



**SECOND CUP INCOME FUND**

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**Annual Information Form**

For the year ended December 31, 2009

**March 30, 2010**

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## GLOSSARY OF TERMS

*In addition to the other terms defined in this Annual Information Form, the following terms are used frequently and are defined below. Unless the context otherwise requires, any reference in this Annual Information Form to any agreement, instrument, indenture, declaration or other document will be deemed to be a reference to that agreement, instrument, indenture or other document, as amended, supplemented and restated from time to time.*

**“Administration Agreement”** means the restated administration agreement effective as of April 11, 2007 among GP Inc. and the Fund, as amended or amended and restated from time to time, pursuant to which GP Inc. agreed to provide or arrange for the provision of services required for the administration of the Fund.

**“affiliate”** means, in respect of a person or company, another person or company that would be considered to be an “affiliated entity” in respect of such person or company for the purposes of Ontario Securities Commission Rule 45-501, as amended or replaced from time to time.

**“associate”** has the meaning ascribed to it in the Securities Act.

**“Bank”** means the Canadian chartered bank affiliate of Scotia Capital Inc.

**“Book-Entry Only System”** means the book-based system administered by CDS for registration of interest in and transfer of the Units.

**“CDS”** means The Canadian Depository for Securities Limited.

**“CDS Participant”** means a participant in the CDS depository service.

**“Closing”** means the completion of the initial public offering of the Fund and the transactions to complete the offering as described in the prospectus.

**“Closing Date”** means December 2, 2004, the date of completion of the initial public offering of the Fund.

**“Declaration of Trust”** means the declaration of trust dated December 1, 2004, as amended or as amended and restated from time to time, establishing and governing Second Cup Royalty Income Fund.

**“Deferred Income Plans”** means registered retirement savings plans, registered retirement income funds and deferred profit sharing plans.

**“EBITDA”** means earnings before interest, taxes, depreciation and amortization.

**“Fund”** means Second Cup Royalty Income Fund.

**“Fund Operating Loan”** means the revolving loan facility in the amount of up to \$1,000,000 established by the Bank in favour of the Fund.

**“Fund Term Loan”** means the term loan in the principal amount of \$11,000,000 made on April 2, 2007 by the Bank to the Fund, any renewal thereof and any replacement thereof by a financial institution carrying on business in Canada as more fully described under “General Development of the Business — Fund Term Loan and Fund Operating Loan”.

“**GP Inc.**” means Second Cup GP Inc., a corporation established under the laws of Ontario and a direct subsidiary of the Fund and sole trustee of GP Trust.

“**GP Trust**” means Second Cup GP Trust, a trust established under the laws of the Province of Ontario pursuant to a declaration of trust and the general partner of MarksLP.

“**Gross Revenue**” has the meaning ascribed to it in “Business of Second Cup — Franchise Operations — Second Cup Franchise Agreements” as it relates to both company-owned cafés and franchised cafés.

“**Licence**” means the licence to use the Second Cup Marks (including for the purpose of trade names and domain names) in all provinces and territories of Canada, excluding the territory of Nunavut, for a period of 99 years.

“**Licence and Royalty Agreement**” means the licence and royalty agreement dated November 26, 2004, as amended, or amended and restated from time to time, between MarksLP and Second Cup pursuant to which Second Cup was granted the Licence and agreed to pay a royalty to MarksLP.

“**Limited Partnership Agreement**” means the limited partnership agreement of MarksLP, as amended or amended and restated from time to time, dated March 28, 2007 between GP Trust and the Fund.

“**MarksCo**” means Second Cup Trade-Marks Inc., which prior to the reorganization was a wholly-owned subsidiary of AcquisitionCo that held the Second Cup Marks and was a party to the Licence and Royalty Agreement.

“**MarksLP**” means Second Cup Trade-Marks Limited Partnership, a limited partnership established under the laws of the Province of Ontario and an indirect wholly-owned subsidiary of the Fund.

“**MarksLP Note**” means the subordinated unsecured promissory note in the principal amount of \$9,170,467 made on April 2, 2007 by MarksLP to MarksCo, and which was assigned by MarksCo to the Fund on April 2, 2007.

“**Redemption Price**” has the meaning ascribed thereto under “Description of the Fund — Redemption Right”.

“**S.C. Coffee Co.**” means The Second Cup Coffee Company Inc. (formerly Dinecorp Hospitality Inc.), a private corporation formed under the laws of the Province of Ontario.

“**Second Cup**” means The Second Cup Ltd., the operating company that carries on the business of franchising Second Cup cafés and operating company-owned cafés in Canada.

“**Second Cup cafés**” refers to the retail outlets dedicated to the sale of specialty coffee and related products operated by Second Cup, or Second Cup franchise partners and identified by the Second Cup Marks.

“**Second Cup Marks**” means the trade-marks owned by MarksLP and registered under the *Trade-marks Act* (Canada), and such trade-marks, trade names, operating procedures, methods, systems and other intellectual property and proprietary rights that are used in connection with the operation of Second Cup cafés in Canada and all associated rights.

“**Securities Act**” means the *Securities Act* (Ontario), as amended.

“**Stock Exchange**” means a stock exchange recognized by the Ontario Securities Commission for such purposes, and where the Units have traded on more than one Stock Exchange during the relevant period, “**Stock Exchange**” means the Stock Exchange where the greatest volume of Units traded during the relevant period.

“**System Sales**” is the basis on which the Royalty is payable; it means the Gross Revenue of all Second Cup cafés in the royalty pool, including (i) the Gross Revenue of the company-owned Second Cup cafés in Canada owned by Second Cup; and (ii) the Gross Revenue reported by Second Cup cafés in the royalty pool which are subject to franchise agreements with Second Cup, without audit or other form of independent assurance.

“**Tax Act**” means the *Income Tax Act* (Canada).

“**trustees**” means, at the relevant time, the trustees of the Fund.

“**Unit**” means a trust unit of the Fund, each such unit representing an equal undivided beneficial interest in any of the Fund’s distributions, whether of net income, net realized capital gains or other amounts, and in any distributions by the Fund in the event of the Fund’s termination.

“**Unit Yield**” as of an Adjustment Date means the amount of the cash distributions paid by the Fund to Unitholders for each Unit held during the year ended immediately prior to such date divided by the Current Market Price of a Unit on such date.

“**Unitholders**” means, at the relevant time, the holders of the Units.

“**Unitholders’ Special Resolution**” means a resolution passed by a majority of not less than  $66\frac{2}{3}\%$  of the votes cast, either in person or by proxy, at a meeting of Unitholders, called for the purpose of approving such resolution, or approved in writing by the holders of not less than  $66\frac{2}{3}\%$  of the Units entitled to be voted on such resolution.

## FORWARD-LOOKING STATEMENTS

Certain statements in this Annual Information Form that are not current or historical factual information may constitute forward-looking information within the meaning of applicable securities legislation. Forward-looking information can be identified by words such as “may”, “will”, “should”, “expect”, “anticipate”, “believe”, “plan”, “intend” and other similar words. Forward-looking information reflects current expectations regarding future events and operating performance and speaks only as of the date of this Annual Information Form. It should not be read as a guarantee of future performance or results and will not necessarily be an accurate indication of whether or not those results will be achieved. Forward-looking information is based upon a number of assumptions and is subject to known and unknown risks, uncertainties and other factors, many of which are beyond the Fund’s control, that may cause the Fund’s actual results, performance or achievements, or those of MarksLP, Second Cup, Second Cup cafés, or industry results to be materially different from any future results, performance or achievements expressed or implied by such forward-looking information. The following are some of the factors that could cause actual results to differ materially from those expressed in or underlying forward-looking information: competition; availability of premium quality coffee beans; the ability to attract qualified franchise partners; the location of Second Cup cafés; the closure of Second Cup cafés; loss of key personnel, compliance with government regulation; potential litigation; the ability to exploit and protect the Second Cup Marks; changing consumer preferences and discretionary spending patterns including, but not restricted to, the impact of weather and economic conditions on such patterns; reporting of Gross Revenue by franchise partners. The foregoing list of factors is not exhaustive, and investors should refer to the risks described under “Risk Factors”.

Although the forward-looking information contained in this Annual Information Form is based upon assumptions, current estimates, expectations and projections, which we believe are reasonable in the circumstances as of the current date, there can be no assurance that actual results will be consistent with this forward-looking information. You should not place undue importance on forward-looking information and should not rely upon this information as of any other date. The Fund is providing the forward-oriented financial information and financial outlook set out in this Annual Information Form for the purpose of helping explain the objectives and strategies of the Fund. Readers are cautioned that this information may not be appropriate for any other purpose.

Other than as required under securities laws, the Fund does not undertake to update any such forward-looking information. Additional information about these assumptions and risks and uncertainties is contained in the Fund’s filings with securities regulators. These filings are also available at [www.sedar.com](http://www.sedar.com) or on the Fund’s website at [www.secondcupincomefund.com](http://www.secondcupincomefund.com).

