



**CANADIAN PREMIUM SELECT INCOME FUND**

**Annual Financial Statements**

**December 31, 2011**

# Canadian Premium Select Income Fund

## MANAGEMENT RESPONSIBILITY FOR FINANCIAL REPORTING

The accompanying financial statements have been prepared by Harvest Portfolios Group Inc. in its capacity as Manager of the Fund and approved by the Board of Directors of the Manager. The Fund's Manager is responsible for the information and representation contained in these financial statements.

The Manager maintains appropriate processes to ensure that relevant and reliable financial information is produced. The financial statements have been prepared in accordance with Canadian generally accepted accounting principles and include certain amounts that are based on estimates and judgments made by the Manager. The significant accounting policies, which the Manager believes are appropriate, are described in Note 2 to the financial statements.

PricewaterhouseCoopers LLP are the external auditors of the Fund. They have audited the financial statements in accordance with Canadian generally accepted auditing standards to enable them to express to the unitholders their opinion on the financial statements. Their report is set out below.

On behalf of Harvest Portfolios Group Inc.,

*(Signed)* "Michael Kovacs"  
President and Chief Executive Officer

*(Signed)* "B. Mark Riden CA"  
Chief Financial Officer

Oakville, Canada  
March 2012



March 19, 2012

## **Independent Auditor's Report**

**To the Unitholders of  
Canadian Premium Select Income Fund (the Fund)**

We have audited the accompanying financial statements of the Fund, which comprise the statements of investments and financial position as at December 31, 2011 and the statements of operations, changes in financial position, and cash flows for the period from November 17, 2011 (commencement of operations) to December 31, 2011, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

### **Management's responsibility for the financial statements**

Management is responsible for the preparation and fair presentation of the 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 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 the financial statements based on our audit. We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform an audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the 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 financial statements.

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

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**Opinion**

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Fund as at December 31, 2011 and the results of its operations, the changes in its financial position, and cash flows for the period from November 17, 2011 (commencement of operations) to December 31, 2011 in accordance with Canadian generally accepted accounting principles.

*(Signed)* "PricewaterhouseCoopers LLP"

Chartered Accountants, Licensed Public Accountants

# Canadian Premium Select Income Fund

## STATEMENT OF FINANCIAL POSITION

<b>As at December 31,</b>	<b>2011</b>
<b>Assets</b>	
Investments, at fair value (cost \$23,712,122)	\$ 24,399,458
Cash and cash equivalents	300,759
Dividends and interest receivable	104,447
	<u>\$ 24,804,664</u>
<b>Liabilities</b>	
Redemptions payable	20,615
Distributions payable	140,079
Payable for options contracts written (cost \$68,398)	215,806
	<u>376,500</u>
<b>Net assets representing unitholders' equity</b>	<b>\$ 24,428,164</b>
<b>Unitholders' equity (Note 3)</b>	
Unitholders' capital	23,666,531
Warrants	388,199
Contributed surplus	861
Retained earnings	372,573
<b>Unitholders' equity</b>	<b>\$ 24,428,164</b>
<b>Number of units outstanding (Note 3)</b>	<b>2,153,162</b>
<b>Number of warrants outstanding (Note 3)</b>	<b>2,156,662</b>
<b>Net assets per unit (Note 9)</b>	<b>\$ 11.35</b>

Approved on behalf of the Manager,

*(Signed)* "Michael Kovacs"  
President and Chief Executive Officer

*(Signed)* "B. Mark Riden CA"  
Chief Financial Officer

*The accompanying notes are an integral part of these financial statements.*

# Canadian Premium Select Income Fund

## STATEMENT OF OPERATIONS

**For the period November 17, 2011 (commencement of operations) to December 31, 2011**

<b>Investment income</b>	
Dividends	\$ 158,305
Interest	10,015
	<hr/> 168,320
<b>Expenses</b>	
Management fees (Note 4)	32,204
Service fees (Note 4)	12,882
Unitholder reporting costs (Note 4)	5,981
Audit fees	25,450
Transfer agency fees	7,474
Custodian fees and bank charges	9,233
Filing fees	1,650
Legal fees	40,311
Independent review committee fees	-
	<hr/> 135,185
Expenses absorbed by manager	-
	<hr/> 135,185
<b>Net investment income</b>	<b>\$ 33,135</b>
<b>Realized and unrealized gain / (loss) on investments</b>	
Realized loss on sale of investments	(40,496)
Transaction costs	(19,915)
Unrealized appreciation of investments	539,928
<b>Net gain on investments</b>	<b>479,517</b>
<b>Increase in net assets from operations</b>	<b>\$ 512,652</b>
<b>Increase in net assets from operations per unit</b>	<b>\$ 0.24</b>

