Consolidated Financial Statements of

MORNEAU SOBECO INCOME FUND

For the Years Ended December 31, 2010 and 2009

MANAGEMENT STATEMENT OF RESPONSIBILITY FOR FINANCIAL REPORTING

The accompanying consolidated financial statements for Morneau Sobeco Income Fund (the "Fund") have been prepared by management and approved by the Board of Trustees of the Fund. Management is responsible for the preparation and presentation of these financial statements and all the financial information contained in the Annual Report within reasonable limits of materiality. The Fund's consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles. In the preparation of these financial statements, estimates are necessary because a precise determination of certain assets and liabilities is dependent on future events. Management believes such estimates have been based on careful judgments and have been properly reflected in the accompanying consolidated financial statements.

To assist management in discharging these responsibilities, the Fund maintains a system of internal controls, which is designed to provide reasonable assurance that the Fund's assets are safeguarded, that transactions are executed in accordance with management's authorization and that the financial records form a reliable base for the preparation of accurate and timely financial information.

Management recognizes its responsibilities for conducting the Fund's affairs in compliance with established financial reporting standards and applicable laws, and for the maintenance of proper standards of conduct in its activities.

KPMG LLP, Chartered Accountants, were appointed as external auditors by the Trustees of the Fund and have audited the consolidated financial statements of the Fund in accordance with Canadian generally accepted auditing standards. Their report outlines the nature of their audit and expresses their opinion on the consolidated financial statements of the Fund.

The Board of Trustees of the Fund has appointed an Audit Committee composed of three Trustees who are not members of management. The Audit Committee meets periodically with management and the external auditors to discuss internal controls over the financial reporting process, auditing matters and financial reporting issues. The Audit Committee is responsible for reviewing the Fund's annual and interim consolidated financial statements and the report of the external auditors. The Audit Committee reports the results of such reviews to the Board of Trustees of the Fund and makes recommendations with respect to the appointment of the Fund's external auditors. In addition, the Board of Trustees may refer to the Audit Committee on other matters and questions relating to the financial position of the Fund and its subsidiaries.

The Board of Trustees of the Fund is responsible for ensuring that management fulfills its responsibilities for financial reporting and is responsible for approving the consolidated financial statements of the Fund.

"Alan Torrie"

Alan Torrie
President and CEO

"Scott Milligan"

Scott Milligan
Chief Financial Officer

KPMG LLP
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INDEPENDENT AUDITORS' REPORT

To the Unitholders' of Morneau Sobeco Income Fund

We have audited the accompanying consolidated financial statements of Morneau Sobeco Income Fund, which comprise the consolidated balance sheets as at December 31, 2010 and 2009, the consolidated statements of income and comprehensive income, unitholders' equity and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of Morneau Sobeco Income Fund as at December 31, 2010 and 2009, and its consolidated results of operations and its consolidated cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

KPMG LLP

Chartered Accountants, Licensed Public Accountants

March 10, 2011
Toronto, Canada

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MORNEAU SOBECO INCOME FUND
CONSOLIDATED BALANCE SHEETS
As at December 31
(In thousands of dollars)

	2010	2009
Assets		
Current assets:		
Cash	$ 360	$ 1,596
Accounts receivable	61,093	55,018
Unbilled fees	16,266	17,526
Income taxes recoverable	173	569
Prepaid expenses and other	1,896	3,298
Current portion of deferred implementation costs	659	167
	80,447	78,174
Foreign exchange contracts	-	479
Deferred implementation costs	2,881	929
Capital assets (note 4)	17,034	15,333
Intangible assets (note 5)	234,650	253,659
Goodwill (note 6)	300,792	300,792
	$ 635,804	$ 649,366
Liabilities and Unitholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities	$ 40,092	39,139
Deferred revenues	1,584	1,795
Current portion of long-term debt (note 7)	11,500	11,500
Current portion of promissory note (note 8)	-	4,306
Future consideration related to acquisition (note 3)	-	2,457
Unitholder distributions payable (including non-controlling)	-	3,759
	53,176	62,956
Insurance premium liabilities:		
Payable to insurance companies	13,946	9,313
Less related cash and investments held	(13,946)	(9,313)
	-	-
Long-term debt (note 7)	183,355	158,887
Interest-rate swaps (note 7)	4,424	6,656
Other liabilities (note 9)	8,575	10,206
Future income taxes (note 13)	5,909	12,179
	255,439	250,884
Non-controlling interests (note 11)	41,591	46,137
Unitholders' equity (note 10)	338,774	352,345
	$ 635,804	$ 649,366

Commitments, Contingencies, and Subsequent Events (notes 1, 3, 7, 10, 11, 17 and 18)
Economic dependence (note 19)

See accompanying notes to consolidated financial statements

"Robert Chisholm"
Robert Chisholm
Trustee, Audit Committee Chair

"Alan Torrie"
Alan Torrie
Trustee, President & CEO

MORNEAU SOBECO INCOME FUND
CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME
(In thousands of dollars, except per unit amounts)

	Year Ended December 31, 2010	Year Ended December 31, 2009
Revenue		
Fees	$ 314,177	$ 309,315
Commissions	20,779	22,044
Other	238	344
	335,194	331,703
Expenses		
Salary, benefit and contractor expenses	221,325	210,243
Other operating expenses	60,330	61,484
Amortization of capital assets	4,645	4,012
Amortization of intangible assets	22,073	41,139
Interest expense (note 7)	10,461	13,211
	318,834	330,089
Income before income taxes and non-controlling interest	16,360	1,614
Income taxes (recovery) (note 13)		
Current	837	813
Future	(5,747)	(11,427)
	(4,910)	(10,614)
Income before non-controlling interest	21,270	12,228
Non-controlling interest (note 11)	(2,341)	(1,402)
Net income	18,929	10,826
Other comprehensive income		
Unrealized gain on interest rate swap hedges, net of tax effect	2,753	4,524
Comprehensive income for the year	$ 21,682	$ 15,350
Net income per Unit (basic) (note 15)	$ 0.45	$ 0.27
Net income per Unit (diluted) (note 15)	$ 0.44	$ 0.26

See accompanying notes to consolidated financial statements

MORNEAU SOBECO INCOME FUND
CONSOLIDATED STATEMENTS OF UNITHOLDERS' EQUITY
Years Ended December 31, 2010 and 2009
(In thousands of dollars)