## GENERAL

All information contained in this Annual Information Form is presented as of December 31, 2009 unless otherwise indicated. All dollar amounts are stated in Canadian currency unless otherwise stated. Reference is made to the glossary for the meaning of certain defined terms.

## FUND STRUCTURE

### *Name, Address and Jurisdiction of Formation*

#### **Second Cup Income Fund**

The Fund is an open-ended trust established under the laws of the Province of Ontario and governed by the Declaration of Trust. The Fund's registered and head office is located at 6303 Airport Road, 2<sup>nd</sup> Floor, Mississauga, Ontario L4V 1R8.

#### **MarksLP**

MarksLP is a limited partnership governed by the laws of the Province of Ontario and is an indirect wholly-owned subsidiary of the Fund. The head office of MarksLP is located at 6303 Airport Road, 2<sup>nd</sup> Floor, Mississauga, Ontario, L4V 1R8.

#### **GP Trust**

GP Trust is a trust governed by the laws of the Province of Ontario and is a wholly-owned subsidiary of the Fund. The head office of GP Trust is located at 6303 Airport Road, 2<sup>nd</sup> Floor, Mississauga, Ontario, L4V 1R8. Effective April 11, 2007, the Fund and GP Inc. entered into an administration agreement pursuant to which GP Inc. provides certain administrative and advisory services required for the administration of the Fund.

#### **GP Inc.**

GP Inc. is a corporation incorporated under the laws of the Province of Ontario and is a wholly-owned subsidiary of the Fund. The head office of GP Inc. is located at 6303 Airport Road, 2<sup>nd</sup> Floor, Mississauga, Ontario, L4V 1R8.

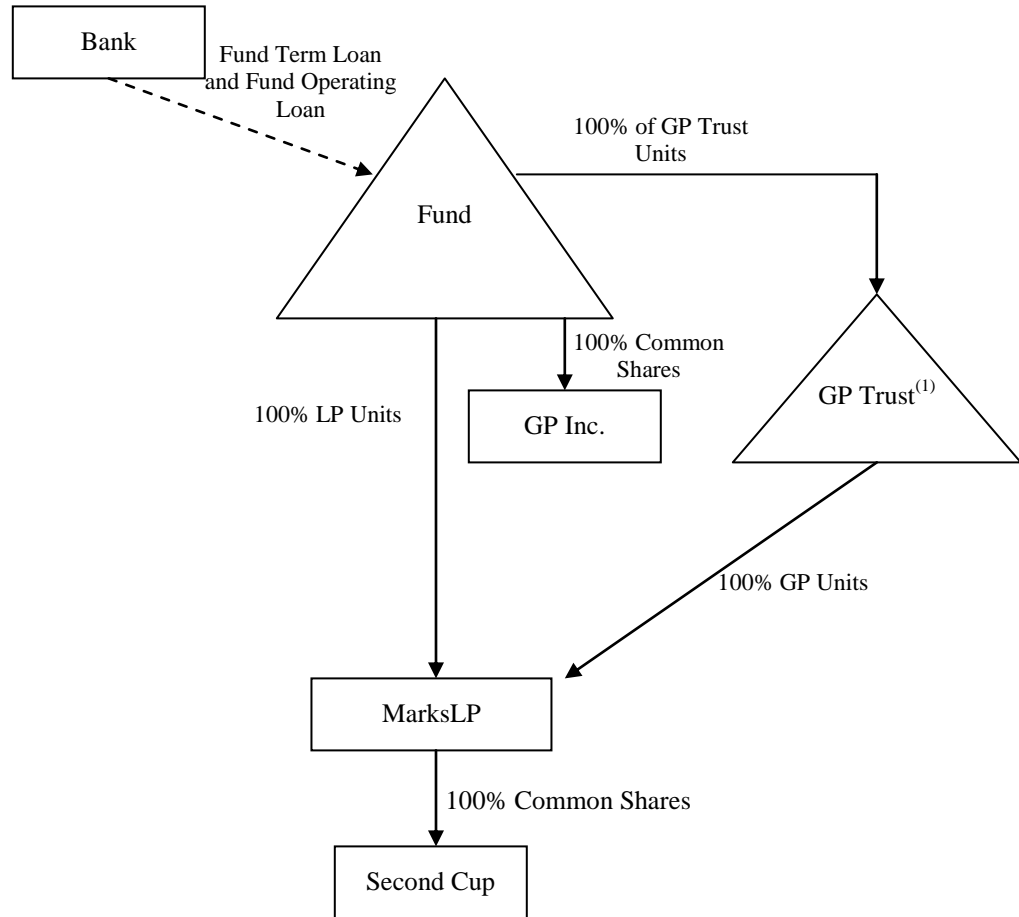
#### **The Second Cup Ltd.**

Second Cup is a wholly-owned subsidiary of MarksLP. The company's registered and head office is located at 6303 Airport Road, 2<sup>nd</sup> Floor, Mississauga, Ontario L4V 1R8.



***Intercorporate Relationships***

The following diagram illustrates the Fund's organizational structure:



(1) The sole trustee of GP Trust is GP Inc.

## **GENERAL DEVELOPMENT OF THE BUSINESS**

### ***Establishment of the Fund***

The Fund was established on October 22, 2004 and completed an initial public offering of 8,145,346 Units on December 2, 2004 at \$10.00 per Unit for aggregate proceeds of \$81,453,000 before cash issuance costs of \$8,887,000. The Units commenced trading on the Toronto Stock Exchange (the “TSX”) on December 2, 2004. In addition, the Fund issued 1,437,414 Units to Second Cup on the Closing Date at \$10.00 per Unit for aggregate proceeds of \$14,374,000. The Fund did not carry on any business prior to that date.

The Fund used the proceeds of its initial public offering (net of fees payable to the Underwriters of the offering and offering expenses) plus the proceeds of Second Cup’s subscription for Units, to indirectly acquire the Second Cup Marks through the indirect acquisition of MarksCo. As a result of this acquisition, MarksCo became an indirect wholly-owned subsidiary of the Fund, a party to the Licence and Royalty Agreement and the borrower under a term loan in the amount of \$11,000,000 obtained from the Bank.

On April 2, 2007 the Unitholder-approved reorganization of the Fund became effective pursuant to which the subsidiary corporations of the Fund, including MarksCo, were replaced with a newly formed trust, GP Trust, and limited partnership, MarksLP. As a result of the reorganization, the Licence and Royalty Agreement was assigned by MarksCo to MarksLP. In addition, the Fund negotiated a new term loan of \$11,000,000 with the Bank (the “Fund Term Loan”) on similar terms and conditions as the MarksCo term loan.

### ***Acquisition of Second Cup***

On June 27, 2009, the Fund through MarksLP acquired all the issued and outstanding shares of Second Cup from S.C Coffee Co. Following the closing, Second Cup and its management team continued to operate the Second Cup business as an indirect wholly-owned subsidiary of the Fund. Prior to the acquisition, the Fund derived its revenue through royalty payments indirectly received from Second Cup pursuant to the License and Royalty Agreement. Following the acquisition, the business of the Fund and the business of Second Cup previously carried on separately were recombined. As a result of the recombination, Unitholders own both the royalty and operating branches of the business and distributions to Unitholders and the value of the Fund’s Units are based upon the performance of the Second Cup business as a whole. The acquisition was the result of a review of the structure of the Fund and the Second Cup business, undertaken by the Fund and S.C. Coffee Co., the previous owner of Second Cup. The acquisition has provided Unitholders with direct oversight over the operation of the Second Cup business through the Fund’s Board of Trustees and will enable Unitholders to enjoy the full upside in the business attributable to operational improvements, new cafe openings, new business opportunities and the eventual strengthening of the Canadian economy.

### ***Fund Term Loan and Fund Operating Loan***

The Fund has outstanding a term loan of \$11,000,000 (“Fund Term Loan”) and an operating loan of \$1,000,000 (“Fund Operating Loan”). The Fund Operating Loan is repayable on demand and provides the Fund with working capital from time to time, if required. As at December 31, 2009, there was no balance owing by the Fund on the Fund Operating Loan.

The indebtedness and liability of MarksLP under the Fund Term Loan and the Fund Operating Loan are secured by a first ranking security interest in all property of MarksLP. The indebtedness secured by the Bank's security interest (including the Fund Term Loan, the Fund Operating Loan and any interest rate hedging facility) ranks senior to all other indebtedness of MarksLP.

Pursuant to the terms of the Fund Operating Loan and Fund Term Loan, MarksLP is subject to certain financial and other customary covenants, including requirements to maintain a ratio of senior debt to EBITDA of less than 1.25:1.0 and to maintain trailing four quarter fixed charge coverage ratio of 3:1. In addition, the Bank may accelerate repayment of the Fund Term Loan and Fund Operating Loan in the case of certain events, including a change in control of MarksLP or a default by MarksLP under material agreements or other indebtedness. During the year ended December 31, 2009, MarksLP was in compliance with all financial and other covenants of the Fund Operating Loan and Fund Term Loan. See "Risk Factors – MarksLP has outstanding indebtedness".

