



Financial Statements

First Trust/Highland Capital Floating Rate
Income Fund II

Years Ended December 31, 2009 and 2008



MANAGEMENT REPORT

Management's Responsibility for Financial Reporting

The accompanying financial statements have been prepared by FT (NSI) Management Co., the Manager of the First Trust/Highland Capital Floating Rate Income Fund II (the "Fund"), and approved by the Board of Directors of the Manager. The Fund's Manager is responsible for the information and representations contained in these financial statements and other sections of the Annual Report. FT (NSI) Management Co. maintains appropriate procedures to ensure that relevant and reliable 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. The significant accounting policies which management believes are appropriate for the Fund are described in Note 2 to the financial statements.



Mark Bradley
Director



Ron McAlister
Director

AUDITORS' REPORT

To the Unitholders of

First Trust/Highland Capital Floating Rate Income Fund II

We have audited the statement of investment portfolio of First Trust/Highland Capital Floating Rate Income Fund II (the "Fund") as at December 31, 2009, the statements of net assets as at December 31, 2009 and 2008, and the statements of operations, of changes in net assets and of cash flows for the years then ended. These financial statements are the responsibility of the Manager of the Fund. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Fund as at December 31, 2009 and 2008, and the results of its operations, the changes in its net assets and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.



Chartered Accountants
Licensed Public Accountants

Toronto, Canada
March 1, 2010

Statements of Net Assets

As at December 31, 2009 and 2008

	2009 \$	2008 \$
Assets:		
Cash and cash equivalents	84,599	76,527
Investments, at fair value (including value of forward agreement)	26,976,126	22,259,849
Short-term investments	3,271,848	-
Accrued interest and dividends receivable	107,831	-
Receivables for portfolio securities sold	808	-
Total Assets	30,441,212	22,336,376
Liabilities:		
Management fees payable (Note 6)	12,550	483
Accrued expenses	175,728	214,392
Goods and services tax payable	2,173	1,211
Payable for portfolio securities purchased	2,373,313	-
Distributions payable to unitholders	-	100,122
Total Liabilities	2,563,764	316,208
Net Assets	27,877,448	22,020,168
Number of units outstanding (Note 7)	5,318,992	4,004,885
Net assets per Unit	5.24	5.50
Cost of investments held – Common share portfolio (Note 4)	11,484,878	29,324,094

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

Approved on behalf of the Board of Directors of the Manager:



Mark Bradley
Director



Ron McAlister
Director

Statements of Operations

For the years ended December 31, 2009 and 2008

	2009 \$	2008 \$
Income		
Interest revenue	138,654	-
Dividend revenue	111	-
Other income	6,718	-
Total Income	145,483	-
Expenses (Note 6)		
Other expenses	126,946	166,819
Legal fees	110,413	37,000
Audit fees	64,893	58,400
Forward agreement fees	63,138	249,435
Management fees	57,116	5,224
Custodial fees	56,933	56,000
Directors' fees	14,488	3,202
Goods and services tax	7,541	7,442
Independent Review Committee fees	3,137	3,454
Securityholder information costs	(266)	18,574
Total Expenses	504,339	605,550
Net Investment Loss	(358,856)	(605,550)
Realized and Unrealized Gain (Loss) on Investments		
Net realized (loss) gain on sale of investments	(1,368,373)	3,621,865
Net realized loss on foreign currency translation	(107,778)	(132)
Change in unrealized (depreciation) appreciation of forward agreement (Note 4)	(6,802,596)	14,392,022
Change in unrealized appreciation (depreciation) of investments (Note 4)	8,180,613	(28,287,938)
Net Realized and Unrealized Loss on Investments	(98,134)	(10,274,183)
Decrease in Net Assets from Operations	(456,990)	(10,879,733)
Decrease in Net Assets from Operations per Unit (based on the average units outstanding during the year)	(0.11)	(2.15)

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

Statements of Changes in Net Assets

For the years ended December 31, 2009 and 2008

	2009 \$	2008 \$
Decrease in Net Assets from Operations	(456,990)	(10,879,733)
Distributions Paid or Payable to Unitholders from Return of capital	(347,784)	(2,295,776)
	(347,784)	(2,295,776)
Changes Due to Capital Unit Transactions (Note 7)		
Amount received from the issuance of units	19,131,525	-
Amount paid for redemptions and repurchases of capital units	(12,469,471)	(15,501,329)
	6,662,054	(15,501,329)
Increase (Decrease) in Net Assets for the Year	5,857,280	(28,676,838)
Net Assets, Beginning of Year	22,020,168	50,697,006
Net Assets, End of Year	27,877,448	22,020,168
Distributions per unit, paid or payable to unitholders		
From return of capital	0.09	0.44
Total distributions (based on the average units outstanding during the year)	0.09	0.44

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

Statements of Cash Flows

For the years ended December 31, 2009 and 2008

	2009 \$	2008 \$
OPERATING ACTIVITIES		
Decrease in net assets from operations	(456,990)	(10,879,733)
Change in unrealized depreciation (appreciation) of forward agreement	6,802,596	(14,392,022)
Change in unrealized (appreciation) depreciation of investments	(8,180,613)	28,288,070
Net realized loss (gain) on sale of investments	1,368,373	(3,621,865)
Change in other assets and liabilities	(133,466)	(83,782)
Proceeds from sale of investments	20,037,127	42,174,049
Amount paid for investments acquired	(22,386,231)	(23,492,559)
Net cash flow (used in) provided by operating activities	(2,949,204)	17,922,158
FINANCING ACTIVITIES		
Distributions to unitholders	(447,906)	(2,550,634)
Proceeds from issuance of units	19,131,525	-
Amounts paid for redemption of units	(12,454,495)	(15,497,666)
Net cash provided by (used in) financing activities	6,229,124	(18,048,300)
Net increase (decrease) in cash during the year	3,279,920	(56,142)
Cash and cash equivalents, beginning of year	76,527	132,669
Cash and cash equivalents, end of year	3,356,447	76,527
Cash and cash equivalents consist of:		
Cash	84,599	76,457
Short-term investments	3,271,848	70
	3,356,447	76,527

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

Statement of Investment Portfolio

As at December 31, 2009

	Average Cost \$	Fair Value \$
Common Share Portfolio - 47.6%	11,484,878	13,257,767
Value of Forward Agreement - (16.2%)		(4,524,229)
Total Value of First Trust/Highland Capital Senior Loan Trust (including Forward Agreement)		8,733,538
Total Value of Directly Held Senior Loan Portfolio - 65.4%	18,908,900	18,242,588
Total Value of Investments (including Forward Agreement)		26,976,126
Short-Term Securities - 11.7%		
3,120,807 BNY Mellon Deposit Trust Reserve, Variable Rate	3,277,524	3,271,848
Other Assets and Liabilities - (8.5%)		(2,370,526)
Net Assets - 100%		27,877,448

As a result of the Forward Agreement described in Note 4, the value of the total investments (including Forward Agreement) of the Fund is equal to the net asset value of the First Trust/Highland Capital Senior Loan Trust and the directly held portfolio of senior loans.

