

# Evolving Our Programs



# Building Our Future



**Davis + Henderson**  
Income Fund

2004  
ANNUAL REPORT



## Our Goal

To deliver value to our unitholders by meeting the needs of Canadian financial institutions

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In addition to historical information, this Annual Report may contain forward-looking statements, subject to risks and uncertainties beyond management's control. Actual results could differ materially from those expressed in this report. Risk factors are discussed in the Annual Information Form ("AIF") filed with the Ontario Securities Commission by Davis + Henderson Income Fund.

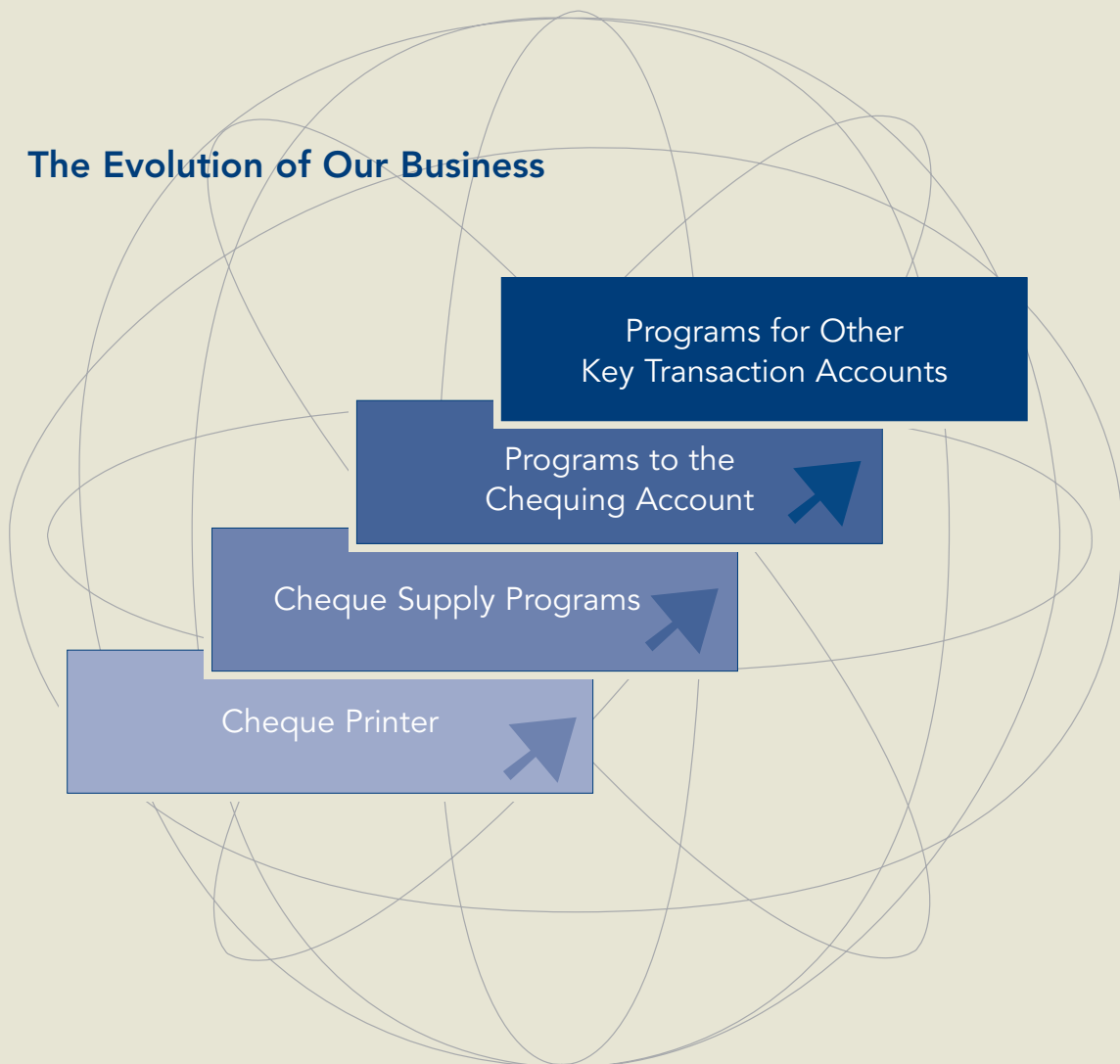
# Our Evolution

**At Davis + Henderson**, we strive to deliver stable and modest growth to our unitholders by being a valued service partner to Canada's financial institutions.

To achieve our purpose, we believe it is important to build on our foundation, developed over the past 130 years, and to continue our evolution. Although our evolution seems subtle, our natural progression from cheque printer to provider of cheque supply programs to our future as a program supplier to the chequing, lending and other key accounts is both logical and important in meeting our objectives.

To learn more about this evolution, please turn to page 8.

## The Evolution of Our Business



# Building our future by meeting our commitments to unitholders

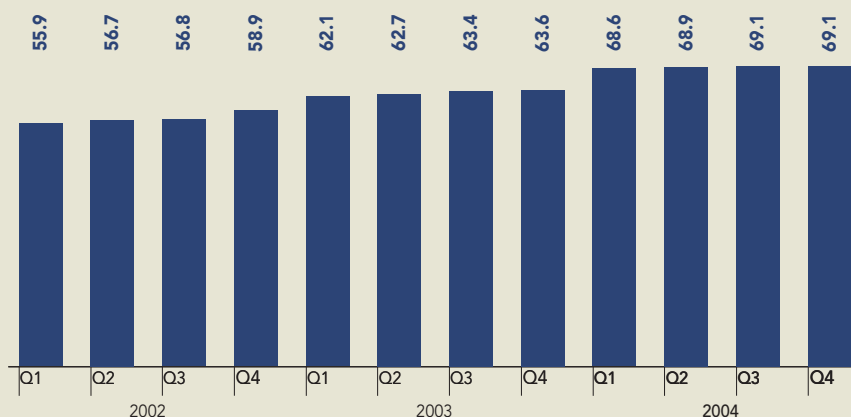
OUR OBJECTIVE for unitholders is to deliver stable and growing cash distributions by targeting annual sales increases in the range of 3% to 5% while maintaining operating margins at traditional levels.

Since listing on the Toronto Stock Exchange in

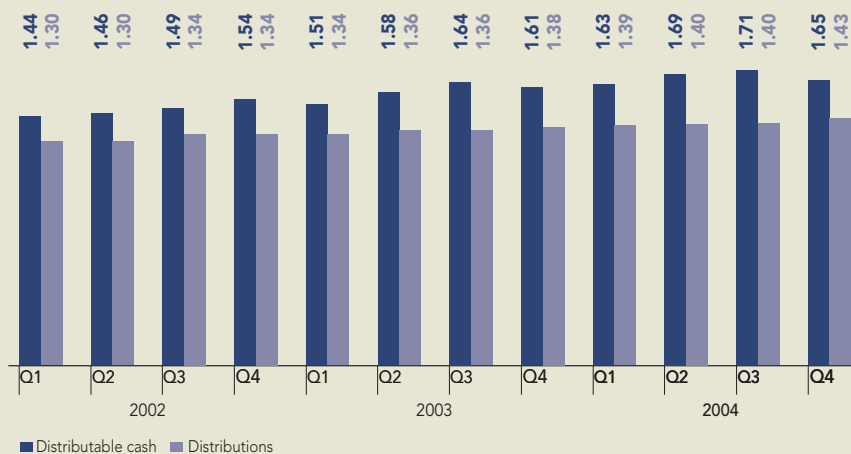
December 2001, we have met this objective.

Davis + Henderson has increased its cash distributions five times since its initial public offering. In 2004, total distributions declared amounted to \$1.40 per unit, 3.3% higher than in 2003.

Revenue by Quarter  
(\$ millions)



Distributable Cash and Distributions by Quarter  
(annualized \$ per unit)



Please Note: The term “Distributable Cash” is not a defined term under Canadian generally accepted accounting principles. Please refer to the detailed definition on page 34 of this Annual Report.

# Building our future by enhancing value for our customers

WE UNDERSTAND that to be successful for our owners, employees and communities we must first ensure that our programs enhance value for our customers. For us, this means meeting their needs for increased productivity, customer retention and value for their customers. We strive to contribute to our customers' priorities in a number of ways that have involved an evolution in our programs and program delivery.

To deliver increased productivity for our customers, we established our integrated ordering channels, *ChequeCentral* and *ChequeAdvisor*. *ChequeCentral* is a web-based electronic product catalogue that enables in-home as well as in-branch ordering. *ChequeAdvisor* allows telephone ordering for those who value direct contact and expert advice from Davis + Henderson staff during the purchase process.

By moving from branch-initiated paper orders to integrated ordering channels, we have helped our customers provide faster, more efficient and flexible service to their customers – with less time required by branch staff and at a lower all-in cost for these institutions. Considering that we deliver cheque supply programs and related services on behalf of our customers to 20 million individual account holders as well as cheque and deposit programs to more than one million small business enterprises, ordering efficiency is highly valued. In 2004, the number of direct orders we received through *ChequeCentral* and *ChequeAdvisor* increased by 41%, to more than 16% of all orders received.

To help deliver increased customer retention for our financial institution customers and increased value for their customers, we have evolved from providing “just cheques” to the delivery of several product and service programs for the chequing account, including our deposit programs and *ChequeEssentials* as well as *eSwitch*™.

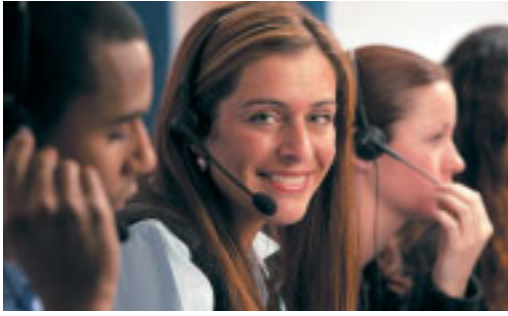
Our deposit programs have expanded from personalized deposits to, more recently, security bags. This program is more convenient not only for small businesses, but also for our financial institution customers.

*ChequeEssentials* is a concept we developed to improve the order process for financial institutions and enhance our product offering for the benefit of their new business customers. We've done this by bundling together popular products such as business cheques, personalized deposit slips, personalized endorsement stamps and a binder. In 2004, this program represented 30% of all new business orders we received.

*eSwitch*™ is built around the new account opening process, and it assists our customers' customers to more easily redirect electronic pre-authorized payments and direct deposits from one account to another. Like our other programs, *eSwitch*™ supports improved customer service. It is now employed by some of our largest customers.

In these and many other subtle ways, Davis + Henderson is evolving and striving to meet our customers' needs while building for our future.





## Building our future by engaging our employees

TO HAVE SATISFIED CUSTOMERS and unitholders, we believe it's important to have engaged and satisfied employees. Our evolution has always reflected this principle as a priority.

Today, we employ more than 800 people in a wide variety of disciplines. With such a diverse workforce, the key to creating satisfied employees is to understand their needs. To do this, regular employee surveys are conducted, the findings are shared and we act together on suggested improvements.

Ongoing and open communication is also important. This is why we hold monthly departmental communication sessions to review significant current issues and key accomplishments. Quarterly, a business overview is sent to all employees reviewing how we are progressing against our annual plans and strategic goals. On an annual basis, a major presentation is given to all employees. These annual presentations outline our goals, accomplishments and

future strategies and ensure each employee understands the role he or she must play in achieving Davis + Henderson's objectives.

We also encourage our employees to lead, and they do. Employee-led initiatives supporting our goal of operational excellence involve programs such as "5S," as well as the adoption of lean and cellular manufacturing. In all of these initiatives our employees are given appropriate support to learn new approaches, but once learned they take full ownership and responsibility. We also apply a continuous improvement methodology. This allows us to constantly raise our expectations of consistently increasing our service and value proposition to our customers.

The culture that supports these initiatives is strong and built on a foundation of trust, integrity and respect. We believe every goal can be accomplished with teamwork – when everyone pulls together for the same common purpose.

# Building our future by giving back to our communities

THE HEALTH AND WELL-BEING of the communities where we live and work are important to Davis + Henderson. Our social responsibility framework is similar to that of our customers – Canada’s financial institutions. We focus our support under three pillars.

The first is the education and wellness of Canada’s youth. We are proud of our involvement in supporting Canada’s number one asset for the future: our children.

Health issue funding and social services is another pillar of our commitment and we support many worthy causes in this area. In addition, Davis + Henderson and our employees have made an ongoing commitment to *United Way* because we believe this organization is able to most effectively support social services across our communities.

The third pillar is Canadian arts and culture. To help make our society vibrant and flourishing, we support creative endeavours such as local musical,

dance and theatrical organizations and events. Contributions to our communities are demonstrated in many ways. Our employees contribute their time as eagerly as their dollars to make their communities better places to be, through their leadership in local sports, social and cultural activities.

Giving back to these communities also means creating opportunities for our customers’ account holders to support their favourite charities. Through the creation of cause-awareness cheques, we enable financial institutions’ customers to donate a portion of their purchase price to designated charities. Moreover, each time they use a cheque, they raise the profile of a charity of importance to them such as *Aboriginal Youth, Canadian Amateur Athletics, Canadian Breast Cancer Foundation, Children’s Wish Foundation, Humane Society of Canada* and *World Wildlife Fund of Canada*.

We will continue supporting these social pillars as a cornerstone of our culture at Davis + Henderson.



## Building our future through active and committed governance

**2004 was an active year for all members of the Davis + Henderson team, including your independent trustees and directors.**

MUCH WAS ACCOMPLISHED. The Fund delivered to unitholders stable and growing cash distributions. Two distribution increases were approved by the trustees during the year and total distributions declared increased 3.3% to \$1.40 per unit in 2004. At the same time, the Fund was able to grow cash flows, allowing the business to invest in capabilities that support managed growth, enhanced efficiency and customer service while continuing to reduce bank debt. Full details of the Fund's performance can be found in the Management's Discussion and Analysis beginning on page 12.

In 2004, we also devoted considerable time to evaluating Davis + Henderson's long-term strategic plan. This plan, which evolves over time, provides us with a roadmap to the future and a means to evaluate performance. We are satisfied with this plan and confident the business has the means to continue to fully implement it.

Special focus was given to succession planning in 2004. During the second quarter, we announced that Sanford McFarlane and Bob Cronin would share the new title of Co-Chief Executive Officer. They have shared executive management responsibilities for some time and this appointment formalized their strong working relationship. However, it will also ensure management continuity and stability for the foreseeable future and therefore meets a key planning objective.