The Fund, GP Inc., GP Trust and Second Cup guarantee the liability of MarksLP under the Fund Term Loan and Fund Operating Loan, which guarantees are secured by all of their respective assets.

### ***Business of the Fund***

The Fund was created as a limited purpose trust to use the proceeds of an initial public offering to indirectly acquire the Second Cup Marks. Units of the Fund are traded on the Toronto Stock Exchange under the symbol "SCU.UN". The Fund's fiscal year ends December 31. The Fund carries on no active business of its own and has no employees. The Fund makes cash distributions to Unitholders from income derived from distributions received from MarksLP, less estimated amounts required for the payment of expenses, any cash redemptions of Units and other amounts. See "Description of the Fund – Cash Distributions".

### ***Business of GP Inc.***

GP Inc. is a wholly-owned subsidiary of the Fund. GP Inc. is the sole trustee of GP Trust and is also responsible for the administration of the Fund pursuant to the Administration Agreement. GP Inc. carries on no active business of its own.

### ***Business of GP Trust***

GP Trust is a wholly-owned subsidiary of the Fund. GP Trust is the general partner of MarksLP. GP Trust carries on no active business of its own other than acting as general partner of MarksLP and has no employees.

### ***Business of MarksLP***

The business of MarksLP is the ownership of both the Second Cup Marks and Second Cup.

## **BUSINESS OF SECOND CUP**

### ***General***

Second Cup is Canada's largest franchisor of specialty coffee cafés and second largest retailer of specialty coffee, as measured by number of cafés. Since the opening of its first café in suburban Toronto in 1975, Second Cup's network has grown to 347 cafés across Canada as at December 26, 2009, of which 339 are franchised and 8 are company-owned. For the 52-week period ended December 26, 2009, Second Cup's system sales were \$190,958,000.

Second Cup cafés offer a wide selection of brewed specialty coffees, hot and cold espresso-based beverages, blender drinks, specialty teas and hot chocolates for in-store, take-out and drive-thru consumption. In addition to coffee-based products and other beverages, Second Cup cafés carry a variety of complementary products, including pastries, muffins, cookies, coffee accessories and coffee-related gift items, with some cafés also offering sandwiches.

### ***What is Specialty Coffee?***

The term "specialty coffee", as used in reference to coffee production, refers to coffee produced from premium quality Arabica coffee beans prepared according to exacting standards. Typically, specialty coffee is sourced from the top 10% of the world's Arabica coffee bean production and must satisfy stringent grading and sorting standards, which results in a distinct, tangible difference in the taste profile of specialty coffee as compared to commodity ground coffee and instant coffee. The term "specialty coffee", as used in reference to the retail market for coffee products, is increasingly being used as a general term to describe the sector within the coffee market characterized by cafés offering an upscale retail experience and premium coffee products such as espresso-based beverages, blender drinks and iced coffee beverages.

### ***History***

Second Cup opened its first café in a shopping mall in suburban Toronto in 1975. Throughout the late 1970s and 1980s, the chain experienced rapid growth. By 1989, Second Cup had approximately 130 cafés, with shopping malls and office tower locations comprising over two thirds of its café network, and sales consisting mainly of brewed coffee, whole bean coffee and coffee-related merchandise.

Throughout the 1990s and early 2000s, Second Cup focused on extending its core product offering to include espresso-based beverages, iced beverages, blender drinks, and complementary food items such as pastries, muffins and cookies. During this period, Second Cup also continued to expand by opening cafés in street-front locations and power and strip centres, as well as in non-traditional retail locations such as hospitals, universities, airports, train stations and other transportation venues.

In December 2004, Second Cup sold the Second Cup Marks to the Fund and entered into the License and Royalty Agreement in conjunction with the Fund's initial public offering. Second Cup retained a 15% interest in the issued and outstanding Units of the Fund.

On November 14, 2006, Mr. Gabriel Tsampalieros, the Chairman and Chief Executive Officer of Second Cup purchased all of the issued and outstanding shares of Second Cup through S.C. Coffee Co., a corporation controlled by

him. The transaction excluded the Fund units previously held by Second Cup. In addition, S.C. Coffee Co. also purchased all the international Second Cup trade-marks which were not transferred to the Fund in connection with the Fund's initial public offering in December 2004.

On June 27, 2009, S.C. Coffee Co. sold all of the issued and outstanding shares of Second Cup to MarksLP recombining the business of the Fund with the business of Second Cup. As a result of the transaction, Second Cup became an indirect wholly-owned subsidiary of the Fund.

By December 26, 2009, Second Cup had 347 cafés in Canada and system sales of \$190,958,000 for the 52-week period ended December 26, 2009.

### ***Competitive Conditions***

The Canadian specialty coffee market is highly competitive and highly fragmented, with few barriers to entry. Management estimates that independent specialty coffee retailers constitute approximately 50% of specialty coffee cafés in Canada as measured by number of locations. Three specialty coffee retailers have a significant presence in Canada: Second Cup, Starbucks and Timothy's. Starbucks and Timothy's operate approximately 1051 and 94 locations in Canada, respectively, based on information obtained from the websites of these retailers as at February 16 2010. The remainder of the branded specialty coffee chains in Canada consist of smaller, mainly regional, participants such as A.L. Van Houtte, Blenz, Café Dépôt, Café Suprême, Café Presse and Williams Coffee Pub.

Management is not aware of any reliable third party comparable data on the trends affecting the Canadian specialty coffee market during the year or the performance of Second Cup's competitors in the Canadian specialty coffee market during this period.

In addition to specialty coffee retailers, there are a number of "mainstream" coffee retail chains, such as Tim Horton's, Coffee Time and Country Style, who compete with Second Cup in the Canadian coffee market and a growing number of "quick service restaurants" such as McDonalds who have also added premium and specialty coffee to their service offerings.

With 347 cafés as at December 26, 2009, Second Cup has the second largest number of specialty coffee retail outlets in Canada.

### ***The Second Cup Café System***

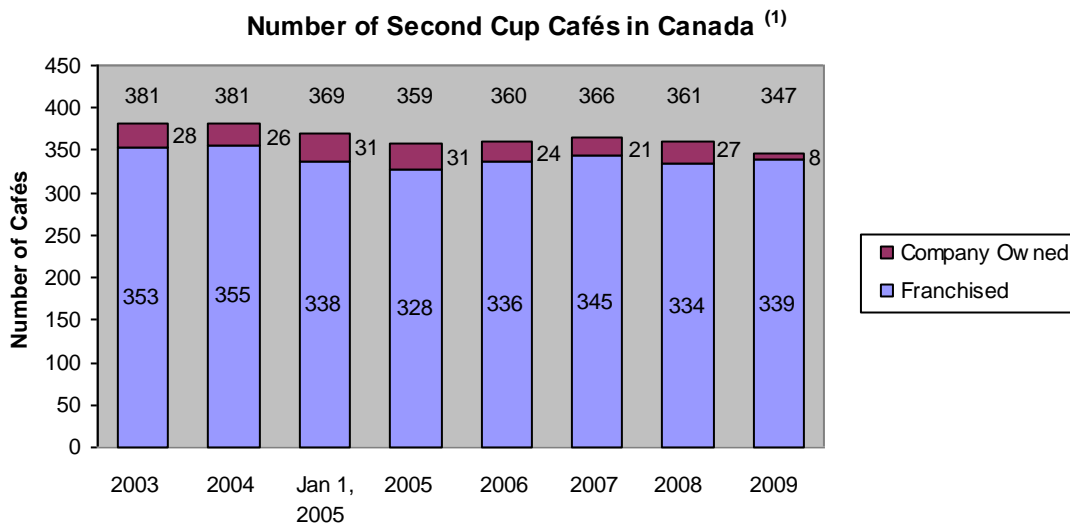
#### ***The Second Cup Concept***

The Second Cup brand has a high degree of retail visibility, with locations in high-traffic areas in almost every major city in Canada. Second Cup is a franchise-driven business focused on delivering a premium experience to its guests, which includes offering products that are "best in class" and focused on developing innovative, market leading products that make Second Cup cafés a destination of choice for Canadian coffee drinkers. Second Cup is focused on continuing the growth of the Second Cup brand through a combination of growing existing café sales and adding new cafés to the Second Cup network.

*Number of Locations*

Since 1975, there has been substantial growth in the number of Second Cup cafés in Canada. Following periods of steady expansion in the 1970s and 1980s, Second Cup experienced rapid growth in net new cafés from 1997 to 2000, adding 99 cafes, many of which were in non-traditional retail sites such as “store-in-store”, hospital, airport and other venues.

Following this period of rapid expansion, the number of cafés declined marginally as management focused on enhancing the performance of existing cafés, closing non-performing locations and solidifying the competitive position of Second Cup.



