

**CHESSWOOD INCOME FUND**

**INTERIM CONSOLIDATED FINANCIAL  
STATEMENTS**

**FOR THE THREE-MONTHS ENDED**

**MARCH 31, 2008 AND 2007**



## **CHESSWOOD INCOME FUND**

### **NOTICE TO READERS**

Accompanying this notice are the unaudited interim consolidated financial statements of the Fund for the three-months ended March 31, 2008 and 2007. These statements have been prepared by, and are the responsibility of, the Fund's management.

Following consultation with management and with the Fund's independent auditors, the Fund's board of trustees concluded that the auditors would not be engaged to perform a review of these financial statements. Under applicable securities legislation, there is no requirement that auditors be engaged to review these statements, but the Fund must advise you if (as noted above) no review engagement is made.

## **TO OUR UNITHOLDERS**

Our first quarter of 2008 unfolded largely as expected in our U.S. business, Pawnee Leasing Corporation, while our Canadian business posted results that were stronger than expected.

Pawnee continued to experience high charge-offs and elevated delinquency levels in its portfolio, as expected. At the same time, Pawnee's strong brand and deep broker community relationships continued to provide increased levels of new applications compared to the same period a year ago. Notwithstanding the strong new application flow, the company's approval levels have remained below traditional levels as we continue to be selective in a difficult credit environment.

Charge-offs in excess of last year generate an increase in our allowance for bad debts, further increasing the actual amount we expense at Pawnee, as our provision for credit losses. This portion of the increase in the provision for credit losses, while a non-cash expense, diminishes the amounts Pawnee can provide to Chesswood but results in Pawnee increasing its debt repayment.

While we paid distributions in the quarter that exceeded our distributable cash, a large portion of the total amount distributed was matched by positive cash flow generated at and retained by Pawnee, for debt repayment. As a result we repaid \$2.5 million of lease financing during the quarter. We believe that's a testament to Pawnee's strong business model.

Our new car dealership enjoyed the best first quarter in its history due primarily to the aggressive programs offered by our manufacturer. With a Canadian dollar that has been at or near par with the U.S. dollar since late in 2007, most auto manufacturers offered Canadian consumers significant discounts in order to offset often sizable differences in the price of a new car in the U.S. versus the price of that same car in Canada.



Barry Shafran  
President & CEO

## **FUND PROFILE**

Chesswood Income Fund ("Chesswood" or the "Fund") is an unincorporated, open-ended, limited purpose trust established under the laws of the Province of Ontario pursuant to a declaration of trust. The Fund was created to indirectly acquire, (i) all of the shares in Pawnee Leasing Corporation ("Pawnee"), a Colorado company, and (ii) all of the shares of cars4U Ltd., pursuant to a plan of arrangement under the *Business Corporations Act* (Ontario).

Through its interest in Pawnee, the Fund is involved in the business of micro and small-ticket equipment leasing to small businesses in the start-up and "B" credit market in the lower 48 states of the United States. Through its interests in Lease-Win Limited ("Lease-Win") and Sherway LP, the Fund is involved in leasing automobiles, and selling, servicing and leasing Acura automobiles, in the Province of Ontario.

The Fund's annual report and annual information form for the year-ended December 31, 2007 are available on SEDAR at [www.sedar.com](http://www.sedar.com), and provide additional information on the Fund and its operating companies.

Our units are listed on the Toronto Stock Exchange under the symbol CHW.UN.

## **BUSINESS OF PAWNEE**

Pawnee is an equipment leasing company that provides lease financing on micro and small-ticket business equipment. Pawnee focuses on small businesses in the start-up and "B" credit segment of the U.S. leasing market, servicing the lower 48 states through a network of approximately 550 independent brokers. As of March 31, 2008, Pawnee administered approximately 7,100 leases in its portfolio, with remaining scheduled lease payments of approximately US\$103.5 million over the next five years.

Pawnee finances equipment leases where generally:

- (i) the equipment is fundamental to the core operations of the lessee's business;
- (ii) the cost of the equipment does not exceed US\$30,000;
- (iii) a personal guarantee of at least the major shareholder/owner is obtained and at least one of the guarantors has a strong personal credit history; and
- (iv) all scheduled lease payments are required to be paid by direct debit out of the lessee's account.

Pawnee's business does not involve leasing of consumer goods.

A key aspect of Pawnee's business is managing potential risks in order to limit defaults to the greatest extent possible. Pawnee has developed a number of risk management tools and processes which it continually monitors and improves to match changes in its market and in the equipment leasing industry.

Management believes that Pawnee is the leading micro and small-ticket funding source available to equipment leasing brokers and lessors in the start-up equipment leasing market in the U.S. and is a well-recognized player in the "B" credit market. Pawnee's success in its higher risk niche markets is due to Pawnee's ability to select creditworthy businesses through its proprietary credit analysis matrix and process, and its efficient servicing and collection processes.

The start-up and "B" credit segments of the micro and small-ticket leasing market has historically been, and continues to be, more sensitive to monthly lease payment amounts than to the effective rates.

Pawnee's business model is different from certain other leasing, consumer sub-prime mortgage and finance companies in a number of important respects, including the following:

- unlike sub-prime mortgage companies, Pawnee does not provide funding to the residential consumer, and funds only "business essential" commercial equipment,
- Pawnee does not sell its leases, but rather retains its leases for their full term,
- Pawnee's revenues are derived directly from its leases and are not derived from (and therefore, and more importantly, Pawnee's revenues are not dependent upon) fees from the sale of its portfolio of leases, and
- not only is there significant geographic diversification (within the United States) within Pawnee's portfolio of leases, there is also significant diversification in terms of the equipment funded and significant diversification in terms of the industries in which Pawnee's lessees operate.

Pawnee's revenues and fundings are not dependent upon continuously finding third party buyers for its lease portfolio (where demand is driven by factors such as prevailing interest rates and the quality of other available portfolios and other available investments). Rather Pawnee has a continuing lending facility.

As of March 31, 2008, Pawnee employed approximately 41 full-time equivalent employees, of which over one-third are specifically dedicated to collection and default remediation.

### **LEASE-WIN AND SHERWAY LP**

Founded in 1971, Lease-Win leases predominantly new vehicles of all makes to individual and corporate clients.

Lease-Win currently has approximately 1,660 leases in its portfolio under administration with remaining scheduled lease payments totaling approximately \$50.1 million as at March 31, 2008. Virtually all of Lease-Win's leases are open-ended leases, which limits Lease-Win's exposure to losses where the fair market value of a leased vehicle is less than its residual value at the end of the lease term.

Sherway LP, through its Acura Sherway dealership, sells new Acura brand vehicles and related automobile services and products, and also sells used vehicles of various brands.

The Fund's automotive business follows a seasonal pattern, with revenue and net earnings traditionally being significantly lower in the first quarter than in other quarterly periods.

## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

The following management's discussion and analysis ("MD&A") is a review of the financial condition and results of operations of Chesswood Income Fund ("Chesswood" or the "Fund") for the three-months ended March 31, 2008. This discussion should be read in conjunction with the consolidated financial statements and accompanying notes of the Fund for the three-months ended March 31, 2008, and the audited consolidated financial statements and the notes thereto and the MD&A for the fiscal year ended December 31, 2007 set forth in the Fund's 2007 Annual Report. The financial statements of the Fund are prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). The fiscal year of the Fund ends on December 31. The date of this MD&A is May 14, 2008.

This discussion contains forward-looking statements. Please see "Forward-Looking Statements" for a discussion of the risks, uncertainties and assumptions relating to these statements. This discussion also makes reference to certain non-GAAP measures to assist in assessing the Fund's financial performance. Non-GAAP measures do not have any standard meaning prescribed by GAAP and are therefore unlikely to be comparable to similar measures presented by other issuers. See "Non-GAAP Measures" for the definition of and reconciliation to GAAP measures of EBITDA, Adjusted EBITDA and Distributable Cash.

All dollar amounts in this MD&A are Canadian dollars, unless otherwise indicated.

Our annual information form in respect of the fiscal year ended December 31, 2007 is available on SEDAR at [www.sedar.com](http://www.sedar.com), and provides additional information and should be read in conjunction with this report, management discussion and analysis, financial statements and notes thereto.

## **OVERVIEW**

The Fund is an unincorporated, open-ended, limited purpose trust established under the laws of the Province of Ontario pursuant to a declaration of trust. Through its interest in Pawnee Leasing Corporation ("Pawnee"), the Fund is involved in the business of micro and small-ticket equipment leasing to small businesses in the start-up and "B" credit market in the lower 48 states of the United States. Through its interests in Lease-Win Limited ("Lease-Win") and Sherway LP, the Fund is involved in leasing automobiles and selling, servicing and leasing Acura automobiles in the Province of Ontario.

## **FORWARD-LOOKING STATEMENTS**

In this report, management makes statements that are considered forward-looking statements. Forward-looking information consists of disclosure regarding possible events, conditions or results that is based on assumptions about future economic conditions and courses of action. Wherever used, the words "may", "could", "should", "will", "anticipate", "intend", "expect", "plan", "predict", "believe", and similar expressions identify forward-looking statements. These statements reflect management's current beliefs and are based on information currently available to management, but indicate management's expectations of future growth, results of operations, business performance, and business prospects and opportunities.

Forward-looking statements should not be read as guarantees of future performance or results, and will not necessarily be accurate indications of whether, or the times at which, such performance or results will be achieved. Forward-looking statements are based on information available at the time they are made, assumptions made by management, and management's good faith belief with respect to future events, and are subject to risks and uncertainties that could cause actual performance or results to differ materially from those expressed in forward-looking statements, historical results or current expectations. The Fund assumes no obligation to publicly update or revise its forward-looking statements even if experience or future changes make it clear that any projected results expressed or implied therein will not be realized.

The Fund operates in a dynamic environment that involves various risks and uncertainties, many of which are beyond the Fund's control and which could have an effect on the Fund's business, revenues, operating results, cash flow, distributable cash and financial condition. Readers should carefully review the risk factors in the Fund's annual information form filed with various Canadian securities regulatory authorities through SEDAR (the System for Electronic Document Analysis and Retrieval) at [www.sedar.com](http://www.sedar.com).

## **KEY PERFORMANCE INDICATORS - PAWNEE**

Management regularly evaluates and analyzes the following key performance indicators to more effectively operate Pawnee's business: lease application, approval and origination volume, asset quality, and operating efficiency.

### *Lease Application, Approval and Origination Volume*

Management regularly reviews lease application, lease approval and lease origination volume, for trends that may indicate changes in the economic or competitive landscape that may necessitate adjustments in Pawnee's approach to doing business in its market segment. Pawnee uses this data in its forecasting and budgeting process. Management reviews application approval data to analyze and predict shifts in the credit quality of Pawnee's lease applicants, and looks at individual broker or lessor approval rates to determine whether a broker or lessor is submitting applications that meet Pawnee's credit criteria. Pawnee refers to total lease originations as a percentage of leases approved as the "close ratio". Pawnee tracks and reviews the close ratio to aid management in determining the efficiency and effectiveness of Pawnee's origination processes. Deterioration in any of these key metrics will result in a more detailed review, which may include review of broker, industry or equipment type, equipment cost, or geographic areas for specific results.

### *Asset Quality*

Pawnee is a niche specialty leasing company that is focused on doing business with commercial enterprises that are not normally considered by conventional financing sources and that generally have a higher risk profile. This exposes the firm to a greater risk level; however management has built an operating model that is based on managing this risk. As a result, Pawnee has been able to generate greater margins with lower volume than many typical lease or finance companies.

Risk management begins with carefully selecting which independent brokers Pawnee does business with. All brokers must have personal credit profiles acceptable to Pawnee, industry references and preferably have been active in the equipment leasing industry for a minimum of one year. Two regional marketing managers are responsible for training and developing a knowledge base with new and existing brokers regarding Pawnee's underwriting policies and procedures. This training process is very important in ensuring that neither the broker nor Pawnee spend extraordinary time in reviewing and handling applicants that can't meet Pawnee's basic qualifications. The managers are also responsible for monitoring the brokers for credit application review and closing efficiencies, including applications submitted, approved and ultimately funded.

The Pawnee credit process is not the automated scoring procedure typical of high volume leasing companies. A credit analyst reviews each application and completes a proprietary credit matrix, which is used as a guide for reaching a prudent credit decision manually. The matrix is designed to ensure that all of Pawnee's analysts are consistent in their review of all applications. Analysts are available to directly assist brokers submitting lease applications and communicate credit decisions, including what would make an applicant more likely to be approved. Four basic principles underscore all credit decisions: (i) all business owners must personally guarantee the lease and must therefore submit their personal credit information for consideration; (ii) all scheduled lease payments must be paid through direct debit; (iii) all leases must be on Pawnee's standard proprietary lease documentation; and (iv) all leases assigned to Pawnee must be approved by Pawnee in accordance with the same criteria used in originating its own leases.

### *Operating Efficiency*

Pawnee manages operating performance using a comprehensive budgetary review process. Included in this review are line-item-level comparisons of revenues and expenses to budget and trend data for the period then ended. If management finds there is a significant or unusual variance from budget or expectations, management will review the variance in detail and take corrective action, if necessary. Management regularly updates Pawnee's budget and forecasting model using actual results. Management focuses its attention on significant changes from prior projections and takes appropriate action, as necessary.

Pawnee's static pool loss analysis measures lease loss performance by identifying a finite pool of lease originations and segmenting this pool into discrete monthly, quarterly or annual vintages according to when the leases were originated. Pawnee also monitors static pool performance by broker, equipment type and industry to identify lease loss performance falling outside of expected ranges. Poorly performing brokers, equipment types and industries are reviewed in more detail to determine if there is a systematic or other identifiable cause on which corrective action can be taken. For example, if management determines that Pawnee has unusually high losses on leases for a particular type of equipment, management may raise the minimum required credit matrix score for those leases to be approved or stop originating leases of that equipment type altogether.

## **KEY PERFORMANCE INDICATORS - Lease-Win**

### *Lease Applications and Origination Volumes*

Management regularly reviews lease applications for trends that may indicate changes in the economic or competitive landscape that may necessitate adjustments or changes in Lease-Win's pricing and/or processes. In addition, management tracks, analyzes and compares - to the prior periods and to one another - the volume and margin performance of Lease-Win's leasing sales staff, in order to support and help drive volume and profitability in its vehicle fleet.

### *Credit Profiles*

Lease-Win is an 'A' lessor that provides leasing services to lessees that are of 'A' or higher credit quality, or have guarantors and/or co-lessees of this quality. Notwithstanding this origination requirement, lessee credit profiles can change once a lease has commenced. Lease-Win reviews its accounts receivable aging regularly in order to identify, when possible, potential changes in the creditworthiness of lessees, based primarily on any changes that may appear in payment patterns. It uses this process in order to be proactive in the protection of its leased assets.

### *OEM Lease Pricing and Short and Long-Term Bond Pricing*

Management monitors the lease pricing offered by the vehicle manufacturers in order to more competitively position the products Lease-Win's leasing representatives can offer customers. Short and long-term bond prices are watched closely as well, in order to help manage Lease-Win's cost of capital and to aid in the determination of interest rates for its lease products.

## **KEY PERFORMANCE INDICATORS – Sherway LP**

### *Gross Margins*

Management monitors and analyzes a number of key indicators of the Acura Sherway dealership's operations, by profit centre/department. One key indicator for each department is the level of gross margins being generated - on a per unit and total volume basis. This measure, along with other metrics that may vary amongst departments, as applicable, is monitored daily. The analyses of these various metrics allows management to react quickly to trends, concerns and opportunities in each department, on a daily, weekly and/or monthly basis.

### *Absorption Rate*

The extent to which the profits from the fixed operations of the dealership (service and parts profit centres) offset the fixed costs of the rest of the dealership is known as the dealership's "Absorption Rate". Management uses this measure as well to assess the overall performance of the dealership's fixed operations.

## **NON-GAAP MEASURES**

The Fund provides non-GAAP measures as supplementary information. Management believes EBITDA, Adjusted EBITDA and distributable cash are useful measures in evaluating the performance of the Fund and in determining whether to invest in Fund Units. Specifically, management views distributable cash as an operating performance measure, as it is a measure generally used by Canadian income trusts as an indicator of financial performance. As the Fund will distribute substantially all of its cash on an on-going basis, and since EBITDA and Adjusted EBITDA are metrics used by many investors to compare issuers on the basis of the ability to generate cash from operations, management believes that, in addition to net income (loss), EBITDA and Adjusted EBITDA are useful supplemental measures from which to make adjustments to determine distributable cash.