The Fund also successfully converted to a trust-on-trust structure at a special meeting of unitholders held in July. The new structure is explained in more detail in the MD&A and brings the Fund in line with the models used by income trusts that have gone public more recently. This structure does not, in any way, change your holdings or the Fund's prospects.

Corporate governance requirements continue to evolve in Canada, and we actively review and adopt new processes and policies as appropriate to this changing environment. We believe that we have good governance guidelines in place and that they are being adhered to.

The Fund is served by five trustees, all of whom are independent of management and have no business dealings with Davis + Henderson. We manage the business through the board of directors of the general partner and all five trustees sit on our seven-person Board. Two of these directors, Bob and Sanford, are management representatives, but neither is a member of our trustee and board committees. Our Chairman and all committee members are independent of, and unrelated to, management and the business.

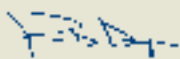
In total, the Board met as a whole 12 times in 2004, while the Audit Committee met five times and

the Compensation and Governance Committee three times. At each meeting, there was an opportunity for the independent trustees and directors to meet without the presence of management.

For additional details on governance and compensation practices at Davis + Henderson Income Fund, please review the Fund's Management Information Circular, which is available online at [www.dhltd.com](http://www.dhltd.com).

We are committed to serving the interests of unitholders through sound corporate governance practices. But more than this, we are committed to applying our collective experience to help the Fund continue to evolve in a manner that meets the needs of all our stakeholders.

Yours sincerely,



Paul Damp  
*Trustee and Director*



Gordon J. Feeney  
*Trustee and Director*



Allan Gotlieb  
*Trustee and Director*



Bradley Nullmeyer  
*Trustee and Director*



Helen K. Sinclair  
*Trustee and Director*

# Evolving Our Programs



## Building Our Future

Davis + Henderson continues to build its future through the evolution of its customer-focused programs. Here, Co-Chief Executive Officers Sanford McFarlane and Bob Cronin discuss recent financial performance, as well as the future of the business.

## Management Q&A

### **You indicate that your objective is to grow revenues in the 3% to 5% range, yet in 2004 you exceeded that target. How were you able to do that?**

2004 was a good year for Davis + Henderson's cheque supply and other evolving programs. What allowed us to exceed our objective was the launch, in January 2004, of our U.S. cheque program for a Canadian customer. As expected, this had the impact of lifting our revenues on a year-over-year basis. Now that this business forms part of our revenue base, our annual objective for 2005 and beyond will be 3% to 5% revenue growth once again.

### **How did your Canadian programs perform in 2004?**

Very well. We continued to enhance our cheque and related product offerings, which allowed us to increase the value of the orders we deliver. We also received more orders over the phone and the Internet directly from our financial institutions' customers, rather than through their branch networks. To be specific, in 2004, 16% of all customer paid orders came to us through these direct channels, up from 11% in 2003. This is gratifying because we invested in these interactive channels as part of our strategy to improve convenience for individual and business consumers while reducing administrative work for branch staff. For Davis + Henderson, this change generally results in higher order values as consumers often choose more products and more premium products when they contact us directly.

Additionally, we continued to find success by expanding other programs, such as our deposit program for small businesses and our pre-authorized switching service, available as part of several of our customers' account opening processes.

### **So what can we conclude from 2004's performance?**

That Davis + Henderson continued to focus on increasing value for our customers, the country's financial institutions. By doing that, we've been able to grow revenues from our programs that service the chequing account. Simply put, these programs provide our customers with value and our unitholders with the steady and reliable cash flows that have allowed us to modestly grow distributions.

**You've used the term "evolution" several times in this Annual Report and elsewhere to describe Davis + Henderson's approach to the future. Can you explain what this means?**

At Davis + Henderson, we've always attempted to build our products and services in support of our customers' changing needs. This saw us evolve from a cheque printer to a supplier of cheque programs. For example, we became more involved in the design of the cheque product (including items such as security features) and more involved in the ordering process, including Internet and telephone ordering. While it sounds subtle, these changes have given more value to our customers and led to more revenues for Davis + Henderson.

**So where is this evolution taking you now?**

More recently, we've been providing additional programs directed towards the chequing account. Examples include our deposit programs and our switching programs. These programs lever our existing capabilities to provide new value-added services. We intend to continue to evolve by providing additional programs directed towards the chequing account. Beyond that, we will look to expand our programs to serve our customers in their other key relationship areas, such as lending. We see all of this as a natural evolution of our business, which we hope will continue for many years to come.

**As you evolve, will we notice any significant difference in the performance of the Business?**

No, we do not believe so. Our business plans are built on numerous incremental growth initiatives which, when combined, are intended to contribute to our target objective of growing revenues in the 3% to 5% range. While there are always risks attached to introducing new products and services, we believe there is far less risk attached to an evolutionary approach to growth.

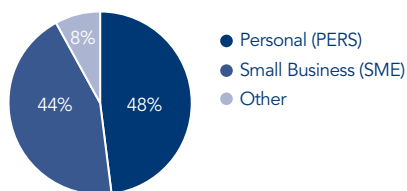
**In 2004, you increased your maintenance capital spending by about \$2 million. As you grow and evolve, will you require significantly more capital?**

In 2004, we invested more capital in support of our call centre and Internet ordering applications. Davis + Henderson has clearly benefited from these capital initiatives. Additionally, we are spending more in updating and replacing portions of our existing technology infrastructure, and we currently have in place the financial capacity to fund this capital. In aggregate, we expect to spend approximately the same or a little more in 2005 compared to 2004. Beyond 2005, as our business continues to evolve, we will need to apply more capital as we deliver new services. However, we are mindful that we must apply capital in a way that is accretive to our unitholders.

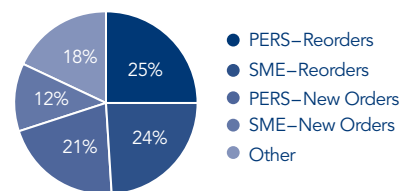
## Last year, you spoke about several trends in your business, including the declining use of cheques. Have there been any significant changes in these trends?

We do not believe there have been any significant changes over the last year. Individuals and small businesses continue to have many payment alternatives and they are using them. In our planning, we assume a decline in our cheque order volumes in the low single digits annually. However, remember that half of our revenue is not impacted by cheque usage as we receive substantial revenue from orders related to the opening of new chequing accounts and from other products and services. We believe we can continue to grow by enhancing the value of our cheque program and by delivering new programs to the chequing and other key accounts our customers have with their customers.

Revenue Split Between Small Business and Individuals



Reorders vs. New Orders



## It seems that you are continuing on the same path you articulated in previous periods. Should we expect to see any significant changes in 2005?

We continue to work on the same plan: to enhance the value of our cheque supply program, expand into new programs to serve the chequing account and to pursue additional opportunities related to other key transaction accounts of our financial institution customers. So you should not expect any significant changes. What you should expect of us is continued application of our evolutionary strategies.

## Any final words?

Only that we are grateful for the efforts and dedication exhibited by our team in 2004 and for the trust our customers and unitholders continue to place in Davis + Henderson. We look forward to meeting our objectives in 2005 for all stakeholders.

### History

Davis + Henderson Income Fund (the "Fund" or the "Business" or "Davis + Henderson") owns 100% of Davis + Henderson, Limited Partnership ("Davis + Henderson L.P.") through its investment in an intermediary trust, D + H Holdings Trust ("Holdings Trust"). Davis + Henderson L.P. and its predecessors have been serving Canadian financial institutions and their account holders for over 130 years.

The Fund's primary source of revenue and cash flow comes from the operation of cheque supply and related programs for Canadian financial institutions.

### Strategy

The Fund's financial goal is to deliver stable and modestly growing cash distributions to unitholders by targeting annual sales growth in the range of 3% to 5% while maintaining operating margins at traditional levels.

The Fund, for 2004, continued to evolve its key strategies to meet its financial goal by enhancing the value of the core cheque supply program, adding new products to its existing programs and offering new programs and services that financial institutions can offer their customers.

In growing the cheque supply program, the Business is focused on increasing the value of its program through continuously introducing product design alternatives, enhancing security components and combining other logical products into convenient and valuable packages for consumers. Additionally, the Business encourages the financial institutions' customers to reorder directly with Davis + Henderson, thereby improving the efficiency of the order process for the financial institution and improving convenience for the consumer. This direct ordering allows the Business to make consumers more aware of their product and service choices, which results in increasing average order value. The Business has, during 2004, continued to increase the value of its offerings and the volume of orders it receives directly.

Also during 2004, the Business launched a cheque program for the U.S. subsidiary of one of its Canadian financial institution customers. The Business is not currently targeting expansion in the U.S. outside of any growth that might occur under this current contract.

The Business has and will continue to expand its other programs as well. On a year-over-year basis, the Business has grown its deposit program in 2004 and expanded its pre-authorized switching services, *eSwitch*<sup>TM</sup>, to several additional financial institutions.

Looking forward, the Business intends to continue working on the same plan: to enhance the value of the cheque supply program, to expand into new programs to serve the chequing account and to pursue additional opportunities to supply program support for other key transaction accounts offered by the Business' financial institution customers.



Serge Rivest,  
Vice President, Sales  
and Marketing

"Our goal remains unchanged – to help our financial institution customers better serve their customers."

## OPERATING RESULTS

### Consolidated Statement of Income

<i>(in thousands of Canadian dollars, except per unit amounts, unaudited)</i>	2004	Year ended December 31,	
		2003	2002 <sup>1</sup>
Sales	\$ 275,586	\$ 251,783	\$ 228,259
Cost of sales	164,023	151,389	133,835
Gross profit	111,563	100,394	94,424
	40.5%	39.9%	41.4%
Operating expenses	32,766	26,315	24,452
	11.9%	10.5%	10.7%
Operating income	78,797	74,079	69,972
	28.6%	29.4%	30.7%
Interest expense	4,193	4,630	4,527
Amortization expense	15,842	16,397	16,620
Income taxes	4,494	4,595	3,314
Non-controlling interest	–	–	6,501
Net income	\$ 54,268	\$ 48,457	\$ 39,010
Net income per unit, basic and diluted	\$ 1.4311	\$ 1.2778	\$ 1.1485

<sup>1</sup>The year ended December 31, 2002 was compiled from audited financial statements adjusted to remove the 12-day period ended December 31, 2001.

### Consolidated Statement of Distributable Cash

<i>(in thousands of Canadian dollars, except per unit amounts, unaudited)</i>	2004	Year ended December 31,	
		2003	2002 <sup>1</sup>
Net income	\$ 54,268	\$ 48,457	\$ 39,010
Add:			
Non-controlling interest	–	–	6,501
Amortization expense	15,842	16,397	16,620
Future income taxes	3,545	3,583	2,305
Cash flow from operations	73,655	68,437	64,436
Less:			
Distributions to non-controlling interest	–	–	6,501
Maintenance capital expenditures			
Capital and other assets	7,179	5,210	5,006
Contract payments	3,145	3,145	3,145
Distributable cash	\$ 63,331	\$ 60,082	\$ 49,784
Distributions declared	\$ 53,256	\$ 51,567	\$ 43,893
Net income per unit	\$ 1.4311	\$ 1.2778	\$ 1.1485
Distributable cash per unit	\$ 1.6701	\$ 1.5844	\$ 1.5025
Distributions per unit	\$ 1.4044	\$ 1.3599	\$ 1.3200

<sup>1</sup>The year ended December 31, 2002 was compiled from audited financial statements adjusted to remove the 12-day period ended December 31, 2001.



Catherine Martin,  
Chief Financial Officer

“To support continuation of our stable and growing distributions, we will actively manage our new revenue programs, operating expenses and capital expenditure programs.”

## Accounting Principles

All financial information provided is determined and presented in accordance with Canadian generally accepted accounting principles unless otherwise noted.

## Year Ended December 31, 2004 Compared to Year Ended December 31, 2003

### Sales

For the year ended December 31, 2004, the Business recorded sales of \$275.6 million, an increase of \$23.8 million, or 9.5%, over the prior year's sales of \$251.8 million. On January 1, 2004, the Business commenced delivery of products and services under its long-term cheque supply contract with the U.S. subsidiary of one of its major Canadian customers. This initiative contributed significantly to the year-over-year increase in sales. Excluding the impact of this new contract, sales increased approximately 6.6%. Other increases in sales related to increased value of orders received as a result of program enhancements such as *ChequeEssentials*, an account opening bundle for small business, and the continued migration of orders to the telephone order channel, *ChequeAdvisor*, and the web-based order channel, *ChequeCentral*. Complementary programs, such as security deposit bags and *eSwitch*<sup>™</sup>, and two additional working days including the leap year, have also contributed to the sales growth.

*ChequeCentral* is the Business' web-based electronic product catalogue for in-home and in-branch ordering. *ChequeAdvisor* is a program that allows telephone ordering for those who value direct contact and advice from Davis + Henderson staff during the purchase process. The Business' experience indicates that when consumers order directly from the Business utilizing these order channels, rather than through the branch of their financial institution, they are more aware of product choices and choose additional products and premium features, resulting in higher order value.

Management believes that declining cheque usage has historically contributed to and will continue to contribute to declining cheque orders. Management further believes that other factors, including a significant number of orders received upon consumers opening new accounts and the migration by consumers towards orders with fewer cheques, will somewhat mitigate the impact related to reduced cheque usage. During 2004, the general impact of declining cheque usage has been somewhat mitigated as the Business has benefited from promotional programs initiated by its customers, including line of credit cheques.

With the continued success of the *ChequeAdvisor* and *eSwitch*<sup>™</sup> programs, the Business' call centres have become more integrated with the ordering and delivery of its products. The Fund, to better present the cost of this sales activity, has reclassified all customer service costs from operating expenses to cost of sales. All comparative balances presented have been adjusted to reflect this new presentation. There is no impact on sales, operating income, net income or distributable cash as a result of this reclassification.



Yves Denommé,  
Vice President, Operations

“*eSwitch*<sup>™</sup> provides us with a platform for new opportunities to better assist our financial institution customers.”

## Gross Profit and Margin

For the year ended December 31, 2004, gross profit increased \$11.2 million, or 11.1%, over the prior year. Gross margin for 2004 was 40.5% compared to 39.9% in 2003. The increase in gross profit percentage is attributed to the success of the Business' revenue programs previously described and continued investments in technology and processes resulting in increased production efficiencies, partially offset by lower margins earned on U.S.-sourced business.