Note:

(1) All figures are as at the end of the respective fiscal period. For 2003 and 2004, figures are for the 52-week fiscal period ended on the Saturday closest to March 31. For January 1, 2005, figures are for the 40-week period ended January 1, 2005. Second Cup recorded a shortened fiscal period consisting of 40 weeks ended January 1, 2005 as a result of the change in its fiscal year end to coincide with that of the Fund. For 2005 onwards, figures are for the 52-week fiscal period ended the last Saturday of December.

As illustrated in the chart above, the vast majority of Second Cup cafés are franchised. Although Second Cup is a franchise-driven business, it operates company-owned cafés in order to remediate under performing franchises and to take advantage of expansion opportunities on a timely basis. These company-owned cafés often will subsequently become franchised.

In addition to focusing on identifying locations for new cafés, Second Cup also carefully monitors the performance of its existing network of franchised cafés and closes under performing cafés on a managed basis. By closing under performing cafés and carefully selecting locations for new cafés, Second Cup seeks to strengthen its café network and increase average sales per café.

## Second Cup Café Openings and Closings<sup>(1)</sup>

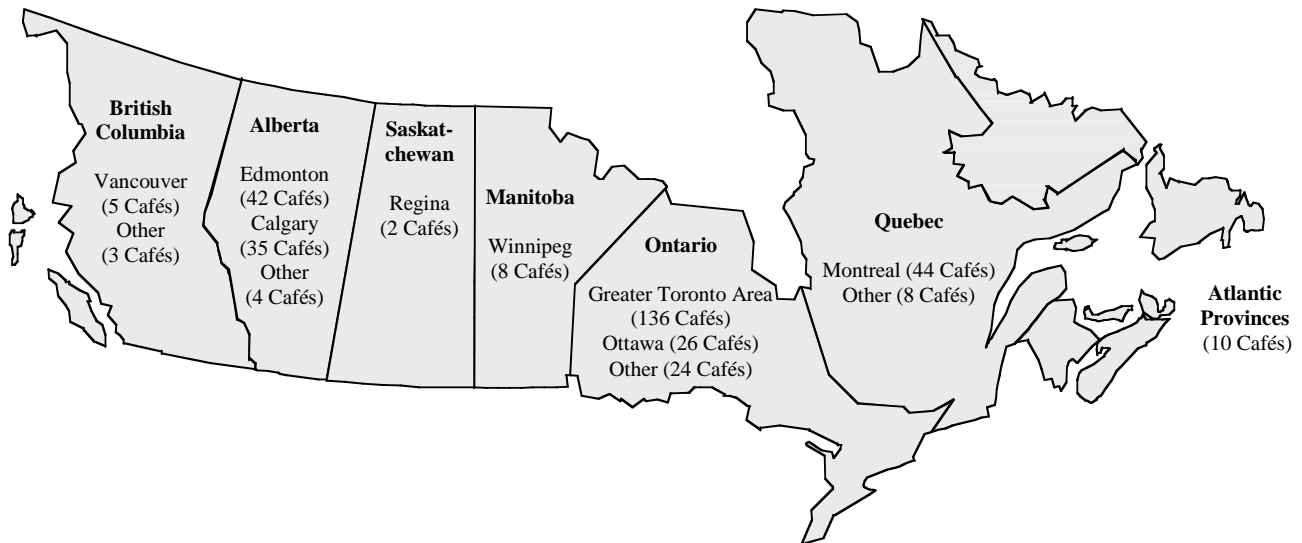
	<u>2003</u>	<u>Mar.</u> <u>2004</u>	<u>Jan.</u> <u>2005<sup>(2)</sup></u>	<u>2005<sup>(3)</sup></u>	<u>2006<sup>(3)</sup></u>	<u>2007</u>	<u>2008</u>	<u>2009</u>
Openings	10	12	7	6	16	14	12	10
Closings	17	12	19	16	15	8	17	27

Notes:

- (1) For 2003 and 2004, figures are for the 52-week fiscal period ended on the Saturday closest to March 31.
- (2) Figures for January, 2005 reflect café openings and closings for the 40-week period ended January 1, 2005. Second Cup recorded a shortened fiscal period consisting of 40 weeks ended January 1, 2005 as a result of the change in its fiscal year to coincide with that of the Fund.
- (3) Figures for 2005 onwards, figures are for the 52-week fiscal period ended the last Saturday of December.

### Geographic Presence

Second Cup cafés are geographically dispersed across Canada and are primarily concentrated in large urban centres such as Toronto, Calgary, Montreal, Edmonton, Ottawa and Vancouver. The following map illustrates the geographic distribution of Second Cup cafés in Canada.



### Café Types

Second Cup cafés are situated in a wide range of high-traffic, high-visibility locations, consisting of street-fronts, shopping malls, office towers, power and strip centres and non-traditional retail sites such as hospitals, universities, “store-in-store” sites, airports, train stations and other transportation venues. Second Cup café sizes range from 60 square foot cappuccino bars to 2,800 square foot street-front locations with self-contained customer seating areas and outdoor patios.

The following table illustrates the relative mix of location types in the Second Cup café network as at December 26, 2009:

	<b>Number of Cafés</b>	<b>% of Total</b>
Street-Fronts .....	94	27%
Power and Strip Centres .....	82	24%
Shopping Malls.....	64	18%
Non-Traditional .....	69	20%
Office Towers .....	38	11%
Total .....	<u>347</u>	<u>100%</u>

- *Street-Fronts* — As at December 26, 2009 there were 94 Second Cup cafés operating in street-front locations, representing 27% of all Second Cup cafés in Canada. Street-front cafés average 1,500 square feet and generally contain seating for approximately 15 or more customers, with many also offering external patio seating.
- *Power and Strip Centres* — With the growth of power and strip centres containing “big box” retailers and factory outlet stores, Second Cup has opened an increasing number of cafés in this type of venue. Second Cup currently has 82 cafés operating in power and strip centres, representing 24% of all Second Cup cafés in Canada. Power and strip centre cafés average 1,700 square feet and typically have self-contained seating and external patio areas, with some having drive-thru access as well.
- *Shopping Malls* — There are currently 64 Second Cup cafés operating in shopping malls, representing 18% of all Second Cup cafés in Canada. These cafés average 600 square feet, but can range from 60 square foot cappuccino bars to 1,600 square foot sites.
- *Non-Traditional* — Second Cup has developed a flexible café format that is suitable for non-traditional retail locations, such as hospitals, universities, “store-in-store” sites, airports, train stations and other transportation venues. Second Cup currently operates 69 non-traditional cafés, representing 20% of all Second Cup cafés in Canada, and consisting of 15 cafés located in hospitals, 21 cafés located in educational venues, 13 cafés located in transportation venues and 20 cafés located in “store-in-store” sites, mainly in combination with Harvey’s branded restaurants within Home Depot stores.
- *Office Towers* — Second Cup currently has 38 cafés operating in office towers, representing 11% of all Second Cup cafés in Canada. Office tower cafés average 850 square feet, but can range from 150 square foot cappuccino bars to 1,600 square foot sites. Office tower locations tend to serve a captive customer base of individuals working in the office tower itself.



### *New Locations*

Prior to entering a particular market area, Second Cup conducts a thorough market assessment to determine the optimal number and placement of cafés. Second Cup's location selection process involves a variety of analytical techniques to evaluate factors that impact upon the viability of a proposed location, such as visibility, accessibility and traffic, as well as population density, household income, local competition and the proximity to major activity centres. New lease commitments entered into by Second Cup are carefully screened by management using a projected return on investment analysis. Second Cup believes that careful diligence in evaluating proposed new café locations has contributed to its success and helped minimize the number of under performing cafés in the Second Cup network.

### *Leases*

Almost all Second Cup cafés are operated in leased premises. Second Cup enters into the head lease for each café location and, in turn, enters into a sublease with each of its franchise partners. Second Cup believes that entering into such arrangements allows it to maintain greater control over, and flexibility with respect to, the development process and the ongoing goodwill generated at its cafés. The leases that have been entered into by Second Cup are renewable over a staggered period, with an average of approximately 35 leases coming up for renewal annually over the next 10 years. The staggered nature of the lease renewal periods provides Second Cup with the flexibility to address under performing cafés, and ensures the periodic refreshment of the café network as franchise partners are required to modernize locations upon the renewal of the franchise agreement.

### ***Products***

Second Cup's coffee portfolio includes over 25 types of coffee, including a number of single origin estate coffees and a variety of blends exclusive to Second Cup, such as Paradiso<sup>®</sup>, Espresso Forte and Second Cup's Holiday Blend. Second Cup has developed a custom five-point roast scale to distinguish each coffee by its degree of roast. Ranging from one to five (with five being the darkest roast), the use of the roast scale permits customers to select the degree of roast that corresponds to their taste preference. Second Cup also offers a wide variety of espresso-based beverages and blender drinks such as espressos, cappuccinos, lattes and iced coffees, and is continually developing variations of these products. Examples of innovative espresso-based beverages and blender drinks developed by Second Cup include the Moccaccino<sup>™</sup>, Caramel Corretto<sup>®</sup>, Chillatte<sup>®</sup>, Frrozen Hot Chocolate<sup>™</sup> and Icepresso Chiller<sup>™</sup>.