EBITDA, Adjusted EBITDA and distributable cash are not earnings measures recognized by GAAP and do not have standardized meanings prescribed by GAAP. Therefore, EBITDA, Adjusted EBITDA and distributable cash may not be comparable to similarly titled measures presented by other issuers. Investors are cautioned that EBITDA, Adjusted EBITDA and distributable cash should not be construed as an alternative to net income (loss) determined in accordance with GAAP as indicators of Chesswood's performance or to cash flows from operating, investing and financing activities as measures of liquidity and cash flows. However, management believes that cash flows from operations is not an appropriate measure from which to derive distributable cash because normal day-to-day lease financing transactions are grouped under financing and investing activities in accordance with GAAP and therefore cash flows from operations do not reflect these core activities.

### *Definitions of EBITDA and Adjusted EBITDA*

"EBITDA" is defined as net income (loss) adjusted to exclude interest, income taxes, depreciation and amortization.

"Adjusted EBITDA" is defined as EBITDA adjusted for (i) interest on leasing and vehicle credit lines, (ii) non-cash gain (loss) on interest rate swaps, (iii) non-cash unrealized gain (loss) on foreign exchange, (iv) elimination of the effects of Accounting Guideline



12 of the Canadian Institute of Chartered Accountant (which is described in Accounting for the Securitization of Leases and Off-Balance Sheet Arrangements under Critical Accounting Policies and Estimates) from Lease-Win's results to provide for a constant yield basis of revenue recognition over the term of Lease-Win's securitized leases, and (v) non-cash unit compensation expenses. See "Distributable Cash" for a reconciliation of EBITDA and Adjusted EBITDA to net income.

## **DISTRIBUTABLE CASH**

Distributable cash is not a defined term under GAAP, but is derived from Adjusted EBITDA, which in turn is derived from net earnings, which is a measure recognized under Canadian GAAP. Management believes that distributable cash is a useful supplemental measure of performance as it provides investors with an indication of the amount of cash available for distribution to unitholders. Distributable cash should not be used as an alternative to using net income as a measure of profitability or as an alternative to the statement of cash flows. However, management believes that cash flows from operations is not an appropriate measure from which to derive distributable cash because normal day-to-day lease financing transactions are required to be grouped under financing and investing activities in accordance with GAAP and therefore cash flows from operations does not reflect these core activities. Our method of calculating distributable cash may not be comparable to similarly titled items reported by other issuers.

	For the three-months ended March 31, 2008
(\$ thousands except per unit amounts)	
<b>Net loss</b>	<b>(\$215)</b>
Interest expense	1,036
Income tax provision (recovery)	(307)
Amortization expense	205
Non-controlling interest	(38)
<b>EBITDA (1)</b>	<b>681</b>
Foreign exchange loss	175
Interest rate swap mark-to-market loss	597
Elimination of AcG-12 in Lease-Win	(61)
Interest on leasing lines	(941)
<b>Adjusted EBITDA (1)</b>	<b>451</b>
Income Taxes – Pawnee provision per GAAP statements	360
Amortization expense – Pawnee	(18)
Capital expenditures	(10)
Interest on long-term debt	(95)
<b>Distributable cash (1)</b>	<b>\$688</b>
Total distributions declared to unitholders & non-controlling interest	\$1,208

Distributions declared per unit \$0.1710

(1) EBITDA, Adjusted EBITDA and Distributable cash are non-GAAP measures. See "Non-GAAP Measures" for a definition of EBITDA, Adjusted EBITDA and Distributable cash.



## **SELECTED QUARTERLY FINANCIAL INFORMATION**

<b><u>Fiscal 2008</u></b> (\$ thousands except per unit figures)	For the three-months ended March 31, 2008
Revenue	\$22,907
Gross profit	9,342
Income before tax, non-controlling interest and loss on foreign exchange and interest rate swaps	212
Loss before tax and non-controlling interest	(560)
Net loss before non-controlling interest	(253)
Net loss	(215)
Basic and diluted loss per unit	(0.03)
Total assets	138,859
Total long-term financial liabilities	69,035
<b><u>Other Data</u></b>	
Adjusted EBITDA (1)	\$451
Distributable cash	688
Distributions declared (unitholders & non-controlling interest)	1,208
Distributions declared per unit (1)(2)	\$0.1710

<b><u>Fiscal 2007</u></b>	For the three-months ended				For the year ended
(\$ thousands except per unit figures)	March 31, 2007	June 30, 2007	September 30, 2007	December 31, 2007	December 31, 2007
Revenue	\$21,082	\$23,008	21,840	22,408	\$88,338
Gross profit	10,457	10,084	9,642	10,020	40,203
Income before tax, non-controlling interest, impairment, and loss on foreign exchange and interest rate swaps	2,615	2,636	2,271	2,550	10,072
Income (loss) before tax and non-controlling interest	2,416	4,542	(7,607)	(4,161)	(4,810)
Net income (loss) before non-controlling interest	1,858	4,751	(7,927)	(3,200)	(4,518)
Net income (loss)	1,580	4,041	(6,742)	(2,721)	(3,842)
Basic and diluted income (loss) per unit	0.22	0.56	(0.93)	(0.38)	(0.53)
Total assets	179,705	165,948	144,355	138,743	138,743
Total long-term financial liabilities	83,905	77,408	72,409	70,712	70,712
<b><u>Other Data</u></b>					
Adjusted EBITDA (1)	\$3,166	\$3,244	2,657	2,184	\$11,251
Distributable cash	2,458	2,321	2,246	1,746	8,771
Distributions declared (unitholders & non-controlling interest)	2,448	2,292	2,220	1,612	8,572
Distributions declared per unit (1)(2)	\$0.2874	\$0.2874	\$0.2874	\$0.2098	\$1.072

<b>Fiscal 2006</b> (\$ thousands except per unit figures)	For the period from	For the three-months ended		For the period from
	May 10, 2006 to June 30, 2006	September 30, 2006	December 31, 2006	May 10, 2006 to December 31, 2006
Revenue	\$12,733	\$22,596	\$22,078	\$57,407
Gross profit	6,093	10,721	10,456	27,270
Income before tax, non-controlling interest, impairment, and loss on foreign exchange	2,311	4,030	3,033	9,374
Income before tax and non-controlling interest	2,032	3,997	1,213	7,242
Net income before non-controlling interest	1,318	2,710	1,280	5,308
Net income	1,120	2,305	1,089	4,514
Basic and diluted income per unit	\$0.16	\$0.32	\$0.14	\$0.62
Total assets (3)	176,360	171,231	180,282	180,282
Total long-term financial liabilities	81,889	82,455	88,229	88,229
<b>Other Data</b>				
Adjusted EBITDA (1)	\$2,712	\$4,730	\$3,781	\$11,223
Distributable cash	1,972	3,215	3,362	8,549
Distributions declared (unitholders & non- controlling interest)	1,363	2,447	2,448	6,258
Distributions declared per unit (1)(2)	\$0.1607	\$0.2874	\$0.2874	\$0.7355

(1) Adjusted EBITDA and Distributable cash are non-GAAP measures. See "Non-GAAP Measures" for the definitions of EBITDA and Adjusted EBITDA. See "Distributable cash" for a description of the calculation methodology for Distributable cash, and for a reconciliation of EBITDA, Adjusted EBITDA and Distributable cash to net income.

(2) Based on weighted average units outstanding during period.

(3) In the quarterly financial statements during 2006, intangible assets and goodwill were converted at the historic exchange rate, although they should have been converted at the current exchange rate. The offsetting entry would have been to the cumulative foreign currency translation account in the equity section of the balance sheet, thus there was no income statement impact from this adjustment at year-end. The total assets value in the prior quarters has been adjusted for this correction.

## **RESULTS OF OPERATIONS FOR THE THREE-MONTHS ENDED MARCH 31, 2008 AND 2007**

Pawnee's U.S. dollar results for the three-months ended March 31, 2008 were converted at 1.0042 which was the average exchange rate for the period; the U.S. dollar results for the three-months ended March 31, 2007 were converted at 1.1716 which was the average exchange rate for the corresponding period.

Revenue from vehicles and related automotive operations totaled \$15.9 million in the three-months compared to \$12.4 million for the same period in the prior year, an increase of \$3.5 million or 27.8% year-over-year. Given the automotive operations' cost of sales of \$13.6 million (\$10.6 million in the same period in the prior year), the Canadian automotive operations generated \$2.3 million in gross profit for the three-months ended March 31, 2008 compared to gross profit of \$1.8 million in the same period in the prior year an increase of \$513,000 or 28.9%. New vehicle sales at our Acura dealership was the predominant reason for the year-over-year increase in automotive revenue and gross profit as a result of incentives offered by the manufacturer; new vehicles sales increased by 91 vehicles during the three-month period compared to the prior year. The Fund's automotive business follows a seasonal pattern, with revenue and net earnings usually being significantly lower in the first quarter than in other quarterly periods, however with the manufacturer's incentives in 2008 the dealership had an unusually strong first quarter this year.

Direct financing lease income totaled \$6.0 million in the three-months ended March 31, 2008 compared to \$7.3 million in the same period in the prior year; a decrease of approximately \$1.3 million year-over-year predominantly due to a \$1.0 million decrease as a result of foreign exchange translation. The remaining \$306,000 decrease in direct financing lease income is the result of the decrease in the leases outstanding.

Ancillary lease and other income totaled \$1.0 million in the three-months ended March 31, 2008 compared to \$1.3 million in the same period in the prior year; a decrease of \$286,000 year-over-year due to \$111,000 decrease in ancillary lease and other income and \$175,000 decrease due to foreign exchange translation.

During the three-month period ended March 31, 2008, the provision for credit losses totaled \$4.5 million compared to \$2.7 million in the same period in the prior year; an increase of \$1.8 million year-over-year due to the effect of higher charge-off levels at Pawnee. Of the \$1.8 million increase in the provision for credit losses during the three-month period ending March 31, 2008, approximately \$1.4 million related to an increase in the actual net charge-offs and \$852,000 related to a non-cash increase in the allowance for doubtful accounts, offset by a \$377,000 decrease due to the change in foreign exchange rates.

Salaries, commissions and benefits totaled \$1.8 million in the three-months ended March 31, 2008 compared to \$1.9 million in the same period in the prior year; a decrease of \$122,000 year-over-year predominantly due to a change in foreign exchange translation.

General and administrative expenses totaled \$1.6 million in the three-months ended March 31, 2008 compared to \$1.7 million in the same period in the prior year; a decrease of \$89,000. General and administrative expenses remained relatively unchanged from the prior year with the change in foreign exchange rates accounting for most of the year-over-year difference.

Interest expense on long-term debt totaled \$972,000 in the three-months ended March 31, 2008 compared to \$1.2 million in the same period in the prior year; a decrease of \$191,000 year-over-year predominantly due to a \$148,000 decrease as a result of the change in foreign exchange translation. Interest expense on Pawnee's leasing line was down approximately \$223,000 year-over-year offset by an increase on interest rate swap interest expense of \$174,000, for a net year-over-year decrease of \$49,000. On March 7, 2007, Pawnee's bank called the interest rate swaps that were outstanding, at their option, as these swaps had rates that were beneficial to Pawnee and replaced them with swaps that had rates that were more favourable to the bank. For the first quarter of 2007, Pawnee received \$59,000 in interest income from the swaps; in 2008 Pawnee paid \$115,000 in interest expense to the bank for the swaps leading to a swing of \$174,000 in interest expense in the three-month period year-over-year. Interest on Lease-Win's long-term leasing line increased by \$6,000 during the three-month period due to increased number of leases financed through the bank compared to the prior year.

Interest expense on short-term financing for Canadian automotive operations totaled \$64,000 in the three-months ended March 31, 2008 compared to \$85,000 in the same period in the prior year; a decrease of \$21,000 year-over-year predominantly due to a decrease in the average inventory balances outstanding during the period compared to the prior year. Inventory totaled \$7.9 million as at March 31, 2008 compared to \$11.8 million at March 31, 2007.

Amortization decreased by approximately \$87,000 year-over-year during the three-months ended March 31, 2008 as a result of lower amortization of intangible assets some of which were written-off in prior years.

Income before gain and losses on foreign exchange and interest rate swaps totaled \$212,000 for the three-months ended March 31, 2008 compared to \$2.6 million in the same period of the prior year, a decrease of \$2.4 million. The increase in the provision for credit losses of \$1.8 million and the \$1.3 million decrease in direct financing lease income were offset by a \$513,000 increase in gross profit from the Canadian automotive operations and a \$212,000 decrease in long-term and short-term interest expense.

The mark-to-market adjustment to revalue the interest rate swaps at Pawnee created a non-cash loss of approximately \$597,000 in the three-months ended March 31, 2008 compared to a non-cash loss of \$292,000 in the prior year, thus a year-over-year increase in interest rate swap mark-to-market expense of \$305,000 in the three month period.

For the three-months ended March 31, 2008, the mark-to-market adjustment to revalue the foreign exchange forward contracts created a non-cash loss of \$270,000, compared to a non-cash gain of \$232,000 in the same period of the prior year, thus a net year-over-year decrease in the mark-to-market adjustment of \$502,000 in the three-month period. The non-cash loss of \$270,000 for the three-months ended March 31, 2008 is the difference between the market value of the contracts at December 31, 2007 of \$1.5 million compared to the \$1.2 million proceeds received when the Fund sold the contracts on March 19, 2008. The Fund had entered into foreign exchange contracts to manage its exposure to the U.S. dollar as significant cash flows are generated in the U.S. Given the significant change in U.S. – Canadian dollar exchange rates in the prior six months, it was determined that liquidation of the hedge was an appropriate and desirable step. Therefore, the Fund sold its foreign exchange forward contracts on March 19, 2008 and received \$1.2 million on settlement.

The loss before taxes totaled \$560,000 for the three-months ended March 31, 2008 compared to income before taxes of \$2.4 million in the same period of the prior year, a decrease of \$3.0 million.

The recovery of income taxes for the three-month period ended March 31, 2008 totaled \$307,000 compared to a provision for income taxes of \$558,000 in the same quarter of the prior year, a decrease of \$865,000. The recovery of income taxes of \$307,000 is

comprised of \$772,000 current tax expense which is booked to accounts payable and accrued liabilities and \$1.1 million future income tax recovery.

For the three-months ended March 31, 2008, the Fund reported a consolidated net loss of \$215,000, or \$0.03 per Fund Unit, compared to net income of \$1.6 million or \$0.22 per Fund Unit, in the three-months ended March 31, 2007, a decrease of \$1.8 million.

## **BALANCE SHEET**

Total consolidated assets of the Fund at March 31, 2008 were \$138.9 million compared to \$138.7 million at December 31, 2007. Over half of the total assets represent Pawnee's and Lease-Win's net investments in direct financing lease receivables. The exchange rate on March 31, 2008 was 1.0279 compared to 0.9881 at December 31, 2007. The change in the foreign exchange rates increased assets by \$4.6 million, thus total assets excluding the foreign exchange impact decreased by \$4.4 million from December 31, 2007.

Cash totaled \$4.5 million at March 31, 2008 compared to \$2.4 million at December 31, 2007, an increase of \$2.1 million. Of the \$2.1 million increase, \$5.9 million is the result of cash inflow from operations and vehicle financing; \$1.2 million in cash received on settlement of foreign exchange forward contracts; \$3.8 million decrease in cash to fund net investment in leases; \$2.6 million inflow of cash from proceeds from lease financing and securitizations, cash received from residual interest in securitizations, and security deposits; \$2.7 million decrease in cash as a result of payments towards lease financing credit facilities, and \$1.2 million in cash distributions paid during the three-months ended March 31, 2008.

Accounts receivable totaled \$2.4 million at March 31, 2008 compared to \$3.3 million at December 31, 2007, a decrease of \$0.9 million. The accounts receivable balance principally relates to the Acura Sherway dealership and includes amounts due from the manufacturer for financing contracts in transit, which are typically collected within seven to ten days, and are usually at their highest levels at month end. Vehicle receivable balances fluctuate throughout the year based on seasonality, and sales volumes of the industry.

Inventory totaled \$7.9 million at March 31, 2008 compared to \$8.1 million at December 31, 2007, a decrease of \$0.2 million. Vehicle inventory balances at dealerships also fluctuate throughout the year based on seasonality, sales volumes and market conditions.

Vehicle inventory is financed through vehicle financing credit facilities, of which \$7.2 million was outstanding at March 31, 2008 compared to \$6.8 million at December 31, 2007, leaving \$0.8 million of inventory that was self-financed as at March 31, 2008 compared to \$1.3 million at December 31, 2007.

As at March 31, 2008, total net investment in leases totaled \$81.9 million compared to \$82.6 million at December 31, 2007, a decrease of \$727,000; the decrease was comprised of:

	<b>CDN\$</b> (thousands)
Increase in allowance for doubtful accounts at Pawnee	1,425
Decrease of 177 leases since December 31, 2007 at Pawnee	2,058
Decrease of US\$57.00 in the average book value of net investment in leases	428
Increase in net investment in leases from change in foreign exchange	(2,984)
Net increase in net investment in leases at Lease-Win	(200)
Total decrease in net investment in leases	<u>\$727</u>

The gross lease receivable of leases under administration as at March 31, 2008 was approximately \$156.5 million, compared to \$158.8 million at December 31, 2007. Pawnee's gross lease receivable represents \$106.4 million (US\$103.5 million) of the total gross lease receivable outstanding at March 31, 2008, compared to \$105.9 million (US\$107.2 million) at December 31, 2007.

