



**Interim Management Report of Fund Performance  
As at April 30, 2008  
Front Street Diversified Income Fund Class**

*This Interim Management Report of Fund Performance contains financial highlights but does not contain the complete interim financial statements for Front Street Diversified Income Fund, a class of shares of Front Street Mutual Funds Limited fund (the "Fund"). The interim financials of the Fund are attached behind this report and you can also get a copy of the interim or annual financial statements at your request, and at no cost, by calling 1-800-513-2832, by writing to us at Front Street Capital 2004, 33 Yonge Street, Suite 600, Toronto, Ontario M5E 1G4 or by visiting our web site at [www.frontstreetcapital.com](http://www.frontstreetcapital.com) or SEDAR at [www.sedar.com](http://www.sedar.com).*

*Security holders may also contact us using one of these methods to request a copy of the Fund's proxy voting policies and procedures, proxy voting disclosure record, or quarterly portfolio disclosure relating to the Fund.*

**Forward Looking Information**

This Interim Management Report of Fund Performance contains forward-looking information and statements relating, but not limited to, anticipated or prospective financial performance and results of operations of the Fund. Forward looking information involves known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by the forward-looking information. For this purpose, any statements that are contained herein that are not statements of historical fact may be deemed to be forward-looking information. Without limiting the foregoing, the words "believes", "anticipates", "plans", "intends", "will", "should", "expects", "projects", and similar expressions are intended to identify forward-looking information.

Although the Fund believes it has a reasonable basis for making the forecasts or projections included in this Interim Management Report of Fund Performance, readers are cautioned not to place undue reliance on such forward-looking information. By its nature, the forward-looking information involves numerous assumptions, inherent risks and uncertainties, both general and specific, that contribute to the possibility that the predictions, forecasts and other forward-looking statements will not occur. These factors include, but are not limited to, those associated with the performance of the equity securities market, expectations about interest rates and factors incorporated by reference herein as risk factors.

The above list of important factors affecting forward looking information is not exhaustive, and reference should be made to the other risks discussed in the Fund's filings with Canadian securities regulatory authorities. The forward looking information is given as of the date of this Interim Management Report of Fund Performance, and the Fund undertakes no obligation to update publicly or revise any forward-looking information, whether as a result of new information, future events or otherwise.



## **Management Discussion of Fund Performance**

### **INVESTMENT OBJECTIVES AND STRATEGIES**

The Fund will seek to provide shareholders with the opportunity to receive monthly distributions targeted to yield of 5.5% per year on the original issue price of the Units and generate capital appreciation on the portfolio with a reduced measure of risk.

The Fund's portfolio consists primarily of securities of income trusts, although the Fund also invests in preferred shares, corporate and government debt securities and common shares.

The Fund's ability to manage risk and volatility through the strategic use of long and short positions is a key element in achieving its investment objective.

The Fund will retain a net long bias to assist its investment strategy.

The Fund's portfolio will consist of securities of Income Trusts, preferred shares and corporate and government debt, although the Fund may also invest in common shares. In managing the portfolio, the Investment Advisor, Front Street Investment Management Inc., intends to use strategies including: investing in undervalued securities, short selling overvalued securities, managing long/short positions, pairs trading, merger arbitrage, convertible arbitrage and participation in restructurings.

From time to time the Fund may invest in other mutual funds and may purchase securities of, or enter into specified derivative transactions for which the underlying interest is based on the securities of other mutual funds. Such investments may be entered into in conjunction with other strategies and investments in a manner considered most appropriate to achieving the Fund's investment objectives stated above and enhancing returns as permitted by securities regulations.

### **RISK**

The Most of the Fund's assets will be invested in income producing securities, some of which will have equity characteristics. The Fund will therefore be subject to stock market risk. The Fund may also invest in foreign securities that may expose the Fund, to a limited extent, to the risk of investments in foreign securities and foreign currency risk. The Fund may invest in relatively illiquid securities that may expose the Fund to liquidity risk. The Fund may also be exposed to sector risk due to its investments being concentrated in a limited number of sectors. The Fund may also be exposed to the risks of selling securities short, the risks of investing in derivatives, and the risk associated with investing in securities of junior industrial, technology and natural resource companies.

Currency risk proved to have an effect on the Fund's returns, as the Canadian dollar strengthened, relative to the U.S. dollar, over the year. Currency risk impacted principally the Fund's investments that had revenue in U.S. dollars. Volatility in currency markets continues to be high, suggesting uncertainty going forward on this front.

Equity risk also affected Fund volatility. Specifically, the threat of oil-supply disruptions kept the price of oil high. While market volatility was high overall, the high price of oil and gas was a positive factor that contributed to Canadian equity market performance, particularly in the energy sector.

Interest-rate risk was also a factor, as global central banks and bond and equity markets closely monitored the U.S. Federal Reserve's monetary policy activities and public communications for indications as to interest rate policy. As higher borrowing costs tend to slow the economy, rising interest rates tend to have a negative impact on the outlook for corporate-profit growth and therefore equity market performance.

Credit risk was another factor this year. Specifically, a weakening housing market in the United States finally became a crisis in August of 2007 as assets backed by sub prime mortgages collapsed, impacting global debt and equity markets. As the autumn progressed, the vicious circle caused by deteriorating credit impacted commercial banks -- holders of bonds and other securities backed by home loans. As a result, lending has been curtailed and the



## FRONT STREET Diversified Income Fund

cost of money is higher. Although the Fund did not hold the debt in question, equity markets have been weak due to the general uncertainty and the fact that global growth could decelerate into 2008 as liquidity dries up.

Political risk continued to be in evidence this past six months following the Alberta government's announced changes in tax policy in the oil and gas sector in October 2007. This has and will continue to increase volatility and risk.

The Fund has multiple risks associated with equity markets. Investors whose primary concern is preservation of capital should not be invested in this Fund. The Fund is suitable for investors seeking monthly income and long-term growth with a tolerance for risk and volatility and a long-term investment horizon.

The risks of investing in the Fund are further discussed in the Fund's Annual Information Form.

### RESULTS OF OPERATIONS

The Fund met its distribution objectives of 5.5% per annum and was able to maintain its net asset value per unit through the year.

Positive contributions from the portfolio came from REITS, oil and gas royalty trusts and business trusts. Marginal contributions came from the interest sensitive sector.

The outlook for the remainder of 2008 is for tax policy clarification and interest rate decreases. Business trusts should perform in line with the economy.

### RECENT DEVELOPMENTS

The Fund anticipates that volatility will continue in the equity markets for the foreseeable future. The perception exists that inventory levels are tight in most commodity groups leading to an inability to cushion any shocks to the system. Despite this, and even with a changing interest rate and credit environment, economic growth has continued unabated.

### RELATED PARTY-TRANSACTIONS

The Fund may place a portion of its portfolio transactions with brokerage firms which are affiliates of Front Street Mutual Funds Limited, the manager of the Fund, and the Investment Advisor, provided it determines that these affiliates' trade execution abilities and costs are comparable to those non-affiliated, qualified brokerage firms, on an execution-only basis. For the six months ended April 30, 2008, Tuscarora Capital Inc. received \$3,151 in commission on portfolio transactions for the Fund.

### FINANCIAL HIGHLIGHTS

The following tables show selected key financial information about the Fund and are intended to help you understand the Fund's financial performance since inception. This information is derived from the Fund's audited annual financial statements and unaudited interim financial statements for the six months ended April 30, 2008.



