continued operations, and, as such, have been accounted for as hedges in accordance with CICA guidelines.

Transactions with Related Parties

- (a) The Corporation entered into transactions with the following related parties:
- Capital Strategies Canada Corp., controlled by the officers of the Corporation
 - Rhodes Resources Corp., related due to common control
 - Rhodes Resources Inc., related due to common control
 - Rhodes Petroleum Corp., related due to common control
 - Terra Capital Corp., parent company
 - Forterra Properties Inc., related due to common control
 - Pioneer Land Services Ltd. – a director, is an employee of Pioneer
 - Borden Ladner Gervais LLP – a director is a partner with the law firm

- (b) Transactions

<i>Three month period ended March 31st</i>	<i>2005</i>	<i>2004</i>
Expenses		
Management fee – Terra Capital Corp. (i) (ii)	\$ 18,000	\$ 327,883
Consulting – Pioneer Land Services Ltd. (i)	9,642	-
Legal Consulting – Borden Ladner Gervais LLP (i)	55,287	-
	\$ 82,929	\$ 327,883
Other		
Recorded as part of Oil and Gas Properties – Terra Capital Corp.(iii.)	\$ 60,000	-
Recorded as part of Oil and Gas Properties – Pioneer Land Services Ltd. (iv.)	62,491	-
Recorded as part of Share issuance cost – Borden Ladner Gervais LLP (v.)	109,732	-
	\$ 232,223	-

- (i) Revenue and expense transactions are in the normal course of operations and have been valued in these consolidated financial statements at the exchange amount which is the amount of consideration established and agreed to by the related parties.
- (ii) Management fees have been paid to Terra Capital Corp. for management personnel services, vehicles, office furniture and equipment leasing. Prior to the amalgamation and up to March 31,

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2004 all personnel were employees of Terra Capital Corp. Subsequent to amalgamation, new employment contracts were implemented with all employees and effective April 1, 2004 employees were paid by the Corporation. The amount of management fees relating personnel services is approximately \$327,000. Any continuing management fees will be for vehicle, office furniture, and equipment leasing at the rate of \$6,000 per month. All management fees are determined on a cost recovery basis.

- (iii) The \$60,000 paid to Terra Capital Corp. consist of a compressor purchase and has been valued at the exchange amount which is the amount of consideration established and agreed to by the related parties.
- (iv) Amounts paid to Pioneer Land Services Ltd. ("Pioneer") are for Pioneer to act as an agent on the Corporation's behalf for landowner negotiations. The amounts have been valued at the exchange amount which is the amount of consideration established and agreed to by the related parties.
- (v) Amounts paid to Borden Ladner Gervais LLP as for legal services provided for both ongoing activities and share issuances. The amounts have been valued at the exchange amount which is the amount of consideration established and agreed to by the related parties.

Critical Accounting Estimates

In preparing financial statements in accordance with generally accepted accounting principles, management undertakes certain judgments and estimates. Changes in these judgments and estimates could have a material impact on the financial results and condition. The following discussion outlines accounting policies and practices that are critical to determining the Corporation's financial results.

Reserves are critical to several accounting estimates, affecting net income through depletion and the ceiling test calculation. Estimating reserves is very complex, requiring many judgments based on available geological, geophysical, engineering, and economic data. Estimated reserves are also utilized by the Corporation's bank in determining credit facilities. Changes in these judgments could have a material impact on the estimated reserves, and subsequently the Corporation's financial results and financial condition.

Ceiling Test

Under the Canadian Institute of Chartered Accountants (CICA) full cost accounting guidelines, the Company calculates a ceiling test annually whereby the carrying value of petroleum and natural gas properties is compared to estimated future cash flow from the production of proved reserves. The Corporation has early adopted the requirement of CICA Accounting Guideline 16 "Oil and Gas Accounting - Full Cost" ("AcG 16"). The requirements of the guideline were to be followed for all fiscal years beginning on or after January 1, 2004, but early adoption was encouraged.

At March 31, 2005, the Corporation calculated the ceiling test using AcG 16 without any material adverse impact on the Corporation's financial position or results of operations.

