Liquor Stores Income Fund

Interim Consolidated Financial Statements
(unaudited)

March 31, 2007
(expressed in Canadian dollars)

Liquor Stores Income Fund
Consolidated Balance Sheets (unaudited)

	March 31, 2007	December 31, 2006
Assets	**$**	**$**
Current assets		
Cash and cash equivalents	1,714,949	3,396,967
Accounts receivable	1,165,209	1,524,689
Inventory	49,233,515	49,702,563
Prepaid expenses and deposits (note 4)	1,693,420	1,158,617
	53,807,093	55,782,836
Pre-opening costs	753,121	818,823
Deposits on future acquisitions (note 4)	1,432,621	1,632,621
Property and equipment	23,500,983	23,040,537
Future income tax asset	60,000	62,400
Intangible assets	768,091	806,044
Goodwill	107,988,784	104,953,874
	188,310,693	187,097,135
Liabilities		
Current liabilities		
Bank indebtedness (note 5)	11,892,852	5,455,414
Accounts payable and accrued liabilities	3,393,097	5,303,678
Current tax payable	20,900	61,800
Distributions payable to unitholders (note 11)	1,273,211	1,193,645
Distributions payable to non-controlling interest (note 11)	908,507	881,282
	17,488,567	12,895,819
Non-controlling interest (note 9)	32,900,282	33,495,557
	50,388,849	46,391,376
Unitholders' Equity		
Fund Units (notes 7)	138,772,764	139,708,519
Cumulative undistributed earnings (excess distributions)	(896,683)	997,240
Contributed surplus	45,763	-
	137,921,844	140,705,759
	188,310,693	187,097,135

Liquor Stores Income Fund

Consolidated Statements of Earnings, Comprehensive Income and Cumulative Undistributed Earnings (unaudited)

	Three month period ended	
	March 31, 2007 $	March 31, 2006 $
Sales	51,809,129	38,020,724
Cost of sales, operating, administrative, acquisition and store development	48,584,722	36,120,331
Operating earnings before amortization	3,224,407	1,900,393
Amortization		
Property and equipment	567,979	416,042
Intangible assets	37,952	29,487
Pre-opening costs	126,553	43,075
	732,484	488,604
Interest		
Interest expense on bank indebtedness	(108,425)	(195,019)
Interest expense on long-term debt	-	(115,381)
	(108,425)	(310,400)
Earnings before non-controlling interest	2,383,498	1,101,389
Non-controlling interest	(616,966)	(417,264)
Net earnings and comprehensive income for the period (note 2)	1,766,532	684,125
Cumulative undistributed earnings, beginning of period	997,240	336,539
Distributions declared (note 11)	(3,660,455)	(2,099,119)
Cumulative undistributed earnings, end of period	(896,683)	(1,078,455)
Basic earnings per unit (note 10)	0.17	0.10
Diluted earnings per unit (note 10)	0.17	0.10

Liquor Stores Income Fund

Consolidated Statements of Cash Flows (unaudited)

	Three month period ended	
	March 31, 2007	March 31, 2006
	$	$
Cash provided by (used in)		
Operating activities		
Net earnings for the period	1,766,532	684,125
Items not affecting cash		
Amortization	732,484	488,604
Other	2,400	(31,900)
Equity income	-	(6,856)
Non-controlling interest	616,966	417,264
Unit-based compensation	45,763	-
	3,164,145	1,551,237
Net change in non-cash working capital items	(717,256)	(514,340)
	2,446,889	1,036,897
Financing activities		
Net proceeds from the issuance of Units (note 7)	-	30,549,000
Units acquired (note 8)	(949,986)	-
Increase (decrease) in bank indebtedness	6,437,438	(15,492,652)
Proceeds of long-term debt	-	(11,352,466)
Repayment of long-term debt	-	-
Distributions paid to unitholders	(3,580,889)	(1,790,631)
Distributions paid to non-controlling interest	(1,155,920)	(1,156,445)
Dividends paid to non-controlling interest by subsidiaries	(14,866)	-
	735,777	756,806
Investing activities		
Business acquisitions (note 3(a))	(4,193,756)	-
Additional goodwill acquired (note 3(b))	(60,508)	-
Deposits on future acquisitions (note 4)	(100,000)	-
Purchase of property and equipment	(449,569)	(687,552)
Pre-opening costs	(60,851)	(194,190)
Repayment from (investment in) equity investee	-	(24,140)
	(4,864,684)	(905,882)
Increase (decrease) in cash and cash equivalents	(1,682,018)	887,821
Cash and cash equivalents balance, beginning of period	3,396,967	2,047,400
Cash and cash equivalents balance, end of period	1,714,949	2,935,221