# FRONT STREET

## Diversified Income Fund

### FRONT STREET DIVERSIFIED INCOME FUND CLASS SERIES A

FOR THE PERIODS ENDED	April 30, 2008 \$	October 31, 2007 \$	October 31, 2006 \$	October 31, 2005 \$	October 31, 2004 \$
<b>The Fund's Net Asset Value (NAV) per Share</b>					
Net asset value, beginning of period <sup>(3)</sup>	9.47	9.92	10.00	-	-
<b>Increase (decrease) from operations:</b>					
Total revenue	0.23	0.44	0.15	-	-
Total expenses	(0.13)	(0.39)	(0.32)	-	-
Realized gains (losses)	(0.18)	0.38	0.04	-	-
Unrealized gains (losses)	(0.17)	(0.26)	0.69	-	-
<b>Total increase (decrease) from operations <sup>(1)</sup></b>	<b>(0.25)</b>	<b>0.17</b>	<b>0.56</b>	<b>-</b>	<b>-</b>
<b>Distributions:</b>					
From income (excluding dividends)	-	-	-	-	-
From dividends	-	-	-	-	-
From capital gains	-	-	-	-	-
Return of capital	(0.28)	(0.55)	(0.15)	-	-
<b>Total distributions <sup>(2)</sup></b>	<b>(0.28)</b>	<b>(0.55)</b>	<b>(0.15)</b>	<b>-</b>	<b>-</b>
<b>Net asset value, end of period <sup>(3)</sup></b>	<b>8.95</b>	<b>9.47</b>	<b>9.94</b>	<b>-</b>	<b>-</b>
<b>Ratios and Supplemental Data Series A</b>					
Net assets (000's) <sup>(4)</sup>	13,006	13,839	5,777	-	-
Number of shares outstanding <sup>(4)</sup>	1,453,941	1,461,992	581,171	-	-
Management expense ratio <sup>(5)</sup>	2.94%	3.98%	9.23%	-	-
Management expense ratio before waivers or absorptions	2.94%	3.98%	9.23%	-	-
Trading expense ratio <sup>(6)</sup>	0.27%	0.45%	0.61%	-	-
Portfolio turnover rate <sup>(7)</sup>	146.00%	347.72%	38.23%	-	-
Net asset value per share <sup>(8)</sup>	8.95	9.47	9.94	-	-
Closing market price or transaccional NAV <sup>(8)</sup>	8.97	9.49	9.94	-	-



# FRONT STREET

## Diversified Income Fund

### FRONT STREET DIVERSIFIED INCOME FUND CLASS SERIES B

FOR THE PERIODS ENDED	April 30, 2008 \$	October 31, 2007 \$	October 31, 2006 \$	October 31, 2005 \$	October 31, 2004 \$
<b>The Fund's Net Asset Value (NAV) per Share</b>					
Net asset value, beginning of period <sup>(3)</sup>	9.47	9.91	10.00	-	-
<b>Increase (decrease) from operations:</b>					
Total revenue	0.23	0.43	0.17	-	-
Total expenses	(0.13)	(0.39)	(0.38)	-	-
Realized gains (losses)	(0.18)	0.39	0.04	-	-
Unrealized gains (losses)	(0.19)	(0.30)	0.85	-	-
<b>Total increase (decrease) from operations <sup>(1)</sup></b>	<b>(0.27)</b>	<b>0.13</b>	<b>0.68</b>	<b>-</b>	<b>-</b>
<b>Distributions:</b>					
From income (excluding dividends)	-	-	-	-	-
From dividends	-	-	-	-	-
From capital gains	-	-	-	-	-
Return of capital	(0.28)	(0.55)	(0.15)	-	-
<b>Total distributions <sup>(2)</sup></b>	<b>(0.28)</b>	<b>(0.55)</b>	<b>(0.15)</b>	<b>-</b>	<b>-</b>
<b>Net asset value, end of period <sup>(3)</sup></b>	<b>8.95</b>	<b>9.47</b>	<b>9.93</b>	<b>-</b>	<b>-</b>
<b>Ratios and Supplemental Data Series B</b>					
Net assets (000's) <sup>(4)</sup>	6,554	7,927	10,512	-	-
Number of shares outstanding <sup>(4)</sup>	732,512	837,203	1,058,552	-	-
Management expense ratio <sup>(5)</sup>	2.92%	3.99%	10.54%	-	-
Management expense ratio before waivers or absorptions	2.92%	3.99%	10.54%	-	-
Trading expense ratio <sup>(6)</sup>	0.27%	0.45%	0.61%	-	-
Portfolio turnover rate <sup>(7)</sup>	146.00%	347.72%	38.23%	-	-
Net asset value per share <sup>(8)</sup>	8.95	9.47	9.93	-	-
Closing market price or transaccional NAV <sup>(8)</sup>	8.97	9.50	9.93	-	-



# FRONT STREET

## Diversified Income Fund

### FRONT STREET DIVERSIFIED INCOME FUND CLASS SERIES F

FOR THE PERIODS ENDED	April 30, 2008 \$	October 31, 2007 \$	October 31, 2006 \$	October 31, 2005 \$	October 31, 2004 \$
<b>The Fund's Net Asset Value (NAV) per Share</b>					
Net asset value, beginning of period <sup>(3)</sup>	9.48	9.96	10.00	-	-
<b>Increase (decrease) from operations:</b>					
Total revenue	0.23	0.41	0.08	-	-
Total expenses	(0.13)	(0.37)	(0.17)	-	-
Realized gains (losses)	(0.18)	0.35	0.04	-	-
Unrealized gains (losses)	(0.16)	(0.78)	0.18	-	-
<b>Total increase (decrease) from operations <sup>(1)</sup></b>	<b>(0.24)</b>	<b>(0.39)</b>	<b>0.13</b>	<b>-</b>	<b>-</b>
<b>Distributions:</b>					
From income (excluding dividends)	-	-	-	-	-
From dividends	-	-	-	-	-
From capital gains	-	-	-	-	-
Return of capital	(0.28)	(0.55)	(0.15)	-	-
<b>Total distributions <sup>(2)</sup></b>	<b>(0.28)</b>	<b>(0.55)</b>	<b>(0.15)</b>	<b>-</b>	<b>-</b>
<b>Net asset value, end of period <sup>(3)</sup></b>	<b>8.96</b>	<b>9.48</b>	<b>9.98</b>	<b>-</b>	<b>-</b>
<b>Ratios and Supplemental Data Series F</b>					
Net assets (000's) <sup>(4)</sup>	464	451	260	-	-
Number of shares outstanding <sup>(4)</sup>	51,825	47,596	26,080	-	-
Management expense ratio <sup>(5)</sup>	2.94%	4.02%	7.72%	-	-
Management expense ratio before waivers or absorptions	2.94%	4.02%	7.72%	-	-
Trading expense ratio <sup>(6)</sup>	0.27%	0.45%	0.61%	-	-
Portfolio turnover rate <sup>(7)</sup>	146.00%	347.72%	38.23%	-	-
Net asset value per share <sup>(8)</sup>	8.96	9.48	9.98	-	-
Closing market price or transactional NAV <sup>(8)</sup>	8.98	9.50	9.98	-	-

(1) Net asset value and distributions are based on the actual number of shares outstanding at the relevant time. The increase/decrease from operations is based on the weighted average number of shares outstanding over the financial year.

(2) Distributions were paid in cash and/or reinvested in additional shares of the Fund.

(3) The relief granted by the Canadian securities regulatory authorities from complying with Section 3855 results in a difference between GAAP NAV and Transactional NAV due to the use of different valuation techniques for certain investments. We have adopted the provisions of Section 3855 retroactively without restatement of prior periods. Accordingly, the beginning of year net asset value for the current period is adjusted.

(4) This information is provided as at period end of the year shown.

(5) Management expense ratio is based on total expenses for the stated year and is expressed as an annualized percentage of daily average net assets during the year. In the year, a series is established, the management expense ratio is annualized from the date of inception to October 31.

(6) The trading expense ratio represents total commissions and other portfolio transaction costs expressed as an annualized percentage of daily average net assets during the year.