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Asset Retirement Obligation

CICA Handbook Section 3110 – Asset Retirement Obligations requires accrued reclamation and abandonment obligations be recognized on the balance sheet by increasing oil and gas properties offset by a liability of an equal amount. Estimates are required to determine the future obligation. The asset and liability are initially measured at fair value, being the discounted future value of the liability, and then capitalized as part of the cost of the asset and subsequently amortized over the life of the asset. The liability then accretes until the retirement obligation is settled.

Litigation

The Corporation is involved in various claims and litigation arising from the normal course of business. While the outcome of these matters is uncertain and there can be no assurance that such matters will be resolved in the Corporation's favor, the Corporation does not currently believe that the outcome of adverse decisions in any pending or threatened proceeding related to these and other matters or any amount which it may be required to pay by reason thereof would have a material adverse effect on its financial position or results of operations.

Change in Accounting Policy

Transportation Costs - Effective for fiscal years beginning on or after October 1, 2003, the CICA issued Handbook Section 1100 "Generally Accepted Accounting Principles" which defines the sources of GAAP that companies must use and effectively eliminates industry practice as a source of GAAP. In prior years, it had been industry practice for companies to net transportation charges against revenue rather than showing transportation charges as a component of operating expense on the consolidated statement of income. Effective January 1, 2003, the Company has recorded revenue gross of transportation charges and has recorded transportation charges as an operating expense on the consolidated statement of income. This adjustment of \$163,971 for the period ending March 31, 2004 has no impact on net earnings, per common share calculations, or cash flow for the Company.

Financial Instruments

The Corporation results are impacted by external market risks associated with fluctuations in commodity prices, operational and safety and environmental risks. The Corporation partially mitigates its exposure to market risks through the use of various financial instruments and physical contracts.

The Corporation does not utilize derivative instruments for speculative purposes.

Business Acquisitions

On January 30, 2004, Terrapet amalgamated with Rhodes Resources Corp. ("Rhodes") and Terra Energy Corp. to form a new company Terra Energy Corp ("Terra"). The common shareholders of Terrapet Energy Corp. received 18,547,304 common shares of Terra, with the Series VI preferred shareholders of Terrapet receiving 3,429,752 common shares of Terra. The shareholders of Rhodes received 5,345,944 common shares of Terra. The share allocation has been based upon the relative valuations for oil and gas properties as determined by independent evidence adjusted for various other assets and liabilities. The purchase increased oil and gas properties by approximately \$2.4 million. Oil and gas reserves have

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increased by approximately 271,000 barrels equivalent as compared to Terrapet's reserves. The amalgamation constitutes a reverse takeover as defined by Policy 5.2 of the TSX-V and is subject to Policy 5.9 of the TSX-V regarding related party transactions. The transaction will be recorded at the exchange value of the assets received from Rhodes as there is sufficient independent evidence available and there is a substantive change in the ownership interests.

On December 28, 2004 the Corporation purchased all of the outstanding shares of Fossil Bay Resources Ltd. ("Fossil Bay"), through a wholly owned subsidiary, Terra Resources Inc. ("Terra Resources"). Fossil Bay and Terra Resources immediately amalgamated to form Terra Resources Inc. Terra Resources Inc. was then wound up into Terra Energy Corp. The consideration paid consisted of the issuance of 616,113 common shares and cash of \$255,000. The assets of Fossil Bay consisted primarily of certain oil and gas properties and non-capital loss carryforwards that can be utilized by Terra Energy Corp.

On December 31, 2004 the Corporation acquired certain oil and gas properties from another company for consideration of \$31,547,844 in cash. The purchase resulted in additional proven and probable reserves of 2.8 million barrels equivalent. The properties comprise approximately 75 sections of developed and undeveloped lands which complement the Company's existing core properties of Stoddart and Boudreau. These properties are currently producing approximately 840 barrels equivalent comprised of 4,100 Mcf/d of natural gas and 170 bbls/d of oil and condensate. The acquisition includes primarily operated properties with significant facilities and pipeline infrastructure. Most of the properties have year round access. The acquisition also includes a significant amount of 2-D and 3-D seismic information.

OUTLOOK 2005

The primary focus of the Company during 2005 will be on the growth of its reserves base. The Company is targeting an exit rate of 4,000 boe/d for 2005, excluding any corporate and major property acquisitions. As some of the development drilling will be directed towards opportunities which will simply change the category of reserves from Non-Producing or Probable into the Proved Producing category, the aggressive exploration program is intended to ensure that our Total Proved + Probable reserves will increase at least in proportion to our overall production rate.