Lease-Win's gross lease receivable under administration totaled \$50.1 million at March 31, 2008 down from \$52.9 million at December 31, 2007. Lease-Win's gross lease receivable has decreased \$2.8 million year-over-year, however their net investment in leases has increased by \$200,000 as a result of self-financing more leases in 2008.

The \$81.9 million in net investment in leases is net of \$9.7 million in allowance for doubtful accounts compared to \$7.9 million at December 31, 2007. At Pawnee, the allowance for doubtful accounts of U.S.\$ 9.0 million represents 12.73% of the net investment in lease receivables less security deposits on hand at March 31, 2008 compared to U.S.\$7.6 million or 10.46% at December 31, 2007. The 12.73% of the net investment in lease receivables less security deposits is determined in accordance with Pawnee's policy of

maintaining an allowance for doubtful accounts, as a percentage of net investment in leases, that is equal to the last twelve-month rolling net charge-off percentage level.

Unlike certain other equipment leasing and finance companies, Pawnee does not sell any of its lease receivables portfolio. All receivables originated by Pawnee are retained for their full term. Pawnee funds its leases through a floating rate facility offered by a banking syndicate, as discussed below and in the notes to the financial statements.

Included in the net investment in lease receivables is \$2.7 million in securitized lease receivables at Lease-Win, relating to \$37.6 million in assets under administration, compared to \$40.1 million at December 31, 2007. At March 31, 2008, 87.3% of Lease-Win's gross lease receivable was securitized compared to 88.4% at December 31, 2007, which reflects Lease-Win's decision to self-finance shorter-term leases. Lease-Win has used securitization as its preferred method of funding its leasing activities since July 1997. These securitization transactions have an off-balance sheet component. See "Critical Accounting Policies and Estimates".

Prepaid expenses totaled \$1.3 million at March 31, 2008. Prepaid personal property taxes paid on behalf of Pawnee's lessees of \$1.0 million comprise the majority of the prepaid expenses balance.

Property and equipment predominantly relates to the land and building located at 4077 Chesswood Drive, Toronto, Ontario and equipment at Sherway LP's Acura dealership in Etobicoke, Ontario. Approximately 92.9% of the Fund's property and equipment is located in Ontario. None of the Fund's operating businesses require significant capital asset expenditures or depend on capital-intensive operations. The significant intangible assets of broker relationships and customer relationships also do not require significant outlay of cash to maintain them, as the creation of organic lease receivables does not require significant outlay of cash, other than commissions.

Intangible assets totaled \$9.6 million at March 31, 2008 compared to \$9.4 million at December 31, 2007. The \$192,000 increase in intangible assets is comprised of a \$325,000 increase as the result of the change in foreign exchange rates offset by \$133,000 in amortization of broker relationships and back-end systems software.

Goodwill totaled \$27.9 million at March 31, 2008 compared to \$26.7 million at December 31, 2007. The \$1.2 million increase is the result of the movement in foreign exchange rates. Goodwill is tested annually for impairment unless certain circumstances arise that would require an assessment prior to an annual review.

Lease financing of \$44.2 million at March 31, 2008 is comprised of:

	<u>March 31, 2008</u>	<u>December 31, 2007</u>
	(\$ thousands)	
Pawnee's credit facility	\$42,026	\$42,810
Lease-Win's credit facility	2,131	2,177
	<u>\$44,157</u>	<u>\$44,987</u>
 Pawnee's credit facility – US\$ - actual balance – gross of deferred financing costs	 <u>\$41,000</u>	 <u>\$43,500</u>

The \$830,000 decrease in lease financing is predominantly due to an increase in foreign exchange translation of \$1.7 million offset against \$2.5 million in net payouts. At March 31, 2008, the deferred financing costs netted against Pawnee's credit facility totaled \$119,000. Pawnee has a credit facility that allows borrowings of up to US\$57.5 million, subject to, among other things, adhering to certain percentages of eligible gross lease receivables, and the maintenance of a minimum debt to tangible net worth ratio.

Pawnee had sufficient cash to fund net lease originations and operating expenses and apply US\$2.5 million against its credit facility. This credit facility is secured by substantially all of Pawnee's assets, contains negative covenants including the maintaining of leverage and interest coverage ratios, requires Pawnee to mitigate its interest rate risk by entering interest rate swaps for a notional amount not less than 50% of the aggregate commitment, and matures on May 10, 2010.

Lease-Win's floating rate lease financing is the amount financed through a Canadian chartered bank and not securitized. Many of the leases financed through the bank have certain characteristics that make them ineligible for securitization, such as: age of vehicle, length of term, or concentration of leases from certain customers. Lease-Win's lease financing is repaid over the term of the corresponding leases.



The majority of the \$9.9 million in customer security deposits relates to security deposits held by Pawnee. Pawnee's primary lease contract requires that the lessee provide two payments as security deposit (not advance payments), which are held for the full term of the lease and then returned or applied to the purchase option of the equipment at the lessee's request, unless the lessee has previously defaulted (in which case the deposit is applied against the lease receivable). Historically, a very high percentage of lessees' deposits are either applied to the purchase option of the leased equipment at the end of the lease term or used to offset delinquencies. The approximate \$79,000 increase in the security deposit balance from December 31, 2007 is due primarily to a \$391,000 increase as a result of foreign exchange conversion which was offset by a \$312,000 decline in security deposits as a result of fewer leases outstanding at March 31, 2008 than December 31, 2007.

Most of Lease-Win's lease receivables are sold on a fully serviced basis. Accordingly, upon each securitization a servicing liability is recorded to recognize the potential reduction in the cash flows receivable by the Fund's automotive leasing operations if an amount was paid by the special purpose entity to a replacement servicer. The estimated fees that would otherwise be payable to a replacement servicer forms the basis of determination of the fair value of the servicing liability that is charged against the gain or loss at the time of recognizing the sale of securitized assets. The \$597,000 in servicing liability would be payable only if Lease-Win was unable to service the lease receivables that have been sold.

Pawnee enters into interest rate swap agreements with its principal lender under its banking facility that provides for payment of an annual fixed rate. In return, Pawnee receives payment of a LIBOR based floating rate amount. Pawnee's bank has the option to terminate the swaps typically one year prior to the maturity date. The interest rate swaps are intended to offset a portion of the variable interest rate risk on the credit facility. At March 31, 2008, the mark-to-market adjustment is a loss of approximately \$1.4 million compared to a loss of \$735,000 at December 31, 2007.

Effective Date	Notional Amount U.S.\$	Annual Fixed Rate	Maturity date	Bank Call Date
October 2005	5,000,000	4.66%	October 2008	October 2007
March 2007	15,000,000	5.14%	March 2009	n/a
March 2007	15,000,000	5.09%	March 2010	n/a

Pawnee's interest rate swaps are not considered trading instruments as it intends to hold them until termination. Nonetheless, the interest rate swaps do not qualify as a hedge for accounting purposes, and are therefore recorded as a separate derivative financial instrument. Accordingly, the estimated fair value of the interest rate swaps are recorded as a liability on the accompanying consolidated balance sheet. Payments made and received pursuant to the terms of the interest rate swaps and adjustments to the fair value of the interest rate swaps are recorded as an adjustment to interest expense. The fair value of interest rate swaps is based upon the estimated net present value of cash flows, and does not necessarily reflect the amount that would be required to settle the interest rate swaps.

The mortgage of approximately \$896,000, which had an original principal amount of \$1.1 million, bears interest at the rate of 7.25% per annum, is payable in monthly installments of principal and interest of \$9,975, is due December 18, 2013 and is secured by the land and building located at 4077 Chesswood Drive, Toronto, Ontario.

The \$3.5 million principal amount of convertible debentures (the "Debentures") were issued by the Fund in exchange for convertible debentures in the same principal amount issued by cars4U Ltd. in February 10, 2003. The Debentures bear interest at the rate of 9% per annum, payable quarterly, and were due on August 10, 2007. The Debentures have since been extended until August 10, 2008. The Debentures are convertible into Fund Units, at the holders' option, at a conversion price of \$15.58 per Fund Unit. The Debentures will be automatically converted into Fund Units in the event that the 20-day average price for the Fund Units is at least \$20.16 per Fund Unit. Debentures in the principal amount of \$2.2 million (out of the aggregate \$3.5 million principal amount of the Debentures) were issued to trustees of the Fund and/or directors of Chesswood GP Limited (who were previously directors of cars4U Ltd.), which is a 100% owned subsidiary of the Fund. The Fund anticipates extending the maturity date of the convertible debentures from August 10, 2008 until August 10, 2009 or beyond.

Future income taxes payable at March 31, 2008 totaled \$9.9 million compared to \$10.8 million at December 31, 2007, a decrease of \$871,000. The decrease in future income taxes payable is comprised of future income tax recovery of \$1.1 million for the period which was offset by a \$208,000 increase in future taxes payable as a result of foreign exchange.

The Fund is subject to United States federal income taxes as Pawnee's business operates in the United States, and subject to Canadian federal and provincial income taxes as Lease-Win operates in Canada. The structure of the Fund, similar to other cross-border income fund structures, includes inter-company debt that generates inter-company interest expense. Taxes payable, and therefore the calculation of income tax expense, have been reduced by this inter-company interest expense. Income taxes in Pawnee and Lease-Win are provided for using the asset and liability method of accounting, this method recognizes future tax assets and liabilities that arise from differences between the accounting basis of the subsidiaries' assets and liabilities and their corresponding tax basis.

The non-controlling interest of \$8.3 million compared to \$8.0 million at December 31, 2007, represents the 1,274,601 Class B common shares of U.S. Acquisitionco that were issued as partial consideration for the acquisition of Pawnee. The change in the foreign exchange rate from December 31, 2007 to March 31, 2008 resulted in an increase of \$310,000 in the value of the non-controlling interest. The shares are fully exchangeable for Fund Units, on a one-to-one basis, through a series of steps. The Class B common shares may be exchanged after November 8, 2008. These exchangeable shares have been classified as a non-controlling interest in the consolidated financial statements. The Class B common shares are entitled to distributions provided that certain minimum distributions on the Fund Units and the Class C common shares of U.S. Acquisitionco have been made. As the Class B common shares are subordinated until November 8, 2008 and their distributions are restricted if certain minimum distributions have not been made, they have been valued with a discount rate of 7.5 percent per EIC 151 (Emerging Issues Committee Abstract 151) - Exchangeable Securities Issued By Subsidiaries Of Income Trusts.

At March 31, 2008, there were 7,040,558 Fund Units and 203,936 in Class C common shares of US Acquisitionco outstanding, totalling \$65.6 million. The Class C common shares of US Acquisitionco were issued as partial consideration for the acquisition of Pawnee and are fully exchangeable at any time for Fund Units, on a one-to-one basis, through a series of steps.

## **LIQUIDITY AND CAPITAL RESOURCES OVERVIEW**

The Fund's primary sources of cash have been cash flows from operating activities, and borrowings under its various subsidiaries' credit facilities. The Fund's primary uses of cash are to fund equipment and vehicle leases, long-term debt principal repayments and distributions to unitholders and non-controlling interest. The majority of the cash required for the acquisition of the Fund's operating businesses and related costs was raised through the Fund's initial public offering.

The Fund's subsidiaries' objective is to maintain low cash balances, investing any free cash in leases as needed and using any excess to pay down debt on the primary financing facilities. The subsidiaries fund working capital needs, lease originations and growth using advances under credit facilities available when operating cash flow is not sufficient. At March 31, 2008, the Fund's operating units had \$18.5 million in additional borrowings available under various credit facilities to fund business operations.

The Fund itself does not have any credit facility. Each of its operating subsidiaries has a credit facility. These credit facilities are used to provide funding for the subject subsidiary's operations (i.e. to provide financing for the purchase of assets which are to be the subject of leases or to acquire vehicle inventory and support working capital). The credit facilities are not intended to directly fund distributions by the Fund (and these facilities generally limit the amount which can be distributed up to the Fund to the net income of the subject subsidiary).

### **Cash Sources and Uses**

#### **For the three-months ended March 31, 2008**

The Fund's operations generated net cash flow from operations of \$5.6 million during the three-months ended March 31, 2008 compared to cash flow from operations of \$977,000 in the three months ended March 31, 2007, an increase of \$4.6 million year-over-year.

Cash flow generated from operations during the three-months ended March 31, 2008 includes the cash inflow from the decrease in inventory of \$172,000 but excludes the \$366,000 increase in short-term vehicle financing relating to the inventory purchased during the three-month period. Cash flow generated from operations during the three-months ended March 31, 2007 includes the cash outflow from the increase in inventory of \$3.5 million but excludes the \$3.7 million increase in short-term vehicle financing relating to the inventory purchased during the three-month period in the prior year.

Thus, cash flow from operations after considering the movement in these short-term working capital items was \$5.9 million in the three months ended March 31, 2008 compared to \$4.7 million in the same period in the prior year, an increase of \$1.2 million or approximately 25.5% year-over-year.



During the three months ended March 31, 2008, investment in net direct financing leases of \$3.8 million (2007 – \$6.1 million) was offset by financing of \$2.6 million (2007 - \$4.5 million) from proceeds from lease financing and securitization, cash received from residual interest in securitizations, and security deposits, resulting in a net usage of \$1.2 million (2007 - \$1.6 million) of cash in the investment of leases prior to payments against lease financing credit facilities.

During the three months ended March 31, 2008, cash payments applied to lease financing credit facilities totalled \$2.7 million (of which \$151,000 was required payments at Lease-Win), thus utilizing \$3.9 million from operations to fund net investment in leases and payments against leasing financing credit facilities.

During the three months ended March 31, 2007, cash payments applied to lease financing credit facilities totalled \$2.0 million (of which \$253,000 was required payments at Lease-Win), thus utilizing \$3.6 million from operations to fund net investment in leases and payments against leasing financing credit facilities. This translates to an increase of \$300,000 in the cash used to fund net investment in leases and payments against leasing financing credit facilities in the three-month period compared to the prior year.

The Fund's subsidiaries could have utilized their credit facilities further to fund the net lease originations but had sufficient cash on hand to cover these originations and normal business operations while allowing Pawnee to apply U.S.\$2.5 million (2007 - U.S.\$1.5 million) against their lease financing credit facility during the three-month period.

Principal payments under long-term debt and capital leases totalled approximately \$16,000 (2007 - \$19,000) during the three-months ended March 31, 2008. Capital expenditures totalled \$10,000 (2007 – \$28,000) during the three-month period.

On March 19, 2008, the Fund sold its U.S. dollar foreign exchange forward contracts and received \$1.2 million on settlement. The Fund had entered into foreign exchange contracts to manage its exposure to the U.S. dollar as significant cash flows are generated in the U.S. Given the significant change in U.S. – Canadian dollar exchange rates in the prior six months, it was determined that liquidation of the hedge was an appropriate and desirable step.

The Fund paid distributions to unitholders and non-controlling interest in the amount of \$1.2 million during the three-months ended March 31, 2008 compared to \$2.4 million in the same period in the prior year; a decrease of \$1.2 million. The decrease is the result of \$820,000 reduction in the monthly distributions to unitholders and \$421,000 reduction in distributions to U.S. Acquisitionco Class B and Class C shareholders as a result of the subordination of Class B distributions and the reduction of distributions on the Class C shares.

In total, in the three-months ended March 31, 2008, there was an increase in cash of \$2.1 million compared to a decrease of cash of \$1.4 million in the prior year; an increase of \$3.5 million year-over-year. Of the \$3.5 million increase in cash during the three-month period compared to the prior period, \$1.26 million is the result of an increase in cash flow from operations and vehicle financing, \$1.24 million received on settlement of foreign exchange forward contracts, \$1.24 million increase in cash as a result of reductions in distributions paid during the period compared to the prior year, \$391,000 decrease in net investment in leases less proceeds from financing offset by \$676,000 increase in payments applied to leasing financing credit facilities.

The Fund expects to finance current operations, planned capital expenditures and internal growth for the foreseeable future using funds generated from operations, existing cash, and the funds available under existing credit facilities. The Fund's methodology for calculating distributable cash, which is based on the earnings of its subsidiaries that can be distributed up to the Fund, is subject to the terms of credit facilities which permit distributions based on net income determined in accordance with GAAP. In the first quarter, Pawnee's increased allowance for bad debts, a non-cash item, resulted in Pawnee's cash flows being significantly higher than the amounts it could distribute to the Fund. While the Fund paid distributions in the quarter that exceeded its distributable cash for the quarter, the Fund's consolidated positive cash flow actually exceeded the total amount distributed, and Pawnee repaid \$2.5 million of lease financing during the quarter. Distributions to date have been funded from operational cash flows (which term is not intended to be a reference to cash flow from operations in the Fund's financial statements, as management believes that cash flow from operations is not an appropriate measure from which to derive or reflect the Fund's distributable cash because normal day-to-day leasing and vehicle financing transactions are required to be grouped under financing and investing activities in accordance with GAAP and therefore cash flows from operations does not reflect these core activities).