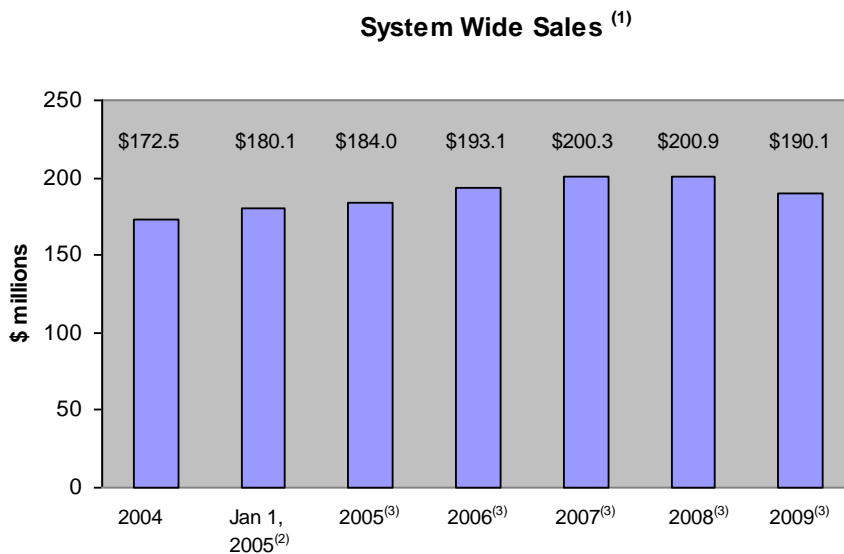
During 2008, Second Cup introduced a new fair-trade and organic certified blend of coffee entitled Cuzco and a retail whole bean program in café in sealed valve bags merchandised in free standing racks. In January 2009, Second Cup launched a light-medium roast blend of coffee named Mellow Blend, sourced from Columbia, Costa Rica and Peru. Two new tea lattes named Green Tea Matcha Latte and London Fog Latte, were introduced to the market in April 2009. During the summer of 2009, Second Cup added a Sparkling Green Tea Lemonade made from green tea concentrate and a Vanilla Yogurt Smoothie that is high in pro-biotic fibre to the cold beverage product offerings.

In addition to coffee-based products and other beverages, Second Cup cafés carry a variety of complementary products, including pastries, muffins, cookies, coffee accessories and coffee-related gift items, with most cafés also offering sandwiches. Second Cup introduced breakfast cookies, snack bars, yogurt parfaits, grilled sandwiches, and hot breakfast sandwiches in order to capitalize on the consumer need for convenience and "one stop shopping" on what it has identified as a trend in customer preference towards snacking occasions as a substitute for traditional meals.

Second Cup has also put more focus on developing its cafés as a destination for high quality, seasonal merchandise such as that offered during the holiday season which customers expect from a premium specialty coffee retailer. The breakfast category of food products was broadened in 2009 with the launch of Summer Berry/Sweet Vanilla Oatmeal and Maple Pecan Oatmeal; both products are made with instant oatmeal and designed for “on the go” consumption.

**Sales**

Since 1995, Second Cup’s system sales have almost tripled, from \$71,400,000 for the 52-week period ended June 24, 1995 to \$190,958,000 for the 52-week period ended December 26, 2009. The increase in system sales has been achieved through a combination of growth in the number of cafés, as well as same café sales growth.



Notes:

- (1) For 2003 and 2004, results are for the 52-week fiscal period ended on the Saturday closest to March 31.
- (2) For January 1, 2005, results shown are for the 52-week period ended January 1, 2005. Second Cup recorded a shortened fiscal period consisting of 40 weeks ended January 1, 2005 as a result of the change in its fiscal year-end to coincide with that of the Fund. Sales for the 40-week period ended January 1, 2005 were \$140,848,000.
- (3) 2005 onwards, figures are for the 52-week fiscal period ended the last Saturday of December.

### *Same Café Sales Growth and Average Sales per Café*

As indicated in the table below, since 2003, annual same café sales growth has averaged approximately 2.0%. Second Cup has achieved such growth by increasing brand awareness and expanding product offerings.

#### **Same Café Sales Growth<sup>(1)</sup>**

	<b><u>40 weeks ended January 1, 2005<sup>(3)</sup></u></b>						
<b><u>2003</u></b>	<b><u>2004<sup>(2)</sup></u></b>	<b><u>1, 2005<sup>(3)</sup></u></b>	<b><u>2005<sup>(4)</sup></u></b>	<b><u>2006<sup>(4)</sup></u></b>	<b><u>2007<sup>(4)</sup></u></b>	<b><u>2008<sup>(4)</sup></u></b>	<b><u>2009<sup>(4)</sup></u></b>
-0.3%	-0.7%	5.8%	4.6%	6.2%	3.1%	0.2%	-3.2%

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Notes:

- (1) For 2003 and 2004, figures are for the 52-week fiscal period ended on the Saturday closest to March 31.
- (2) Second Cup results were impacted by the power outage that occurred in Ontario in August 2003 and the outbreak of SARS in the Greater Toronto Area in April 2003 through June 2003. The financial results for these periods are reflected in fiscal 2004.
- (3) As a result of a change in its fiscal year-end subsequent to the creation of the Fund, Second Cup changed its year-end from the Saturday closest to March 31 to the Saturday closest to December 31. Same Café Growth of 5.8% represents growth for the 40-week period ended January 1, 2005.
- (4) 2005 onwards, figures are for the 52-week fiscal period ended the last Saturday of December.

Second Cup has increased average sales per café from approximately \$420,000 in 1997 to approximately \$554,000 for the 52-week period ended December 26, 2009. With the exception of the 2009 results which were impacted by the economic downturn, Second Cup has consistently maintained or improved average sales per café each year.

#### **Average Sales per Café<sup>(1)</sup>** (thousands)

	<b><u>January 1, 2005<sup>(3)</sup></u></b>						
<b><u>2003</u></b>	<b><u>2004<sup>(2)</sup></u></b>	<b><u>2005<sup>(3)</sup></u></b>	<b><u>2005<sup>(4)</sup></u></b>	<b><u>2006<sup>(4)</sup></u></b>	<b><u>2007<sup>(4)</sup></u></b>	<b><u>2008<sup>(4)</sup></u></b>	<b><u>2009<sup>(4)(5)</sup></u></b>
\$462	\$464	\$489	\$512	\$549	\$565	\$565	\$554

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Notes:

- (1) For 2003 and 2004, results are for the 52-week fiscal period ended on the Saturday closest to March 31.
- (2) Second Cup results were impacted by the power outage that occurred in Ontario in August 2003 and the outbreak of SARS in the Greater Toronto Area in April 2003 through June 2003. The financial results for these periods are reflected in fiscal 2004.
- (3) As a result of a change in its fiscal year-end subsequent to the creation of the Fund, Second Cup changed its year-end from the Saturday closest to March 31 to the Saturday closest to December 31. This number represents average sales for cafés reporting at least 50 weeks of sales in the 52-week period ended January 1, 2005.
- (4) For 2005 onwards, figures are for the 52-week fiscal period ended the last Saturday of December. This number represents average sales figures for cafés reporting at least 50 weeks of sales in the respective 52-week period.
- (5) Second Cup results were impacted by the economic downturn in 2009.

### *Seasonality*

The first quarter represents the lowest average system sales quarter for the year due to the seasonality of the business. The final quarter, which includes the holiday sales periods of November and December in the retail industry, generally constitutes the highest average system sales quarter of the fiscal year.

### ***Advertising and Marketing***

Second Cup's marketing and advertising initiatives are directed toward enhancing the Second Cup brand, promoting new products and driving traffic into cafés. Second Cup strives to create highly relevant and appealing programs that are consistent with the delivery of the "Trusted Coffee Expert" which our customers have come to expect.

Second Cup's marketing program is funded through contributions made by company-owned and franchised cafés to a national co-operative fund, which is administered by Second Cup. All Second Cup cafés are required to remit a fixed percentage of their Gross Revenue (typically 3.0%, depending on the type of café) to this fund. These contributions are used to pay for the development and execution of marketing plans, product research and development, training, in-café improvement initiatives and other programs that benefit the Second Cup system as a whole. Examples of such initiatives include print advertising (magazine and newspaper), outdoor advertising (billboard) and internet marketing. The fund is also applied towards other programs such as Café Card administration.

In addition to contributing to the national co-operative fund, as part of the standard franchise agreement, a franchise partner is required to make expenditures on local advertising and promotion of the café in an amount equal to the greater of 2% of the franchise partner's annual Gross Revenue and the amount required to be expended pursuant to the provisions of the relevant lease relating to the premises.

### ***Purchasing and Distribution***

In order to differentiate its specialty coffee products on the basis of quality, Second Cup has established exacting standards for the sourcing, roasting, packaging, distribution and blending of Second Cup coffee.