Supplemental disclosure of cash flow information (note 12)

1 Nature of operations and organization

Liquor Stores Income Fund (the "Fund") is an unincorporated, open ended, limited purpose trust established under the laws of the Province of Alberta pursuant to a Declaration of Trust dated August 10, 2004.

As at March 31, 2007, the Fund operated 97 (March 31, 2006 – 71) retail liquor stores in Alberta and 8 (March 31, 2006 - 5) retail liquor stores in British Columbia. Of these stores, 94 (March 31, 2006 – 72) were acquired by the Fund and 11 (March 31, 2006 - 4) were developed by the Fund.

2 Significant accounting policies and basis of presentation

The accompanying unaudited interim consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles ("GAAP") for interim financial statements. The accounting principles and methods of computation adopted in these financial statements are the same as those of the audited financial statements for the year ended December 31, 2006. However, these interim consolidated financial statements do not include all information and footnote disclosures required under Canadian GAAP for annual financial statements. Accordingly, these unaudited consolidated interim financial statements should be read in conjunction with the audited financial statements and notes thereto, for the year ended December 31, 2006.

Effective January 1, 2007, the Fund has adopted Canadian Institute of Chartered Accountants ("CICA") Handbook sections 1530 – Comprehensive Income, 3855 – Financial Instruments – Recognition and Measurement, and 3865 – Hedges.

As the Fund has no items of other comprehensive income, net earnings for the period is equivalent to comprehensive income.

3 Business acquisitions

(a) Current period acquisition

During the quarter ended March 31, 2007, the Fund completed the acquisition of one retail liquor store business. The business acquisition has been accounted for using the purchase method, whereby the purchase consideration was allocated to the estimated fair values of the assets acquired and liabilities assumed at the effective date of the purchase. The purchase price allocation is preliminary and is subject to change once the final valuations of assets acquired are completed and the final determination of costs related to the acquisition has been made.

The purchase price allocated to the assets acquired and the liabilities assumed, based on their preliminary fair values, is as follows:

	$
Purchase price:	
Cash deposit paid in 2006	300,000
Cash paid in 2007	4,193,756
	4,493,756
Net assets acquired:	
Working capital	992,456
Property and equipment	526,898
Goodwill	2,974,402
	4,493,756

* Of the goodwill resulting from business acquisitions, $2,591,183 is deductible for tax purposes at 7% per year.

(b) Contingent consideration

For three agreements entered into in 2005 for the purchase of certain retail liquor stores, the Fund may be required to make contingent payments as follows: i) $100,000 each year for the next five years provided that certain sales thresholds are achieved; ii) 1% of gross sales of certain stores payable quarterly for the next five years to a cumulative maximum of $450,000; and iii) on March 15, 2008 and 2009, a payment equal to 50% times a multiple of earnings less payments to date .

Given the uncertainty with respect to the amount and timing of such payments, no amount was recorded with respect to this contingent consideration at the time of the respective acquisitions. The Fund will recognize additional consideration payable and goodwill when the outcome of these contingencies becomes determinable. During the period, additional goodwill of $60,508 was recorded relating to the payment of contingent consideration and the finalization of prior period purchase price allocations.

4 Deposits on future acquisitions

At March 31, 2007 the Fund had tendered deposits for five retail liquor stores in the amount of $1,432,621 (December 31, 2006 – 1,632,621). In addition, deposits for inventory and working capital in the amount of $962,857 were included in prepaid expenses and deposits at March 31, 2007 (December 31, 2006 - $306,252). During the period ended March 31, 2007 the Fund drew down the future business acquisitions deposits by $300,000 through the purchase of one retail liquor store, and tendered additional deposits totalling $100,000.