(7) The Fund's portfolio turnover rate indicates how actively the Fund's portfolio adviser manages its portfolio investments. A portfolio turnover rate of 100% is equivalent to the Fund buying and selling all of the securities in its portfolio once in the course of the year. The higher a Fund's portfolio turnover rate in a year, the greater the trading costs payable by the Fund in the year, and the greater the chance of an investor receiving taxable capital gains in the year. There is not necessarily a relationship between a high turnover rate and the performance of a Fund.

(8) The relief granted by the Canadian securities regulatory authorities from complying with Section 3855 results in a difference between GAAP NAV and Transactional NAV due to the use of different valuation techniques for certain investments. We have adopted the provisions of Section 3855 retroactively without restatement of prior periods. Accordingly, the beginning of year net asset value for the current period is adjusted.



## MANAGEMENT AND PERFORMANCE FEES

The Fund pays Investment Advisor a monthly fee equal to one-twelfth of 2% of net asset value of the applicable series of the Fund, payable monthly in arrears, calculated without regard to any accrual of performance bonuses (as described below) and before payment of such fee.

The Investment Advisor may earn an annual performance bonus (a “Performance Bonus”) in each fiscal quarter if the percentage gain in the new asset value of a series of the Fund (as adjusted for any prior return deficiencies) over the preceding calendar quarter or quarters since a performance fee was last payable exceeds the percentage gain or loss of the benchmark (the ‘Benchmark’) over the same period. The Benchmark for the Fund is calculated as follows:

- 50% of the percentage gain or loss in the S&P/TSX Income Trust Index
- + 50% of the percentage gain or loss in the ScotiaMcleod Bond Index.

The fee will be equal to this excess return per security multiplied by the number of securities outstanding at the end of the quarter multiplied by 20%, provided that the net asset value per security of the Fund (including distributions) is greater than all previous values at the end of each previous calendar quarter. The starting reference point for the next calendar quarter’s calculation will be based on the higher of either the Benchmark performance adjusted net asset value per security or the adjusted actual net asset value per security, both with respect to the previous quarter in which a performance fee was payable.

## DEALER COMPENSATION

Brokers, dealers and advisors may be paid a share of the management fee – called a “trailer commission”, for assets that their sales representatives place in the Series A and Series B Fund securities. The Fund may, at its discretion, negotiate, change the terms and conditions of, or discontinue the trailer commission with brokers, dealers and advisors.

The trailer commission is calculated as a percentage of assets each broker, dealer or advisor has placed in the Fund series. The trailer commission is calculated based on the closing balance of client accounts for each calendar month. The trailer commission will not be paid if the assets are removed from the Funds. Trailer commissions are paid quarterly at rates set within ranges according to the following table.

<b>Series</b>	<b>Trailer Annual Rate</b>	<b>Annual Payment per \$1,000 of Fund securities held</b>
A	0.75%	\$10.00
B	1.00%	\$10.00
F	0.00%	Nil

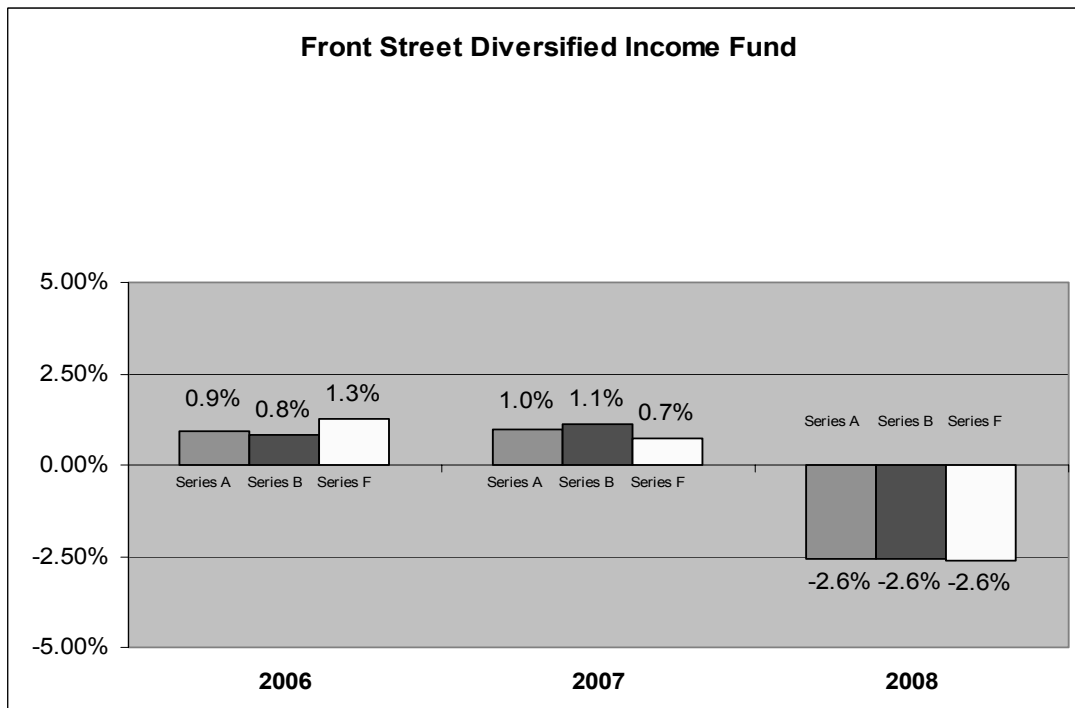


**PAST PERFORMANCE**

The past performance of the Fund is set out below and includes year-to-date returns.

With respect to the charts displayed below, please note the following:

- (a) the returns or performance information shown assumes that all distributions made by the Fund in the periods shown were reinvested in additional shares of the Fund;
- (b) the return or performance information does not take into account sales, redemption, distribution or other optional charges or income taxes payable that would have reduced returns or performance; and
- (c) how the Fund has performed in the past does not necessarily indicate how it will perform in the future.







**ANNUAL COMPOUND RETURNS**

The following table shows the Fund's historical annual compound total return since inception as compared to the performance of the S&P/TSX Income Trust Index.

	<b>Since Inception June 22, 2006</b>
Front Street Diversified Income Fund Series A	-0.59%
Front Street Diversified Income Fund Series B	-0.57%
S&P/TSX Capped Income Trust Index	-4.29%
	<b>Since Inception August 11, 2006</b>
Front Street Diversified Income Fund Series F	-0.49%
S&P/TSX Capped Income Trust Index	-11.61%

The S&P/TSX Capped Income Trust Index is a modified-market cap weighted index and represents a broad-based composite Index which may encompass any or all GICS sectors of the income trust market place.



## Summary of Investment Portfolio as at April 30, 2008

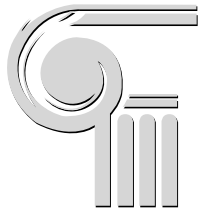
	% of Total
<b>Cash and Cash Equivalents</b>	<b>19.9%</b>
<b>Total Income Funds</b>	
<b>LONG POSITIONS</b>	
Corporate Bonds	21.7%
Financials	16.1%
Energy	10.1%
Materials	9.2%
Government Bonds	8.6%
Industrials	4.0%
Consumer Staples	3.2%
Consumer Discretionary	2.1%
Information Technology	1.8%
Health Care	1.1%
Telecommunication Services	0.9%
Currency Forwards	0.2%
<b>SHORT POSITIONS</b>	
Industrials	0.0%
Energy	-0.1%
Financials	-1.0%
<b>Total Investments Portfolio</b>	<b>77.9%</b>
<b>Total Investments Portfolio Including Cash and Short-Term</b>	<b>97.8%</b>
<b>Other Assets</b>	<b>2.2%</b>
<b>Total Net assets</b>	<b>100.0%</b>