All revenues and substantially all expenses relating to the U.S.-sourced business are contracted for in U.S. dollars. However, as the net U.S. dollar contribution from this activity is relatively modest, the change in relative dollar valuations is not meaningful, and as a result, the Business does not currently hedge its U.S. net receipts.

## Expenses and Income

Operating expense of \$32.8 million for the year ended December 31, 2004 increased from the prior year by \$6.5 million, or 24.5%. This increase is primarily attributed to growth in technology expenses in support of the *ChequeCentral* and *ChequeAdvisor* programs, the implementation of the U.S. cheque supply program and, more recently, the increase in costs related to technology infrastructure upgrade initiatives. Variable compensation related to the financial performance of the Business also contributed to the increase in expenses.

Another factor related to the increasing operating costs was the internal reorganization undertaken by Davis + Henderson. On July 23, 2004, unitholders approved a change in corporate structure that replaced the intermediary corporation, D + H Holdings Corp., with a trust, thereby converting the Davis + Henderson organization to a trust-on-trust-on-partnership structure. Total charges for legal and professional fees to complete the internal reorganization, included in 2004's operating expenses, were approximately \$1.0 million.

Operating income of \$78.8 million for the year ended December 31, 2004 represents an increase of \$4.7 million, or 6.4%, over the prior year, primarily due to the current year's increase in sales, described above.

Net interest expense of \$4.2 million for the year ended December 31, 2004 is \$0.4 million, or 9.4%, lower than amounts recorded in the previous year. Lower interest expenses are a result of the reduction of average loan balances throughout the year.

Amortization of \$15.8 million for the year ended December 31, 2004 decreased \$0.6 million, or 3.4%, mainly due to certain deferred costs becoming fully amortized. Partially offsetting this decrease was an increase in amortization related to technology investments made in 2003 and 2004.

Income earned by the Business that is distributed annually to unitholders is not subject to taxation in the Business, but is taxed at the individual unitholder level. However, prior to the internal reorganization (as discussed under Corporate Structure Changes), the Fund had a corporate subsidiary that was subject to corporate income and capital taxes.



Chad Alderson,  
Vice President and  
Chief Technology Officer

“In 2005, enhancements to our call centre and information technology systems will be made to improve performance and to expand our capabilities.”

After the internal reorganization, which converted the Davis + Henderson corporate structure to a trust-on-trust-on-partnership structure, the Fund and its subsidiaries are not anticipated to be subject to any of these taxes as long as all taxable income generated by the structure is paid to unitholders in the form of distributions. Accordingly, there are no provisions for income taxes recorded under this new structure and the future income tax asset, previously recorded on the balance sheet, has been charged directly to deficit.

Income taxes recognized in 2004, including large corporations tax and corporate minimum tax, were \$4.5 million and related exclusively to the period prior to the internal reorganization. Although there was no tax provision recorded in the fourth quarter of 2004 as a result of the internal reorganization, the tax provision of \$4.5 million is comparable to that recorded in 2003 for the full year because of the higher level of income year-over-year.

With respect to delivery of product and services under the U.S. cheque supply contract, the Business does not have a permanent establishment in the U.S. for purposes of determining tax liability and therefore does not have U.S. income tax liability.

Net income of \$54.3 million for the year ended December 31, 2004 increased \$5.8 million, or 12.0%, over the comparable period in the prior year.

#### Consolidated Statement of Distributable Cash

Distributable cash is not a defined term under Canadian generally accepted accounting principles but is determined by the Business as net income for the period adjusted to remove specific non-cash items, including amortization and future income taxes, and reduced by maintenance capital expenditures. Non-maintenance capital expenditures are not recorded as a reduction from distributable cash since these expenditures are considered non-recurring and are generally intended to generate future growth in distributable cash and distributions.

Management believes that distributable cash is a useful supplemental measure of performance as it provides investors with an indication of the amount of cash available for distribution to unitholders. Investors are cautioned, however, that distributable cash should not be construed as an alternative to using net earnings as a measure of profitability or as an alternative to the statement of cash flows. Further, the Fund's method of calculating distributable cash may not be comparable to similarly titled amounts reported by other issuers.

Distributable cash increased \$3.2 million, or 5.4%, to \$63.3 million for 2004 relative to \$60.1 million recorded in 2003. The increase was primarily attributable to growth in net income before amortization and future income taxes partially offset by increases in maintenance capital expenditures. This increased investment level supports growth in the core cheque supply business and will enable the replacement and enhancement of certain components of the Business' existing computer and telephony infrastructure. More detail concerning capital expenditures is provided under the Cash Flow and Liquidity section.



Suzanne Mandrozos,  
Vice President, Human Resources

“Development of our employees’ skills will continue so that we can better serve our customers’ evolving requirements.”

Declared distributions of \$53.3 million for the year ended December 31, 2004 represent an increase of \$1.7 million, or 3.3%, compared with 2003. This reflects two increases in declared monthly distributions per unit in 2004. The monthly distribution rate for December 2004 was \$0.1200 per unit, or \$1.44 per unit annualized.

## Year Ended December 31, 2003 Compared to Year Ended December 31, 2002

### Sales

For the year ended December 31, 2003 the Business recorded sales of \$251.8 million, an increase of \$23.5 million, or 10.3%, over the prior year's sales of \$228.3 million. One of two main factors contributing to the increase in sales was a change in the structure of one of the Business' customer contracts, which increased sales and cost of sales with minimal impact on gross profit for 2003. Excluding the impact of the changes in structure of this contract, the year-over-year increase in sales for the year ended December 31, 2003 would have been \$9.4 million, or 4.2%. The other factor that drove the year-over-year improvement was the increase in the value of the orders received. This increase is attributable to product launches in late 2002 and higher revenues from the sale of security deposit bags, as well as increased order values associated with customer migration to the Business' *ChequeCentral* and *ChequeAdvisor* programs.

### Gross Profit and Margin

For the year ended December 31, 2003 gross profit increased \$6.0 million, or 6.3%, from the prior comparable year. This increase was primarily attributed to the growth in sales described above, as well as increased efficiencies related to ordering and production.

The decrease in gross profit percentage to 39.9% in 2003 from 41.4% in the prior year was a result of the customer contract change described above.

### Expenses and Income

Operating expense of \$26.3 million for the year ended December 31, 2003 increased from the prior year by \$1.9 million, or 7.6%. The higher operating expenses in 2003 resulted from increased product launch support costs and increased costs associated with being a public company. Increased corporate costs include higher registration fees, increased insurance costs and increased advisor and professional fees.

Operating income of \$74.1 million for the year ended December 31, 2003 increased \$4.1 million, or 5.9%, over the prior year, primarily due to the current year's increase in sales, described above.



Joanne Sisco,  
Vice President, Corporate  
Data Services

“To provide improved delivery of programs to our customers, we have been enhancing our project management skills to build on our existing capabilities.”

Amortization of \$16.4 million for the year ended December 31, 2003 decreased \$0.2 million, or 1.3%. This decrease in amortization occurred because deferred expenses became fully amortized during the current year. Partially offsetting this reduction was an increase in amortization related to investments made in 2002 and 2003 in digital printing technology and in the development of the *ChequeCentral* cheque ordering application.

Interest expense of \$4.6 million for the year ended December 31, 2003 was consistent with amounts recorded in the previous year although there were changes in the level of debt outstanding and effective interest rates during that 24-month period.

Income tax expense of \$4.6 million increased \$1.3 million for the year ended December 31, 2003 when compared to the prior year. The increase, which related to future income taxes, resulted from higher net income. Large corporations tax was the only cash tax paid and was approximately \$1.0 million in both years.

During the first quarter of 2002, the Business expensed \$6.5 million of paid and accrued distributions to the previous owner of the Davis + Henderson business. This was reflected as a charge against income for the 2002 fiscal year. As a result of the Business' purchase of the balance of the Davis + Henderson business from the previous owner on April 2, 2002, there were no further distributions of this nature and, therefore, there was no comparable charge to income in 2003.

Net income of \$48.5 million for the year ended December 31, 2003 increased \$9.4 million, or 24.2%, over the comparable period in the prior year. Excluding the charge for non-controlling interest, the 12-month growth in net income was \$2.9 million, or 6.5%.

### Distributable Cash

On a per unit basis, distributable cash increased 5.5% in 2003, while cash distributions increased 3.0% year-over-year. The increase was primarily attributable to growth in net income, partially offset by a 2.5% increase in maintenance capital expenditures.

### Eight Quarter Consolidated Statement of Income – Summary

(in thousands of Canadian dollars, except per unit amounts, unaudited)	2004				2003			
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Sales	\$69,068	\$69,065	\$68,864	\$68,589	\$63,636	\$63,404	\$62,676	\$62,067
Cost of sales	40,758	41,274	40,914	41,077	38,231	38,061	37,683	37,414
Operating expenses	8,366	8,177	8,514	7,709	6,628	6,611	6,625	6,451
Operating income	19,944	19,614	19,436	19,803	18,777	18,732	18,368	18,202
Interest expense	958	1,105	1,045	1,085	1,157	1,151	1,171	1,151
Amortization expense	3,888	3,847	3,973	4,134	3,949	4,106	4,188	4,154
Income taxes	–	955	1,873	1,666	1,366	1,186	974	1,069
Net income	\$15,098	\$13,707	\$12,545	\$12,918	\$12,305	\$12,289	\$12,035	\$11,828
Net income per unit	\$0.3981	\$0.3615	\$0.3308	\$0.3407	\$0.3245	\$0.3241	\$0.3174	\$0.3119

Steve Rotz,  
Vice President, Corporate  
Development

“Looking forward, we intend to utilize internal resources combined with external partners to support our evolution.”

Over the last eight quarters, the Business has reported stable and growing revenues. During this period, the Business was not affected by seasonal fluctuations other than the number of business days in a particular quarter, which can cause minor quarter-over-quarter variances. A significant contributor to quarter-over-quarter growth in revenue and cost of sales in the first quarter of 2004 was the commencement of the long-term U.S. cheque supply contract with a subsidiary of a major Canadian financial institution customer.

Operating expenses trended upward over the eight quarters, reflecting, among other items, growing technology costs. Operating income, after the deduction of operating costs, showed modest but consistent growth through the eight quarters of 2004 and 2003.

Income taxes were no longer recorded subsequent to July 25, 2004 with the reorganization of the corporate structure to a trust-on-trust-on-partnership structure from a trust-on-corporation-on-partnership structure.

#### Eight Quarter Consolidated Statement of Distributable Cash

	<i>(in thousands of Canadian dollars, except per unit amounts, unaudited)</i>							
	2004 Q4	2004 Q3	2004 Q2	2004 Q1	2003 Q4	2003 Q3	2003 Q2	2003 Q1
Net income	\$15,098	\$13,707	\$12,545	\$12,918	\$12,305	\$12,289	\$12,035	\$11,828
Add:								
Amortization expense	3,888	3,847	3,973	4,134	3,949	4,106	4,188	4,154
Future income taxes	–	745	1,437	1,363	1,114	933	717	819
Cash flow from operations	18,986	18,299	17,955	18,415	17,368	17,328	16,940	16,801
Less:								
Maintenance capital expenditures:								
Capital and other assets	2,715	1,451	1,317	1,696	1,476	1,202	1,312	1,220
Contract payments	645	625	625	1,250	645	625	625	1,250
Distributable cash	\$15,626	\$16,223	\$16,013	\$15,469	\$15,247	\$15,501	\$15,003	\$14,331
Distributions declared	\$13,530	\$13,287	\$13,287	\$13,151	\$13,083	\$12,889	\$12,888	\$12,708
Distributable cash per unit	\$0.4121	\$0.4278	\$0.4223	\$0.4079	\$0.4021	\$0.4088	\$0.3956	\$0.3779
Distributions declared per unit	\$0.3568	\$0.3504	\$0.3504	\$0.3468	\$0.3450	\$0.3399	\$0.3399	\$0.3351

Cash flow from operations showed consistent growth throughout the eight quarters. Distributable cash per unit increased through the quarters with some variation from quarter to quarter as a result of the timing of maintenance capital expenditures. The capital expenditure program increased year-over-year by \$2.0 million with more than half of the increased asset purchases made during the fourth quarter of 2004.

**Selected Balance Sheet Information**

<i>(in thousands of Canadian dollars, unaudited)</i>	2004	Year ended December 31,	
		2003	2002
Total assets	\$ 430,595	\$ 458,844	\$ 476,405
Total long-term liabilities	\$ 67,603	\$ 71,980	\$ 84,789

Total assets of \$430.6 million at December 31, 2004 decreased by \$28.2 million, or 6.2%, from 2003, primarily as a result of the elimination of the future income tax asset and the continued amortization of intangible assets.

With the reorganization of the corporate structure to a trust-on-trust-on-partnership structure and the consequential replacement of the corporate entity with an intermediary trust, the consolidated entity ceased to record future income taxes. As a result, the previously recorded future income tax asset of \$28.2 million no longer represented an asset to the Business and accordingly was charged directly to deficit. This accounting treatment is in accordance with Canadian Institute of Chartered Accountants ("CICA") guidelines.

Total assets of \$458.8 million at December 31, 2003 decreased by \$17.6 million, or 3.7%, as a result of reduced cash balances upon repayments of debt, the draw down of future tax assets and amortization of intangible assets.

Long-term liabilities decreased by \$4.4 million to \$67.6 million at December 31, 2004, primarily as a result of repayment of term debt totalling \$7.0 million during 2004, partially offset by increases in disbursement obligations under long-term customer contracts.

The increase in disbursement obligations was a result of the renewal of two long-term customer contracts during 2004. Future fixed payment obligations related to these contracts were recorded as disbursement obligations on customer contracts and as other assets. These contracts have been renewed with substantially the same business terms and conditions and, therefore, their extensions are not expected to result in changes to distributable cash generation.

Long-term liabilities of \$72.0 million as at December 31, 2003 decreased \$12.8 million from 2002 as a result of repayments of debt totalling \$13.0 million.

**Cash Flow and Liquidity**

**Consolidated Statement of Cash Flows – Summary**

<i>(in thousands of Canadian dollars, unaudited)</i>	2004	Year ended December 31,	
		2003	2002 <sup>1</sup>
Cash flows from operating activities	\$ 77,271	\$ 68,569	\$ 64,590
Cash flows used for distributions	(53,066)	(51,442)	(47,827)
Cash flows from (used in) other financing activities	(7,000)	(13,000)	204,945
Cash flows used for investing activities	(11,928)	(11,192)	(218,392)
Net change in cash	\$ 5,277	\$ (7,065)	\$ 3,316

<sup>1</sup>The year ended December 31, 2002 was compiled from audited financial statements adjusted to remove the 12-day period ended December 31, 2001.

