Liquor Stores Income Fund

Interim Consolidated Financial Statements
(unaudited)

March 31, 2010
(expressed in thousands of Canadian dollars)

Liquor Stores Income Fund

Consolidated Balance Sheets

(**expressed in thousands of Canadian dollars)**

	March 31, 2010	December 31, 2009 (restated – note 2)
Assets		
Current assets		
Cash and cash equivalents	$ 1,236	$ 5,288
Accounts receivable	1,089	1,846
Inventory (at cost)	113,471	122,571
Prepaid expenses and deposits (note 4)	1,810	2,031
	117,606	131,736
Deposits on future acquisitions (note 4)	20	-
Property and equipment	45,864	47,013
Intangible assets (note 5)	47,372	47,963
Goodwill	282,545	283,097
	$ 493,407	$ 509,809
Liabilities		
Current liabilities		
Bank indebtedness	$ 40,430	$ 41,094
Accounts payable and accrued liabilities	20,046	24,554
Distributions payable to unitholders (note 6)	2,501	2,493
Distributions payable to non-controlling interest (note 6)	542	547
	63,519	68,688
Long-term debt	100,022	100,126
Future income tax liability (note 7)	9,350	9,254
	172,891	178,068
Unitholders' Equity		
Equity attributable to Unitholders (note 8 (a))	277,496	286,165
Non-controlling interest (note 8 (b))	43,020	45,576
	320,516	331,741
	$ 493,407	$ 509,809

Liquor Stores Income Fund

Consolidated Statements of Earnings and Comprehensive (Loss) Income

(**expressed in thousands of Canadian dollars**)

	Three months ended March 31, 2010	March 31, 2009 (restated – note 2)
Sales	$ 115,798	$ 106,352
Cost of sales	87,688	79,649
Gross margin	28,110	26,703
Operating and administrative expense	24,012	21,850
Operating earnings before amortization, interest and other	4,098	4,853
Amortization		
Property and equipment	1,797	1,515
Intangible assets	641	759
	2,438	2,274
	1,660	2,579
Interest expense and other		
Bank indebtedness	458	265
Long-term debt	438	258
Convertible debentures	1,328	1,294
Gain on foreign exchange	(697)	(90)
	1,527	1,727
Earning before income tax	133	852
Future income tax expense (recovery)	79	(803)
Net earnings for the period	54	1,655
Other comprehensive (loss) gain		
Net (loss) gain on translation of self-sustaining foreign operations	(1,861)	1,067
Comprehensive (loss) income for the period	$ (1,807)	$ 2,722
Net (loss) earnings attributable to:		
Unitholders of the Fund	$ (5)	$ 1,486
Non-controlling interest	59	169
	$ 54	$ 1,655
Comprehensive (loss) income attributable to:		
Unitholders of the Fund	$ (1,535)	$ 2,553
Non-controlling interest	(272)	169
	$ (1,807)	$ 2,772
Earnings per Unit (note 9)		
Basic	$ 0.00	$ 0.08
Diluted	$ 0.00	$ 0.07

Liquor Stores Income Fund

Consolidated Statements of Changes in Unitholders' Equity

(**expressed in thousands of Canadian dollars**)