First Trust/Highland Capital Senior Loan Trust

The Senior Loan Trust Portfolio and other net assets of Senior Loan Trust as at December 31, 2009 are listed below:

Principal Par Value US \$	Sector Breakdown and Company Name	Facility	Maturity Date	Average Cost \$	Fair Value \$
	Senior Floating Rate Interests and Equities - 94.1%				
	Senior Floating Rate Interests - 92.3%				
	Aerospace and Defense - 4.0%				
500,000	US Airways Group, Inc.	Loan	2014/03/21	358,615	352,508
				358,615	352,508
	Beverage, Food and Tobacco - 2.8%				
237,500	Pierre Foods, Inc.	Loan	2014/09/30	250,855	248,983
				250,855	248,983
	Broadcasting and Entertainment - 8.4%				
748,097	Charter Communications Operating, LLC	New Term Loan	2014/03/06	745,077	734,270
				745,077	734,270
	Buildings and Real Estate - 7.3%				
502,277	Custom Building Products, Inc.	First Lien Term Loan	2011/10/29	467,467	510,766
1,360,807	Ginn LA Conduit Lender, Inc.	First Lien Tranche A			
		Credit-Linked Deposit	2011/06/08	1,151,731	89,163
634,006	Ginn LA Conduit Lender, Inc.	First Lien Tranche B Term Loan	2011/06/08	536,596	41,541
				2,155,794	641,470
	Cargo Transport - 3.1%				
656,189	SIRVA Worldwide, Inc.	Second Lien Term Loan	2015/05/12	678,343	68,792
136,977	SIRVA Worldwide, Inc.	Revolving Credit Loan			
		(Exit Finance)	2012/05/12	145,337	72,518
279,036	SIRVA Worldwide, Inc.	Term Loan (Exit Finance)	2012/05/12	280,906	131,637
				1,104,586	272,947
	Diversified and Conglomerate Service - 5.4%				
500,000	Sabre Inc.	Initial Term Loan	2014/09/30	444,296	475,034
				444,296	475,034
	Electronics - 11.1%				
500,000	CDW Corporation	Term Loan	2014/10/10	439,527	450,791
545,275	SCS Holdings II, Inc. (Sirius Computer Solutions)	First Lien Term Loan	2012/11/30	587,403	528,766
				1,026,930	979,557
	Finance - 6.2%				
500,000	Nuveen Investments, Inc.	Second Lien Term Loan	2015/07/31	550,731	544,705
				550,731	544,705
	Healthcare, Education and Childcare - 6%				
927,483	CCS Medical, Inc. (Chronic Care)	First Lien Term Loan	2012/09/30	1,045,202	529,918
				1,045,202	529,918

First Trust/Highland Capital Floating Rate Income Fund II

Statement of Investment Portfolio (continued)

As at December 31, 2009

Principal Par Value US \$	Sector Breakdown and Company Name	Facility	Maturity Date	Average Cost \$	Fair Value \$
1,000,000	Hotels, Motels, Inns & Gaming - 3.8% Fontainebleu Florida Hotel, LLC/Fontainebleau Florida Tower 2, LLC	Tranche C Term Loan	2012/06/06	1,069,100	335,472
				1,069,100	335,472
	Insurance - 5.5%				
91,761	HUB International Limited	Delayed Draw Term Loan	2014/06/13	83,943	87,781
408,239	HUB International Limited	Initial Term Loan	2014/06/13	373,456	390,529
				457,399	478,310
	Personal and Non Durable Consumer Products - 8.7%				
750,000	Revlon Consumer Products Corporation	Term Loan	2012/01/15	768,803	766,325
				768,803	766,325
	Telecommunications - 11.2%				
500,000	Avaya Inc.	Term Loan	2014/10/24	451,441	452,101
500,000	Springboard Finance, LLC	Dollar Term Loan	2014/11/19	511,119	537,541
				962,560	989,642
	Utilities - 8.5%				
994,034	Bosque Power Company, LLC	Term Loan	2015/01/16	1,024,211	746,836
865,081	Mirant Americas Development Capital, LLC	Holdback - Term Loan A	2020/01/01		
122,107	Mirant Americas Development Capital, LLC	Holdback - Term Loan B	2020/01/01		
12,813	Mirant Americas Development Capital, LLC	Holdback - Term Loan C	2020/01/01		
				1,024,211	746,836
	Total Senior Floating Rate Interests			11,964,159	8,095,977
	Equities - 1.8%				
	Cargo Transport - 1.8%				
3,455	SIRVA Worldwide, Inc.			230,470	159,444
				230,470	159,444
	Total Senior Floating Rate Interests and Equities			12,194,629	8,255,421
	Short-Term Securities - 9.0%				
	United States - 9.0%				
750,350	BNY Mellon Deposit Trust Reserve, Variable Rate			795,361	786,629
				795,361	786,629
	Total Securities - 103.1%			12,989,990	9,042,050
	Adjustment from bid price to closing price - 1.7%				146,942
					9,188,992
	Other Assets and Liabilities of the Trust - (4.8)%				(455,454)
	Net Assets of Senior Loan Trust - 100%				8,733,538
	Less: Common Share Portfolio				13,257,767
	Value of Forward Agreement				(4,524,229)

Statement of Investment Portfolio (continued)

The Directly Held Senior Loan Portfolio as at December 31, 2009 are listed below:

Principal Par Value US \$	Sector Breakdown and Company Name	Facility	Maturity Date	Average Cost \$	Fair Value \$
Senior Floating Rate Interests - 96.8%					
Aerospace & Defense - 5.2%					
624,868	AWAS Capital, Inc.	Second Lien Term Loan	2013/03/15	313,984	493,493
500,000	Delta Air Lines, Inc.	Credit- Linked Deposit Loan	2012/04/30	471,945	461,711
				785,929	955,204
Automobile - 5.4%					
500,000	Dana Holding Corporation	Term Advance	2015/01/30	495,129	501,242
498,080	Ford Motor Company	Tranche B-1 Term Loan	2013/12/15	465,496	481,694
				960,625	982,936
Beverage, Food & Tobacco - 3.8%					
500,000	DSW Holdings, Inc.	Loan	2012/03/02	464,424	450,791
512,313	Nellson Nutraceutical, Inc.	First Lien Term Loan	2009/10/04	280	246
237,500	Pierre Foods, Inc.	Loan	2014/09/30	250,855	248,983
				715,559	700,020
Broadcasting and Entertainment - 5.4%					
997,462	Charter Communications Operating, LLC	New Term Loan	2014/03/06	993,436	979,027
				993,436	979,027
Buildings and Real Estate - 1.2%					
2,038,617	Ginn LA Conduit Lender, Inc.	First Lien Tranche A Credit-Linked Deposit	2011/06/08	222,688	133,574
951,009	Ginn LA Conduit Lender, Inc.	First Lien Tranche B Term Loan	2011/06/08	103,883	62,312
973,657	LBREP/L-Suncal Master I LLC	First Lien Term Loan	2010/01/18	5,318	20,415
				331,889	216,301
Cargo Transport - 0.9%					
381,317	SIRVA Worldwide, Inc.	Second Lien Term Loan	2015/05/12	62,850	39,975
79,598	SIRVA Worldwide, Inc.	Revolving Credit Loan (Exit Finance)	2012/05/12	79,167	42,141
162,150	SIRVA Worldwide, Inc.	Term Loan (Exit Finance)	2012/05/12	88,562	76,496
				230,579	158,612
Chemical, Plastic & Rubber - 2.5%					
126,177	Texas Petrochemical, LP	Incremental Term Loan B	2013/06/27	121,104	116,845
373,823	Texas Petrochemical, LP	Term B Loan	2013/06/27	358,794	346,176
				479,898	463,021
Diversified Natural Resources, Precious Metals & Minerals - 12.9%					
1,032,501	Euramax International, Inc.	Domestic Term Loan (Cash Pay)	2013/06/29	422,945	703,574
1,038,498	Euramax International, Inc.	Domestic Term Loan (Payment In Kind)	2013/06/29	450,208	707,661
1,000,000	Sabre Inc.	Initial Term Loan	2014/09/30	897,313	950,067
				1,770,466	2,361,302
Electronics - 2.9%					
498,741	SunGard Data Systems Inc (Solar Capital Corp.)	Incremental Term Loan	2014/02/28	545,068	526,253
				545,068	526,253
Finance - 2.6%					
500,000	First Data Corporation	Initial Tranche B-1 Term Loan	2014/09/24	446,540	464,332
				446,540	464,332
Healthcare, Education & Childcare - 12.1%					
1,944,304	LifeCare Holdings (Rainier Acquisition Corp.)	Term Loan	2012/08/11	1,571,657	1,691,798
500,000	Rehabcare Group, Inc.	Term Loan B	2015/11/24	523,247	518,278
				2,094,904	2,210,076
Hotels, Motels, Inns & Gaming - 11.9%					
4,000,000	Fontainebleu Florida Hotel, LLC / Fontainebleau Florida Tower 2, LLC	Tranche C Term Loan Term B Delayed Draw	2012/06/06	2,730,875	1,341,888
307,157	VML US Finance LLC (aka Venetian Macau)	Project Loan	2012/05/25	312,818	304,136
531,768	VML US Finance LLC (aka Venetian Macau)	Term B Funded Project Loan	2013/05/27	541,570	526,539
				3,585,263	2,172,563

First Trust/Highland Capital Floating Rate Income Fund II

Statement of Investment Portfolio (continued)

The Directly Held Senior Loan Portfolio as at December 31, 2009 are listed below:

Principal Par Value US \$	Sector Breakdown and Company Name	Facility	Maturity Date	Average Cost \$	Fair Value \$
	Personal and Non Durable Consumer Products (Mfg. Only) - 5.6%				
1,000,000	Revlon Consumer Products Corporation	Term Loan	2012/01/15	1,021,347	1,021,767
				1,021,347	1,021,767
	Personal Transportation - 5.0%				
945,427	Remy International, Inc.	First Lien Tranche B Term Loan	2013/12/06	872,663	906,892
				872,663	906,892
	Printing and Publishing - 2.6%				
500,000	Cengage Learning Acquisitions, Inc. (Thomson Learning)	Term Loan	2014/07/03	450,468	476,999
				450,468	476,999
	Retail Stores - 7.7%				
1,000,000	Burlington Coat Factory Warehouse Corporation	Term Loan	2013/05/28	977,119	967,976
500,000	Guitar Center, Inc.	Term Loan	2014/10/09	439,879	441,617
				1,416,998	1,409,593
	Telecommunications - 2.8%				
500,000	Digicel International Finance Limited	Tranche A	2012/03/30	499,037	501,898
				499,037	501,898
	Utilities - 6.3%				
967,500	Coletto Creek Power, LP (aka Coletto Creek WLE, LP)	Second Lien Term Loan	2013/06/28	686,952	730,281
865,081	Mirant Americas Development Capital, LLC	Holdback - Term Loan A	2020/01/01		
122,107	Mirant Americas Development Capital, LLC	Holdback - Term Loan B	2020/01/01		
12,813	Mirant Americas Development Capital, LLC	Holdback - Term Loan C	2020/01/01		
2,000,000	Mirant Corporation	Holdback - 03 REV	2020/01/01		
500,000	Texas Competitive Electric Holdings Company, LLC (TXU)	Initial Tranche B-2 Term Loan	2014/10/10	412,288	425,892
				1,099,240	1,156,173
	Total Senior Floating Rate Interests			18,299,909	17,662,969
	Bonds - 1.4%				
399,000	Wellman Holdings, Inc, 5.000%		2019/01/29	264,996	250,975
				264,996	250,975
	Equities - 1.8%				
	Cargo Transport - 0.5%				
2,008	SIRVA Worldwide, Inc.			98,123	92,676
				98,123	92,676
	Chemical, Plastic & Rubber - 1.3%				
20,650	Panda Hereford Ethanol, L.P.			245,872	235,968
389	Wellman Holdings, Inc.			-	-
				245,872	235,968
	Total Equities			343,995	328,644
	Total Directly Held Senior Floating Rate Interests and Equities and Bonds - 100%			18,908,900	18,242,588

NOTES TO FINANCIAL STATEMENTS

For the years ended December 31, 2009 and 2008

1. The Fund

First Trust/Highland Capital Floating Rate Income Fund II (the "Fund") is an investment trust established under the laws of the Province of Ontario.

The Fund was established on May 16, 2005.

FT (NSI) Management Co., a wholly-owned subsidiary of First Defined Portfolio Management Co. and an affiliate of First Trust Advisors L.P. (the "Advisor"), is the Manager and Trustee of the Fund and is responsible for providing or arranging for the provision of administrative services required by the Fund and for engaging and monitoring the Advisor. Highland Capital Management L.P. (the "Sub-Advisor") has been retained by the Advisor to act as the sub-advisor to the Fund and First Trust/Highland Capital Senior Loan Trust (the "SLT") and will actively manage the Senior Loan Portfolio (as defined below) and the SLT.

The investment objectives of the Fund are to: (i) provide holders of units with monthly distributions which will fluctuate with changes in U.S. short-term interest rates; and (ii) preserve and potentially enhance the net asset value of the Fund.

The Fund's investment objective and strategies were changed on August 18, 2009 in connection with the merger of the Fund with First Trust/Highland Capital Floating Rate Income Fund ("Fund I"). The declaration of trust of the Fund was amended and restated on that date. Prior thereto, the Fund invested in accordance with the Common Share Portfolio Investment Strategy (as described below) only.