	Unitholders' Capital	Contributed Surplus	Accumulated Other Comprehensive Income/(Loss)	Deficit	Total
Balance, December 31, 2008	$ 362,223	$ -	$ (10,469)	$ (32,997)	$ 318,757
Exchange of Class B LP Units	1,721	-	-	-	1,721
Issuance of Units	55,000	-	-	-	55,000
Issuance costs, net of future income tax benefits	(2,467)	-	-	-	(2,467)
Long-term incentive plan – conversion	(3,176)	1,650	-	-	(1,526)
Long-term incentive plan – non-cash expense	-	2,258	-	-	2,258
Long-term incentive plan – vested Units	73	(73)	-	-	-
Long-term incentive plan – sale of Treasury Units	2,293	-	-	(407)	1,886
Net income for the year	-	-	-	10,826	10,826
Comprehensive income for the year	-	-	4,524	-	4,524
Distributions	-	-	-	(38,634)	(38,634)
Balance, December 31, 2009	$ 415,667	$ 3,835	$ (5,945)	$ (61,212)	$ 352,345
Exchange of Class B LP Units (note 10)	1,905	-	-	-	1,905
Long-term incentive plan – non-cash expense (note 12)	-	2,919	-	-	2,919
Long-term incentive plan – DRIP (note 12)	-	209	-	(209)	-
Long-term incentive plan – settlement of awards through Treasury (note 10)	169	(69)	-	(49)	51
Long-term incentive plan – settlement of awards through issuance of Units (note 10)	1,601	(1,601)	-	-	-
Net income for the year	-	-	-	18,929	18,929
Comprehensive income for the year	-	-	2,753	-	2,753
Distributions	-	-	-	(40,128)	(40,128)
Balance, December 31, 2010	$ 419,342	$ 5,293	$ (3,192)	$ (82,669)	$ 338,774

See accompanying notes to consolidated financial statements

MORNEAU SOBECO INCOME FUND
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands of dollars)

	Year Ended December 31, 2010	Year Ended December 31, 2009
Cash provided by (used in):		
Operating activities		
Net income	$ 18,929	$ 10,826
Items not involving cash:		
Amortization of capital assets	4,645	4,012
Amortization of intangible assets	22,073	41,139
Amortization of debt issue costs (note 7)	469	469
Non-controlling interest of Class B LP Units (note 11)	2,341	1,402
Long-term incentive plan	2,919	2,258
Future income taxes (recovery)	(5,747)	(11,427)
Accretion on promissory notes (note 7)	194	3,488
Fair value of forward exchange contracts	478	(1,299)
Write-down of proprietary software (note 5)	2,417	-
Write-down of leasehold improvements	-	1,338
Changes in sublease loss provisions	(1,446)	1,322
Other	(139)	37
	47,133	53,565
Change in non-cash operating working capital (note 16)	(4,719)	(4,610)
	42,414	48,955
Financing activities		
Issuance of units	-	55,000
Expenses related to issuance of units	-	(3,500)
Proceeds from long-term debt (note 7)	24,000	23,000
Repayment of promissory note (note 8)	(4,500)	(74,730)
Change in revolving loan	-	4,500
Proceeds from sale of treasury Units	-	1,886
Distributions paid	(48,869)	(43,377)
	(29,369)	(37,221)
Investing activities		
Business acquisition – Leong & Associates (note 3)	(2,457)	-
Business acquisition – Cowan	-	(930)
Proceeds from sale of intangible assets	-	218
Additions to intangible assets	(5,482)	(4,325)
Purchase of capital assets	(6,342)	(4,587)
	(14,281)	(9,624)
Net (decrease) increase in Cash for the year	(1,236)	2,110
Cash (Bank indebtedness), beginning of year	1,596	(514)
Cash, end of year	$ 360	$ 1,596

Supplement disclosure of cash flow information (note 16)

See accompanying notes to consolidated financial statements

1. ORGANIZATION AND NATURE OF THE BUSINESS

Morneau Sobeco Income Fund (the "Fund") is an unincorporated, open-ended, limited purpose trust established under the laws of the Province of Ontario on August 22, 2005.

The Fund is a Canadian-owned firm providing human resource consulting and outsourcing services, delivering solutions to assist employers in managing the financial security, health and productivity of their employees. The Fund offers its services to organizations that are situated in Canada, in the United States and around the globe.

On December 2, 2010, the Fund received the requisite regulatory approvals and third-party consents required to complete the reorganization (the "Reorganization") of the Fund from an income trust structure into a public corporation named Morneau Shepell Inc. ("Morneau Shepell"), effective January 1, 2011. Pursuant to this plan of arrangement under the *Business Corporations Act (Ontario)*, the Fund converted into Morneau Shepell effective January 1, 2011. The Reorganization will be accounted for as a continuity of interest, whereby the assets and liabilities assumed by Morneau Shepell are measured at the Fund's carrying amounts.

2. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements of the Fund have been prepared by management in accordance with Canadian generally accepted accounting principles and the significant accounting policies are summarized below:

a) Basis of presentation

These consolidated financial statements include the assets, liabilities, revenue and expenses of the following entities:

	% Ownership
Morneau Sobeco Trust ("Trust")	100.0
Morneau Sobeco GP Inc.	100.0
Morneau Sobeco Limited Partnership	89.2
Morneau Sobeco Group Limited Partnership ("MS Group LP")	89.2
Morneau Sobeco, Ltd.	89.2
HRCO Inc ("HRCO")	89.2
FGI World France S.A.R.L.	89.2
FGI World New Caledonia	89.2
1137273 Ontario Limited	89.2
Morneau Sobeco IT Solutions Inc.	89.2
Innu-Med Inc.	42.8

All intercompany transactions and balances have been eliminated upon consolidation.

(b) Use of estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period.

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

The most significant estimates that the Fund is required to make relate to the recoverability of its intangible assets, goodwill and accounts receivable as well as the valuation of derivative financial instruments, future income tax assets and liabilities. The estimated value of these assets and liabilities usually depend upon estimates of the profitability of the related business which, in turn, depend upon assumptions regarding future conditions in the general or specific industry, including the effects of economic cycles, and other factors that affect the operating revenue.

These assumptions are limited by the availability of reliable comparable data, economic uncertainty and the uncertainty of predictions concerning future events. Accordingly, by their nature, estimates of fair value are subjective and do no necessarily result in precise determinations. Should the underlying assumptions change, the estimated value could change by a material amount.

(c) Revenue recognition and unbilled fees

Revenues include fees generated from administrative, actuarial, and consulting services, employee assistance programs (EAP), and outsourcing contracts.

Fees for administrative, actuarial and consulting services are billed either on a time-and-material basis or on a fixed-fee basis. On time-and-material engagements, revenue is recognized as services are rendered and expenditures are incurred. On fixed-fee engagements, revenue is recognized in the period in which the services are rendered.

EAP revenue is recognized through a combination of the minimum contracted amount and incremental usage above the minimum thresholds. The minimum contracted amount is recognized on a basis consistent with provision of EAP services. Incremental usage is recognized when the minimum usage threshold is exceeded.

Outsourcing engagements typically involve both an implementation and administration component. Revenues associated with these contracts have been recognized in accordance with CICA Handbook EIC-142 *Revenue Arrangements with Multiple Deliverables*, to determine whether each component of the outsourcing contract qualifies for treatment as a separate unit of account. Multiple deliverable arrangements are determined to exist if all of the following criteria are met:

- The delivered item has value to the customer on a stand-alone basis;
- There is objective evidence of the fair value of the undelivered item; and
- If the arrangement includes a general right of return relative to the delivered item, delivery or performance of the undelivered item is considered probable and substantially in the control of the vendor.

If these criteria are not met, deliverables (components) included in an arrangement are accounted for as a single unit of accounting and revenue is deferred and recognized on a basis consistent with elements of the service contract.

Unbilled fees are recorded at the lower of unbilled hours worked at normal billing rates and the amount which is estimated to be recoverable upon invoicing.

