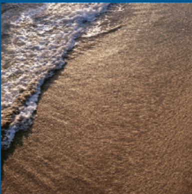
Morneau Sobeco Income Fund

2008 Second Quarter Results



MORNEAU SOBECO

Fresh thinking.
Innovative solutions.

August 13, 2008

To Our Unitholders

Morneau Sobeco Income Fund (the "Fund") is pleased to present its financial results for the period ended June 30, 2008. These results reflect the solid performance of the Fund's operating business in the quarter. Our revenue growth was 41.3% for the period, our Cash distributions increased by 7% in the quarter, and the integration and transition activities related to our acquisition of Shepell•fgi are well underway. Our organization is doing well and we continue to believe that 2008 will be another strong year for the Fund.

For the 2008 second quarter, we had revenue growth of $15.3 million to $52.4 million compared to $37.1 million for the same period in 2007. The increase in revenue was primarily due to revenue of $12.4 million related to the Fund's acquisition of Shepell•fgi. This transaction closed on June 2, 2008 and the second quarter included, for the first time, one month of results from Shepell•fgi.

Net income for the three months ended June 30, 2008 was $2.5 million compared to net income of $1.7 million for the same period in 2007.

In the quarter, EBITDA increased by $2.4 million to $10.5 million compared to $8.1 million for the same period in 2007. The EBITDA margin remained strong at 21.0% after adjusting for a salary component of $0.5 million related to our acquisition of Heath Benefits Consulting in June 2006.

On June 2nd, a subsidiary of the Fund acquired substantially all the assets of Shepell•fgi from Clairvest Group Inc. and its minority partners for total consideration of approximately $320 million payable over two years. The performance of Shepell•fgi is meeting our expectations. We are pleased with the rapid and very efficient efforts of the combined transition team at Shepell•fgi and Morneau Sobeco. Already, the Fund has created some synergies in the Finance, IT and Office Support areas. Several business initiatives have been undertaken to improve efficiencies and add measurable value to our organization.

This transaction confirms our growth efforts in the health and productivity field in Canada. As the leading Canadian provider

of Employee Assistance, Health Management, and Workplace Training and Education Programs, Shepell•fgi has deep expertise in improving workplace health and productivity. Together, Shepell•fgi and Morneau Sobeco create a dynamic new leader for the provision of human resources services to Canadian organizations.

This acquisition will also provide approximately $220 million in eligible tax deductions. As a result of the tax savings, the Fund will be favourably positioned post 2010, when the tax treatment of income funds changes.

On May 12th, the Fund announced a strategic alliance with Sibson Consulting, the human resource consulting division of The Segal Company. This announcement reflects our goal to strengthen our distribution capability in the U.S. market through alliances with firms offering complementary services. In the second quarter, Morneau Sobeco and Sibson have started to work on joint proposals and marketing initiatives for mutual and prospective clients.

In the quarter, the Fund announced an increase to its cash distribution. The June 2008 distribution, which was paid on July 15, 2008 to holders of record of Units of the Fund on June 30, 2008, reflected the previously announced 7% increase to our monthly distribution target from $0.07356 to $0.07871 per Unit.

Standardized Distributable Cash increased by $2.4 million to $8.2 million compared to $5.8 million for the same period in 2007. Adjusted Consolidated Distributable Cash (the metric focused on by management) increased by $2.5 million to $9.7 million compared to $7.2 million for the same period in 2007. The Adjusted Consolidated Distributable Cash Payout Ratio decreased by almost 10% in the second quarter of 2008, from 84.9% to 75.0%.

Management continues to have a positive outlook for 2008 in terms of our financial performance, business, and acquisition strategies.

On behalf of the Board of Trustees and management team at Morneau Sobeco Income Fund, I thank you for your continued support.

WILLIAM MORNEAU
Chairman & Chief Executive Officer

HIGHLIGHTS

QUARTERLY REVENUE INCREASED BY 41.3%
OVER SAME PERIOD IN 2007

ADJUSTED CONSOLIDATED DISTRIBUTABLE
CASH PER UNIT (BASIC) INCREASED BY 17.3%

INTEGRATION AND PERFORMANCE OF
SHEPELL•FGI IS ON TARGET

CASH DISTRIBUTIONS INCREASED BY 7%
IN THE QUARTER

MORNEAU SOBECO INCOME FUND

CONSOLIDATED BALANCE SHEETS

(Unaudited)

(In thousands of dollars)

	As at June 30, 2008	As at December 31, 2007
Assets		
Current assets:		
Cash	$ —	$ 2,898
Accounts receivable	45,799	27,855
Unbilled fees	12,205	2,067
Income taxes recoverable	1,489	388
Prepaid expenses and other	5,416	2,016
	64,909	35,224
Future income taxes (note 14)	5,901	3,258
Interest-rate swaps (note 7)	951	785
Capital assets (note 4)	16,941	10,186
Intangible assets (note 5)	304,450	115,524
Goodwill (note 6)	295,652	169,451
	$688,804	$334,428
Liabilities and Unitholders' Equity		
Current liabilities:		
Bank indebtedness (note 7)	$ 1,701	$ —
Accounts payable and accrued liabilities	36,031	12,689
Deferred revenue	3,068	807
Current portion of long-term debt (note 7)	2,300	—
Unitholder distributions payable (including non-controlling)	3,212	2,045
	46,312	15,541
Insurance premium liabilities:		
Payable to insurance companies	8,356	9,946
Less related cash and investments held	(8,356)	(9,946)
	—	—
Long-term debt (note 7)	135,162	34,913
Promissory notes (note 8)	71,928	—
Other liabilities (note 9)	6,885	—
Future considerations related to acquisition (note 3)	2,044	2,044
Future income taxes (note 14)	30,156	29,810
	292,487	82,308
Non-controlling interests (note 11)	56,120	54,452
Unitholders' equity	340,197	197,668
	$688,804	$334,428

Commitments and Contingencies (notes 3,7,18 and 19)

Robert Chisholm
Trustee,
Audit Committee Chair

William Morneau
Trustee,
Chairman and CEO

See accompanying notes to consolidated financial statements

MORNEAU SOBECO INCOME FUND

CONSOLIDATED STATEMENTS OF INCOME AND OTHER COMPREHENSIVE INCOME

(Unaudited)

(In thousands of dollars, except per unit amounts)

	Three Months Ended		Six Months Ended	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
Revenue				
Fees	$47,433	$32,289	$81,596	$63,467
Commissions	4,790	4,626	9,606	9,402
Other	140	142	295	279
	52,363	37,057	91,497	73,148
Expenses				
Salary, benefit and contractor expenses	32,428	21,574	56,765	43,247
Other operating	9,449	7,377	15,857	13,930
Amortization of capital assets (note 4)	1,015	547	1,675	1,070
Amortization of intangible assets (note 5)	5,931	3,807	9,574	7,582
Interest expenses (note 7)	1,915	315	3,006	768
	50,738	33,620	86,877	66,597
Income before income taxes and non-controlling interest	1,625	3,437	4,620	6,551
Income taxes (recovery) (note 14)				
Current	(333)	173	(49)	307
Future	(988)	1,149	(1,748)	294
	(1,321)	1,322	(1,797)	601
Income before non-controlling interest	2,946	2,115	6,417	5,950
Non-controlling interest (note 11)	(490)	(435)	(1,181)	(1,225)
Net income	2,456	1,680	5,236	4,725
Other comprehensive income				
Unrealized gain on interest rate cash flow hedges	951	—	951	—
Comprehensive income for the period	$ 3,407	$ 1,680	$ 6,187	$ 4,725
Net income per Unit (note 16)				
—Basic	$ 0.093	$ 0.076	$ 0.215	$ 0.214
—Diluted	$ 0.091	$ 0.076	$ 0.212	$ 0.214

See accompanying notes to consolidated financial statements

MORNEAU SOBECO INCOME FUND

CONSOLIDATED STATEMENTS OF CHANGES IN UNITHOLDERS' EQUITY

For the six months ended June 30, 2008
(Unaudited)
(In thousands of dollars)

	Unitholders' Capital	Accumulated Other Comprehensive Income (Loss)	Deficit	Total
Balance, December 31, 2006	$210,607	$ —	$ (6,988)	$203,619
Exchange of Class B LP Units	1,226	—	—	1,226
Net income for the period	—	—	12,120	12,120
Distributions	—	—	(19,297)	(19,297)
Balance, December 31, 2007	$211,833	$ —	$(14,165)	$197,668
Exchange of Class B LP Units (note 11)	1,626	—	—	1,626
Issuance of Units (note 10)	153,000	—	—	153,000
Units issuance costs, net of future income tax benefits (note 10)	(7,316)	—	—	(7,316)
Net income for the period	—	—	5,236	5,236
Comprehensive income for the period	—	951	—	951
Distributions (note 12)	—	—	(10,968)	(10,968)
Balance, June 30, 2008	$359,143	$951	$(19,897)	$340,197

See accompanying notes to consolidated financial statements

MORNEAU SOBECO INCOME FUND

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(In thousands of dollars)

	Three Months Ended		Six Months Ended	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
Cash provided by (used in):				
Operating activities				
Net income	$ 2,456	$ 1,680	$ 5,236	$ 4,725
Items not involving cash:				
Amortization of capital assets	1,015	547	1,675	1,070
Amortization of intangible assets	5,931	3,807	9,574	7,582
Amortization of debt issue costs (note 7)	108	13	121	26
Amortization of leasehold inducement	37	—	37	—
Non-controlling interest of Class B LP Units	490	435	1,181	1,225
Future income taxes	(988)	1,149	(1,748)	294
Salary component of Heath acquisition (note 3(c))	518	300	758	520
Accretion on promissory notes (note 7)	570	—	570	—
Fair value of interest-rate swap agreements (note 7)	86	(132)	785	(68)
	10,223	7,799	18,189	15,374
Change in non-cash operating working capital (note 17)	305	124	(7,717)	(8,483)
	10,528	7,923	10,472	6,891
Financing activities				
Issuance of units (note 10)	153,000	—	153,000	—
Expenses related to issuance of units (note 10)	(10,467)	—	(10,467)	—
Proceeds from long-term debt (note 7)	137,000	—	137,000	—
Repayment of term loan (note 7)	(35,000)	—	(35,000)	—
Deferred financing cost (note 7)	(1,875)	—	(1,875)	—
Operating line of credit (note 7)	2,300	3,800	2,300	3,800
Distributions paid	(6,131)	(6,092)	(12,262)	(12,143)
	238,827	(2,292)	232,696	(8,343)
Investing activities				
Business acquisition – Shepell•fgi (note 3(a))	(246,466)	—	(246,466)	—
Business acquisition – Cowan (note 3(b))	—	(3,783)	—	(3,783)
Business acquisition – Heath (note 3(c))	(813)	—	(813)	—
Cash assumed from acquisitions (note 3)	272	256	272	256
Purchase of capital assets	(493)	(576)	(760)	(712)
	(247,500)	(4,103)	(247,767)	(4,239)
Net increase (decrease) in cash for the period	1,855	1,528	(4,599)	(5,691)
Cash (bank indebtedness), beginning of period	(3,556)	(1,962)	2,898	5,257
Cash (bank indebtedness), end of period	$ (1,701)	$ (434)	$ (1,701)	$ (434)

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the three and six months ended June 30, 2008 and 2007
(Unaudited)
(In thousands of dollars, except unit and per unit amounts)

1. ORGANIZATION AND NATURE OF THE BUSINESS

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

The Fund is the largest Canadian-owned firm providing human resource consulting and outsourcing services. The firm delivers solutions to assist employers in managing the financial security, health and productivity of their employees. With over 2,300 employees in offices across North America, the Fund offers its services to organizations that are situated in Canada, in the United States and around the globe.

On June 2, 2008, the Fund indirectly acquired substantially all the assets of Shepell FGI LP ("Shepell•fgi") (Note 3(a) – Business Acquisition). The primary services provided by Shepell•fgi are employee assistance programs ("EAP"), employee health management and workplace training and education.

2. SIGNIFICANT ACCOUNTING POLICIES

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

(a) Basis of presentation

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

	% Ownership
Morneau Sobeco Trust ("Trust")	100.0
Morneau Sobeco GP Inc. ("MS GP")	100.0
Morneau Sobeco Limited Partnership ("MSLP")	86.1
Morneau Sobeco Group Limited Partnership ("MS Group LP")	86.1
Morneau Sobeco, Ltd. ("MSUS")	86.1
HRCO Inc ("HRCO") (formerly Morneau Sobeco Corporation)	86.1
FGI World France S.A.R.L.("FGIW")	86.1
FGI World New Caledonia ("FGIN")	86.1
1137273 Ontario Limited ("ONTL")	86.1
Innu-Med Inc. ("IMI")	41.3

All material intercompany transactions and balances have been eliminated upon consolidation.

(b) Measurement uncertainties

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

(c) Revenue recognition and unbilled fees

Fees for administrative, actuarial and consulting services are recognized when the services are rendered.

EAP revenue is recognized through a combination of the minimum contracted amount and incremental usage above the minimum thresholds. The minimum contracted amount is recognized on a straight-line basis over the term of the contract. Incremental usage is recognized when the minimum usage threshold is exceeded.

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

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

Other revenue includes investment income recorded on the accrual basis.

(d) Foreign currency translation

Monetary assets and liabilities denominated in foreign currencies have been translated into Canadian dollars at the exchange rates prevailing at the consolidated balance sheet dates. Non-monetary items have been

translated into Canadian dollars at the exchange rates prevailing when the assets were acquired or obligations incurred. Revenue and expenses have been translated at rates in effect on the transaction dates. Exchange gains or losses are reflected in income for the period.

(e) Capital assets

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

Asset	Basis	Rate
Computer equipment	Declining balance	30%
Computer software	Declining balance	50%
Furniture and equipment	Declining balance	20%
Leasehold improvements	Straight-line	Over term of the lease

(f) Intangible assets

Intangible assets are recorded at cost less accumulated amortization. Intangible assets acquired through acquisitions or business combinations are initially recognized at fair value based on an allocation of the purchase price. Intangible assets with finite life are amortized on a straight-line basis over their estimated useful lives. Intangible assets with an indefinite life are not amortized but are tested for impairment annually or more frequently if events or circumstances indicate there may be an impairment by comparing the estimated discounted future net cash flows from the asset to its carrying amount.

Amortization is calculated using the straight-line method based on following estimated useful lives:

Asset	Estimated useful lives
Customer relationships	15 to 20 years
Customer contracts	1 to 2 years
Proprietary software	5 years
Non-compete agreements	16 months
Trade names	Indefinite

(g) Impairment of long-lived assets

Long-lived assets with finite lives are reviewed for impairment annually or whenever events or changes in circumstances cause

their carrying amount to exceed the total undiscounted cash flow expected from their use and eventual disposition. An impairment loss is measured at the amount by which the carrying amount of the long-lived asset exceeds its fair value.

(h) Goodwill

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

(i) Insurance premium liabilities and related cash and investments

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

(j) Long-term incentive plan

The Fund has a long-term incentive plan under which participants are eligible to receive Units. The amount awarded under this plan is recorded as salary, benefit and contractor expenses over the three-year vesting period.

(k) Employee future benefits

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

The defined benefit option was closed effective January 1, 1998 and included 8 employees, 5 retirees and 54 deferred vested members as at June 30, 2008. All other employees are covered by the defined contribution option of the plan.

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

(l) Income taxes

The Fund uses the asset and liability method of accounting for income taxes. Future income taxes are recognized for the temporary differences between the financial statement carrying amounts of assets and liabilities and their respective tax bases. Future income tax assets and liabilities are measured using enacted or substantively enacted tax rates and laws that are expected to apply to taxable income in the years in which those temporary differences are expected to be reversed or settled. The effect on future income tax assets and liabilities of a change in tax rate is recognized in income in the period that includes the date of enactment or substantive enactment.