### Cash Flows from Operating Activities

During 2004, the Business generated \$77.3 million in cash flow from operating activities, including \$2.8 million and \$0.8 million from non-cash working capital balances and changes in other long-term liabilities, respectively. The reduction in non-cash working capital relates primarily to temporary increases in short-term liabilities, which are expected to reverse in 2005.

Increase in cash flows from operating activities of \$4.0 million from 2002 to 2003 is consistent with the increase in net income before non-controlling interest, future income taxes and amortization.

### Cash Flows Used for Distributions

Monthly distributions are declared by the Fund for unitholders of record on the last business day of each month and are paid within 31 days following each month end. Distributions paid during 2004 include distributions declared for the month of December 2003, but do not include amounts declared for December 2004 as this amount will not be paid until January 31, 2005.

The Fund paid distributions of \$53.1 million during 2004 compared to \$51.4 million for the prior year. On a per unit basis, distributions paid in 2004 were \$1.40, an increase of 3.2% over 2003.

During 2004, the Fund announced increases in distributions in both March and November. Distributions to unitholders of record on March 31, 2004 were increased from \$0.1150 per unit (equivalent to \$1.38 per annum) to \$0.1168 per unit (equivalent to \$1.40 per annum). The November distribution payable to unitholders of record on November 30, 2004 was increased from \$0.1168 per unit to \$0.1200 (equivalent to \$1.44 per annum).

In 2003, distributions were increased for unitholders of record on April 30, 2003 and October 31, 2003 from \$0.1117 per unit (equivalent to \$1.34 per annum) to \$0.1133 per unit (equivalent to \$1.36 per annum), then to \$0.1150 per unit (equivalent to \$1.38 per annum).

The tax allocation of distributions declared for 2004 is 15.0% dividend income, 75.2% interest income, and 9.8% return of capital. The 2003 tax allocation was 19.5% dividend income, 69.5% interest income, and 11.0% return of capital.

The Fund may issue an unlimited number of trust units. Each trust unit is transferable and represents an equal, undivided beneficial interest in any distribution from the Fund and the net assets of the Fund. All units are of the same class with equal rights and privileges and are not subject to future calls or assessments. Each unit entitles the holder to one vote at all meetings of unitholders.

As at December 31, 2004 and February 28, 2005, 37,920,792 trust units were outstanding. This total amount has remained unchanged since April 2, 2002.

### Cash Flows Used in Other Financing Activities

Cash flows used in other financing activities in both 2004 and 2003 relate to the reduction of the Business' long-term indebtedness.

### Cash Flows Used in Investing Activities

#### Expenditures on Capital and Other Assets

<i>(in thousands of Canadian dollars, unaudited)</i>	Year ended December 31,		
	2004	2003	2002
Maintenance capital			
Machinery and equipment	\$ 399	\$ 734	\$ 281
Computer and software	5,903	4,391	4,728
Furniture, fixtures and leasehold improvements	877	85	47
Total maintenance capital	\$ 7,179	\$ 5,210	\$ 5,056
Contract payments, maintenance	3,145	3,145	3,145
Total maintenance expenditures	\$ 10,324	\$ 8,355	\$ 8,201
Non-maintenance capital			
U.S. services development	\$ –	\$ 389	\$ 897
Production efficiency initiatives	–	1,736	1,350
Other new services	356	12	381
Total non-maintenance capital	\$ 356	\$ 2,137	\$ 2,628
Contract payments, non-maintenance	1,250	700	1,850
Total non-maintenance expenditures	\$ 1,606	\$ 2,837	\$ 4,478
Total capital investments	\$ 11,930	\$ 11,192	\$ 12,679

The table above sets out capital expenditures, which include both capital assets and payments under customer contracts. The Fund has various payment obligations under customer contracts. Certain long-term customer contracts provide for fixed contract or program initiation payments to be made and these are treated as non-maintenance capital as they are not regularly recurring disbursements. Other fixed customer contract payments are made annually over the life of the contract and therefore are treated as recurring maintenance capital. The aggregate of all contract payments, both fixed and variable, recognizes, among other things, the high degree of integration and sharing between Davis + Henderson and the financial institutions of the many activities related to ordering, data handling, customer service and other activities undertaken by financial institutions related to the operation of the cheque supply and other programs.

The Fund's capital program provides for continued annual maintenance expenditures to be funded by the cash flows from operations. These expenditures are generally directed toward direct ordering technology, the implementation of new programs within the cheque supply business and the maintenance and upgrading of the Business' technology infrastructure.

Maintenance expenditures in 2004 of \$7.2 million increased \$2.0 million over the prior year's expenditures. This increase was primarily related to investments in telephony, related call centre infrastructure and the updating and upgrading of the existing technology infrastructure.

Non-maintenance expenditures support the development of new programs and services, major production efficiency initiatives and certain contract payments.

### **Cash Balances and Long-term Indebtedness**

At December 31, 2004, cash and cash equivalents totalled \$10.3 million, compared to \$5.0 million at December 31, 2003.

At December 31, 2004, the Business continued to have access to \$98.0 million of term credit facilities due June 30, 2006, which consisted of a \$60.0 million non-revolving term loan and a \$38.0 million revolving credit facility. As of December 31, 2004, the Business had drawn \$60.0 million under the non-revolving term loan. The Business was permitted to draw on the revolving credit facility's available balance of \$38.0 million to fund capital expenditures or for other general corporate purposes.

On January 24, 2005, the Business amended the terms of its term credit facilities and extended the maturity dates to January 24, 2009. The total of the facilities was reduced to \$90.0 million, and includes a \$50.0 million non-revolving term loan and a \$40.0 million revolving term credit facility.

Immediately following the extension and amendment of the facilities on January 24, 2005, the Business made a voluntary payment of \$3.0 million. Subsequent to this payment, the total long-term indebtedness of the Business was \$57.0 million consisting of \$50.0 million drawn under the non-revolving term loan and \$7.0 million drawn under the revolving term facility.

As of December 31, 2004, the Business had fixed interest rates on \$40.0 million of its outstanding debt at rates of between 5.89% and 7.33% for swap terms ending between March 27, 2006 and June 30, 2008. The average effective interest rate applicable to the Fund's total indebtedness was 5.89% as at December 31, 2004. Subsequent to December 31, 2004, the Business entered into an additional interest-rate swap for a notional amount of \$10.0 million with a term ending January 4, 2009. With the additional swap and the amended credit facilities, the Business has fixed interest rates on 87.7% of its outstanding debt as at February 28, 2005, with interest rates ranging between 5.13% and 6.83% with swap terms ending between March 27, 2006 and January 4, 2009.

Cash flows from operations together with cash balances on hand and unutilized term credit facilities are expected to be sufficient to fund the Business' operating requirements, capital expenditures, contractual obligations and anticipated distributions.

### Contractual Obligations – Payments Due by Period

Contractual obligations of the Business as at December 31, 2004 and the timing of the expected payments are as follows:

<i>(in thousands of Canadian dollars, unaudited)</i>	Total	Less than 1 year	1–3 years	4–5 years	After 5 years
Long-term indebtedness <sup>1</sup>	\$60,000	\$ –	\$ –	\$60,000	\$ –
Disbursement obligations on customer contracts	9,180	3,745	4,040	1,395	–
Operating leases	13,850	2,719	4,511	3,629	2,991
Employee future benefits	1,402	126	281	294	701
Obligations relating to a deferred compensation program	766	–	766	–	–
	<b>\$85,198</b>	<b>\$6,590</b>	<b>\$9,598</b>	<b>\$65,318</b>	<b>\$3,692</b>

<sup>1</sup>The timing of the expected payment on long-term indebtedness reflects the extension of the maturity date on the Business' credit facility to January 24, 2009 subsequent to year end.

### Operating Results for the Fourth Quarter

#### Consolidated Statement of Income

<i>(in thousands of Canadian dollars, except per unit amounts, unaudited)</i>	Quarter ended December 31,	
	2004	2003
Sales	\$69,068	\$63,636
Cost of sales	40,758	38,231
Gross profit	28,310	25,405
	41.0%	39.9%
Operating expenses	8,366	6,628
	12.1%	10.4%
Operating income	19,944	18,777
	28.9%	29.5%
Interest expense	958	1,157
Amortization expense	3,888	3,949
Income taxes	–	1,366
Net income	\$15,098	\$12,305
Net income per unit, basic and diluted	\$0.3981	\$0.3245

For the fourth quarter of 2004, sales increased \$5.4 million, or 8.5%, when compared to the same quarter in the prior year. Factors contributing to the change between the two quarters are the same as those for the full year and include additional revenue from the U.S.-sourced business, higher order values and increased revenues from complementary programs.

Gross profit for the fourth quarter of 2004 of \$28.3 million increased \$2.9 million, or 11.4%, when compared to the gross profit of \$25.4 million for the fourth quarter of 2003. Gross profit as a percentage of sales increased from 39.9% in the fourth quarter of 2003 to 41.0% in the fourth quarter of 2004 as a result of higher operating efficiency partially offset by lower margins earned on U.S.-sourced business.

Operating expenses in the fourth quarter of 2004 were \$8.4 million, an increase of \$1.7 million over the comparable period in the prior year. This increase is related to increased spending on technology in support of the web-based and call centre ordering channels and increased technology expenditures related to technology infrastructure upgrade initiatives. As well, variable compensation, based on the financial performance of the Business, increased year-over-year.

Operating income of \$19.9 million increased \$1.2 million, or 6.2%, over the same period last year.

Net interest expense of \$1.0 million for the fourth quarter of 2004 was \$0.2 million less than that reported for the same quarter in the prior year as a result of lower indebtedness.

In the fourth quarter of 2004, amortization expense decreased by \$0.1 million compared with the prior year as certain balances became fully amortized.

There was no income tax provision recorded in the fourth quarter of 2004, as a result of the reorganization of the corporate structure, as previously discussed.

Net income of \$15.1 million for the quarter ended December 31, 2004, increased \$2.8 million, as compared with the same quarter in the previous year.

#### Consolidated Statement of Distributable Cash

<i>(in thousands of Canadian dollars, except per unit amounts, unaudited)</i>	Quarter ended December 31,	
	2004	2003
Net income	\$ 15,098	\$ 12,305
Add:		
Amortization	3,888	3,949
Future income taxes	–	1,114
	<u>18,986</u>	<u>17,368</u>
Less:		
Maintenance capital expenditures		
Capital and other assets	2,715	1,476
Contract payments	645	645
Distributable cash	<u>\$ 15,626</u>	<u>\$ 15,247</u>
Net income per unit	<u>\$ 0.3981</u>	<u>\$ 0.3245</u>
Distributable cash per unit	<u>\$ 0.4121</u>	<u>\$ 0.4021</u>
Distributions per unit	<u>\$ 0.3568</u>	<u>\$ 0.3450</u>

Distributable cash of \$15.6 million for the fourth quarter, or \$0.4121 per unit, increased 2.5% over the same period last year. The Business invested \$1.2 million more on maintenance capital in the fourth quarter of 2004 compared to the same period in 2003. While capital expenditures can vary from period to period, the Business is currently directing additional capital in support of direct ordering and technology infrastructure upgrade initiatives.

In November 2004, the Fund announced an increase in its monthly distribution from \$0.1168 per unit (equivalent to \$1.40 per annum) to \$0.1200 per unit (equivalent to \$1.44 per annum) effective for unitholders of record on November 30, 2004. During the fourth quarter of 2004, the Fund declared distributions of \$13.5 million compared to \$13.1 million for the same period in the prior year, an increase of 3.4%.

**Consolidated Statement of Cash Flows – Summary**

<i>(in thousands of Canadian dollars, unaudited)</i>	Quarter ended December 31,	
	2004	2003
Cash flows from operating activities	\$ 19,427	\$ 17,321
Cash flows used for distributions	(13,409)	(13,018)
Cash flows used in other financing activities	(3,000)	(5,000)
Cash flows used in investing activities	(4,407)	(2,591)
Net change in cash	\$ (1,389)	\$ (3,288)

Cash flow from operating activities increased to \$19.4 million in the fourth quarter of 2004, up \$2.1 million over the same quarter in 2003, as a result of increased operating income, lower cash taxes and lower interest expense.

Cash flows used in other financing activities in both quarters relate to the paydown of the Business' long-term indebtedness.

The Business recorded higher capital expenditures in the fourth quarter of 2004 compared with 2003, as a result of increased expenditures related to direct ordering initiatives and technology infrastructure upgrade initiatives.

**Corporate Structure Changes**

On July 23, 2004, unitholders approved an internal reorganization to replace the Fund's subsidiary, D + H Holdings Corp., which owned the Fund's operating business (represented by 100% ownership of the partnership units of Davis + Henderson L.P.), with a newly created trust, D + H Holdings Trust. On July 26, 2004, the reorganization was completed with the Fund retaining the same indirect interest in the assets of Davis + Henderson L.P. as it had prior to the reorganization. The effect of the reorganization is to allow the Fund to operate in a more tax-efficient manner consistent with a structure that has now become common industry practice for most new income funds.

As a result of the reorganization, the new corporate structure is no longer subject to corporate income taxes and federal and provincial capital taxes. Furthermore, as long as all taxable income generated by the organization is paid to unitholders, and therefore taxed in the hands of the unitholders, it is not anticipated that the entities will pay income taxes. Accordingly, there are no provisions for income taxes under this new structure. As a result, the previously recorded future income tax asset of \$28.2 million no longer represented an asset to the Business and accordingly was charged directly to deficit. This accounting treatment is in accordance with CICA guidelines.

## Accounting Estimates

A long-term incentive plan for management was implemented on January 1, 2004, which, subject to the performance criteria and vesting terms, would be paid shortly after December 31, 2006. For 2004, a pro-rated portion of the estimated ultimate obligation, assuming key goals and objectives are met, was recognized in operating expenses. A key assumption in making this estimate was the use of the Fund's market unit price at the balance sheet date. For a full description of this plan, please see the Fund's most recent Management Information Circular, available on SEDAR at [www.sedar.com](http://www.sedar.com).