Commissions are recognized when earned, which is at the later of the billing or the effective date of the policy, net of a provision for return commissions due to policy cancellations or change of brokers.

Other revenue includes investment income recorded on the accrual basis.

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

(d) Deferred implementation costs and deferred outsourcing revenues

Implementation costs incurred in connection with the outsourcing service contracts, relate to those costs necessary to set up clients and their human resource or benefit programs onto the Fund's systems and operating processes. Such costs may include internal and external costs for coding and customizing systems, client data conversion costs, and contract negotiation costs. On outsourcing contracts that are accounted for as a combined unit of accounting, specific, incremental, and direct costs of the implementation component are deferred and amortized over the term of the service contract. For outsourcing contracts where each component is considered a separate unit of accounting, those costs are deferred and amortized over the remaining term of each component.

Implementation fees are typically received from clients either up-front or over the course of the implementation period. These fees are initially deferred and recognized as revenue over the term of the service contract if accounted for as a combined unit of accounting, or over the term of the implementation period, if accounted for as a separate unit of accounting. If a client terminates an outsourcing contract prior to its end, a loss on the contract may be recorded (if necessary), and any remaining deferred implementation revenues and costs would be recognized into income over the remaining implementation period through to the date of termination.

(e) Foreign currency translation

The Fund's and its subsidiaries' functional currency is the Canadian dollar. Monetary assets and liabilities denominated in foreign currencies have been translated into Canadian dollars at the exchange rates prevailing at the consolidated balance sheet dates. Non-monetary items have been translated into Canadian dollars at the exchange rates prevailing when the assets were acquired or obligations incurred. Revenues and expenses have been translated at rates in effect on the transaction dates. Exchange gains or losses are reflected in income for the year.

(f) Capital assets

Capital assets are stated at their initial capital cost less accumulated amortization. Amortization is recognized over the assets' estimated useful lives as follows:

Asset	Basis	Rate
Computer equipment	Declining balance	30%
Furniture and equipment	Declining balance	20%
Leasehold improvements	Straight-line	Over term of the lease

(g) Intangible assets

Intangible assets consist of customer relationships, customer contracts, proprietary software, non-compete agreements, and trade names acquired through acquisitions or business combinations, internally-developed software for internal use, and purchased software. Intangible assets acquired through acquisitions or business combinations are initially recognized at fair value based on an allocation of the purchase price. Internally-developed proprietary software for internal use is recognized at the aggregate amount of all eligible development costs, determined in accordance with Section 3064, *Goodwill and Intangible Assets*. Eligible expenditures capitalized as part of proprietary software developed for internal use include external direct costs of materials and services consumed in development, and payroll and payroll-related costs for employees who are directly associated with and who devote time to the internal-use computer software project (to the extent that their time was spent directly on the project). All costs incurred in the preliminary research stage of the projects are expensed as incurred.

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

Intangible assets with a finite life are amortized on a straight-line basis over their estimated useful lives, or on a declining balance basis for purchased software. Intangible assets with an indefinite life are not amortized, but are tested for impairment annually or more frequently if events or circumstances indicate there may be an impairment by comparing the estimated discounted future net cash flows from the asset to its carrying amount.

Amortization is recognized over the assets' estimated useful lives as follows:

Asset	Estimated useful lives
Customer relationships	15 to 20 years
Customer contracts	1 to 2 years
Proprietary software	5 years
Non-compete agreements	16 months
Trade names	Indefinite
Internally-developed software	5 to 10 years
Purchased software	30% to 50% declining balance

(h) Impairment of long-lived assets

Long-lived assets with finite lives are reviewed for impairment annually or whenever events or changes in circumstances cause their carrying amount to exceed the total undiscounted cash flows expected from their use and eventual disposition. An impairment loss is measured at the amount by which the carrying amount of the long-lived asset exceeds its fair value

i) Goodwill

Goodwill is not amortized and is subject to an annual impairment test. Goodwill impairment is assessed based on a comparison of the estimated fair value of each of the Fund's reporting units and the carrying value of its net assets including goodwill. An impairment loss will be recognized if the carrying amount of the reporting unit's net assets exceeds its estimated fair value.

(j) Insurance premium liabilities and related cash and investments

In its capacity as consultants, the Fund collects premiums from insurers and remits premiums, net of agreed deductions, such as taxes, administrative fees and commissions, to insurance underwriters. These are considered flow-through items for the Fund and, as such, the cash and investment balances relating to these liabilities are deducted from the related liability in the consolidated balance sheets.

(k) Long-term incentive plan

Under the Fund's long-term incentive plan ("LTIP") consisting of a restricted stock unit plan (the "RSU plan") and a deferred stock unit plan (the "DSU plan"), participants are eligible to receive Units. The amount awarded under the DSU plan is valued at the Unit's fair value on the date of the award, and the RSU plan is based on the purchased amount. The amounts awarded are recorded as salary, benefit and contractor expenses in line with the vesting dates which range from one to three years. As the Units vest, they are transferred or issued to the plan participant and are recorded as Unitholders' Capital. Holders of the DSUs are either entitled to cash bonuses equivalent to the distributions paid on the Fund Units (if issued prior to 2010) or additional DSUs (if issued in 2010) determined by dividing the amount of the distributions payable in respect of the DSUs by the Fair Market Value per Unit on the date credited. DSUs credited under this Distribution Reinvestment Policy ("DRIP") shall vest at the same rate as the Units on

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

which they are determined. Cash bonuses are recorded as expenses as distributions are declared. DSUs issued under DRIP have been accounted for as a credit to Contributed Surplus, with a corresponding charge to Deficit.

(l) Employee future benefits

The Fund offers a pension benefit plan for its eligible employees, which includes a defined benefit option and a defined contribution option.

The defined benefit option was closed effective January 1, 1998 and included 6 employees, 10 retirees and 45 deferred vested members as at December 31, 2010. All other employees are covered by the defined contribution option of the plan.

The Fund accrues its obligations under the defined benefit option of the plan as the employees render the services necessary to earn the pension. For the defined contribution option, the Fund matches member contributions and may be required to make additional contributions at the option of the member, up to the limits defined in the plan text.

(m) Income taxes

The Fund uses the asset and liability method of accounting for income taxes. Future income taxes are recognized for the temporary differences between the financial statement carrying amounts of assets and liabilities and their respective tax bases. Future income tax assets and liabilities are measured using enacted or substantively enacted tax rates and laws that are expected to apply to taxable income in the years in which those temporary differences are expected to be reversed or settled. A valuation allowance is recorded against a future income tax asset if it is not anticipated that the asset will be realized in the foreseeable future. The effect on future income tax assets and liabilities of a change in tax rate is recognized in income in the period that includes the date of enactment or substantive enactment.

(n) Deferred lease inducements

Lease inducements comprise rent-free periods and leasehold improvement allowances. Lease inducements are deferred and amortized to rental expense on a straight-line basis over the term of the related lease.

(o) Financial instruments

Financial assets and financial liabilities are initially measured at fair value, defined as the amount of consideration that could be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act. In certain circumstances, however, the initial fair value may be based on other observable current market transactions in the same instrument, without modification or on a valuation technique using market based inputs. Subsequent measurement of the Fund's financial assets and liabilities is dependent on their classification as held for trading, loans and receivables, other financial liabilities, or derivative instruments.