DETAILS

Below is a summary of our forecasted activity for the year. Terra Energy is planning to drill 15 (gross) wells in northeast British Columbia and the remaining 13 (gross) wells in Alberta and Saskatchewan. Based upon success and upon an increase in the Budget by the Board of Directors, many follow-up locations will be drilled to increase the reserves and the production in the latter part of the year and into 2006. The specific details of our CAPEX Plan cannot be disclosed for competitive reasons, but the general highpoints are as follows:

Fort St. John, British Columbia

Fort St. John is the Company's Core Area, and it is comprised of several fields. Starting with the Eagle Field, and moving in a counter-clockwise fashion, are the Stoddart Field, the Red Creek Field, the Boudreau Field, the Wilder/Monias Field, the Septimus Field, the Tower Field, the Eight Mile Field and the Mica Field.

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Eagle

Terra Energy is planning three wells for the Eagle Field in 2005. These wells are predominantly development wells offsetting production from the Halfway and Belloy formations in the area. The Company has working interests ranging from 22% to 100%.

Stoddart

Terra Energy is planning only modest capital expenditures at Stoddart. Work will be carried out to convert an existing suspended well into a water disposal well for use in conjunction with our oil battery and plant site.

Red Creek

At Red Creek, Terra Energy will drill one (100%) exploratory well targeting a new horizon which appears to be prospective. If successful, the Company will benefit from already having tremendous infrastructure in place for handling production. In addition, the Company will re-complete two existing wells (100%) to increase current production rates.

Boudreau

Terra Energy will drill and/or re-enter as many as four wells in 2005, to pursue Charlie Lake, Belloy, Baldonnel and Halfway potential. There are plans to re-complete as many as two wells to further optimize production from this field. The Company has various interests in this field ranging from 50% to 100%.

Monias/Wilder

The Company is targeting several recompletions in the Monias/Wilder area. The field is located on an anticline and has seen production from five different formations, including the Halfway, Charlie Lake and Belloy. The Company plans to shoot a 2D seismic program across two sections which it owns in order to firm up locations for the 2006 winter drilling season.

Septimus

The secondary target in this play is the Halfway formation. There is current production offsetting our lands and our technical analysis indicates a very favourable chance of encountering the same or similar Halfway reservoir. Our first well, the 15-34-81-19W6M, is located on the apex of a seismically defined anticline, structurally higher than the offsetting producer. Our primary target and tertiary targets make this an exciting opportunity. Upon success, the Company will proceed with the construction of a new gathering line which will tie the field into the production facilities at Monias/Wilder, and the Company will proceed with two additional development wells into the same reservoir. There will be secondary targets associated with these drilling operations.

Tower

Terra Energy is licensing a well in Section 25-81-17W6M with the Halfway formation as its secondary target. There is currently offsetting Halfway production both east and west of the Company's lands. The primary target is confidential and there are several tertiary targets for this well. Based upon success, as many as three follow up wells may be drilled during 2005. Infrastructure is available in the immediate vicinity.

Eight Mile

Terra Energy has several exploration plays across its Eight Mile acreage. The field consists of 30 sections of land (predominantly 100%), with offsetting production in two different horizons. The Company is

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planning four exploration wells during 2005. With success, there is potential for several development wells in 2006.

Mica

The Company has plans to recomplete one well during 2005. Depending upon further investigations an additional well may be drilled targeting a new horizon which is prospective.

Grande Prairie, Alberta

Terra Energy will follow up its 2004 drilling program with three additional wells and one re-entry in 2005. The Company has an undeveloped land position of nine sections (60% to 100%) in this area. The Company will license a well for Section 15-71-6W6M, which will target no fewer than three different horizons.

Heathdale, Alberta

At Heathdale, the Company has an undeveloped land position of ten sections of land, in addition to its developed lands and production. The Company is targeting three wells in Heathdale for 2005, with multiple zones being targeted in each well.

Tableland, Saskatchewan

Terra Energy has four separate Winnipegosis reef structures which have been identified on its lands with the benefit of 3D seismic which was shot during 2004. These four structures are proximal to existing oil pools.

Bow Island, Alberta

Terra Energy is planning to drill one well in Bow Island targeting the Sawtooth and the Bow Island formations. The Company is also planning to tie-in two gas wells in this field.