The investment strategy of the Fund is to invest its assets in a common share portfolio (the "Common Share Portfolio") and a senior loan portfolio (the "Senior Loan Portfolio") in accordance with the Common Share Portfolio Investment Strategy and Senior Loan Portfolio Investment Strategy set out below. The Advisor allocates the assets of the Fund between the two investment strategies in its discretion.

Pursuant to its Common Share Investment Strategy, the Fund obtains exposure to SLT, an investment trust established under the laws of Ontario and a reporting issuer under the *Securities Act* (Quebec), by virtue of one or more forward transactions (collectively, the "Forward Agreement") with The Bank of Nova Scotia and/or such other Canadian financial institutions or their affiliates (the "Counterparty"). The Fund does not invest directly in the SLT. As a result of this structure, the returns of the Fund's Common Share Portfolio are intended to correlate with an investment in the SLT. The portfolio of the SLT consists primarily of senior secured floating rate interest loans ("Senior Loans") of U.S. issuers.

The Common Share Portfolio of the Fund consists of common shares of Canadian companies. Under the Forward Agreement, the Fund will be entitled to sell securities in the Common Share Portfolio from time to time to fund monthly distributions, redemptions and repurchases of units, its operating expenses and other liabilities and general liquidity requirements. The purchase price payable by the Counterparty is calculated by reference to the redemption proceeds of a notional investment (the "Notional Investment") in units of the SLT at the time of the closing of the initial public offering of an amount equal to the net proceeds of the offering. The Notional Investment is reduced proportionately to reflect the redemption and repurchase of Units.

Pursuant to the Fund's Senior Loan Portfolio Investment Strategy, the Senior Loan Portfolio is invested primarily in a portfolio of Senior Loans issued by debtors that are primarily United States issuers. The Fund may also invest to a limited extent in U.S. dollar denominated Senior Loans of non-U.S. issuers and special situation investments such as securities of distressed issuers.

2. Summary of Significant Accounting Policies

These financial statements have been prepared in accordance with Canadian generally accepted accounting principles. The following is a summary of significant accounting policies followed by the Fund in the preparation of the financial statements.

NOTES TO FINANCIAL STATEMENTS *(continued)*

For the years ended December 31, 2009 and 2008

2. Summary of Significant Accounting Policies *(continued)*

(a) (i) Adoption of New Accounting Standard

Effective on January 1, 2009, the Fund adopted the recent amendments to CICA 3862, Financial Instruments – Disclosures. Disclosures about fair value of financial instruments, requiring the additional disclosure of the estimated fair value of financial instruments. The fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. The Fund's financial instruments are recorded at fair value or at amounts that approximate fair value in the financial statements.

This amendment to CICA 3862, Financial Instruments – Disclosures, establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The CICA 3862 amendments do not affect the valuation of assets and liabilities held by the Fund, but does result in enhanced and increased disclosure requirements. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurement) and the lowest priority to unobservable inputs (level 3 measurements). The three levels of the fair value hierarchy are as follows.

Level 1 Inputs that reflect unadjusted quoted prices in active markets for identical assets or liabilities that the Advisor has the ability to access at the measurement date.

Level 2 Inputs other than quoted prices that are observable for the asset or liability either directly or indirectly, including inputs in markets that are not considered to be active.

Level 3 One or more significant pricing inputs are unobservable for the financial asset or liability and include situations where there is little, if any, market activity for the financial asset or liability. The inputs into the determination of fair value require significant management judgment or estimation.

(ii) Credit Risk and the Fair Value of Financial Assets and Financial Liabilities

Effective January 1, 2009, the Fund adopted EIC-173 – Credit Risk and the Fair Value of Financial Assets and Financial Liabilities (“EIC-173”). EIC-173 clarifies how the Fund's own credit risk and counterparty credit risk should be taken into account in determining the fair value of financial assets and financial liabilities, including derivatives.

(b) Cash and Cash Equivalents

Cash and cash equivalents consist of cash on deposit and short-term investments, which are interest bearing notes with a term to maturity of less than three months from the date of purchase, and overdrafts.

(c) Valuation of Investments

The Senior Loans in the SLT and the Senior Loan Portfolio are not listed on any securities exchange or board of trade. Senior Loans are typically bought and sold by institutional investors in individually negotiated private transactions that function in many respects like an over-the-counter secondary market, although typically no formal market-makers exist. This market, while having grown substantially in the past several years, generally has fewer trades and less liquidity than the secondary market for other types of securities. Some Senior Loans have few or no trades, or trade infrequently, and information regarding a specific Senior Loan may not be widely available or may be incomplete. Accordingly, determinations of the fair value of Senior Loans may be based on infrequent and dated information. Because there is less reliable, objective data available, judgment and estimates may play a greater role in valuation of Senior Loans than for other types of securities.

Senior Loans with readily available quotations are valued at fair value using the current bid price quotations provided by Loan Pricing Corporation or another prominent pricing service. Senior Loans for which current quotations are not readily available are valued at fair value as determined by the Sub-Advisor.

NOTES TO FINANCIAL STATEMENTS *(continued)*

For the years ended December 31, 2009 and 2008

2. Summary of Significant Accounting Policies *(continued)*

(d) Forward Agreement

The value of the Forward Agreement on any date shall be the gain or loss with respect thereto that would be realized, as of the date, if the positions in the Forward Agreement were to be closed out in accordance with its terms, in which case the value shall be based on the current market value of the underlying securities using the closing sale prices on the Toronto Stock Exchange ("TSX"). If no sale has taken place on that day, the value of the Forward Agreement will be the average of the bid and ask price of the underlying securities. The value takes into account the value of other assets including cash, prepaids and distributions declared less the liabilities attributed to the Forward Agreement on such date.

The unrealized appreciation (depreciation) on the Forward Agreement (which is the difference between the net asset value of the SLT and the market value of the Common Share Portfolio), realized gains on partial settlement of the Forward Agreement and the Forward Agreement fees are included in the net gain on the Forward Agreement in the Statement of Operations.

(e) Investment Transactions and Income Recognition

All investment transactions are accounted for on the trade date. Realized gains and losses from investment transactions and unrealized appreciation or depreciation in the value of investments are calculated on an average cost basis. Interest income and expenses are recognized daily on an accrual basis. Dividend income is recognized on the ex-dividend date.

(f) Foreign Currency Translation

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

(g) Foreign Currency Forward Contract

The value of the foreign currency forward contract of the SLT that was in place until November 13, 2009 was the gain or loss that would be realized if, on a Valuation Date (the date upon which the net asset value ("NAV") per Unit is calculated and which is Friday of each week, or if any Friday is not a Business Day, the immediately preceding Business Day, and the last Business Day of each month, and includes any other date on which the Manager elects, in its discretion, to calculate the NAV per Unit), the position in the forward contract was closed out in accordance with its terms. The unrealized gains or losses on the forward contract were reported as part of any change in unrealized appreciation or depreciation of the forward contract in the Statement of Operations.

