



*Financial Statements of*

# **BOND TRUST**

*Audited*

*For the year ended June 30, 2008*

26,934,730 BOND UN \$75,900,000

## TABLE OF CONTENTS

---

<b>1</b>	<b>Auditors' Report</b>
<b>2</b>	<b>Statements of Net Assets</b>
<b>3</b>	<b>Statements of Operations</b>
<b>4</b>	<b>Statements of Changes in Net Assets</b>
<b>5</b>	<b>Statement of Investments</b>
<b>6 - 10</b>	<b>Notes to the Financial Statements</b>



Deloitte & Touche LLP  
Brookfield Place  
181 Brookfield Street  
Suite 1400  
Toronto ON M5J 2V1  
Canada

Tel: 416-601-6150  
Fax: 416-601-6151  
www.deloitte.ca

## Auditors' Report

To the Unitholder of  
Bond Trust

We have audited the statements of net assets of Bond Trust (the "Fund") as at June 30, 2008 and 2007, the statement of investments at June 30, 2008 and the statements of operations and of changes in net assets for the years then ended. These financial statements are the responsibility of the Fund manager. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the net assets of the Fund as at June 30, 2008 and 2007, and the results of its operations and changes in net assets for the years then ended in accordance with Canadian generally accepted accounting principles.

*"Deloitte & Touche LLP"*

Chartered Accountants  
Licensed Public Accountants

August 1, 2008

## Financial Statements

### STATEMENTS OF NET ASSETS

As at June 30,	2008	2007
<b>ASSETS</b>		
Cash and short-term investments	\$ 201,978	\$ 234,003
Interest receivable	248,442	285,777
Investments at fair value (Cost 2008 - \$64,781,831; 2007 - \$64,308,302)	59,204,376	68,019,120
	<b>59,654,796</b>	<b>68,538,900</b>
<b>LIABILITIES AND UNITHOLDER'S EQUITY</b>		
Due to manager (Note 4)	50,941	122,484
Interest payable	248,442	285,777
	<b>299,383</b>	<b>408,261</b>
<b>NET ASSETS AND UNITHOLDER'S EQUITY</b>		
<b>(Notes 5 and 8)</b>	<b>\$ 59,355,413</b>	<b>\$ 68,130,639</b>
<b>NUMBER OF UNITS OUTSTANDING (Note 5)</b>	<b>7,200,000</b>	<b>7,200,000</b>
<b>NET ASSET VALUE PER UNIT (Note 8)</b>	<b>\$ 8.24</b>	<b>\$ 9.46</b>

APPROVED BY THE TRUSTEE,

(signed) Wayne L. Pushka  
Director

(signed) Thomas I. A. Allen  
Director

The accompanying notes are integral to these financial statements.

## Financial Statements

continued

## STATEMENTS OF OPERATIONS

For the year ended June 30,	2008	2007
<b>INCOME</b>		
Interest	\$ 4,150,991	\$ 4,356,090
Accretion on strip bonds	2,338,812	2,209,851
	<b>6,489,803</b>	<b>6,565,941</b>
<b>EXPENSES</b>		
Management fees (Note 4)	118,688	119,247
Accounting and audit and legal fees	38,095	69,326
Custody, valuation and transfer fees	17,783	15,821
Administrative expenses	50,007	40,027
Regulatory and listing expenses	1,535	2,973
	<b>226,108</b>	<b>247,394</b>
<b>NET INVESTMENT INCOME</b>	<b>6,263,695</b>	<b>6,318,547</b>
<b>PARTIAL SETTLEMENT OF SWAP CONTRACT (Note 6b)</b>	<b>(1,865,283)</b>	<b>(4,941,720)</b>
<b>CHANGES IN UNREALIZED APPRECIATION (DEPRECIATION) OF INVESTMENTS</b>	<b>(9,288,273)</b>	<b>4,237,389</b>
<b>INCREASE (DECREASE) IN NET ASSETS FROM OPERATIONS</b>	<b>\$ (4,889,861)</b>	<b>\$ 5,614,216</b>
<b>INCREASE (DECREASE) IN NET ASSETS FROM OPERATIONS PER UNIT <sup>(1)</sup></b>	<b>\$ (0.68)</b>	<b>\$ 0.78</b>

<sup>(1)</sup> Based on the weighted average number of Units outstanding during the period

The accompanying notes are integral to these financial statements.