*The accompanying notes are an integral part of these financial statements*

# Canadian Premium Select Income Fund

## STATEMENT OF CHANGES IN FINANCIAL POSITION

**For the period November 17, 2011 (commencement of operations) to December 31, 2011**

<b>Net assets, beginning of the period</b>	<b>\$ -</b>
Increase in net assets from operations	512,652
<b>Unitholders' transactions</b>	
Proceeds from issue of units	25,879,944
Payments on cancellation of units	(38,516)
Agents' fees	(1,358,697)
Cost of issue	(427,140)
<b>Net unitholders' transactions</b>	<b>24,055,591</b>
<b>Distributions to unitholders</b>	
Return of capital	(140,079)
<b>Total distributions to unitholders</b>	<b>(140,079)</b>
<b>Net assets, end of the period</b>	<b>\$ 24,428,164</b>
<b>Retained earnings, beginning of the period</b>	<b>\$ -</b>
Increase in net assets from operations	512,652
Distributions to unitholders	(140,079)
<b>Retained earnings, end of the period</b>	<b>\$ 372,573</b>
<b>Contributed surplus, beginning of the period</b>	<b>\$ -</b>
Cost of shares repurchased at less than par value	861
<b>Contributed surplus, end of the period</b>	<b>\$ 861</b>

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# Canadian Premium Select Income Fund

## STATEMENT OF CASH FLOWS

**For the period November 17, 2011 (commencement of operations) to December 31, 2011**

<b>Operating activities</b>	
Increase in net assets from operations	\$ 512,652
<b>Add (deduct) items not affecting cash:</b>	
Realized loss on sale of investments	40,496
Unrealized appreciation of investments	(539,928)
Proceeds from sale of investments	1,043,331
Purchases of investments	(24,727,552)
Net change in non-cash assets and liabilities	(104,446)
<b>Net cash flow used in operating activities</b>	<b>(23,775,447)</b>
<b>Financing activities</b>	
Proceeds from units issued	25,879,944
Payment on cancellation of units	(17,901)
Agents' fees	(1,358,697)
Issuance costs	(427,140)
<b>Net cash flow provided by financing activities</b>	<b>24,076,206</b>
<b>Net increase in cash and cash equivalents during the period</b>	<b>300,759</b>
Cash and cash equivalents, beginning of the period	-
<b>Cash and cash equivalents, end of the period</b>	<b>\$ 300,759</b>

*The accompanying notes are an integral part of these financial statements.*

# Canadian Premium Select Income Fund

## STATEMENT OF INVESTMENTS

<b>As at December 31, 2011</b>				
<b>Number of Shares</b>	<b>Security</b>	<b>Average Cost (\$)</b>	<b>Fair Value (\$)</b>	<b>% of Net Assets</b>
<b>EQUITIES</b>				
<b>Banking and Other Financial Issuers</b>				
27,085	Bank of Montreal	1,569,333	1,512,155	6.2
21,727	Canadian Imperial Bank of Commerce	1,563,993	1,602,149	6.6
77,300	Great-West Lifeco Inc.	1,608,132	1,570,736	6.4
34,816	Royal Bank of Canada	1,562,319	1,807,647	7.4
32,607	The Bank of Nova Scotia	1,637,326	1,654,805	6.8
		7,941,103	8,147,492	33.4
<b>Consumer Discretionary Issuers</b>				
77,900	Shaw Communications Inc. Cl. B Non-Voting	1,649,206	1,575,917	6.4
57,880	Thomson Reuters Corporation	1,646,737	1,573,757	6.4
		3,295,943	3,149,674	12.8
<b>Consumer Staples Issuers</b>				
36,500	Shoppers Drug Mart Corporation	1,532,435	1,498,690	6.1
		1,532,435	1,498,690	6.1
<b>Energy Issuers</b>				
74,300	Canadian Oil Sands Limited	1,554,353	1,724,503	7.1
47,200	Cenovus Energy Inc.	1,593,582	1,594,888	6.5
44,700	Enbridge Inc.	1,598,717	1,702,623	7.0
		4,746,652	5,022,014	20.6
<b>Real Estate</b>				
61,700	Riocan Real Estate Investment Trust	1,554,231	1,628,880	6.7
		1,554,231	1,628,880	6.7
<b>Telecommunications Service Issuers</b>				
39,050	BCE Inc.	1,557,019	1,657,282	6.8
42,190	Rogers Communications Inc., Cl. B	1,549,025	1,655,536	6.8
28,500	Telus Corporation	1,535,714	1,639,890	6.7
		4,641,758	4,952,708	20.3
	<b>Total equities</b>	<b>23,712,122</b>	<b>24,399,458</b>	<b>99.9</b>
<b>OPTIONS</b>				
<b>Banking and Other Financial Issuers</b>				
(6,700)	Bank of Montreal - Jan 2012 @ CAD \$59	(3,250)	-	-
(5,400)	Canadian Imperial Bank of Commerce - Jan 2012 @ CAD \$73	(2,646)	(6,356)	-
(18,500)	Great-West Lifeco Inc. - Jan 2012 @ CAD \$20	(2,405)	(2,915)	-
(8,700)	Royal Bank of Canada - Jan 2012 @ CAD \$46	(5,873)	(51,223)	(0.2)
(7,800)	The Bank of Nova Scotia - Jan 2012 @ CAD \$51	(3,705)	(1,837)	-
		(17,879)	(62,331)	(0.2)
<b>Consumer Discretionary Issuers</b>				
(17,900)	Shaw Communications Inc. - Jan 2012 @ CAD \$22	(1,611)	(1)	-
(13,500)	Thomson Reuters Corporation - Jan 2012 @ CAD \$29	(4,590)	(71)	-
		(6,201)	(72)	-
<b>Energy Issuers</b>				
(18,600)	Canadian Oil Sands Ltd. - Jan 2012 @ CAD \$20	(11,532)	(54,192)	(0.2)
(11,700)	Cenovus Energy Inc. - Jan 2012 @ CAD \$32	(9,594)	(21,987)	(0.1)
(10,600)	Enbridge Inc. - Jan 2012 @ CAD \$37	(5,671)	(13,674)	(0.1)
		(26,797)	(89,853)	(0.4)