(h) Net Asset Value (or NAV) per Unit

NAV is calculated by the Valuation Agent (CIBC Mellon Global Securities Services Company) on each Valuation Date, by subtracting the aggregate amount of the liabilities of the Fund from the total assets of the Fund. NAV per Unit is calculated by dividing the NAV by the number of units outstanding at that time.

(i) Accounting Estimates

The preparation of financial statements in accordance with Canadian generally accepted accounting principles requires the Manager to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of increases and decreases in net assets from operations during the reporting period. Actual results could differ from those estimates. The most significant estimates relate to the valuation of investments.

(j) Transaction Costs

Transaction costs are not incurred on transactions in the Common Share Portfolio and in the Senior Loan Portfolio.

NOTES TO FINANCIAL STATEMENTS (continued)

For the years ended December 31, 2009 and 2008

3. Fair Value Disclosures

The Fund's assets recorded at fair value have been categorised based upon a fair value hierarchy in accordance with the amendments to CICA 3862. See Note 2 for a discussion of the Fund's policies regarding CICA 3862 and this hierarchy. The following fair value hierarchy table presents information about the Fund's assets measured at fair value on a recurring basis as at December 31, 2009.

	Financial Assets at Fair Value as at December 31, 2009			
	Level 1	Level 2	Level 3	Total
Senior loans	\$ -	\$ 14,481,836	\$ 3,181,133	\$ 17,662,969
Bonds	-	-	250,975	250,975
Short-term Investments	3,271,848	-	-	3,271,848
Equities	13,257,767	-	328,644	13,586,411
Forward contracts excluding currency	-	-	(4,524,229)	(4,524,229)
Total	\$ 16,529,615	\$ 14,481,836	(\$ 763,477)	\$ 30,247,974

For the year ended December 31, 2009, there were no transfers of investments between level 1 and level 2.

Reconciliation of financial asset and liability movement – Level 3

The following table shows a reconciliation of all movements in the level 3 financial assets and liabilities from January 1, 2009 until December 31, 2009:

Classification	Balance, Jan. 1, 2009	Purchases	Sales	Net transfers	Realized gains/ (losses)	Change in unrealized appreciation/ (depreciation)	Balance, Dec. 31, 2009	Total change in unrealized appreciation (depreciation) for assets held at the end of the year
Financial Assets								
Senior Loans	\$ -	\$ 4,505,467	\$ (201,517)	\$ -	\$ 51,827	\$ (657,359)	\$ 3,432,108	\$ (790,513)
Bonds	-	-	-	-	-	-	-	-
Equities	-	343,994	-	-	-	(15,350)	328,644	(15,350)
Forward contracts excluding currency	2,417,779	-	-	-	-	(6,942,008)	(4,524,229)	(6,942,008)
Total Financial Assets	\$ 2,417,779	\$ 4,849,461	\$ (201,517)	\$ -	\$ 51,827	\$ (7,614,717)	\$ (763,477)	\$ (7,747,871)
Financial Liabilities								
Senior Loans	-	-	-	-	-	-	-	-
Bonds	-	-	-	-	-	-	-	-
Equities	-	-	-	-	-	-	-	-
Total Financial Liabilities	-	-	-	-	-	-	-	-
Total Financial Assets and Liabilities	\$ 2,417,779	\$ 4,849,461	\$ (201,517)	\$ -	\$ 51,827	\$ (7,614,717)	\$ (763,477)	\$ (7,747,871)

Fair values of certain level 3 instruments are based on broker quotes and other unobservable borrower specific information and therefore no possible alternative assumptions could be applied to the valuations.

NOTES TO FINANCIAL STATEMENTS (continued)

For the years ended December 31, 2009 and 2008

4. Forward Agreement

To provide the Fund with the means to meet its investment objectives, pursuant to the Common Share Investment Strategy, the Fund entered into the Forward Agreement with the Counterparty, pursuant to which the Counterparty will pay the Fund on the termination date of the Fund, as the purchase price of the Common Share Portfolio an amount equal to 100% of the redemption proceeds of a corresponding number of units of the SLT. The Fund will partially settle the Forward Agreement prior to the termination date in order to fund monthly distributions as well as redemption of Units by Unitholders from time to time and expenses of the Fund. The Forward Agreement is unconditionally guaranteed by the Counterparty, a company with a credit rating as at December 31, 2009 of AA (low) as rated by the Dominion Bond Rating Service.

The value of the Forward Agreement is primarily derived from the difference between the fair value of the Common Share Portfolio which will be delivered to the Counterparty and the fair value of the SLT which will be received from the Counterparty pursuant to the terms of the Forward Agreement. The value of the Fund's investments, which includes the Common Share Portfolio and the Forward Agreement, is equal to the Transactional NAV (net asset value) of the SLT and the Senior Loan Portfolio. The shares in the Common Share Portfolio are valued at the closing price in accordance with the terms of the Forward Agreement and its value is reflected through the valuation of the Forward Agreement. (See Note 12 for related discussion on net assets and net asset value).

The Fund has legal title to the Common Share Portfolio. As explained above, the Fund has no interest in the net assets of the SLT but obtains exposure to them only through the Forward Agreement.

The following shares are all the securities in the Common Share Portfolio as at December 31, 2009:

Number of Shares	Issuer Name	Average Cost (\$)	Fair Value (\$)
15,857	ATS Automation Tooling Systems Inc.	80,078	118,610
148,962	Celestica Inc.	1,000,028	1,483,662
195,322	CGI Group Inc., Class 'A'	1,683,663	2,781,385
66,068	Eldorado Gold Corp.	400,373	985,735
7,058	FirstService Corp.	211,958	143,277
30,984	FNX Mining Co. Inc.	926,422	358,175
34,683	Galleon Energy Inc., Class 'A'	570,535	182,779
44,674	Gildan Activewear Inc.	693,644	1,148,123
79,556	Ivanhoe Mines Ltd.	716,004	1,233,914
62,110	Nuvista Energy Ltd.	1,069,530	775,133
18,788	Petrobank Energy & Resources Ltd.	989,753	962,133
6,798	Research in Motion Ltd.	228,704	482,862
67,263	RONA Inc.	1,240,499	1,039,213
137,498	UTS Energy Corp.	570,617	313,495
100,829	WestJet Airlines Ltd.	1,103,070	1,249,271
Total Common Share Portfolio		11,484,878	13,257,767

5. Taxation

The Fund is subject to tax in each taxation year under Part I of the *Income Tax Act* (Canada) (the "Tax Act") on the amount of its income for the year, including the taxable portion of net realized capital gains, less the portion thereof that it deducts in respect of the amounts paid or payable to Unitholders in the year. The Fund intends to deduct, in computing its income in each taxation year, the full amount available for deduction in each year and, therefore, provided the Fund makes distributions in each year of its net income and net realized capital gains, it will generally not be liable in such year for income tax under Part I of the Tax Act. As at December 31, 2009, the Fund had a capital loss of \$1,058,492 that can be applied to offset capital gains in subsequent years. As at December 31, 2009, the Fund had a non-capital loss of \$5,508,552 of which \$1,564,279 expires in 2015, \$756,405 expires in 2026, \$1,719,142 expires in 2027 and \$1,468,726 expires in 2029.