Certain statements contained in the above Management's Discussion and Analysis, including, without limitation, statements containing the words believes, anticipates, estimates, expects, and words of similar import, constitute forward-looking statements. Forward looking statements are not guarantees of future performance and involve risks and uncertainties, which could cause actual results to differ materially from those anticipated in these forward-looking statements. Among the key factors that could cause such differences are: fluctuations in petroleum and natural gas prices, and/or changes in petroleum and natural gas reservoir performance.

We disclaim any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, unless required to do so by applicable securities law.

Consolidated Balance Sheet

As at March 31, 2005
(Unaudited, prepared by Management)

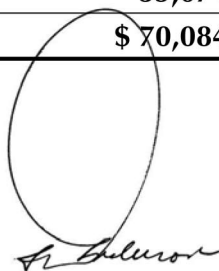
	March 31, 2005 (unaudited)	December 31, 2004 (audited) (Note 1)
Assets		
Current Assets		
Accounts receivable	\$ 3,783,173	\$ 2,397,420
Income taxes receivable	-	28,801
Prepaid expenses	705,983	859,865
	4,489,156	3,286,086
Non Current Assets		
Oil and gas properties	65,595,240	64,308,278
Deferred financing costs	-	2,969,500
	\$ 70,084,396	\$ 70,563,864
Liabilities and Shareholders' Equity		
Current Liabilities		
Bank overdraft	\$69,230	\$295,529
Accounts payable and accrued liabilities	10,996,665	11,154,141
Subordinated debt (Note 4)	-	10,000,000
	11,065,895	21,449,670
Non Current Liabilities		
Revolving line of credit	14,716,518	15,862,373
Asset retirement obligations	4,111,533	4,021,143
Future income taxes	3,967,121	4,816,300
Preferred shares	1,148,641	1,148,641
	35,009,708	47,298,127
Shareholders' Equity		
Share capital (Note 5)	31,877,606	20,780,818
Contributed Surplus (Notes 5(d) and 6)	5,902,079	4,196,192
Deficit	(2,704,997)	(1,711,273)
	35,074,688	23,265,737
	\$ 70,084,396	\$ 70,563,864

Commitments and Contingencies (Note 8)

Approved on behalf of the Board:



Robert Penner, Director



Ted Anderson, Director

Consolidated Statement of Income (Loss)

As at March 31, 2005
(Unaudited, prepared by Management)

	For the three months ended March 31	
	2005	2004
Revenue		
Petroleum and natural gas	\$ 7,932,681	\$ 3,762,921
Royalties and production taxes	(984,507)	(684,760)
	6,948,174	3,078,161
Expenses		
Production	2,000,190	900,231
Amortization and depletion	2,040,000	673,000
Financing fee amortization (Note 4)	2,969,500	-
General & administrative	786,695	509,619
Stock based compensation	155,000	215,000
Interest charges (Note 7)	351,678	72,771
Accretion	90,390	20,000
	8,393,453	2,390,621
Income (loss) before income taxes	(1,445,279)	687,540
Income taxes (recovery)		
Current provision	-	100,800
Future provision (recovery)	(451,555)	235,200
	(451,555)	336,000
Net Income (loss) for the period	\$(993,724)	\$351,540
Earnings (loss) per common share – basic and diluted	\$(0.02)	\$0.01
Weighted average number of shares outstanding - basic	49,499,711	24,429,913
Weighted average number of shares outstanding - diluted	51,284,179	26,972,668

Consolidated Statement of Deficit

As at March 31, 2005

(Unaudited, prepared by Management)

	For the three months ended March 31	
	2005	2004
Deficit, beginning of period	\$ (1,711,273)	\$ (2,026,546)
Net Income (loss) for the period	(993,724)	351,540
Dividends	-	(770,816)
Deficit, end of period	\$ (2,704,997)	\$ (2,445,822)

Consolidated Statement of Cashflows

As at March 31, 2005
(Unaudited, prepared by Management)