5 Bank indebtedness and long-term debt

Bank indebtedness

The Fund has an available $32 million operating line, with a seasonal bulge to $38 million between October 1 and February 28. Interest on bank indebtedness is payable at the lender's prime rate. As at March 31, 2007, the bank indebtedness rate of interest was 6% (December 31, 2006 – 6.0%) and $12,963,535 (December 31, 2006 - $7,532,285) was drawn on the operating line, offset by outstanding cheques and deposits of $1,070,683 (December 31, 2006 - $2,076,871).

Long-term debt

Interest on long-term debt is payable at the lender's prime rate plus 0.25%. As of March 31, 2007 the effective long-term debt rate of interest was 6.25% (December 31, 2006 – 6.25%). There was no long-term debt outstanding at March 31, 2007.

The Fund has an available $30.8 million credit facility consisting of a $14.5 million committed non-revolving loan to be used in financing capital assets of the Fund, a $15 million committed non-revolving loan to assist in financing the acquisition and development of liquor stores, a $0.65 million demand loan to cover electronic funds transfer payments, and a $0.65 million demand non-revolving loan to be used in financing motor vehicle and other asset acquisitions.

The bank indebtedness and long-term debt are collateralized by a general security agreement covering all present and after acquired personal property of Liquor Stores LP, a subsidiary of the Fund, and also by a floating charge over all of Liquor Stores LP's present and after acquired real property and an assignment of Liquor Stores LP's insurance. The assets of Liquor Stores LP represent substantially all of the Fund's assets.

6 Related party transactions

A director of a subsidiary of the Fund is a partner in a law firm to which, during the three month period ended March 31, 2007, the Fund incurred professional fees of $89,417. Rent paid to companies controlled by directors of a subsidiary of the Fund amounted to $21,034. One such arrangement was terminated effective April 1, 2007. Further, the Fund paid fees and expenses to a company controlled by the Chief Executive Officer of the Fund, relating to the supervision of construction of developed stores and lease administration, in the amount $10,674. Subsequent to March 31, 2007 this arrangement has ended. The Fund has entered into a lease for new office premises with a company controlled by the Chief Executive Officer. The Fund has received independent fairness and legal opinions concerning the terms of the lease. Rent payments for this lease are scheduled to begin June 1, 2007. These operating and administrative expenses are incurred in the normal course of business at terms similar with unrelated parties and are measured at the exchange amount. Included in accounts payable and accrued liabilities is $6,469 (December 31, 2006 - $4,307) relating to these transactions.

7 Unitholders' equity

Fund Units

Units outstanding and capital contributions are as follows:

	Number of units #	Issue costs $	Net capital contributions $
Balance – December 31, 2006	10,228,320	10,271,305	139,708,519
Issued for Exchangeable LP Units	1,425	-	14,231
Units issued on March 9, 2007	2,492	-	50,014
Treasury Units	(46,543)		(1,000,000)
Balance – March 31,2007	10,185,694	10,271,305	138,772,764

An unlimited number of Fund Units may be created and issued pursuant to the Declaration of Trust. Each Fund Unit is transferable and represents an equal undivided beneficial interest in any distributions from the Fund, whether of net income, net realized capital gains or other amounts and in the net assets of the Fund in the event of a termination or winding up of the Fund. All Fund Units entitle the holder thereof to one vote and each Fund Unit has equal voting rights and privileges.

Consideration for units issued on exchange of Liquor Stores LP Exchangeable LP Units during the three months ended March 31, 2007 was recorded at the carrying amount of the Liquor Stores LP Exchangeable LP Units in accordance with EIC-151.

Treasury Units represent unvested Units held in the LTIP (note 8(a)) and the 2007 Incentive Plan (note 8(c)).

8 Unit-based compensation plans

a) Long term incentive plan

The Fund has adopted a long-term incentive plan (the "Plan") to provide key senior management of the Fund with compensation opportunities that will enhance the ability of the Fund to attract, retain and motivate key personnel and reward these key employees for significant performance and associated per unit cash flow growth. Fund bonuses, in the form of Units of the Fund, will be provided to eligible employees on an annual basis where the distributable cash of the Fund exceeds certain specified threshold amounts. The monthly cash distributions received by the Plan will be remitted to the participant when the Units become vested.

The Plan is managed through a separate trust, which is considered a variable interest entity. As the Fund is the primary beneficiary, the Fund consolidates the Plan in its financial statements.