The accompanying notes are an integral part of these financial statements.

# Canadian Premium Select Income Fund

## STATEMENT OF INVESTMENTS (continued)

<b>As at December 31, 2011</b>				
<b>Number of Shares</b>	<b>Security</b>	<b>Average Cost (\$)</b>	<b>Fair Value (\$)</b>	<b>% of Net Assets</b>
<b>Consumer Staples Issuers</b>				
(9,100)	Shoppers Drug Mart Corporation - Jan 2012 @ CAD \$42	(5,368)	(302)	-
		(5,368)	(302)	-
<b>Real Estate Issuers</b>				
(15,200)	RioCan Real Estate Investment Trust - Jan 2012 @ CAD \$26	(1,520)	(1,520)	-
		(1,520)	(1,520)	-
<b>Telecommunications Service Issuers</b>				
(9,700)	BCE Inc. - Jan 2012 @ CAD \$40	(1,892)	(20,452)	(0.1)
(10,500)	Rogers Communications Inc. - Jan 2012 @ CAD \$37	(4,410)	(19,315)	(0.1)
(7,100)	TELUS Corporation - Jan 2012 @ CAD \$55	(4,331)	(21,961)	(0.1)
		(10,633)	(61,728)	(0.3)
	<b>Total options</b>	<b>(68,398)</b>	<b>(215,806)</b>	<b>(0.9)</b>
	<b>Total investments</b>	<b>23,643,724</b>	<b>24,183,652</b>	<b>99.0</b>
	<b>Other assets less liabilities</b>		<b>244,512</b>	<b>1.0</b>
	<b>Net Assets</b>		<b>24,428,164</b>	<b>100.0</b>

*The accompanying notes are an integral part of these financial statements.*

# Canadian Premium Select Income Fund

## NOTES TO THE FINANCIAL STATEMENTS

December 31, 2011

### 1. ORGANIZATION

Canadian Premium Select Income Fund (the “Fund”) is an investment trust established under the laws of the Province of Ontario pursuant to a Declaration of Trust dated October 28, 2011, being the inception date. There was no significant activity in the Fund from the date of inception, October 28, 2011 to commencement of operations on November 17, 2011. On November 17, 2011, the Fund completed an initial public offering of 2,101,662 units at \$12.00 per unit for gross proceeds of \$25,219,944. On December 7, 2011, an over-allotment option was exercised for an additional 55,000 units at a price of \$12.00 per unit for gross proceeds of \$660,000.

The Fund will become an open-end mutual fund on November 22, 2013 (the “Conversion Date”). On and after the Conversion Date, the Fund units will be redeemable at NAV per unit on a daily basis, at such time the Fund will become subject to NI 81-102. The Fund will provide all unitholders with written notice at least 60 days prior to the Conversion Date.

### 2. SIGNIFICANT ACCOUNTING POLICIES

#### Basis of presentation

These financial statements are prepared in accordance with Canadian generally accepted accounting principles (“GAAP”) and are presented in Canadian dollars. The preparation of financial statements in accordance with Canadian GAAP requires management to make estimates and assumptions. Such estimates and assumptions affect reported amounts of assets and liabilities and disclosure of contingencies at the date of the financial statements and reported amounts of income and expenses during the reporting period. Actual results could differ from these estimates.