## Changes in Accounting Policy

The Business reviews all revisions to the CICA Handbook when issued. All revisions are considered and applied by the effective date or earlier if practical.

The following is a discussion of relevant Handbook revisions that were released or became effective during the year ended December 31, 2004:

Handbook Section 3461, Employee Future Benefits, was amended to expand the disclosure requirements for employee future benefits. Relevant new disclosure requirements include disclosure of the date used to measure the benefit obligations; effective date of the last and next required actuarial valuation; balance sheet classification; disclosure of the discount rate used to determine the net benefit cost and the accrued benefit obligation; and the effects of a one-percentage-point increase and decrease in the assumed health care cost trend rates. The amended disclosure requirements are effective for fiscal years ending on or after June 30, 2004.

Obligations under the Business' non-pension post-retirement benefit plan were actuarially calculated for December 31, 2004 and disclosure requirements consistent with the amended section have been included in the notes to the financial statements for the year ended December 31, 2004.

## Business Risk

The following describes certain risks, events and uncertainties that could cause the reported financial information to not necessarily be indicative of future operating results. For a more comprehensive discussion of these and other risks, refer to the Fund's most recently filed Annual Information Form and Management Information Circular available on SEDAR at [www.sedar.com](http://www.sedar.com).

### Reliance on Contracts with Financial Institution Customers

The Business is dependent upon certain significant financial institutions in providing services for their account holders. Services and products provided to the Business' six major financial institution customers accounted for approximately 79% of the Business' 2004 revenue.

The contracts with financial institution customers are typically for terms ranging from three to five years. There can be no assurance that those contracts will be renewed. There could be material adverse effects on the Business if it fails to renew its contracts with the financial institutions, if the financial institutions are acquired by foreign businesses that already have established relationships with cheque suppliers or if a financial institution decides to perform its cheque supply functions in-house.

Further, there is no assurance that any new agreement entered into by the Business will have terms similar to those contained in current arrangements with financial institution customers and the failure to obtain those terms could have a material adverse effect on the Business' financial condition and results of operations.

During fiscal 2004, the Business renewed two contracts on financial terms similar to those in the previously existing contracts.

Consolidation in the financial institution industry could affect revenues from cheque supply outsourcing programs. Margins on cheque orders obtained through financial institutions could be pressured as those financial institutions seek their own merger synergies. Typically, upon the merger of branches and systems in a bank combination, the Business has historically assisted the merging financial institutions by supplying replacement cheque products as well as additional services as part of a conversion program.

### Competition from Substitute Products

Banking and related industries have introduced alternatives to paper-based payment products including automated teller machines, pre-authorized debits, credit cards, debit cards, and electronic payment systems, such as telephone and web-based payment systems. Additional forms of alternative payment methods, including e-commerce and software programs, are being developed continually and may also compete with the products and

services offered by the Business. Use of these payment alternatives as a replacement for cheques negatively affects the number of cheques written and can affect the number of cheque package reorders that the Business receives.

Approximately 49% of the Business' revenues are related to reorders and are, therefore, affected by cheque usage. The balance of the Business' revenues is derived from either new orders or other products unaffected by cheque usage. Approximately 25% of the Business' revenues are related to reorders for cheques on personal chequing accounts and 24% of revenues are for business cheque reorders on current accounts. Management believes that the adoption of alternative payment methods has primarily affected personal cheque reorders and business cheque reorders to a less significant degree. Management also believes that this occurs as businesses prefer utilizing cheques for managing, controlling and tracking cash flow, whereas individuals often choose payment alternatives based upon convenience. A mitigating trend affecting the number of reorders the Business receives from individuals has been the migration to order quantities which have a fewer number of cheques in a package. While reduced cheque usage lengthens the reorder cycle, migration to cheque packages containing fewer cheques shortens the reorder cycle.

If the Business' revenue related to personal and business cheque reorders decreased by 1%, this would result in a revenue decline of approximately \$1.4 million.

### **Competition from Competitors Supplying Similar Products and Services**

Some of the Business' competitors (particularly those in the United States) have economic resources greater than those of the Business and are well-established suppliers.

The Business looks to continually strengthen its leading position in the market segments in which it competes by increasing the value it delivers to its customers. The Business has enhanced and continues to enhance the value of its products, the efficiency of its interactive processes with its customers and its development of new programs.

### **Development of Products and Services Options**

The Business' ability to continue to generate comparable net income and cash flow is based, in part, on the addition of new products and services, which could be sold to existing financial institution customers of the Business. It seeks to add new products and services by leveraging its core capabilities, including electronic order processing, data management, customer contact service and fulfillment capabilities. The failure to develop and successfully market new products and services at favourable margins could have an adverse impact on the Business' future prospects.

The Business is bound by a non-competition agreement under which it cannot compete in certain non-cheque related businesses operated by the previous owner of the Davis + Henderson business for a period ending on April 2, 2007. This may limit the ability of the Business to introduce new products or services in those applicable areas.

### **Leverage**

The Business has debt service obligations under its credit facilities that mature and are fully repayable on January 24, 2009 subject to compliance with covenants as outlined in the debt agreement. As at February 28, 2005, the Business had drawn \$57.0 million of its term facility and is permitted to draw an additional \$33.0 million available for general corporate purposes.

If the amounts become repayable due to an inability to comply with covenants, or if the Business is unable to extend the terms of the facilities at time of renewal, the loss of the credit facilities would have an adverse impact on the continuing operations of the Business.

The Business continuously re-examines its financing strategy with the intent of reducing refinancing risk. With respect to interest rate risk, as discussed in more detail in Note 7 to the financial statements, the Business has hedged, at December 31, 2004, with interest-rate swaps, 67% of the total debt currently outstanding for terms ending between March 27, 2006 and June 30, 2008.

### **Financial Instruments**

The main risks to the Business associated with interest-rate swaps are counterparty (credit) risk and early termination risk. The Business mitigates counterparty risk by conducting swaps only with highly rated financial institutions. Should the Business reduce its indebtedness that the swaps relate to, the Business would likely choose also to reduce the relevant swap amounts at such time. To the extent that market interest rates applicable to the remaining term of such swaps are lower than the fixed rate agreed to in the swap, the Business would incur a break cost to do so. The aggregate value of such unrealized loss as at December 31, 2004 was \$0.9 million. Under the Business' accounting policies, the relevant portion of such unrealized loss would be recognized within interest expense upon early termination or reduction of the swap amount. Upon maturity of the swaps, or in the event that the Business increases its outstanding indebtedness, the Business would be exposed to the risk that higher interest rates may exist at such time.

### **Foreign Exchange Exposure**

Revenues and expenses of the business are primarily contracted in Canadian dollars. In January 2004, the Business began to provide its cheque supply program to the U.S. subsidiary of a Canadian financial institution customer. This long-term supply contract is priced in U.S. dollars. Most of the costs incurred to deliver these programs are also contracted in U.S. dollars. The net profit of this business will be subject to exchange rate fluctuations, but such fluctuations are not expected to be material to the reported results.

### **Reliance on Outsourcing Arrangements**

In some areas of its operations, the Business relies on third parties to supply production, fulfillment, or other services. Examples of such services by third parties include contracts with service providers for Canadian postal services and for production and fulfillment of the Business' U.S. cheque supply program. The Business has committed to delivery of products and services to its customers and may be exposed to claims from customers if the Business' outsource providers fail to perform under their contractual obligations for any reason or if continued outsourcing arrangements are not secured. Current profit margins reflect these contractual arrangements; therefore if the Business was required to find an alternative outsourcing arrangement, margins and cash flows could be negatively impacted.

### **Cash Distributions Are Not Guaranteed and Will Fluctuate with Davis + Henderson L.P.'s Performance**

Although the Fund intends to distribute the interest and distributions received by the Fund on the units and notes of Holdings Trust 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 Davis + Henderson L.P. and paid, indirectly, to the Fund. The actual amount distributed in respect of the Fund units will depend upon numerous factors associated with Davis + Henderson L.P., including its profitability, fluctuations in its working capital, the sustainability of its margins, interest expenses and its requirements for repayment of indebtedness and incurrence of capital expenditures. The market value of the units may deteriorate significantly if the Fund is unable to continue to distribute cash to unitholders at current distribution levels.

### **Nature of Units**

Unitholders own an equal undivided interest in the Fund. The units do not and will not represent a direct investment in the Business. As holders of Fund units, unitholders do 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. The units represent a fractional interest in the Fund. The Fund's primary assets will be notes and units of D + H Holdings Trust. D + H Holdings Trust, in turn, is a limited partner in Davis + Henderson L.P. The price per unit is, in part, a function of anticipated distributable income, distributions, as well as the consolidated indebtedness, net of cash and cash equivalents of the Fund including the net indebtedness of Davis + Henderson L.P. The price per unit may also be a function of interest rates or expected returns available, or perceived to be available, on alternative investments and, for example, it is believed by some investment professionals that, if market interest rates increase, the Fund's unit price would likely decline.

## Outlook

For the year ended December 31, 2004, the percentage of year-over-year revenue growth has benefited from the inclusion of revenues from the U.S. cheque supply program, which was launched January 1, 2004. This allowed the Business to exceed, in fiscal 2004, its long-term annual revenue growth objective of 3% to 5%. The contribution margin from the U.S. business is less than the average margin for the balance of Davis + Henderson's business and, as such, has had only a modest impact on cash flow. The Fund's long-range objective for 2005 and future periods remains unchanged. The Fund will continue to target annual sales growth of 3% to 5%, while maintaining operating margins, with the overall objective to modestly grow distributions.

As set out in the Fund's statement of strategy, the objective is to grow profits by enhancing the value of our cheque supply program, by expanding into new programs to serve the chequing account and by pursuing additional opportunities related to other key transactional accounts of our financial institution customers.

The Business' operational plans include many initiatives which, when combined, are intended to allow the Fund to meet its objectives. Meeting its growth objective is not dependent on any one of the initiatives as most of the new programs and services are individually not large. Examples of such programs include rolling out *eSwitch*<sup>TM</sup> services to additional national customers and delivering other account opening services and products for chequing and lending accounts. Additionally, the continued increase in the adoption rate of *ChequeCentral* and *ChequeAdvisor* programs is expected to increase average value per order. Growth in the U.S. over the next few years is expected to come solely from the Business' existing cheque supply contract.

Looking forward, operating expenses are expected to show modest growth over 2004 levels.

The Business' capital program provides for continued annual maintenance expenditures to be funded by cash flows from operations. The annual cost is expected to increase in line with the growth in business, which is expected to be directed primarily towards its call centre activities, the implementation of new programs within the cheque supply business and the maintenance and replacement of its technology infrastructure. Currently, the 2005 capital program for maintenance expenditures is expected to be slightly higher than the 2004 capital program.

Certain information included in this report is forward looking and based upon assumptions and anticipated results that are subject to risks and uncertainties associated with Davis + Henderson's business and the economic environment in which the Business operates. Should one or more of these uncertainties materialize or should the underlying assumptions prove incorrect, actual results may vary significantly from those expected. Risks and uncertainties are discussed above, as well as in greater detail in the Fund's most recently filed Annual Information Form and Management Information Circular, each of which are available on SEDAR at [www.sedar.com](http://www.sedar.com).

#### **Additional Information**

Additional information relating to the Fund, including the Fund's most recently filed Annual Information Form, is available on SEDAR at [www.sedar.com](http://www.sedar.com).

February 28, 2005

## SUPPLEMENTARY FINANCIAL INFORMATION

### Operating Results by Period<sup>1,2</sup>

<i>(in thousands of Canadian dollars, except per unit amounts, unaudited)</i>	Year ended December 31, 2004	Three months ended December 31, 2004	Three months ended September 30, 2004	Three months ended June 30, 2004	Three months ended March 31, 2004
Sales	\$ 275,586	\$ 69,068	\$ 69,065	\$ 68,864	\$ 68,589
Cost of sales <sup>1</sup>	164,023	40,758	41,274	40,914	41,077
Operating expenses <sup>1</sup>	32,766	8,366	8,177	8,514	7,709
Operating income	78,797	19,944	19,614	19,436	19,803
Interest expense	4,193	958	1,105	1,045	1,085
Amortization and income taxes	20,336	3,888	4,802	5,846	5,800
Net income	54,268	15,098	13,707	12,545	12,918
Add:					
Amortization expense	15,842	3,888	3,847	3,973	4,134
Future income taxes	3,545	–	745	1,437	1,363
Cash flow from operations	73,655	18,986	18,299	17,955	18,415
Less: Maintenance capital expenditures:					
Capital and other assets	7,179	2,715	1,451	1,317	1,696
Contract payments	3,145	645	625	625	1,250
Distributable cash <sup>2</sup>	\$ 63,331	\$ 15,626	\$ 16,223	\$ 16,013	\$ 15,469
Distributions declared	\$ 53,256	\$ 13,530	\$ 13,287	\$ 13,287	\$ 13,151
Net income per unit	\$ 1.4311	\$ 0.3981	\$ 0.3615	\$ 0.3308	\$ 0.3407
Cash flow from operations per unit	\$ 1.9423	\$ 0.5007	\$ 0.4826	\$ 0.4735	\$ 0.4856
Distributable cash per unit	\$ 1.6701	\$ 0.4121	\$ 0.4278	\$ 0.4223	\$ 0.4079
Distributions declared per unit	\$ 1.4044	\$ 0.3568	\$ 0.3504	\$ 0.3504	\$ 0.3468

<sup>1</sup> Certain comparative figures have been reclassified to conform to the current period's presentation.

<sup>2</sup> Distributable cash is not a defined term under Canadian generally accepted accounting principles but is determined by the Fund as net income for the period adjusted to remove non-cash expenses, including amortization and future income taxes, and reduced by maintenance capital expenditures. Non-maintenance capital expenditures are not recorded as a reduction from distributable cash as these expenditures are considered non-recurring expenditures which are intended to generate future growth in distributable cash and distributions. Management believes that this earnings measure is a useful supplemental measure of performance as it provides investors with an indication of the amount of cash available for distribution to unitholders. Investors are cautioned, however, that distributable cash should not be construed as an alternative to using net earnings as a measure of profitability or as an alternative to the statement of cash flows. Further, the Fund's method of calculating distributable cash may not be comparable to similarly titled amounts reported by other issuers.