## Financial Statements

continued

## STATEMENTS OF CHANGES IN NET ASSETS

For the year ended June 30,	2008	2007
NET ASSETS, BEGINNING OF YEAR	\$ 68,130,639	\$ 66,638,423
INCREASE (DECREASE) IN NET ASSETS FROM OPERATIONS	(4,889,861)	5,614,216
PAYMENT BY THE COUNTERPARTY TO REDUCE NOTIONAL VALUE OF SWAP CONTRACT (Note 6)	6,162,635	-
DISTRIBUTIONS TO UNITHOLDER (Note 7)	(10,048,000)	(4,122,000)
NET ASSETS, END OF YEAR	\$ 59,355,413	\$ 68,130,639

The accompanying notes are integral to these financial statements.

## Financial Statements

continued

## STATEMENT OF INVESTMENTS

As at June 30, 2008

BOND PAR VALUE	DESCRIPTION	COUPON	MATURITY	AVERAGE COST	FAIR VALUE	% OF NET ASSETS
<b>Capital Repayment Portfolio (Par Value in CAN \$ except as noted)</b>						
\$ 16,000,000	Ontario Hydro	0.000%	15/04/2012	\$ 12,883,626	\$ 13,767,325	23.2
2,494,000	Ontario Hydro	0.000%	06/02/2013	1,994,255	2,070,679	3.5
4,200,000	Ontario Hydro	0.000%	18/02/2013	3,230,885	3,481,571	5.9
1,500,000	Province of British Columbia	0.000%	18/06/2012	1,192,268	1,282,064	2.2
4,500,000	Province of British Columbia	0.000%	23/08/2012	3,542,525	3,816,942	6.4
4,000,000	Province of Ontario	0.000%	02/12/2012	3,109,373	3,350,399	5.6
13,900,000	Province of Ontario	0.000%	13/01/2013	10,724,400	11,583,255	19.5
7,200,000	Province of Quebec	0.000%	01/04/2012	5,816,874	6,201,042	10.4
1,600,000	US \$ Credit Suisse First Boston	6.500%	15/01/2012	2,517,384	1,684,567	2.8
800,000	US \$ Goldman Sachs Group	5.700%	01/09/2012	1,211,072	814,186	1.4
1,600,000	US \$ Morgan Stanley Dean Witter	6.600%	01/04/2012	2,549,853	1,650,421	2.8
12,584,000	UBS Default Contingency Zero Swap (Note 6a)	0.000%	31/12/2012	4,021,385	8,535,279	14.4
				<b>52,793,900</b>	<b>58,237,730</b>	<b>98.1</b>
<b>Distribution Portfolio (Par Value in U.S. \$)</b>						
738,000	Anthem Inc. (Wellpoint Inc.)	6.800%	01/08/2012	1,250,420	775,007	1.3
165,000	AOL Time Warner Inc.	6.875%	01/05/2012	258,741	171,259	0.3
729,000	AON Corp.	7.375%	14/12/2012	1,240,147	761,553	1.3
217,000	Arvinmeritor Inc.	8.750%	01/03/2012	396,057	193,739	0.3
154,000	CIT Group Inc.	7.750%	02/04/2012	255,724	132,512	0.2
512,000	Coca Cola Enterprises Inc.	6.125%	15/08/2011	858,202	538,067	0.9
164,000	Disney (Walt) Co.	6.375%	01/03/2012	264,449	174,772	0.3
802,000	Electronic Data Systems	7.125%	15/10/2009	1,223,645	839,109	1.4
247,000	Falconbridge Ltd.	7.350%	05/06/2012	388,623	260,069	0.4
618,000	Ford Motor Credit Co.	7.375%	01/02/2011	853,451	508,814	0.9
256,000	General Electric Capital Corp.	4.625%	15/09/2009	396,168	261,811	0.4
749,000	Safeco Corp.	7.250%	01/09/2012	1,255,401	789,700	1.3
931,000	Sprint Capital Corp.	8.375%	15/03/2012	1,259,266	935,101	1.6
722,000	Sun Microsystems Inc.	7.650%	15/08/2009	1,251,207	753,088	1.3
633,000	Teco Energy Inc.	7.200%	01/05/2011	836,430	658,978	1.1
				<b>11,987,931</b>	<b>7,753,579</b>	<b>13.0</b>
	<b>Swap Contract (Note 6b)</b>				<b>(6,786,933)</b>	<b>(11.4)</b>
				<b>11,987,931</b>	<b>966,646</b>	<b>1.6</b>
<b>TOTAL INVESTMENTS</b>				<b>\$ 64,781,831</b>	<b>59,204,376</b>	<b>99.7</b>
<b>OTHER ASSETS LESS LIABILITIES</b>					<b>151,037</b>	<b>0.3</b>
<b>TOTAL NET ASSETS</b>					<b>\$ 59,355,413</b>	<b>100.0</b>