### *Sourcing*

Second Cup uses only Arabica coffee beans, which it seeks to buy from the best growers around the globe. Second Cup's green coffee beans are sourced from a diverse set of suppliers in Central America (Costa Rica and Panama), South America (Colombia, Peru and Brazil), Africa (Kenya and Ethiopia) and Indonesia (Sumatra and Java). Management estimates only 1% to 2% of the world's Arabica coffee beans grown each year meet Second Cup's stringent standards for procurement.

Second Cup has spent years developing and nurturing long-term relationships with farmers, co-operatives and processors in order to secure its supply of high quality coffee. These relationships permit Second Cup to offer many coffees on an exclusive basis. One example is La Minita, an estate coffee from Costa Rica regarded by many in the specialty coffee industry as one of the world's finest. Second Cup continuously aims to strengthen its coffee sourcing programs by visiting coffee growing regions on a regular basis, solidifying relationships with suppliers, sharing best practices with growers and finding additional sources of the highest quality coffee.

Second Cup believes that it has developed relationships with a sufficient number of growers to have a secure source of premium coffee beans. However, Second Cup does not enter into long-term or written agreements with its growers. Second Cup also believes that it has established a sufficient number of alternative sources of high quality coffee beans that could be accessed if any coffee currently purchased from existing suppliers became unavailable or economically unviable.

As with all commodities, coffee is subject to fluctuations in price. Second Cup utilizes the services of a major North American coffee & tea company that carries out the purchasing of Second Cup's coffee beans pursuant to a custom coffee processing and distribution agreement described below. Through its agreement with this company, Second Cup typically locks in a portion of its future coffee costs rather than leaving itself exposed to changes in spot prices. By locking in supply costs, Second Cup and its franchise partners can better predict costs and availability of key ingredients.

#### *Roasting, Packaging and Distribution*

As part of its commitment to deliver roaster-fresh, quality products to each café, Second Cup combines the purchase of high quality coffee beans with high standards for roasting, packaging and distribution. Second Cup has the benefit of a custom coffee processing and packaging agreement (the "Coffee Processing Agreement") with one of the largest private label coffee and tea manufacturers in North America under which Second Cup has control over the inventory, roasting, and packaging of its coffee products. The Coffee Processing Agreement enables Second Cup to maintain control of its costs and quality standards while leveraging the manufacturing skills of a third party. Second Cup also has a distribution agreement with a national distribution company which provides Second Cup with access to a national system of warehousing and distribution that affords each café continuous availability of freshly roasted coffee and other products. Furthermore, by virtue of these agreements, Second Cup does not have to invest in production facilities, equipment or working capital and can remain focused on the retail aspect of the business.

#### *Quality Control*

Second Cup believes that it is essential to maintain quality control standards at every step in the purchasing and distribution process in order to meet customer expectations.

Second Cup's quality control procedures begin upon delivery of green coffee beans, when each shipment is inspected and sampled for compliance with specifications prior to being shipped to Second Cup's roasting facility. Once inspected, Second Cup coffees are roasted using a "batch roasting" method. This method calls for roasting comparatively small amounts of beans at any one time to maximize the taste profile of each roast. Batch roasting allows Second Cup to ensure superior coffee quality because of the ability to determine the exact temperature and length of time for its various roasts. In addition, by using a dedicated roasting facility, Second Cup is able to maintain a consistently high standard of coffee beans free of contamination from beans of lower quality used by other coffee producers.

Second Cup also adheres to a strict packaging policy. As is standard in the specialty coffee industry, coffee is packaged in special one-way valve bags, which allow gases emitted by the freshly roasted coffee to escape while preventing air or moisture from entering the bag and causing the coffee to become stale. This contrasts with the majority of non-specialty coffee, which is packaged in tins or brick packs in which the coffee cannot be packaged until after gases cease emission and the staling process commences.

Second Cup has also established quality control standards for the blending of its coffee. For in-café preparation, coffee must be used within four hours of being ground and must be sold according to Second Cup's exacting standards for freshness.

### ***Franchise Operations***

Second Cup is the largest specialty coffee café franchisor in Canada. It views its franchise system as the principal means to successfully enhance and expand the Second Cup brand and café network. As at December 26, 2009, Second Cup had 339 franchise partner developed cafés in operation, owned by a total of approximately 230 different Second Cup franchise partners.

Second Cup's rigorous and systematic franchise partner screening and selection process has been developed to ensure that only candidates with appropriate skill levels, professional experience, financial capital, passion for the business and drive to succeed are selected to become Second Cup franchise partners. Franchise partners go through a pre-screening process that consists of financial and background checks as well as a series of interviews with senior management prior to receiving approval to become a Second Cup franchise partner.

As of December 31, 2009, Second Cup's candidate selection process had yielded a pool of 52 approved candidates to whom Second Cup could offer Second Cup franchises.

Second Cup franchise partners typically invest between \$240,000 and \$400,000 to open a new Second Cup café. They own and operate the Second Cup cafés as independent businesses, licensed under a franchise agreement to use the Second Cup Marks. Second Cup franchise partners are required to devote their full time and attention to the business and to personally play a leadership role in the café's operations.

Second Cup has a proven ability to select, develop, manage and motivate franchise partners to drive long-term growth both within existing cafés and through new café growth. Over the past three decades, Second Cup has developed an operating system that provides each franchise partner with the training, tools and guidance to enable each franchise partner to maximize its business potential. Key components of this system include effective site selection, café design and build out, equipment selection and maintenance programs, "best in class" products and services from suppliers, and innovative product development and category management.

At Second Cup, franchise partners who consistently meet high operational standards are given the opportunity to become franchisees of additional units and are known as "multi-unit" operators. Multi-unit franchising has helped accelerate new café growth and has served as a motivating incentive for single-café franchise partners.

### ***Second Cup Franchise Agreements***

The relationship between Second Cup and each of its franchise partners is governed by a franchise agreement. Although the terms of the franchise agreements entered into with Second Cup franchise partners may differ for certain franchise partners (e.g., Cara Operations Limited and certain non-traditional franchise partners, such as hospitals and universities), they are substantially similar and are summarized below.

Upon execution of a franchise agreement, a Second Cup franchise partner must pay certain fees, including an initial non-refundable franchise fee, which is currently \$40,000. In addition to the initial franchise fee, the franchise partner must pay all expenses incurred in order to fully construct or complete all improvements to the premises to ensure that it is in accordance with Second Cup's standards.

Under the standard Second Cup franchise agreement, a franchise partner pays an ongoing royalty of 9% of the café's Gross Revenue. While there are certain cafés which pay a lower royalty rate, the vast majority of these cafés are located in institutions such as hospitals and educational facilities which typically require less franchisor support. As a result, the overall effective average royalty rate for all Second Cup franchise partners is approximately 8.5%. Royalties are payable in instalments, on or before the 10<sup>th</sup> day immediately following the end of a four-week period determined in accordance with Second Cup's accounting system.

"Gross Revenue" is defined generally in the standard Second Cup franchise agreement to mean the total amount of all sales and other income whatsoever, from whatever source (whether it be of a retail, wholesale or other nature), derived from operating a Second Cup café or any other business activity whatsoever at the Second Cup café, or derived from selling any products from any location, whether or not such amounts are collected and whether payment is made by way of cash, credit or otherwise. Without limiting the generality of the foregoing, Gross Revenue includes:

- All sales made pursuant to telephone, electronic communication or other similarly placed orders;
- The amount of all sales assumed to have been lost by the interruption of the operation of a Second Cup café and which is the basis upon which an insurer has or will pay business interruption insurance;
- All sales made in any part of the shopping mall, building, complex or development in which the Second Cup café is located and/or of which it is a part.

The following is not included in calculating Gross Revenue:

- The amount of any tax imposed by the provincial government of the province within Canada in which the Second Cup café is located, directly on retail sales and collected from customers in their presence at the time of the sale, provided that the amount of any such tax is in fact paid by the operator of the Second Cup café to the provincial government;
- The amount of any sales tax imposed by the federal government of Canada, directly on retail sales and collected from customers in their presence at the time of sale, provided the amount of the sales tax is in fact paid by the operator of the Second Cup café to the federal government of Canada.

In calculating Gross Revenue, the following is deducted:

- The amount of any cash refunded to a customer on account of the return of any products, provided that the amount refunded in respect of such products was originally included in calculating Gross Revenue;
- An exchange of products made between the operator of the Second Cup café and a customer, provided that the amount paid for the products by the customer was originally included in calculating Gross Revenue;
- An amount equal to the value of any discount given to a customer on account of the purchase of any products through the use of a coupon or other similar promotions approved by Second Cup, provided the sale upon which the discount is given was recorded at full value in calculating Gross Revenue.

In calculating Gross Revenue, no allowance whatsoever is made for bad debts. Each sale of products made upon instalment or credit is treated as a sale at the full price at the time such products are ordered, irrespective of the time when the operator of the Second Cup café delivers the products or receives payment for such products.