#### Valuation of investments

The fair value of investments as at the financial reporting date is as follows:

a) Investments are categorized as held for trading in accordance with CICA Handbook Section 3855 Financial Instruments – Recognition and Measurement. Investments held that are traded on an active market are valued at their bid prices through recognized public stock exchanges or through recognized investment dealers on the valuation date. Investments held include equities, listed warrants, short-term notes, treasury bills, bonds and other debt instruments. Investments held with no available bid prices are valued at their closing sale price.

b) Investments held that are not traded on an active market are valued using valuation techniques, on such basis and in such a manner established by the Manager. The value of any security for which, in the opinion of the Manager, the published market quotations are not readily available shall be the fair value as determined by the Manager in accordance with CICA Handbook Section 3855 methodologies. The fair values of certain securities are determined using valuation models that are based, in part, on assumptions that are not supported by observable market inputs. These methods and procedures may include, but are not limited to, performing comparisons with prices of comparable or similar securities, obtaining valuation related information from issuers and/or other analytical data relating to the investment and using other available indication of value. These values are independently assessed internally to ensure that they are reasonable. However, because of the inherent uncertainty of valuation, the estimated fair values for the aforementioned securities and interests may be materially different from the values that would be used had a ready market for the security existed. The fair values of such securities are affected by the perceived credit risks of the issuer, predictability of cash flows and length of time to maturity. At December 31, 2011, there were no securities that required pricing using assumptions.

# Canadian Premium Select Income Fund

## NOTES TO THE FINANCIAL STATEMENTS

December 31, 2011

National Instrument 81-106 – “Investment Fund Continuous Disclosure” (“NI 81-106”) requires all investment funds to calculate net asset value for all purposes other than for financial statements in accordance with part 14.2, which differs in some respects from the requirements of Section 3855 of Canadian GAAP. Canadian GAAP includes the requirement that the fair value of financial instruments listed on a recognized public stock exchange be valued at their last bid price for securities held in a long position and at their last ask price for securities held in a short position, instead of their close price or the last sale price of the security for the day as required by NI 81-106. This results in differences between net asset value (“NAV”) calculated based on NI 81-106 and on net assets calculated based on Canadian GAAP (“Net assets”). A reconciliation between NAV per unit and Net assets per unit at the period end is provided in Note 9.

### **Cash and cash equivalents**

Cash is comprised of cash on deposit. Cash equivalents are comprised of highly liquid investments having terms to maturity of 90 days or less.

### **Other assets and liabilities**

For the purposes of categorization in accordance with CICA Handbook Section 3862, accrued interest and dividends, prepaid interest, receivable for securities issued, amounts due from brokers, the Manager, and other Funds, and other assets are designated as loans and receivables and recorded at cost or amortized cost. Similarly, amounts due to brokers, accrued expenses and other liabilities are designated as other financial liabilities and reported at cost or amortized cost, which approximates fair value for these assets and liabilities.

### **Transaction costs**

Transaction costs, such as brokerage commissions, incurred on the purchase and sale of securities by the Fund are expensed in accordance with Section 3855 and are recognized in the Statement of Operations in the period in which they are incurred.

### **Investment transactions and income recognition**

Investment transactions are accounted for on the trade date. The cost of investments represent the amount paid for each security and is determined on an average cost basis excluding transaction cost. Realized gains/(losses) from the sale of investments and unrealized appreciation/(depreciation) of investments are calculated on an average cost basis.

Investment income is recorded on an accrual basis. Interest income is recorded on an accrual basis and dividend income is recorded on the ex-dividend date.

Distributions received from income trusts are recorded as income, capital gains or a return of capital, based on the best information available to the Manager. Due to the nature of these investments, actual allocations could vary from this information. Distributions from investment trusts treated as a return of capital reduce the average cost of the underlying investment trust. Distributions received from mutual funds are recognized in the same form in which they are received from the underlying funds.

### **Securities valuation**

The NAV on a particular date will be equal to the aggregate value of the assets of the Fund less the aggregate value of the liabilities of the Fund, expressed in Canadian dollars at the applicable exchange rate on such date. The NAV and NAV per trust unit will be calculated as of 4:00 p.m. (Toronto time) or such other time as the Manager or its agent deem appropriate (the valuation time) every business day (valuation date). A valuation date is each day on which the Toronto Stock Exchange (the “TSX”) is open for business.