	Attributable to Unitholders of the Fund							
	Fund Units	**Equity component of convertible debentures**	**Contributed surplus**	**Accumulated other comprehensive income**	**Cumulative undistributed earnings (excess distributions)**	**Total**	**Non-controlling interest**	**Total Unitholders' equity**
Opening balance – January 1, 2009	$ 309,638	$ 4,970	$ 1,156	$ 1,404	$ (22,523)	$ 294,645	$ 48,013	$ 342,658
Units issued for exchangeable units	74	-	-	-	-	74	(74)	-
Vested long-term incentive plan units	674	-	(674)	-	-	-	-	-
Forfeited long-term incentive plan units	68	-	-	-	-	68	-	68
Cash distributions on vested units	(40)	-	-	-	-	(40)	-	(40)
Unit-based compensation expense	-	-	73	-	-	73	-	73
Foreign currency translation adjustment	-	-	-	1,067	-	1,067	-	1,067
Net earnings for the period	-	-	-	-	1,486	1,486	169	1,655
Exchangeable LP Unit conversion	-	-	-	-	-	-	(5)	(5)
Distributions declared	-	-	-	-	(7,450)	(7,450)	(1,667)	(9,117)
Dividends declared	-	-	-	-	-	-	(183)	(183)
Balance – March 31, 2009	$ 310,414	$ 4,970	$ 555	$ 2,471	$ (28,487)	$ 289,923	$ 46,253	$ 336,176
Opening balance – January 1, 2010	$ 311,044	$ 4,970	$ 857	$ (2,025)	$ (28,681)	$ 286,165	$ 45,576	$ 331,741
Units issued for exchangeable units	464	-	-	-	-	464	(464)	-
Vested long-term incentive plan units	635	-	(635)	-	-	-	-	-
Cash distributions on vested units	(112)	-	-	-	-	(112)	-	(112)
Unit-based compensation expense (note 10)	-	-	27	-	-	27	-	27
Foreign currency translation adjustment	-	-	-	(1,530)	-	(1,530)	(331)	(1,861)
Exchangeable LP Unit conversion	-	-	-	-	(12)	(12)	-	(12)
Net (loss) earnings for the period	-	-	-	-	(5)	(5)	59	54
Distributions declared (note 6)	-	-	-	-	(7,501)	(7,501)	(1,628)	(9,129)
Dividends declared	-	-	-	-	-	-	(192)	(192)
Balance – March 31, 2010	$ 312,031	$ 4,970	$ 249	$ (3,555)	$ (36,199)	$ 277,496	$ 43,020	$ 320,516

Liquor Stores Income Fund

Consolidated Statements of Cash Flows

(**expressed in thousands of Canadian dollars**)

	Three months ended March 31, 2010	March 31, 2009 (restated – note 2)
Cash provided by (used in)		
Operating activities		
Net earnings for the period	$ 54	$ 1,655
Items not affecting cash		
Amortization	2,438	2,274
Amortization of inventory fair value adjustment	-	155
Amortization of financing charges	108	-
Non-cash interest on convertible debentures	348	314
Future income tax expense (recovery)	79	(803)
Unrealized gain on foreign currency	(817)	-
Unit-based compensation (note 10 (a))	27	191
Loss on sale of forfeited incentive plan units	-	30
	2,237	3,816
Net change in non-cash working capital items (note 12)	4,560	11,490
	6,797	15,306
Financing activities		
Decrease in bank indebtedness	(342)	(7,012)
Distributions paid to unitholders (note 6)	(7,493)	(7,444)
Distributions paid to non-controlling interest (note 6)	(1,633)	(1,669)
Dividends paid to non-controlling interest by subsidiaries	(192)	(183)
Net distributions and proceeds on long-term incentive plan units	(112)	(3)
	(9,772)	(16,311)
Investing activities		
Business acquisitions, including contingent consideration paid (note 3)	(200)	(135)
Net deposits on future acquisitions	(20)	10
Purchase of property and equipment	(355)	(339)
Purchase of intangible assets (note 5)	(450)	-
	(1,025)	(464)
Foreign exchange (loss) gain on cash held in foreign currency	(52)	78
Decrease in cash and cash equivalents	(4,052)	(1,391)
Cash and cash equivalents balance, beginning of period	5,288	3,530
Cash and cash equivalents balance, end of period	$ 1,236	$ 2,139

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, 2010, the Fund operated 236 retail liquor stores, of which 173 (2009 – 169) were in Alberta, 35 (2009 - 35) were in British Columbia, 20 (2009 – 19) were in Alaska and eight (2009 – nil) were in Kentucky. Of the stores operated, 204 (2009 – 196) were acquired by the Fund and 32 (2009 - 27) 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, 2009, except as noted below. 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, 2009.