As part of the standard franchise agreement, a franchise partner is also required to make expenditures on local advertising and promotion of the café in an amount equal to the greater of 2% of the franchise partner's annual Gross Revenue and the amount required to be expended pursuant to the provisions of the relevant lease relating to the premises. In addition to local advertising and promotion, the majority of franchise partners are required to contribute 3.0% of their annual Gross Revenue to Second Cup's national co-operative fund. This fee is payable to Second Cup at the same time as the royalty fee described above. See "Advertising and Marketing" above.

Second Cup typically enters into the head lease for a café location and, in turn, enters into a sublease with the franchise partner concurrently with the entering into of the franchise agreement. Pursuant to the sublease, the franchise partner agrees to observe and perform all of the terms and conditions contained in the head lease. The franchise partner is generally responsible for paying all rent and other amounts to be paid by Second Cup under the head lease in addition to all amounts payable under the franchise agreement, which are deemed to be additional rent owing under the head lease and sublease, entitling Second Cup to the remedies provided for the non-payment of rent. Any default by the franchise partner under the sublease is deemed to be a default under the franchise agreement, allowing Second Cup to terminate the franchise agreement. Similarly, any default by the franchise partner under the franchise agreement is deemed to be a default under the sublease, allowing Second Cup to terminate the sublease.

Aside from the head lease, Second Cup is not obliged to provide any financial covenants or guarantees in connection with a franchise partner's financial arrangements, including with respect to equipment leases and supply purchases. Further, each franchise partner is required to maintain risk insurance in respect of the leased premises and equipment (to their full replacement value), comprehensive general liability insurance, business interruption insurance, insurance required pursuant to the lease of the premises and such other coverage as Second Cup may require from time to time.

Unless terminated earlier by Second Cup in accordance with its terms, the term of each Second Cup franchise agreement commences on execution of the agreement and terminates at the close of business on the day which is one day prior to the earlier of: (i) the date upon which the specific term of the lease governing the occupancy of the premises at the time of entering into of the franchise agreement expires and (ii) the date on which the lease for the premises is terminated. Upon completion of this term, which is typically 10 years, but without execution of a new franchise agreement, a franchise partner may, with the consent of Second Cup, continue to occupy the premises and carry on business as a franchise partner of Second Cup on a calendar month-to-month basis upon the same terms and conditions set out in the original franchise agreement. The Second Cup franchise agreement does not confer on the franchise partner any right of renewal.

The Second Cup franchise agreement permits transfers of a franchise partner's interest in a Second Cup café, subject to Second Cup's consent. In the case of a transfer, a franchise partner is required to pay to Second Cup 10% of the purchase price to be paid by the purchaser. Prior to the completion of the transfer, the purchaser is subject to the same screening process as other new candidates and is required to successfully complete any training that may be required by Second Cup.

### *Franchise Reporting*

In accordance with their franchise agreements, franchise partners are required to provide a Gross Revenue report as well as a cash report on a weekly basis. Within 10 days of the end of each four-week period, franchise partners are required to submit a statement of Gross Revenue which sets out daily Gross Revenue and total Gross



Revenue for such period. Franchise partners are also required to furnish profit and loss statements and various other reports, including completed labour schedules, production reports, purchase records and inventory forms.

In addition to self-reporting by franchise partners, Second Cup's territory managers are required to "score" Second Cup cafés three times per year against an exhaustive list of operational standards to ensure quality and consistency in the chain.

### *Franchise Support Systems*

Second Cup's franchise system is managed by its Chief Operating Officer, who is supported by two regional directors and 12 regional managers, as well as a number of other employees in customer service, training and other operational functions. Second Cup seeks to provide a variety of support services to its franchise partners to assist them in becoming successful operators, including the following:

- *Franchise Partner Selection and Approval* — Second Cup continuously improves upon its systematic approach to the selection of franchise partners. Potential franchise partners, whether they are acquiring cafés from Second Cup or from existing Second Cup franchise partners, are required to go through a series of checks, interviews and hands-on performance evaluations to ensure that the quality of Second Cup's franchise partner base is continuously improving.
- *Real Estate and Development* — Second Cup's real estate and development teams take a lead role in identifying and securing prime development locations for new cafés. This includes market and site analysis and site-specific financial projections, allowing senior management the opportunity to make informed decisions on potential sites prior to franchise partner selection. In addition, the team negotiates with landlords on all new and renewal lease agreements. Second Cup provides full management services (including design, equipment procurement and construction management services) to franchise partners for both the construction of new cafés, as well as the remodelling and upgrading of existing cafés, to ensure that the cafés conform to current design standards.
- *Second Cup School of Business* — Second Cup strongly believes that coffee knowledge and training represent points of meaningful differentiation in the specialty coffee market. Following the decision to join Second Cup's franchise family, franchise partners enrol in Second Cup's School of Business training program. Over a six-week period, franchise partners are given detailed instruction on the management of a Second Cup café, the fundamentals of coffee and the coffee retailing business. The program includes both classroom sessions and in-café instruction.
- *Training and Development* — In addition to the School of Business, training sessions are conducted periodically throughout the year. Second Cup also provides ongoing guidance for franchise partners through regular visits from regional managers, the holding of periodic seminars, workshops and meetings, and by providing an on-line training program to assist franchise partners in properly training their staff. Additionally, in order to promote a deeply rooted understanding of the coffee industry, each operator is required to make an educational trip to Costa Rica upon entering into the franchise agreement, to experience first hand the growing, harvesting and processing of high quality coffee.
- *Café Opening Support* — Second Cup provides a minimum of 12 to 14 days of full time, in-café support for new café openings. A regional manager provides three days of advance planning and training services to the franchise partner and then remains at the café for a full week following the

opening of the café. Furthermore, two one-day follow-up sessions are scheduled 30 and 90 days after the opening of the café to ensure that operating standards are being met.

- *Conventions, Special Events and Franchise Partner Advisory Council* — Second Cup hosts a convention at which franchise partners, management and key suppliers interact and participate in educational sessions, workshops and social activities. In addition, regional meetings are held periodically during the year. Furthermore, Second Cup has established a Franchise Partner Advisory Council that provides management with franchise partner feedback and input into key decision processes. The council is comprised of 11 members elected by the franchise partners and generally meets three times a year to discuss strategy and business objectives with management.
- *I.T. Support Desk* – Second Cup provides technical support services to its franchise partners for cafe cards, debit/credit facilities, cash point of sale systems and wireless internet systems. The Second Cup I.T. help desk operates Monday 9 a.m. – 5 p.m., Tuesday-Friday 8 a.m. - 6 p.m. and Saturday 9 a.m. – 5 p.m. EST.
- *National Marketing and Program Development* — Second Cup is responsible for collecting all contributions from franchise partners to the national co-operative fund, which are then used to advertise the Second Cup brand, promote new and existing products and develop chain-wide programs on behalf of franchise partners.
- *Product Sourcing* — To maintain the quality and consistency of ingredients and products, as well as to ensure that franchise partners obtain favourable pricing, Second Cup establishes product specifications and negotiates supply arrangements with authorized suppliers.
- *Finance and Technology* — Second Cup provides appropriate customized tools and training for franchise partners to manage the financial performance of their cafés and ensure appropriate financial reporting to Second Cup on an ongoing basis. Additional information technology assistance is also provided in the form of standardized point of sale platforms and web-based information systems focused on operational knowledge.

### ***The Second Cup Marks***

MarksLP currently owns the Second Cup Marks, which are trade-marks that are registered or the subject of pending applications for registration under the *Trade-marks Act* (Canada), and other unregistered trade-marks used by Second Cup in connection with its business in Canada. The Second Cup Marks also include the methods, systems and procedures for the operation of Second Cup cafés using certain types of equipment, supplies, ingredients, recipes, merchandising and advertising, and business techniques in Canada.

The Second Cup Marks do not include the rights outside of Canada to any trade-marks or trade names used by Second Cup or any affiliated entities in their business, and in particular they do not include the rights outside of Canada to the trade-marks registered or pending registration under the *Trade-marks Act* (Canada).

The following are some of the Second Cup Marks that are held by MarksLP: Amoureux de Choco\*lattes<sup>®</sup>, Caramel Corretto<sup>®</sup>, Chillatte<sup>®</sup>, Chiller<sup>®</sup>, Chocolat Chaud... Glacé<sup>®</sup>, Chocolate Lovers<sup>®</sup>, Chocolate Lovers' Lattes<sup>®</sup>, Coffee College<sup>®</sup>, Corazon<sup>®</sup>, Crème Brûlée Ristretto<sup>®</sup>, Early Edition Blend<sup>®</sup>, Encanto<sup>®</sup>, For Just a Second<sup>®</sup>, Frrrozen Hot Chocolate<sup>®</sup>, Fruizzi<sup>®</sup>, Icepresso<sup>®</sup>, Icepresso Chiller<sup>®</sup>, Jumpin' Juice<sup>®</sup>, Les Amoureux Du Chocolat<sup>®</sup>, Melange Passion Matin<sup>®</sup>, Mocca Mandarino<sup>®</sup>, Nouvelles Express<sup>®</sup>, Paradiso<sup>®</sup>, Passport<sup>®</sup>, Profitmaker<sup>®</sup>, Rwandan Cup of

Hope<sup>®</sup>, Second Cup<sup>®</sup>, Steamy Monday<sup>®</sup>, Take A Second For Yourself<sup>®</sup>, The Second Cup<sup>®</sup>, The Second Scoop<sup>®</sup>, The Ultimate Coffee Experience<sup>®</sup>, Tiamo<sup>®</sup>, Treat-a-Friend<sup>®</sup>, Trebella<sup>®</sup>, Veneto Blend<sup>®</sup>, What's Brewing<sup>®</sup>, Where The World Stops, White Mocca<sup>®</sup>, and related design marks.