### Condensed Balance Sheet<sup>1</sup>

<i>(in thousands of Canadian dollars, unaudited)</i>	December 31, 2004	September 30, 2004	June 30, 2004	March 31, 2004
Cash and cash equivalents	\$ 10,258	\$ 11,647	\$ 7,357	\$ 7,152
Other current assets	15,352	15,744	16,672	15,898
Future income taxes	–	28,170	28,915	30,352
Capital and other assets	36,345	36,888	32,643	34,589
Goodwill and other intangible assets	368,640	369,223	369,806	370,389
	\$ 430,595	\$ 461,672	\$ 455,393	\$ 458,380
Payables and other current liabilities <sup>1</sup>	\$ 34,422	\$ 35,632	\$ 33,473	\$ 31,235
Other long-term liabilities <sup>1</sup>	7,603	7,867	4,167	4,650
Long-term indebtedness	60,000	63,000	63,000	67,000
Unitholders' equity	328,570	355,173	354,753	355,495
	\$ 430,595	\$ 461,672	\$ 455,393	\$ 458,380

<sup>1</sup> Certain comparative figures have been reclassified to conform to the current period's presentation.

Year ended December 31, 2003	Three months ended December 31, 2003	Three months ended September 30, 2003	Three months ended June 30, 2003	Three months ended March 31, 2003	Year ended December 31, 2002 <sup>3</sup>	Three months ended December 31, 2002	Three months ended September 30, 2002	Three months ended June 30, 2002	Three months ended March 31, 2002 (pro forma) <sup>4</sup>
\$ 251,783	\$ 63,636	\$ 63,404	\$ 62,676	\$ 62,067	\$ 228,259	\$ 58,938	\$ 56,770	\$ 56,689	\$ 55,862
151,389	38,231	38,061	37,683	37,414	133,835	34,531	32,808	33,002	33,494
26,315	6,628	6,611	6,625	6,451	24,452	6,517	6,085	6,152	5,698
74,079	18,777	18,732	18,368	18,202	69,972	17,890	17,877	17,535	16,670
4,630	1,157	1,151	1,171	1,151	4,527	1,138	1,183	1,212	994
20,992	5,315	5,292	5,162	5,223	19,934	5,510	5,054	4,737	4,633
48,457	12,305	12,289	12,035	11,828	45,511	11,242	11,640	11,586	11,043
16,397	3,949	4,106	4,188	4,154	16,620	4,426	4,186	4,047	3,961
3,583	1,114	933	717	819	2,305	831	616	437	421
68,437	17,368	17,328	16,940	16,801	64,436	16,499	16,442	16,070	15,425
5,210	1,476	1,202	1,312	1,220	5,006	1,245	1,683	1,590	488
3,145	645	625	625	1,250	3,145	645	625	625	1,250
\$ 60,082	\$ 15,247	\$ 15,501	\$ 15,003	\$ 14,331	\$ 56,285	\$ 14,609	\$ 14,134	\$ 13,855	\$ 13,687
\$ 51,568	\$ 13,083	\$ 12,889	\$ 12,888	\$ 12,708	\$ 50,055	\$ 12,707	\$ 12,707	\$ 12,320	\$ 12,320
\$ 1.2778	\$ 0.3245	\$ 0.3241	\$ 0.3174	\$ 0.3119	\$ 1.2002	\$ 0.2965	\$ 0.3070	\$ 0.3055	\$ 0.2912
\$ 1.8047	\$ 0.4579	\$ 0.4570	\$ 0.4467	\$ 0.4431	\$ 1.6992	\$ 0.4351	\$ 0.4336	\$ 0.4238	\$ 0.4068
\$ 1.5844	\$ 0.4021	\$ 0.4088	\$ 0.3956	\$ 0.3779	\$ 1.4843	\$ 0.3853	\$ 0.3727	\$ 0.3654	\$ 0.3609
\$ 1.3599	\$ 0.3450	\$ 0.3399	\$ 0.3399	\$ 0.3351	\$ 1.3200	\$ 0.3351	\$ 0.3351	\$ 0.3249	\$ 0.3249

<sup>3</sup> The year ended December 31, 2002 was compiled from audited financial statements adjusted to remove the 12-day period ended December 31, 2001.

<sup>4</sup> The above information sets forth unaudited quarterly information and has been prepared on a pro forma basis as if the Davis + Henderson business was 100% owned by Davis + Henderson Income Fund since December 20, 2001 (as compared to 45.4% and 49.9% ownership for the periods ending December 31, 2001, and March 31, 2002, respectively). The pro forma balances presented for the twelve-day period ending December 31, 2001 and for the three-month period ending March 31, 2002 are based on the actual statements of the Fund adjusted to remove the expense related to distributions paid to the non-controlling owner and to increase the number of units outstanding to 37,920,792 as at December 20, 2001 (versus the 17,235,000 units outstanding from December 20, 2001 to January 9, 2002; 18,955,000 units outstanding from January 10, 2002 to April 1, 2002; and 37,920,792 units outstanding subsequent to April 1, 2002).

December 31, 2003	September 30, 2003	June 30, 2003	March 31, 2003	December 31, 2002	September 30, 2002	June 30, 2002	March 31, 2002
\$ 4,981	\$ 8,269	\$ 14,573	\$ 11,255	\$ 12,046	\$ 11,876	\$ 11,203	\$ 8,429
15,779	17,187	16,000	16,531	16,142	15,775	14,749	17,256
31,715	32,829	33,762	34,479	35,298	36,129	36,745	37,182
35,396	36,916	38,074	37,605	39,614	41,196	42,981	43,853
370,973	371,556	372,139	372,722	373,305	373,889	374,472	185,911
\$ 458,844	\$ 466,757	\$ 474,548	\$ 472,592	\$ 476,405	\$ 478,865	\$ 480,150	\$ 292,631
\$ 31,136	\$ 32,652	\$ 31,223	\$ 30,311	\$ 32,778	\$ 34,407	\$ 33,374	\$ 33,845
4,980	5,599	6,220	4,323	4,789	4,154	5,404	5,413
67,000	72,000	80,000	80,000	80,000	80,000	80,000	80,000
355,728	356,506	357,105	357,958	358,838	360,304	361,372	173,373
\$ 458,844	\$ 466,757	\$ 474,548	\$ 472,592	\$ 476,405	\$ 478,865	\$ 480,150	\$ 292,631

SUPPLEMENTARY FINANCIAL INFORMATION (continued)

**Distribution History**

Month	Distributions <sup>1</sup> per unit			
	2004	2003	2002	2001
January	\$ 0.1150	\$ 0.1117	\$ 0.1083	\$ –
February	0.1150	0.1117	0.1083	–
March	0.1168	0.1117	0.1083	–
April	0.1168	0.1133	0.1083	–
May	0.1168	0.1133	0.1083	–
June	0.1168	0.1133	0.1083	–
July	0.1168	0.1133	0.1117	–
August	0.1168	0.1133	0.1117	–
September	0.1168	0.1133	0.1117	–
October	0.1168	0.1150	0.1117	–
November	0.1200	0.1150	0.1117	–
December <sup>2</sup>	0.1200	0.1150	0.1117	0.0427
	<b>\$ 1.4044</b>	<b>\$ 1.3599</b>	<b>\$ 1.3200</b>	<b>\$ 0.0427</b>

<sup>1</sup>Monthly distributions are made to unitholders of record on the last business day of each month and are paid within 31 days following each month end.

<sup>2</sup>Distribution paid in 2001 is in respect of the 12 calendar days from December 20, 2001 to December 31, 2001.

**Tax Allocation of Distributions**

	2004		2003	
	Amount	Per unit	Amount	Per unit
Dividend income	\$ 8,003	\$ 0.2110	\$ 10,037	\$ 0.2647
Interest income	40,040	1.0559	35,828	0.9448
Return of capital	5,213	0.1375	5,702	0.1504
Total distributions for the period	\$ 53,256	\$ 1.4044	\$ 51,567	\$ 1.3599

As a result of the recent reorganization to a trust-on-trust-on-partnership structure, the 2005 distributions will not have a dividend component.

**Other Statistics**

Quarter ended (in thousands of Canadian dollars, except per unit amounts)	Trading price range of units (TSX: "DHFUN")			Average daily volume	Number of units outstanding at period end	Market capitalization at quarter end
	High	Low	Close			
2004 Q4	\$ 23.25	\$ 18.80	\$ 22.70	81	37,921	\$ 860,802
Q3	\$ 19.62	\$ 16.75	\$ 19.45	58	37,921	\$ 737,559
Q2	\$ 19.34	\$ 15.05	\$ 18.00	93	37,921	\$ 682,574
Q1	\$ 19.40	\$ 16.71	\$ 19.40	92	37,921	\$ 735,663
2003 Q4	\$ 17.50	\$ 15.10	\$ 17.45	67	37,921	\$ 661,718
Q3	\$ 15.65	\$ 14.52	\$ 15.30	99	37,921	\$ 580,188
Q2	\$ 15.20	\$ 12.91	\$ 15.00	82	37,921	\$ 568,812
Q1	\$ 13.69	\$ 12.48	\$ 12.94	92	37,921	\$ 490,695
2002 Q4	\$ 13.25	\$ 11.22	\$ 12.86	139	37,921	\$ 487,661
Q3	\$ 12.13	\$ 10.45	\$ 12.10	165	37,921	\$ 458,842
Q2	\$ 11.25	\$ 10.00	\$ 10.95	176	37,921	\$ 415,233
Q1	\$ 11.20	\$ 10.11	\$ 10.51	149	18,955	\$ 199,217

## FINANCIAL REPORTING RESPONSIBILITY OF MANAGEMENT

The accompanying consolidated financial statements for Davis + Henderson Income Fund (the “Fund”) have been prepared by management of Davis + Henderson, Limited Partnership (“Davis + Henderson L.P.”) and approved by the Board of Directors of Davis + Henderson G.P. Inc. (the “General Partner”) and by the Trustees of the Fund. Management is responsible for the preparation and presentation of these financial statements and all the financial information contained within this Annual Report within reasonable limits of materiality. The Fund’s consolidated financial statements have been prepared in accordance with generally accepted accounting principles in Canada. In the preparation of these statements, estimates are sometimes necessary because a precise determination of certain assets and liabilities is dependent on future events. Management believes such estimates have been based on careful judgments and have been properly reflected in the accompanying consolidated financial statements. The financial information throughout the text of this annual report is consistent with that in the financial statements.

To assist management in discharging these responsibilities, Davis + Henderson L.P. maintains a system of internal controls which are designed to provide reasonable assurance that the Fund’s consolidated assets are safeguarded, that transactions are executed in accordance with management’s authorization and that the financial records form a reliable base for the preparation of accurate and timely financial information.

Management recognizes its responsibilities for conducting the Davis + Henderson L.P. affairs in compliance with established financial standards and applicable laws, and for the maintenance of proper standards of conduct in its activities.

KPMG LLP, Chartered Accountants, are appointed by the unitholders and have audited the consolidated financial statements of the Fund in accordance with Canadian generally accepted auditing standards. Their report outlines the nature of their audit and expresses their opinion on the consolidated financial statements of the Fund.

The Board of Directors of the General Partner and the Trustees of the Fund have each appointed an Audit Committee composed of three directors who are not members of management. The Audit Committees meet periodically with management and the auditors to discuss internal controls over the financial reporting process, auditing matters and financial reporting issues. They are responsible for reviewing the Fund’s annual and interim consolidated financial statements and the report of the auditors. The Audit Committees report the results of such reviews to the Board of Directors and the Trustees of the Fund and make recommendations with respect to the appointment of the Fund’s auditors. In addition, the Board of Directors and the Trustees may refer to the Audit Committees on other matters and questions relating to the financial position of the Fund and its subsidiaries.

The Board of Directors of the General Partner and the Trustees of the Fund are responsible for ensuring that management of Davis + Henderson L.P. fulfills its responsibilities for financial reporting and are responsible for approving the consolidated financial statements of the Fund.



C. Sanford McFarlane  
*Co-Chief Executive Officer*  
Davis + Henderson G.P. Inc.



Robert J. Cronin  
*Co-Chief Executive Officer*  
Davis + Henderson G.P. Inc.



Catherine Martin  
*Chief Financial Officer*  
Davis + Henderson G.P. Inc.

February 28, 2005

## AUDITORS' REPORT

To the Unitholders of Davis + Henderson Income Fund

We have audited the consolidated balance sheets of Davis + Henderson Income Fund as at December 31, 2004 and 2003 and the consolidated statements of income, deficit and cash flows for each of the years then ended. These financial statements are the responsibility of the management of Davis + Henderson, Limited Partnership on behalf of the Trustees of the Fund. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Fund as at December 31, 2004 and 2003 and the results of its operations and its cash flows for each of the years then ended in accordance with Canadian generally accepted accounting principles.