The effective interest rates of the bonds range from 4.55% to 8.75%.

The accompanying notes are integral to these financial statements.

## Notes to the Financial Statements

**June 30, 2008**

### **1. THE BOND TRUST**

The Bond Trust (the “Fund”) is a special purpose investment trust established under the laws of the Province of Ontario on January 28, 2003 (date of inception). The outstanding units are owned by UBS AG (Canada Branch) (the “Unitholder”). Crown Hill Investment Corporation was the manager (the “Manager”) of the Fund until June 6, 2008, at which time it was replaced by Crown Hill Capital Corporation.

Reference is made to the Fund’s prospectus dated January 29, 2003 for a complete description of the objectives, investment guidelines and purpose of the Fund.

### **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

These financial statements, prepared in accordance with Canadian generally accepted accounting principles (“GAAP”), include estimates and assumptions by management that affect the reported amounts of assets, liabilities, income and expenses during the reporting period. Actual amounts could differ from those estimates. The following is a summary of significant accounting policies followed by the Fund in the preparation of its financial statements.

*a) Adoption of CICA Handbook Section 3855*

The Fund adopted Canadian Institute of Chartered Accountants (“CICA”) Handbook Section 3855, effective July 1, 2007, on a retroactive basis, without restatement of the financial statements of prior years. Section 2855 requires that the fair value of financial instruments which are traded in active markets be measured based on the bid price for long securities and the ask price for securities held short. Previously, the fair value was based on the last traded price for the day, when available. The effect of the initial adoption of this new accounting policy, using the closing bid price as at June 30, 2007, did not result in a change in the Net Assets of the Fund at the beginning of the year. See Note 8.

Section 3855 also requires that transaction costs, such as brokerage commissions, incurred in the purchase and sale of securities be charged to net income in the period. Previously, these costs if any, would have been added to the cost of the securities purchased or deducted from the proceeds of sale. This change had no impact on the Fund since the Fund does not pay transaction costs.

*b) Investment Valuation*

Debt securities are valued at their bid price provided by independent security pricing services. Investments for which market quotations are not readily available are valued at the Manager’s best estimate of fair value. The difference between fair value and average cost, as recorded in the accounts, is shown as an unrealized gain (loss) on investments. Average cost is used to determine the gain or loss on portfolio securities sold. Short-term investments are valued at cost plus accrued interest which approximates fair value.

Strip bonds are valued at their bid price on the valuation date. The discount on the strip bond is recorded as interest income over the life of the bond using the effective interest rate method and added to the cost of the strip bond. The difference between the fair value and the accreted cost of the strip bond is recorded as part of the unrealized gain (loss) on investments on the Statements of Operations.