### Top 25 Investments

#### LONG POSITIONS

Province of Quebec Real Return 3.30% December 1, 2013	5.3%
Graoch Associates #161 Limited Partnership 12.25% September 15, 2008	5.0%
TimberWest Forest Corporation	2.9%
Discover Financial Services Floating Rate June 11, 2010	2.9%
Brookfield Asset Management Series 18 4.75% Preferred	2.7%
ARC Energy Trust	2.4%
Holloway Lodging Real Estate Investment Trust 8.00% August 1, 2011	2.3%
Province of Manitoba 5.25% March 2, 2009	2.2%
RioCan Real Estate Investment Trust	2.1%
Pembina Pipeline Income Fund	2.1%
Vermilion Energy Trust	2.1%
Baytex Energy Trust	2.1%
Centurion Apartment Properties Limited Partnership	2.1%
Boardwalk Real Estate Investment Trust	2.0%
Manulife Financial Corporation	2.0%
Post Properties Inc.	1.9%
Teranet Income Fund	1.8%
Royal Host Real Estate Investment Trust 6.00% Debentures October 31, 2015	1.8%
AG Growth Income Fund	1.6%
Mullen Group Income Fund	1.5%
Fording Canadian Coal Trust	1.5%
Aecon Group Inc.	1.5%
Westshore Terminals Income Fund	1.4%
Harvest Energy Trust 7.25% September 30, 2013	1.2%
Annaly Capital Management Inc.	1.1%

The information contained in the foregoing list may change due to the ongoing portfolio transactions of the Fund. A quarterly update may be obtained by contacting the Investment Advisor.



**FRONT STREET**  
Diversified Income Fund

**INTERIM FINANCIAL STATEMENTS**

**FRONT STREET DIVERSIFIED INCOME FUND CLASS**

FOR THE SIX MONTHS ENDED APRIL 30, 2008

**Front Street Diversified Income Fund Class**  
**Statement of Net Assets**  
**As at April 30, 2008 (unaudited) and October 31, 2007**

	<b>2008</b>	<b>2007</b>
<b>Assets</b>		
Investments, at fair value (cost - \$16,373,032; 2007 - \$14,240,544)	\$ 15,797,579	\$ 13,824,005
Currency forward contracts, at fair value	30,553	-
Cash and cash equivalents	3,989,010	7,744,479
Accounts receivable relating to shares issued	-	99,159
Accounts receivable relating to portfolio assets sold	857,139	2,724,294
Amounts receivable relating to accrued income	131,848	129,033
	<u>20,806,129</u>	<u>24,520,970</u>
<b>Liabilities</b>		
Obligations from portfolio assets sold short, at fair value	\$ 241,000	\$ 706,800
Accrued expenses, note 7	141,332	111,170
Income tax payable	34,848	34,848
Liabilities for portfolio assets purchased	336,204	1,450,255
Accounts payable relating to shares redeemed	27,989	1,000
	<u>781,373</u>	<u>2,304,073</u>
<b>Net assets representing shareholders' equity</b>	<b>\$ 20,024,756</b>	<b>\$ 22,216,897</b>

**Net assets applicable to outstanding shares allocated as follows:**

Net assets, Series A	\$ 13,006,209	\$ 13,838,855
Shares outstanding, Series A, note 3	1,453,941	1,461,992
Net assets per share, Series A	<u>8.95</u>	<u>9.47</u>
Net assets, Series B	\$ 6,554,409	\$ 7,926,968
Shares outstanding, Series B, note 3	732,512	837,203
Net assets per share, Series B	<u>8.95</u>	<u>9.47</u>
Net assets, Series F	\$ 464,138	\$ 451,074
Shares outstanding, Series F, note 3	51,825	47,596
Net assets per share, Series F	<u>8.96</u>	<u>9.48</u>

**On behalf of the Board of Front Street Mutual Funds Limited:**



Gary P. Selke  
Chief Executive Officer and Director



Murray Plasket  
Chief Financial Officer

See accompanying notes to the financial statements

**Front Street Diversified Income Fund Class**  
**Statement of Operations (unaudited)**  
**For the Periods Ended April 30**

	<b>2008</b>	<b>2007</b>
<b>Investment income</b>		
Interest	\$ 472,970	\$ 383,346
Dividend	53,015	50,680
Less: foreign withholding taxes	(1,484)	(201)
	<u>524,501</u>	<u>433,825</u>
<b>Expenses</b>		
Management fees, notes 4 and 7	216,572	206,316
Performance fees, notes 4 and 7	-	101,721
Audit fees	13,426	13,142
Custodial fees	7,559	30,213
Legal fees	23,079	40,168
Securityholder reporting costs	9,597	20,907
Administration fees	31,555	20,834
Other expenses	1,283	2,921
	<u>303,071</u>	<u>436,222</u>
Net investment income (loss) for the period	221,430	(2,397)
<b>Net realized and unrealized gain on investments</b>		
Net realized gain on sale of investments	(400,248)	124,272
Transaction costs, notes 2 and 6	(56,031)	(41,847)
Change in unrealized appreciation of value of investments	(347,107)	304,785
Net gain (loss) on investments for the period	<u>(803,386)</u>	<u>387,210</u>
<b>Increase (decrease) in net assets from operations for the period</b>	<b>\$ (581,956)</b>	<b>\$ 384,813</b>
<b>Net assets from operations applicable to outstanding shares allocated as follows:</b>		
Increase (decrease) in net assets from operations, Series A	\$ (357,789)	\$ 231,403
Increase (decrease) in net assets from operations per share, Series A	<u>\$ (0.25)</u>	<u>\$ 0.26</u>
Increase (decrease) in net assets from operations, Series B	\$ (212,399)	\$ 161,962
Increase (decrease) in net assets from operations per share, Series B	<u>\$ (0.27)</u>	<u>\$ 0.14</u>
Decrease in net assets from operations, Series F	\$ (11,768)	\$ (8,552)
Decrease in net assets from operations per share, Series F	<u>\$ (0.24)</u>	<u>\$ (0.36)</u>

See accompanying notes to the financial statements

**Front Street Diversified Income Fund Class**  
**Statement of Changes in Net Assets (unaudited)**  
**For the Periods Ended April 30**

<b>Series A</b>	<b>2008</b>	<b>2007</b>
Net assets, beginning of period	\$ 13,838,855	\$ 5,776,755
Initial adoption of new accounting policy (note 2)	-	(10,544)
<b>Adjusted net assets, beginning of period</b>	<b>13,838,855</b>	<b>5,766,211</b>
<b>Increase (decrease) in net assets from operations</b>	<b>(357,789)</b>	<b>231,403</b>
<b>Distributions to shareholders</b>		
Return of Capital	(393,732)	(270,544)
<b>Shareholder transactions</b>		
Proceeds from the issuance of shares	198,585	4,786,611
Aggregate amounts paid on redemption of shares	(304,646)	(62,053)
Net transfer to shares of other funds	(260,153)	(139,505)
Shares issued on reinvestment of distributions	285,089	172,349
	(81,125)	4,757,402
<b>Net increase (decrease) in net assets for the period</b>	<b>(832,646)</b>	<b>4,718,261</b>
<b>Net assets, end of period</b>	<b>\$ 13,006,209</b>	<b>\$ 10,484,472</b>
 <b>Series B</b>		
Net assets, beginning of period	\$ 7,926,968	\$ 10,511,832
Initial adoption of new accounting policy (note 2)	-	(19,178)
<b>Adjusted net assets, beginning of period</b>	<b>7,926,968</b>	<b>10,492,654</b>
<b>Increase (decrease) in net assets from operations</b>	<b>(212,399)</b>	<b>161,962</b>
<b>Distributions to shareholders</b>		
Return of Capital	(204,051)	(312,192)
<b>Shareholder transactions</b>		
Proceeds from the issuance of shares	177,656	2,135,804
Aggregate amounts paid on redemption of shares	(1,292,922)	(2,271,287)
Net transfer from (to) shares of other funds	(11,224)	169,992
Shares issued on reinvestment of distributions	170,381	250,341
	(956,109)	284,850
<b>Net increase (decrease) in net assets for the period</b>	<b>(1,372,559)</b>	<b>134,620</b>
<b>Net assets, end of period</b>	<b>\$ 6,554,409</b>	<b>\$ 10,627,274</b>