The Fund may require additional funds to finance future acquisitions. It will seek such additional funds, if necessary, through public or private equity or debt financings from time to time, as market conditions permit.

## Financial Covenants, Restrictions and Events of Default

Each of the Fund's operating subsidiaries is subject to bank and/or manufacturer covenants relative to leverage and/or working capital.

Pawnee funds its business primarily through variable rate borrowings and has a revolving credit facility for up to US\$57.5 million which can, subject to certain conditions, be increased to US\$65 million. As of March 31, 2008, Pawnee had used approximately US\$41.0 million of its available borrowing under this facility. Pawnee's ability to access funding at competitive rates through various economic cycles enables it to maintain the liquidity necessary to manage its business, and its ability to continue to access funding is an important condition to its future success. Pawnee is required to purchase fixed interest rate hedges for at least 50% of the total commitment under its credit facility, and as of March 31, 2008 Pawnee has hedged US\$35.0 million, representing approximately 85.4% of the US\$41.0 million outstanding under the credit facility.

Pawnee's secured borrowing agreement has financial covenants and other restrictions with which it must comply in order to obtain continued funding and avoid default. Events of default under these arrangements include a change in control without lender-approval.

Advances on the revolving facility may be drawn at any time, subject to compliance with borrowing base calculations and compliance with the covenants set out therein. As of March 31, 2008, US\$41.0 million was outstanding under the facility and Pawnee had capacity to draw up to and in excess of the US\$57.5 million commitment and remain within the borrowing base under the facility.

Pawnee is restricted in its ability to further merge, acquire companies or be acquired, or incur additional debt without lender approval. Furthermore, dividends are limited to compliance with all bank covenants and may not exceed 95% of Pawnee's consolidated net income, as determined in accordance with U.S. GAAP, excluding mark-to-market adjustments for interest rate swaps.

Pawnee is subject to the risk of increases in interest rates as the credit facility used to fund the business operations has a variable interest rate, while the yields on its equipment leases are fixed. Pawnee seeks to mitigate that risk through the use of swap agreements that effectively convert floating rate debt to fixed rates.

If the current variable rate credit facility were to become unavailable and Pawnee was unable to obtain replacement facilities on acceptable terms, or at all, Pawnee may not have access to the financing necessary to conduct business, which would limit its ability to fund operations.

## Distribution to Unitholders

The Fund declared cash distributions during the three-months ended March 31, 2008 were as follows:

Unitholder Record Date	Per Unit
January 31, 2008	\$0.0570
February 28, 2008	\$0.0570
March 31, 2008	\$0.0570
	<u>\$0.1710</u>

## Distribution Policy

Our policy is to pay monthly distributions to unitholders of record on the last business day of each month by the 15<sup>th</sup> of the following month (or the next business day thereafter if the 15<sup>th</sup> is not a business day). Unitholder distributions are subject to review and approval by the trustees of the Fund and the board of directors of Chesswood GP Limited.

Pursuant to the purchase agreement by which the Fund acquired Pawnee, the holders of Class B and Class C shares of U.S. Acquisitionco, agreed to a reduction of U.S.\$888,762 in 2007, against the dividends otherwise payable on such shares. This reduction became effective in May 2007 and therefore the distributions to the holders of Class B and Class C shares are reduced by U.S.\$74,063 a month, for one year. This reduction does not relate to any subordination of distributions. If Pawnee's distributable cash exceeds a targeted increased annual level, the holders may be entitled to be paid all or a portion of the reduction amount.

The Fund announced on October 30, 2007, that it was reducing its monthly distributions to 5.70 cents from 9.58 cents per unit commencing with the distribution in respect of the month-ended November 30, 2007, which was paid on December 17, 2007.

Pursuant to the purchase agreement by which the Fund acquired Pawnee, the holders of Class B shares of U.S. Acquisitionco agreed to

subordinate the dividends payable on such shares if the monthly distributions to unitholders of the Fund were less than 9.58 cents per unit. The subordination of Class B distributions ends in November 2008. The decision to reduce monthly distributions was made as a result of the impact of the current competitive environment faced by Pawnee as well as the general erosion in the U.S. economy.

Following a review by the Fund's trustees and the directors of Chesswood GP Limited (the Fund's administrator subsidiary) of cash flow and cash position as of the end of February 2008, it was determined that the Fund's current policy of making monthly distributions of 5.70 cents per unit would be continued. The Fund's trustees and directors will continue to review the Fund's cash flow and cash position, to determine any appropriate change to the distribution policy going forward.

Given the fluctuations in monthly earnings at Pawnee due to market volatility, it is difficult to project charge-off levels and the resultant cash flow. Chesswood's distributable cash may or may not attain the levels necessary to generate this level of distribution.

### **Minimum payments**

The aggregate amount of minimum payments required on debt is as follows:

(\$ thousands)	2008	2009	2010	2011	2012 and beyond	Total
Lease-Win's lease financing (*)	\$2,131	\$-	\$-	\$-	\$-	\$2,131
Pawnee's lease financing credit facility	-	-	42,026	-	-	42,026
Mortgage payable	43	61	65	70	657	896
Convertible debentures	3,500	-	-	-	-	3,500
<b>Total</b>	<b>\$5,674</b>	<b>\$61</b>	<b>\$42,091</b>	<b>\$70</b>	<b>\$657</b>	<b>\$48,553</b>

(\*) \$2.1 million of the long-term debt would only be payable in 2008 if the bank called the loan, which is not anticipated. Otherwise the loan is payable over the term of the underlying leases.

### **OUTLOOK**

Management expects the challenging conditions in the U.S. financial services markets to continue, at a minimum, for most of 2008. Recessionary effects may further dampen the shorter-term economic outlook in the U.S.

Management continues to be focused on analyzing the performance and behavior of its portfolio, assessing its credit adjudication processes and market trends, so as to adjust, where possible, for changing economic conditions. These adjustments can include a tightening of credit standards, which in turn could affect the level of new lease originations.

Management is also focused on positioning its U.S. based business for opportunities that it believes may present themselves as market conditions ultimately improve.

The recently announced Stimulus Package in the U.S. included a provision which allows for businesses to claim depreciation for tax purposes at accelerated rates. This provision will allow Pawnee to reduce its cash taxes otherwise payable for 2008 by several million dollars, at minimum, thereby improving Pawnee's expected cash flow and leverage for the year.

In Canada, the Federal government's introduction of taxation of income trusts in 2011, which was first announced on October 31, 2006, has impacted upon income trusts generally. The trustees of the Fund and directors of Chesswood GP Limited, working with management and legal, tax and financial advisers, have been and will continue to consider the Fund's current structure and any changes or initiatives, which might provide enhanced unitholder value.

### **RISK FACTORS**

An investment in Fund Units entails certain risk factors that should be considered carefully.

The Fund operates in a dynamic environment that involves various risks and uncertainties, many of which are beyond the Fund's control and which could have an effect on the Fund's business, revenues, operating results, cash flow, distributable cash and financial condition. Readers should carefully review the risk factors in the Fund's annual information form filed with various Canadian securities regulatory authorities through SEDAR (the System for Electronic Document Analysis and Retrieval) at [www.sedar.com](http://www.sedar.com), a summary of which are set out below.

#### ***Dependence on Key Personnel***

Our operating companies depend to a large extent upon the abilities and continued efforts of their key operating and sales (leasing) personnel and senior management teams.

#### ***Relationships with Brokers and Other Origination Sources***

Pawnee has formed relationships with hundreds of origination sources, comprised primarily of lease brokerage firms. Pawnee relies on these relationships to generate lease applications and originations. The failure to maintain effective relationships with its brokers and other origination sources or decisions by them to refer leasing transactions to, or to sign contracts with, other financing sources could impede Pawnee's ability to generate lease transactions.

#### ***Risk of Future Legal Proceedings***

Our operating companies are threatened from time to time with, or are named as defendants in, or may become subject to, various legal proceedings, fines or penalties in the ordinary course of conducting their respective businesses. A significant judgment or the imposition of a significant fine or penalty on an operating company (or on a company engaged in a similar business, to the extent the operating company operates in a similar manner) could have a material adverse impact on our business, financial condition and results of operations, and on the amount of cash available for distribution to our unitholders.

#### ***Interest Rate Fluctuations***

Our operating companies (and, in particular, Pawnee and Lease-Win) are exposed to fluctuations in interest rates under their borrowings. Increases in interest rates (to the extent not mitigated by interest hedging arrangements) may have a material adverse impact on our businesses, financial condition and results of operations, and on the amount of cash available for distribution to our unitholders.

Pawnee and Lease-Win's leases are written at fixed interest rates and terms. Pawnee and Lease-Win generally finance their activities using both fixed rate funds and floating rate funds. To the extent Pawnee and Lease-Win finance fixed rate leases with floating rate funds, they are exposed to fluctuations in interest rates such that an increase in interest rates could narrow or eliminate the margin between the yield on a lease and the effective interest rate paid by the lessor to finance the lease. While Pawnee enters into interest rate swaps to mitigate rate fluctuation risk, there can be no assurances that these arrangements will be sufficient to fully protect Pawnee against interest rate risks, or that Pawnee will be able to maintain such arrangements on a continuing basis.

#### ***Portfolio Delinquencies; Inability to Underwrite Lease Applications***

Pawnee's receivables consist primarily of lease receivables originated under leasing programs designed to serve smaller, often owner-operated businesses who have limited access to traditional financing. There is a high degree of risk associated with leasing to such parties. The typical lessee in Pawnee's portfolio is a start-up business that has not established business credit or to a more established business that has experienced some business or personal credit difficulty at sometime in their history. As a result, such leases entail a relatively higher risk and may be expected to experience higher levels of delinquencies and loss levels. Pawnee cannot guarantee that the delinquency and loss levels of its receivables will correspond to the historical levels Pawnee has experienced on its portfolio and there is a risk that delinquencies and losses could increase significantly.

In addition, since defaulted leases and certain delinquent leases can neither be used as collateral under its variable rate financing facilities, higher than anticipated lease defaults and delinquencies could adversely affect Pawnee's liquidity by reducing the amount of funding available to it under these financing arrangements. Furthermore, increased rates of delinquencies or loss levels could result in adverse changes to the terms of future financing arrangements, including increased interest rates payable to lenders and the imposition of more burdensome covenants and increased credit enhancement requirements.

### ***Deterioration in Economic or Business Conditions***

Our operating companies' operating results may be negatively impacted by various economic factors and business conditions, including the level of economic activity in the markets in which they operate. To the extent that economic activity or business conditions deteriorate, delinquencies and credit losses may increase. Delinquencies and credit losses generally increase during economic slowdowns or recessions. As Pawnee extends credit primarily to small businesses, many of Pawnee's customers may be particularly susceptible to economic slowdowns or recessions, and may be unable to make scheduled lease payments during these periods. Unfavourable economic conditions may also make it more difficult for Pawnee and Lease-Win to maintain new lease origination volumes and the credit quality of new leases at levels previously attained. Unfavourable economic conditions could also increase funding costs or operating cost structures, limit access to credit facilities, securitizations and other capital markets or result in a decision by lenders not to extend further credit. Sherway LP, as the operator of a premium brand new car dealership, could also be negatively affected by deteriorating economic conditions which result in reduced new car sales.

In addition, the leasing industry generally may be affected by changes in accounting treatment for leases, and negative publicity with respect to, among other things, fraud or deceptive practices by certain participants in the industry. Greater governmental scrutiny is also a risk, especially as to the tax treatment of certain transaction structures or other aspects of these transactions that, if changed, could result in additional tax, fee or other revenue to that governmental authority. Any of these factors may make leasing less attractive or diminish the profitability of the existing financing alternatives offered by our operating companies.

### ***Losses from Leases***

Losses from leases in excess of Pawnee's or Lease-Win's expectations would have a material adverse impact on our businesses, financial condition and results of operations, and on the amount of cash available for distribution to our unitholders. In connection with financing new leases, Pawnee and Lease-Win determine and record a provision for credit losses in order to maintain an appropriate allowance for credit losses to cover the estimated credit losses for all of the leases in their portfolios. Pawnee and Lease-Win reserve for losses based on their respective historical experience for losses adjusted by management's assessment of the current condition of their portfolios, general economy, condition of the leasing industry and other factors. Should there be a significant change in the above noted factors, then Pawnee and Lease-Win may have to set aside additional reserves which could have a material adverse impact on their respective business, financial condition and results of operations and on the amount of cash available for distribution to our unitholders.

Determining the appropriate level of the allowance is an inherently uncertain process and therefore the determination of this allowance may prove to be inadequate to cover losses in connection with a portfolio of leases. Factors that could lead to the inadequacy of an allowance for credit losses may include the inability to appropriately underwrite credit risk of new lease originations, effectively manage collections, or anticipate adverse changes in the economy or discrete events adversely affecting specific leasing customers, industries or geographic areas.

### ***Adverse Events or Legal Determinations in Areas With High Geographic Concentrations of Leases***

If judicial or other governmental rulings or actions or interpretations of laws adverse to the leasing business in general or to business practices engaged in by Pawnee, or adverse economic conditions or the occurrence of other significant events such as natural disasters and terrorist attacks, were to occur in a geographic region with a high concentration of leases or equipment leased from Pawnee, there could be a material adverse impact on our business, financial condition and results of operation, and the amount of cash available for distribution to our unitholders.

### ***External Financing***

Pawnee and Lease-Win depend and will continue to depend on the availability of credit (and, for Lease-Win, securitization financing) from external financing sources to continue to finance new leases, refinance existing leases and satisfy their other working capital needs. Pawnee and Lease-Win may be unable to obtain additional financing on acceptable terms or at all. If any or all of their funding sources become unavailable on acceptable terms or at all, or if any of their credit (or, for Lease-Win, securitization) facilities are not renewed or re-negotiated upon expiration of their terms, Pawnee and Lease-Win may not have access to the financing necessary to conduct their respective businesses, which would limit their ability to finance their operations.

### ***"Characterization" Risks***

If an applicable court or regulatory authority were to make an adverse finding, or take an adverse action on the basis that one of Pawnee's leases is not a true lease, for commercial law, tax law, or other legal purposes, adverse consequences could result with respect to such lease



including the loss of preferred creditor status (which would impact upon Pawnee's rights to recover on its claim), limitations on finance changes and other fees that can be enforced, and additional federal, state and other (income or sales) taxes payable by Pawnee.

Management of Pawnee believes that the leases currently being originated and those leases originated since July of 2003 are true leases for commercial law, tax law, and other legal purposes. However, Pawnee's management has determined that as at March 31, 2008 approximately 0.34% of the gross lease receivable balance of its existing portfolio consists of nominal purchase option leases which would probably be interpreted by a court to be non-true leases. If Pawnee were to become the subject of adverse judicial or regulatory action resulting in penalties, fines, or the inability to collect lease payments and/or interest with respect to a significant amount of its leases as a result of a determination that such leases were not true leases, it could have a material adverse impact on our business, financial condition and results of operations, and the amount of cash available for distribution to our unitholders.

#### ***Defenses to Enforcement of a Significant Amount of Leases***

Certain defenses and recovery impediments are more common in micro and small-ticket equipment finance transactions than with respect to equipment finance providers in other segments of the equipment finance industry. Management believes that certain of these risks are sufficiently addressed in Pawnee's existing lease documentation and related business practices. However, there are other risks that Pawnee has not addressed for various reasons, including that certain of these risks are not susceptible to being addressed either at all, or without incurring cost inefficiencies or taking other measures deemed unacceptable by Pawnee's management based on a risk-reward assessment. Pawnee has never experienced any material occurrence of these risks nor have these risks historically had a material adverse impact on Pawnee. However, there is no assurance that these risks will not have a material adverse impact on Pawnee's business, financial condition and results of operations in the future.

#### ***Origination, Funding and Administration of Transactions***

Pawnee's origination, funding and transaction administration practices could result in certain vulnerabilities in its enforcement rights. For example, certain of Pawnee's leases are assignments of transactions already documented by its lease brokers. Acquiring leases by this "indirect" process subjects Pawnee to various risks, including risks that might arise by reason of the broker's insolvency, administrative inadequacies or fraudulent practices, as well as any third party claims against the broker or its rights with respect to the assigned lease. Any of these broker related risks can impair Pawnee's rights with respect to recovering the rents and/or leased property under its leases. Pawnee has not been involved in any claims or litigation in relation to such risks and Pawnee does not conduct lien searches in the name of, require lien releases from or file financing statements against the lease broker.