**June 30, 2008****2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)***c) Foreign Currency Translation*

Investments at market value and other assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the rate of exchange applicable on the valuation date. Investment transactions and income and expenses are translated at the rate of exchange on the date of such transactions.

*d) Derivative Contracts*

Derivative contracts are valued by UBS AG (London Branch) at the gain or loss that would arise as a result of closing out the contract on the valuation date.

*e) Interest Income*

Interest income is accounted for on the accrual basis using the effective interest method and includes amounts earned under the derivative contracts.

*f) Net Asset Value per Unit*

The Net Asset Value per Unit of the Fund is computed by dividing the Net Assets of the Fund on the valuation date by the number of Units outstanding on the valuation date.

*g) Future Accounting Changes*

The CICA has issued the following accounting standards that apply to interim and annual financial statements relating to fiscal years beginning on or after October 1, 2007:

- i. Section 1535, "Capital Disclosure"
- ii. Section 3862, "Financial Instruments – Disclosure"
- iii. Section 3863, "Financial Instruments – Presentation"

Section 1535 established standards for disclosing information about an entity's capital and how it is used. Sections 3862 and 2863 place increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how an entity manages those risks. The Fund adopted these sections effective July 1, 2008.

**3. TAXATION**

The Fund qualifies as a unit trust and a financial institution within the meaning of the Income Tax Act (Canada). The Fund is subject to applicable federal and provincial taxes on the amount of its net income for tax purposes for the year, to the extent such net income for tax purposes has not been paid or made payable to the Unitholder in the year. No provision for income taxes has been recorded in the accompanying financial statements as all income is distributed or distributable to the Unitholder.

**June 30, 2008****4. RELATED PARTY TRANSACTIONS***a) Manager*

The Fund has entered into a trust agreement (the "Declaration of Trust") dated January 28, 2003. Under the terms of the Declaration of Trust, the Manager provides all administrative services required by the Fund and receives a fee of approximately \$9,375 per month plus applicable taxes. All other expenses of the Fund are initially paid by the Manager and the Manager is reimbursed by the Fund. The amount owing to the Manager at June 30, 2008 is \$50,941 (2007 - \$122,484).

*b) Trustee*

Under the terms of the Declaration of Trust, Hollister Capital Corporation, now called Crown Hill Investment Corporation, was appointed Trustee of the Fund. Crown Hill Investment Corporation was replaced by Crown Hill Capital Corporation on June 6, 2008. All assets are currently held in custody by UBS AG.

*c) Unitholder*

Interest income includes \$4,190,090 (2007 - \$4,356,000) from UBS AG under the terms of the Swap Contract described in Note 6(b).

**5. UNITHOLDER'S EQUITY**

The Fund is authorized to issue an unlimited number of transferable, redeemable trust units of one class, each of which represents an equal, undivided interest in the net assets of the Fund. The Unitholder is entitled to redeem its units outstanding in December of each year. Units will be redeemed at the net asset value per unit on the redemption date. On February 28, 2003, the Fund issued 7,200,000 units for cash proceeds of \$68,199,998.

**6. DERIVATIVE CONTRACTS**

- (a) The Fund has entered into the UBS Default Contingency Zero Swap derivative contract with UBS AG. This swap has a notional and stated maturity value of \$12,584,000, adjusted for credit events in certain debt securities, and has the economic effect of creating a synthetic strip bond with exposures to Credit Suisse First Boston, Goldman Sachs Group and Morgan Stanley Dean Witter, held in the investment portfolio.
- (b) The Fund has also entered into a derivative contract (the "Swap Contract") with UBS AG (the "Counterparty"). The Swap Contract has a notional amount and a termination value of \$72,000,000, adjusted for credit events in certain debt securities (the "final settlement amount"). At the termination or expiry date, the Swap Contract requires delivery of all securities in the capital repayment portfolio to the Counterparty in exchange for the final settlement amount. The Swap Contract also has three additional purposes: a) to provide a currency hedge; b) to smooth the uneven cash flows arising from bond maturities and receipt of interest; and c) to enhance yield by gaining exposure to other credits. The other credits are those listed in the distribution portfolio with the exception of Coca-Cola Enterprises Inc., and includes Bombardier Inc., Comcast Corp., Capital One Financial Corp., Dow Chemical Co., Supervalu Inc., Hilton Hotels Corp., Motorola Inc., Noranda Inc., Phelps Dodge Corp., Park Place Entertainment Corp., Sears Roebuck Acceptance Corp., Toys R Us Inc., Tyco International Ltd., Tyson Foods Inc., Visteon Corp., Valero Energy Corp. and Weyerhaeuser Co. ("additional credits").