**Front Street Diversified Income Fund Class**  
**Statement of Changes in Net Assets (unaudited)**  
**For the Periods Ended April 30**

**Series F**

Net assets, beginning of period	\$	451,074	\$	260,148
Initial adoption of new accounting policy (note 2)		-		(477)
<b>Adjusted net assets, beginning of period</b>		<b>451,074</b>		<b>259,671</b>
<b>Decrease in net assets from operations</b>		<b>(11,768)</b>		<b>(8,552)</b>
<b>Distributions to shareholders</b>				
Return of Capital		(13,920)		(4,611)
<b>Shareholder transactions</b>				
Proceeds from the issuance of shares		38,000		243,500
Aggregate amounts paid on redemption of shares		(13,168)		-
Net transfer to shares of other funds		-		(239,126)
Shares issued on reinvestment of distributions		13,920		4,338
		<b>38,752</b>		<b>8,712</b>
<b>Net increase (decrease) in net assets for the period</b>		<b>13,064</b>		<b>(4,451)</b>
<b>Net assets, end of period</b>	<b>\$</b>	<b>464,138</b>	<b>\$</b>	<b>255,220</b>

**Total**

Net assets, beginning of period	\$	22,216,897	\$	16,548,735
Initial adoption of new accounting policy (note 2)		-		(30,199)
<b>Adjusted net assets, beginning of period</b>		<b>22,216,897</b>		<b>16,518,536</b>
<b>Increase (decrease) in net assets from operations</b>		<b>(581,956)</b>		<b>384,813</b>
<b>Distributions to shareholders</b>				
Return of Capital		(611,703)		(587,347)
<b>Shareholder transactions</b>				
Proceeds from the issuance of shares		414,241		7,165,915
Aggregate amounts paid on redemption of shares		(1,610,736)		(2,333,340)
Net transfer to shares of other funds		(271,377)		(208,639)
Shares issued on reinvestment of distributions		469,390		427,028
		<b>(998,482)</b>		<b>5,050,964</b>
<b>Net increase (decrease) in net assets for the period</b>		<b>(2,192,141)</b>		<b>4,848,430</b>
<b>Net assets, end of period</b>	<b>\$</b>	<b>20,024,756</b>	<b>\$</b>	<b>21,366,966</b>

See accompanying notes to the financial statements

**FRONT STREET DIVERSIFIED INCOME FUND CLASS**  
**STATEMENT OF INVESTMENT PORTFOLIO (unaudited)**  
As at April 30, 2008

	Number of Shares / Units or Par Value	Cost \$	Fair Value \$
<b>Financials (15.1%)</b>			
<b>Long Positions (16.1%)</b>			
Allied Properties Real Estate Investment Trust	10,460	199,784	212,861
* Annaly Capital Management Inc.	13,600	223,699	230,078
Bank of Montreal	4,250	200,338	212,925
Boardwalk Real Estate Investment Trust	9,930	388,271	394,221
Brookfield Asset Management Series 18 4.75% Preferred	30,000	561,000	537,900
Canadian Apartment Properties Real Estate Investment Trust	12,860	235,004	215,919
* Carlyle Capital Corporation Limited	18,000	342,141	3,270
Huntingdon Real Estate Investment Trust	75,000	158,770	151,500
InnVest Real Estate Investment	11,940	147,748	114,863
InterRent Real Estate Investment Trust	49,250	225,929	140,855
* Lafayette Square CDO Limited Preferred	300	191,013	190,776
Manulife Financial Corporation	9,930	388,673	390,845
RioCan Real Estate Investment Trust	20,400	415,740	427,380
		<u>3,678,110</u>	<u>3,223,393</u>
<b>Short Positions (-1.0%)</b>			
National Bank of Canada	(3,880)	(207,939)	(208,705)
		<u>3,470,171</u>	<u>3,014,688</u>
<b>Energy (10.0%)</b>			
<b>Long Positions (10.1%)</b>			
ARC Energy Trust	18,780	477,962	489,031
Baytex Energy Trust	16,560	331,199	417,643
Big Eagle Energy Services Trust	16,000	48,000	38,400
Daylight Resources Trust	8,150	74,207	79,707
Duvernay Oil Corporation	600	22,214	28,842
Pembina Pipeline Income Fund	25,082	425,293	426,394
Spectra Energy Income Fund	12,530	139,166	140,837
Vermilion Energy Trust	10,630	383,894	420,417
		<u>1,901,935</u>	<u>2,041,271</u>
<b>Short Positions (-0.1%)</b>			
Fairborne Energy Limited	(1,500)	(10,814)	(13,755)
Paramount Energy Trust	(1,620)	(13,542)	(15,439)
		<u>(24,356)</u>	<u>(29,194)</u>
		<u>1,877,579</u>	<u>2,012,077</u>
<b>Materials (9.2%)</b>			
Aecon Group Inc.	18,390	316,913	290,746
Agrium Inc.	2,362	141,448	187,023
Fording Canadian Coal Trust	4,900	300,690	304,094
Potash Corporation of Saskatchewan Inc.	1,027	130,304	190,396
TimberWest Forest Corporation	43,801	644,857	580,801
Westshore Terminals Income Fund	17,093	238,011	282,889
		<u>1,772,223</u>	<u>1,835,949</u>
<b>Industrials (4.0%)</b>			
<b>Long Positions (4.0%)</b>			
AG Growth Income Fund	9,550	269,207	313,049
Mullen Group Income Fund	15,640	309,971	307,639
SuiteWorks Inc. 'A'	5,143	180,005	180,005
		<u>759,183</u>	<u>800,693</u>
<b>Short Positions (0.0%)</b>			
Eveready Income Fund	(838)	(3,273)	(3,101)
		<u>755,910</u>	<u>797,592</u>
<b>Consumer Staples (3.2%)</b>			
* Post Properties Inc.	10,134	419,949	372,140
Urbanfund Corporation Restricted	176,836	53,051	61,115
Viterra Inc.	15,000	207,600	206,550
		<u>680,600</u>	<u>639,805</u>
<b>Consumer Discretionary (2.1%)</b>			
Centurion Apartment Properties Limited Partnership	19,470	409,981	413,718
<b>Information Technology (1.8%)</b>			
Teranet Income Fund	38,709	401,749	367,736
<b>Health Care (1.1%)</b>			
Medical Facilities Corporation	22,437	243,488	223,921
<b>Telecommunication Services (0.9%)</b>			
BCE Inc.	4,658	163,602	170,902



**FRONT STREET DIVERSIFIED INCOME FUND CLASS**  
**STATEMENT OF INVESTMENT PORTFOLIO (unaudited)**  
As at April 30, 2008