If the lessee or broker is the party to whom the vendor of the leased equipment has agreed to sell the leased property at the time of its delivery, then, under applicable commercial law, the lessee or broker, as applicable, may be deemed to have acquired title to the leased property prior to Pawnee's having funded the transaction. It has not been Pawnee's practice to ensure that the title to the leased property has not already passed or to obtain assurances that it is acquiring good title to that property free of liens and other third party claims. The manner in which Pawnee purchases the leased equipment is typical in this market segment, especially with respect to similarly situated equipment financing providers. Pawnee has not yet faced any meaningful challenge or adverse consequence from this practice, but there can be no assurance that such a challenge or consequence will not occur in the future.

In circumstances where the leased equipment is less than US\$15,000 (or US\$10,000, if for a home business), Pawnee's practice of requiring only a verbal confirmation that the leased property has been delivered and irrevocably accepted under the subject lease, and/or inspecting the leased property to confirm the same, could make Pawnee vulnerable to certain defenses. By way of example, Pawnee's deemed failure to deliver conforming property under the lease documents could be a defense to a lessee's "unconditional" obligation to pay the rents and certain other amounts under the related lease. Pawnee has not suffered any material losses relating to these practices, however, there can be no assurance that it would not in the future.

#### ***Changes in Governmental Regulations, Licensing and Other Laws and Industry Codes of Practice***

Leasing companies are subject to laws and regulations relating to extending financing generally and are also members of industry associations which have adopted, among other things, codes of business practice. Laws, regulations and codes of business practice may be adopted with respect to existing leases or the leasing, marketing, selling, financing and collections processes which might increase the costs of compliance of Pawnee and Lease-Win, or require them to alter their respective businesses, strategies or operations.

### ***State Licensing Requirements***

If an applicable court or regulatory authority were to make an adverse finding or otherwise take adverse action with respect to Pawnee based on its failure to have a finance lender's or other license or registration required in the applicable state, Pawnee would have to change business practices and could be subject to financial or other penalties.

### ***Fees and Charges***

Pawnee's lease documents require payment of late payment fees, late charge interest, and other charges either relating to the non-payment, or enforcement of its leases. It could be determined that these fees and interest exceed applicable statutory or other legal limits. If the charges are deemed to be punitive and not compensatory, or to have other attributes that are inconsistent with or in violation of applicable laws, they could be difficult to enforce. A number of charges payable with respect to lease transactions in the micro and small-ticket equipment finance market have been the subject of litigation by customers against financing parties over the past few years. Although Pawnee is not currently the subject of any such litigation, there can be no assurance that a lessee or a group of lessees will not attempt to bring a lawsuit against Pawnee in relation to fees and charges, which Pawnee may or may not be successful in defending.

Pawnee believes that its fee programs are designed and administered so as to comply with legal requirements and are within the range of leasing company practices in its market segment. Nevertheless, certain attributes of these fees or charges, and Pawnee's practices, including that its leases typically provide for several different fees and charges resulting in a substantial amount of fee income and the possibility that the fees and charges may exceed actual costs involved or may otherwise be deemed excessive, could attract litigation, including class actions, that would be costly even if Pawnee were to prevail and as to which no assurance can be given of Pawnee's successful defense. In addition to the risk of litigation, fee income is important to Pawnee and the failure of Pawnee to continue to collect most or all of these fees could have a material adverse impact on our business, financial condition and results of operations, and on the amount of cash available for distribution to our unitholders.

### ***Possible Acquisitions***

The growth strategy for the Fund includes seeking out acquisitions in the financial services industries. Acquisitions, if they occur, may increase the size of the operations as well as increase the amount of indebtedness that may have to be serviced by the Fund and its subsidiaries. There is no assurance that such acquisitions can be made on satisfactory terms, or at all. The successful integration and management of acquired businesses involve numerous risks that could adversely affect the growth and profitability of the Fund and its subsidiaries. There is no assurance that such acquisitions will be successfully integrated.

### ***Insurance***

To ensure that the lessor of the item of leased property suffering a loss receives the related insurance proceeds, the lease also requires that the lessor be named as a loss payee under the requisite casualty coverage. However, each lessee is ultimately relied upon to obtain and maintain the required coverage for leased equipment but there is no certainty that they will obtain the requisite coverage either conforming to the requirements of the lease, or at all. Additionally, there are often policy provisions including exclusions, deductibles and other conditions that by their terms, or by reason of a breach, could limit, delay or deny coverage. There can be no assurance that any insurance will protect our operating company's interest in the equipment, and the failure by the lessee to obtain insurance or the failure by the operating companies to receive the proceeds from such insurance policies could have a material adverse impact on our business, financial condition and results of operations, and on the amount of cash available for distribution to our unitholders.

### ***Lessor Liability***

There is a risk that a lessor, such as Pawnee or Lease-Win, could be deemed liable for harm to persons or property in connection with, among other things, the ownership or leasing of the leased property, or the conduct or responsibilities of the parties to the lease relating to that property. The liability may be contractual (such as warranties regarding the equipment), statutory such as federal, state or provincial environmental liability or pursuant to various legal theories (such as negligence). There have been cases in which a lessor has been held responsible for damage caused by leased property without a showing of negligence or wrong-doing on the lessor's part. Even if a lessor ultimately succeeds in defending itself or settling any related litigation, the related costs and any settlement amount could be significant.



### ***Liability for Misuse of Leased Equipment***

There is no practical manner to ensure that leased equipment or a leased vehicle will be used, maintained or caused to comply with applicable law. Pawnee requires its lessees to deliver evidence of compliance with same as a condition to funding but has no assurance (and Lease-Win has no assurance) that a lessee will take the appropriate actions during the lease term to address any use, maintenance or compliance issues which may arise. A lessee's conduct (or lack thereof) could subject Pawnee or Lease-Win, as applicable, to liability to third parties.

### ***Estimates Relating to Value of Leases***

Based on the particular terms of a lease, leasing companies estimate the residual value of the financed equipment or vehicle, which is recorded as an asset on its balance sheet. At the end of the lease term, leasing companies seek to realize the recorded residual for the equipment or vehicle by selling the equipment or vehicle to the lessee or in the secondary market or through renewal of the lease by the lessee. The ultimate realization of the recorded residual values depends on numerous factors, including: accurate initial estimate of the residual value; the general market conditions and interest rate environment at the time of expiration of the lease; the cost of comparable new equipment or vehicle; the obsolescence of the leased equipment or vehicle; any unusual or excessive wear and tear on or damage to the equipment or vehicle; and the effect of any additional or amended government regulations.

If Pawnee or Lease-Win (in connection with those leases where the lessee is not obligated to either purchase the equipment or guarantee the residual value of the equipment at the end of the term of the lease) is unable to accurately estimate or realize the residual values of the leased equipment or vehicles subject to their leases, the amount of recorded assets on its balance sheet will have been overstated.

### ***Competition From Alternative Sources of Equipment Financing***

The business of micro and small-ticket equipment leasing in the United States is highly fragmented and competitive. Pawnee focuses its business on the segment of the micro and small-ticket leasing market involving start-up businesses that have not established business credit or established businesses that have experienced some credit difficulty in their history that do not meet the credit standards of more traditional financing sources. Pawnee's main competition comes from leasing companies, home equity loans, and credit cards.

If Pawnee expands its suite of products to target potential lessees with higher credit scores or if the creditworthiness of its potential customers increases for various external reasons, it can expect to face competition from more traditional financing sources as well, including: national, regional and local finance companies; captive finance and leasing companies affiliated with major equipment manufacturers; and financial services companies, such as commercial banks, thrifts and credit unions.

Many of the firms and institutions providing financing alternatives are substantially larger than Pawnee and have considerably greater financial, technical and marketing resources. Some of them may have a lower cost of funds and access to funding sources that are unavailable to Pawnee. A lower cost of funds could enable a competitor to offer leases with pricing lower than that of Pawnee, potentially forcing Pawnee to decrease its prices or lose origination volume. In addition, some financing sources may have higher risk tolerances or different risk assessments, which could allow them to establish more origination sources and customer relationships to increase their market share.

Further, because there are fewer barriers to entry with respect to the micro and small-ticket leasing market, new competitors could enter this market at any time, especially if an improvement in the economy leads to a greater ability of small businesses to establish improved levels of creditworthiness.

### ***Fraud by Lessees, Vendors or Brokers***

While Pawnee makes every effort to verify the accuracy of information provided to it when making a decision whether to underwrite a lease and has implemented systems and controls to protect itself against fraud, in a small number of cases in the past Pawnee has been a victim of fraud by lessees, vendors and brokers. In cases of fraud, it is difficult and often unlikely that Pawnee will be able to collect amounts owing under a lease or repossess the related equipment. Increased rates of fraud could have a material adverse impact on our business, financial condition and results of operations, and on the amount of cash available for distribution to our unitholders.

### ***Protection of Intellectual Property***

Pawnee continually develops and improves its brand recognition, which has been an important factor in maintaining its competitive position. No assurance can be given that others will not independently develop substantially similar branding. Despite Pawnee's efforts to protect its proprietary rights, unauthorized parties may attempt to obtain and use information that Pawnee regards as proprietary. Stopping unauthorized use of Pawnee's proprietary rights may be difficult, time-consuming and costly. There can be no assurance that Pawnee will be successful in protecting its proprietary rights.

### ***Failure of Computer and Data Processing Systems***

Our operating companies are dependent upon the successful and uninterrupted functioning of their computer and data processing systems. The failure of these systems could interrupt operations or materially impact Pawnee and Lease-Win's ability to originate and service their lease portfolios and broker networks. If sustained or repeated, a system failure could negatively affect the operations of Pawnee and Lease-Win. Pawnee and Lease-Win maintain confidential information regarding lessees in their computer systems. This infrastructure may be subject to physical break-ins, computer viruses, programming errors, attacks by third parties or similar disruptive problems. A security breach of computer systems could disrupt operations, damage reputation and result in liability.

### ***Competition in the Automobile Retailing Industry***

The automotive retailing industry is competitive. In large metropolitan areas, consumers have a number of choices in deciding where to purchase a new or used vehicle and where to have such vehicle serviced.

### ***Competition in the Automobile Leasing Industry***

The automotive leasing industry is competitive. Lease-Win's competition, being in many cases financial institutions and finance companies, often have a lower cost of funds than Lease-Win. Any increase in activity by these institutions or the entry into this market of new participants with a lower cost of funds or other competitive advantages could have a material adverse impact on our business, financial condition and results of operations, and on the amount of cash available for distribution to our unitholders. Additionally, increased competition may adversely affect operating margins and result in loss of market share.

### ***Manufacturers' Control Over Dealerships and the Acura Framework Agreement***

Automobile dealerships operate pursuant to dealer agreements with automobile manufacturers. Through the terms and conditions of these dealer agreements, automobile manufacturers exert considerable influence over the operations of dealerships.

The success of an automobile dealership is highly dependent upon the overall success of the line of vehicles that each dealership sells. Sherway LP's business is affected to varying degrees by the demand for its manufacturers' vehicles, and by the financial condition, management, marketing, production and distribution capabilities of such manufacturers. In addition, the timing, structure and amount of manufacturer incentives may impact the timing and profitability of sales transactions. Events such as labour disputes and other production disruptions that may adversely affect a manufacturer may also adversely affect Sherway LP. Similarly, the delivery of vehicles from manufacturers later than scheduled or diminished availability to Sherway LP of popular makes, models and/or accessories, which may occur particularly during periods of new product introductions, can lead to reduced sales during such periods. Moreover, any event that causes adverse publicity involving such manufacturers may have an adverse effect on Sherway LP.

### ***Accounting for the Securitization of Leases***

Lease-Win is party to various securitization transactions with an off-balance sheet component. The policies discussed below are considered by management to be critical to securing an understanding of Chesswood's financial statements, as they require the use of significant judgment and estimation in order to measure, at a specific point in time, matters that are inherently uncertain. For all of these policies, management cautions that future events rarely develop precisely as forecasted, and estimates routinely require adjustment and may require material adjustment.

Substantially all leases originated by Lease-Win are sold to a securitization trust. Lease-Win removes the leases from its balance sheet and records a gain on the sale. Lease-Win retains an interest in the leases in the form of a interest-only strip and deferred proceeds (residual

interest), and assumes first risk of credit losses up to the amount of the reserve held at the Securitization Trust. As the cash flows of the underlying leases and market conditions change, the value of Lease-Win's residual interests may also change, resulting in either additional unrealized gains or impairment of the residual interests.

All leases securitized are transferred with servicing rights retained. Servicing activities include processing of lease payments and the administration of leases. Lease-Win provides for an estimated servicing fee of 1.5% on the outstanding gross receivable of leases securitized, as well as the right to receive certain ancillary income including, but not limited to, late fees and prepayment penalties. Estimated lease servicing costs are recorded in the current liabilities at allocated carrying amounts based on original lease receivable balances. Variations in the prepayment rate assumptions could materially affect the carrying value of the estimated lease servicing liabilities.

Lease-Win is required, under the terms of the securitization, to build and/or maintain reserves to specified levels, using the excess cash flows received, until specified percentages of the securitized portfolio are attained. Lease-Win funds the reserve account from the proceeds of the sale. Upon maturity of the leases, any remaining amounts in the securitization trust are distributed. The estimated future cash flows to be distributed to Lease-Win are included as part of the residual interest and are valued upon the timing of the distribution from the reserve account.

Revenues consist of proceeds from the sale of lease receivables, accretion or impairment on residual interests and excess interest spread received on leases.

### ***Security Risks***

Despite implementation of network security measures similar to most other on-line e-commerce sites, the infrastructure of the cars4U.com website is potentially vulnerable to computer break-ins and similar disruptive problems.

### ***Cyclical and Seasonality***

Sales of motor vehicles, particularly new vehicles, historically have been subject to cyclical and seasonal variations. Management believes that the industry is affected by many factors, including general economic conditions, consumer confidence, and the level of personal discretionary spending, interest rates and credit availability. There can be no assurance that the industry will not experience sustained periods of decline in vehicle sales, particularly new vehicle sales, in the future.

### ***Imported Products***

A significant portion of the new vehicle business of the Sherway LP dealership involves the sale of vehicles, parts or vehicles composed of parts that are manufactured outside North America. As a result, the operations of the Sherway LP dealership are subject to customary risks of selling imported merchandise, including fluctuations in the value of currencies, changes in import duties, exchange controls, trade restrictions, work stoppages and general political and economic conditions in foreign countries.

### ***Environmental Matters***

Sherway LP is subject to a wide range of federal, provincial and local environmental laws and regulations, including those governing discharges to the air and water, the storage of petroleum substances and chemicals, the handling and disposal of wastes and the remediation of contamination arising from spills and releases. As with automobile dealerships generally, and parts, service and collision service centre operations in particular, Sherway LP's business involves the generation, use, handling and disposal of hazardous or toxic substances or wastes.

Environmental laws and regulations have become very complex and it has become very difficult for businesses that routinely handle hazardous and non-hazardous wastes to achieve and maintain full compliance with all applicable environmental laws. From time to time, Sherway LP can be expected to experience incidents and encounter conditions that will not be in compliance with environmental laws and regulations.

However, Sherway LP has not been subject to any material environmental liabilities in the past and it is not anticipated that any material environmental liabilities will be incurred by it in the future. In addition, to minimize the risk of environmental liability related to acquired dealerships, Sherway LP intends to obtain environmental studies on such dealerships as a condition to their acquisition.

Environmental laws and regulations and their interpretation and enforcement are changed frequently and the trend of more expansive and stricter environmental legislation and regulations is likely to continue. Hence, there can be no assurance that compliance with environmental laws or regulations or the future discovery of unknown environmental conditions will not require additional expenditures or that such expenditures would not be material.

#### ***Risks Related to our Structure and Exchange Rate Fluctuations***

The distributions expected to be made to our unitholders will be denominated in Canadian dollars, however, a significant percentage of our revenues are expected to be derived from the revenues of Pawnee, which is in U.S. dollars. Changes in the value of the U.S. dollar could have a negative impact on the amount in Canadian dollars available for distribution to our unitholders.

#### ***Unpredictability and Volatility of Unit Price***

A publicly-traded income trust will not necessarily trade at values determined by reference to the underlying value of its business. The prices at which the Fund Units will trade cannot be predicted. The market price of the Fund Units could be subject to significant fluctuations in response to variations in quarterly operating results and other factors. The annual yield on the Fund Units as compared to the annual yield on other financial instruments may also influence the price of Fund Units in the public trading markets. In addition, the securities markets have experienced significant price and volume fluctuations from time to time in recent years that often have been unrelated or disproportionate to the operating performance of particular issuers. These broad fluctuations may adversely affect the market price of the Fund Units.