(m) Deferred lease inducements

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

(n) Financial instruments

Financial assets and financial liabilities held-for-trading are measured at fair value with changes in those fair values recognized in the income statement. Loans and receivables and other financial liabilities are measured at amortized cost using the effective interest method of amortization. The Fund had neither available-for-sale nor held-to-maturity instruments.

Transaction costs are expensed as incurred for financial instruments classified or designated as held-for-trading. For other financial instruments, transaction costs are capitalized on initial recognition and are included in the underlying balance.

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

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

(o) New accounting policies

Effective January 1, 2008 the Fund adopted the following new accounting standards:

(i) Section 3862, *Financial Instruments – Disclosures* and Section 3863, *Financial Instruments – Presentation*, which replace the existing Section 3861, *Financial Instruments – Disclosure and Presentation*. These new sections revise and enhance disclosure requirements and carry forward unchanged existing presentation requirements. These new sections place an increased emphasis on disclosures and presentation regarding the risks associated with both recognized and unrecognized financial instruments and how the Fund manages those risks.

(ii) Section 1535, *Capital Disclosure*. This section requires disclosure of the Fund's objectives, policies and processes for managing capital, quantitative data about what the Fund regards as capital and whether the Fund has complied with any capital requirements.

These new standards relate to disclosures and presentation only and did not have an impact on the Fund's financial results or position. Disclosures required as a result of adopting the above sections can be found in notes 22 and 23.

(p) Future accounting changes

(i) Goodwill and intangible assets – In February 2008, the CICA issued new Handbook Section 3064, *Goodwill and Intangible Assets*, replacing Section 3062, *Goodwill and Other Intangible Assets* and Section 3450, *Research and Development Costs*. The new standard will be applicable to financial statements relating to fiscal years beginning on or after October 1, 2008. This section establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets. The standards concerning goodwill are unchanged from the standards included in the previous section 3062. The Fund is currently assessing the impact this new standard will have on its consolidated financial statements, if any.

(ii) International Financial Reporting Standards – The Canadian Accounting Standards Board confirmed in February 2008 plans to converge Canadian GAAP with International Financial Reporting Standards ("IFRS") over a transition period expected to be effective for interim and annual periods commencing January 1, 2011. The Fund is currently assessing the new standards and has not yet determined the impact on its consolidated financial condition.

3. BUSINESS ACQUISITIONS

(a) Shepell•FGI Holdings LP ("Shepell•fgi")

On June 2, 2008, the Fund indirectly acquired certain assets, shares of certain subsidiaries, liabilities and contracts of Shepell•fgi. The total purchase price is $319,960 including estimated transaction cost of $1,243. The consideration was satisfied by cash of $247,359 and two non-interest bearing promissory notes of $75,000 and $4,500 repayable on July 2, 2009 and July 2, 2010 respectively. The promissory notes have been recorded at their combined present value of $71,358.

The acquisition was financed by the issuance of Fund's units for proceeds of $153,000, net of underwriters' fees and estimated issuance expenses of approximately $10,467. The remaining amount was financed through cash from operations and the utilization of a new credit facility. $246,466 of the cash consideration was paid on closing and the remainder of $2,136 was settled in July 2008 after the finalization of the working capital and included under accounts payable and accrued liabilities as at June 30, 2008

The acquisition has been accounted for using the purchase method. The purchase price allocation is preliminary pending finalization of valuations of the net identifiable assets acquired and liabilities assumed. The preliminary estimated fair values of the assets acquired and liabilities assumed in the acquisition are as follows:

Assets and liabilities acquired:	
Cash	$ 272
Accounts receivable	14,672
Unbilled fees	8,041
Income taxes recoverable	572
Prepaid expenses and other	2,225
Capital assets	7,669
Intangible assets:	
Customer relationship	90,000
Customer contracts	27,500
Trade name	70,000
Non-compete agreements	5,000
Proprietary software	6,000
Goodwill	121,604
Accounts payable and accrued liabilities	(21,848)
Deferred revenue	(2,298)
Future income tax liabilities	(2,601)
Other liabilities	(6,848)
	$319,960
Consideration:	
Cash	$247,359
Transaction costs	1,243
Promissory notes issued to vendors, at present value	71,358
	$319,960

As a result of the transaction being an asset purchase, a subsidiary of the Fund has approximately $220,000 of eligible tax deductions which are deductible from taxable income at 7% per annum on a declining balance basis.

These consolidated financial statements include the results of Shepell•fgi from the date of acquisition on June 2, 2008.

(b) Cowan Benefits Consulting Limited ("Cowan")

On June 1, 2007, a subsidiary of the Fund directly acquired certain assets, liabilities and contracts of the defined benefit pension administration and actuarial consulting practices ("Cowan DB business") of Cowan, a benefits consulting firm based in the Waterloo region, in Ontario. The purchase price is based on the final pension administration and actuarial consulting services revenue and certain other integration conditions and is expected to be approximately $6 million. The acquisition will be paid in three instalments.

The first instalment was made on the closing date of June 1, 2007 and was funded by $3,800 of the operating line of credit. In addition, the Fund issued a standby letter of credit in the amount of $400, which will be paid on or before December 31, 2008 to the extent the vendor has performed all of its transition services obligations. The second instalment is $960 and payable on August 1, 2008. The third instalment is subject to the purchase price adjustment and will be payable on August 1, 2009.

The contingent consideration has been recognized to the extent the acquired assets net of liabilities assumed exceed the first and second installments of the purchase price. The acquisition has been accounted for by the purchase method based on management's best estimate of the relative fair value of the identifiable assets and liabilities acquired.

Assets and liabilities acquired:

Cash	$ 256
Prepaid expenses and other	6
Intangible assets	5,821
Accounts payable and accrued liabilities	(256)
	$5,827

Consideration:

Cash	$3,783
Instalment 2 payable on August 1, 2008	960
Future considerations	1,084
	$5,827

These consolidated financial statements include the results of the Cowan DB business from the date of acquisition on June 1, 2007.

(c) Heath Benefits Consulting Inc. ("Heath")

On June 1, 2006, the Fund indirectly acquired all of the issued and outstanding shares of Heath, a Vancouver-based benefits consulting firm with over 90 employees across Canada.

The purchase price is $16,853. The consideration was satisfied primarily through cash, the assumption and repayment of the Heath debt and the issuance of Class B LP Units of MS Group LP based on a predetermined value of $12.52 per unit and a final installment of cash and units of MS Group LP due on December 1, 2008.

A portion of the purchase price is conditional on the continuing employment of certain selling shareholders ("salary component of the Heath acquisition") and is being recorded as salary expense over the required employment period to December 2008.

The expenses related to the salary component of the Heath acquisition for the three months ended June 30, 2008 and June 30, 2007 were $518 and $300 and for the six months ended June 30, 2008 and June 30, 2007 were $758 and $520, respectively. The expense for this quarter included an adjustment as a result of the finalization of the contingent consideration.

Total consideration also includes amounts to compensate for forgone distributions payable on the unpaid purchase price since June 1, 2006 which amounted to $408 as at June 30, 2008.

The acquisition has been accounted for by the purchase method based on management's best estimate of the relative fair value of the identifiable assets and liabilities assumed. The purchase price has been accounted as follows:

Assets and liabilities acquired:	
Cash	$ 827
Accounts receivable	1,530
Income taxes recoverable	66
Prepaid expenses and other	101
Capital assets	365
Intangible assets	8,090
Goodwill	7,776
Bank indebtedness	(1,734)
Accounts payable and accrued liabilities	(969)
Future income tax liability	(1,923)
Payable to insurance companies	(3,156)
Related cash and investments held	3,156
	$14,129
Consideration:	
Cash	$ 1,261
Debt assumed and repaid	4,648
Exchangeable Units	6,960
Future considerations	3,984
	$16,853
Salary component of the Heath acquisition	(2,724)
	$14,129

These consolidated financial statements include the results of Heath from the date of acquisition on June 1, 2006.

4. CAPITAL ASSETS

The Fund's capital assets are comprised of:

	Cost	Accumulated Amortization June 30, 2008	Net Book Value June 30, 2008	Net Book Value December 31, 2007
Computer equipment	$ 3,253	$ (985)	$ 2,268	$ 1,201
Computer software	638	(437)	201	230
Furniture and equipment	6,626	(1,705)	4,921	2,381
Leasehold improvements	13,047	(3,496)	9,551	6,374
	$23,564	$(6,623)	$16,941	$10,186

Amortization for the three months ended June 30, 2008 and June 30, 2007 were $1,015 and $547 and for the six months ended June 30, 2008 and June 30, 2007 were $1,675 and $1,070, respectively.

5. INTANGIBLE ASSETS

The Fund's intangible assets are comprised of:

	Cost	Accumulated Amortization June 30, 2008	Net Book Value June 30, 2008	Net Book Value December 31, 2007
Customer relationships	$193,911	$(14,459)	$179,452	$ 92,666
Customer contracts	32,500	(6,089)	26,411	858
Proprietary software	46,000	(22,100)	23,900	22,000
Non-compete agreements	5,000	(313)	4,687	—
Trade names	70,000	—	70,000	—
	$347,411	$(42,961)	$304,450	$115,524

Amortization for the three months ended June 30, 2008 and June 30, 2007 were $5,931 and $3,807 and for the six months ended June 30, 2008 and June 30, 2007 were $9,574 and $7,582, respectively.

6. GOODWILL

	June 30, 2008	December 31, 2007
Balance, beginning of year	$169,451	$169,451
Acquisition (note 3(a))	121,604	—
Acquisition (note 3(c))	4,597	—
	$295,652	$169,451

$3,179 of goodwill related to the Heath acquisition was recognized as part of the first instalment paid on June 1, 2006.

7. BANK INDEBTEDNESS AND LONG-TERM DEBT

	June 30, 2008	December 31, 2007
Non-revolving term loan	$137,000	$35,000
Revolving loan	2,300	—
	139,300	35,000
Less: current portion of long term debt	(2,300)	—
Less: debt issue costs, net of accumulated amortization	(1,838)	(87)
	$135,162	$34,913

New credit agreement

As part of the Shepell•fgi acquisition the Fund entered into a new credit agreement with a syndicate of Canadian chartered banks for a period of four years maturing on June 1, 2012. Under the agreement, the following credit facilities are available:

- $20,000 senior secured revolving facility ("revolving loan").
- $137,000 senior secured non-revolving term loan ("term loan").
- $40,000 senior secured non-revolving delayed draw term facility. This facility shall be available until July 2, 2009 by way of a single draw to fund a portion of the $75,000 promissory note issued in connection with the Shepell•fgi acquisition.

The interest rates for the facilities are floating, based on a margin over certain reference rates of interest. The applicable margin may vary up and down depending on the ratio of the Fund's consolidated debt to Adjusted EBITDA as calculated in the new credit agreement. Adjusted EBITDA is defined as the rolling twelve months earnings before interest, taxes, deprecation and amortization of the Fund and Shepell•fgi.

The credit facilities are secured by a general assignment of all the assets of the Fund. The new credit agreement also requires the Fund to maintain the following financial covenants on a consolidated basis:

(i) Debt to Adjusted EBITDA ratio shall not exceed 3.5:1.0 for the period up to December 30, 2009 and declining to 2.5:1.0 by June 30, 2011.

(ii) EBITDA to interest expense ratio of not less than 3.0 to 1.0

EBITDA is defined as net income before interest expense, income taxes (recovery), depreciation, amortization and non-controlling interest.

The Fund complied with all the required financial covenants and the ratios as at June 30, 2008 were 3.0 and 16.0 respectively.

At June 30, 2008 the Fund has utilized the following credit facilities:

- $137,000 of term loan. The term loan is repayable in full on June 1, 2012 and bears interest at one month banker acceptance ("BA") rate plus an applicable margin.
- $2,300 of revolving loan. The loan matures on September 2, 2008 and bears interest at three months banker acceptance rate plus an applicable margin.
- Bank indebtedness of $1,701 under the revolving facilities. The overdraft carries interest at prime plus an applicable margin.
- $400 letter of credit under the revolving facility, as part of the Cowan DB business acquisition.

As a result of the new credit agreement, the Fund wrote off the remaining $74 of debt issue costs related to the previous credit agreement and incurred $1,875 of new costs.

Interest-rate swap

In connection with the term loan, the Fund entered into new interest-rate swap agreements for a total notional amount of $102,000, increasing to $137,000 from July 2, 2008 to and ending on June 1, 2012. These swaps are used to fix the variable component of the interest rate at 3.657%, before the applicable margin, for the duration of the loan and have been designated as cash flow hedges. The fair value of the swaps as at June 30, 2008 was $951.

The Fund also terminated its existing swap agreements associated with the original $35,000 borrowing and incurred a loss of $282, which represents a mark to market adjustment of $196 on the cancellation date and the write off the remaining

fair value of $86. These swap agreements were not designated as cash flow hedges and as such are included in the interest expense.

Interest expenses

Interest expense is comprised of the following:

	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
Interest on term loan	$ 907	$ 384	$1,278	$759
Accretion of interest on promissory notes (note 8)	570	—	570	—
Interest on revolving loan, bank indebtedness and other charges	48	50	56	51
Amortization of debt issue costs	108	13	121	26
Swap termination fees	196	—	196	—
Interest-rate swap agreements fair value adjustment	86	(132)	785	(68)
	$1,915	$ 315	$3,006	$768

8. PROMISSORY NOTES

The promissory notes issued as part of the Shepell•fgi acquisition in the amounts of $75,000 and $4,500 are due on July 2, 2009 and July 2, 2010, respectively. The notes are non-interest bearing and are secured by a general assignment of all the assets of the Fund, which is subordinated to the credit facilities. The notes have been recorded at their initial combined present value of $71,358 plus accreted interest to date of $570.

The Fund has the option to repay up to 50% of the $75,000 promissory note and 100% of the $4,500 promissory note through the issuance of Units at a 5% discounted value, subject to the Fund's ability to issue new Units under the guidance for income trusts that qualify for the four-year transitional relief. It is the Fund's intention is to repay the notes through future cash flow and as a result the notes are recorded as liabilities.

The promissory notes also include a covenant that the Fund and its subsidiaries shall not incur any debt other than permitted debt as defined in the promissory note agreements unless, after the incurrence of such debt, the Fund would have on a pro forma consolidated basis of ratio of debt to adjusted EBITDA of not greater than 4.5:1.0 determined as of end of the fiscal quarter ending immediately prior to the date of determination.

9. OTHER LIABILITIES

	June 30, 2008	December 31, 2007
Acquired above market rent leases	$5,835	$—
Sub-lease loss	1,050	—
	$6,885	$—

As part of the Shepell•fgi acquisition, the Fund assumed lease agreements for several offices. The above amounts represent the difference between estimated market rates and the lease agreements as well as the estimated sub-lease loss as a result of a planned office relocation.

10. FUND UNITS

The Fund is authorized to issue an unlimited number of Units and an unlimited number of special voting units ("Special Voting Units"). Special Voting Units are not entitled to any beneficial interest in any distribution from the Fund.

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

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

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

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

	Units Issued	Special Voting Units	Total Units	Amount
Balance, December 31, 2006	22,062,916	5,721,444	27,784,360	$210,607
Exchange of Class B LP Units	130,003	(130,003)	—	1,226
Balance, December 31, 2007	22,192,919	5,591,441	27,784,360	211,833
Exchange of Class B LP Units	153,994	(153,994)	—	1,626
Class A LP Units – (i)	12,750,000	—	12,750,000	153,000
Units issuance costs, net of future income tax benefits – (i)	—	—	—	(7,316)
Class B LP Units – (ii)	—	242,997	242,997	—
Balance, June 30, 2008	35,096,913	5,680,444	40,777,357	$359,143

(i) On June 2, 2008, as part of the Shepell•fgi acquisition, the Fund completed a public offering and issued 12,750,000 Units at price of $12.00 per unit for cash proceeds of $153,000. The Unit issuance costs, net of future income tax benefits of $3,151, is $7,316.