# Canadian Premium Select Income Fund

## NOTES TO THE FINANCIAL STATEMENTS

December 31, 2011

### Increase / (decrease) in net assets from operations per unit

“Increase / (decrease) in net assets from operations per unit” in the Statement of Operations represents the increase / (decrease) in net assets from operations, divided by the weighted average units outstanding for the financial period.

The “increase / (decrease) in net assets from operations per share – diluted” takes into account the dilutive impact of issuing shares from warrants outstanding when the price that it trades at is higher than the exercise price of \$12.00.

### Fair value of financial instruments

The table below summarizes the fair value of the Fund’s financial instruments using the following fair value hierarchy:

**Level 1:** Quoted prices (unadjusted) in active markets for identical assets or liabilities.

**Level 2:** Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

**Level 3:** Inputs for the asset or liability that are not based on observable market data. Additional quantitative disclosures are required for Level 3 securities.

There were no Level 3 securities held by the Fund as at December 31, 2011.

Securities Classification:

Investments at Fair Values as at December 31, 2011				
	Level 1	Level 2	Level 3	Total
Investments at fair value				
<b>Equities</b>				
Common Shares	22,770,578	-	-	22,770,578
REIT	1,628,880	-	-	1,628,880
<b>Total equities</b>	24,399,458	-	-	24,399,458
Total written option contracts	-	(215,806)	-	(215,806)
<b>Total investments at fair value</b>	<b>24,399,458</b>	<b>(215,806)</b>	-	<b>24,183,652</b>

### Transition to International Financial Reporting Standards (“IFRS”)

As previously confirmed by the Canadian Accounting Standards Board (“AcSB”), most Canadian publicly accountable entities adopted all IFRS, as published by the International Accounting Standards Board (“IASB”), on January 1, 2011. However, the AcSB had initially allowed most investment funds to defer adoption of IFRS until fiscal years beginning on or after January 1, 2013. At its December 12, 2011 meeting, the AcSB decided to extend the deferral of mandatory adoption of IFRS for Investment Companies and Segregated Accounts of Life Insurance Enterprises to 2014. The decision was in response to the possibility that the IASB may not complete its Investment Entities project before January 1, 2013. The AcSB expects to issue the amendment in March 2012. Accordingly, the Fund will adopt IFRS for the fiscal period beginning January 1, 2014 and will issue its initial financial statements in accordance with IFRS, including comparative financial information, for the interim period ending June 30, 2014. Management has been monitoring developments in the IFRS conversion program and has been assessing the likely impacts on implementation decisions, internal controls, information systems and training.

# Canadian Premium Select Income Fund

## NOTES TO THE FINANCIAL STATEMENTS

December 31, 2011

In May 2011, the IASB issued IFRS 13 Fair Value Measurement, which defines fair value, sets out a single IFRS framework for measuring fair value and requires disclosure about fair value measurements. It only applies when other IFRSs require or permit fair value measurement. If an asset or a liability measured at fair value has a bid price and an ask price, it requires valuation to be based on a price within the bid-ask spread that is most representative of fair value. It allows the use of mid-market pricing or other pricing conventions that are used by market participants as a practical expedient for fair value measurements within a bid-ask spread. This may result in elimination of the differences between the net assets per series unit and NAV per series unit at the financial statements reporting dates.

Based on management's current assessment of the differences between Canadian GAAP and IFRS, other than the impact due to IFRS 13 noted above, it is not expected that there would be any other impact on the Funds' NAV per series unit or net assets per series unit. Management has presently determined that the impact of IFRS to the financial statements would be otherwise limited to additional note disclosures and potential modifications to presentation including unitholders' equity. However, this determination is subject to change as we finalize our assessment of potential IFRS differences and as new standards are issued by the IASB prior to the Fund's adoption of IFRS.

### 3. UNITHOLDERS' EQUITY

The authorized capital of the Fund consists of an unlimited number of transferable, units of one class, each of which represents an equal, undivided interest in the net assets of the Fund. Each unit consists of one trust unit and one warrant. Except as provided in the Declaration of Trust, all units have equal rights and privileges. Each whole unit is entitled to one vote at all meetings of unitholders and is entitled to participate equally in any and all distributions made by the Fund.

The Fund entered into a normal course issuer bid programme for the period from December 14, 2011 to December 13, 2012 which allows the Fund to purchase up to 215,566 listed trust units and listed warrants of the Fund for cancellation by way of a normal course issuer bid through the facilities of the TSX. During the period ended December 31, 2011, 3,500 trust units were purchased for cancellation. No warrants were purchased for cancellation.

If the price for the redemption of the Fund units is lower than the original average price, the difference is included in "contributed surplus" on the Statement of Financial Position. If the price is greater than the original issue price, the difference is charged to "Contributed surplus" until the entire amount is eliminated, and the remaining amount is charged to "Retained earnings (deficit)".