#### ***Leverage, Restrictive Covenants***

Pawnee, Lease-Win and Sherway LP have third party debt service obligations under their respective credit facilities. The degree to which our subsidiaries are leveraged could have important consequences to our unitholders, including: (i) the ability of such subsidiaries to obtain additional financing for working capital in the future may be limited; (ii) a portion of the cash flow from the assets of such subsidiaries may be dedicated to the payment of the principal of and interest on their respective indebtedness, thereby reducing funds available for distribution to the Fund; and (iii) certain of the respective borrowings of such subsidiaries will be at variable rates of interest, which will expose them to the risk of increased interest rates. The ability of such subsidiaries to make scheduled payments of the principal of or interest on, or to refinance, their indebtedness will depend on their future cash flow, which is subject to their respective assets prevailing economic conditions, prevailing interest rate levels, and financial, competitive, business and other factors, many of which are beyond their control.

#### ***Loss of Limited Liability***

On December 16, 2004, the *Trust Beneficiaries' Liability Act, 2004*, a new Ontario Statute included in Bill 106, received Royal Assent. That statute provides, in effect, that our unitholders are not liable, as beneficiaries of a trust, for any act, default, obligation or liability of the Fund or as trustees, arising after December 16, 2004. That statute has not yet been judicially considered and it is possible that reliance on the statute by a unitholder could be successfully challenged on jurisdictional or other grounds.

#### ***Statutory Remedies***

Although the Fund is a legal entity, it is not generally regulated by established corporate law and unitholders' rights are governed primarily by the specific provisions of our Declaration of Trust, which addresses such items as the nature of the Fund Units, the entitlement of our unitholders to cash distributions, restrictions respecting non-resident holdings, meetings of our unitholders, delegation of authority, administration, Fund governance and liabilities and duties of the Fund's trustees to our unitholders. As well, under certain existing legislation such as the *Bankruptcy and Insolvency Act* (Canada) and the *Companies Creditor's Arrangement Act* (Canada), the Fund is not a legally recognized entity within the definitions of these statutes. In the event of an insolvency or restructuring of the Fund, the rights of our unitholders will be different from those of shareholders of an insolvent or restructuring corporation.

#### ***Restrictions on Potential Growth***

The payout by our operating companies of a significant portion of their distributable cash will make additional capital and operating expenditures dependent upon increased cash flow or additional financing in the future. Lack of those funds could limit the future growth of our operating companies and their cash flow. In addition, recently proposed federal taxation measures would provide expedited applicability of taxation of income trusts to the Fund if we issue equity in excess of certain prescribed annual limits.

### ***Canadian Income Tax Matters***

The income of the Fund and its related entities must be computed in accordance with Canadian and foreign tax laws, as applicable, and the Fund is subject to Canadian tax laws, all of which may be changed in a manner that could adversely affect the amount of distributable cash. There can be no assurance that Canadian federal income tax laws and administrative policies respecting the treatment of mutual fund trusts will not be changed in a manner which will adversely affect our unitholders. On October 31, 2006, the Minister of Finance (Canada) announced proposals to amend Canadian tax laws such that many income trusts which are not currently taxable will become taxable as of 2011. If the proposed amendments are enacted, then to the extent they are determined to apply to the Fund, the amount of cash available for distribution to our unitholders would be reduced.

### ***United States Income Tax Matters***

There can be no assurance that U.S. federal income tax laws and administrative policies will not develop or be changed in a manner that adversely affects our unitholders.

Subject to the “earnings stripping” rules and other restrictions on deductibility of interest, U.S. Acquisitionco treats the US\$33.5 million subordinated note it has issued to a Canadian subsidiary of the Fund (the “Subordinated Acquisitionco Debt”) as debt for all purposes, and claims interest deductions with respect to the Subordinated Acquisitionco Debt in computing its income for U.S. federal income tax purposes. There is a risk that the U.S. Internal Revenue Service (the “IRS”) could successfully argue that the Subordinated Acquisitionco Debt should be treated as equity rather than debt for U.S. federal income tax purposes, however, in which case the otherwise deductible interest on such indebtedness would be treated as non-deductible distributions (and potentially subject to a divided withholding tax).

A successful challenge of this position would increase the U.S. federal income tax liability of U.S. Acquisitionco, due to the absence of tax deductions for interest payments. Together with the possible dividend withholding tax on such payments, the amount of after-tax cash generated that would otherwise be available to make payments on the Subordinated Acquisitionco Debt and distributions to the Canadian subsidiary of the Fund which is a shareholder of U.S. Acquisitionco would be reduced, thereby having an adverse effect on the cash flow of the Fund available for distribution to our unitholders.

Even if the Subordinated Acquisitionco Debt is respected as debt for U.S. federal income tax purposes, there is a risk that the IRS may challenge the interest rate on such indebtedness as being in excess of an arm’s length rate. If the IRS were successful in challenging the interest rate, U.S. Acquisitionco would not be able to fully deduct interest paid on such indebtedness, and a dividend withholding tax may result, both of which could increase the U.S. federal income tax liability and thereby reduce cash flow of the Fund available for distribution to our unitholders.

In addition, there can be no assurance that future changes to U.S. federal income tax provisions will not otherwise restrict or eliminate the ability of U.S. Acquisitionco to claim a deduction for U.S. federal income tax purposes for interest paid on such indebtedness. In this regard, proposed legislation has been introduced, through not enacted, several times in recent years to amend existing laws or regulations, particularly with respect to “earning stripping” rules.

Other limitations on the deductibility of interest under U.S. federal income tax laws, potentially including limitations applicable to certain high-yield debt obligations, could apply under certain circumstances to defer and/or eliminate all or a portion of the interest deduction that U.S. Acquisitionco would otherwise be entitled to with respect to interest on such indebtedness. Furthermore, if the payment were recharacterized as a dividend, the imposition of a dividend withholding tax with respect to the payments coupled with the increased U.S. federal income tax liability of U.S. Acquisitionco would reduce the cash flow of the Fund available for distribution to our unitholders.

There is a risk that the “portfolio interest exemption” may not be available to any of the Fund’s non-U.S. unitholders. If that occurs, U.S. withholding tax at a rate of 30% (subject to possible reduction to 10% under the Canada – U.S. tax treaty) may be imposed on interest payments on the Subordinated Acquisitionco Debt, and thus the cash flow of the Fund available for distribution to our unitholders may be adversely affected. U.S. Acquisitionco intends to take the position that the “portfolio interest exemption” should apply for those non-U.S. unitholders who meet certain ownership, identity and certification requirements, provided that the Fund is classified as a partnership for U.S. federal income tax purposes (and as long as it meets the “qualifying income exception” to the U.S. publicly traded partnership rules). U.S. Acquisitionco has received an opinion from U.S. tax counsel that the portfolio interest exemption should apply to non-U.S. unitholders. There is limited, non-binding IRS authority that the 10% threshold should be determined at the Fund unitholder level, not at the Fund level, which generally would allow for the portfolio interest exemption to apply. There can be no certainty, however, that the IRS will not take a contrary position. Furthermore, Treasury or the U.S. Congress may enact regulations or legislation, respectively, that supersede



this position. If the portfolio interest exemption did not apply, U.S. withholding tax would arise on the interest payments made to the Fund that are attributable to our non-U.S. unitholders. This would have an adverse effect on the cash flow of the Fund available for distribution to our unitholders.

Although the burden of the U.S. tax liability would fall ultimately upon the non-U.S. unitholder that does not qualify for the portfolio interest exception, the obligation to withhold the U.S. taxes due would fall on U.S. Acquisitionco. U.S. Acquisitionco is not anticipating the imposition of any withholding obligation provided that the ownership, identity and certification requirements are met, and is not establishing any reserves or hold-backs to fund any such obligation. If the IRS were to seek collection of unpaid withholding taxes from U.S. Acquisitionco, U.S. Acquisitionco may also be subject to interest and penalties, which would reduce the available cash flow for all our unitholders.

U.S. Acquisitionco has not established any procedure for monitoring the level of investment of non-U.S. unitholders, so its assumption that individual non-U.S. unitholders will hold less than 10% of the stock of U.S. Acquisitionco (after the application of U.S. attribution rules) is based solely upon its observations of patterns of trading in similar Canadian investment funds.

If any non-U.S. unitholder is or becomes ineligible for the portfolio interest exemption, such unitholder is required to give notice to the Fund, pursuant to our Declaration of Trust. The Declaration of Trust contains provisions that allow U.S. Acquisitionco and the Fund to recover from a unitholder amounts that should have been but were not withheld from a distribution to such unitholder because of failure to provide such notice. However, there can be no assurance that U.S. Acquisitionco and the Fund will be able to recover these amounts in full or at all, which could result in a reduction in cash available for distribution to other unitholders.

It is possible that new U.S. “corporate inversion” tax rules could apply to U.S. Acquisitionco’s acquisition of Pawnee. If these rules were to apply, they could prevent certain types of income of Pawnee from being offset by certain tax attributes such as loss carryforwards. However, because it is not anticipated that Pawnee will have significant amounts of the types of income that are subject to these rules, the potential adverse effect of these rules should not be significant.

## **RELATED PARTY TRANSACTIONS**

1) Debentures in the principal amount of \$2.2 million (out of the aggregate \$3.5 million principal amount of the Debentures) were issued to trustees of the Fund and/or directors of Chesswood GP Limited, which is a 100% owned subsidiary of the Fund.

2) Pawnee leases a 10,800 square foot office facility. The lessor is a related party because of common ownership between itself and the holders of the Class B and C common shares of U.S. Acquisitionco. As of March 31, 2008, the minimum lease payments are US\$189,000 per year triple net and run through 2011, with options for two additional five-year terms.

## **CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

Understanding the Fund’s accounting policies is essential to understanding the results of the Fund’s operations and financial condition. The Fund’s significant accounting policies are described in Note 1 to the Fund’s consolidated financial statements for the year ended December 31, 2007. The new accounting policies adopted on January 1, 2008 are described in Note 1 to the Fund’s interim consolidated financial statements for the three-months ended March 31, 2008. The preparation of these financial statements requires us to make estimates and judgments that affect reported amounts of assets and liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities at the date of our financial statements. On an ongoing basis, we evaluate our estimates, including credit losses, residuals, initial direct costs and fees, other fees and realizability of deferred tax assets. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Critical accounting policies are defined as those that are reflective of significant judgments and uncertainties. Our financial statements are based on the selection and application of critical accounting policies, the most significant of which are described below.

### **Revenue Recognition**

Direct financing lease income is recognized under the effective interest method. The effective interest method of income recognition applies a constant rate of interest equal to the internal rate of return on the lease.

### **Late Fee and Other Income**

Late fee and other income consists of charges and fees for such things as administration fees to process each lease at origination, late fees, collection call charges, property tax management fees, interim rental fees, insurance fees and lease termination fees. Fee income also includes net residual income, which includes income from lease renewals and gains and losses on the realization of residual values of equipment disposed of at the end of term. Fees are recognized when received. Net residual income includes charges for the reduction in estimated residual values on equipment for leases in renewal and is recognized during the renewal period.

### **Lease Residual Values**

A direct financing lease is recorded at the aggregate future minimum lease payments plus the estimated residual values less unearned income. Residual values reflect the estimated amounts to be received at lease termination from lease extensions, sales or other dispositions of leased equipment. These estimates are based on industry data and on our experience. Management performs periodic reviews of the estimated residual values and any impairment, if other than temporary, is recognized in the current period.

### **Allowance for Credit Losses**

Pawnee's policy is to maintain an allowance for doubtful accounts, as a percentage of its net investment in leases, equal to the last twelve-month rolling net charge-off percentage level. Pawnee uses a comprehensive proprietary software tracking system that permits it to track all of the receivables by various categories. Receivables are normally tracked by type of industry and equipment, geographic location, size of lease, and broker. Additional tracking is created on a case-by-case basis as new programs are added or management desires to evaluate specific aspects of the portfolio's performance. A provision is charged against earnings to maintain the allowance for credit losses at the appropriate level.

Projections of Pawnee's probable net credit losses are inherently uncertain, and as a result we cannot predict with certainty the amount of such losses. Changes in economic conditions, the risk characteristics and composition of the portfolio, bankruptcy laws, and other factors could impact Pawnee's actual and projected net credit losses and the related allowance for credit losses.

At Lease-Win, management reviews each outstanding receivable, on an individual basis, for collectibility and for reserve requirements, if any.

### **Accounting for the Securitization of Leases and Off-Balance Sheet Arrangements**

The Fund, through its subsidiary Lease-Win, transfers or sells receivables to a securitization trust (the "Securitization Trust") as a means of financing its automobile finance contracts. These securitization transactions have an off-balance sheet component. These transactions are currently considered a sale under Canadian GAAP. As such, Lease-Win is required to make estimates in respect of frequency, timing and severity of losses and prepayment on the underlying pools of assets sold, which impacts the future expected cash flows Lease-Win would expect to receive from the sale of the receivables. The expected cash flows are discounted at a rate that Lease-Win feels is commensurate with the underlying risk of the receivables. Changes in these estimates or significant variations in actual performance from these estimates could significantly impact Lease-Win's financial results in a period.

Substantially all leases originated are sold to the Securitization Trust which result in the sale of the leases. Lease-Win removes the leases from its balance sheet and records a gain on the sale. Lease-Win retains an interest in the leases in the form of an interest-only strip and deferred proceeds (residual interest and cash reserve monies), that is recorded as an asset on the balance sheet and assumes first risk of credit losses up to the amount of the reserve held by the Securitization Trust. As the cash flows of the underlying leases and market conditions change, the value of Lease-Win's residual interests may also change, resulting in either additional unrealized gains or impairment of the residual interests.

All leases securitized are transferred with servicing rights retained. Servicing activities include processing of lease payments and the administration of leases. Lease-Win provides for an estimated servicing fee of 1.5% on the outstanding gross receivable of leases securitized, as well as the right to receive certain ancillary income including, but not limited to, late fees and prepayment penalties. Estimated lease servicing costs are recorded in the liabilities at allocated carrying amounts based on original lease receivable balances. Variations in the prepayment rate assumptions could materially affect the carrying value of the estimated lease servicing liabilities.

Lease-Win is required, under the terms of its securitizations, to build and/or maintain reserves to specified levels, using the excess cash flows received, until specified percentages of the securitized portfolio are attained. Lease-Win funds the reserve account from the proceeds of the sale. Upon maturity of the leases, any remaining amounts in the Securitization Trust are distributed. The



estimated future cash flows to be distributed to Lease-Win are included as part of the residual interest and are valued upon the timing of the distribution from the reserve account.

Revenue from automotive operations include revenues from proceeds from the sale of lease receivables, accretion or impairment on residual interests, lease servicing fees and excess interest spread received on leases.

### **Gains on Sale of Lease Receivables**

When Lease-Win securitizes its lease receivables, it records a gain on sale. Lease-Win calculates the gains on sale as the cash proceeds less the allocated cost of leases sold and the estimated servicing liability. The relative fair value of the receivable is determined using discounted cash flow models, which require various management assumptions (see discussion below under “Valuation of Residual Interests”). Variations in these assumptions affect the estimated fair values, which would affect the reported gains on sale.

### **Valuation of Residual Interests**

Lease-Win uses discounted cash flow models to arrive at the estimated fair values of its residual interests. The fair value of residual interests is estimated by computing the present value of the future cash flows from the retained interest and the reserve account less expected losses to be incurred on the portfolio of the leases sold (as projected to occur) over the terms of the leases. Prepayment and loss assumptions used in estimating the cash flows are based on evaluations of the actual experience of Lease-Win’s servicing portfolio, the characteristics of the applicable lease portfolio, as well as taking into consideration the current economic and interest rate environments and their expected impact. The prepayment speeds are somewhat correlated with the movement of market interest rates. As market interest rates decline there is a corresponding increase in actual and expected borrower prepayments as customers refinance existing leases under more favourable interest rate terms. This, in turn, reduces the anticipated cash flows from the residual interests. The estimated cash flows are discounted at an interest rate Lease-Win believes an unaffiliated third-party purchaser would require as a rate of return on a financial instrument with a similar risk profile. Lease-Win evaluates the fair values of residual interests quarterly by updating the actual and expected assumptions in the discounted cash flow models based on current information and events and by estimating, or validating with third-party experts, if necessary, what a market participant would use in determining the current fair value. Variations in the above assumptions, as well as the discount rate and interest rate assumptions, could materially affect the estimated fair values, which may require Lease-Win to record impairments or unrealized gains. In addition, variations will also affect the amount of residual interest accretion recorded on a monthly basis.

As the cash flows of the underlying leases and market conditions change, the value of Lease-Win’s residual interest may also change, resulting in either additional unrealized gains or impairment of the value of the residual interests.

### **Accounting for Goodwill and Intangible Assets**

Current GAAP require that goodwill and other intangible assets with indefinite useful lives no longer be amortized, but instead evaluated for impairment on an annual basis, or more frequently if certain events or circumstances exist. The Fund will evaluate the goodwill balances in the last quarter of each fiscal year. If the fair value of a subsidiary is less than its carrying value, then the implied fair value of the goodwill must be compared to the carrying value of that goodwill. In the instance that the fair value of the goodwill is less than the carrying value, goodwill is deemed to be impaired and an impairment loss, equal to the amount by which the fair value exceeds the carrying value, must be recorded.