(ii) On June 30, 2008, the Fund issued 242,997 Special Voting Units in connection with the settlement of the second instalment of the Heath acquisition.

11. NON-CONTROLLING INTERESTS

The former shareholders of Morneau Sobeco and Heath own 5,680,444 Class B LP Units of MS Group LP. The Class B LP Units are fully exchangeable for an equal number of Units in the Fund and provide the former shareholders of Morneau Sobeco and Heath with a non-controlling interest of 13.9% (December 31, 2007 – 20.1%) in the Fund. Some of the Class B LP Units were subordinated in their rights to receive distributions.

Distributions on the Subordinated Class B LP Units were subordinated in favour of the Fund Units and the Non-subordinated Class B LP Units. The distributions on the

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Subordinated Class B LP Units were paid at the end of a fiscal quarter to the extent that an average monthly distribution of at least $0.06875 per Unit and Non-subordinated Class B LP Unit in respect of that quarter had been paid. On October 16, 2007, the Audit Committee of the Fund declared that the conditions of the subordination provisions had been satisfied and the subordination end date was determined to be September 30, 2007.

	Class B LP Units Issued			
	Subordinated	Non-subordinated	Total	Amount
Balance, December 31, 2006	4,095,060	1,626,384	5,721,444	$56,520
Exchange Units	—	(130,003)	(130,003)	(1,226)
Subordinated conditions met	(4,095,060)	4,095,060	—	—
Salary component of Heath acquisition				999
Share of income for the year				3,119
Distribution for the year				(4,960)
Balance, December 31, 2007	—	5,591,441	5,591,441	54,452
Units issued related to Heath acquisition		242,997	242,997	3,042
Salary component of Heath acquisition				758
Heath 3rd instalment excluding salary component				773
Exchange Units	—	(153,994)	(153,994)	(1,626)
Share of income for the period				1,181
Distributions for the period				(2,460)
Balance, June 30, 2008	—	5,680,444	5,680,444	$56,120

12. DISTRIBUTIONS TO UNITHOLDERS

The Board of Trustees determines the amount of distributions. The Fund's Declaration of Trust provides that distributions must be made to ensure that the Fund will not be liable for ordinary income taxes under the Income Tax Act *(Canada)*. Any taxable income of the Fund that is unavailable for cash distribution will be distributed to Unitholders in the form of additional Units, which Units will be immediately consolidated such that each Unitholder will hold after consolidation the same number of Units as the Unitholder held prior to the distribution, subject to certain exceptions.

Distributions announced during the six months ended June 30, 2008 and 2007 were as follows:

Unitholder record date	Total	Per Unit	Paid or payable for the six months ended June 30, 2008
Trust Units			
January 31, 2008	$ 1,635	$0.07356	February 15, 2008
February 28, 2008	1,642	0.07356	March 17, 2008
March 31, 2008	1,642	0.07356	April 15, 2008
April 30, 2008	1,643	0.07356	May 15, 2008
May 30, 2008	1,643	0.07356	June 16, 2008
June 30, 2008	2,763	0.07871	July 15, 2008
	$10,968	$0.44651	
Class B LP Units			
Non-subordinated			
January 31, 2008	$ 409	$0.07356	February 15, 2008
February 28, 2008	403	0.07356	March 17, 2008
March 31, 2008	401	0.07356	April 15, 2008
April 30, 2008	400	0.07356	May 15, 2008
May 30, 2008	400	0.07356	June 16, 2008
June 30, 2008	447	0.07871	July 15, 2008
	$ 2,460	$0.44651	

Unitholder record date	Total	Per Unit	Paid or payable for the six months ended June 30, 2007
Trust Units			
January 31, 2007	$ 1,517	$0.06875	February 15, 2007
February 28, 2007	1,517	0.06875	March 15, 2007
March 30, 2007	1,623	0.07356	April 16, 2007
April 30, 2007	1,623	0.07356	May 15, 2007
May 31, 2007	1,623	0.07356	June 15, 2007
June 29, 2007	1,623	0.07356	July 16, 2007
	$ 9,526	$0.43174	

Unitholder record date	Total	Per Unit	Paid or payable for the six months ended June 30, 2007
Class B LP Units			
Non-subordinated			
January 31, 2007	$112	$0.06875	February 15, 2007
February 28, 2007	112	0.06875	March 15, 2007
March 30, 2007	120	0.07356	April 16, 2007
April 30, 2007	120	0.07356	May 15, 2007
May 31, 2007	120	0.07356	June 15, 2007
June 29, 2007	120	0.07356	July 16, 2007
	$704	$0.43174	
Subordinated			
March 30, 2007	$864	$0.21106	April 16, 2007
June 29, 2007	903	0.22068	July 16, 2007

13. LONG-TERM INCENTIVE PLAN

Senior management is eligible to participate in Morneau Sobeco's Long-Term Incentive Plan ("LTIP"), which is designed to align compensation with the performance of the Fund's subsidiaries and to aid in the retention of a select group of senior professionals. The Fund's Compensation, Nominating and Corporate Governance Committee of the Board of Trustees determines (i) who will participate in the LTIP; (ii) the level of participation; and (iii) the time or times when LTIP awards will vest or be paid to each participant.

Pursuant to the LTIP, Morneau Sobeco sets aside a pool of funds in an amount determined by the Board. Morneau Sobeco or a trustee purchases Units in the market with this pool of funds and holds the Units until such time as ownership vests to each participant. Generally, Units will either vest upon departure from the firm after a period of at least three years, or in equal amounts over a period of three years following the grant of the awards. LTIP participants are entitled to receive distributions on all Units held for their account prior to the applicable vesting date. Unvested Units held by the trustee for an LTIP participant will be forfeited if the participant resigns or is terminated prior to the applicable vesting date and those Units will be sold and the proceeds returned to Morneau Sobeco, or as otherwise directed.

Amounts awarded under the terms of the LTIP since inception of the plan and their associated expenses by year based on vesting periods are summarized as follow:

Year awarded	Year units purchased	Award amount	Expense by year – December 31			
			2007	2008	2009	2010
2006	2007	$ 386	$146	$198	$ 42	$ —
2007	2008	1,340		484	439	417
		$1,726	$146	$682	$481	$417

Once awarded, the LTIP amount to be recognized as an expense in future periods is classified as a prepaid expense on the consolidated balance sheet. As at June 30, 2008 the amount recorded under prepaid is $1,231 The expense recognized for the three months ended June 30, 2008 and June 30, 2007 was $170 and $32 and for the six months ended June 30, 2008 and June 30, 2007 was $341 and $64 respectively. Under the LTIP, the Fund redeemed proceeds of $17 related to 2006 awards forfeited.

14. INCOME TAXES

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

On June 22, 2007, legislation relating to the federal income taxation of a "specified investment flow-through" trust or partnership (a "SIFT"), received Royal Assent (the "SIFT Rules"). A SIFT includes a publicly-listed or traded partnership

and trust, such as an income trust and a real estate investment trust. The Fund is a SIFT, as discussed below.

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

A SIFT which was publicly listed on or before October 31, 2006 (an "Existing Trust") will become subject to the tax on distributions commencing with the 2011 taxation year end. However, an Existing Trust may become subject to this tax prior to the 2011 taxation year if its equity capital increases beyond certain limits measured against the market capitalization of the Existing Trust at the close of trading on October 31, 2006.

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

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

	Three Months ended June 30		Six Months ended June 30	
	2008	2007	2008	2007
Income taxes at statutory rates:				
Federal	19.50%	22.12%	19.50%	22.12%
Provincial	12.64%	12.25%	12.64%	12.25%
	32.14%	34.37%	32.14%	34.37%
Income tax provision applied to income before income taxes:				
Combined basic federal and provincial income taxes at statutory rates applied to income from continuing operations	$ 574	$ 1,181	$ 1,538	$ 2,251
Income taxed in the hands of the Unitholders	(2,025)	(1,906)	(3,608)	(3,773)
Non-deductible expenses	197	141	301	244
Adjustment as a result of new SIFT rules	—	2,670	—	2,670
Adjustment to future income assets and liabilities for change in income tax rate	—	(306)	—	(284)
Change in taxable subsidiary share of temporary differences between the carrying amounts and tax bases of its assets and liabilities	—	(300)	—	(300)
Other	(67)	(158)	(28)	(207)
	$(1,321)	$ 1,322	$(1,797)	$ 601

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

	June 30, 2008	December 31, 2007
Future income tax assets:		
Fund Unit issuance costs	$ 5,157	$ 2,581
Capital assets	744	652
Other	—	25
	$ 5,901	$ 3,258
Future income tax liability:		
Intangible assets	$27,737	$29,810
Other liabilities	2,419	—
	$30,156	$29,810

15. EMPLOYEE FUTURE BENEFITS

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

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

The pension fund assets and obligations are measured as at June 30, 2008. Information about the pension plan's defined benefit option is as follows:

	June 30, 2008	December 31, 2007
Fair value of plan assets	$3,076	$2,897
Accrued benefit obligation	3,100	3,218
Funded status – deficit	$ (24)	$ (321)
Plan assets:		
Fair value, beginning of year	$2,897	$2,562
Actual return on plan assets	64	108
Employer contributions	144	285
Benefits paid	(29)	(58)
Fair value, end of period/year	$3,076	$2,897
Accrued benefit obligation:		
Balance, beginning of year	$3,218	$3,164
Current service cost	28	91
Interest cost	89	161
Benefits paid	(29)	(58)
Actuarial gains	(206)	(140)
Balance, end of period/year	$3,100	$3,218
Reconciliation of plan assets to accrued benefit obligation, end of period/year:		
Fair value of plan assets	$3,076	$2,897
Accrued benefit obligation	3,100	3,218
Funded status – deficit	(24)	(321)
Unamortized net actuarial loss (gain)	(288)	(36)
Unamortized transitional obligation	314	359
Accrued benefit asset	$ 2	$ 2
End of year allocation of fair value of plan assets (%):		
Pooled Equities Fund	45%	45%
Pooled Bond Fund	55%	55%
	100%	100%

	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
Pension plan cost				
Current service cost	$ 14	$ 23	$ 28	$ 46
Interest cost on accrued benefit obligation	45	40	89	80
Return on plan assets	(60)	11	(64)	(12)
Actuarial losses (gains) during the period on accrued benefit obligation	(1)	(237)	(206)	(237)
	$ (2)	$(163)	$(153)	$(123)
Other adjustments:				
Difference between actual and expected return on plan assets	8	(58)	(39)	(80)
Amortization of actuarial losses (gains)	42	298	291	298
Transitional amounts	22	22	45	45
Net pension plan expense	$ 70	$ 99	$ 144	$ 140

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

	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
Employer contributions	$70	$101	$144	$140
Benefits paid	$14	$ 14	$ 29	$ 29

Actuarial valuation for the Fund's pension plan is generally required every three years. The most recent actuarial valuation of the Fund's pension plan was conducted as of December 31, 2006.

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Weighted average assumptions:

	June 30, 2008	December 31, 2007
Weighted average of the amounts assumed in accounting for the plan:		
Discount rate at the end of the current fiscal period used to determine the accrued benefit obligation	6.00%	5.50%
Discount rate at the end of preceding period used to determine the benefit cost	5.50%	5.00%
Rate of compensation increase used to determine the accrued benefit obligation	2.50%	2.50%
Rate of compensation increase used to determine the benefit cost	2.50%	2.50%
Expected long-term rate of return on plan assets	7.00%	7.00%

The net expense for the Fund's defined contribution option for the three months ended June 30, 2008 and 2007 was $527 and $449 and for the six months ended June 30, 2008 and 2007 was $1,038 and $918, respectively.

16. NET INCOME PER UNIT

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

	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
Basic:				
Net income	$ 2,456	$ 1,680	$ 5,236	$ 4,725
Weighted average number of Units outstanding	26,402,372	22,062,916	24,326,996	22,062,916
Diluted:				
Net income	$ 2,456	$ 1,680	$ 5,236	$ 4,725
Non-controlling interest	490	435	1,181	1,225
Net income available to Unitholders and Class B LP Unitholders	$ 2,946	$ 2,115	$ 6,417	$ 5,950
Weighted average number of Units outstanding – Basic	26,402,372	22,062,916	24,326,996	22,062,916
Weighted average exchangeable Class B LP Units outstanding	5,447,845	5,721,444	5,490,293	5,721,444
Dilutive effect of Class B LP Units in connection with the Heath acquisition	483,321	—	484,656	—
Total weighted average number of diluted Units	32,333,538	27,784,360	30,301,945	27,784,360
Net income per Unit				
– Basic	$ 0.093	$ 0.076	$ 0.215	$ 0.214
– Diluted	$ 0.091	$ 0.076	$ 0.212	$ 0.214

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17. SUPPLEMENT DISCLOSURE OF CASH FLOW INFORMATION

Change in non-cash operating working capital:

	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
Accounts receivable	$(1,362)	$(3,755)	$(3,272)	$(6,072)
Unbilled fees	(1,580)	1,870	(2,097)	772
Income taxes recoverable/payable	(321)	166	(529)	840
Prepaid expense and other	(1,694)	(236)	(1,175)	(22)
Accounts payable and accrued liabilities	5,457	2,079	(607)	(4,001)
Deferred revenue	(195)	—	(37)	—
	$ 305	$ 124	$(7,717)	$(8,483)

	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
Interest paid	$ 908	$ 468	$ 1,212	$ 845
Income taxes paid (refunded)	$ 142	$ (9)	$ 240	$ (486)

18. COMMITMENTS

The Fund has lease commitments for office premises and equipment with options for renewal. As at June 30, 2008 the minimum payments not including operating expenses, due in each of the next five years and thereafter, are expected to be as follows for each year ending December 31:

2008 (remainder)	$ 6,786
2009	13,031
2010	12,476
2011	11,164
2012	9,733
Thereafter	35,953
Total	$89,143

In addition, the Fund has two subleases for which the Fund is liable for the rent in case of a default by the subtenants. The average annual rent for the leases are $192 and $244 and expire on October 30, 2011 and June 29, 2017, respectively. The fair value of the total future lease payments as at June 30, 2008 was $2,028. The Fund considers the risk of default by the subtenants to be low therefore no accrual has been set up for the guarantee.

19. CONTINGENCIES

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

20. ECONOMIC DEPENDENCE

Revenue from the Fund's largest client for the three and six months ended June 30, 2008 was approximately 7% and 9%, respectively (for three and six months ended June 30, 2007– 10%) and its top 10 clients, in the aggregate, accounted for approximately 26% and 27%, respectively (for three and six months ended June 30, 2007 – 33%).

Accounts receivable from the Fund's largest client was approximately 1% of the total accounts receivable as at June 30, 2008 (December 31, 2007 – 2%). The Fund's top 10 clients accounted for approximately 19% of the total accounts receivable as at June 30, 2008 (December 31, 2007 – 24%).

21. SEGMENTED INFORMATION

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

	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
Revenue				
Canada	$48,967	$35,322	$85,668	$69,365
United States	3,396	1,735	5,829	3,783
	$52,363	$37,057	$91,497	$73,148

	June 30, 2008	December 31, 2007
Assets:		
Canada	$682,613	$332,397
United States	6,191	2,031
Liabilities:		
Canada	$346,655	$136,367
United States	1,952	393

22. MANAGEMENT OF CAPITAL

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

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

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

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

23. FINANCIAL INSTRUMENTS

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

	June 30, 2008	December 31, 2007
Held for trading[(i)]	$ —	$ 3,683
Loans and receivables[(ii)]	47,288	28,243
Other financial liabilities[(iii)]	261,236	50,454

(i) Includes cash and Interest-rate swap agreements not designated as hedges.