Held for trading financial assets and liabilities are measured at fair value as at the date of the consolidated balance sheet, and any unrealized gains or losses from market fluctuations are included in the consolidated statement of income.

Loans and receivables and other financial liabilities are measured at amortized cost using the effective interest method of amortization.

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

Derivative financial instruments are used by the Fund in the management of its interest rate risk exposure on debt financing and foreign exchange risk arising due to fluctuations in the United States dollar. Derivatives that have been designated and function effectively as a hedge are accounted for using hedge accounting principles. The effective portions of changes in fair value of derivatives that qualify for hedge accounting are recorded in other comprehensive income. Any ineffective portions of changes in the fair value are recognized in net income in the period in which the change occurred. If the hedging relationship ceases to be effective, the cumulative change in the fair value of the interest-rate swap are recognized into income beginning in the period in which the change occurs. Derivatives that do not qualify for hedge accounting are recorded on the consolidated balance sheet at fair value with changes in fair value recorded as income or expense in the consolidated statement of income.

Fair value measurements recognized in the balance sheet are categorized using a fair value hierarchy that reflects the significant inputs used in determining the fair values, in accordance with the amendment to CICA Handbook Section 3862 in June 2009:

(i) Level–1 - Inputs unadjusted quoted prices of identical instruments in active markets

(ii) Level–2 - Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly

(iii) Level 3 – One or more significant inputs used in a valuation technique are unobservable in determining fair values of the instruments

Each type of fair value is categorized based on the lowest level input that is significant to the fair value measurement.

The Fund does not use derivative financial instruments for trading or speculative purposes.

(p) Future accounting change

International Financial Reporting Standards ("IFRS") – The Canadian Accounting Standards Board confirmed in February 2008 plans to converge Canadian Generally Accepted Accounting Principles ("GAAP") with IFRS for interim and annual reporting periods commencing January 1, 2011. The Fund's first annual IFRS consolidated financial statements will be for the year ended December 31, 2011, and will include the comparative period for the year ended December 31, 2010.

3. BUSINESS ACQUISITION

Leong & Associates Actuaries And Consultants Inc. ("Leong & Associates")

On October 1, 2008, a subsidiary of the Fund acquired all the issued and outstanding shares of Leong & Associates, a British Columbia based actuarial and pension consulting firm in Western Canada. The purchase price is contingent on business results and is expected to be payable in three instalments. The first instalment of $3,010 was satisfied on closing through cash and equity consideration. The second instalment of $2,457, which was subject to revenue adjustments plus interest calculated at annual rates of 3.27%, was paid during the year. The third and final instalment is subject to revenue adjustments plus interest calculated at annual rates of 3.87%, and will be settled on April 1, 2011.

4. CAPITAL ASSETS

The Fund's capital assets are comprised of:

	Cost	Accumulated Amortization December 31, 2010	Net Book Value December 31, 2010
Computer equipment	$ 11,513	$ (4,578)	$ 6,935
Furniture and equipment	7,252	(3,793)	3,459
Leasehold improvements	13,493	(6,853)	6,640
	$ 32,258	$ (15,224)	$ 17,034

	Cost	Accumulated Amortization December 31, 2009	Net Book Value December 31, 2009
Computer equipment	$ 7,319	$ (2,566)	$ 4,753
Furniture and equipment	6,985	(2,936)	4,049
Leasehold improvements	11,622	(5,091)	6,531
	$ 25,926	$ (10,593)	$ 15,333

5. INTANGIBLE ASSETS

The Fund's intangible assets are comprised of:

	Cost	Accumulated Amortization December 31, 2010	Net Book Value December 31, 2010
Customer relationships	$ 199,557	$ (43,863)	$ 155,694
Customer contracts	27,900	(27,722)	178
Proprietary software	41,000	(40,517)	483
Purchased software	5,111	(2,697)	2,414
Internally-developed software	6,081	(200)	5,881
Trade names	70,000	-	70,000
	$ 349,649	$ (114,999)	$ 234,650

During the year, as a result of the development of a new software platform, the Fund recognized an impairment loss of $2,417 on certain proprietary software acquired in the Shepell•fgi acquisition, that had a cost of $5,000 and accumulated amortization of $2,583 at the time of impairment. This amount has been included in Other Operating Expenses.

As at December 31, 2010, $332 (December 31, 2009 - $3,169) of internally-developed software remained under development and had not been put into use.

5. INTANGIBLE ASSETS (continued)

	Cost	Accumulated Amortization December 31, 2009	Net Book Value December 31, 2009
Customer relationships	$199,557	$ (32,057)	$ 167,500
Customer contracts	27,500	(26,125)	1,375
Proprietary software	46,000	(35,900)	10,100
Internally-developed software	3,169	-	3,169
Purchased software	2,943	(1,428)	1,515
Non-compete agreements	5,000	(5,000)	-
Trade names	70,000	-	70,000
	$354,169	$ (100,510)	$ 253,659

6. GOODWILL

	2010	2009
Balance, beginning of year	$ 300,792	$ 299,676
Acquisition - Cowan	-	246
Acquisition - Leong & Associates (note 3)	-	870
	$ 300,792	$ 300,792

On August 1, 2009, the final instalment relating to the Cowan acquisition was made for cash consideration of $930, of which $684 was accrued for as contingent consideration on acquisition in 2007. The remaining $246 was recorded as goodwill.

7. LONG-TERM DEBT

	2010	2009
Non-revolving term loans	$ 160,000	$ 160,000
Revolving loans	35,500	11,500
	195,500	171,500
Less: current portion of long-term debt	(11,500)	(11,500)
Less: debt issue costs, net of accumulated amortization	(645)	(1,113)
	$ 183,355	$ 158,887

On April 15, 2010, the credit available under the revolving facility was amended for an increase of $25 million to $40 million. The terms of the facility remain consistent to those of the initial facility.

At December 31, 2010 the Fund had available and utilized the following credit facilities:

- $160,000 of term loans. The term loans are repayable in full on June 1, 2012 and bear interest at prime rate plus an applicable margin of 2.00%.
- $35,500 of $40,000 revolving loans. The revolving loans are prime loans which are repayable in full on June 1, 2012, and bear interest at prime rate plus an applicable margin of 2.00%.
- $Nil of the $5,000 swing line available. The swing line carries interest at prime plus an applicable margin of 2.00%.

7. LONG-TERM DEBT (continued)

The credit facilities are secured by a general assignment of all of the assets of the Fund, and require the Fund to maintain, on a consolidated basis, a Debt to Adjusted EBITDA not greater than 3.25:1.0, and an EBITDA to interest expense ratio of not less than 3.0:1.0.

EBITDA is defined as net income before interest expense, income taxes (recovery), depreciation, amortization, non-controlling interest, and non-recurring expenditures. Adjusted EBITDA is defined as EBITDA plus the pro-forma EBITDA from Permitted Acquisitions' entities.

The Fund complied with all the required financial covenants and the ratios as at December 31, 2010 were 3.0 and 6.3 respectively.