KPMG LLP  
*Chartered Accountants*  
*Toronto, Canada*

February 28, 2005

## CONSOLIDATED BALANCE SHEET

December 31, 2004 and 2003  
(in thousands of Canadian dollars)

	2004	2003
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$ 10,258	\$ 4,981
Accounts receivable	8,936	7,432
Inventory	5,404	6,527
Prepaid expenses	1,012	1,820
	25,610	20,760
Future income taxes (note 2)	–	31,715
Capital assets (note 3)	24,333	25,408
Other assets (note 4)	12,012	9,988
Intangible assets (note 5)	9,255	11,588
Goodwill	359,385	359,385
	\$ 430,595	\$ 458,844
<b>LIABILITIES AND UNITHOLDERS' EQUITY</b>		
Current Liabilities:		
Accounts payable and accrued liabilities	\$ 26,126	\$ 23,750
Distributions payable to unitholders	4,551	4,361
Current portion of disbursement obligations on customer contracts (note 6)	3,745	3,025
	34,422	31,136
Disbursement obligations on customer contracts (note 6)	5,435	3,625
Long-term indebtedness (note 7)	60,000	67,000
Other long-term liabilities (note 8)	2,168	1,355
	102,025	103,116
Unitholders' Equity:		
Trust units (note 9)	365,385	365,385
Deficit	(36,815)	(9,657)
	328,570	355,728
Commitments (note 10)		
	\$ 430,595	\$ 458,844

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



Paul Damp  
Trustee



Gordon J. Feeney  
Trustee



Allan Gotlieb  
Trustee



Brad Nullmeyer  
Trustee



Helen K. Sinclair  
Trustee

## CONSOLIDATED STATEMENTS OF INCOME

Years ended December 31, 2004 and 2003

(in thousands of Canadian dollars, except per unit amounts)

	2004	2003
Sales	\$ 275,586	\$ 251,783
Cost of sales	164,023	151,389
	111,563	100,394
Operating expenses	32,766	26,315
	78,797	74,079
Interest expense	4,193	4,630
Amortization expense	15,842	16,397
Income before income taxes	58,762	53,052
Income taxes (note 2):		
Current	949	1,012
Future	3,545	3,583
	4,494	4,595
Net income	\$ 54,268	\$ 48,457
Net income per unit, basic and diluted	\$ 1.4311	\$ 1.2778

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

## CONSOLIDATED STATEMENTS OF DEFICIT

Years ended December 31, 2004 and 2003

(in thousands of Canadian dollars)

	2004	2003
Deficit, beginning of year	\$ (9,657)	\$ (6,547)
Net income	54,268	48,457
Distributions	(53,256)	(51,567)
Elimination of future tax asset (note 2)	(28,170)	–
Deficit, end of year	\$ (36,815)	\$ (9,657)

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

## CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended December 31, 2004 and 2003  
(in thousands of Canadian dollars)

	2004	2003
Cash and cash equivalents provided by (used in):		
<b>OPERATING ACTIVITIES</b>		
Net income	\$ 54,268	\$ 48,457
Add:		
Amortization expense	15,842	16,397
Future income taxes	3,545	3,583
	73,655	68,437
Changes in non-cash working capital items	2,803	66
Changes in other long-term liabilities	813	66
	77,271	68,569
<b>FINANCING ACTIVITIES</b>		
(Repayment of) proceeds from revolving credit facility	(7,000)	7,000
Repayment of non-revolving credit facility	-	(20,000)
Distributions paid to public unitholders	(53,066)	(51,442)
	(60,066)	(64,442)
<b>INVESTING ACTIVITIES</b>		
Expenditures on capital assets	(7,533)	(7,265)
Expenditures on other assets	(4,395)	(3,927)
	(11,928)	(11,192)
Increase (decrease) in cash and cash equivalents for the year	5,277	(7,065)
Cash and cash equivalents, beginning of year	4,981	12,046
Cash and cash equivalents, end of year	\$ 10,258	\$ 4,981
Supplementary information:		
Cash interest paid	\$ 3,942	\$ 5,728
Cash income taxes paid	\$ 1,104	\$ 993

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

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Years ended December 31, 2004 and 2003

(in thousands of Canadian dollars, except unit and per unit amounts)

### NATURE OF BUSINESS

Davis + Henderson Income Fund (the “Fund”) is a limited-purpose trust, formed under the laws of the Province of Ontario by a declaration of trust dated November 6, 2001 and as amended and restated on July 23, 2004. The Fund was formed to indirectly acquire the partnership units of Davis + Henderson, Limited Partnership (“Davis + Henderson L.P.”).

Davis + Henderson L.P. is engaged primarily in the business of providing cheque supply program services to Canadian financial institutions. Davis + Henderson L.P. commenced operations on December 20, 2001, when it acquired the Davis + Henderson business. Simultaneously, on December 20, 2001, the Fund completed an initial public offering and acquired a 45.4% interest in Davis + Henderson L.P. On January 10, 2002, under an over-allotment option, the Fund acquired an additional 4.5% interest in Davis + Henderson L.P. On April 2, 2002, the Fund acquired the remaining balance of Davis + Henderson L.P. and now holds 100%.

### 1. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared using the following accounting policies generally accepted in Canada. The preparation of financial statements requires that management makes 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 sales and expenses during the reporting period. Actual results could differ from these estimates.

#### Principles of Consolidation

The consolidated financial statements include the accounts of the Fund and its wholly owned subsidiaries, consisting of D + H Holdings Trust, D + H Holdings Corp. (prior to July 26, 2004), Davis + Henderson G.P. Inc., and Davis + Henderson L.P. All inter-company transactions and accounts have been eliminated upon consolidation.

#### Financial Instruments

The Fund’s financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, disbursement obligations on customer contracts, distributions payable to unitholders, interest-rate swaps and long-term indebtedness. The Fund does not enter into financial instruments for trading or speculative purposes.

*Credit Risk* The Fund’s financial assets that are exposed to credit risk consist primarily of cash and cash equivalents, accounts receivable and interest-rate swaps. The Fund, in its normal course of business, is exposed to credit risk from its customers. The Fund is exposed to credit loss in the event of non-performance by counterparties to the interest-rate swaps. Risks associated with concentrations of credit risk with respect to accounts receivable and interest-rate swaps are limited due to the credit rating of customers and swap counterparties serviced by the Fund and the generally short payment terms and frequent settlement of swap differences.

*Fair Value* The fair value of indebtedness that bears interest at fixed rates is based on discounted future cash flows using rates currently available for debt of similar terms and maturities. The carrying value of other financial instruments, being cash and cash equivalents, accounts receivable, accounts payable, accrued liabilities and the current portion of the disbursement obligations on customer contracts, approximates fair value due to their short-term maturities.

*Derivative Financial Instruments* Derivative financial instruments are utilized to reduce interest-rate risk on the Fund's debt. The Fund's policy is to formally designate each derivative financial instrument as a hedge of a specifically identified debt instrument. The Fund believes the derivative financial instruments are effective as hedges, both at inception and over the term of the instrument, as the term to maturity, the (notional) principal amount and the interest-rate basis in the instruments all match the terms of the debt instrument being hedged.

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 and are recorded as an adjustment of interest expenses on the hedged debt instrument. The related amount payable to or receivable from swap counterparties is included as an adjustment to accrued interest.

In the event of a termination of an interest-rate swap agreement, gains and losses would be deferred under other current, or non-current, assets or liabilities on the balance sheet and amortized as an adjustment to interest expense related to the obligation over the remaining term of the original contract life of the terminated swap agreement. In the event of early extinguishments of the debt obligation, any realized or unrealized gain or loss from the swap is recognized in the consolidated statement of income at the time of extinguishment.

#### **Cash and Cash Equivalents**

All temporary investments with an original maturity of three months or less when purchased are considered to be cash equivalents.

The Fund and its subsidiaries maintain cash balances in bank deposit accounts or investments in amounts that exceed federally insured limits. The Fund has not experienced any losses in such accounts.

#### **Inventory**

Inventory of raw materials is stated at the lower of cost and replacement cost. Cost is determined on a first-in, first-out basis.

#### **Capital Assets**

Capital assets are recorded at cost. Amortization is provided annually at rates calculated to write off the assets over their estimated useful lives as follows:

Computer, furniture and fixtures	10% to 30% declining balance
Machinery and equipment	10% to 20% declining balance
Leasehold improvements	straight-line over term of the lease

#### **Deferred Charges**

The Fund capitalizes direct costs related to the development of new products and services until the commencement of commercial operation, at which time all related costs are amortized on a straight-line basis over their estimated useful life.

Payments associated with certain major customer contracts are amortized over the term of the related long-term supply contracts.

#### **Goodwill**

Goodwill reflects the price paid for the Davis + Henderson business in excess of the fair market value of net tangible assets and identifiable intangible assets acquired. Goodwill is not amortized but is tested for impairment annually.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

Years ended December 31, 2004 and 2003

*(in thousands of Canadian dollars, except unit and per unit amounts)*

### **Intangible Assets**

Intangible assets represent the fair market value of rights related to the cheque supply outsourcing contracts obtained by the Fund upon the acquisition of the Davis + Henderson business. Intangible assets are amortized over seven years. The carrying value of the intangible assets is tested for impairment whenever events or changes in circumstances indicate that its carrying amount may not be recoverable.

### **Revenue Recognition**

The Fund is the principal on all sales transactions and has presented sales based on the gross amount billed to the customers. Revenue for services and product sales is recognized when the services are completed and the products are shipped.

### **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.

### **Foreign Currency Translation**

Monetary items denominated in foreign currency are translated to Canadian dollars at exchange rates in effect at the balance sheet date, and non-monetary items are translated at rates of exchange in effect when the assets were acquired or obligations incurred. Revenues and expenses are translated at rates in effect at the time of the transaction. Foreign exchange gains and losses are included in income.

### **Future Income Taxes**

Future income taxes of the Fund's subsidiary, D + H Holdings Corp., prior to July 26, 2004, are determined using the asset and liability method. Under this method of tax allocation, future tax assets and liabilities are determined on the basis of differences between the financial reporting and tax bases of assets and liabilities and are measured using the substantially enacted tax rates and laws that will be in effect when the differences are expected to reverse.

Subsequent to July 26, 2004, the Fund and its subsidiaries are not subject to any income taxes provided all taxable income generated is distributed to unitholders in the form of distributions. Accordingly, subsequent to this date, the Fund no longer records a provision for income taxes.

### **Employee Future Benefits**

The Fund provides certain post-retirement benefits for eligible employees, which are not funded. These benefits include health care, life insurance and dental benefits. Obligations under the post-retirement benefit plan are actuarially determined and are accrued by the Fund.

For the Fund's defined contribution pension plan, annual pension expense is based on the Fund's actual contributions to the plan.

### **Related Parties**

For the purposes of the financial statements, parties are considered related to the Fund if the Fund has the ability to, directly or indirectly, control the party or exercise significant influence over the party in making financial and operating decisions or vice versa, or where the Fund and the party are subject to common control or common significant influence. Related parties may be individuals or other entities.

## 2. INCOME TAXES

Income earned by the Fund that is distributed annually to unitholders is not subject to taxation in the Fund, but is taxed at the individual unitholder level. A provision for income taxes is recognized for the Fund's former subsidiary, D + H Holdings Corp., as this subsidiary was subject to tax, including large corporations tax and corporate minimum tax.

In July 2004, unitholders approved an internal reorganization which resulted in the replacement of D + H Holdings Corp. with a trust entity, D + H Holdings Trust. Income of D + H Holdings Trust will not be subject to income taxes as long as all taxable income generated is distributed to the Fund and, ultimately, to the unitholders in the form of distributions. Accordingly, no provision has been made for income taxes subsequent to July 2004 and the future income tax asset of \$28.2 million, previously recorded on the balance sheet, has been charged directly to deficit.

For the year ended December 31, 2004, the provision for income taxes in the consolidated statement of income represents taxes attributable to D + H Holdings Corp. for the period up to July 2004 and was at an effective rate different from the Canadian statutory rate of 34.11% (2003 – 34.27%). The differences are as follows:

	2004	2003
Income before income taxes	\$ 58,762	\$ 53,052
Income subject to tax in the hands of the unitholders	48,519	41,709
	10,243	11,343
Canadian statutory rate	34.11%	34.27%
Income taxes at statutory rate	3,494	3,887
Increase (decrease) resulting from:		
Large corporations tax	451	1,012
Corporate minimum tax	498	–
Other	51	(304)
Income tax expense, current and future	\$ 4,494	\$ 4,595

The tax effect of temporary differences of the Fund's subsidiary that give rise to significant portions of the future income tax assets is presented below:

	2004	2003
Future income tax assets:		
Goodwill	\$ –	\$ 28,451
Capital assets	–	(1,386)
Loss carryforward	–	4,339
Other	–	311
	\$ –	\$ 31,715

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

Years ended December 31, 2004 and 2003

*(in thousands of Canadian dollars, except unit and per unit amounts)*

### 3. CAPITAL ASSETS

	2004		
	Cost	Accumulated amortization	Net
Machinery and equipment	\$ 13,954	\$ 4,172	\$ 9,782
Computer equipment and software	22,715	10,923	11,792
Furniture, fixtures and leasehold improvements	5,905	3,146	2,759
	<u>\$ 42,574</u>	<u>\$ 18,241</u>	<u>\$ 24,333</u>

	2003		
	Cost	Accumulated amortization	Net
Machinery and equipment	\$ 13,566	\$ 2,646	\$ 10,920
Computer equipment and software	22,901	11,397	11,504
Furniture, fixtures and leasehold improvements	5,126	2,142	2,984
	<u>\$ 41,593</u>	<u>\$ 16,185</u>	<u>\$ 25,408</u>

Amortization during the year ended December 31, 2004 was \$8,608 (2003 – \$8,270). Fully amortized capital assets totalling \$6,539 were removed from the accounts during the year ended December 31, 2004 (2003 – nil).

### 4. OTHER ASSETS

	2004	2003
Cost:		
Long-term supply contracts	\$ 17,788	\$ 18,495
Deferred charges and other	370	2,353
	<u>18,158</u>	<u>20,848</u>
Accumulated amortization	<u>(6,146)</u>	<u>(10,860)</u>
	<u>\$ 12,012</u>	<u>\$ 9,988</u>

Amortization during the year ended December 31, 2004 was \$4,901 (2003 – \$5,795). Fully amortized other assets totalling \$9,616 were removed from the accounts during the year ended December 31, 2004 (2003 – \$1,272).

### 5. INTANGIBLE ASSETS

	2004	2003
Cost	\$ 16,328	\$ 16,328
Accumulated amortization	(7,073)	(4,740)
	<u>\$ 9,255</u>	<u>\$ 11,588</u>

Amortization during the year ended December 31, 2004 was \$2,333 (2003 – \$2,332).

## 6. DISBURSEMENT OBLIGATIONS ON CUSTOMER CONTRACTS

	2004	2003
Current portion	\$ 3,745	\$ 3,025
Long-term portion	5,435	3,625
Total disbursement obligations on customer contracts	\$ 9,180	\$ 6,650

The Fund has customer fixed contract disbursement obligations payable as of December 31, 2004 as follows:

2005	\$ 3,745
2006	2,645
2007	1,395
2008	1,395
	\$ 9,180

## 7. LONG-TERM INDEBTEDNESS

	2004	2003
Non-revolving term loan	\$ 60,000	\$ 60,000
Revolving credit facility	–	7,000
	\$ 60,000	\$ 67,000

The Fund has \$98.0 million of term credit facilities due June 30, 2006 (December 31, 2003 – \$98.0 million), consisting of a \$60.0 million non-revolving term loan and a \$38.0 million revolving credit facility. The facilities bear interest at rates that depend on certain financial ratios of the Fund and vary in accordance with borrowing rates in Canada and the United States. The credit facilities, including any hedge contracts with the lenders, are secured in first priority by a pledge of substantially all of the Fund's assets and by a pledge of the Fund's indirect ownership interests in Davis + Henderson L.P. The fair value of long-term indebtedness approximates its carrying value.