(ii) Includes accounts receivable and income taxes recoverable.

(iii) Includes accounts payable and accrued liabilities, accrued compensation and related benefits, deferred revenue, Unitholder distributions payable, bank indebtedness, operating line of credit, long-term debt, promissory notes and other liabilities

Fair value

The fair value of the Fund's financial assets and liabilities approximate carrying values due to their short-term nature or with respect to the long-term debt instruments, because they bear interest at market rates. The fair value of interest-rate swaps was determined using estimated future discounted cash flows using a comparable market rate of interest. The Fund does not enter into financial instruments for trading or speculative purposes.

Interest rate risk

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

A sensitivity analysis that assumes interest rates increased or decreased by 50 basis points with all other variables held constant would result in an increase (decrease) of the Fund's interest expense, excluding the interest subjected to interest-rate swap agreements, by $3.

Credit risk

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

The aging of fees receivable was:

	June 30, 2008	December 31, 2007
Current	$19,306	$ 9,524
Past due 0- 30 days	11,660	9,416
Past due 31- 90 days	9,484	5,643
Past due over 90 days	5,987	2,946
	$46,437	$27,529

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

(1) Risk associated with concentration of credit risk with respect to accounts receivable is limited due to the credit rating of the Fund's top 10 clients (note 20). The Fund has over 8,000 clients, with no client accounting for greater than 1% of total revenue with the exception of the top 10 clients.

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

The Fund determines its allowance for doubtful accounts based on it's best estimate of the net recoverable amount by customer account. Accounts that are considered uncollectible are written off. The allowance for doubtful accounts as at June 30, 2008 was $941 (December 31, 2007 - $76).

The Credit risk on cash and interest-rate swap agreements is limited because the counterparties are banks with high credit ratings assigned by international credit-rating agencies.

Foreign exchange risk

The Fund realizes a portion of sales in U.S. dollars and has operations in the United States and thus is exposed to fluctuations in the value of the U.S. dollar relative to the Canadian dollar. The net revenue exposure after accounting for related expenses denominated in U.S. dollars for three and six months ended June 30, 2008 were approximately US$1,503 and US$2,681, respectively.

The Fund is not engaged in currency hedging activities and does not own other instruments that may be settled by the delivery of non-financial assets. The exchange gain (loss) for the three months ended June 30, 2008 and 2007 were $(43) and $271 and for the six months ended June 30, 2008 and June 30, 2007 were $(115) and $218, respectively.

As at June 30, 2008, the Fund's net exposure to currency risk through its current assets and liabilities dominated in US dollars was US$4,202. Assuming that all other variables remain constant, a 5% depreciation or appreciation of the Canadian dollar against the US dollars would result in an increase (decrease) of $210 in the Fund's net income.

Liquidity risk

Liquidity risk is the risk that the Fund is not able to meet its financial obligations as they fall due. The Fund manages

liquidity risk through regular monitoring of financial results and actual cash flows, and also the management of its capital structure and financial leverage as outlined in Note 22.

All current liabilities are due for payment within twelve months of the balance sheet date. The maturities date for Future considerations related to acquisitions and long-term debt are disclosed in Notes 3, 7 and 8.

24. ENVIRONMENTAL REPORTING

As a consulting company, the Fund does not have environmental concerns.

25. COMPARATIVE FIGURES

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

Morneau Sobeco Income Fund (the "Fund") was formed on August 22, 2005 and commenced operations on September 30, 2005 when it completed an initial public offering ("IPO").

This Management's Discussion and Analysis ("MD&A") covers the three and six months ended June 30, 2008 and should be read in conjunction with the accompanying unaudited interim Consolidated Financial Statements of the Fund and notes thereto for the three and six months ended June 30, 2008 as well as the MD&A, and the Audited Consolidated Financial Statements and notes thereto contained in the Fund's Annual Report for the year ended December 31, 2007.

All financial information is presented in Canadian dollars and in accordance with Canadian generally accepted accounting principles ("GAAP") unless otherwise noted. Certain totals, subtotals and percentages may not reconcile due to rounding.

This MD&A contains "forward-looking statements" within the meaning of applicable securities laws, such as statements concerning anticipated future events, results, circumstances, performance or expectations that are not historical facts. Use of words such as "may", "will", "expect", "believe", or other words of similar effect may indicate a "forward-looking" statement. These statements are not guarantees of future performance and are subject to numerous risks and uncertainties, including those described in our publicly filed documents (available on SEDAR at *www.sedar.com*) and in this MD&A under the heading "Risks and Uncertainties". Those risks and uncertainties include income tax matters, ability to maintain profitability and manage growth, reliance on information systems and technology, reputational risk, dependence on key clients, reliance on key professionals and general economic conditions. Many of these risks and uncertainties can affect our actual results and could cause our actual results to differ materially from those expressed or implied in any forward-looking statement made by us or on our behalf. Given these risks and uncertainties, investors should not place undue reliance on forward-looking statements as a prediction of actual results. All forward-looking statements in this MD&A are qualified by these cautionary statements. These statements are made as of the date of this MD&A and, except as required by applicable law, we undertake no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events or otherwise. Additionally, we undertake no obligation to comment on analyses, expectations

or statements made by third parties in respect of the Fund, its financial or operating results or its securities.

To assist investors in assessing the Fund's financial performance, this discussion also makes reference to certain non-GAAP measures such as EBITDA, Standardized Distributable Cash, Adjusted Consolidated Distributable Cash, Standardized Distributable Cash Payout Ratio and Adjusted Consolidated Distributable Cash Payout Ratio. We believe that EBITDA is a useful measure in evaluating performance of the Fund. It is used to monitor compliance with debt covenants and to make decisions related to distributions to Unitholders rather than net income due to the significant amount of amortization expense related to our intangible assets. We also believe that Standardized Distributable Cash, Adjusted Consolidated Distributable Cash, Standardized Distributable Cash Payout Ratio and Adjusted Consolidated Distributable Cash Payout Ratio are useful supplemental measures of performance as they are generally used by Canadian open-ended business income funds as indicators of financial performance. See the footnotes to the "Results of Operations" chart for more details. Non-GAAP measures do not have any standard meaning prescribed by GAAP and therefore may not be comparable to similar measures presented by other issuers.

This MD&A is in all material respects in accordance with the recommendations provided in CICA's publication *Standardized Distributable Cash in Income Trusts and Other Flow-Through Entities: Guidance on Preparation and Disclosure*.

FORMATION AND OWNERSHIP STRUCTURE OF THE FUND

The Fund is an unincorporated, open-ended, limited purpose trust established under the laws of Ontario. It indirectly owns 35,096,913 Class A Limited Partnership units of Morneau Sobeco Group Limited Partnership ("MS Group LP"), which represents a 86.1% ownership interest. MS Group LP owns directly and indirectly 100% of Morneau Sobeco Limited Partnership, HRCO Inc. and Morneau Sobeco, Ltd. (the "Morneau Sobeco Operating Entities"). The 13.9% non-controlling interest in MS Group LP is held through Class B LP units of the limited partnership (the "Class B LP Units") and an equal number of Special Voting Units of the Fund, which together are exchangeable into Units. Management employees and former owners of the predecessors of the Morneau Sobeco Operating Entities ("Management Securityholders") hold this non-controlling interest.

On June 2, 2008, the Fund acquired substantially all the assets of Shepell FGI LP ("Shepell•fgi") from Clairvest Group Inc. and its partners. The Canadian Shepell•fgi business has been incorporated into HRCO Inc. (formerly Morneau Sobeco Corporation), a 100% owned subsidiary of MS Group LP. The US Shepell•fgi business has been amalgamated with Morneau Sobeco, Ltd.

As at June 30, 2008, 35,096,913 Units and 5,680,444 Special Voting Units of the Fund were issued and outstanding, and 5,680,444 MS Group LP Class B LP Units were issued and outstanding.

BUSINESS OVERVIEW

Morneau Sobeco Income Fund is the largest Canadian-owned firm providing human resource consulting and outsourcing services. The firm delivers solutions to assist employers in managing the financial security, health and productivity of their employees. With over 2,300 employees in offices across North America, Morneau Sobeco Income Fund offers its services to over 7,000 organizations situated in Canada, in the United States and around the globe.

We derive our revenue primarily from fees charged to clients for consulting engagements, outsourcing engagements and employee assistance program services. Fees from consulting engagements are charged based on billable hours or a fee-for-service basis. In some cases, consulting engagements may be billed on a fixed-fee basis, although these engagements are typically much smaller and the services are delivered over a shorter period of time. For some benefits consulting assignments which involve the purchase of an insurance policy underwritten by an insurance company, we may be paid commissions (in lieu of fees) by the client's insurance company, which is a common practice in the industry. These commissions are based on a percentage of the premiums paid by the client to the insurance company and our policy is to disclose them to our client. We assume no underwriting risk as the insurance policy is underwritten by the insurance company. In addition, we earn interest income from our cash balances which is included in other revenue. Fees from outsourcing engagements are generally based on negotiated fees or a formula tied to the nature of the service being provided.

Our outsourcing business is characterized by fixed contracts, which typically have three-year to five-year terms. Most outsourcing contracts contain an upfront implementation fee and an ongoing monthly service fee. Implementations usually take three to twelve months and involve transferring the

administration of a client's pension and/or benefits plans onto our systems, tailoring our systems and training our employees. Additional services provided that are outside the scope of the outsourcing contract are usually paid on a fee-for-service basis.

As a result of the acquisition of the business of Shepell•fgi , the firm offers employee assistance program ("EAP") services. The terms of many EAP client agreements require payment of a minimum retainer and incremental usage-based fees. The remainder of EAP agreements are billed based on a actual usage or fixed fees. Most EAP agreements may be terminated by the client upon 30 to 60 days' notice to the firm, however, it is typical for EAP agreements to continue for multiple years and many automatically renew on an annual basis.

Our largest operating expense is compensation and related costs. This includes salaries, annual performance-based bonuses, benefits (e.g., pension, health, dental), payroll taxes, independent service providers and temporary staffing services. The remaining operating expenses include occupancy costs, technology costs (equipment leases, telecommunications and software), non-recoverable client service costs (such as printing, travel and third-party professional services), training, marketing, office costs, professional services (legal and audit) and insurance.

SUMMARY AND OUTLOOK

In the second quarter of 2008 we met our expectations, from both a revenue and profitability standpoint. This quarter includes, for the first time, one month of results from the acquisition of Shepell•fgi which closed June 2, 2008. For the three and six months ended June 30, 2008 revenue growth including the one month of revenue from Shepell•fgi was 41.3% and 25.1%. Net Income for the three and six months ended June 30, 2008 was $2.5 million and $5.2 million respectively. Our EBITDA margin for the three and six months ended June 30, 2008 remained strong at 20.0% and 20.6%, respectively. Adjusting for the salary component of the Heath acquisition[1] in the amount of $0.5 million and $0.8 million for the three and six months ended June 30, 2008 and in the amount of $0.3 million and 0.5 million for the three and six months ended June 30, 2007, respectively, the EBITDA

(1) On June 1, 2006, the Fund indirectly acquired all of the issued and outstanding shares of Heath Benefits Consulting Inc. ("Heath"). A portion of the purchase price, which is conditional on the continuing employment of certain selling shareholders, is being recorded as salary expense over the required employment period to December 2008.

margin was 21.0% and 21.5% for the three and six months ended June 30, 2008 compared to 22.7% and 22.5% for the same period in 2007, respectively. EBITDA per Unit (basic) for the three and six months ended June 30, 2008 was $0.329 and $0.633 respectively which represents an increase of 12.7% and 10.1% respectively over the same periods in 2007. This is consistent with the growth in the Adjusted Consolidated Distributable Cash per Unit (basic) which grew 17.3% and 10.8% over the same periods and reflects the structure and accretion of the Shepell•fgi acquisition.

During the quarter, we completed our acquisition of Shepell•fgi. The total purchase price is $320 million including estimated transaction cost of $1.2 million. The consideration was satisfied by cash of $247.4 million and two non-interest bearing promissory notes of $75 million and $4.5 million repayable on July 2, 2009 and July 2, 2010, respectively. The promissory notes have been recorded at their combined present value of $71.4 million. The integration is proceeding as planned and the acquisition is immediately accretive. In addition as a result of the transaction being an asset purchase, a subsidiary of the Fund has approximately $220 million of eligible tax deductions which are deductible from taxable income at 7% per annum on a declining balance basis. Management believes the net present value of these tax deductions to be approximately $25 million and that they will result in substantial tax savings of approximately $15 million in 2011, with additional benefits beyond. As a result of these savings, the Fund is favourably positioned post 2010, when tax treatment of income funds changes.

On May 12, 2008, we announced our alliance with Sibson Consulting ("Sibson"), a division of Segal Company. This announcement reflects our goal to strengthen our presence in the US market through alliances with a firm offering complementary services. Sibson will turn to Morneau Sobeco to offer employee benefits administration outsourcing services to its clients in the U.S. Likewise, Morneau Sobeco will refer U.S. consulting mandates to Sibson. Since forming of the alliance, Morneau Sobeco and Sibson have been working on joint proposals for mutual and prospective clients. We have committed key resources to ensure we are effective in our efforts to coordinate our interactions with Sibson.

We are pleased with our results so far in 2008. We are achieving solid organic growth and are starting to realize the investment we have made in our outsourcing business over

previous quarters. In addition, the market for our services continues to be positive as we have successfully obtained a number of new clients which we have invested in and are contributing positively to our organic growth.

DISTRIBUTIONS TO UNITHOLDERS

Monthly distributions are declared by the Fund for Unitholders of record on the last business day of each month and are paid on about the 15th day of the following month.

As a result of the Shepell•fgi acquisition, which is immediately accretive to the Fund's distribution to Unitholders, the Board of Trustees authorized a 7% increase to our target monthly distribution from $0.07356 per Unit to $0.07871 per Unit effective to Unitholders of record on June 30, 2008.

The following table presents excess / (shortfall) cash flow from operating activities and net income over distributions to Unitholders for the three and six months ended June 30, 2008 and 2007 and for the years ended December 31, 2007 and 2006.

	Three Months Ended June 30, 2008	Three Months Ended June 30, 2007	Six Months Ended June 30, 2008	Six Months Ended June 30, 2007	Year Ended December 31, 2007	Year Ended December 31, 2006
	(In thousands of dollars)					
Cash flow from / (used in) operating activities	$10,528	$ 7,923	$10,472	$ 6,891	$ 27,878	$31,023
Net income	2,456	1,680	5,236	4,725	12,120	13,973
Distributions to Unitholders, including Class B LP Units	7,296	6,132	13,428	11,997	24,257	23,134
Excess/(shortfall) of cash flow from operating activities over distributions	3,232	1,791	(2,956)	(5,106)	3,621	7,889
(Shortfall) of net income from operating activities over distributions	(4,840)	(4,452)	(8,192)	(7,272)	(12,137)	(9,161)

We consider the amount of cash generated by the business in determining the amount of distributions payable to Unitholders. In general, we do not take into account quarterly working capital fluctuations as these tend to be temporary in nature. We do not generally consider net income in setting the level of distributions as this is a non-cash metric and is not reflective of the level of cash flow that we generate. The divergence is particularly relevant for us since we have a relatively high level of amortization expense as well as non-controlling interest related to the Class B LP Units. Our annual excess cash from operating activities over distributions has been used to finance growth in accounts receivable, capital expenditures and acquisitions.