	Number of Shares / Units or Par Value	Cost \$	Fair Value \$
<b>Corporate Bonds (21.7%)</b>			
Artis Real Estate Investment Trust 7.50% Convertible Debentures November 9, 2010	14,000	13,885	15,890
Citigroup/Starling/Botticelli CDO Notes September 22, 2014	400,000	400,000	180,000
Discover Financial Services Floating Rate June 11, 2010	700,000	579,796	571,274
Duke Funding Limited 2003-5A 4A Floating Rate August 7, 2033	400,000	414,786	100,940
Eveready Income Fund 7.00% Convertible Debentures June 30, 2011	75,000	68,715	69,750
Fairborne Energy Limited 6.50% Convertible Unsecured Subordinated Debentures December 31, 2011	211,864	202,829	207,627
Graoch Associates #161 Limited Partnership 12.25% September 15, 2008	1,000,000	1,019,253	1,009,397
Harvest Energy Trust 7.25% September 30, 2013	266,770	243,839	242,761
Holloway Lodging Real Estate Investment Trust 8.00% August 1, 2011	460,000	461,638	450,800
Huntingdon Real Estate Investment Trust 8.00% June 30, 2010	114,000	114,025	114,000
Paramount Energy Trust 6.25% Convertible Unsecured Subordinated Debentures June 30, 2010	222,300	218,085	215,653
Progress Energy 6.75% Convertible Debentures June 30, 2010	130,500	128,492	135,068
Royal Host Real Estate Investment Trust 6.00% Debentures October 31, 2015	384,000	380,842	363,072
Superior Propane 5.75% Convertible Debentures December 31, 2012	206,145	190,256	200,991
Trinidad Energy Trust 7.75% Convertible Debentures July 31, 2012	218,998	208,819	218,998
True Energy Trust 7.50% Convertible Debentures June 30, 2011	99,000	89,142	93,654
Whitehorse Limited Floating Rate 2006-1A May 1, 2018	200,000	155,720	169,768
		<u>4,890,122</u>	<u>4,359,643</u>
<b>Government Bonds (8.6%)</b>			
Province of Manitoba 5.25% March 2, 2009	433,000	442,695	440,720
Province of New Brunswick 4.25% December 2, 2008	210,000	210,214	211,378
Province of Quebec Real Return 3.30% December 1, 2013	916,000	1,084,530	1,068,450
		<u>1,737,439</u>	<u>1,720,548</u>
<b>Currency Forwards (0.2%)</b>			
Currency forward contract to sell USD 2,300,000 for CDN 2,347,840 with an exchange rate of 1.0208 maturing May 27, 2008		-	30,553
		<u>-</u>	<u>30,553</u>
<b>TOTAL LONG POSITIONS</b>		<u>16,638,432</u>	<u>15,828,132</u>
<b>TOTAL SHORT POSITIONS</b>		<u>(235,568)</u>	<u>(241,000)</u>
<b>Transaction costs, notes 2 and 6</b>		<u>(29,832)</u>	<u>-</u>
<b>Total investments (77.9%)</b>		<u>\$ 16,373,032</u>	<u>15,587,132</u>
<b>Cash and cash equivalents(19.9%)</b>			3,989,010
<b>Other assets less other liabilities (2.2%)</b>			448,614
<b>Net assets (100.0%)</b>			<u>\$ 20,024,756</u>

\* Non Canadian Holdings

See accompanying notes to the financial statements

# FRONT STREET DIVERSIFIED FUND CLASS

## NOTES TO THE FINANCIAL STATEMENTS

APRIL 30, 2008

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### 1. THE FUND

Front Street Diversified Income Fund Class (the "Fund") is a class of shares of Front Street Mutual Funds Limited (the "Corporation"), a mutual fund corporation incorporated under the Canada Business Corporations Act on April 11, 2006, and is authorized to issue an unlimited number of classes of shares in multiple series. Reference is made to the Fund's simplified Prospectus for additional information on the Fund's structure. Series A commenced operations on June 22, 2006. Series B commenced operations on June 22, 2006. Series F commenced operations on August 11, 2006.

The foregoing financial statements and accompanying notes to the financial statements presented herein are for the Fund. Separate financial statements of each of the other classes of shares of the Corporation have also been prepared as at April 30, 2008.

Management of Front Street Mutual Funds Limited is the manager of the Fund (the "Manager"). Front Street Investment Management Inc. (the "Investment Advisor") has been retained by the Manager, on behalf of the Fund, to provide investment advisory and portfolio management services to the Fund. NBCN Inc. is the custodian and Felcom Data Services Inc. provides fund accounting and shareholder recordkeeping services.

The Fund's investment objective is to provide Fund security holders with capital appreciation through investment in a diversified portfolio of income trusts, preferred shares and corporate and government debt. The Fund's portfolio (the "Portfolio") will include securities the Fund's Investment Advisor believes are undervalued and may include short positions in securities the Investment Advisor believes are overvalued.

The Investment Advisor will manage the relative weightings of the Fund's long and short positions to achieve the Fund's investment objective. The Fund will also engage in pairs trading, special warrant arbitrage, merger arbitrage, convertible arbitrage and trading in securities of issuers that may be involved in restructurings or business unit dispositions. The Portfolio will consist primarily of investments which generate capital gains, but will also include investments, which generate income.

### 2. SIGNIFICANT ACCOUNTING POLICIES

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

a) Adoption of new accounting standards - Financial instruments

On November 1, 2007 the Fund adopted CICA Section 3862, Financial Instruments – Disclosures (“Section 3862”) and CICA Section 3863, Financial Instruments – Presentation (“Section 3863”), replacing Section 3861. Section 3862 requires enhanced disclosure of the nature and extent of the risks arising from financial instruments and how the Funds manage those risks. Section 3863 carries forward unchanged the presentation requirement of 3861 with respect to financial instruments.

In April 2005, the Canadian Institute of Chartered Accountants ("CICA") issued Section 3855, Financial Instruments - Recognition and Measurement, effective for financial statements relating to fiscal years beginning on or after October 1, 2006. This section establishes standards for the valuation of financial instruments, including the Fund's investments, and the accounting for transaction costs. Section 3855 requires that the fair value of financial instruments which are traded

## FRONT STREET DIVERSIFIED FUND CLASS

### NOTES TO THE FINANCIAL STATEMENTS

APRIL 30, 2008

in active markets be measured based on the bid price for long securities and the ask price for short securities. Prior to the implementation of this new standard, the fair value was based on the last traded price for the day, when available. Section 3855 also requires that transaction costs, such as brokerage commissions, incurred in the purchase and sale of securities be charged to net income in the period. Prior to this new standard, these costs were added to the cost of the securities purchased or deducted from the proceeds of sale. Section 3855 has been applied retrospectively without restatement of prior periods effective November 1, 2006. The cost of individual investments in the Statement of Investment Portfolio are recorded at total cost including transaction costs. Accordingly, the opening net assets in the Statement of Changes in Net Assets for the period ended April 30, 2008 has been adjusted to reflect these changes in valuation.

National Instrument 81-106 ("NI 81-106") issued by the Canadian Securities Administrators ("CSA") in 2005, requires the daily net asset value ("NAV") of an investment fund to be calculated in accordance with Canadian GAAP. The CSA had granted relief to investment funds from the requirement to comply with Section 3855, for the purposes of calculating of net asset value used for the investor transactions ("Transactional NAV") to the earlier of (i) September 30, 2008, or (ii) the date on which changes to Section 14.2 of NI 81-106 come into effect. The CSA are currently reviewing the suitability of applying Section 3855 for the purposes other than the preparation of financial statements. Depending on the outcome of such review, the method by which net asset value is calculated may change on October 1, 2008. These financial statements have been prepared on a basis consistent with the proposed amendments including a reconciliation between net assets and net asset value.

In accordance with the decision made by the Canadian securities regulatory authorities, a reconciliation between the transactional net asset value ("NAV") and net assets calculated using generally accepted accounting principles ("GAAP NAV") of an investment fund is required for financial reporting periods commencing October 31, 2007. For investments that are traded in an active market where quoted prices are readily and regularly available, Section 3855 requires bid prices (for investments held) and ask prices (for investments sold) to be used in the fair valuation of investments, rather than the use of closing sale prices currently used for the purpose of determining transactional NAV. For investments that are not traded in an active market, Section 3855 requires the use of specific valuation techniques, rather than the use of valuation techniques by virtue of general practice in the investment funds industry.