If the distributable cash flow per unit exceeds the base distribution, a percentage of the distributable cash (the participation rate) is contributed by the Fund into a separate trust (the "LTIP Trust"). The LTIP Trust will use the funds to purchase Units in the open market or from treasury, and such Units will vest to the eligible employees over a three-year period. Threshold amounts and participation rates are as follows:

Excess percentage	Participation rate
5% or less	Nil
Greater than 5% and up to 10%	10% of any excess over 5%
Greater than 10% and up to 20%	10% of any excess over 5%, plus 20% of any excess over 10%
Greater than 20%	10% of any excess over 5%, plus 20% of any excess over 10%, plus 25% of any excess over 20%

The following table summarizes the status of the Plan:

	For the quarter ended March 31, 2007 #	For the quarter ended March 31, 2006 #
Unvested Units, beginning of period	492	-
Granted	2,492	-
Vested Units transferred to participants	(292)	-
Unvested Units, end of period	2,692	-

On March 9, 2007, 2,492 Units were granted and issued from treasury at a price of $20.07 per Unit for a total cost of $50,014. The compensation expense will be recognized over the vesting period of three years. Compensation expense of $2,288 was recorded for the three months ended March 31, 2007 (March 31, 2006 - $ nil).

b) Trustee and director deferred unit plan

The Fund maintains a deferred share unit plan (the "DSU Plan") to enhance the ability of the Fund to attract and retain non-employee Trustees and Directors whose training, experience and ability will promote the interests of the Fund and to align the interests of such non-employee Trustees and Directors with the interests of Unitholders. The DSU Plan is designed to permit such non-employee Trustees and Directors to defer the receipt of a maximum of 50% of the cash compensation otherwise payable to them for services to the Fund. As the Fund intends to settle its obligations related to the DSU Plan through cash payments, these obligations are accrued as a liability, which is adjusted to fair value based on the current market value of Units at each balance sheet date. Awards accruing to DSU Plan participants in the quarter ended March 31, 2007 totalled $58,634 (2006 - $ nil), which were recorded as compensation expense in the period. As at March 31, 2007 participants have accumulated an entitlement to the equivalent cash value of 7,174 Units under the DSU Plan (December 31, 2006 – 5,183).

c) 2007 Incentive Plan

A special one-time discretionary compensation plan (the "2007 Plan") was implemented in the first quarter of 2007 in order to retain and motivate key personnel and reward these key employees for significant performance and associated per unit cash flow growth. Fund bonuses, in the form of Units of the Fund, will be provided to eligible employees. The Units will vest over a three-year period from the March 7, 2007 grant date to January 7, 2010. The monthly cash distributions received by the 2007 Plan will be remitted to the participant when the Units become vested.

The following table summarizes the status of the 2007 Plan:

	For the quarter ended March 31, 2007 #	**For the quarter ended March 31, 2006** #
Unvested Units, beginning of period	-	-
Granted	43,851	-
Vested Units transferred to participants	-	-
Unvested Units, end of period	43,851	-

$950,000 was granted effective March 7, 2007 to purchase Units under the 2007 Plan. In total, 43,851 Units were purchased in the open market at an average price of $21.66 per Unit. The $950,000 compensation expense will be recognized over the vesting period of three years. Compensation expense of $43,475 was recorded for the three months ended March 31, 2007 (March 31, 2006 - $ nil).

9 Non-controlling interest

Exchangeable and Subordinated Unitholders

	Liquor Stores LP Exchangeable LP Units	Liquor Stores LP Subordinated LP Units	Total
	#	#	#
Liquor Stores Limited Partnership			
Balance – December 31, 2005	2,025,317	2,125,000	4,150,317
Exchanged for Fund units	(848,637)	-	(848,637)
Balance – December 31, 2006	1,176,680	2,125,000	3,301,680
Exchanged for Fund units	(1,425)	-	(1,425)
Balance – March 31, 2007	1,175,255	2,125,000	3,300,255
Fund Special Voting Units – March 31, 2007	1,175,255	2,125,000	3,300,255
	$	$	$
Balance – December 31, 2005	20,351,876	21,348,354	41,700,230
Earnings	1,561,740	2,776,427	4,338,167
Units exchanged for Fund Units	(8,390,994)	-	(8,390,994)
Distributions declared	(1,642,824)	(2,656,463)	(4,299,287)
Balance – December 31, 2006	11,879,798	21,468,318	33,348,116
Earnings	209,751	379,437	589,188
Exchanged for Fund Units	(14,231)	-	(14,231)
Distributions declared (note 11)	(421,543)	(761,600)	(1,183,145)
Balance – March 31, 2007	11,653,775	21,086,155	32,739,930
Subsidiaries			
Balance – December 31, 2005			-
Acquisitions during the period			70,992
Earnings			124,467
Dividends paid			(48,018)
Balance - December 31, 2006			147,441
Earnings			27,778
Dividends paid			(14,867)
Balance – March 31, 2007			160,352
Total			**32,900,282**