Subsequent to the year end, the Fund entered into an amended and restated credit agreement effective January 1, 2011 for a term of four years. The credit facility provides for a term loan of $130,000 and a revolving facility of $75,000, which includes a swing line of $7,000. The terms of the amended and restated credit agreement remain similar to those contained in the previous agreement, with the exception of a change in the required Debt to Adjusted EBITDA financial covenant of 3.25:1.00 effective as at December 30, 2010 and up to December 30, 2011, and 3.00:1:00 on December 31, 2011, and thereafter.

Interest-rate swaps

In order to fix the variable interest rate component of the Fund's term loans outstanding at 3.647% and 2.22% before the applicable margin, the Fund previously entered into interest-rate swap agreements in the notional amounts of $137,000 and $23,000, respectively, and had designated these interest-rate swaps as cash flow hedges against the term loans outstanding.

As at December 31, 2010, the unfavorable fair value of the Fund's interest-rate swap agreements in the notional amounts of $137,000 and $23,000 were $4,198 (December 31, 2009 - $6,358) and $226 (December 31, 2009 - $298) respectively.

Subsequent to the year end, the Fund terminated the above noted interest-rate swap agreements, effectively eliminating the designated hedging items from the cash flow hedge relationships. As a result, $4,150, representing the cumulative loss on the interest rate swap cash flows hedges recognized through other comprehensive income up to the date of hedge termination, will be amortized into net income as interest expense concurrently with term loan variable interest payments, over the remaining term of the original term facility until maturity in June 2012.

Interest expense

Interest expense is comprised of the following:

	Year Ended December 31, 2010	Year Ended December 31, 2009
Interest on term loans	$ 8,733	$ 8,581
Accretion of interest on promissory notes (note 8)	194	3,488
Interest on Leong & Associates' instalments (note 3)	96	156
Interest on revolving loan, bank indebtedness and other charges	969	517
Amortization of debt issue costs	469	469
	$ 10,461	$ 13,211

8. PROMISSORY NOTES

On July 1, 2010, the Fund fully repaid the $4,500 promissory note issued as part of Shepell•fgi acquisition. The note was non-interest bearing and was secured by a general assignment of all the assets of the Fund, subordinate to the credit facilities.

9. OTHER LIABILITIES

	2010	2009
Acquired above-market rent leases	$ 4,571	$ 5,221
Sub-lease losses	1,890	3,336
Deferred lease obligations	2,114	1,649
	$ 8,575	$ 10,206

As part of the Shepell•fgi acquisition, the Fund assumed lease agreements for several offices. The above amounts include the difference between estimated market rates and the lease agreements. The estimated sub-lease losses are as a result of excess office spaces assumed from the Shepell•fgi and Leong & Associates acquisitions of previous years.

In 2009, the Fund sub-leased out, in two separate transactions ("Subleases"), excess office space. As a result of the Subleases, the Fund recognized an aggregate loss of $3,538, which includes a write down of the carrying value of leasehold improvements associated with the sub-leased premises of $1,338. The loss is reported under Other operating expenses.

10. FUND UNITS

The Fund is authorized to issue an unlimited number of Units and an unlimited number of special voting units ("Special Voting Units"). Special Voting Units are not entitled to any beneficial interest in any distribution from the Fund. The Special Voting Units may be issued in series and will only be issued in connection with, or in relation to, Class B LP Units or other securities that are, directly or indirectly, exchangeable for Units, in each case for the sole purpose of providing voting rights at the Fund level to the holders of such securities.

Units are redeemable at any time on demand by the Unitholders up to an aggregate maximum monthly amount of $50. Trustees may, in their sole discretion, waive this limitation. The redemption price is calculated based on the lesser of:

a) 90% of the "market price", as defined in the prospectus, as of the date on which the Units were surrendered for redemption; and

b) 100% of the "closing market price", as defined in the prospectus, on the redemption date.

10. FUND UNITS (continued)

The following details the issued and outstanding Units and Special Voting Units:

	Units Issued	Special Voting Units	Total Units	Amount
Balance, December 31, 2008	35,380,524	5,696,591	41,077,115	$ 362,223
Exchange of Class B LP Units	233,265	(233,265)	-	1,721
Units issued in public offering	6,666,700	-	6,666,700	55,000
Issuance costs, net of future income tax benefits	-	-	-	(2,467)
Treasury Units related to Long-term incentive plan	-	-	-	(810)
Balance, December 31, 2009	42,280,489	5,463,326	47,743,815	$ 415,667
Exchange of Class B LP Units	272,132	(272,132)	-	1,905
Settlement of LTIP awards through Treasury	-	-	-	169
Settlement of LTIP awards through issuance	196,594	-	196,594	1,601
Balance, December 31, 2010	42,749,215	5,191,194	47,940,409	$ 419,342

On December 6, 2010, the Fund issued 196,594 Units to settle DSU awards owing to a former employee. This settlement has been recorded at $1,601, representing the fair value of the Units on the date of their award, and accounted for through Contributed Surplus.

On January 2, 2010, the Fund utilized 14,745 Treasury Units to settle DSU awards to a former employee resulting in a loss of $49, which represented the difference between the average price of the Treasury Units and the price used to determine the award, has been accounted for through the deficit balance in Unitholders' Capital. The Fund has 43,793 Treasury Units as at December 31, 2010 (December 31, 2009 – 68,587).

On March 24, 2009, the Fund completed a public offering ("Offering"). Pursuant to the Offering, the Fund issued 6,666,700 Units at a price of $8.25 per unit for cash proceeds of $55,000. The issuance costs, net of future income tax benefits of $1,033, were $2,467.

On May 13, 2009, certain participants of the RSU plan exchanged their awarded Units for new LTIP DSUs (note 12). Pursuant to the exchange, the Fund indirectly re-acquired 277,016 Fund Units, of which 200,000 Units were sold in December 2009 at an average price of $9.431 per unit, for net proceeds of $1,886. The Units were valued at a cost of $11.465 per Unit, resulting in a loss of $407, which has been accounted for through the deficit balance in Unitholders' Capital. In December 2009, 8,429 of the re-acquired Units were also used to satisfy vested RSU awards.

Subsequent to the year-end and pursuant to the Reorganization (note 1), all Units and Special Units outstanding were exchanged on a one-to-one basis for shares of Morneau Shepell.

11. NON-CONTROLLING INTERESTS

The former shareholders of Morneau Sobeco, Heath Benefits Consulting Inc., and Leong & Associates own 5,191,194 Class B LP Units of MS Group LP (a subsidiary of the Fund). The Class B LP Units are fully exchangeable for an equal number of Units in the Fund which equates to a non-controlling interest of 10.8% (December 31, 2009 – 11.4%) in the Fund.

	Unit issued	Amount
Balance, December 31, 2008	5,696,591	$ 51,724
Exchanged Units	(233,265)	(1,721)
Share of income for the year	-	1,402
Distributions for the year	-	(5,268)
Balance, December 31, 2009	5,463,326	$ 46,137
Exchanged Units	(272,132)	(1,905)
Share of income for the year	-	2,341
Distributions for the year	-	(4,982)
Balance, December 31, 2010	5,191,194	$ 41,591

Pursuant to the Reorganization (note 1), and subsequent to the year on January 1, 2011, all Class B Units were sold on a one-to-one basis, for common shares of Morneau Shepell.