These changes account for the difference between transactional NAV and GAAP NAV. The impact of the adoption of Section 3855 on the net asset value of the Fund is as follows:

As at April 30, 2008	Net Asset Value			Net Asset Value per Share	
	Transactional NAV	Section 3855 Adjustment	GAAP NAV	Transactional NAV	GAAP NAV
	\$	\$	\$	\$	\$
Series A	13,036,840	(30,631)	13,006,209	8.97	8.95
Series B	6,569,850	(15,441)	6,554,409	8.97	8.95
Series F	465,231	(1,093)	464,138	8.98	8.96
<b>Total Net Asset Value</b>	<b>20,071,921</b>	<b>(47,165)</b>	<b>20,024,756</b>		

## FRONT STREET DIVERSIFIED FUND CLASS

### NOTES TO THE FINANCIAL STATEMENTS

APRIL 30, 2008

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b) Valuation of investments

- i) Investments listed on an exchange are valued at the last bid price reported by the principal securities exchange on which the issue is traded on the financial statement date. The difference between this amount and cost is shown as the change in the unrealized appreciation (depreciation) of the value of investments. Securities for which reliable quotations are not readily available are valued at fair value, as determined in good faith and pursuant to procedures established by the Manager.
- ii) Any investment for which a market quotation is not readily available (“private companies”) shall be valued at cost, in the absence of any subsequent financing, or shall be valued at its fair value as determined by the Manager.
- iii) Investments which are restricted as to transferability are valued at the fair value of the unrestricted investment as provided in paragraphs (i) and (ii) above less a discount of 2% per month up to four months.

The process of valuing investments for which no published market exists is inevitably based on inherent uncertainties and the resulting values may differ from values that would have been established had a ready market existed for these investments.

- iv) Short-term investments are valued at amortized cost, which approximates fair value.
- v) Trust units are valued at the last bid price reported by the principal securities exchange on which the issue is traded on the financial statement date. The cost of the trust units is reduced on an annual basis by distributions from the trust and increased by the annual income allocated to the units by the trust.
- vi) The Fund values its investments in limited partnerships at fair value as determined by the Manager. The Fund calculates the cost value of its investment in limited partnerships using the equity method. Under this method, the limited partnership investments are recorded at cost plus the Fund's pro rata share in undistributed earnings since acquisition.
- vii) The Fund may make short sales whereby a security that it does not own is sold in anticipation of a decline in the fair value of the security. Securities which are sold short are valued at the last ask price reported by the principal securities exchange on which the issue is traded on the financial statement date. To enter a short sale, the Fund may need to borrow the security for delivery to the buyer.

While the transaction is open, the Fund will also incur a liability for any paid dividends or interest which are due to the lender of the security.

- viii) The fair value of other financial assets and liabilities approximate their carrying values due to the short-term nature of these instruments.

## FRONT STREET DIVERSIFIED FUND CLASS

### NOTES TO THE FINANCIAL STATEMENTS

APRIL 30, 2008

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c) Transaction costs

In accordance with Section 3855, portfolio transaction costs are expensed and are included in "Transaction costs" in the Statement of Operations. Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of an investment, which include fees and commissions paid to agents, advisors, brokers and dealers, levies by regulatory agencies and securities exchanges. The individual security's cost shown on the Statement of Investment Portfolio includes only those transaction costs incurred on the acquisition of portfolio investments. Prior to the adoption of Section 3855, transaction costs were capitalized and included in the cost of purchase or proceeds from sale of investments. The impact on the net assets of the investment fund is the same regardless of which accounting method is utilized.

d) Cash and cash equivalents

Cash and cash equivalents consist of cash balances with banks and highly liquid short-term investments with original terms to maturity of less than three months.

e) Investment transactions and income recognition

Investment transactions are accounted for on a trade date basis. Gains and losses from such transactions are calculated using the average cost of the securities on disposition.

Interest income is recorded on an accrual basis. Dividend income is recorded on the ex dividend date.

f) Foreign currency translation

Income, expenses and investment transactions in foreign currencies are translated into Canadian dollars at the rate of exchange prevailing on the dates of such transactions. Assets and liabilities in foreign currencies are translated into Canadian dollars at the closing exchange rates on each valuation day.

g) Earnings (loss) per share

Earnings (loss) per share are based on the increase (decrease) in net assets from operations attributable to each series of shares divided by the weighted average number of shares outstanding of that series during the period.

h) Net assets per share

The net assets per share is calculated by dividing the net assets of a series of shares by the total number of shares of the series outstanding at the end of the period.

i) Estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires the Manager to make estimates and assumptions that affect the reported amount of assets and liabilities, the disclosure of contingent assets and liabilities at the date of financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from those estimates.

## FRONT STREET DIVERSIFIED FUND CLASS

### NOTES TO THE FINANCIAL STATEMENTS APRIL 30, 2008

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#### 3. SHARES ISSUED AND OUTSTANDING

The authorized capital of the Fund consists of an unlimited number of mutual fund shares, available in three series. Redemption and commission fees vary according to each series of shares as follows:

##### Series A shares

Redemption fees payable to the Manager may be applicable upon the sale of shares of this series based on the original cost amount and the time to disposition. A redemption fee of 3% applies to shares of this series sold within the first 18 months following acquisition. A redemption fee of 2% applies to shares of this series sold after the first 18 months and prior to 36 months following acquisition. No redemption fee applies to shares of this series sold after the first 36 months following acquisition.

##### Series B shares

Commission fees payable to brokers, dealers or advisors may be applicable upon the purchase of shares of this series up to 3% of the gross purchase amount, at the discretion of the broker, dealer or advisor.

##### Series F shares

No redemption or commission fees are applicable to shares of this series.

The Fund allocates income and expenses, and realized and unrealized capital gains and losses to each class of shares outstanding based on the average class allocation for the period.

The following shares were issued and redeemed during the periods indicated:

<b>For the Periods Ended April 30,</b>	<b>2008</b>	<b>2007</b>
Shares outstanding, beginning of the period:		
Series A	1,461,992	581,171
Series B	837,203	1,058,552
Series F	47,596	26,080
Shares issued during the period:		
Series A	82,895	495,561
Series B	40,380	250,913
Series F	4,131	24,956
Shares reinvested during the period:		
Series A	32,168	17,799
Series B	19,138	25,934
Series F	1,552	448
Shares redeemed during the period:		
Series A	123,114	20,711
Series B	164,209	246,579
Series F	1,454	25,378

## FRONT STREET DIVERSIFIED FUND CLASS

### NOTES TO THE FINANCIAL STATEMENTS APRIL 30, 2008

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Shares outstanding end of period:		
Series A	1,453,941	1,073,820
Series B	732,512	1,088,820
Series F	51,825	26,106

#### 4. MANAGEMENT AND PERFORMANCE FEES

The Fund pays the Investment Advisor a monthly management fee equal to 1/12 of 2% of the net asset value of the Fund calculated and paid at the end of each month in arrears from each Fund series.

The Fund is responsible for payment of all operating and administrative expenses of the Fund. The main components of these expenses are legal and accounting fees, printing expenses, reporting issuer filing and sustaining fees, custodial fees, fees payable to and expenses incurred by the Independent Review Committee and expenses of making distributions to shareholders. As the Fund has more than one series of shares, the shareholders of each series, bear their pro rata share of those expenses which are common to the operation of all series as well as those expenses which are attributable solely to that series.

The Fund pays the Investment Advisor a performance fee if the percentage gain in the net asset value of a series of the Fund (as adjusted for any prior return deficiencies) over the preceding fiscal quarter or quarters since a performance fee was last payable exceeds the percentage gain or loss of the benchmark (the "Benchmark") over the same period. The Benchmark for the Fund is calculated as follows: 50% of the percentage gain or loss in the S&P/TSX Income Trust Index and 50% of the percentage gain or loss in the ScotiaMcLeod Bond Index over the same period. The fee will be equal to this excess return per share multiplied by the number of shares outstanding at the end of the quarter multiplied by 20%, provided that the net asset value per share of the Fund (including distributions) is greater than all previous values at the end of each previous fiscal quarter, in which a performance fee was paid. The starting reference point for the next fiscal quarter's calculation will be based on the higher of either the Benchmark performance adjusted net asset value per share or the adjusted actual net asset value per share, both with respect to the previous quarter in which a performance fee was payable.