Adoption of new accounting standards

Business combinations

Effective January 1, 2010, the Fund adopted CICA Handbook Section 1582, *Business Combinations*, which replaces Section 1581. This new standard aligns accounting for business combinations under Canadian GAAP and International Financial Reporting Standards (“IFRS”). The standard requires assets and liabilities acquired in a business combination to be measured at fair value at the acquisition date. The standard also requires acquisition-related costs, such as advisory or legal fees, incurred to effect a business combination to be expensed in the period in which they are incurred. The adoption of this standard will impact the accounting treatment of future business combinations. This standard was applied prospectively as required by the transitional provisions of the standard and past business combinations have not been restated.

Consolidated Financial Statements and Non-controlling Interests

Effective January 1, 2010, the Fund adopted CICA Handbook Sections 1601, *Consolidated Financial Statements* and 1602, *Non-controlling Interests*, which together replace the former consolidated financial statements standard. Section 1602 introduces the following changes:

- In the consolidated balance sheets and consolidated statements of unitholders’ equity, non-controlling interest is now presented as a separate component of unitholders’ equity, rather than as a liability;
- Non-controlling interest is no longer recorded as a deduction from net earnings;
- Net earnings and other comprehensive income are attributed to the Unitholders of the Fund and non-controlling interest based on their respective ownership interests.

The Fund elected to early adopt these standards effective January 1, 2010 in order to more closely align its accounting treatment of those items with IFRS at the changeover date. Theses standards have been applied prospectively, except for the presentation requirements for non-controlling interest, which were applied retrospectively as required by the transitional provisions of the standards.

3 Business acquisitions

During the three month period ended March 31, 2010, there were adjustments to goodwill for $200,000 (2009 - $135,125) for contingent payments relating to prior year acquisitions.

4 Deposits on future acquisitions

Deposits represent refundable and non-refundable amounts paid for the acquisition of retail liquor stores where the purchase transaction is incomplete at the balance sheet date. Deposits for the acquisition of inventory and working capital are included in prepaid expenses and deposits.

Current year activity is as follows:

(expressed in thousands of Canadian dollars)	Non-current Deposits	Current Deposits
Balance – December 31, 2009	$ -	$ 234
Deposits tendered	20	-
Holdbacks released	-	(2)
Balance – March 31, 2010	$ 20	$ 232

5 Intangible assets

During the three month period ended March 31, 2010, the Fund acquired two liquor licenses for $450,000 (2009 – nil) related to existing stores. The original licenses purchased had finite lives. The incremental payments made during the three month period ended March 31, 2010 will extend the lives of the liquor licenses indefinitely.

6 Distributions

Distributions are determined in accordance with the Trust Indenture, and are based on earnings, before amortization and adjusted by capital expenditures. Distributions totalling $0.405 (2009 - $0.405) per Unit for each of Fund Units, Liquor Stores Exchangeable LP Units and Series 1 Exchangeable LP Units were declared by the Fund for the period ended March 31, 2010.

(expressed in thousands of Canadian dollars)		Fund Units		Liquor Stores Exchangeable LP Units		Liquor Stores Series 1 Exchangeable LP		Total	
Date distribution declared	**Date distribution paid**	**Declared**	**Paid**	**Declared**	**Paid**	**Declared**	**Paid**	**Declared**	**Paid**
Jan 15, 2010	Feb 15, 2010	$ 2,500	$ 2,500	$ 432	$ 432	$ 111	$ 111	$ 3,043	$ 3,043
Feb 15, 2010	Mar 15, 2010	2,500	2,500	432	432	111	111	3,043	3,043
Mar 15, 2010	Apr 15, 2010	2,501	-	431	-	111	-	3,043	-
		$ 7,501	$ 5,000	$ 1,295	$ 864	$ 333	$ 222	$ 9,129	$ 6,086

7 Future income taxes

Prior to June 12, 2007, the Fund provided for current and future income taxes only for its incorporated subsidiaries. On June 22, 2007, Bill C-52, including provisions related to the taxation of income trusts commencing January 1, 2011 (or sooner in certain circumstances), received Royal Assent. As a consequence, Canadian income trusts are required to provide for future income taxes arising from those temporary tax differences expected to reverse after January 1, 2011. The substantively enacted tax rates for 2011 and 2012 are 26.5% and 25.0% respectively.