The following units were issued and redeemed during the period:

	Trust units outstanding	Warrants Outstanding
Initial issuance November 17, 2011 and over-allotment December 7, 2011	2,156,662	2,156,662
Units cancelled	(3,500)	-
<b>Total outstanding as at December 31, 2011</b>	<b>2,153,162</b>	<b>2,156,662</b>

#### Warrants

Each whole warrant entitles the holder to purchase one trust unit at a subscription price of \$12.00 on or before 5:00 p.m. (Toronto time) on, and only on, May 31, 2013. Warrants not exercised will be void and of no value. Holders of warrants who exercise the warrants will become holders of trust units issued through the exercise of the warrants. Upon the exercise of a warrant, the Fund will pay a fee equal to \$0.18 per warrant to the registered dealer whose client is exercising the warrant and \$0.12 per warrant to the Agents.

The warrants trade on the TSX under the symbol HCS.WT. At December 31, 2011, the closing price was \$0.065.

# Canadian Premium Select Income Fund

## NOTES TO THE FINANCIAL STATEMENTS

December 31, 2011

### Redemptions

Prior to the Conversion Date, trust units may be surrendered prior to 5:00 p.m. (Toronto time) on the 10th business day before the last business day of the applicable month by the holders thereof for monthly redemption. Upon receipt by the Fund of the redemption notice, the holder of a trust unit shall be entitled to receive a price per trust unit equal to the lesser of:

- (a) 95% of the “market price” of the trust units on the principal market on which the trust units are quoted for trading during the 20 trading day period ending immediately before the monthly redemption date; and
- (b) 100% of the “closing market price” on the principal market on which the trust units are quoted for trading on the monthly redemption date.

In accordance with the Fund prospectus, in addition to the monthly redemption rights, units may be surrendered for redemption at the Fund’s NAV per unit on the October 25, 2013 (the “First NAV Redemption Date”). Units must be surrendered for redemption during the notice period and the unitholder will receive payment on or before the seventh Business Day following the First NAV Redemption Date.

On and after the Conversion Date, unitholders may redeem units on any business day at the NAV per unit

### Issue costs

Certain offering expenses such as costs of creating the Fund, the cost of printing and preparing the prospectus, legal expenses of the Fund and other out-of-pocket expenses incurred by the agents together with the agents’ fees payable by the Fund are reflected as a reduction of unitholders’ equity. The expenses paid are shown in the Statement of Changes in Financial Position.

### Distributions

The Fund intends to make monthly cash distributions to unitholders of record on the last business day of each month and pay such cash distributions on or before the 15<sup>th</sup> day of the following month. Beginning in November 2011, the Fund will annually determine and announce the indicative distribution amount for the following year based upon the prevailing market conditions. The indicative distribution amount was \$140,079 or \$0.065 per unit per month (\$0.065 in total) for the period ended December 31, 2011.

## 4. EXPENSES

### Management and service fees

HARVEST Portfolios Group Inc. is the Manager of the Fund and is responsible for managing or arranging for managing the Fund’s overall business and operations. The Manager has retained Highstreet Asset Management Inc. (“Highstreet” or the “Investment Manager”) to provide investment management services to the Fund and pays Highstreet a fee for its portfolio advisory service, from the management fee received from the Fund, calculated on the basis of the Fund’s net assets.

The Manager is entitled to a fee of 1.00 per cent of the NAV plus HST per annum of the Fund. The Fund pays service fees to registered dealers at the rate on 0.40 per cent of the NAV plus HST per annum of the Fund. Service fees are accrued daily and paid monthly to the Manager, who in turn pays the dealers.

# Canadian Premium Select Income Fund

## NOTES TO THE FINANCIAL STATEMENTS

December 31, 2011

### **Independent Review Committee (“IRC”) Fees**

The IRC, is required under National Instrument 81-107, reviews conflict of interest matters referred to it by the manager and provided recommendations or approves actions, as appropriate, that are in the best interest of the Fund. There are currently three members of the IRC who are independent of Harvest and its affiliates. IRC members are compensated by way of an annual retainer fee and a per meeting attendance fee, as well as reimbursed for expenses associated with IRC duties. These costs are allocated among the individual funds appropriately by assets.

### **Other expenses**

The Fund is responsible for all expenses relating to the operation and the carrying on of its business, including legal fees and audit fees, interest, taxes and administrative costs relating to the redemption of securities as well as the cost of financial and other reports and compliance with applicable laws, regulations and policies.