The shortfall of cash flow from operating activities over distributions for the six months ended June 30, 2008 and 2007 are the result of the annual payment of employee bonuses which are paid in the first quarter of each year. We are confident based on our current budget and past history that our cash flow from operating activities will exceed our distributions on a year to date basis in future quarters.

The Standardized Distributable Cash Payout Ratios for the three and six months ended June 30, 2008 were 73.9% and 138.4% respectively compared to 83.4% and 194.1% for the same period in 2007. The Standardized Distributable Cash Payout Ratio was 87.0% on a twelve-month rolling basis ending June 30, 2008 compared to 90.6% for the same period in 2007. The Adjusted Consolidated Distributable Cash Payout Ratio for the three and six months ended June 30, 2008 was 75.0% and 77.0% compared to 84.9% and 81.8% for the same period in 2007. The Adjusted Consolidated Distributable Cash Payout Ratio was 82.9% on a twelve-month rolling basis ending June 30, 2008 compared to 84.3% for the same period in 2007. The favorable decline in the above ratios is due to the Shepell•fgi acquisition which, as expected, has provided a positive impact on the Fund's Standardized and Adjusted Consolidated Distributable Cash.

ANALYSIS OF 2008 SECOND QUARTER OPERATING RESULTS

Results of Operations

Selected Unaudited Consolidated Financial Information

	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
	(In thousands of dollars except per unit amounts)			
Revenue	$52,363	$37,057	$91,497	$73,148
Deduct:				
Salary, benefit and contractor expenses	32,428	21,574	56,765	43,247
Other operating expenses	9,449	7,377	15,857	13,930
Interest	1,915	315	3,006	768
Amortization of capital and intangible assets	6,946	4,354	11,249	8,652
Income taxes (recovery)	(1,321)	1,322	(1,797)	601
Non-controlling interest	490	435	1,181	1,225
Net income for the period	2,456	1,680	5,236	4,725
Add (deduct):				
Amortization of capital and intangible assets	6,946	4,354	11,249	8,652
Income taxes (recovery)	(1,321)	1,322	(1,797)	601
Interest	1,915	315	3,006	768
Non-controlling interest	490	435	1,181	1,225
EBITDA[(1)]	$10,486	$ 8,106	$18,875	$15,971
EBITDA margin	20.0%	21.9%	20.6%	21.8%
Cash from operating activities	$10,528	$ 7,923	$10,472	$ 6,891
Deduct: Capital expenditures	493	576	760	712
Consolidated Distributable Cash[(2)]	10,035	7,347	9,712	6,179
Deduct: Consolidated Distributable Cash available to non-controlling interest	1,853	1,512	1,789	1,272
Standardized Distributable Cash (available for Unitholders)[(3)]	$ 8,182	$ 5,835	$ 7,923	$ 4,907
Consolidated Distributable Cash[(2)]	$10,035	$ 7,347	$ 9,712	$ 6,179
Add (deduct): Non-cash operating working capital	(305)	(124)	7,717	8,483
Adjusted Consolidated Distributable Cash[(4)]	$ 9,730	$ 7,223	$17,429	$14,662
Net income per Unit (basic)	$ 0.093	$ 0.076	$ 0.215	$ 0.214
Net income per Unit (diluted)	$ 0.091	$ 0.076	$ 0.212	$ 0.214
EBITDA per Unit (basic)	$ 0.329	$ 0.292	$ 0.633	$ 0.575
Standardized Distributable Cash per Unit (basic)	$ 0.310	$ 0.264	$ 0.326	$ 0.222
Adjusted Consolidated Distributable Cash per Unit (basic)	$ 0.305	$ 0.260	$ 0.585	$ 0.528
Standardized Distributions declared per Unit (basic)	$ 0.226	$ 0.221	$ 0.447	$ 0.432
Standardized Distributable Cash Payout Ratio[(5)]	73.9%	83.4%	138.4%	194.1%
Adjusted Consolidated Distributable Cash Payout Ratio[(6)]	75.0%	84.9%	77.0%	81.8%
Twelve-month rolling Standardized Distributable Cash Payout Ratio	87.0%	90.6%	87.0%	90.6%
Twelve-month rolling Adjusted Consolidated Distributable Cash Payout Ratio	82.9%	84.3%	82.9%	84.3%

Footnotes:

(1) "EBITDA" is defined as net income before interest expense, income taxes (recovery), depreciation, amortization and non-controlling interest.

(2) "Consolidated Distributable Cash" is defined as cash from operating activities adjusted for maintenance capital expenditures.

(3) "Standardized Distributable Cash" is defined as cash from operating activities, including the effects of changes in non-cash operating working capital, less maintenance capital expenditures and Consolidated Distributable Cash available to non-controlling interest.

(4) "Adjusted Consolidated Distributable Cash" is defined as Consolidated Distributable Cash excluding changes in non-cash operating working capital.

(5) "Standardized Distributable Cash Payout Ratio" is defined as declared distributions divided by Standardized Distributable Cash.

(6) "Adjusted Consolidated Distributable Cash Payout Ratio" is defined as declared distributions divided by Adjusted Consolidated Distributable Cash.

ANALYSIS OF 2008 SECOND QUARTER RESULTS

Revenue

Revenue for the three months ended June 30, 2008 increased by $15.3 million, or 41.3%, to $52.4 million compared to $37.1 million for the same period in 2007. The increase in revenue was primarily due to revenue related to Shepell•fgi of $12.4 million, the inclusion of Cowan DB business[(2)] of $1.1 million and additional outsourcing business from a variety of clients.

Salary, benefit and contractor expenses

Salary, benefit and contractor expenses for the three months ended June 30, 2008 increased by $10.8 million, or 50.3%, to $32.4 million compared to $21.6 million for the same period in 2007. The increase was attributable to salary, benefit and contractor costs of $8.2 million due to the Shepell•fgi acquisition, $0.5 million due to the Cowan DB business acquisition, the additional staffing costs related to the outsourcing business of $0.7 million, adjustment related to Heath salary component of $0.2 million and general increases of $1.1 million.

Other Operating Expenses

Other operating expenses for the three months ended June 30, 2008 increased by $2.1 million or 28.1%, to $9.5 million compared to $7.4 million for the same period in 2007. The increase was primarily attributable to operating expenses of $1.9 million related to Shepell•fgi and general increases of $0.2 million.

Interest Expense

Interest expense for the three months ended June 30, 2008 increased by $1.6 million to $1.9 million compared to $0.3 million for the same period in 2007. The increase was primarily due to $0.5 million higher interest expense on the new term loan obtained to finance the Shepell•fgi acquisition, accretion interest of $ 0.6 million on the promissory notes issued as part

[(2)] On June 1, 2007, a subsidiary of the Fund directly acquired certain assets, liabilities and contracts of the defined benefit pension administration and actuarial consulting practices ("Cowan DB business") of Cowan Benefits Consulting Limited, a benefits consulting firm based in the Waterloo region, in Ontario.

of the Shepell•fgi acquisition and $0.4 million of loss incurred related to the termination of the interest rate swap agreements and write off of debt issue costs associated with the previous term loan.

Amortization of Capital and Intangible Assets

Amortization for the three months ended June 30, 2008 increased by $2.6 million, or 59.1%, to $7.0 million compared to $4.4 million for the same period in 2007. The increase was attributable to the increase in capital and intangible assets as a result of the acquisition of Shepell•fgi on June 2, 2008.

Income Tax Expense (Recovery)

Income tax recovery for the three months ended June 30, 2008 increased by $2.6 million to $1.3 million compared to income tax expenses of $1.3 million for the same period in 2007. The increase was primarily attributable to the recognition of a future tax expense of $2.7 million at the initial application of the SIFT rules in June 2007 and current income tax recovery of $0.3 million for the quarter due to the availability of the eligible tax deductions resulting from the acquisition of Shepell•fgi. This is partially offset by the favorable change in future tax rate in June 2007 of $0.3 million.

Net Income

As a result of the changes noted above, the net income for the three months ended June 30, 2008 was $2.5 million compared to the net income of $1.7 million for the same period in 2007.

Cash from Operating Activities

Cash from operating activities for the three months ended June 30, 2008 increased by $2.6 million to $10.5 million compared to $7.9 million for the same period in 2007. This increase was primarily due to improved EBITDA of $2.6 million after taking into account the salary component of Heath acquisition of $0.2 million and a net decrease in current taxes of $0.5 million and a net increase in changes in non-cash operating working capital of $0.2 million (see below). This is offset by additional interest paid (including swap termination fees) of $0.7 million related to the refinancing of the Fund's debt.

Changes in Non-Cash Operating Working Capital

Changes in non-cash operating working capital for the three months ended June 30, 2008 increased by $0.2 million to $0.3 million compared to $0.1 million for the same period in 2007.

The increase was primarily attributable to increased accounts payable and accrued liabilities net of deferred revenue of $3.2 million. This was partially offset by increased receivables net of unbilled fees of $1.1 million, increased prepaid expenses of $1.4 million and increased income tax recoverable of $0.5 million.

Non-GAAP Financial Measures: EBITDA, Standardized Distributable Cash and Adjusted Consolidated Distributable Cash

EBITDA

EBITDA for the three months ended June 30, 2008 increased by $2.4 million, or 30.0%, to $10.5 million compared to $8.1 million for the same period in 2007. The increase was due to increased revenue of $15.3 million offset by increased salary, benefit and contractor expenses and other operating expenses of $12.9 million.

Standardized Distributable Cash

Standardized Distributable Cash for the three months ended June 30, 2008 increased by $2.4 million to $8.2 million compared to $5.8 million for the same period in 2007. This increase was primarily due to increased cash from operating activities of $2.6 million and lower capital expenditures of $0.1 million, which was partially offset by an increase of $0.3 million in Consolidated Distributable Cash available to non-controlling interest.

Adjusted Consolidated Distributable Cash

Adjusted Consolidated Distributable Cash for the three months ended June 30, 2008 increased by $2.5 million to $9.7 million compared to $7.2 million for the same period in 2007. The increase was primarily due to increased EBITDA of $2.6 million after taking into account the salary component of Heath acquisition of $0.2 million, a net decrease in current taxes of $0.5 million and lower capital expenditures of $0.1 million. This was partially offset by additional interest paid (including swap termination fees) of $0.7 million.

ANALYSIS OF SIX MONTHS ENDED JUNE 30, 2008 AND 2007 RESULTS

Revenue

Revenue for the six months ended June 30, 2008 increased by $18.3 million, or 25.1%, to $91.5 million compared to $73.2 million for the same period in 2007. The increase in revenue was primarily due to revenue related to Shepell•fgi of $12.4 million, the inclusion of Cowan DB business[2] of $2.5 million and additional outsourcing business from a variety of clients.

Salary, benefit and contractor expenses

Salary, benefit and contractor expenses for the six months ended June 30, 2008 increased by $13.5 million, or 31.3%, to $56.7 million compared to $43.2 million for the same period in 2007. The increase was attributable to increased salary, benefit and contractor costs of $8.2 million due to the Shepell•fgi acquisition and $1.2 million due to the Cowan DB business acquisition, the additional staffing costs related to the outsourcing business of $1.3 million, adjustment related to Heath salary component of $0.2 million and general increases of $2.5 million.

Other Operating Expenses

Other operating expenses for the six months ended June 30, 2008 increased by $1.9 million or 13.8%, to $15.8 million compared to $13.9 million for the same period in 2007. The increase was primarily attributable to operating expenses of $1.9 million related to Shepell•fgi.

Interest Expense

Interest expense for the six months ended June 30, 2008 increased by $2.2 million to $3.0 million compared to $0.8 million for the same period in 2007. The increase was primarily due to higher interest expense of 0.5 million on new term loan obtained to finance the Shepell•fgi acquisition, accretion interest of $0.6 million on the promissory notes issued as part of the acquisition and $0.4 million in loss incurred related to the termination of the interest rate swap agreements and write off of debt issue costs associated with the previous term loan. In addition, the Fund recognized a loss of $0.7 million during the first quarter of 2008 due to change in the market value of the interest-rate swap.

Amortization of Capital and Intangible Assets

Amortization for the six months ended June 30, 2008 increased by $2.6 million, or 30.0%, to $11.3 million compared to $8.7 million for the same period in 2007. The increase was attributable to the increase in capital and intangible assets as a result of the acquisition of Shepell•fgi on June 2, 2008.

Income Tax Expense (Recovery)

Income tax recovery for the six months ended June 30, 2008 increased by $2.4 million to $1.8 million compared to income tax expenses of $0.6 million for the same period in 2007. The increase was primarily attributable to the recognition of a future tax expense of $2.7 million at the initial application of the SIFT rules in June 2007 and current income tax recovery of $0.1 million for the period due the availability of the eligible tax deductions resulting from the acquisition of Shepell•fgi. This is partially offset by the favorable change in future tax rate in June 2007 of $0.3 million.

Net Income

As a result of the changes noted above, the net income for the six months ended June 30, 2008 was $5.2 million compared to the net income of $4.7 million for the same period in 2007.

Cash from Operating Activities

Cash from operating activities for the six months ended June 30, 2008 increased by $3.6 million to $10.5 million compared to $6.9 million for the same period in 2007. This increase was primarily due to improved EBITDA of $3.1 million after taking into account the salary component of Heath acquisition of $0.2 million, a net decrease in current taxes of $0.4 million and a net increase in change in non-cash operating working capital of $0.8 million (see below). This is offset by additional interest paid (including swap termination fees) of $0.7 million.

Changes in Non-Cash Operating Working Capital

Changes in non-cash operating working capital for the six months ended June 30, 2008 increased by $0.8 million to a use of cash of $7.7 million compared to use of cash of $8.5 million for the same period in 2007. The increase was primarily attributable to increased accounts payable and accrued liabilities net of deferred revenue of $3.4 million, partially offset by

increased receivable net of unbilled fees of $0.1 million, increased prepaid expenses of $1.1 million and increased income tax recoverable of $1.4 million.

Non-GAAP Financial Measures: EBITDA, Standardized Distributable Cash and Adjusted Consolidated Distributable Cash

EBITDA

EBITDA for the six months ended June 30, 2008 increased by $2.9 million, or 18.2%, to $18.9 million compared to $16.0 million for the same period in 2007. The increase was due to increased revenue of $18.3 million offset by increased salary, benefit and contractor expenses and other operating expenses of $15.4 million.

Standardized Distributable Cash

Standardized Distributable Cash for the six months ended June 30, 2008 increased by $3.0 million to $7.9 million compared to $4.9 million for the same period in 2007. This increase was primarily due to increased cash from operating activities of $3.6 million, which was partially offset by an increase in capital expenditures of $0.1 million and $0.5 million in Consolidated Distributable Cash available to non-controlling interest.

Adjusted Consolidated Distributable Cash

Adjusted Consolidated Distributable Cash for the six months ended June 30, 2008 increased by $2.7 million to $17.4 million compared to $14.7 million for the same period in 2007. The increase was primarily due to increased EBITDA of $3.1 million after taking into account the salary component of Heath acquisition of $0.2 million, a net decrease in current taxes of $0.4 million. This is partially offset by additional interest paid (including swap termination fees) of $0.7 million and higher capital expenditures of $0.1 million.

LIQUIDITY AND CAPITAL RESOURCES

Cash Flows

The following table provides an overview of the Fund's cash flows for the periods indicated:

Cash Flow Information

Selected Unaudited Consolidated Financial Information

	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
	(In thousands of dollars)			
Cash provided by (used in):				
Operating activities	$ 10,528	$ 7,923	$ 10,472	$ 6,891
Investing activities	(247,500)	(4,103)	(247,767)	(4,239)
Financing activities	238,827	(2,292)	232,696	(8,343)
Increase (decrease) in cash . . .	$ 1,855	$ 1,528	$ (4,599)	$(5,691)

2008 Second Quarter Results

Cash from operating activities for the three months ended June 30, 2008 increased by $2.6 million to $10.5 million compared to $7.9 million for the same period in 2007. This increase was primarily due to improved EBITDA of $2.6 million after taking into account the salary component of Heath acquisition of $0.2 million and a net decrease in current taxes of $0.5 million and a net increase in changes in non-cash operating working capital of $0.2 million. This is offset by additional interest paid (including swap termination fees) of $0.7 million related to the refinancing of the Fund's debt.