	For the three months ended March 31	
	2005	2004
Cash flows from operating activities		
Net income (loss) for the period	\$ (993,724)	\$ 351,540
Items not affecting cash:		
Amortization and depletion	2,040,000	673,000
Future income taxes	(451,555)	235,200
Stock based compensation	155,000	215,000
Accretion	90,390	20,000
Financing fee amortization	2,969,500	-
	3,809,611	1,494,740
Net change in non-cash working capital balances	(3,510,363)	(459,713)
	299,248	1,035,027
Cash flows from financing activities		
Issuance of share capital, net of share issuance costs	12,268,935	-
Repayment of revolving line of credit	(1,145,855)	(1,186,405)
Repayment of subordinated debt	(10,000,000)	-
	1,123,080	(1,186,405)
Cash flows from investing activities		
Acquisition of oil and gas properties	(1,196,029)	(2,473,305)
Interest on note receivable		(72,540)
Due from related party		15,000
Cash assumed on acquisition of Rhodes Resources Corp.		2,502,459
	(1,196,029)	(28,386)
Increase (decrease) in cash and cash equivalents	226,299	(179,764)
Cash and cash equivalents (bank overdraft), beginning of period	(295,529)	512,051
Cash and cash equivalents (bank overdraft), end of period	\$ (69,230)	\$ 332,287

Notes to Consolidated Financial Statements

March 31, 2005

(Unaudited, prepared by Management)

***note 1* NATURE OF OPERATIONS**

Terra Energy Corp. (the "Corporation") was formed on January 30, 2004 as a result of the amalgamation of Rhodes Resources Corp. ("Rhodes"), Terrapet Energy Corp. ("Terrapet"), and Terra Energy Corp. ("Terra") pursuant to the Business Corporations Act of Alberta. The amalgamated Corporation operates under the name Terra Energy Corp. The Corporation's principal business is the exploration, development, and production of oil and natural gas.

The amalgamation has been recorded as a reverse takeover by Terrapet and the comparative financial statements represent a continuation, for accounting purposes, of the financial statements of Terrapet and its subsidiaries ("Terrapet Consolidated").

***note 2* SIGNIFICANT ACCOUNTING POLICIES**

The interim consolidated financial statements of Terra Energy Corp. have been prepared by management in accordance with Canadian generally accepted accounting principles. The interim consolidated financial statements have been prepared following the same accounting policies and methods of computation as the financial statements for Terra Energy Corp. for the year ended December 31, 2004. The interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements of Terra Energy Corp. and the notes thereto for the year ended December 31, 2004.

***note 3* COMPARATIVE PERIOD AMENDMENT**

During the second quarter of the prior year, the Corporation revisited its first quarter calculations related to stock based compensation expense and determined that an adjustment of \$196,200 was required for the first quarter. This resulted in an increase in the first quarter compensation expense for \$18,800 to \$215,000 and a decrease in the first quarter income from \$547,740 to \$351,540.

***note 4* SUBORDINATED DEBT**

During the period, the Corporation had available a standby mezzanine financing credit facility of up to \$10.0 million, with an interest rate of 10% per annum.

At March 31, 2005, the facility was repaid in full. As a result of the repayment related deferred financing fees of \$2,969,500 have been recorded as an expense in the current period.

The subordinated debt proceeds were used to purchase certain properties.

Notes to Consolidated Financial Statements

March 31, 2005

(Unaudited, prepared by Management)

note 5 SHARE CAPITAL

a) Authorized

- i) Unlimited number of common voting shares
- ii) Unlimited number of preferred shares

b) Common Shares Issued

	Number	Amount
Balance, December 31, 2004	42,008,611	\$ 20,780,818
Issued on exercise of warrants	343,000	344,600
Issued on exercise of options	42,000	43,800
Issued pursuant to a flow through share agreement, net of tax effected share issuance costs	3,366,361	4,409,211
Issued pursuant to share placement agreement net of tax effected share issuance costs, at \$1.25 per share	6,561,200	6,161,178
Reclassification of contributed surplus amounts	-	138,000
Balance, March 31, 2005	52,321,172	\$ 31,877,606

The Corporation obtained permission from the TSX Venture Exchange for a Normal Course Issuer Bid to repurchase for cancellation up to 250,000 common shares to April 22, 2005. During the period ended March 31, 2005, 249,400 common shares were purchased. No amounts were repurchased subsequent to March 31, 2005.

c) Stock Options:

The Corporation has adopted an Employee Stock Option Plan whereby officers, directors, employees, and consultants may be granted options of up to 3,000,000 to purchase common shares of the Corporation subject to various vesting periods and other terms and conditions specified in the stock option plan. At March 31, 2005 options have been granted to purchase 2,721,000 common shares (December 31, 2004 – 2,483,000) ranging at prices between \$0.75 and \$1.15 with an expiry date of February 11, 2009.