The Manager will be reimbursed by the Fund for all reasonable costs, expenses and liabilities incurred by the Manager for performance of extraordinary services on behalf of the Fund in connection with the discharge by the Manager of its duties hereunder. Such costs and expenses may include, without limitation: mailing and printing expenses for reports to unitholders and other unitholder communications; a reasonable allocation of salaries, benefits and consulting fees; and other administrative expenses and costs incurred in connection with the Fund’s continuous public filing and other obligations. These expenses were \$5,981 for the period ended December 31, 2011 and are included in the unitholder reporting costs in the Statement of Operations

## **5. OPTIONS**

A written covered call options strategy may be used by the Fund, but only to the extent considered appropriate by the Manager. Option premiums received by the Fund are, so long as the options are outstanding, reflected in the Statement of Investments. Exchange traded options are valued at current fair value on each valuation day, based on the value that would be realized if the option was closed out in the valuation date.

Realized gains and losses relating to written options may arise from:

- i) Expiration of the written options – realized gains will arise equal to the premium received;
- ii) Exercise of the written options – realized gains or losses will arise equal to the sum of the premium received and the realized gain or loss from the disposition of the related portfolio investment at the exercise price of the option; or
- iii) Closing of the written options – realized gains or losses will arise equal to the cost of purchasing options to close the position net of any premium received.

Realized gains and losses related to options are included in “realized gain (loss) on sale of investments” in the Statement of Operations

## **6. FINANCIAL RISK MANAGEMENT**

The investment objectives of the Fund are to provide unitholders with

- (i) monthly cash distributions;
- (ii) the opportunity for capital appreciation; and
- (iii) lower overall volatility of the portfolio returns than would otherwise be experienced by owning the equity securities held by the Fund directly.

# Canadian Premium Select Income Fund

## NOTES TO THE FINANCIAL STATEMENTS

December 31, 2011

The Fund invests in a diversified portfolio of equity securities of 15 Canadian issuers with a market capitalization of at least \$1 billion, selected and rebalanced semi-annually on an equally weighted basis by the Investment Manager from the S&P/TSX Composite Dividend Index, such that the Portfolio will meet the investment characteristics described below.

In generate additional returns, the Investment Manager will sell covered call options each month on the equity securities held in the Portfolio. The Investment Manager will not sell call options on more than 33% of the equity securities of each Canadian Issuer held in the Portfolio. Such call options may be either exchange-traded options or over-the-counter options.

### Investment Strategy

The Investment Manager selected the equity securities for the Fund's Portfolio and will rebalance the Portfolio semi-annually such that the Portfolio, at the time of initial investment and immediately following each selection and rebalancing, will have the following investment characteristics:

- Growth** - A median 5-year average compound Earnings per Share growth rate greater than the median for the S&P/TSX Composite Dividend Index;
- Value** - A median Price-to-Earnings Ratio lower than the median for the S&P/TSX Composite Dividend Index;
- Quality** - A median 5-year average Return-on-Equity greater than the median for the S&P/TSX Composite Dividend Index; and
- Yield** - A median yield greater than the median for the S&P/TSX Composite Dividend Index.

### Other price risk

Other price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. The value of securities in the Fund's portfolio may be affected by the stock market conditions rather than each company's performance. Developments in the market are affected by general economic and financial conditions. Political, social and environmental factors can also affect the value of any investment.

As at December 31, 2011, 99.9% of the Fund's portfolio investments were traded on public stock exchanges. If equity prices on these exchanges had increased or decreased by 5%, as at period end, with all other factors remaining constant, net assets would have increased or decreased by approximately \$1,219,973.

In practice, the actual trading results may differ and the difference could be material.

### Currency risk

Currency risk is the risk that the value of investments denominated in currencies other than the financial currency of the Fund will fluctuate as a result of changes in foreign exchange rates. When the Fund buys an investment priced in a foreign currency and the exchange rate between the Canadian dollar and the foreign currency changes unfavorably, it could reduce the value of the Fund's investment.

The Fund exclusively invests in Canadian securities, therefore the Fund's exposure to currency risk is insignificant.

# Canadian Premium Select Income Fund

## NOTES TO THE FINANCIAL STATEMENTS

December 31, 2011

### Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or fair value of financial instruments. A fund that invests in fixed income securities, such as bonds and money market instruments, is sensitive to changes in interest rates. The Fund does not hold any bonds or money market instruments, therefore, the Fund's exposure to interest rate risk is insignificant.

### Liquidity risk

Liquidity risk is defined as the risk that a fund may not be able to settle or meet its obligations on time or at a reasonable price.

The Fund primarily invests in securities that are actively traded in public markets and can be readily disposed of to raise liquidity.