12. LONG-TERM INCENTIVE PLAN

The Fund has two types of long-term incentive plans: a restricted stock unit plan (“RSU plan”) and a Deferred Stock Unit Plan (“DSU plan”).

RSU plan

Under the Fund’s RSU plan an individual is awarded a dollar amount, which will be used by the trustees of the RSU plan to purchase Units of the Fund in the open market. The Units will be held by the trustees until such time as ownership vests to each participant. Units will vest within a period of three years from end of the year in respect of which the grant was made, based upon the determination made by the Compensation, Nominating and Corporate Governance Committee (“CNCG Committee”) and/or Board at the time of the grant. Participants will be entitled to receive distributions on all Units held for their account prior to the applicable vesting date. Unvested Units held by the trustees for a participant will typically be forfeited if the participant resigns or is terminated prior to the applicable vesting date. Forfeited Units will be sold and the proceeds returned to the Fund, or as otherwise directed by the Fund.

The expense recognized for the year ended December 31, 2010 was $75 (December 31, 2009 - $599).

DSU Plan

The Fund’s DSU plan offered by its subsidiary, HRCO Inc., received Unitholders’ approval on May 13, 2009.

At the option of the Fund, each DSU represents the right of the employee to receive, on a deferred basis: one Fund Unit issued from treasury; or the equivalent cash value; or an award of one exchangeable share of HRCO Inc., subject to such restrictions as the compensation committee may determine. Holders of DSUs receive cash bonuses equivalent to the distributions paid on the Units. DSUs are non-assignable other than by will or the laws of descent and distribution, and generally vest over one to three years. The compensation committee can accelerate the vesting of DSUs at its discretion.

12. LONG-TERM INCENTIVE PLAN (continued)

A maximum of 1,750,000 Units or securities exchangeable for Units that are issued and outstanding, may be issued under the DSU Plan.

On March 9, 2010 the Fund granted 334,012 LTIP DSUs to senior management of the Fund, where the vesting period commenced on May 1, 2010. These DSUs have the same features as the previous DSUs granted, except Holders of the DSUs do not receive cash bonuses equivalent to the distributions paid on the Units. Instead, Holders of the DSUs receive additional DSUs determined by dividing the amount of the distributions payable in respect of the DSUs by the Fair Market Value per Unit on the date credited. DSUs credited under this Distribution Reinvestment Policy (“DRIP”) shall vest at the same rate as the Units on which they are determined.

DSUs issued under DRIP have been accounted for as a credit to Contributed Surplus, with a corresponding charge to Deficit. As at December 31, 2010, a total of $209 has been credited to Contributed Surplus and charged to Deficit.

In 2009, the Fund granted 535,284 DSUs primarily to senior management of Shepell•fgi, related to the 2008 acquisition of Shepell•fgi. In addition, certain participants of the RSU plan exchanged their awarded Units under the RSU plan for new LTIP DSUs (“the exchange”) on a one for one basis with identical vesting. The exchange resulted in the Fund indirectly re-acquiring 277,016 Fund Units.

The measurement date for the awards for accounting purposes occurred once the DSU plan received Unitholder approval. It is the Fund’s intention to settle all of the DSU obligations through the issuance of Units. Consequently, the DSUs will not be re-measured at each reporting period.

As at December 31, 2010, the total LTIP DSUs held by the participants was 834,810 Units (December 31, 2009 – 812,300) and the expense recognized for the year ended December 31, 2010 was $3,526 (December 31, 2009 - $3,003).

13. INCOME TAXES

The Fund qualified as a Mutual Fund Trust for Canadian income tax purposes. Prior to new legislation relating to the federal income taxation of publicly-listed or traded trusts, as discussed below, income earned by the Fund and distributed annually to Unitholders was not, and would not be, subject to taxation in the Fund. For financial statement reporting purposes, the tax deductibility of the Fund’s distributions was treated as an exemption from taxation as the Fund distributed and was committed to continue distributing all of its income to its Unitholders. Accordingly, the Fund did not previously record a provision for income taxes, or future income tax assets or liabilities, in respect of the Fund and its flow-through entities. The Fund, however, recorded current and future income tax liabilities relating to the corporate subsidiaries.

On June 22, 2007, legislation relating to the federal income taxation of a “specified investment flow-through” trust or partnership (a “SIFT”), received Royal Assent (the “SIFT Rules”). A SIFT includes a publicly-listed or traded partnership and trust, such as an income trust and a real estate investment trust. The Fund is a SIFT, as discussed below.

Under the SIFT Rules, following a transition period for qualifying SIFTs, certain distributions from a SIFT will no longer be deductible in computing a SIFT’s taxable income, and a SIFT will be subject to tax on such distributions at a rate that is substantially equivalent to the general tax rate applicable to a Canadian corporation. Distributions paid by a SIFT as returns of capital will not be subject to the tax.

13. INCOME TAXES (continued)

A SIFT which was publicly listed on or before October 31, 2006 (an "Existing Trust") will become subject to the tax on distributions commencing with the 2011 taxation year.

As a result of the SIFT Rules, the Fund commenced recognizing future income tax assets and liabilities with respect to the temporary differences between the carrying amounts and tax bases of its assets and liabilities, and those of its flow-through entities that are expected to reverse in or after 2011. Future income tax assets or liabilities are recorded using tax rates and laws expected to apply when the temporary differences are expected to reverse.

The difference between income taxes calculated using the Fund's effective income tax rates and the amounts that would result from the application of the statutory income tax rates arises from the following:

	Year Ended December 31, 2010	Year Ended December 31, 2009
Income taxes at statutory rates:		
Federal	18.00%	19.00%
Provincial	12.31%	12.98%
	30.31%	31.98%

	Year Ended December 31, 2010	Year Ended December 31, 2009
Income tax provision applied to income before income taxes:		
Combined basic federal and provincial income taxes at statutory rates applied to income from continuing operations	$ 3,618	$ 517
Income taxed in the hands of the Unitholders	(11,190)	(13,091)
Non-deductible expenses	1,202	999
Adjustment to future income assets and liabilities for change in income tax rate	613	(1,559)
Non-deductible portion of intangible amortization	825	1,911
Other	22	609
	$ (4,910)	$ (10,614)

The significant components of future income tax assets and liabilities related to continuing operations are as follows:

	2010	2009
Future income tax assets:		
Fund Unit issuance costs	$ 1,700	$ 3,191
Capital assets	982	748
Loss carryforward	13,476	7,532
Interest-rate swaps	1,233	709
Other assets	230	-
	$ 17,621	$ 12,180
Future income tax liabilities:		
Intangible assets	$ 23,487	$ 24,300
Other liabilities	43	59
	$ 23,530	$ 24,359

The Fund has losses available to offset future taxable income of $47,901, of which $9,517 expire in 2027, $16,362 expire in 2029, and the remainder in 2030.

14. EMPLOYEE FUTURE BENEFITS

The Fund offers a pension benefit plan for its employees, which includes a defined benefit option and a defined contribution option. The defined benefit option was closed to new members effective January 1, 1998.