10 Earnings per Unit

	March 31, 2007 (3 months) $	March 31, 2006 (3 months) $
Net Earnings (numerator utilized in basic Earnings per Unit)	1,766,532	684,125
Non-controlling interest	589,188	417,264
Earnings (numerator utilized in diluted Earnings per Unit)	2,355,720	1,101,389
	#	#
Units outstanding, beginning of period	10,228,320	6,179,683
Weighted average of Units issued less treasury Units acquired	(4,720)	436,497
Denominator utilized in basic earnings per unit	10,223,600	6,616,180
Exchangeable and Subordinated Units	3,301,440	3,998,265
Denominator utilized in diluted earnings per unit	13,525,040	10,614,445
	$	$
Earnings per Unit - Basic	$0.17	$0.10
Earnings per Unit - Diluted	$0.17	$0.10

11 Distributions

Distributions are determined in accordance with the Trust Indenture, and are based on earnings, before amortization, but reduced by capital expenditures. Distributions totalling $0.3584 (2006 - $0.30) per Unit for each of Fund Units, Exchangeable LP Units and Subordinated LP Units were declared by the Fund for the three months ended March 31, 2007.

		Fund Units		Exchangeable LP Units and Subordinated LP Units		Total	
Date distribution declared	Date distribution paid	Declared $	Paid $	Declared $	Paid $	Declared $	Paid $
January 15, 2007	February 15, 2007	1,193,622	1,193,622	137,319	137,319	1,330,941	1,330,941
February 15, 2007	March 15, 2007	1,193,622	1,193,622	137,319	137,319	1,330,941	1,330,941
March 15, 2007	April 13,2007	1,273,211		908,507		2,181,718	
		3,660,455	2,387,244	1,183,145	274,638	4,843,600	2,661,882

At March 31, 2007, distributions payable to unitholders was $1,273,211 (December 31, 2006 – $1,193,645) and distributions payable to non-controlling interest was $908,507 (December 31, 2006 - $881,282). Distributions outstanding as at March 31, 2007 were paid in April 2007.

12 Supplemental disclosure of cash flow information

	For the quarter ended March 31, 2007 $	For the quarter ended March 31, 2006 $
Interest paid	108,425	310,400
Income taxes paid	278	-

13 Segmented information

The Fund identifies operating segments based on business activities, management responsibility, and geography. The Fund operates within a single operating segment, being the operation of retail liquor stores in Canada. All of the Fund's assets are located in Canada.

14 Seasonal nature of the business

The Fund's results for the first quarter of 2007 are not necessarily indicative of the results that may be expected for the full year due to seasonal variations in sales levels. The Fund historically experiences higher sales in the third and fourth quarters, while the first and second quarter typically experience lower sales levels due to seasonal shopping patterns. Occupancy related expenses, operating and administrative expense, amortization and interest expense remain relatively steady throughout the year.

15 Subsequent events

On April 10, 2007 the Fund made an offer to acquire all of the outstanding trust units of Liquor Barn Income Fund ("Liquor Barn"). The Fund is offering 0.53 of a trust unit of the Fund for each trust unit of Liquor Barn. There are approximately 14 million Liquor Barn trust units outstanding. This transaction values the outstanding Liquor Barn units at approximately $158 million. Liquor Barn unitholders have until May 17, 2007 to accept the offer unless extended or withdrawn.

On April 30, 2007 the Fund acquired a 50% interest in a retail liquor store in British Columbia. The purchase price on the acquisition will be allocated to the fair value of the acquired assets when determined. The acquisition will not have a material impact on the assets, liabilities or future operations of the Fund.