#### 5. INCOME TAX AND DISTRIBUTION

The Fund qualifies as a mutual fund corporation under the Income Tax Act (Canada). The Corporation will earn three types of income being Canadian dividends, taxable capital gains and other net taxable income. The income of the Fund, including taxable capital gains, will be subject to tax at applicable corporate tax rates, after claiming allowable deductions for expenses and applicable credits for foreign taxes paid on foreign source income. Tax on capital gains is refundable to the Fund to the extent that such gains are distributed to shareholders as capital gains dividends or the Fund's share are redeemed. Gains and losses realized by the Fund in relation to certain derivative transactions and short sale transactions may be taxed on account of income as opposed to on account of capital. Other income is subject to tax at normal corporate rates and is not subject to refundable tax treatment.

The Fund may elect in the prescribed manner and form in order to have the dividends it distributes treated as capital gains dividends to the extent that the dividends do not exceed the Fund's capital gains dividend account. The capital gains dividend account will be represented by the amount by which capital gains realized by the Fund while it was a mutual fund corporation exceed the aggregate of:

## FRONT STREET DIVERSIFIED FUND CLASS

### NOTES TO THE FINANCIAL STATEMENTS

APRIL 30, 2008

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- (a) capital losses realized by the Fund while it was a mutual fund corporation;
- (b) certain capital gains dividends previously paid by it; and
- (c) amounts in respect of which the Fund received capital gains tax refunds.

The Fund anticipates that gains and losses realized on the disposition of investments will normally give rise to capital gains not ordinary income. The Fund intends to declare sufficient capital gains dividends so that it is entitled to a refund of the full amount of tax paid or payable on their capital gains. The suspended loss rules in the Income Tax Act (Canada) may prevent the Fund from recognizing capital losses on the disposition of securities in certain circumstances, which may increase the amount of capital gains dividends that the Fund must pay to Fund shareholders.

If allowable capital losses exceed taxable capital gains of the Fund in any taxation year, the excess cannot be allocated to shareholders, but may be carried back three years and carried forward indefinitely and be applied against taxable capital gains in such previous or subsequent years.

The Fund will allocate taxes payable and recoverable of the Fund to each of the classes. The Fund can pay ordinary taxable dividends or capital gains dividends to shareholders of any class in order to receive a refund of taxes on Canadian dividends or capital gains taxes. The Fund intends to pay out such dividends so as to maximize tax refunds and minimize taxes payable at the corporate level.

The Fund may be subject to provincial capital taxes. The Fund may also be subject to large corporations' capital tax under Part 1.3 of the Income Tax Act (Canada) although it is proposed that such tax be reduced and then eliminated by 2008.

The corporation's shares are qualified investments for registered plans.

#### 6. TRANSACTION COSTS

The total brokerage commissions paid by the Fund with respect to securities transactions for the period ended April 30, 2008 was \$56,031 (2007 - \$41,847).

#### 7. RELATED PARTY TRANSACTIONS

Management fees of \$216,572 (2007 - \$206,316) were paid to the Investment Advisor, a company under common control to the Manager, during the period (see note 4). Performance fees of \$Nil (2007 - \$101,721) were also paid to the Investment Advisor during the period (see note 4). Included in accrued expenses are \$34,701 (2007 - \$11,995) of management fees payable to the Investment Advisor.

The Fund may place a portion of its portfolio transactions with brokerage firms which are affiliates of the Manager provided it determines that these affiliates' trade execution abilities and costs are comparable to those non affiliated, qualified brokerage firms, on an execution only basis. During the period ended April 30, 2008, Tuscarora Capital Inc, a company under common control to the Manager, received \$3,151 (2007 - \$6,528) in commissions on portfolio transactions for the Fund.

Management fees and performance fees are measured at the exchange amount of consideration prescribed by the offering documents of the Fund. When related parties enter shareholder transactions with the Company, the exchange amount of consideration is the transactional NAV available to all other shareholders on the trade date. In the case of brokerage commissions, the exchange amount of consideration is that which is negotiated by the related parties.



## FRONT STREET DIVERSIFIED FUND CLASS

### NOTES TO THE FINANCIAL STATEMENTS APRIL 30, 2008

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#### 8. MANAGEMENT OF FINANCIAL RISKS

The Fund's investment activities expose it to various types of risk associated with the financial instruments and markets in which it invests directly. The following is a summary of the main risks:

##### *Credit risk*

Financial assets which potentially expose the Fund to credit risk consist principally of investments in bonds, amounts due from brokers and derivatives. The Fund seeks to mitigate its exposure to credit risk by placing its cash and transacting its securities activity with large financial institutions. The Fund also invests in corporate bonds. Until the bonds are sold or mature, the Fund is exposed to credit risk relating to whether the bond issuer will meet its obligation when they come due. The extent of the Fund's exposure to credit risk in respect of these financial assets is reflected in their carrying value as recorded in the Fund's Statement of Net Assets.

##### *Liquidity risk*

Liquidity risk is the risk the Fund will encounter difficulty in meeting obligations associated with financial liabilities. Shareholder redemption requests are the main liquidity risk for the Fund.

The Fund maintains sufficient cash and marketable securities, and manages liquidity risk through its ability to close out market positions

##### *Price risk*

Price risk, is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from interest rate risk or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting similar financial instruments traded in the market.

The Fund is exposed to market price risk arising from its investments in securities and derivatives. The Investment Advisor manages the Fund's market risk on a daily basis in accordance with the Fund's investment objective and policies.

##### *Price sensitivity*

The following details the Fund's sensitivity to 5% increase and decrease in the fair value, with 5% being the sensitivity rate used when reporting price internally to key management personnel and representing management's assessment of possible change in fair value.

At April 30, 2008, if the fair value had been 5% higher with all other variables held constant, the increase in net assets representing shareholders' equity for the period would have been \$777,829 higher, arising due to the increase in the fair value of financial assets at fair value by \$789,879 offset by the increase in the fair value of the financial liabilities at fair value by \$12,050

If fair value had been 5% lower with all other variables held constant, the decrease in net assets representing shareholders' equity for the period would have been \$777,829 lower, arising mainly due to the decrease in the fair value of financial assets at fair value by \$789,879 set off by decrease in fair value of the financial liabilities at fair value by \$12,050.

## FRONT STREET DIVERSIFIED FUND CLASS

### NOTES TO THE FINANCIAL STATEMENTS APRIL 30, 2008

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#### 8. MANAGEMENT OF FINANCIAL RISKS (Continued)

##### *Currency risk*

The Fund holds assets denominated in currencies other than Canadian Dollars which is the functional currency. The Fund is therefore exposed to currency risk, as the value of the securities denominated in other currencies fluctuates due to change in exchange rates.

##### *Interest rate risk*

The Fund may invest in fixed and floating rate securities. The income of the Fund may be affected by changes to interest rates relevant to particular securities or as a result of management being unable to secure similar returns on the expiry of contracts or sale of securities. The value of fixed interest securities may be affected by interest rate movements or the expectation of such movement in the future. Interest payable on bank overdraft or broker margin account positions will be affected by fluctuations in interest rates. As at April 30, 2008, there were 30.3% of investments owned which are held in bonds. There were investments in short-term investments representing 8.1% of the investments owned, all maturing in less than 30 days. The remaining portion of the Fund's assets is substantially non-interest bearing equity investments and its exposure to interest rate changes is minimal.

##### *Capital management*

Management considers the Fund's capital to consist of the issued ordinary share capital and the net assets attributable to participating shareholders.

The Investment Advisor manages the capital of the Fund in accordance with the Fund's investment objectives, policies and restrictions, as outlined in the Fund's offering memorandum, while maintaining sufficient liquidity to meet participating shareholder redemptions. The Fund's overall strategy for managing capital remains unchanged from 2007.

The Fund does not have any externally imposed capital requirements.