## Notes to the Financial Statements

continued

## June 30, 2008

**6. DERIVATIVE CONTRACTS (continued)**

Further, through the Swap Contract, the Fund's risk profile is modified such that it has an initial exposure of 3.6% to each of the credits in the distribution portfolio as well as the additional credits. This percentage will decrease over time as coupons from the distribution portfolio are paid. As of June 30, 2008 this exposure has been reduced to 1.8% of the notional amount. The contract matures on December 31, 2012.

On January 7, 2008, the Counterparty paid \$6,162,635 as partial settlement of the Swap Contract so as to reduce the notional value of the Swap Contract by 9.5% from \$72,000,000 to \$65,160,000.

**Partial Settlement of Swap Contract**

Year ended June 30,		2008		2007
Cost of investments beginning of year	\$	64,308,302	\$	67,040,171
Cost of investments end of year		64,781,831		64,308,302
Decrease (increase) in cost of investments		(473,529)		2,731,869
Add: Increase in bond cost due to accretion for the year		2,338,812		2,209,851
Cost of investments disposed of under partial settlement of swap contract	\$	1,865,283	\$	4,941,720

**7. DISTRIBUTIONS**

The Fund was designed to provide the unitholder with a stable stream of semi-annual distributions starting June 30, 2003. It has done so since inception.

During the year ended June 30, 2008, the Fund made distributions to the Unitholder of \$2,196,000 on December 31, 2007 (2006 - \$2,178,800 on December 31, 2006) and \$2,200,000 on June 30, 2008 (\$1,944,000 on June 29, 2007), as well as a distribution of \$5,652,000 on January 7, 2008 (2007 - Nil).

**8. NET ASSETS RECONCILIATION**

On July 1, 2007 the Fund adopted Section 3855 on a retroactive basis without restatement of prior periods for financial reporting purposes. However, the Canadian Securities Administrators have granted temporary relief to investment funds from complying with Section 3855, for the purposes of calculating and reporting of Net Assets and Net Asset Value ("NAV") per Unit (other than for financial reporting purposes) until September 30, 2008 to permit review of the suitability of these financial reporting requirements for purposes other than the financial statements, such as the purchase and redemption of an investment fund.

As at June 30, 2008 and 2007, there was no difference between Net Assets and NAV per Unit calculated at the current year's last traded price for the day ("Transactional") and at the current year's bid price for the day ("GAAP"). Any adjustment to the fair value of the securities in the investment portfolio by changing from Transactional Net Assets to GAAP Net Assets was offset by a change in the fair value of the Swap Contract.

**June 30, 2008**

**9. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT**

The investments of the Fund are managed in accordance with the investment objectives and strategies as detailed in the Fund's Management Report on Fund Performance, which also details the specific risks that the Fund could be exposed to. Such risks primarily arise because the value of the investments is affected by changes in the local and global economies including interest rates, foreign exchange rates, financial markets and company-specific news. The Manager monitors these risks on a regular basis.

The risk of derivative contracts arises from the potential inability of the Counterparty to meet the terms of its contracts and from future movement in currency and interest rates. The credit rating of the Counterparty is currently AA- (as per Standard & Poor's). The maximum credit risk exposure is the aggregate of all derivative contracts with a positive value as disclosed on the Statement of Investments.