Determining future income taxes involves a number of assumptions and variables that could reasonably change in the period to January 1, 2011, including: the useful lives of recorded property and equipment and intangible assets that determine the amount of amortization recorded thereon; the amount of discretionary tax deductions the Fund will claim from its existing tax depreciation pools, the rates of tax applicable to various jurisdictions in which the Fund is taxable and the allocation of taxable income to those jurisdictions; and the acceptance of the Fund's tax filing positions by the taxation authorities. Changes in these assumptions and variables, which are re-evaluated at each balance sheet date, could result in changes in the recorded amount of future income taxes, and these changes could be material.

Future income tax assets and liabilities are recognized based on temporary differences between accounting and tax bases of existing assets and liabilities as follows:

(expressed in thousands of Canadian dollars)	**March 31, 2010**	**December 31, 2009**
Future income tax liabilities:		
Intangible assets	$ 5,863	$ 5,806
Property and equipment	2,248	2,081
Goodwill	3,673	3,263
	11,784	11,150
Future income tax assets:		
Issue and financing costs	678	696
Deferred lease inducements	563	237
Long term incentive plans	192	67
Non-capital losses	1,001	896
	2,434	1,896
	$ 9,350	$ 9,254

The above includes a net future income tax asset recorded by wholly-owned US subsidiaries of $126,073 (2009 – $184,979).

Future income taxes of $2,027,052 attributable to the Fund’s exchangeable interests are not recorded. During the period ended March 31, 2010, 23,333 (2009 – 8,263) units were exchanged resulting in an increase to future income taxes of $11,686 (2009 – $4,557).

The Fund has recognized future income taxes related to non-capital losses of $3,243,211 (2009 - $2,748,407) available in subsidiaries to offset income of future years. Realization of the non-capital losses is considered to be more likely than not. If not utilized, $475,435 will expire in 2028, $2,064,077 will expire in 2029 and $703,699 will expire in 2030.

Future income taxes are not recorded on $103,745,778 of non tax-deductible goodwill.

8 Unitholders' equity

(a) Equity attributable to Unitholders

Units outstanding are as follows:

	Number of units
Balance – December 31, 2009	# 18,470,448
Issued for Exchangeable Units	23,333
Vested Units (note 10 (a))	29,403
Balance – March 31, 2010	# 18,523,184

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 Exchangeable LP Units and Series 1 Exchangeable LP Units during the period ended March 31, 2010 was recorded at the carrying amount of the Liquor Stores Exchangeable LP Units and Series 1 Exchangeable LP Units.

(b) Non-controlling interest

Units outstanding are as follows:

	Liquor Stores Exchangeable LP Units	Series 1 Exchangeable LP Units	Total
Balance – December 31, 2009	# 3,196,842	# 845,409	# 4,042,251
Exchanged for Fund Units	-	(22,333)	(23,333)
Balance – March 31, 2010	# 3,196,842	# 822,076	# 4,018,918

Liquor Stores LP Exchangeable LP Units ("Exchangeable LP Units") and Liquor Stores LP Series 1 Exchangeable LP Units ("Series 1 Exchangeable LP Units")

The Exchangeable LP Units and Series 1 Exchangeable LP Units issued by Liquor Stores LP have economic and voting rights equivalent to the Fund Units, except in connection with the exchangeability terms as described below. They are exchangeable, directly or indirectly, on a one-for-one basis for Fund Units at the option of the holder, under the terms of the Exchange Agreement. The Exchangeable LP Units are not required to be exchanged for Fund Units before transferring to third parties. Exchangeable LP Units and Series 1 Exchangeable Units have been treated as non-controlling interest.