The table below analyzes the Fund's financial liabilities into groupings based on the remaining period at the period end date to contractual maturity date. The amounts in the table are the contractual undiscounted cash flows. Balances due within 12 months equal their carrying balances, as the impact of discounting is not significant.

As of December 31, 2011	Less than 1 month	1-3 months	No stated maturity
Redemptions payable	20,615	-	-
Distributions payable	140,079	-	-
Payable for options contracts written	215,806	-	-
<b>Total financial liabilities</b>	<b>376,500</b>	-	-

### Credit risk

Credit risk is the risk that the counterparty to a financial instrument will fail to discharge an obligation or commitment that it has entered into with a fund. The Fund has exposure to credit risk in its trading of listed securities, as it does not invest in fixed income securities. The Fund minimizes the concentration of credit risk by trading with a large number of brokers and counterparties on recognized and reputable exchanges. The risk of default is considered minimal as all transactions are settled and paid for upon delivery using approved brokers.

## 7. SOFT DOLLAR COMMISSIONS

Brokerage commissions paid to certain brokers may, in addition to paying for the cost of brokerage services in respect of security transactions, also provide for the cost of investment research services provided to the investment manager.

The value of such research services included in commissions paid to brokers for the period ended December 31, 2011 amounted to \$NIL.

# Canadian Premium Select Income Fund

## NOTES TO THE FINANCIAL STATEMENTS

December 31, 2011

### 8. INCOME TAXES

The Fund qualifies as a mutual fund trust under the provisions of the Income Tax Act (Canada). The Fund is subject to tax on their income including net realized capital gains which are not paid or payable to unitholders. It is the intention of the Fund to distribute all of its net income and sufficient net realized capital gains so the Fund will not be subject to income taxes.

The amount of net realized taxable capital gains available for distribution is reduced by the amount of net capital gains to be retained in the Fund. This is done in order to enable the Fund to fully utilize any available tax credits due to application of the capital gain refund formula attributable to redemptions during the year. In certain circumstances, the fund may distribute a return of capital. A return of capital is taxable but will generally reduce the adjusted cost of the units.

Capital losses may be carried forward indefinitely to reduce future realized capital gains. Non-capital losses may be applied against future taxable income.

As at December 31, 2011, the Fund had \$126,586 in non-capital losses .

### Harmonized sales tax

Effective July 1, 2010, certain provinces have harmonized their provincial sales tax (“PST”) with the federal goods and services tax (“GST”). The harmonized sales tax (“HST”) combines the GST rate of 5% with the PST rate of certain provinces. For the province of Ontario the HST rate is 13%. As the manager is a resident of Ontario, the expenses paid by the Fund include HST of 13%. HST is calculated using the residency of unitholders in the Fund as at specific times, rather than the physical location of the manager. A blended rate refund is filed with Revenue Canada on behalf of the Fund, in arrears, using each province’s HST rate or GST rate in the case of non-participating provinces. Any refund received is applied against future HST payable.

### 9. NET ASSET VALUE AND NET ASSETS

CICA Handbook Section 3855 requires that the fair value of financial instruments which are actively traded be measured based on the bid price for long positions held and the asking price for short positions held.

The NAV per unit for purposes of unitholder transactions (i.e. purchases, switches, redemptions) and net assets per unit calculated in accordance with CICA Handbook Section 3855 are shown below:

Per Unit (\$):	NAV	Net assets
As at December 31, 2011	\$11.36	\$11.35

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**CAUTION REGARDING FORWARD-LOOKING STATEMENTS**

This document may contain forward-looking statements relating to anticipated future events, results, circumstances, performance or expectations that are not historical facts but instead represent our beliefs regarding future events. By their nature, forward-looking statements require us to make assumptions and are subject to inherent risks and uncertainties. There is significant risk that predictions and other forward-looking statements will not prove to be accurate. We caution readers of this document not to place undue reliance on our forward-looking statements as a number of factors could cause actual future results, conditions, actions or events to differ materially from the targets, expectations, estimates or intentions expressed or implied in the forward-looking statements. Actual results may differ materially from management expectations as projected in such forward-looking statements for a variety of reasons, including but not limited to market and general economic conditions, interest rates, regulatory and statutory developments, the effects of competition in the geographic and business areas in which the Fund may invest and the risks detailed from time to time in the Fund's simplified prospectus or offering memorandum. We caution that the foregoing list of factors is not exhaustive and that when relying on forward-looking statements to make decisions with respect to investing in the Fund, investors and others should carefully consider these factors, as well as other uncertainties and potential events, and the inherent uncertainty of forward-looking statements. Due to the potential impact of these factors, the Fund does not undertake, and specifically disclaims, any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, unless required by applicable law.