NOTES TO FINANCIAL STATEMENTS (continued)

For the years ended December 31, 2009 and 2008

6. Expenses of the Fund

(a) Management Fees

The Manager manages the on-going business and administrative affairs of the Fund. As compensation for its management services rendered to the Fund, the Manager is entitled to receive an annual management fee from the Fund equal to 0.75% of Managed Assets (as defined below) calculated and payable monthly in arrears plus applicable taxes and an amount equal to the Service Fee payable to registered dealers. A service fee of 0.40% is calculated and paid to registered dealers whose clients hold units of the Fund at the end of each quarter based on the net asset value of the Fund held by clients of the dealer. The Manager is responsible for payment of fees to the Advisor. The Advisor is responsible for payment of fees to the Sub-Advisor. "Managed Assets" means, in respect of any particular month, the average daily gross asset value of the Fund during such month (including assets attributable to the principal amount of borrowings) minus the sum of the accrued liabilities of the Fund outstanding as at the end of such month (other than the principal amount of any borrowings incurred) and minus the value of the Common Share Portfolio and the fair market value of the Forward Agreement. In this regard, if the Fund uses leverage in an amount equal to 100% of its pre-leverage net assets, the Management Fee will be 1.5% of net assets of the Fund.

(b) Forward Agreement Fees

The amounts payable by the Counterparty to the Fund under the Forward Agreement will be reduced by approximately 0.45% per annum on the value of the Notional Investment in units of the SLT and 0.15% per annum on the value of the Common Share Portfolio. This reduction occurs in arrears on the 10th Business Day of each month.

(c) Other Expenses

The Fund incurs expenses in connection with its operation and administration. These expenses include, without limitation: mailing and printing expenses for periodic reports to Unitholders; fees that may be payable to the Valuation Agent for performing certain valuation services; fees payable to the custodian for acting as Custodian of the assets of the Fund; fees payable to the transfer agent and registrar for performing certain financial, record-keeping, reporting and general administrative services; fees payable to the auditors and legal advisors; on-going regulatory filing fees and other fees; and any reasonable out-of-pocket expenses incurred by the Manager or its agents in connection with their on-going obligations to the Fund. The Fund is responsible for any taxes payable by the Fund or to which the Fund may be subject, for interest expense on borrowings, and for expenses relating to portfolio transactions, as well as any extraordinary expenses which may be incurred from time to time.

7. Unitholders' Equity

The Fund is authorized to issue an unlimited number of a single class of transferable, redeemable units, each of which represents an equal, undivided beneficial interest in the net assets of the Fund. Units are freely transferable, except as provided in the Declaration of Trust of the Fund or as otherwise restricted by the Manager in order to comply with any applicable laws, regulations or other requirements imposed by regulatory authorities or to obtain, maintain or renew any licenses, rights, status or powers pursuant to any applicable laws, regulations or other requirements imposed by any stock exchange or other applicable regulatory authorities.

	December 31, 2009					December 31, 2008			
	Balance beginning of year	Issuance	Repurchases	Redemptions	Balance end of year	Balance beginning of year	Repurchases	Redemptions	Balance end of year
Units	4,004,885	3,576,733	(122,400)	(2,140,226)	5,318,992	6,088,857	(121,100)	(1,962,872)	4,004,885
Dollars		\$ 19,131,525	\$ (565,705)	\$ (11,903,766)		\$ (740,956)	\$ (14,760,373)		

On August 18, 2009, the Fund acquired the assets and assumed the liabilities of First Trust/Highland Capital Floating Rate Income Fund (the "Terminating Fund"). The Fund acquired total net assets of the Terminating Fund in the amount of \$19,131,525 in exchange for 3,576,733 units of the Fund. The Terminating Fund distributed the units of the Fund received to its unitholders. The financial statements do not include the operating results of the Terminating Fund prior to the merger.

NOTES TO FINANCIAL STATEMENTS *(continued)*

For the years ended December 31, 2009 and 2008

7. Unitholders' Equity *(continued)*

Subject to the limit on redemptions, Units may be surrendered for redemption not more than 60 days, and at least 30 days, prior to the last Business Day in June of any year (the "Annual Redemption Date"), to CIBC Mellon Trust Company for a redemption price (the "Annual Redemption Price") equal to the NAV per unit on that date less any expenses incurred by the Fund (including those incurred to partially settle the Forward Agreement and brokerage costs). Units properly surrendered for redemption will be redeemed as at such Annual Redemption Date and the unitholder will receive payment in respect of such units on or before the tenth Business Day following such date. The maximum number of units that can be redeemed on each Annual Redemption Date in 2010 and 2011 is 10% of the units outstanding on the applicable Annual Redemption Date.

In addition to the annual redemption right, Units may be surrendered for redemption at least 20 Business Days prior to the second last Business Day of each month, (the "Monthly Redemption Date"). Unitholders whose units are redeemed on any Monthly Redemption Date will receive a redemption price per Unit (the "Monthly Redemption Price") equal to the lesser of (i) 95% of the weighted average trading price of the units on the TSX for the 10 trading days prior to the redemption date, and (ii) 100% of the closing price of the units on the TSX (or if there was no trade on such date, the average of the last bid and ask price) on the applicable Monthly Redemption Date less, in each case, any costs associated with the redemption, including expenses related to partial settlement of the Forward Agreement and brokerage costs.

Units surrendered on the date that falls within both an annual redemption notice period and a monthly redemption notice period will be deemed to be surrendered for the Annual Redemption Price. A redemption notice submitted during the annual notice period in 2010 and 2011 shall indicate whether any units that cannot be redeemed for the Annual Redemption Price shall be (i) returned to the holder or (ii) redeemed at the Monthly Redemption Price.

The Fund may suspend redemptions of Units or payment of redemption proceeds in certain circumstances. In addition, under the Forward Agreement, if the SLT suspends redemptions or otherwise does not pay redemption proceeds, the Counterparty will suspend payment in respect of a settlement of the Forward Agreement until such time as such redemptions are reinstated. In such circumstances, the Fund may be unable to pay the redemption proceeds in respect of Units tendered for redemption.

8. Termination of the Fund

The Fund will terminate operations on May 31, 2015 (the "Termination Date") and the net assets will be distributed pro-rata to Unitholders unless an alternative termination date is chosen in accordance with the Declaration of Trust.

9. Foreign Currency Forward Contract

The SLT entered into a 10 year forward foreign currency contract on May 31, 2005 to hedge at least 90% of its U.S. currency risk from U.S. dollar denominated investments, back to the Canadian dollar. On March 12, 2009, the SLT reduced the original notional value of the forward contract by \$9,855,813, from \$40,753,850 to \$30,898,037 at an exchange rate of \$1.24 with an expected maturity of May 29, 2015. A loss of \$45,934 was realized as a result of this reduction and was reflected in the June 30, 2009 financial statements of the SLT. Subsequently, on July 14, 2009, the SLT further reduced the original notional value of the forward contract by \$20,358,037, from \$30,898,037 to \$10,540,000. A gain of \$1,280,533 was realized as a result of this reduction and was reflected in the June 30, 2009 financial statements of the SLT. In addition, a gain of \$1,080,727 was realized as a result of the full unwind of the forward contract on November 13, 2009. A Schedule 1 Canadian bank was the counterparty to the forward contract.