Cash outflows from investing activities for the three months ended June 30, 2008 decreased by $243.4 million to $247.5 million compared to cash outflows of $4.1 million for the same period in 2007. This increase was primarily attributable to cash consideration paid, net of cash assumed, during the quarter for the Shepell•fgi acquisition of $246.2 million and the second instalment of the Heath acquisition of $0.8 million compared to cash consideration paid for Cowan DB business acquisition in June 2007 of $3.5 million.

Cash from financing activities for the three months ended June 30, 2008 increased by $241.1 million to $238.8 million compared to cash outflows of $2.3 million for the same period in 2007. This increase was primarily attributable to the proceeds from the public offering net of share issuance cost of

$142.5 million and net proceeds from long term debt net of debt issue costs of $100.1 million. This was partially offset by a lower utilization of the revolving loan of $1.5 million which was used to finance a small portion of the Shepell•fgi acquisition compared to the Cowan DB business acquisition in 2007.

Six Months Ended June 30, 2008 and 2007

Cash from operating activities for the six months ended June 30, 2008 increased by $3.6 million to $10.5 million compared to $6.9 million for the same period in 2007. This increase was primarily due to improved EBITDA of $3.1 million after taking into account the salary component of Heath acquisition of $0.2 million, a net decrease in current taxes of $0.4 million and a net increase in changes in non-cash operating working capital of $0.8 million. This was partially offset by additional interest paid (including swap termination fees) of $0.7 million.

Cash outflows from investing activities for the six months ended June 30, 2008 decreased by $243.5 million to $247.7 million compared to cash outflows of $4.2 million for the same period in 2007. This increase was primarily attributable to cash consideration paid, net of cash assumed, during the quarter for the Shepell•fgi acquisition of $246.2 million and the second instalment of the Heath acquisition of $0.8 million compared to cash consideration paid for Cowan DB business acquisition in June 2007 of $3.5 million.

Cash from financing activities for the six months ended June 30, 2008 increased by $241.0 million to $232.7 million compared to cash outflows of $8.3 million for the same period in 2007. This increase was primarily attributable to the proceeds from the public offering net of share issuance cost of $142.5 million and net proceeds from long term debt net of debt issue costs of $100.1 million. This was partially offset by lower utilization of revolving loan of $1.5 million which was used to finance a small portion of the Shepell•fgi acquisition compared to Cowan DB business acquisition in 2007 and $0.1 million increased in distribution payment due to the 7% increase to our target monthly distribution from $0.07356 per Unit to $0.07871 per Unit, following the closing of Shepell•fgi acquisition.

Capital Expenditures

Human resource consulting and outsourcing are not capital intensive. Our capital expenditures typically include office

furniture, facility improvements and information technology hardware and software. Additional capital expenditure requirements may result from significant business expansion. Such amounts are expected to be funded from our operating cash flow.

Contractual Obligations

Commitments

We lease office space and selected equipment under operating lease agreements with terms ranging from one to fifteen years. We also have a term loan, a revolving loan and two promissory notes described under "Capital Resources". Future expected payments are as follows:

Summary of Contractual Obligations

	Total	2008 to 2009	2010 to 2011	Beyond 2011
		(In thousands of dollars)		
Term loan	$137,000	$ —	$ —	$137,000
Revolving loan	2,300	2,300	—	—
Promissory notes	79,500	75,000	4,500	—
Operating leases	89,143	19,817	23,640	45,686
Total	$307,943	$97,117	$28,140	$182,686

In addition, the Fund has two subleases for which the Fund is liable for the rent in case of a default by the subtenants. The average annual rent for each of the leases is $0.2 million, expiring on October 30, 2011 and June 29, 2017, respectively.

Contingent Considerations

The purchase price for the Cowan DB business is expected to be approximately $6.0 million and the amount will be paid in three instalments. The first instalment of $3.8 million was made on the closing date of June 1, 2007. The second instalment has been determined to be $1.0 million and was paid on August 1, 2008. The third instalment is subject to adjustment based on final pension administration and actuarial consulting services revenue and will be payable on August 1, 2009. In addition, we have issued a standby letter of credit in the amount of $0.4 million which will be paid before December 31, 2008 to the extent the vendor has performed all of its transition services obligations.

The purchase price for Heath is $16.8 million, including estimated consideration to compensate for forgone distributions

payable on its third instalment during the period June 1, 2006 to December 31, 2008. The purchase price is being paid in three instalments. The first instalment of $9.0 million was made on closing in 2006. The second instalment of was paid on June 30, 2008 by cash of $0.8 million and $3.0 million in Class B LP Units of MS Group LP based on a predetermined value of $12.52 per Unit. The third instalment will be settled on December 1 of 2008 in the same manner as the second instalment.

The Fund has no material contractual obligations other than those described in this MD&A and has no off-balance sheet financing arrangements.

Capital Resources

The following table provides an overview of the Fund's capital resources:

Capital Resources	As at June 30, 2008	As at December 31, 2007
	(In thousands of dollars)	
Cash (bank indebtedness)	$ (1,701)	$ 2,898
Revolving loan	$ 2,300	$ —
Long-term debt, net of unamortized debt issue cost	$135,162	$ 34,913
Promissory notes	$ 71,928	$ —
Unitholders' equity	$340,197	$197,668

We have historically utilized cash from operations to finance working capital requirements and fund growth. As at June 30, 2008, the Fund's working capital (current assets minus current liabilities) was approximately $18.6 million.

New credit agreement

As part of the Shepell•fgi acquisition the Fund entered into a new credit agreement with a syndicate of Canadian chartered banks for a period of four years maturing on June 1, 2012. Under the agreement, the following credit facilities are available:

- $20 million senior secured revolving facility ("revolving loan").
- $137 million senior secured non-revolving term loan ("term loan").
- $40 million senior secured non-revolving delayed draw term facility. This facility shall be available until

July 2, 2009 by way of a single draw to fund a portion of the $75 million promissory note issued in connection with the acquisition.

The interest rates for the facilities are floating, based on a margin over certain reference rates of interest. The applicable margin may vary up and down depending on the ratio of the Fund's consolidated debt to Adjusted EBITDA as calculated in the new credit agreement. Adjusted EBITDA is defined as the rolling twelve months earnings before interest, taxes, deprecation and amortization of the Fund and Shepell•fgi.

The credit facilities are secured by a general assignment of all the assets of the Fund. The new credit agreement also requires the Fund to maintain the following financial covenants on a consolidated basis:

(i) Ratio of debt to Adjusted EBITDA shall commence at 3.5:1.0 for the period up to December 30, 2009 and decline to 2.5:1.0 by June 30, 2011.

(ii) Ratio of EBITDA to interest expense of not less than 3.0 to 1.0

EBITDA is defined as net income before interest expense, income taxes (recovery), depreciation, amortization and non-controlling interest.

The Fund complied with all the required financial covenants and the ratios as at June 30, 2008 were 3.0 and 16.0 respectively.

Promissory notes

The promissory notes issued as part of the Shepell•fgi acquisition in the amounts of $75 million and $4.5 million are due on July 2, 2009 and July 2, 2010, respectively. The notes are non-interest bearing and are secured by a general assignment of all the assets of the Fund, which is subordinated to the credit facilities. The notes have been recorded at their initial combined present value of $71.4 million plus accreted interest to date of $0.57 million.

The Fund has the option to repay up to 50% of the $75 million promissory note and 100% of the $4.5 million promissory note through the issuance of Units at a 5% discounted value, subject to the Fund's ability to issue new Units under the guidance for income trusts and other flow-through entities that qualify for

the four-year transitional relief. It is the Fund's intention to repay the notes through future cash flow and as a result, the notes are recorded as liabilities.

The promissory notes also include a covenant that the Fund and its subsidiaries shall not incur any debt other than permitted debt as defined in the promissory note agreements unless, after the incurrence of such debt, the Fund would have on a pro forma consolidated basis a ratio of debt to adjusted EBITDA of not greater than 4.5:1.0 determined as of end of the fiscal quarter ending immediately prior to the date of determination.

SELECTED BALANCE SHEET DATA

The following table provides an overview of the Fund's selected balance sheet data:

Selected Balance Sheet Data	As at June 30, 2008	As at December 31, 2007
	(in thousands of dollars)	
Current assets	$ 64,909	$ 35,224
Other long-term assets	$623,895	$299,204
Current liabilities	$ 46,312	$ 15,541

Current Assets

Current assets as at June 30, 2008 increased by $29.7 million to $64.9 million from $35.2 million as at December 31, 2007. The increase was primarily due increased accounts receivable net of unbilled fees of $28.1 million, increased prepaid expenses of $3.4 million and increased income tax recoverable of $1.1 million, largely due to the Shepell•fgi acquisition. This was partially offset by decreased cash of $2.9 million due to the payment of our annual bonuses in the first quarter of 2008.

Other Long-Term Assets

Other long-term assets as at June 30, 2008 increased by $324.7 million to $623.9 million from $299.2 million as at December 31, 2007. The increase was primarily due to the addition of capital assets net of amortization of $6.8 million, the addition of intangible assets net of amortization of $188.9 million, the addition of goodwill of $121.6 million, an increase in future income tax assets of $2.6 million and an increase in the interest-rate-swap of $0.2 million, primarily related to the Shepell•fgi acquisition. In addition, goodwill also increased by $4.6 million during the period due to the recognition of the second and third instalments with respect to the Heath acquisition.

Current Liabilities

Current liabilities as at June 30, 2008 increased by $30.8 million to $46.3 million from $15.5 million as at December 31, 2007. The increase was primarily related to increased accounts payable and accrued liabilities of $23.3 million, increased deferred revenue of $2.3 million, increased bank borrowing of $4.0 million and increased Unitholder distributions payable of $1.2 million, largely due to the Shepell•fgi acquisition.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of financial statements, in accordance with GAAP, requires us to make estimates and assumptions that affect the reported values of assets and liabilities as well as disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. These estimates are reviewed periodically and, as adjustments become necessary, they are reported in earnings in the periods in which they become known. Accordingly, actual results could differ from these estimates. The accounting policies and estimates that are critical to the Fund's business relate to the following items:

Revenue Recognition

We earn fee-for-service revenue based on hourly rates and the time spent delivering those services. We also earn contracted revenue based on negotiated fixed amounts or on a formula tied to the nature of the service, rather than the time spent. Revenue is recognized in the period that the service is rendered, irrespective of when it is invoiced. EAP revenue is recognized through a combination of the minimum contracted amount and incremental usage above the minimum thresholds. The minimum contracted amount is recognized on a straight-line basis over the term of the contract. Incremental usage is recognized when the minimum usage threshold is exceeded. Unbilled fees are recorded at the lower of unbilled hours worked at standard billing rates and the amount which we estimate can be recovered upon invoicing. Expenses are recognized as incurred. Losses on fixed-fee contracts are recognized during the period in which the loss becomes probable. Billings in excess of revenue are recorded as a deferred revenue liability until services are rendered. Revenue does not include reimbursements for recoverable expenses, such as employee travel expenses, outside printing and third-party professional services. Reimbursements are accounted for as a reduction to expenses.

We also earn commission revenue as payment for the provision of benefits consulting services to clients, as a percentage of insurance premiums paid by our clients. Commission revenue is received annually, semi-annually, quarterly or monthly. Annual commissions are typically paid at the beginning of the insurance policy period and are recognized as income at the later of the billing or effective date of the policy, net of a provision for return commissions due to policy cancellations or change of broker.

Intangible Assets and Goodwill

Intangible assets consist of trade names, customer relationships, proprietary software, customer contracts and non-compete agreements. Intangible assets with a finite life are amortized on a straight-line basis over their estimated useful lives. Intangible assets with an indefinite life are not amortized but are tested for impairment annually or more frequently if events or circumstances indicate there may be an impairment by comparing the estimated discounted future net cash flows from the asset to its carrying amount.

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

Allowance for Doubtful Accounts

A provision for accounts receivable resulting from the potential risk that the accounts receivable will not be collected has been recorded. We continually monitor past due accounts to assess the likelihood of collection to estimate the required provision.

Litigation and Claims

We are involved in litigation and other claims arising in the normal course of business. We must use judgment to determine whether or not a claim has any merit, the amount of the claim and whether to record a provision, which is dependent upon the potential success of the claim. We believe that none of the current claims will have a material adverse impact on the financial position of the Fund.

Future Income Taxes

The Fund uses the asset and liability method of accounting for income taxes. Future income taxes are recognized for the

temporary differences between the financial statement carrying amounts of assets and liabilities and their respective tax bases. Future income tax assets and liabilities are measured using enacted or substantively enacted tax rates and laws that are expected to apply to taxable income in the years in which those temporary differences are expected to be reversed or settled. The effect on future income tax assets and liabilities of a change in tax rate is recognized in income in the period that includes the date of enactment or substantive enactment.

Financial Instruments

Financial assets and financial liabilities held-for-trading are measured at fair value with changes in those fair values recognized in the income statement. Loans and receivables and other financial liabilities are measured at amortized cost using the effective interest method of amortization. The Fund had neither available-for-sale nor held-to-maturity instruments.

Transaction costs are expensed as incurred for financial instruments classified or designated as held–for-trading. For other financial instruments, transaction costs are capitalized on initial recognition and are included in the underlying balance.

The interest-rate swap agreements, that are not subject to hedge accounting are classified as held-for-trading and are recorded at their fair value with a corresponding adjustment to interest expense.

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

New Accounting Policies

Effective January 1, 2008 the Fund adopted the following new accounting standards:

1. Section 3862, *Financial Instruments – Disclosures* and Section 3863, *Financial Instruments – Presentation*, which replace the existing Section 3861, *Financial Instruments – Disclosure and Presentation*. These new sections revise and enhance disclosure requirements and carry forward unchanged existing presentation requirements. These new sections place an increased emphasis on disclosures and presentation regarding the risks associated with both recognized and unrecognized financial instruments and how the Fund manages those risks.

2. Section 1535, *Capital Disclosure*. This section requires disclosure of the Fund's objectives, policies and processes for managing capital, quantitative data about what the Fund regards as capital and whether the Fund has complied with any capital requirements.

These new standards relate to disclosures and presentation only and did not have an impact on the Fund's financial results or position.

Future Accounting Changes

1. Section 3064, *Goodwill and intangible assets* – In February 2008, the CICA issued the new Handbook replacing Section 3062, *Goodwill and Other Intangible Assets* and Section 3450, *Research and Development Costs*. The new standard will be applicable to financial statements relating to fiscal years beginning on or after October 1, 2008. This section establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets. The standards concerning goodwill are unchanged from the standards included in the previous section 3062. The Fund is currently assessing the impact this new standard will have on its consolidated financial statements, if any.

2. International Financial Reporting Standards – The Canadian Accounting Standards Board confirmed in February 2008 plans to converge Canadian GAAP with International Financial Reporting Standards ("IFRS") over a transition period expected to be effective for interim and annual periods commencing January 1, 2011. The Fund is currently assessing the new standards and has not yet determined the impact on its consolidated financial condition.

RISKS AND UNCERTAINTIES

The results of operations, business prospects and financial condition of the Fund are subject to a number of risks and uncertainties and are affected by a number of factors outside our control.

Risk Related to the Business of Morneau Sobeco

Ability to Maintain Profitability and Manage Growth

There can be no assurance that Morneau Sobeco will be able to sustain profitability in future periods. Morneau Sobeco's future operating results will depend on a number of factors, including its ability to continue to successfully execute its strategic initiatives.