Notes to Consolidated Financial Statements

March 31, 2005

(Unaudited, prepared by Management)

note 5 SHARE CAPITAL (continued)

Details of all options outstanding are as follows:

	Number	Weighted Average Exercise Price
Employee Stock Options		
Balance December 31, 2004	2,483,000	\$ 0.98
Granted under the stock option plan in the current period	400,000	1.15
Exercised during the current period	(42,000)	(1.04)
Expired during the current period	(120,000)	(1.15)
Employee Stock Options Balance, March 31, 2005	2,721,000	1.00
Agent Options		
Balance December 31, 2004	1,054,216	1.32
Granted as part of share issuance. These options will expire January 26, 2007	694,929	1.40
Agent Options Balance, March 31, 2005	1,749,145	1.35
Other Options		
Balance December 31, 2004	329,730	1.21
Other Options Balance, March 31, 2005	329,730	1.21
Total Options Balance March 31, 2005	4,799,875	\$ 1.07

Options Exercise Price	Weighted Average Remaining Contract Life	Outstanding March 31, 2005	Weighted Average Share Price for Outstanding Options	Exercisable March 31, 2005	Weighted Average Share Price for Exercisable Options
\$0.75	3.88 years				
1.00	3.88 years	2,123,000		872,000	
1.00	0.75 years	210,936		210,936	
1.15	4.70 years	400,000		80,000	
1.21	1.75 years	329,730		329,730	
1.40	1.42 years	241,500		241,500	
1.40	1.75 years	601,780		601,780	
1.40	1.83 years	694,929		694,929	
	2.46 years	4,799,875	\$ 1.07	3,228,875	\$ 1.15

Notes to Consolidated Financial Statements

March 31, 2005

(Unaudited, prepared by Management)

note 5 SHARE CAPITAL (continued)

d) Stock-based compensation

For stock options granted to employees compensation expense of \$155,000 has been recorded for the period ending March 31, 2005 (\$216,000 – March 31, 2004) with the offsetting charge to contributed surplus. The fair value of share options was estimated using the Black-Scholes option-pricing model with the following assumptions: Dividend yield (Nil); expected volatility at 50%; risk-free interest rate of 3.5%; weighted average life of 5 years.

e) Warrants

During the period ended March 31, 2005 the Corporation issued the following warrants:

- i) 3,280,600 warrants exercisable to purchase one-half common share at \$1.40 per share until January 26, 2006 and at \$1.60 per share until January 26, 2007 when these warrants expire.

note 6 CONTRIBUTED SURPLUS

Contributed Surplus consists of the fair value of both share warrants issued for various financing agreements and for the stock based compensation on employee stock options. Values were determined using the Black Scholes Model using the assumptions of no dividends being paid; risk free interest rate of 4%; and an expected volatility of 50%.

The details of contributed surplus are as follows:

	Amount
Balance, December 31, 2004	\$ 4,196,192
Stock based compensation provision for the period	155,000
Deemed issue costs of agent's options granted during the period [Note 5(c)]	275,924
Deemed issue costs of warrants granted during the period [Note 5(e)]	1,412,963
Reclassification resulting from exercise of options and warrants	(138,000)
Balance, March 31, 2005	\$ 5,902,079

Notes to Consolidated Financial Statements

March 31, 2005

(Unaudited, prepared by Management)

note 7 INTEREST CHARGES

Interest charges consist of the following amounts:

Period ended March 31, 2005	2005	2004
Interest on revolving line of credit	\$ 167,615	\$ 72,771
Interest on preferred share	22,972	-
Interest on subordinated debt	161,091	-
	\$ 351,678	\$ 72,771

note 8 COMMITMENTS AND CONTINGENCIES

- (a) The Corporation had outstanding letters of credit to various parties for a total of \$879,000. Of these amounts \$754,000 will expire at various dates during 2005 and the remaining 125,000 expire at various dates during 2006.
- (b) The Corporation is currently involved in litigation with an industry participant who is claiming \$685,850 in respect of an alleged breach of contract arising from a failure to pay on account of Authorizations for Expenditures relating to the development of certain lands and pipelines. The Corporation is contesting this claim and has issued a counterclaim in respect of the same subject. It is management's opinion that an adequate provision has been recorded in these consolidated financial statements. Additional amounts, if any, required to resolve these matters, will be recorded in the period of settlement or when management changes its estimate of an adequate provision.
- (c) The Corporation is currently involved in litigation with three registered landowners who are claiming \$85,000 in respect of breach of contract and trespass arising from pipeline construction and related operation and carried on by the Corporation on or near land owned by the plaintiffs. The Corporation is contesting this claim. No provision has been recorded in these consolidated financial statements. Additional amounts, if any, required to resolve these matters, will be recorded in the period of settlement or when management can reasonably assess the likelihood and balance of amounts owing, if any.
- (d) The Corporation is currently involved in litigation brought by an industry participant relating to a claim of ownership or equitable ownership in a natural gas lease covering a one-quarter Section of land. The Corporation is contesting this claim. No provision has been recorded in these consolidated financial statements. Additional amounts, if any, required to resolve these matters will be recorded in the period of settlement or when management changes its estimate of an adequate provision.

Notes to Consolidated Financial Statements

March 31, 2005

(Unaudited, prepared by Management)

note 8 COMMITMENTS AND CONTINGENCIES (continued)

- (e) The Corporation has entered into contracts to hedge commodity prices and deliver petroleum and natural gas. The terms of the contracts are summarized as follows:

Contract Type	Floor Price	Ceiling Price	Remaining Volume	Contract Term
Financial	\$6.00 per GJ Floor with Protection of \$1.00 per GJ	\$8.95 per GJ	214,000 GJ	November 1, 2004 to October 31, 2005
Financial	\$35.35	N/A	27,500 bbl	January 1, 2005 to December 31, 2005
Financial	\$36.65	N/A	27,500 bbl	January 1, 2005 to December 31, 2005

N/A – not applicable

The amount that the Corporation would be required to pay if all the contracts were cancelled at March 31, 2005 would approximate \$1,638,000 (December 31, 2004 - \$833,334).

- (f) The Corporation has available a financial swap facility of up to \$3 million. The Corporation may enter commodity swap contracts with terms of less than one year and may not exceed 2/3 of the Corporation's average daily production, net of royalties, for the fiscal quarter prior to the date the contract is entered into. The facility is secured by a general security agreement; a floating charge debenture in the amount of \$35 million and an unlimited liability guarantee by the Corporation and its subsidiaries. At March 31, 2005 (December 31, 2004 - \$nil) there were no outstanding swap contracts.
- (g) The Corporation is required to incur exploration and development activities by December 31, 2005 of approximately \$13,915,600 as a result of flow through shares issued in 2004. As at March 31, 2005, the Corporation has incurred qualifying expenditures of approximately \$2,848,000.
- (h) The Corporation is required to incur exploration and development activities by December 31, 2006 of approximately \$4,713,000 as a result of flow through shares issued in 2005. As at March 31, 2005, the Corporation has not incurred any qualifying expenditures.

note 9 SUBSEQUENT EVENT

Subsequent to the period end, the Corporation obtained permission from the TSX Venture Exchange for a Normal Course Issuer Bid to repurchase for cancellation up to 2,500,000 common shares to April 24, 2006.

Notes to Consolidated Financial Statements

March 31, 2005

(Unaudited, prepared by Management)

note 10 COMPARATIVE FIGURES

Prior year comparative figures have been reclassified to conform to the presentation used in the current year.

Corporate Information

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Borden Ladner Gervais LLP, Calgary, Alberta

Auditor

BDO Dunwoody LLP, Calgary, Alberta

Evaluation Engineers

McDaniel & Associates Consultants Ltd., Calgary, Alberta
Status Engineering Associates Ltd., Calgary, Alberta
Ryder Scott Company, Calgary, Alberta

Banker

CIBC, Calgary, Alberta

Transfer Agent

Computershare Trust Company
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Shareholders are encouraged to contact our Registrar and Transfer Agent for information regarding their securities holdings.

Stock Exchange

TSX-Venture

Stock Symbol

TTR

Investor Contact

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TSX Venture: **TTR**