On August 18, 2009, the Fund acquired the assets of the Terminating Fund including a forward foreign currency contract of the Terminating Fund. On November 13, 2009, the Fund fully unwound this forward contract. A gain of \$2,224,410 was realized as a result of the full unwind. A Schedule 1 Canadian bank was the counterparty to the forward contract.

NOTES TO FINANCIAL STATEMENTS (continued)

For the years ended December 31, 2009 and 2008

10. Leverage

Each of the Fund or SLT may borrow an amount representing not more than 100% of the value of its pre-leverage net assets under a credit facility. The Senior Loan Trust's initial leverage was repaid in full on July 18, 2008. Effective July 31, 2008, the SLT's credit facility was terminated by the lender. Prior to its termination, the SLT paid interest, program and standby fees to the lender under its credit facility on a monthly basis. For the year ending December 31, 2009, interest and fees incurred totaled nil (2008: \$688,957).

11. Distributions

The Fund endeavors to make monthly cash distributions to Unitholders. However, it suspended distributions in May, 2009. The amount of distributions in any particular month will be determined by the Manager, having regard to the investment objectives of the Fund, the net realized capital gains and net income of the Fund, if any, during the month and in the year to date, the net realized capital gains and net income of the Fund anticipated in the balance of the year, distributions made in previous months and the current market environment. Monthly cash distributions over the life of the Fund will be derived from the proceeds of disposition of the Senior Loan Portfolio and Common Share Portfolio securities. The proceeds from the Common Share Portfolio will be received by the Fund from the Counterparty under the Forward Agreement. Distributions, if any, paid to Unitholders will be comprised of the Fund's net income and distributions from the SLT. Distributions from the SLT will be derived primarily from net income earned on the Senior Loan Portfolio and, in certain circumstances, from net gains from dispositions of investments in the Senior Loan Portfolio and, as a result, will fluctuate from month to month. Under the Forward Agreement, if the SLT suspends redemptions or fails to pay distributions on its units corresponding to the Fund's targeted distributions, the Counterparty will suspend payment in respect of a partial settlement until such time as such redemptions and distributions are reinstated. In such circumstances, the Fund would be unable to pay its targeted distributions.

If in any year after its monthly distributions, there would otherwise remain in the Fund additional net income or net realized capital gains, the Fund intends to make, on or before December 31st of that year, a special distribution, paid in Units unless the Manager otherwise determines, of such portion of the remaining net income and net realized capital gains as is necessary to ensure that the Fund will not be liable for income tax thereon under the *Income Tax Act*.

12. Reconciliation of Net Asset Value

The Canadian securities regulatory authorities amended National Instrument NI 81-106 effective September 8, 2008 to remove the requirement that net asset value for redemptions and subscriptions of units ("Transactional Net Asset Value") be calculated in accordance with Canadian GAAP. As a result of the amendments, the Transactional Net Asset Value of the Fund will continue to be calculated based on the fair value of investments using the close or last trade price of portfolio securities. The Net Assets per unit for financial reporting purposes (the "GAAP Net Assets") and the Transactional Net Asset Value per unit could be different due to the use of different valuation techniques. The Common Shares in the Common Share Portfolio are valued at the closing price in accordance with the terms of the Forward Agreement and the Common Share Portfolio's value is reflected through the valuation of the Forward Agreement. Therefore, there is no difference between net asset value and net assets.

The Transactional Net Asset Value per unit of the Fund at December 31 and the difference between the GAAP Net Assets and Transactional Net Asset Value is as follows:

	December 31, 2009	December 31, 2008
Transactional Net Asset Value per unit	\$5.24	\$5.51
Adjustment	(0.07)	(0.01)
GAAP Net Assets per unit	\$5.31	\$5.50

NOTES TO FINANCIAL STATEMENTS (continued)

For the years ended December 31, 2009 and 2008

13. Financial Risk Management

Through the Senior Loan Portfolio and Forward Agreement described in Note 4, the Fund is exposed to its own investments and the investments of the SLT, which consist of cash, short-term investments, senior loan investments and payables. As a result, the Fund is exposed to various types of risks that are associated with its investment strategies, financial instruments and the markets in which it invests. These risks and related management practices employed by the Fund and SLT are discussed below and are consistent with prior years.

Foreign currency exposure

Net asset value (or NAV) is measured in Canadian dollars and payments to Unitholders will be made in Canadian dollars. However, most of the Senior Loan Portfolio and SLT's investments are in Senior Loans denominated in U.S. dollars. Accordingly, the Fund's and SLT's NAVs and their abilities to make payments to Unitholders may be affected by fluctuations in the value of the Canadian dollar relative to the U.S. dollar. The Fund and the SLT intend to use foreign currency contracts to hedge its U.S. currency exposures to the Canadian dollar. There can be no assurance that such hedging strategies will be successful. The Fund and the SLT did not have foreign currency forward contracts in place as of December 31, 2009.

The table below shows the Fund's U.S. dollar holdings:

	December 31, 2009		December 31, 2008	
	Currency risk exposed holdings	As a % of Net Assets	Currency risk exposed holdings	As a % of Net Assets
U.S. Dollar	\$21,490,791	76.26	Nil	Nil

As at December 31, 2009, had the Canadian dollar strengthened or weakened by 5% in relation to the U.S. dollar, with all other variables held constant, the Fund's net assets would have decreased or increased, respectively, by approximately \$1,074,540 (2008: nil).

The table below shows the SLT's U.S. dollar holdings.

	December 31, 2009		December 31, 2008	
	Currency risk exposed holdings	As a % of Net Assets	Currency risk exposed holdings	As a % of Net Assets
U.S. Dollar	\$8,996,830	104.40	\$19,629,234	90.43

As at December 31, 2009, had the Canadian dollar strengthened or weakened by 5% in relation to the U.S. dollar, with all other variables held constant, the SLT's net assets would have decreased or increased, respectively, by approximately \$449,842 (2008: \$981,462).

Interest Rate Risk

The Fund invests in interest-bearing securities. As a result, the income of the Fund may be affected by changes in interest rates relevant to particular securities or as a result of the Manager being unable to secure similar returns on the expiry or sale of securities.

In addition, the price of interest-bearing securities will also fluctuate with interest rate changes. The SLT and Senior Loan Portfolio primarily hold Senior Loans that have an interest rate reset period of approximately 31 days and 40 days, respectively. As a result, the Fund is not exposed to a significant risk, relative to a fixed rate fund, that the Net Asset Value of the Fund will fluctuate due to changes in the prevailing levels of market interest rates.