As of December 31, 2004, the Fund has entered into interest-rate swap hedge contracts with its lenders, such that the borrowing rates on \$40.0 million or 66.7% of its outstanding term indebtedness are effectively fixed at interest rates of between 5.89% and 7.33% per annum for terms ending between March 27, 2006 and June 30, 2008. As of December 31, 2004, the fair value of outstanding interest-rate swaps was approximately \$0.9 million (December 31, 2003 – \$1.2 million), which the Fund would be required to pay if it were to close out the contracts.

Subsequent to December 31, 2004, on January 24, 2005, the Business extended and amended the terms of its term credit facilities to a due date of January 24, 2009. Total facilities were reduced to \$90.0 million, and were amended to consist of a \$50.0 million non-revolving term loan and a \$40.0 million revolving term loan.

Immediately following the extension and amendment of the facilities on January 24, 2005, the Fund made a voluntary payment of \$3.0 million. As at January 24, 2005, total long-term indebtedness of the Fund was \$57.0 million consisting of \$50.0 million drawn under the non-revolving term loan and \$7.0 million drawn under the revolving term loan.

Subsequent to December 31, 2004, the Business entered into an additional interest-rate swap for a notional amount of \$10.0 million with a term ending January 4, 2009. With the additional swap, the Business has fixed rates on 87.7% of its outstanding debt as at February 28, 2005, with interest rates ranging between 5.13% and 6.83%.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

Years ended December 31, 2004 and 2003

*(in thousands of Canadian dollars, except unit and per unit amounts)*

### 8. OTHER LONG-TERM LIABILITIES

	2004	2003
Deferred compensation program	\$ 766	\$ –
Employee future benefits	1,402	1,355
	<b>\$ 2,168</b>	<b>\$ 1,355</b>

The deferred compensation program is a long-term incentive plan for management, subject to certain performance criteria and vesting terms, payable shortly after December 31, 2006. This incentive plan was implemented on January 1, 2004.

Employee future benefits consist of a defined contribution pension plan and a non-pension post-retirement benefit plan. Obligations relating to employee future benefits relate to the non-pension post-retirement benefit plan.

The Fund's principal pension plan is the "Defined Contribution Pension Plan for the Employees of Davis + Henderson," a defined contribution pension plan that provides pensions to substantially all employees with greater than two years of service. Total expense for the Fund's defined contribution pension plan for the year ended December 31, 2004 was \$1.0 million (2003 – \$1.0 million).

The Fund's non-pension post-retirement benefit plan provides certain health care, life insurance and dental benefits to eligible employees. Terms of the plan were amended effective January 1, 2005, resulting in a reduction in obligations of \$1.8 million and actuarial losses of \$1.6 million. Reduction in obligations from the plan amendment will be amortized over three and one-half years and the actuarial losses will be amortized over the next six years starting in 2005. Information about the Fund's non-pension post-retirement benefit plan, including the effects of the plan amendments, is as follows:

	2004	2003
Accrued non-pension post-retirement benefit obligation:		
Balance at beginning of year	\$ 1,355	\$ 1,289
Service cost – benefits earned	54	50
Interest cost	91	84
Plan amendments	(1,791)	–
Actuarial losses	1,594	–
Benefits paid	(98)	(68)
Balance at end of year	<b>1,205</b>	<b>1,355</b>
Accrued non-pension post-retirement benefit liability:		
Funded status	1,205	1,355
Unamortized net actuarial loss	(1,594)	–
Unamortized past service benefits	1,791	–
Accrued non-pension post-retirement benefit liability	<b>\$ 1,402</b>	<b>\$ 1,355</b>

	2004	2003
Fund expense:		
Service cost – benefits earned	\$ 54	\$ 50
Interest cost	91	84
Net non-pension post-retirement plan expense	\$ 145	\$ 134
Actuarial assumptions:		
Discount rate to determine benefit obligation	5.75%	6.75%
Discount rate to determine benefit cost <sup>1</sup>	6.75%	6.75%
Medical inflation <sup>2</sup>	10.00%	9.00%
Dental inflation	5.00%	5.00%

<sup>1</sup>Discount rate to determine benefit cost is assumed to be 5.75% in 2005 and subsequent years.

<sup>2</sup>Medical inflation is assumed to be 10% in 2005, grading down to 5% in 2010.

#### Effects of change in assumed health cost trend rates:

##### 1% increase

Effect on total service and interest cost components	\$ 12
Effect on post-retirement accrued benefit obligation	9

##### 1% decrease

Effect on total service and interest cost components	(10)
Effect on post-retirement accrued benefit obligation	(9)

## 9. TRUST UNITS

An unlimited number of trust units may be issued by the Fund pursuant to the Fund's declaration of trust. Each unit is transferable and represents an equal, undivided beneficial interest in any distributions from the Fund and in the net assets of the Fund. All units are of the same class with equal rights and privileges and are not subject to future calls or assessments. Each unit entitles the holder to one vote at all meetings of unitholders. Trust unit transactions from inception of the Fund were as follows:

	Number of units	Gross proceeds	Issue costs	Net proceeds
Initial issuance of trust units, December 20, 2001	17,235,000	\$ 172,350	\$ 11,910	\$ 160,440
Units issued January 10, 2002	1,720,000	17,200	989	16,211
Units issued April 2, 2002	18,965,792	199,141	10,407	188,734
Balances, December 31, 2004 and 2003	37,920,792	\$ 388,691	\$ 23,306	\$ 365,385

The weighted average number of units outstanding during 2004 and 2003 was 37,920,792.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

Years ended December 31, 2004 and 2003

*(in thousands of Canadian dollars, except unit and per unit amounts)*

### 10. COMMITMENTS

As of December 31, 2004, the Fund has annual lease obligations with respect to real estate, vehicles and equipment as follows for the years ending:

2005	\$ 2,719
2006	2,465
2007	2,046
2008	1,872
2009	1,757
Thereafter	2,991
	<hr/> \$ 13,850

### 11. RELATED PARTY TRANSACTIONS

The Fund has a supplies and equipment maintenance contract with an entity related to an Officer of the Fund. Total amounts paid during the year ended December 31, 2004 was \$0.2 million (2003 – \$0.2 million). Based on a review of amounts charged by third parties for similar services, the Fund determined the contract to be at fair market value.

During the year ended December 31, 2004, a Trustee of the Fund was appointed Chairman of the Board of Canada Post Corporation, one of the Business' major suppliers. Total purchases from this supplier during the year ended December 31, 2004 was \$24.4 million (2003 – \$25.5 million).

### 12. SIGNIFICANT CUSTOMERS

The Fund operates in one segment, an integrated service offering to Canadian financial institutions and their account holders. For the year ended December 31, 2004, the Fund earned 79% (2003 – 78%) of its revenue from its six largest customers.

### 13. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform to the current year's presentation.

## TRUSTEES AND BOARD OF DIRECTORS

Directors of Davis + Henderson G.P. Inc and Trustees of Davis + Henderson Income Fund:

### **Paul Damp**

Chairman, Director and Trustee

*Managing Partner, Kestrel Capital Partners*

Paul Damp was non-executive vice-chairman and director of AIT Advanced Information Technologies Inc. from September 1999 to July 2002. He served as non-executive chairman and director of Architel Systems Corporation from June 1998 to July 2000. From October 1996 to June 1998, Mr. Damp was chairman, director and chief executive officer of Accugraph Corporation. Prior to November 1994, he was president and chief operating officer of SHL Systemhouse Inc., and prior to October 1990, a partner at KPMG LLP. Mr. Damp is also a director of Cognos Incorporated, and a director and trustee of Home Equity Income Trust as well as a director of several other private companies.

### **Allan Gotlieb**

Director and Trustee

*Chairman, Sotheby's Canada and Senior Advisor, Stikeman Elliott LP*

Allan Gotlieb was chairman of Canada Council (1989 to 1994), Canadian Ambassador to the United States (1981 to 1989), and Undersecretary of State for External Affairs (1977 to 1981). Mr. Gotlieb is also chairman of Donner Canadian Foundation and a Trustee of the Art Gallery of Ontario. Mr. Gotlieb is a Companion of the Order of Canada.

### **Bradley Nullmeyer**

Director and Trustee

*President and CEO, A&A Capital*

Bradley Nullmeyer was, prior to 2001, CEO Vendor Finance of CIT Group and, prior to 1999, president of Newcourt Financial.

### **Helen K. Sinclair**

Director and Trustee

*CEO and Chairman, Bank Works Trading Inc.*

Helen Sinclair was president of the Canadian Bankers Association from October 1989 to June 1996 and previously with The Bank of Nova Scotia. She is currently also a director of The Toronto-Dominion Bank, York University, McCain Capital Corporation, the Canada Pension Plan Investment Board and Transat A.T. Inc.

### **Gordon J. Feeney**

Director and Trustee

*Corporate Director*

Gordon Feeney joined RBC Financial Group in 1959 and retired as deputy chairman in June 2001. Mr. Feeney is currently chairman of Canada Post Corporation, Finance Corporation of Bahamas, Canadian Management Centre, Moneris Solutions Corporation and RBC Mutual Funds Inc. Mr. Feeney is also a director of American Management Association, International Survey Research Group and Rideau Inc.

### **C. Sanford McFarlane**

Director and Officer

*Co-Chief Executive Officer, Davis + Henderson G.P. Inc.*

Sanford McFarlane joined Davis + Henderson in 1975 as vice president of finance and became president in 1983. He has held the position of CEO since 1992. Mr. McFarlane has served on several boards and charitable organizations and is currently on the cabinet of the Toronto division of the United Way.

### **Robert J. Cronin**

Director and Officer

*Co-Chief Executive Officer, Davis + Henderson G.P. Inc.*

Robert Cronin has been employed by Davis + Henderson since 1996 when he became president and chief operating officer. He was named to his current position in 2004. Prior to joining Davis + Henderson, he held senior management roles with SHL Systemhouse Inc. and Integrated Network Services Inc.

## COMMITTEES OF THE BOARD

The members of each committee are:

### Audit<sup>1</sup>

Gordon J. Feeney (Committee Chair)  
Paul Damp  
Bradley Nullmeyer

<sup>1</sup>Separate audit committees exist for the board of directors of Davis + Henderson G.P. Inc. and for the trustees of Davis + Henderson Income Fund consisting of the same individuals.

### Compensation and Corporate Governance<sup>2</sup>

Helen K. Sinclair (Committee Chair)  
Paul Damp  
Allan Gotlieb

<sup>2</sup>A committee of the board of directors of Davis + Henderson G.P. Inc.

## EXECUTIVE TEAM

**C. Sanford McFarlane**  
*Co-Chief Executive Officer*

**Robert J. Cronin**  
*Co-Chief Executive Officer*

**Chad Alderson**  
*Vice President and Chief Technology Officer*

**Yves Denommé**  
*Vice President, Operations*

**Suzanne Mandrozos**  
*Vice President, Human Resources*

**Catherine Martin**  
*Chief Financial Officer*

**Serge Rivest**  
*Vice President, Sales and Marketing*

**Stephen Rotz**  
*Vice President, Corporate Development*

**Joanne Sisco**  
*Vice President, Corporate Data Services*

## CORPORATE INFORMATION

**Independent Auditors:**  
*KPMG LLP*

**Transfer Agent:**  
*CIBC Mellon Trust Company*

**Corporate Counsel:**  
*Torys LLP*

**Investor Relations:**  
*Catherine Martin 416-696-7700*  
*Email: investorrelations@dhltd.com*

**Corporate Office:**  
Suite 201, 939 Eglinton Avenue East,  
Toronto, Ontario M4G 4H7

**Telephone:** 416-696-7700

**Facsimile:** 416-696-9720

**Website:** [www.dhltd.com](http://www.dhltd.com)

**Toronto Stock Exchange Symbol:**  
*DHF.UN*

## Trademarks

“Davis + Henderson”, “Custom Cheques of Canada”, “Intercheques” and “eSwitch™” are registered trademarks in Canada, and “ChequeCentral”, “ChequeEssentials” and “ChequeAdvisor” are unregistered trademarks of Davis + Henderson, Limited Partnership. All other marks are trademarks of their respective holders.

## Annual Meeting

The annual general meeting of unitholders of Davis + Henderson Income Fund will be held at 4:00 p.m. on Wednesday, May 4, 2005 at the TSX Conference Centre, The Exchange Tower, 130 King Street West, Toronto, Ontario.

## Submissions of Concerns

Submissions of concerns regarding accounting, internal controls or auditing matters may be made in writing to the Chair of the Audit Committee on a confidential basis:  
Gordon J. Feeney,  
Chair of the Audit Committee,  
Davis + Henderson Income Fund,  
270 The Kingsway, P.O. Box 74569,  
Toronto, Ontario M9A 3T0.

Copies of this Annual Report may be obtained from:

The Secretary,  
Davis + Henderson Income Fund,  
Suite 201, 939 Eglinton Avenue East,  
Toronto, Ontario M4G 4H7.  
La version française: Sur simple demande, nous nous ferons un plaisir de vous faire parvenir la version française du présent rapport. Veuillez composer le 416-696-7700 ou nous faire parvenir un courriel [investorrelations@dhltd.com](mailto:investorrelations@dhltd.com).

## Our Core Values

We live by a well-defined set of core values – principles that we believe in and strive to uphold.

As a customer-focused organization, we believe that innovation and accountability are at the heart of our core values.

As a publicly traded company, we believe that meeting our commitments to unitholders is critical.

As an employer, we believe teamwork and mutual respect for others make great things happen.

And, as a business, we believe in making a positive difference through our actions. We encourage employee volunteerism and support charities across the country.

## Did You Know

- > Davis + Henderson has been serving Canada's financial institutions since 1875.
- > We deliver our programs, on behalf of these financial institutions, to 20 million account holders and more than one million small businesses.
- > We process more than 11 million orders annually.
- > 16% of our customer paid orders were placed directly with us over the telephone or Internet during 2004, up from 11% in 2003.
- > Through our charitable cheque programs, customers are able to improve cause awareness for charities of importance to them. In 2004, our customers donated over \$237,000 to their favourite charities through this program.
- > Almost half of our revenue is independent of cheque usage, as a significant portion of our revenue comes from new bank account openings and other services.
- > About 44% of our revenue is derived from serving small- and medium-sized businesses.
- > We declared distributions of \$1.40 per unit in 2004, up from \$1.36 per unit in 2003 and \$1.32 in 2002.
- > Our market capitalization at December 31, 2004 was \$860 million.



## Davis + Henderson

### Income Fund

Toronto Stock Exchange: "DHF.UN" Website: [www.dhltd.com](http://www.dhltd.com)