Each Exchangeable LP Unit and Series 1 Exchangeable LP Unit entitles the holder to receive distributions pro-rata with distributions made on Fund Units.

9 Earnings per Unit

(expressed in thousands of Canadian dollars, except per unit amounts)	Three months ended March 31, 2010	March 31, 2009
Net (loss) earnings attributable to Unitholders of the Fund (numerator utilized in basic Earnings per Unit)	$ (5)	$ 1,486
Net earnings attributable to non-controlling interest	-	153
Net (loss) earnings (numerator utilized in diluted Earnings per Unit)	$ (5)	$ 1,639
Units outstanding, beginning of period	# 18,470,447	# 18,356,996
Weighted average of Units issued less treasury Units acquired	45,092	34,719
Denominator utilized in basic earnings per unit	# 18,515,539	# 18,391,715
Exchangeable units	-	4,117,641
Potential units under unit-based compensation plans (note 10 (a))	-	2,314
Denominator utilized in diluted earnings per unit	# 18,515,539	# 22,511,670
Earnings per Unit – Basic	$ 0.00	$ 0.08
Earnings per Unit – Diluted	$ 0.00	$ 0.07

Due to their anti-dilutive effect, 2010 and 2009 potential units for convertible debentures, 2010 exchangeable units and the net earnings attributable to those units, and 2010 potential units under unit-based compensation plans have been excluded from the diluted earnings per unit calculation.

10 Unit-based compensation plans

(a) Long-term incentive plan ("LTIP") and 2007 Incentive Plan ("2007 Plan")

The following table summarizes the status of the Plans:

	LTIP	2007 Plan	Total
Unvested Units – December 31, 2009	# 31,038	# 13,232	# 44,270
Vested Units transferred to participants	(16,171)	(13,232)	(29,403)
Unvested Units – March 31, 2010	# 14,867	# -	# 14,867

Compensation expense for the LTIP was $25,271 (2009 - $76,738) and for the 2007 Incentive Plan was $1,292 (2009 - $26,541) for the period ended March 31, 2010.

(b) Trustee and director deferred unit plan ("DSU Plan")

The following table summarizes the status of the Plan:

	Total
Unvested Units – December 31, 2009	# 39,180
Vested Units (settled in cash)	(6,802)
Awards	3,314
Unvested Units – March 31, 2010	# 35,692

Awards accruing to DSU Plan participants for the period ended March 31, 2010 totalled $112,486 (2009 – $118,054), which was recorded as compensation expense.

11 Related party transactions

The Fund paid fees and incurred expenses to a law firm for legal services of $65,104 (2009 - $65,761) where a director of a subsidiary company of the Fund is a partner. Rent paid to companies controlled by the Executive Chairman of the Fund amounted to $133,938 (2009 - $152,384). 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. There was $36,865 included in accounts payable and accrued liabilities (December 31, 2009 - $17,294) relating to these transactions.

12 Supplemental disclosure of cash flow information

Changes in non-cash working capital items:

(expressed in thousands of Canadian dollars)	**2010**	**2009**
Accounts receivable	$ 752	$ 1,091
Inventory	8,240	14,424
Prepaid expenses and deposits	205	204
Accounts payable and accrued liabilities	(4,637)	(4,229)
	$ 4,560	$ 11,490

	Three months ended	
(expressed in thousands of Canadian dollars)	**March 31, 2010**	**March 31, 2009**
Interest paid	$ 787	$ 527
Income taxes paid	43	4

13 Segmented information

The Fund's reportable segments are Canadian Operations and US Operations. Segmentation is based on differences in the regulatory environments of Canada and the US and reflects the basis on which management measures performance and makes decisions regarding the allocation of resources. Both segments operate retail liquor stores in their respective jurisdictions. The following segmented information is regularly reported to the Fund's President and Chief Executive Officer (the Fund's chief operating decision maker).