Under the defined contribution option, each member is required to contribute a specific dollar amount based on the member's job level classification. Each member may elect to make an optional contribution of between 50% and 300% of the member's required contribution. The Fund matches required contributions. For employees with less than 10 years of service, the Fund contributes 50% of optional contributions and for members with 10 or more years, 75% of optional contributions.

The pension fund assets and obligations are measured as at December 31, 2010. Information about the pension plan's defined benefit option is as follows:

	Year Ended December 31, 2010	Year Ended December 31, 2009
Fair value of plan assets	$ 3,332	$ 2,855
Accrued benefit obligation	3,631	3,129
Funded status – (deficit)	$ (299)	$ (274)
Plan assets:		
Fair value, beginning of year	$ 2,855	$ 2,662
Actual return on plan assets	428	206
Employer contributions	142	215
Benefits paid	(93)	(228)
Fair value, end of year	$ 3,332	$ 2,855

	Year Ended December 31, 2010	Year Ended December 31, 2009
Accrued benefit obligation:		
Balance, beginning of year	$ 3,129	$ 2,594
Current service cost	60	46
Interest cost	181	183
Benefits paid	(93)	(228)
Actuarial loss	354	534
Balance, end of year	$ 3,631	$ 3,129
Reconciliation of plan assets to accrued benefit obligation, end of year:		
Fair value of plan assets	$ 3,332	$ 2,855
Accrued benefit obligation	3,631	3,129
Funded status – (deficit)	(299)	(274)
Unamortized net actuarial gain	318	190
Unamortized transitional obligation	89	179
Accrued benefit asset	$ 108	$ 95
End of year allocation of fair value of plan assets (%):		
Pooled Equities Fund	50%	55%
Pooled Bond Fund	50%	45%
	100%	100%

14. EMPLOYEE FUTURE BENEFITS (continued)

	Year Ended December 31, 2010	Year Ended December 31, 2009
Pension plan cost		
Current service cost	$ 60	$ 46
Interest cost on accrued benefit obligation	181	183
Return on plan assets	(428)	(206)
Actuarial loss (gain) during the year on accrued benefit obligation	354	534
	$ 167	$ 557
Other adjustments:		
Difference between actual and expected return on plan assets	226	20
Amortization of actuarial losses	(354)	(545)
Transitional amounts	90	90
Net pension plan expense	$ 129	$ 122

Other information about the Fund's defined benefit option is as follows:

	Year Ended December 31, 2010	Year Ended December 31, 2009
Employer contributions	$ 142	$ 215
Benefits paid	$ 93	$ 228

Actuarial valuation for the Fund's pension plan is generally required every three years. The most recent actuarial valuation of the Fund's pension plan was conducted as of December 31, 2009.

Weighted average assumptions:

Weighted average of the amounts assumed in accounting for the plan:	Year Ended December 31, 2010	Year Ended December 31, 2009
Discount rate at the end of the current fiscal period used to determine the accrued benefit obligation	5.00%	5.75%
Discount rate at the end of preceding period used to determine the benefit cost	5.75%	7.25%
Rate of compensation increase used to determine the accrued benefit obligation	3.50%	3.50%
Rate of compensation increase used to determine the benefit cost	3.50%	3.50%
Expected long-term rate of return on plan assets	7.00%	7.00%

The net expense for the Fund's defined contribution option for the year ended December 31, 2010 was $3,237 (for the year ended December 31, 2009 - $2,268). In addition, until September 1, 2010, employees of Shepell•fgi participated in a Group RRSP program in which Shepell•fgi matched 50% of the first 6% of salary contribution. The related expense for the period ended December 31, 2010 was $493 (for the year ended December 31, 2009 - $600). Subsequent to September 1, 2010, these employees commenced participation in the Fund's defined contribution option.

15. NET INCOME PER UNIT

Net income per Unit is calculated by dividing net income by the weighted average number of Units outstanding during the year. The following table reconciles the weighted average number of Units outstanding used in computing basic net income per Unit to weighted average number of Units in computing diluted Net income per Unit:

	Year Ended December 31, 2010	Year Ended December 31, 2009
Basic:		
Net income	$ 18,929	$ 10,826
Weighted average number of Units outstanding	42,431,680	40,509,313
Diluted:		
Net income	$ 18,929	$ 10,826
Non-controlling interest	2,341	1,402
Net income available to Unitholders and Class B LP Unitholders	$ 21,270	$ 12,228
Weighted average number of Units outstanding – Basic	42,431,680	40,509,313
Weighted average exchangeable Class B LP Units outstanding	5,289,114	5,584,311
Dilutive effect of LTIP – DSU plan	469,770	239,858
Weighted average number of Units outstanding - Diluted	48,190,564	46,333,482
Net income per Unit – Basic	$ 0.45	$ 0.27
Net income per Unit – Diluted	$ 0.44	$ 0.26

Due to its anti-dilutive effect, the effect of the promissory note has been excluded from the 2009 net income per unit calculation.

16. SUPPLEMENT DISCLOSURE OF CASH FLOW INFORMATION

Change in non-cash operating working capital:

	Year Ended December 31, 2010	Year Ended December 31, 2009
Accounts receivable	$ (6,075)	$ (12)
Unbilled fees	1,260	(1,665)
Income taxes recoverable/payable	396	615
Prepaid expense and other	1,402	668
Deferred implementation costs	(2,444)	(1,096)
Accounts payable and accrued liabilities	953	(840)
Deferred revenue	(211)	(450)
	$ (4,719)	$ (4,610)

	Year Ended December 31, 2010	Year Ended December 31, 2009
Interest paid	$ 9,687	$ 8,958
Income taxes paid	$ 88	$ 1,768

17. COMMITMENTS

The Fund has lease commitments for office premises and equipment with options for renewal. As at December 31, 2010 the minimum payments not including operating expenses, due in each of the next five years and thereafter, are expected to be as follows for each year ending December 31:

	Gross Commitment	Sublease Income	Net Commitment
2011	$ 9,830	$ (2,319)	$ 7,511
2012	8,555	(2,157)	6,398
2013	8,355	(2,098)	6,257
2014	8,312	(2,098)	6,214
2015	7,857	(2,098)	5,759
Thereafter	51,340	(10,595)	40,745
Total	$ 94,249	$ (21,365)	$ 72,884

The Fund is party to various subleases to which the Fund would be liable for the rental payment in the case of a default by the subtenants. The minimal payments and the aggregate sublease income related to these premises have been included above. The Fund considers the risk of default by the subtenants to be low therefore no accrual has been set up for the guarantee.

18. CONTINGENCIES

From time to time, the Fund is involved in routine litigation incidental to the Fund's business. Management believes that adequate provisions have been made where required and the ultimate resolution with respect to any claim will not have a material adverse effect on the financial position or results of operations of the Fund.

19. ECONOMIC DEPENDENCE

Revenue from the Fund's largest client was approximately 5% of the Fund's total revenue for the year ended December 31, 2010 (for the year ended December 31, 2009 – 5%). The Fund's top 10 clients, in the aggregate, accounted for approximately 22% of the total revenue for the year ended December 31, 2010 (for the year ended December 31, 2009 – 22%).