The performance of the goodwill impairment test is subject to significant judgment in determining the fair value of the subsidiaries, due to the estimation of future cash flows, discount rates, and other assumptions. Changes in these estimates and assumptions could -- have a significant impact on the fair value and/or goodwill impairment.

### **Interest Rate Swaps and Foreign Exchange Contracts**

Hedge accounting requires recognition of the fair value of all derivative instruments on the balance sheet as either assets or liabilities. Changes in a derivative’s fair value are recognized currently in earnings unless specific hedge accounting criteria are met. Gains and losses on derivative hedging instruments must be recorded in either other comprehensive income or current earnings, depending on the nature and designation of the instrument.

Pawnee’s interest rate swaps are not considered trading instruments as Pawnee intends to hold them until termination. Nonetheless, the interest rate swaps do not qualify as a hedge for accounting purposes, and are therefore recorded as separate derivative financial instruments. Accordingly, the estimated fair value of the interest rate swaps are recorded as an asset or a liability on the

accompanying consolidated balance sheet. Payments made and received pursuant to the terms of the interest rate swaps are recorded as an adjustment to interest expense, and adjustments to the fair value of the interest rate swaps are recorded as gain or loss on interest rate swaps. The fair value of interest rate swaps is based upon the estimated net present value of cash flows, and does not necessarily reflect the amount that would be required to settle the interest rate swaps.

Chesswood Holdings LP, a wholly owned subsidiary of the Fund, had entered into foreign exchange contracts to manage its exposure to the U.S. dollar as significant cash flows for unitholder distributions are generated in the U.S. As the foreign exchange contracts related to equity transactions, they did not qualify as a hedge for accounting purposes, and were therefore recorded as separate derivative financial instruments. The fair value was determined from a monthly market valuation report obtained from its bank counterparty.

### **Income Taxes**

Pawnee and Lease-Win use the asset and liability method to account for income taxes. Under the asset and liability method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. The measurement of deferred tax assets is reduced, if necessary, by a valuation allowance for future tax benefits for which realization is not considered more likely than not. Pawnee and Lease-Win account for their lease arrangements as operating leases for federal income tax reporting purposes. This results in temporary differences between financial and income tax reporting for which deferred taxes have been provided.

Significant management judgment is required in determining the provision for income taxes, deferred tax assets and liabilities and any necessary valuation allowance recorded against net deferred tax assets. The process involves summarizing temporary differences resulting from the different treatment of items, for example leases for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within the consolidated balance sheet. Our management must then assess the likelihood that deferred tax assets will be recovered from future taxable income or tax carry-back availability and, to the extent our management believes recovery is not likely, a valuation allowance must be established. To the extent that we establish a valuation allowance in a period, an expense must be recorded within the tax provision in the statement of operations.

On October 31, 2006, the Minister of Finance for Canada ("Finance") announced proposed changes to the Income Tax Act (Canada) which modify the taxation of certain flow-through entities including mutual fund trusts and their unitholders. On June 22, 2007, this legislation received royal assent and applies a 30.5% tax at the trust level on distributions of certain income from a "specified investment flow through" ("SIFT") trust and treats such distributions as dividends to unitholders. The legislation provides that existing SIFT trusts will be grandfathered and the trust distribution tax will not apply until 2011 as long as normal growth guidelines are met.

The Fund is considered a SIFT trust and is expected to be subject to the trust distribution tax commencing in 2011 assuming no changes in the current structure occur. GAAP requires the Fund to recognize future income tax assets and liabilities based on estimated temporary differences expected as at January 1, 2011, and on the basis of its structure at the balance sheet date. GAAP does not permit the Fund to consider future changes to its structure.

Most of the Fund's future income tax assets and liabilities are already recorded as substantially all operating assets are held by Pawnee and Lease-Win which are corporations and are tax paying entities. The Fund estimates that the unrecognized temporary differences, in the other subsidiaries, outstanding as of March 31, 2008 that will remain outstanding as of January 1, 2011 is approximately \$3 million resulting in a future tax asset of \$914,000, based on an effective tax rate of 30.5%. The Fund's estimate of its future income taxes will vary based on actual results of the factors described above, and such variations may be material.

### **RECENT ACCOUNTING PRONOUNCEMENTS**

On January 1, 2008, the Fund adopted the following new accounting standards that were issued by the Canadian Institute of Chartered Accountants: Section 1535, Capital Disclosures; Section 3031, Inventories; and Section 3862, Financial Instruments – Disclosures. There was no adjustment to the financial statements upon adoption of these new standards, but additional disclosure is presented in note 4.

### **Future changes in accounting policy**

On January 31, 2008, the CICA issued a new accounting standard: Handbook Section 3064 Goodwill and Intangible Assets. Section 3064 will replace Handbook Section 3062 Goodwill and Other Intangible Assets and Handbook Section 3450 Research and Development Costs. Section 3064 establishes standards for the recognition, measurement and disclosure of goodwill and intangible assets. This new standard will be effective for the Fund in the first quarter of 2009. The Fund is currently in the process of evaluating the potential impact of this new standard to the consolidated financial statements.

In 2006, Canada's Accounting Standards Board ratified a strategic plan that will result in Canadian GAAP, as used by public entities being converged with International Financial Reporting Standards over a transitional period currently expected to be until 2011. The impact this transition will have on the Fund's consolidated financial statements has not been determined; however management continues to monitor these regulatory developments.

### **CONTROLS & PROCEDURES**

Disclosure controls and procedures have been designed under the supervision of the Chief Executive Officer and Director of Finance, with the participation of management under their supervision, to provide reasonable assurance that all material information relating to the Fund, including its consolidated subsidiaries, is made known to such officers by others within those entities.

The Fund's Chief Executive Officer and Director of Finance are responsible for designing internal controls over financial reporting or causing them to be designed under their supervision to provide reasonable assurance regarding the reliability of the Fund's financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP.

The Fund's Chief Executive Officer and Director of Finance have evaluated the effectiveness of the Fund's disclosure controls and procedures as at March 31, 2008, and have concluded that such controls and procedures provide reasonable assurance that all material information relating to the Fund, including its consolidated subsidiaries, is made known to such officers in a timely fashion. Although the individuals comprising the members of the Fund's management and Pawnee's management responsible for financial reporting are considered to have appropriate proficiency and experience to effectively perform their duties, the nature and size of operations are such that the duties are performed by a small number of persons. As a result, further consideration must be made on a continuing basis as to whether additional persons are required.

There were no changes to the Fund's internal control over financial reporting during the quarter ended March 31, 2008 that have materially affected, or are reasonably likely to materially affect, the Fund's internal control over financial reporting.

Note, however that a control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues, including instances of fraud, if any, have been detected. These inherent limitations include, amongst other items: (i) that management's assumptions and judgments could ultimately prove to be incorrect under varying conditions and circumstances; and (ii) the impact of isolated errors.

Additionally, controls may be circumvented by the unauthorized acts of individuals, by collusion of two or more people, or by management override. The design of any system of controls is also based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential (future) conditions.

## **MARKET FOR SECURITIES**

The Fund Units are traded on the Toronto Stock Exchange under the symbol CHW.UN. The following table summarizes the high and low sales prices of the Fund Units and the average daily trading volume for each month in the period ended March 31, 2008, as reported by the Toronto Stock Exchange.

2008	High	Low	Average Daily Volume
January	\$3.64	\$2.01	6,283
February	\$2.90	\$2.40	3,819
March	\$2.87	\$2.19	6,461
	\$3.64	\$2.01	5,446

## **ADDITIONAL INFORMATION**

Additional information about the Fund is available:

- At the [www.chesswoodfund.com](http://www.chesswoodfund.com) website
- At the [www.sedar.com](http://www.sedar.com) website
- Via email to [investorrelations@Chesswoodfund.com](mailto:investorrelations@Chesswoodfund.com), or
- Via phone at 416-386-3099

**CHESWOOD INCOME FUND**  
**CONSOLIDATED BALANCE SHEETS**  
(in thousands of dollars)

	(unaudited) March 31, 2008	(audited) December 31, 2007
<b>ASSETS</b>		
Cash	\$ 4,455	\$ 2,352
Accounts receivable	2,444	3,250
Inventories	7,923	8,096
Prepaid expenses and other assets	1,300	1,396
Foreign currency forward exchange contracts	-	1,505
Net investment in leases	81,850	82,577
Future income tax asset	914	914
Property and equipment	2,509	2,534
	<u>101,395</u>	<u>102,624</u>
Intangible assets	9,613	9,421
Goodwill	27,851	26,698
<b>TOTAL ASSETS</b>	<u><u>\$ 138,859</u></u>	<u><u>\$ 138,743</u></u>
<b>LIABILITIES</b>		
Accounts payable and accrued liabilities	\$ 4,394	\$ 4,213
Distributions payable	401	403
Vehicle financing	7,160	6,794
Lease financing	44,157	44,987
Customer security deposits	9,977	9,898
Servicing liability	597	638
Interest rate swap contracts	1,376	735
Mortgage payable	896	910
Convertible debentures	3,500	3,500
Future income taxes	9,908	10,779
	<u>82,366</u>	<u>82,857</u>
Non-controlling interest	<u>8,298</u>	<u>8,027</u>
<b>UNITHOLDERS' EQUITY</b>		
Fund units	65,558	65,558
Contributed surplus	74	74
Accumulated other comprehensive loss	(3,685)	(5,443)
Deficit	<u>(13,752)</u>	<u>(12,330)</u>
	<u>48,195</u>	<u>47,859</u>
<b>TOTAL LIABILITIES AND UNITHOLDERS' EQUITY</b>	<u><u>\$ 138,859</u></u>	<u><u>\$ 138,743</u></u>

*Please see notes to consolidated financial statements.*

**CHESSWOOD INCOME FUND**  
**INTERIM CONSOLIDATED STATEMENTS OF INCOME (LOSS)**  
**FOR THE THREE-MONTHS ENDED MARCH 31, 2008 AND 2007**  
(in thousands of dollars, except per unit amounts)  
(unaudited)

	<b>FOR THE THREE MONTHS ENDED MARCH 31,</b>	
	<b>2008</b>	<b>2007</b>
<b>REVENUE</b>		
Revenue - automotive operations	\$ 15,855	\$ 12,402
Direct financing lease income	6,005	7,347
Ancillary lease and other income	1,047	1,333
	<u>22,907</u>	<u>21,082</u>
<b>COST OF SALES</b> - automotive operations	<u>13,565</u>	<u>10,625</u>
<b>GROSS PROFIT</b>	<b>9,342</b>	<b>10,457</b>
<b>EXPENSES</b>		
Salaries and commissions	1,837	1,959
Provision for credit losses	4,489	2,691
General and administrative	1,563	1,652
Interest on long-term debt	972	1,163
Other interest	64	85
Amortization	205	292
	<u>9,130</u>	<u>7,842</u>
<b>INCOME BEFORE ITEMS BELOW</b>	<b>212</b>	<b>2,615</b>
Unrealized loss on interest rate swaps	(597)	(292)
Unrealized gain (loss) on foreign exchange contracts	(270)	232
Net gain (loss) on foreign exchange	95	(139)
	<u>(772)</u>	<u>(199)</u>
<b>INCOME (LOSS) BEFORE INCOME TAXES</b>	<b>(560)</b>	<b>2,416</b>
(Recovery of) / Provision for income taxes	<u>(307)</u>	<u>558</u>
<b>INCOME (LOSS) BEFORE NON-CONTROLLING INTEREST</b>	<b>(253)</b>	<b>1,858</b>
Non-controlling interest	<u>(38)</u>	<u>278</u>
<b>NET INCOME (LOSS)</b>	<b>\$ (215)</b>	<b>\$ 1,580</b>
Basic and diluted earnings (loss) per unit	<b>\$ (0.03)</b>	<b>\$ 0.22</b>

*Please see notes to consolidated financial statements.*

**CHESSWOOD INCOME FUND**  
**INTERIM CONSOLIDATED STATEMENTS OF DEFICIT**  
**FOR THE THREE-MONTHS ENDED MARCH 31, 2008 AND 2007**  
(in thousands of dollars)  
(unaudited)

	FOR THE THREE MONTHS ENDED MARCH 31,	
	2008	2007
Deficit, balance at beginning of period	\$ (12,330)	\$ (806)
Net income (loss)	(215)	1,580
Distributions	(1,207)	(2,083)
Deficit, balance at end of period	<u>\$ (13,752)</u>	<u>\$ (1,309)</u>

**INTERIM CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)**  
**FOR THE THREE-MONTHS ENDED MARCH 31, 2008 AND 2007**  
(in thousands of dollars)  
(unaudited)

	FOR THE THREE MONTHS ENDED MARCH 31,	
	2008	2007
Net income (loss)	<u>\$ (215)</u>	<u>\$ 1,580</u>
Other comprehensive income (loss), net of tax		
Change in unrealized (losses) gains on translating financial statements of self-sustaining foreign operations	<u>1,758</u>	<u>(621)</u>
Total other comprehensive income (loss), net of tax	<u>1,758</u>	<u>(621)</u>
Comprehensive income for the period	<u>\$ 1,543</u>	<u>\$ 959</u>

**INTERIM CONSOLIDATED STATEMENTS OF ACCUMULATED  
OTHER COMPREHENSIVE INCOME (LOSS)**  
**FOR THE THREE-MONTHS ENDED MARCH 31, 2008 AND 2007**  
(in thousands of dollars)  
(unaudited)

	FOR THE THREE MONTHS ENDED MARCH 31,	
	2008	2007
Accumulated other comprehensive loss, beginning of period	\$ (5,443)	\$ -
Transitional adjustment on adoption of new accounting policies	-	2,790
Other comprehensive income (loss) for the period	<u>1,758</u>	<u>(621)</u>
Accumulated other comprehensive income (loss), end of period	<u>\$ (3,685)</u>	<u>\$ 2,169</u>



**CHESSWOOD INCOME FUND**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**FOR THE THREE-MONTHS ENDED MARCH 31, 2008 AND 2007**  
(in thousands of dollars)  
(unaudited)

	FOR THE THREE MONTHS ENDED	
	MARCH 31,	
	2008	2007
<b>CASH PROVIDED BY (USED IN)</b>		
<b>OPERATING ACTIVITIES</b>		
Net income (loss) for the period	\$ (215)	\$ 1,580
Add (deduct) items not involving cash:		
Non-controlling share of net income	(38)	278
Amortization	205	292
Accretion expense on lease financing	59	69
Gain on sale of leased vehicles	(78)	(132)
Unrealized (gain) loss on interest rate swap contracts	597	292
Unrealized gain on sale of lease receivables, net of provision for prepayment and provision for credit losses	(102)	(115)
Impairments of retained interest in securitizations	(302)	(119)
Amortization of securitization servicing liability	(69)	(69)
Provision for credit losses	5,132	3,325
Provision for income taxes	(1,078)	(1,132)
Unrealized (gain) loss on foreign exchange contracts	270	(232)
Net (gain) loss on foreign exchange	(95)	139
	<u>4,286</u>	<u>4,176</u>
Changes in non-cash working capital items relating to operations		
Accounts receivable	806	(938)
Inventories	172	(3,500)
Prepaid and other assets	144	439
Accounts payable and accrued liabilities	163	800
	<u>1,285</u>	<u>(3,199)</u>
<b>Cash provided by operating activities</b>	<u>5,571</u>	<u>977</u>
<b>INVESTING ACTIVITIES</b>		
Purchases of property and equipment	(10)	(28)
Cash received from residual interest in securitization	549	650
Increase in net investment in leases	(3,779)	(6,056)
Decrease in security deposits	(304)	(2)
<b>Cash used in investing activities</b>	<u>(3,544)</u>	<u>(5,436)</u>
<b>FINANCING ACTIVITIES</b>		
Proceeds from securitization of leases	2,201	3,754
Vehicle financing	366	3,705
Proceeds from lease financing	116	28
Lease financing payments	(2,672)	(1,996)
Servicing liability	28	46
Mortgage principal payments	(14)	(13)
Obligations under capital leases	(2)	(6)
Proceeds from sale of foreign exchange forward contracts	1,235	-
Cash distributions paid to non-controlling interest	-	(367)
Cash distributions paid	(1,208)	(2,082)
<b>Cash provided by financing activities</b>	<u>50</u>	<u>3,069</u>
Unrealized foreign exchange (loss) gain on cash	26	(14)
Net increase (decrease) in cash	2,103	(1,404)
Cash, beginning of period	2,352	4,902
<b>Cash, end of period</b>	<u>\$ 4,455</u>	<u>\$ 3,498</u>

*Please see notes to consolidated financial statements.*



Notes to Consolidated Financial Statements  
For the three-months ended March 31, 2008 and 2007

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These consolidated financial statements of Chesswood Income Fund (the "Fund") have been prepared by management in accordance with Canadian generally accepted accounting principles. The disclosures contained in the unaudited interim consolidated financial statements do not include all requirements of generally accepted accounting principles for annual financial statements. The unaudited interim consolidated financial statements should be read in conjunction with the annual consolidated financial statements for the period ended December 31, 2007. The unaudited interim consolidated financial statements are based upon accounting principles consistent with those used and described in the annual consolidated financial statements, except those listed in note 1.