There can be no assurance that Morneau Sobeco will be successful in achieving its strategic plan or that its strategic plan will enable the firm to maintain its historical revenue growth rates or to sustain profitability. Failure to successfully execute any material part of Morneau Sobeco's strategic plan could have a material adverse effect on its business, financial condition and operating results, and the ability of the Fund to make distributions on the Units.

There can be no assurance that Morneau Sobeco will be able to effectively manage its growth, and any failure to do so could have a material adverse effect on the Fund's business, financial condition and operating results, and on the ability of the Fund to make distributions on the Units.

Integration of Shepell•fgi

While Management believes that the operation of Morneau Sobeco and Shepell•fgi can be successfully integrated, there can be no assurance that this will be the case. Morneau Sobeco could face impediments in its ability to implement its integration strategy. In addition, there can be no assurance that unforeseen costs and expenses or other factors will not offset, in whole or in part, the expected benefits of Morneau Sobeco’s integration and operating plans.

The successful integration and management of the business involves numerous risks that could adversely affect the Fund’s growth and profitability, including: (i) the risk that Management may not be able to successfully manage the operations of Shepell•fgi and the integration may place

significant demands on Management, diverting their attention from existing operations; (ii) the risk that the Fund's operational, financial and management systems may be incompatible with or inadequate to effectively integrate and manage the acquired systems; (iii) the risk that the acquisition may require unforeseen substantial financial resources that otherwise could be used in the development of other aspects of the business; and (iv) the risk that customers and channel partners may not be retained following the acquisition, which could be significant to the Fund's operation. The successful integration of the acquisition is also subject to the risk that personnel from the Shepell•fgi business and the existing Morneau Sobeco business may not be able to work together successfully, which could affect the operation of the combined business.

Failure to successfully integrate the operations of Morneau Sobeco and Shepell•fgi could have a material adverse effect on the Fund's business, financial condition, liquidity and results of operations.

Potential Undisclosed Liabilities Associated with Acquisition/ Limited Indemnification

In connection with the acquisitions completed by the Fund, there may be liabilities and contingencies that the Fund failed to discover or was unable to quantify in its due diligence which it conducted prior to the execution of an acquisition, and the Fund may not be indemnified for some or all of these liabilities and contingencies. The existence of any material liabilities or contingencies could have a material adverse effect on the Fund's business, financial condition, liquidity and results of operations.

Reliance on Information Systems and Technology

Information systems are an integral part of Morneau Sobeco's business and the products and services offered to its clients. Morneau Sobeco relies on systems to maintain accurate records and to carry out required administrative functions in accordance with the terms of its contractual obligations to its clients. Morneau Sobeco relies on the Internet as a key mechanism for delivering services to clients and achieving efficiencies in its service model. The Internet has experienced, and is expected to continue to experience, significant growth in the number of users and volume of traffic. As a result, its performance and reliability may decline. In order to maintain

the level of security, service and reliability that clients require, Morneau Sobeco may be required to make significant investments in the online means of delivering consulting and outsourcing services. In addition, Web sites and proprietary online services have experienced service interruptions and other delays. If these outages or delays occur frequently in the future, Internet usage as a medium of exchange of information could decline and the Internet might not adequately support the firm's Web-based tools. The adoption of additional laws or regulations with respect to the Internet may impede the efficiency of the Internet as a medium of exchange of information and decrease the demand for Morneau Sobeco's services.

Any disruptions in Morneau Sobeco's systems, the failure of the systems to operate as expected or the firm's ability to use the Internet effectively to deliver services could, depending on the magnitude of the problem, result in a loss of current or future business and/or potential claims against Morneau Sobeco, all of which could have a material adverse effect on Morneau Sobeco's business, financial condition and operating results, and on the ability of the Fund to make distributions on the Units.

Reputational Risk

Morneau Sobeco depends, to a large extent, on its relationships with its clients and its reputation for high-quality outsourcing and consulting services. As a result, the impact of a client not being satisfied with Morneau Sobeco's services or products may be more damaging in Morneau Sobeco's business than in other businesses. Moreover, if the firm fails to meet its contractual obligations, Morneau Sobeco could be subject to legal liability and a loss of client relationships.

Dependence on Key Clients

For the three and six months ended June 30, 2008, Morneau Sobeco's largest client accounted for approximately 7% and 9% of revenue (three and six months ended June 30, 2007 – 10%) and its top 10 clients, in the aggregate, accounted for approximately 26% and 27% of revenue, respectively (three and six months ended June 30, 2007 – 33%). As clients may terminate engagements with minimal notice, there can be no assurance that Morneau Sobeco will be able to retain relationships with its largest clients. Moreover, there can be no assurance that such clients will continue to use Morneau Sobeco's services in the future. Any negative change involving any of Morneau Sobeco's largest clients, including but not

limited to a client's financial condition or desire to continue using the firm's services, could result in a significant reduction in revenue which could have a material adverse effect on Morneau Sobeco's business, financial condition and operating results, and on the ability of the Fund to make distributions on the Units.

Risk of Future Legal Proceedings

Morneau Sobeco may be threatened with, or may be named as a defendant in, or may become subject to, various legal proceedings in the ordinary course of conducting its business, including lawsuits based upon professional errors and omissions.

The pension and benefits consulting and outsourcing service involves assumptions and estimates concerning future events, the actual outcome of which cannot be known with certainty in advance. In addition, computational, software programming or data management errors could occur. For example, possible legal proceedings could result from:

(i) a client's assertion that actuarial assumptions used in a pension plan were unreasonable, leading to plan underfunding;

(ii) a claim that inaccurate data was used, which could lead to an underestimation of plan liabilities; or

(iii) a claim that employee benefits plan documents were misinterpreted or plan amendments were misstated in plan documents, which could lead to overpayments to beneficiaries.

The employee health and productivity services involve confidential counseling, occupational health activities and case management. Each of these activities could potentially put the Fund in conflict with its customers, their employees, or both.

Defending lawsuits of this nature could require much management attention, which could divert its focus from operations. Such claims could produce negative publicity that could hurt Morneau Sobeco's reputation and business. A significant judgment against Morneau Sobeco, or the imposition of a significant fine or penalty as a result of a finding that Morneau Sobeco failed to comply with laws or regulations, could have a material adverse effect on Morneau Sobeco's business, financial condition and operating results, and on the ability of the Fund to make distributions on the Units.

Reliance on Key Professionals

Morneau Sobeco's operations are dependent on the abilities, experiences and efforts of its professionals, many of whom have excellent reputations and a significant number of contacts in the industry in which Morneau Sobeco operates. Morneau Sobeco's business depends, in part, on its professionals' ability to develop and maintain alliances with businesses such as brokerage firms, financial services companies, healthcare organizations, insurance companies, business process outsourcing organizations and other companies, in order to develop, market and deliver its services. If Morneau Sobeco's strategic alliances are discontinued due to the loss of professional staff or if the firm has difficulty developing new alliances, profitability could be negatively impacted. Should any member of its professional staff be unable or unwilling to continue his or her relationship with Morneau Sobeco, this change could have a material adverse effect on Morneau Sobeco's business, financial condition and operating results, and on the ability of the Fund to make distributions on the Units.

Reliance on Service Providers

Morneau Sobeco relies on a network of independent service providers to provide its EAP services to clients in numerous countries. There can be no assurance that the cost of retaining these service providers in the future will not increase or that any increases can be passed on to the clients. In addition, some of EAP service providers in certain jurisdictions have, in the past, become its competitors. This could have a material adverse effect on Morneau Sobeco's business, financial condition and operating results, and on the ability of the Fund to make distributions on the Units.

Relationships with Channel Partners

Morneau Sobeco markets its services directly to end user employers as well as through certain channel partners, primarily insurance companies (many of which compete amongst themselves directly). There can be no assurance that Morneau Sobeco will be able to maintain its existing relationships with all these channel partners which could have a material adverse effect on Morneau Sobeco's business, financial condition and operating results, and on the ability of the Fund to make distributions on the Units.

Competition

Morneau Sobeco operates in a highly competitive North American market. As a result, Morneau Sobeco competes with

many domestic and international firms. Some of its competitors have achieved substantially more market penetration in certain of the areas in which Morneau Sobeco competes. In addition, some of Morneau Sobeco's competitors have substantially more financial resources and/or financial flexibility than Morneau Sobeco. Competitive forces could result in reduced market share and thus have a material adverse effect on Morneau Sobeco's business, financial condition and operating results, and on the ability of the Fund to make distributions on the Units.

Legislative and Regulatory Changes

The business of pension and benefits consulting and outsourcing is highly regulated and laws are constantly evolving. Currently the provisions of employee health and productivity services are not generally subject to government regulation. However, there is no certainty that regulation will not be introduced as governments in these countries adjust their policies and practices in the health care industry.

Any changes to laws, rules, regulations or policies could have a material adverse effect on Morneau Sobeco's business, financial condition and operating results, and on the ability of the Fund to make distributions on the Units.

Changes in Business Conditions

Morneau Sobeco's future success depends, in part, on its ability to develop and implement technology solutions that anticipate and keep pace with rapid and continuing changes in technology, industry standards and client preferences. The firm may not be successful in anticipating or responding to these developments on a timely basis and its ideas may not be accepted in the marketplace. The effort to gain technological expertise and develop new technologies in its business requires Morneau Sobeco to incur significant expenses. If Morneau Sobeco cannot offer new technologies as quickly as its competitors, or if the competition develops more cost-effective technologies, Morneau Sobeco could lose market share. Also, products and technologies developed by Morneau Sobeco's competitors may make the firm's service or product offerings non-competitive or obsolete. Any one of these circumstances could have a material adverse effect on Morneau Sobeco's ability to obtain and fulfill important client engagements, and thus could have a material adverse effect on Morneau Sobeco's business, financial condition and operating results, and on the ability of the Fund to make distributions on the Units.

Timely Completion of Projects and Performance of Obligations

In its contracts with clients, Morneau Sobeco is sometimes committed to complete a project by a scheduled date. If the project is not completed by the scheduled date, Morneau Sobeco may either incur significant additional costs or be held responsible for the costs incurred by the client to rectify damages due to the late completion. Morneau Sobeco's success depends in large part on whether it fulfills these and other contractual obligations with clients and maintains client satisfaction. If Morneau Sobeco fails to satisfactorily perform its contractual obligations, its clients could terminate contracts and/or take legal action against Morneau Sobeco. Such occurrences could result in a loss of its professional reputation and in extra costs needed to defend or rectify the situation and thus have a material adverse effect on Morneau Sobeco's business, financial condition and operating results, and on the ability of the Fund to make distributions on the Units.

Timing of Revenue Collection Related to Fixed-Price Contract with Predetermined Threshold

The Fund recognizes certain revenues related to the EAP services that arise when clients' usage exceeds predetermined thresholds. Frequently, these revenues cannot be billed and collected until the anniversary date of the agreement. The time delay between earning this revenue and collecting it potentially increases the risk of not collecting on these unbilled receivables, which may negatively affect the ability of the Fund to make distribution on the Units.

Implications of Fixed-Price Contracts

A portion of Morneau Sobeco's revenue comes from fixed-price contracts. A fixed-price contract requires Morneau Sobeco to perform either all or a specified portion of work under the contract for a fixed price. Fixed-price contracts expose Morneau Sobeco to a number of risks, including underestimation of costs, ambiguities in specifications, unforeseen costs or difficulties, problems with new technologies, delays beyond the control of Morneau Sobeco, failures of subcontractors to perform, and economic or other changes that may occur during the contract period. Increasing use of fixed-price contracts and/or increasing the size of such contracts would increase Morneau Sobeco's exposure to these risks. Losses under fixed-price contracts could have a material adverse effect on Morneau Sobeco's business, financial condition and operating results, and on the ability of the Fund to make distributions on the Units.

Confidentiality of Client Information

Morneau Sobeco depends to a large extent on its relationships with its customers and its ability to properly maintain confidential client information. The failure of Morneau Sobeco to maintain client confidentiality could, depending on the magnitude of the problem, result in a loss of future business and/or potential claims against Morneau Sobeco which could have a material adverse effect on Morneau Sobeco's business, financial condition and operating results, and on the ability of the Fund to make distributions on the Units.

Foreign Exchange Risk

A portion of Morneau Sobeco's sales are in U.S. dollars and thus Morneau Sobeco is exposed to fluctuations in the value of the U.S. dollar relative to the Canadian dollar. The firm is not currently engaged in currency hedging activities. The net revenue exposure after accounting for related expenses denominated in U.S. dollars was approximately US$1.5 million and US$2.7 million, respectively for the three and six months ended June 30, 2008. An increase in foreign revenues would expose the Fund to fluctuations in exchange rates which may have a material adverse effect on Morneau Sobeco's business, financial condition, and operating results, and on the ability of the Fund to make distributions on the Units.

Interest Rate Fluctuations

Morneau Sobeco may be exposed to fluctuations in interest rates under its borrowings. Interest-rate swap agreements are used as part of the Fund's program to manage the fixed and floating interest rate mix of the Fund's total debt outstanding and related overall cost of borrowing. Increases in interest rates may have a material adverse effect on Morneau Sobeco's business, financial condition and operating results, and on the ability of the Fund to make distributions on the Units.

Protection of Intellectual Property

Morneau Sobeco continually develops and improves its proprietary technology solutions for clients. No assurance can be given that Morneau Sobeco's competitors will not develop substantially similar technology. Morneau Sobeco relies on one or more of the following to protect its proprietary rights: trademarks, copyrights, trade secrets, confidentiality procedures and contractual provisions. Despite Morneau Sobeco's efforts to protect its proprietary rights, unauthorized parties may

attempt to obtain and use information that Morneau Sobeco regards as proprietary. Stopping unauthorized use of Morneau Sobeco's intellectual property may be difficult, time-consuming and costly. There can be no assurance that Morneau Sobeco will be successful in protecting its proprietary rights and, if it is not, this could have a material adverse effect on Morneau Sobeco's business, financial condition and operating results, and on the ability of the Fund to make distributions on the Units.

Rising Insurance Costs

The cost of maintaining professional errors and omissions insurance as well as director and officer liability insurance is significant. Morneau Sobeco could experience higher insurance premiums as a result of adverse claims experience or because of general increases in premiums by insurance carriers for reasons unrelated to its own claims experience. Generally, Morneau Sobeco's insurance policies must be renewed annually. Its ability to continue to obtain insurance at affordable premiums depends upon its ability to continue to operate with an acceptable claims record. A significant increase in the number of claims, the existence of one or more claims in excess of its policy limits or the inability to obtain adequate insurance coverage at acceptable rates, or at all, could have a material adverse effect on Morneau Sobeco's business, financial condition and operating results, and on the ability of the Fund to make distributions on the Units.

Risk Related to the Structure of the Fund

Income Tax Matters

There can be no assurance that Canadian federal income tax laws and administrative policies respecting the treatment of mutual fund trusts will not be changed in a manner which may adversely affect the Unitholders.

The Fund's Declaration of Trust provides that a sufficient amount of the Fund's net income and net realized capital gains shall be distributed each year to Unitholders in order to eliminate the Fund's liability for tax under Part 1 of the *Income Tax Act (Canada)*. Where such amount of net income and net realized capital gains of the Fund in a taxation year exceeds the cash available for distribution in the year, such excess net income and net realized capital gains will be distributed to Unitholders in the form of additional Units. Unitholders are generally required to include an amount equal to the fair market value of those Units in their taxable income, in circumstances when they do not directly receive a cash distribution.

On June 22, 2007, legislation that proposed changes to the taxation of publicly traded income trusts ("the SIFT Rules") received Royal Assent. Certain income of (and distributions made by) the Fund will be taxed in a manner similar to income earned by (and distributions made by) a corporation in the 2011 taxation year.