NOTES TO FINANCIAL STATEMENTS (continued)

For the years ended December 31, 2009 and 2008

13. Financial Risk Management (continued)

Interest Rate Risk (continued)

The table below summarizes the Fund's exposure to interest rate risk. It includes the Fund's assets and trading liabilities at fair values, categorized by the earlier of contractual re-pricing or maturity dates.

	December 31, 2009			Total \$
	Less than 1 month \$	30-90 days \$	Non-interest bearing \$	
Assets				
Short-term investments	3,271,848	-	-	3,271,848
Investments, at fair value	-	13,450,112	13,526,014	26,976,126
Other assets	84,599	-	108,639	193,238
Total Assets	3,356,447	13,450,112	13,634,653	30,441,212
Liabilities				
Bank Overdraft	-	-	-	-
Other Liabilities	-	-	2,563,764	2,563,764
Total Liabilities	-	-	2,563,764	2,563,764
Net Interest Rate Exposure	3,356,447	13,450,112	11,070,889	27,877,448

Credit Risk

The Fund's ability to pay distributions is dependent upon the performance of the Fund's assets. That performance, in turn, is subject to a number of risks, and in particular, the credit risk of the Senior Loans held by the Senior Loan Portfolio and the SLT. Credit risk is the risk of non-payment of scheduled interest and/or principal payments. Credit risk is also the risk that one or more investments in the portfolio of the Senior Loan Portfolio and/or of the SLT will decline in price, or fail to pay interest or principal when due, because the issuer of the security experiences a decline in its financial status. The value of Senior Loans is affected by the creditworthiness of borrowers and by general economic and specific industry conditions. If the Senior Loan Portfolio and/or the SLT acquire a Senior Loan from another lender, for example, by acquiring a participation, the Senior Loan Portfolio and/or the SLT may also be subject to credit risks with respect to that lender. As at December 31, 2009, the maximum credit risk exposure of the Fund is \$26,498,009.

As at December 31, 2009, the Senior Loan Portfolio and SLT invested in Senior Loans and other debt securities with the following credit rating:

	December 31, 2009	December 31, 2008
Debt securities by Moody rating	% of Net Assets	% of Net Assets
B1	18.87%	26.57%
B2	18.99%	16.72%
B3	12.60%	9.57%
Ba2	10.20%	9.42%
Ba3	14.20%	21.78%
Baa3	-	6.89%
Caa1	11.66%	-
Caa2	2.06%	-
Caa3	0.74%	1.38%
Not Rated	10.68%	7.67%
Total	100.00%	100.00%

NOTES TO FINANCIAL STATEMENTS *(continued)*

For the years ended December 31, 2009 and 2008

13. Financial Risk Management *(continued)*

Liquidity Risk

Liquidity risk is the possibility that investments in the Fund cannot be readily converted into cash when required. The Fund is exposed to liquidity risk as the resale, or secondary market, for Senior Loans held by the Fund or the SLT is limited. There is no organized exchange or board of trade on which Senior Loans are traded. Instead, the secondary market for Senior Loans is an unregulated inter-dealer or inter-bank resale market. The secondary market has limited transparency so that information about actual trades may be difficult to obtain. Accordingly, some of the Senior Loans in which the Fund and the SLT invest may be relatively illiquid. Illiquid securities may be difficult to dispose of at a fair price and/or at a time when the Fund or SLT believes it is desirable to do so. In addition, the market price of illiquid securities generally is more volatile which may affect the price of the security. As of December 31, 2009, the Fund had significant liquidity risk. This impacts portfolio diversification and the risk-adjusted return of the Fund.

The units of the Fund may be redeemed on monthly and annual redemption dates. Subject to the limits on redemption in 2010 and 2011, the units of the Fund may be redeemed on the Annual Redemption Date (refer to Note 7) at the current Net Asset Value per unit at the option of the unitholder. The Fund may also repurchase units. Subject to certain exceptions, the units of the Fund are repurchased by the Manager pursuant to a mandatory market repurchase program when the difference between the Net Asset Value per unit and market price of the unit is more than 5% (See Note 14).

Market and Other Price Risk

Market and other price risk is the risk that the value of financial instruments will fluctuate as a result of changes in market prices (other than those arising from interest rate or currency risk), whether caused by factors specific to an individual investment, or factors affecting all instruments traded in a market. The Manager moderates this risk through a careful selection and diversification of securities and other financial instruments in accordance with the Fund's investment mandate which outlines its objectives and strategy.

Although the Fund's Common Share Portfolio is comprised of equity securities that are subject to market risk, the Fund itself is not exposed to the market risk of the equity securities as a result of the Forward Agreement but, the Fund is subject to the market risk of the securities held by the SLT by virtue of the Forward Agreement.

14. Mandatory Repurchase Program

To enhance liquidity and to provide market support for the Units, the Fund has a mandatory market purchase program under which the Fund will, subject to certain exceptions contained in the Declaration of Trust and in compliance with any applicable regulatory requirements, be obligated to purchase for cancellation any Units offered in the market at the then prevailing market price if the price at which Units are then offered for sale is less than 95% of the NAV per Unit determined as at the close of business on the immediately preceding Business Day. The maximum number of Units to be purchased in any three month period (commencing with the three month period that began June 1, 2005) will be 1.25% of the number of Units outstanding at the beginning of such period. The Declaration of Trust provides that the Fund will not be obligated to make such purchases if, among other things, (i) the Fund lacks the cash, debt capacity or other resources to make such purchases, or (ii) in the opinion of the Manager, such market purchases would adversely affect the on-going activities of the Fund or the remaining unitholders. The Fund repurchased 122,400 (2008: 121,100) Units for cancellation during the year ended December 31, 2009 equivalent to \$565,705 (2008: \$740,956).

NOTES TO FINANCIAL STATEMENTS *(continued)*

For the years ended December 31, 2009 and 2008

15. Future Accounting Policy Changes

The Accounting Standards Board (AcSB) of the CICA has announced its intention to replace Canadian generally accepted accounting principles ("GAAP") with International Financial Reporting Standards ("IFRS") for all publicly accountable entities (which includes investment funds) effective January 1, 2011. The Manager is currently working with its service providers to develop a changeover plan and determine the impact on information systems and business arrangements. Based on a preliminary assessment, the Manager does not believe any significant changes to the Funds' information systems are required, and does not anticipate the changeover to IFRS will materially impact the Fund's existing business arrangements.

The Manager identified significant policy differences between GAAP and IFRS, but does not expect a material impact on NAV per unit on adoption. The impact of IFRS on accounting policies and implementation decisions will mainly be in the areas of additional note disclosures in the financial statements of the Fund particularly in relation to consolidation. Due to anticipated changes to International Accounting Standard 27 ("IAS 27"), the Manager cannot conclude on the impact of consolidation on the Fund.

16. Comparative Figures

Certain comparative figures have been reclassified to conform to the presentation for the year ended December 31, 2009.