(expressed in thousands of Canadian dollars)				**March 31, 2010**
	Canadian	**US**	**Intersegment Eliminations**	**Consolidated**
Sales to external customers	$ 86,388	$ 29,410	$ -	$ 115,798
Intersegment revenue [(i)]	938	-	(938)	-
	$ 87,326	$ 29,410	$ (938)	$ 115,798
Operating margin before amortization, interest and other	$ 3,984	$ 114	$ -	$ 4,098
Property & equipment amortization	$ 1,636	$ 161	$ -	$ 1,797
Intangible asset amortization	608	33	-	641
Interest income [(i)]	(676)	-	676	-
Interest expense	2,188	712	(676)	2,224
Gain on foreign exchange	(697)	-	-	(697)
Earnings (loss) before income tax and non-controlling interest	$ 925	$ (792)	$ -	$ 133
Future income tax expense	13	66	-	79
Net earnings (loss)	$ 912	$ (858)	$ -	$ 54
Other information				
Expenditures for additions to:				
Property and equipment	$ 314	$ 41	$ -	$ 355
Goodwill	200	-	-	200
Total assets	429,261	64,146	-	493,407

(i) Intersegment revenue consists of management fees charged by Canadian Operations to US subsidiaries for the provision of management services. Intercompany interest charged by Canadian Operations to US subsidiaries is related to financing arrangements. These charges are in the normal course of business and are recorded at the exchange amounts established by transfer pricing agreements, which reflect market rates.

Liquor Stores Income Fund

Notes to Consolidated Financial Statements
March 31, 2010

(expressed in thousands of Canadian dollars)				March 31, 2009
	Canadian	US	Intersegment Eliminations	Consolidated
Sales to external customers	$ 88,003	$ 18,349	$ -	$ 106,352
Intersegment revenue (i)	371	-	(371)	-
	$ 88,374	$ 18,349	$ (371)	$ 106,352
Operating margin before amortization, interest and other	$ 4,683	$ 170	$ -	$ 4,853
Property & equipment amortization	$ 1,408	$ 107	$ -	$ 1,515
Intangible assets amortization	754	5	-	759
Interest income (i)	(417)	-	417	-
Interest expense	1,807	427	(417)	1,817
Gain on foreign exchange	(90)	-	-	(90)
Earnings (loss) before income tax and non-controlling interest	$ 1,221	$ (369)	$ -	$ 852
Future income tax recovery	(765)	(38)	-	(803)
Net earnings (loss)	$ 1,986	$ (331)	$ -	$ 1,655
Other information				
Expenditures for additions to:				
Property and equipment	$ 143	$ 196	$ -	$ 339
Goodwill	100	35	-	135
Total assets – December 31, 2009	443,274	66,535	-	509,809

(i) Intersegment revenue consists of management fees charged by Canadian Operations to US subsidiaries for the provision of management services. Intercompany interest charged by Canadian Operations to US subsidiaries is related to financing arrangements. These charges are in the normal course of business and are recorded at the exchange amounts established by transfer pricing agreements, which reflect market rates.

14 Economic dependence

Under Alberta provincial legislation the Fund is required to purchase liquor and related products sold in Alberta from the Alberta Gaming and Liquor Commission. As the Fund's income in Alberta is derived entirely from the sale of liquor and related products, its ability to continue viable operations is largely dependent upon maintaining its relationship with this main supplier.

The Fund is dependent on Connect Logistics Services Inc. and Brewers Distributor Ltd. in Alberta and the Liquor Distribution Branch in British Columbia for the majority of its products. Any significant disruption in the operations of these organizations resulting in interruption in supply would have a material adverse effect on liquor store operations including the operations of the Fund.

15 Seasonal nature of the business

The Fund historically experiences higher sales in the third and fourth quarters, while the first and second quarters typically experience lower sales levels due to seasonal shopping patterns. Occupancy related expenses, operating and administrative expense and amortization remain relatively steady throughout the year.