As a result, the Fund has recognized a $2.7 million future income tax liability as at June 30, 2007 on temporary differences in the reported amounts for financial statement and tax purposes relating to the intangible and capital assets. The Fund will be liable for income tax at a rate of 29.5% on its taxable income earned in 2011 and 28.0% thereafter.

This legislation is effective for the 2007 taxation year with respect to trusts which commenced public trading after October 31, 2006, but the application of the rules will be delayed to the 2011 taxation year with respect to trusts which were publicly traded prior to November 1, 2006.

On December 15, 2006, the Department of Finance (Canada) released guidance for income trusts and other flow-through entities that qualify for the four-year transitional relief. The guidance establishes objective tests with respect to how much an income trust is permitted to grow without jeopardizing its transitional relief. In general, the Fund will be permitted to issue new equity over the next four years equal to its market capitalization as of the end of trading on October 31, 2006 (subject to certain annual limits). Market capitalization, for these purposes, is to be measured in terms of the value of the Fund's issued and outstanding publicly traded Units. If these limits are exceeded, the Fund may lose its transitional relief and thereby become immediately subject to the proposed SIFT Rules.

On December 20, 2007, the Department of Finance (Canada) announced proposed technical amendments to clarify certain aspects of the new rules (which, as discussed above, will be effective on January 1, 2011, subject to compliance with the normal growth guidelines). One of the proposed amendments is intended to exempt from the new rules a subsidiary partnership that (i) is not publicly traded, and (ii) is wholly-owned by a publicly traded trust or partnership, a taxable Canadian corporation or a combination of these entities. Although the MS Group LP is not publicly traded, the proposed amendments do not appear to exempt a partnership with individual partners. Draft legislation implementing these amendments has been released on July 14, 2008. However, the

Fund believes that the MS Group LP will not be subject to tax under the new rules prior to January 2011, assuming that the Fund complies with the normal growth guidelines.

This legislation may adversely affect the marketability of the Fund's Units and the ability of the Fund to undertake financings and acquisitions, and, at such time as the SIFT Rules apply to the Fund, the distributable cash of the Fund may be materially reduced.

Dependence on Morneau Sobeco Group LP and Its Subsidiaries

The Fund is an unincorporated open-ended, limited purpose trust that is entirely dependent on the operations and assets of the Trust. Cash distributions to Unitholders will be dependent on, among other things, the ability of the Trust to pay interest on the Trust Notes and to make cash distributions in respect of the Trust Units, which, in turn, are dependent on MS Group LP making cash distributions. MS Group LP's ability to make cash distributions is dependent on the ability of its subsidiaries to make cash distributions or other payments or advances. This will be subject to applicable laws and regulations and contractual restrictions contained in the instruments governing any indebtedness of those entities, including restrictive covenants in the credit facilities.

Cash Distributions Are Not Guaranteed and Will Fluctuate With the Business Performance

Although the Fund intends to distribute the interest received in respect of the Trust Notes and the cash distributions received in respect of the Trust Units, less expenses and amounts, if any, paid by the Fund in connection with the redemption of Units, there can be no assurance regarding the amounts of income to be generated by MS Group LP's businesses or ultimately distributed to the Fund. The ability of the Fund to make cash distributions, and the actual amount distributed, will be entirely dependent on the operations and assets of MS Group LP (and its subsidiaries), and will be subject to various factors including each of its financial performance, its obligations under applicable credit facilities, fluctuations in its working capital, the sustainability of its margins and its capital expenditure requirements. The market value of the Units may deteriorate if the Fund is unable to meet its distribution targets in the future, and that deterioration may be significant. In addition, the composition of cash distributions for tax purposes may change over time and may affect the after-tax return for investors.

Restrictions on Potential Growth

The payout by Morneau Sobeco of substantially all of its operating cash flow will make additional capital and operating expenditures dependent on increased cash flow or additional financing in the future. Lack of those funds could limit the future growth of Morneau Sobeco and its cash flow.

Nature of Units

The Units share certain attributes common to both equity securities and debt instruments. The Units do not represent a direct investment in the businesses of Morneau Sobeco and should not be viewed by investors as direct securities of HRCO Inc. (formerly Morneau Sobeco Corporation) or its subsidiaries. Unitholders will not have the statutory rights normally associated with ownership of shares of a corporation including, for example, the right to bring "oppression" or "derivative" actions or rights of dissent. The Units represent a fractional interest in the Fund. The Fund's primary assets are Trust Units and Trust Notes.

The Units are not "deposits" within the meaning of the *Canada Deposit Insurance Corporations Act (Canada)* and are not insured under the provisions of that Act or any other legislation. Furthermore, the Fund is not a trust company and, accordingly, is not registered under any trust and loan company legislation, as it does not carry on or intend to carry on the business of a trust company.

Market Price of Units

Publicly traded investment trusts such as the Fund do not necessarily trade at prices determined solely by reference to the underlying value of their investments. Increases in market rates of interest may lead purchasers to demand a higher yield on the Units, which may adversely affect their price. In addition, the market price for the Units may be affected by changes in general market conditions, fluctuations in the markets for equity securities and other factors beyond the Fund's control.

The market value of the Units may deteriorate if the Fund is unable to meet its distribution targets in the future, and that deterioration may be material. In addition, the composition of cash distributions for tax purposes may change over time and may affect the after-tax return for investors.

Leverage and Restrictive Covenants in Agreements Relating to Indebtedness of Morneau Sobeco

The ability of the Trust and its subsidiaries to make distributions or make other payments or advances will be subject to applicable laws and contractual restrictions contained in the instruments governing any indebtedness of those entities. The degree to which MS Group LP or Morneau Sobeco is leveraged could have important consequences to the Unitholders including: Morneau Sobeco's ability to obtain additional financing for working capital, capital expenditures or acquisitions in the future may be limited; a significant portion of Morneau Sobeco's cash flow from operations may be dedicated to the payment of the principal of and interest on its indebtedness, thereby reducing funds available for future operations; certain borrowings will be at variable rates of interest, which exposes Morneau Sobeco to the risk of increased interest rates; and Morneau Sobeco may be more vulnerable to economic downturns and be limited in its ability to withstand competitive pressures. These factors may increase the sensitivity of Standardized Distributable Cash to interest rate variations.

The advance of the new credit facilities at the closing of the Shepell•fgi acquisition has significantly increased the amount of Morneau Sobeco's debt compared to historical levels. The new credit facilities contain numerous restrictive covenants that limit the discretion of Management with respect to certain business matters. These covenants place significant restrictions on, among other things, the ability of Morneau Sobeco to create liens or other encumbrances, to pay distributions or make certain other payments, investments, loans and guarantees and to sell or otherwise dispose of assets and merge or consolidated with another entity. In addition, the new credit facilities contain a number of financial covenants that require Morneau Sobeco to meet certain financial ratios and financial condition tests. A failure to comply with the obligations in Morneau Sobeco's credit facilities could result in a default which, if not cured or waived, could result in a reduction or termination of distributions by Morneau Sobeco and permit acceleration of the relevant indebtedness. If the indebtedness under the new credit facilities were to be accelerated, there can be no assurance that the assets of Morneau Sobeco would be sufficient to repay in full that indebtedness. In addition, the new credit facilities mature on June 1, 2012. There can be no assurance that future borrowings or equity financing will be available to the Fund or Morneau Sobeco, or available on acceptable terms, in an amount sufficient to fund the Fund's or Morneau Sobeco's needs.

Distribution of Securities on Redemption or Termination of the Fund

It is anticipated that the redemption right will not be the primary mechanism for Unitholders to liquidate their investments. Upon redemption of Units or termination of the Fund, the Trustees may distribute the Trust Notes and Trust Units directly to the Unitholders, subject to obtaining all required regulatory approvals. Trust Units and Trust Notes so distributed may not be qualified investments for registered plans (i.e., trusts governed by registered retirement savings plans, registered retirement income funds, deferred profit sharing plans and registered education savings plans, each as defined in the *Income Tax Act* (Canada), depending upon the circumstances at the time. There is currently no market for the Trust Notes and the Trust Units.

Dilution of Existing Unitholders and MS Group LP Unitholders

The Fund's Declaration of Trust authorizes the Fund to issue an unlimited number of Units for that consideration and on those terms and conditions as shall be established by the Trustees without the approval of any Unitholders. The Unitholders will have no pre-emptive rights in connection with such further issues. Additional Units will be issued by the Fund in connection with the indirect exchange of the Class B MS Group LP Units. In addition, MS Group LP is permitted to issue additional MS Group LP Units for any consideration and on any terms and conditions.

Future Sales of Units by the Management Securityholders

The Management Securityholders hold all of the Class B LP Units, representing in aggregate 13.9% of the outstanding MS Group LP Units, which, pursuant to the Exchange Agreement, can be exchanged for Units at any time, subject to certain conditions. Certain of the Management Securityholders have also been granted certain registration rights by the Fund. If the Management Securityholders sell a substantial number of Units in the public market, the market price of the Units could fall. The perception among the public that these sales will occur could also contribute to a decline in the market price of the Units.

Restrictions on Certain Unitholders and Liquidity of Units

The Fund's Declaration of Trust imposes various restrictions on Unitholders. Non-resident Unitholders are prohibited from

beneficially owning either more than 40% of Units and/or the Special Voting Units (on non-diluted and fully diluted bases). These restrictions may limit (or inhibit the exercise of) the rights of certain persons, including non-residents of Canada and U.S. persons, to acquire Units, to exercise their rights as Unitholders and to initiate and complete takeover bids in respect of the Units. As a result, these restrictions may limit the demand for Units from certain Unitholders and thereby adversely affect the liquidity and market value of the Units held by the public.

Statutory Remedies

The Fund is not a legally recognized entity within the relevant definitions of the *Bankruptcy and Insolvency Act*, the *Companies' Creditors Arrangement Act* and in some cases, the *Winding- up and Restructuring Act*. As a result, in the event that a restructuring of the Fund is necessary, the Fund and its stakeholders may not be able to access the remedies and procedures available thereunder.

SUPPLEMENTARY SUMMARY OF QUARTERLY RESULTS

Operating results, distribution summary and condensed balance sheet history are as follows:

Operating Results, Distribution and Condensed Balance Sheets

Selected Unaudited Consolidated Financial Information

	Quarter ended							
	June 30 2008	March 31 2008	December 31 2007	September 30 2007	June 30 2007	March 31 2007	December 31 2006	September 30 2006
	(In thousands of dollars except per unit amounts)							
Revenue	$ 52,363	$ 39,134	$ 36,707	$ 37,231	$ 37,057	$ 36,091	$ 34,079	$ 33,037
Net income	2,456	2,780	4,489	2,907	1,680	3,045	3,010	2,482
EBITDA[(1)]	10,486	8,389	7,391	7,481	8,106	7,865	7,890	7,053
EBITDA margin	20.0%	21.4%	20.1%	20.1%	21.9%	21.8%	23.2%	21.3%
Standardized Distributable Cash[(2)]	10,035	(258)	7,812	8,097	5,835	(927)	7,210	8,725
Adjusted Consolidated Distributable Cash	9,730	7,700	7,025	6,515	7,223	7,439	6,977	6,736
Distributions declared	7,296	6,132	6,131	6,131	6,131	5,865	6,050	5,731
Net income per Unit (basic)[(1)]	$ 0.093	$ 0.125	$ 0.203	$ 0.132	$ 0.076	$ 0.138	$ 0.136	$ 0.112
Net income per Unit (diluted)[(1)]	$ 0.091	$ 0.125	$ 0.203	$ 0.132	$ 0.076	$ 0.138	$ 0.136	$ 0.112
EBITDA per Unit (basis)	$ 0.329	$ 0.302	$ 0.266	$ 0.269	$ 0.292	$ 0.283	$ 0.284	$ 0.254
Standardized Distributable Cash per Unit (basic)	$ 0.310	$ (0.012)	$ 0.352	$ 0.366	$ 0.264	$ (0.042)	$ 0.327	$ 0.396
Adjusted Consolidated Distributable Cash per Unit (basic)	$ 0.305	$ 0.277	$ 0.253	$ 0.234	$ 0.260	$ 0.268	$ 0.251	$ 0.243
Distributions declared per Unit (basic)	$ 0.226	$ 0.221	$ 0.221	$ 0.221	$ 0.221	$ 0.211	$ 0.218	$ 0.206
Standardized Distributable Cash Payout Ratio-basic[(3)]	73.9%	NM	62.6%	60.2%	83.4%	NM	66.6%	52.1%
Adjusted Consolidated Distributable Cash Payout Ratio	75.0%	79.6%	87.3%	94.1%	84.9%	78.8%	86.7%	84.9%
Twelve-month rolling Standardized Distributable Cash Payout Ratio	87.0%	90.8%	92.7%	95.0%	90.6%	83.5%	77.9%	85.2%
Twelve-month rolling Adjusted Consolidated Distributable Cash Payout Ratio	82.9%	86.2%	86.0%	85.9%	84.3%	83.3%	85.3%	85.3%
Total assets	$688,804	$328,665	$334,428	$337,391	$342,569	$338,530	$345,872	$345,398
Total long-term debt	$135,162	$ 34,926	$ 34,913	$ 34,901	$ 34,888	$ 34,876	$ 35,000	$ 35,000

(1) In the second quarter of 2007 we recorded a non-cash charge to earnings of $2.7 million. The charge relates to our future tax liabilities recorded as a result of Bill C-52 which received Royal Assent on June 22, 2007. This non-cash charge relates to temporary differences between the accounting and tax bases of our assets and liabilities primarily related to intangible assets. The charge has no current impact on our cash flow, EBITDA, Standardized Distributable Cash and Adjusted Consolidated Distributable Cash.

(2) The Standardized Distributable Cash for the three months ended March 31, 2008 and 2007 are significantly lower than the distributions declared, as the Fund pays its employees their annual bonuses in the first quarter of each year.

(3) This ratio is not presented for the quarter ended March 31, 2008 since it is not a meaningful % when the Standard Distributable Cash per unit is a negative figure.

Disclosure Controls and Procedures

The Fund's disclosure controls and procedures have been designed to provide reasonable assurance that all relevant information is identified to its Disclosure Committee to ensure appropriate and timely decisions are made regarding public disclosure.

The Chief Executive Officer and the Chief Financial Officer have concluded that the disclosure controls and procedures are operating effectively based on the evaluation of these controls and procedures conducted at June 30, 2008.

Internal Control over Financial Reporting

Management is responsible for designing internal controls over financial reporting, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP.

No changes were made in the Fund's internal controls over financial reporting during the six months ended June 30, 2008, that have materially affected, or are reasonably likely to materially affect, the Fund's internal controls over financial reporting, with the exception of internal controls related to the Shepell•fgi business.

The Fund acquired the Shepell•fgi business on June 2, 2008. The Fund is continuing the documentation and integration of internal controls over financial reporting for that business and will finalize the review during 2009.

Additional Information

The Fund's Units trade on the Toronto Stock Exchange under the symbol MSI.UN. Additional information relating to the Fund, including all public filings, is available on the SEDAR Web site (*www.sedar.com*) and on our own Web site at *www.morneausobeco.com*.

The content of this MD&A reflects information known as of August 13, 2008.

MORNEAU SOBECO

Human Resource Consulting and Administrative Solutions

Morneau Sobeco Income Fund is the largest Canadian-owned firm providing human resource consulting and outsourcing services. Through Morneau Sobeco and Shepell•fgi, the firm delivers solutions to assist employers in managing the financial security, health and productivity of their employees. With over 2,300 employees in offices across North America, Morneau Sobeco Income Fund offers its services to organizations that are situated in Canada, in the United States and around the globe.

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