Accounting measurements at interim dates inherently involve greater reliance on estimates than at year-end and the results of operations for the interim periods shown in this report are not necessarily indicative of results to be expected for the fiscal year. In the opinion of management, the accompanying unaudited interim consolidated financial statements reflect all adjustments (of a normal recurring nature) which are necessary to present fairly the financial position of the Fund as of March 31, 2008 and the results of operations and cash flows for the three-months ended March 31, 2008.

All financial information is presented in Canadian dollars, unless otherwise noted.

## **1. Change in Accounting Policies**

On January 1, 2008, the Fund adopted CICA Handbook Section 1535, Capital Disclosures. This standard requires the disclosure of information related to the objectives, policies and processes for managing capital.

On January 1, 2008, the Fund adopted CICA Handbook Section 3031, Inventories. Under this new section, inventories are required to be measured at the lower of cost and net realizable value. The standard provides guidance on the determination of cost, including allocation of overheads and other costs to inventory. The standard also requires the consistent use of either the first-in, first-out (FIFO) or other weighted average cost method to measure automobile parts. The standard requires the reversal of previously recorded write downs to realizable value when there is clear evidence that net realizable value has increased.

On January 1, 2008, the Fund adopted CICA Handbook Section 3862, Financial Instruments – Disclosures. This new section requires disclosure of information related to the significance of financial instruments to the Fund's performance. The Fund is also required to disclose information related to the risks of its use of financial instruments and how those risks are managed.

There was no adjustment to the financial statements upon adoption of these new standards, but additional disclosure is presented in note 4.

### **Future accounting changes**

On January 31, 2008, the CICA issued a new accounting standard: Handbook Section 3064 Goodwill and Intangible Assets. Section 3064 will replace Handbook Section 3062 Goodwill and Other Intangible Assets and Handbook Section 3450 Research and Development Costs. Section 3064 establishes standards for the recognition, measurement and disclosure of goodwill and intangible assets. This new standard will be effective for the Fund in the first quarter of 2009. The Fund is currently in the process of evaluating the potential impact of this new standard to the consolidated financial statements.

In 2006, Canada's Accounting Standards Board ratified a strategic plan that will result in Canadian GAAP, as used by public entities being converged with International Financial Reporting Standards over a transitional period currently expected to be until 2011. The impact this transition will have on the Fund's consolidated financial statements has not been determined; however management continues to monitor these regulatory developments.



Notes to Consolidated Financial Statements  
For the three-months ended March 31, 2008 and 2007

**2. Net investment in leases**

The Fund's net investment in direct finance leases includes the following:

	<b>March 31, 2008</b>	<b>December 31, 2007</b>
	(\$ thousands)	
Total minimum lease payments for non-securitized leases	<b>\$110,794</b>	\$110,292
Estimated residual values of leased equipment	<b>10,691</b>	10,177
Initial direct costs of lease acquisition	<b>5,374</b>	5,371
	<b>126,859</b>	125,840
Unearned income	<b>(38,093)</b>	(38,062)
	<b>88,766</b>	87,778
Allowance for doubtful accounts	<b>(9,657)</b>	(7,850)
	<b>79,109</b>	79,928
Securitized lease receivable	<b>2,741</b>	2,649
<b>Net investment in leases</b>	<b>81,850</b>	82,577
Less: Current portion	<b>(23,002)</b>	(24,041)
Net investment in leases - long-term portion	<b>\$58,848</b>	\$58,536

	<b>For the three months ended</b>	
	<b>March 31, 2008</b>	<b>March 31, 2007</b>
	(\$ thousands)	
The activity in the allowance for doubtful accounts is as follows:		
Opening balance	<b>\$7,850</b>	\$6,753
Provision for credit losses	<b>4,489</b>	2,691
Impact of change in foreign exchange rates over period	<b>419</b>	(111)
Direct write-downs, net of recoveries	<b>(3,101)</b>	(1,992)
Ending balance	<b>\$9,657</b>	\$7,341

**Securitization lease receivable** - Lease-Win sells financing leases through securitization transactions. In all of those securitizations, Lease-Win retained servicing responsibilities and subordinated interests. Lease-Win retains the right to a portion of the future cash flows arising after investors in the securitization trust have received the return for which they have contracted. The investors and the securitization trust have no recourse to Lease-Win's other assets for failure of debtors to pay when due. Lease-Win's retained interests are subordinate to the investors' interests. Their value is subject to credit, prepayment, and interest rate risks on the transferred receivables.

	<b>March 31, 2008</b>	<b>December 31, 2007</b>
	(\$ thousands)	
Assets under administration from the securitization of leases	<b>\$37,630</b>	\$40,120



Notes to Consolidated Financial Statements  
For the three-months ended March 31, 2008 and 2007

### 3. Minimum payments

The aggregate amount of minimum payments required on debt is as follows:

(\$ thousands)	2008	2009	2010	2011	2012 and beyond	Total
Lease-Win's lease financing (*)	\$2,131	\$ -	\$ -	\$ -	\$ -	\$2,131
Pawnee's lease financing credit facility	-	-	42,026	-	-	42,026
Mortgage payable	43	61	65	70	657	896
Convertible debentures	3,500	-	-	-	-	3,500
Total	\$5,674	\$61	\$42,091	\$70	\$657	\$48,553

(\*) \$2.1 million of the lease financing would only be payable in 2008 if the bank called the loan, which is not anticipated, otherwise the loan is payable over the term of the underlying leases.

### 4. Financial Risk and Capital Management

The carrying amounts of cash, accounts receivable, accounts payable and accrued liabilities and distributions payable approximate their fair market value due to the short-term maturity of these instruments.

The stated value of the vehicle financing, lease financing and long-term debt approximates fair values, as the interest rates attached to these instruments are representative of current market rates, for loans with similar terms, conditions and maturities.

As at March 31, 2008, the estimated fair value of other financial assets and liabilities approximates their carrying values.

#### a) Credit risk

Accounts receivable principally relates to the Acura Sherway dealership and includes amounts due from the manufacturer and financing contracts in transit, which are typically collected within seven to ten days. Credit risk is limited to the concentration of the receivable with the automotive manufacturer.

Pawnee's lease receivables predominantly serve smaller, often owner-operated businesses that have limited access to traditional financing. There is a high degree of risk associated with leasing to such parties. The typical lessee in Pawnee's portfolio is a start-up business that has not established business credit or a more established business that has experienced some business credit difficulty at sometime in its history. As a result, such leases entail a relatively higher credit risk and may be expected to experience higher levels of delinquencies and loss levels. The credit risk is mitigated by Pawnee funding only "business essential" commercial equipment, the value of the equipment is less than \$30,000, at least one personal guarantee is obtained for each lease, and having diversification by geographic location (within the United States), by types of equipment funded and significant diversification in terms of the industries in which Pawnee's lessees operate with no concentration with any one customer.

Lease-Win is exposed to credit risk due to delinquencies. The credit risk associated with Lease-Win's leases receivables is mitigated by liens placed against the vehicles, personal guarantees, and ability to repossess vehicles for non-payment.

Credit risk also exists at Lease-Win as a result of using only one financial company to securitize its lease receivable and that company's ability to source funding for its financing especially at fixed rates. This risk is mitigated with having a long-standing relationship with our bank where we could obtain financing if the need arises.



Notes to Consolidated Financial Statements  
For the three-months ended March 31, 2008 and 2007

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*b) Interest rate risk*

The Fund's cash is used to finance working capital, which is short-term in nature, and is at floating interest rates. The vehicle financing used to finance the inventory, which is short-term in nature, is also at floating interest rates thus exposing the Fund to interest rate fluctuations.

Pawnee and Lease-Win's leases are written at fixed interest rates and terms. Pawnee and Lease-Win generally finance their activities using both fixed rate and floating rate funds. To the extent Pawnee and Lease-Win finance fixed rate leases with floating rate funds, they are exposed to fluctuations in interest rates such that an increase in interest rates could narrow or eliminate the margin between the yield on a lease and the effective interest rate paid by the lessor to finance the lease.

Pawnee's credit facility requires Pawnee to mitigate its interest rate risk by entering interest rate swaps for a notional amount not less than 50% of the aggregate commitment. The interest rate swap agreements provide for payment of an annual fixed rate. In return, Pawnee receives payment of a LIBOR based floating rate amount. The interest rate swaps are intended to offset a portion of the variable interest rate risk on the credit facility.

Lease-Win finances its activities using both fixed rate and floating rate funds. To the extent Lease-Win finances fixed rate leases with fixed rate funds, it is not exposed to fluctuations in interest rates. All of Lease-Win's \$2.2 million lease financing is at the floating rate. Lease-Win has the right to fix the rate on all its floating rate debt at the bank's prime rate plus 0.75%. The leases financed through securitization can be financed at fixed or floating rate. As at March 31, 2008, approximately \$9.4 million of Lease-Win's \$43.7 million securitized gross lease receivables were funded on a floating rate basis. Lease-Win has the right to convert all or any part of the floating rate pool to a fixed rate basis at any time.

*c) Foreign exchange risk*

The Fund is exposed to fluctuations in the U.S. dollar as some cash flows are generated in the U.S. and distributions are paid in Canadian dollars.

**Capital Management**

The Fund's capital is comprised of unitholders' equity, non-controlling interest, and subordinated debentures. The Fund's objective when managing capital is to safeguard the Fund's ability to continue as a going concern in order to provide returns for unitholders and to maintain financial strength.

The Fund's capital is not subject to any capital requirements imposed by a regulator. However, each of the Fund's operating subsidiaries is subject to bank and/or manufacturer covenants relative to leverage and/or working capital. Pawnee is restricted in its ability to further merge, acquire companies or be acquired, or incur additional debt without lender approval. Furthermore, dividends from Pawnee are limited to compliance with all bank covenants and may not exceed 95% of Pawnee's consolidated net income, as determined in accordance with U.S. GAAP, excluding mark-to-market adjustments for interest rate swaps. These bank covenants safeguard the capital in each of its operating subsidiaries.

The Fund's Declaration of Trust requires it to distribute to its unitholders in each year an amount not less than the Trust's income for the year, as calculated in accordance with the Income Tax Act (Canada) (the "Act") after all permitted deductions under the Act have been taken. Unitholder distributions are subject to review and approval by the trustees of the Fund.

The Fund anticipates extending the maturity date of the convertible debentures from August 10, 2008 until August 10, 2009 or beyond.



Notes to Consolidated Financial Statements  
For the three-months ended March 31, 2008 and 2007

**5. Cash flow supplementary disclosure**

For the three-months ended March 31,		
	2008	2007
	(\$ thousands)	
Interest paid	<b>\$936</b>	\$1,211
Income tax installments paid	<b>115</b>	41

**6. Related Party Transactions**

1) Debentures in the principal amount of \$2.2 million (out of the aggregate \$3.5 million principal amount of the Fund Issued Debentures) were issued to directors of Chesswood GP Limited, which is a wholly-owned subsidiary of the Fund.

2) Pawnee leases a 10,800 square foot office facility. The lessor is a related party due to common ownership between itself and the holders of the Class B and C shares of U.S. Acquisitionco. The minimum lease payments are U.S. \$189,000 per year triple net and run through 2011 with options for two additional five-year terms. These transactions were recorded at the average exchange rate.

**7. Economic dependence**

Sherway LP operates under a Dealer Sales and Service Agreement whereby it has the right to act as an authorized dealer for Acura vehicles. The manufacturer may cancel the agreement if the dealership does not observe certain established guidelines.

As the sole source of income of Sherway LP is derived from the sales of the manufacturer's automobiles and related products and services, its ability to continue viable operations is dependent on maintaining its right to act as an authorized dealer. Accordingly, the absence of the dealership would have a material adverse effect on the Fund.

**8. Seasonal Operations and Significant Estimates**

The Fund's automotive business follows a seasonal pattern, with revenue and net earnings based on past experience of the predecessor companies being significantly lower in the first quarter than in other quarterly periods.

The accounting for the securitization of leases requires the use of significant judgment and estimations in order to measure, at a specific point in time, matters that are inherently uncertain. Due to the fact that future events rarely develop as forecasted and the estimates routinely require adjustments, and may require material adjustment.

**9. Comparative Figures**

Certain of the comparative figures have been reclassified to conform to the presentation adopted in the quarterly financial statements.

**10. Segmented Information:**

The Fund's operations consist of two reporting segments, equipment leasing and automotive operations. The two reporting segments are also in separate geographic locations. The automotive operations are located in Canada and the equipment leasing is located in the United States. Segmented information is as follows:





Notes to Consolidated Financial Statements  
For the three-months ended March 31, 2008 and 2007

For the three-months ended March 31, 2008			
(\$ thousands)			
	Canada	U.S.	Total
Revenue	\$15,993	\$6,914	\$22,907
Gross profit	2,428	6,914	9,342
Interest expense	202	834	1,036
Amortization	62	143	205
Corporate overhead	388	-	388
<b>Income(loss) before other items</b>	<b>234</b>	<b>(22)</b>	<b>212</b>
Unrealized loss on interest rate swaps	-	(597)	(597)
Loss on foreign exchange	(175)	-	(175)
<b>Net loss before income taxes</b>	<b>59</b>	<b>(619)</b>	<b>(560)</b>
Provision for (recovery of) income taxes	53	(360)	(307)
Loss before non-controlling interest	6	(259)	(253)
<b>Net loss</b>	<b>5</b>	<b>(220)</b>	<b>(215)</b>
Total Assets	30,876	107,983	138,859
Net investment in leases	8,702	73,148	81,850
Goodwill	3,300	24,551	27,851
Intangible assets	1,300	8,313	9,613
Property and equipment expenditures	3	7	10

For the three-months ended March 31, 2007			
(\$ thousands)			
	Canada	U.S.	Total
Revenue	\$12,402	\$8,680	\$21,082
Gross profit	1,777	8,680	10,457
Interest expense	216	1,032	1,248
Amortization	122	170	292
Corporate overhead	393	-	393
<b>Income (loss) before other items</b>	<b>(408)</b>	<b>3,023</b>	<b>2,615</b>
Unrealized loss on interest rate swaps	-	(292)	(292)
Gain on foreign exchange	93	-	93
<b>Net income (loss) before income taxes</b>	<b>(315)</b>	<b>2,731</b>	<b>2,416</b>
Provision for (recovery of) income taxes	(3)	561	558
Income (loss) before non-controlling interest	(312)	2,170	1,858
<b>Net income (loss)</b>	<b>(266)</b>	<b>1,846</b>	<b>1,580</b>
Total Assets	35,585	144,120	179,705
Net investment in leases	6,910	90,441	97,351
Goodwill	6,740	41,817	48,557
Intangible assets	2,185	9,933	12,118
Property and equipment expenditures	24	6	30

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**Directors, Trustees and Officers**

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**Trustees, Directors and Officers**

**Edward Sonshine, Q.C.\***

Trustee (1)  
Chairman of the Fund  
*President & C.E.O.,  
RioCan Real Estate Investment Trust  
\*Queen's Counsel*

**Clare Copeland**

Trustee (1)  
Chairman, Compensation Committee  
*C.E.O., Falls Management Company  
Chairman, Toronto Hydro Corporation*

**Frederick W. Steiner**

Trustee (1)  
Chairman, Audit and Governance Committee  
*President & C.E.O.,  
Imperial Coffee and Services Inc.*

**Jeffrey Wortsman**

Trustee (1)  
*President & C.E.O.,  
Danier Leather Inc.*

**Barry Shafran**

Director (2)  
*President & C.E.O.,  
Chesswood GP Limited*

**David Obront**

Director (2)  
*President,  
DOit Investments Ltd.*

**Robert Day**

Director (2)  
*Chairman,  
Pawnee Leasing Corporation*

**Samuel Leeper**

Director (2)  
*C.E.O.,  
Pawnee Leasing Corporation*

**Fund Executive Team**

**Barry Shafran**

*President & C.E.O.*

**Lisa Stevenson**

*Director of Finance*

**Other Information**

**Auditors**

*BDO Dunwoody LLP*

**Transfer Agent**

*Equity Investment Services Inc.*

**Corporate Counsel**

*McCarthy Tétrault LLP*

**Website**

*www.chesswoodfund.com*

**Toronto Stock Exchange Symbol**

*CHW.UN*

(1) – Each of the Trustees is also a director of Chesswood GP Limited, (please refer to note (2) below).

(2) - Director of Chesswood GP Limited, which is a 100% owned subsidiary of the Fund.



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