Accounts receivable from the Fund's largest client was approximately 2% of the total accounts receivable as at December 31, 2010 (December 31, 2009 – 1%). The Fund's top 10 clients accounted for approximately 16% of the Fund's total accounts receivable as at December 31, 2010 (December 31, 2009 – 19%).

20. SEGMENTED INFORMATION

The Fund's operations consist of one reporting segment, which provides human resource, consulting and outsourcing services. Geographic data is as follows:

	Year Ended December 31, 2010	Year Ended December 31, 2009
Revenue:		
Canada	$ 315,004	$ 308,464
United States	20,190	23,239
	$ 335,194	$ 331,703

	2010	2009
Assets:		
Canada	$ 627,845	$ 642,516
United States	7,959	6,850
Liabilities:		
Canada	$ 293,350	$ 294,119
United States	3,680	2,902

21. MANAGEMENT OF CAPITAL

The Fund views its capital as the combination of its cash (bank indebtedness), long-term debt, non-controlling interests and Unitholders' equity. The Fund's objectives when managing capital are to safeguard the entity's ability to continue as a going concern while maintaining the distributions to its Unitholders and the growth of the Fund's business through organic growth and new acquisitions.

The Fund manages the capital structure and makes adjustments to it in accordance with the aforementioned objectives, as well as taking into consideration changes in economic conditions and the risk characteristics of the underlying assets. To maintain or adjust the capital structure, the Fund may adjust the amount of distributions paid to Unitholders, issue new or repurchase existing Units and assume new or repay existing debt. The Fund will also review its level of equity in the context of the change in taxation impacting the Fund commencing in 2011.

The credit facilities require the Fund to maintain certain financial covenants. Management also uses these ratios as key indicators in managing the Fund's capital.

Distributions are made to Unitholders monthly. Various ratios of distributions to available cash, cash from operating activities and Adjusted EBITDA are used by management and the Board of Trustees to assist with the determination of distributions.

22. FINANCIAL INSTRUMENTS

Fair value represents management's estimates of the market value at a given point in time. The fair value of the Fund's financial assets and liabilities approximate their carrying values due to their short-term nature or, in relation to long-term debt instruments, because they bear interest at market rates.

22. FINANCIAL INSTRUMENTS (continued)

The following table summarizes information regarding the carrying and fair value of the Fund's financial instruments:

	Year Ended December 31, 2010	Year Ended December 31, 2009
Held for trading [i]	$ 360	$ 2,085
Loans and receivables [ii]	61,093	53,791
Other financial liabilities [iii]	247,946	230,254

(i) Includes cash and derivative financial instruments not designated as hedges.
(ii) Includes accounts receivable.
(iii) Includes accounts payable and accrued liabilities, interest rate swaps, future considerations related to acquisition, long-term debt, promissory notes and other liabilities.

The fair value hierarchy of financial instruments measured at fair value on the balance sheet is as follows:

	Level 1	Level 2	Level 3
Financial Assets:			
Cash	360	-	-
Financial Liabilities:			
Interest-rate swaps liability	-	4,424	-

The fair value of interest-rate swaps was determined using estimated future discounted cash flows using a comparable market rate of interest. Since fair value estimates represent point-in-time estimates, they may not reflect fair value in the future. These calculations are subjective in nature, involve uncertainties, and are a matter of significant judgment; as a result, changes in assumptions could significantly affect these estimates.

Interest rate risk

The Fund is subject to interest rate risk as its secured term loan bears interest at market rates. Interest-rate swap agreements are used as part of the Fund's program to manage the fixed and floating interest rate mix of the Fund's total debt outstanding and related overall cost of borrowing. The interest-rate swap agreements involve the periodic exchange of payments without the exchange of the notional principal amount upon which the payments are based.

A sensitivity analysis that assumes interest rates increased or decreased by 50 basis points with all other variables held constant would result in an increase (decrease) of the Fund's interest expense, excluding the interest subjected to interest-rate swap agreements, by $135.

22. FINANCIAL INSTRUMENTS (continued)

Credit risk

The Fund's exposure to credit risk is limited to carrying amount of cash and accounts receivable recognized at the balance sheet date.

The aging of fees receivable was:

	Year Ended December 31, 2010	Year Ended December 31, 2009
Current	$ 24,908	$ 22,309
Past due 1 - 30 days	16,152	12,835
Past due 31 - 90 days	10,845	11,298
Past due over 90 days	7,427	7,236
	$ 59,332	$ 53,678

The Fund believes that the credit risk of accounts receivable is limited for the following reasons:

(1) Risk associated with concentration of credit risk with respect to accounts receivable is limited due to the credit rating of the Fund's top 10 clients.

(2) Management regularly reviews and assesses customer accounts and credit risk. Historically, bad debt as a percentage of revenue has been minimal.

The Fund determines its allowance for doubtful accounts based on it's best estimate of the net recoverable amount by customer account. Accounts that are considered uncollectible are written off. The allowance for doubtful accounts as at December 31, 2010 was $426 (December 31, 2009 - $632).

The credit risk on cash is limited because the counterparties are banks with high credit ratings assigned by international credit-rating agencies.

Foreign exchange risk

The Fund realizes a portion of sales in U.S. dollars and has operations in the United States and thus is exposed to fluctuations in the value of the U.S. dollar relative to the Canadian dollar. The net revenue exposure after accounting for related expenses denominated in U.S. dollars for the year ended December 31, 2010 was $6,460. To manage the foreign exchange exposure on U.S. dollars sales transactions and collection of related accounts receivable, the Fund had entered into multiple forward exchange contracts during the period to hedge against this exposure. These contracts were not accounted for using hedge accounting, however, and therefore, were measured at fair value with changes recognized in earnings.

As at December 31, 2010, the Fund's net exposure to currency risk through its current assets and liabilities dominated in U.S. dollars was US$4,053. Assuming that all other variables remain constant, a 5% depreciation or appreciation of the Canadian dollar against the US dollars would result in an increase (decrease) of $209 in the Fund's net income.

Liquidity risk

Liquidity risk is the risk that the Fund is not able to meet its financial obligations as they fall due. The Fund manages liquidity risk through regular monitoring of financial results and actual cash flows, and also the management of its capital structure and financial leverage as outlined in note 21.

22. FINANCIAL INSTRUMENTS (continued)

The Fund's principal liquidity needs arise from working capital requirements, debt servicing and repayment obligations, capital expenditures, distributions to Unitholders and acquisition funding requirements.

The Fund has historically utilized cash from operations to satisfy the above needs, with the exception of acquisition funding requirements.

The Fund's credit facility is comprised of two components: a revolving facility which matures monthly but is eligible for renewal until expiry in 2012, and a non-revolving facility which matures in 2012. Subsequent to the year and as mentioned in note 7, the Fund entered into an amended and restated credit agreement whereby the term of the facility was extended to January 5, 2015.

The accounts payable and accrued liabilities are due for payment within twelve months of the balance sheet date, along with the final instalment related to the Leong & Associates payable in April 2011.

23. COMPARATIVE FIGURES

Certain comparative figures have been reclassified or regrouped to conform with the financial presentation adopted in the current year.