### ***Employees***

As at December 26, 2009, 59 individuals were employed by Second Cup at its head office, as well as an estimated 104 employees in company-owned cafés. Second Cup's employees are not unionized, and Second Cup has never experienced a strike or work stoppage. Second Cup believes that its relations with its employees are very positive.

### ***Government Regulation***

Second Cup and its cafés are subject to the laws and regulations that typically apply to a Canadian foodservice operator. For instance, company-owned and franchised Second Cup cafés are subject to regulation by a number of health, sanitation, safety, fire, building and other agencies or governmental authorities in the provinces or municipalities in which cafés are located. Second Cup must also comply with the laws and regulations adopted in the Provinces of Ontario, Alberta and Prince Edward Island that require certain disclosure to be made with respect to the offer and sale of franchises. These laws require Second Cup to furnish prospective franchise partners located in Ontario, Alberta and Prince Edward Island, as applicable, with a disclosure document containing information prescribed by these laws. In addition, Second Cup and its franchise partners are subject to provincial labour and employment laws that govern their relationship with employees, such as minimum wage requirements, overtime and working conditions.

## **RISK FACTORS**

An investment in the Units involves a number of risks. In addition to the other information contained in this Annual Information Form, investors and prospective investors should give careful consideration to the following factors.

### ***Risks Related to the Business of Second Cup***

#### **The Canadian specialty coffee industry is characterized by intense competition.**

The Canadian specialty coffee industry is intensely competitive with respect to price, location and coffee and food quality. In addition to Second Cup there are two major specialty coffee retailers in Canada, as well as a growing number of smaller, mainly regional, competitors. In addition to competing directly with specialty coffee retailers, Second Cup competes with "mainstream" coffee retailers as well as all restaurants and food service outlets that serve coffee and in particular a national quick services food chain has introduced premium coffee to its menu items. In the whole and ground bean segment of the specialty coffee industry, Second Cup franchise partners will compete against specialty coffee chains as well as supermarkets, many of which have substantially greater financial and other resources than Second Cup franchise partners will have. If Second Cup franchise partners are unable to successfully compete in the Canadian specialty coffee industry, System Sales may be adversely affected.

**General economic conditions and a reduction in discretionary revenue/spending could affect the business.**

The Canadian specialty coffee industry is also affected by changes in discretionary spending patterns, which in turn are dependent on consumer confidence, disposable consumer income and general economic conditions. Factors such as change in general economic conditions, recessionary or inflationary trends, job security and unemployment, equity market levels, consumer credit availability and overall consumer confidence levels may affect the business. Adverse changes to these factors could reduce customer traffic at Second Cup cafés or impose practical limits on pricing, either of which could reduce System Sales. Because the industry's revenues are predominantly derived from the sale of coffee and coffee beverages, changes in consumer preferences which result in decreases in coffee consumption would have an adverse effect on the industry, including Second Cup and the Second Cup franchise partners. The coffee business is also affected by changes in demographic trends, traffic and weather patterns and the type, number and proximity of competing cafés. In addition, factors such as inflation, increased ingredient, raw material, labour and benefit costs and the availability of experienced management and hourly employees may adversely affect the Canadian specialty coffee industry in general and therefore potentially affect Second Cup and the Second Cup franchise partners.

**A shortage in the supply or an increase in the price of premium quality coffee beans could adversely affect Second Cup.**

The success of Second Cup franchise partners to generate System Sales will depend to a large extent upon the availability of premium quality green coffee beans at reasonable prices. The availability and price of premium quality green coffee beans are influenced by several factors that are beyond Second Cup's and Second Cup franchise partners' control, including changes in weather patterns and other natural phenomena, political events or disruptions of shipping and port channels. In addition, green coffee bean prices have been affected in the past, and could be affected in the future, by the actions of governments or organizations which have attempted to influence commodity prices of green coffee beans through agreements establishing export quotas or restricting coffee supplies worldwide. Price increases for green coffee beans could result in increases in the retail price of coffee beverages and other coffee products sold in Second Cup cafés, which could adversely affect System Sales. Similarly, a significant reduction in the availability of coffee beans purchased by Second Cup could have a material adverse effect on System Sales.

Second Cup has no long-term or written contracts with coffee bean suppliers and relies upon historical relationships to ensure availability. While there are a number of coffee bean suppliers, there can be no assurance that coffee bean suppliers that have relationships with Second Cup will continue to supply coffee beans at competitive prices.

**The growth of the café network is dependent on Second Cup's ability to attract qualified franchise partners.**

The growth of the café network is dependent upon the ability of Second Cup to attract qualified franchise partners. The opening and success of Second Cup cafés is dependent on a number of factors, including: availability of suitable sites; negotiations of acceptable leases for new locations; availability, training and retention of management and other employees necessary to staff new Second Cup cafés; adequately supervising construction; and securing suitable financing; among other factors, some of which are beyond the control of Second Cup. Adverse credit markets, such as these currently being experienced, may affect the ability of franchises to obtain new credit or refinance existing credit on economically reasonable terms. Furthermore, Second Cup franchise partners may not have all the business abilities or access to financial resources necessary to successfully develop or operate a Second Cup café. Second Cup provides training and support to its franchise partners, but the quality of franchised operations may be diminished by any number of factors beyond Second Cup's control. There is no assurance that Second Cup franchise partners will successfully operate cafés in a manner consistent with Second Cup's standards and requirements, or hire and train

qualified managers and other personnel. If they do not, the image and reputation of Second Cup may suffer, and System Sales and results of operations of the Second Cup cafés could decline.

**The ability to locate and secure acceptable Second Cup cafés sites may be limited and Second Cup may be required to contribute to the franchise partner lease obligations.**

Second Cup faces competition for café locations and franchise partners from its competitors and from franchisors and operators of other businesses. The success of Second Cup franchise partners is significantly influenced by the location of their cafés. There can be no assurance that current Second Cup café locations will continue to be attractive, or that additional café sites can be located and secured as demographic patterns change. Also, there is no guarantee that the property leases in respect of the Second Cup cafés will be renewed or suitable alternative locations will be obtained and, in such event, one or several cafés could be closed. It is possible that the current locations or economic conditions where Second Cup cafés are located could decline in the future, resulting in potentially reduced sales in those locations, which will have an adverse effect on System Sales. There is no assurance that future sites will produce the same results as past sites. There is also no assurance that a franchise partner will continue to pay its lease obligations in a timely manner which could result in Second Cup being obligated to pay the lease obligations pursuant to its head lease commitment which would adversely affect the profitability of Second Cup's business.

**The closure of Second Cup cafés may affect the profitability of the Second Cup business.**

The profitability of the Second Cup business will depend on System Sales, which will in turn depend on the number of Second Cup cafés that are operating. Each year, a number of Second Cup cafés may close in the normal course and such closures may result in a decrease in the profitability of the Second Cup business as a result of cafe closing costs, ongoing lease obligations incurred by Second Cup under its head lease and unpaid royalty payments owed by the franchise partner at closing.

**Second Cup's ability to generate revenue will depend primarily on the ability of franchise partners to generate Gross Revenue.**

The ability of Second Cup to earn royalties will depend primarily on Second Cup franchise partners' ability to generate Gross Revenue and to pay royalties to Second Cup. Failure to achieve adequate levels of collection from Second Cup franchise partners could have an adverse effect on Second Cup's revenue.

**Franchise partners report Gross Revenue to Second Cup without audit or other form of independent assurance.**

Pursuant to the franchise agreements, franchise partners report Gross Revenue to Second Cup on a weekly basis without audit or other form of independent assurance. Although Second Cup has developed various mechanisms to seek to verify Gross Revenue reported by its franchise partners, Second Cup does not have a centralized accounting system in place to monitor such Gross Revenue. Second Cup seeks to substantiate Gross Revenue reported by its franchise partners through, among other things, analytical and financial reviews performed by management, on site visits, and analysis of raw material purchases by the cafés. Furthermore, audits are performed at random by an internal audit team on cafés throughout the network. There can be no assurance, however, that Gross Revenue reported by franchise partners is accurate and in accordance with the terms of the franchise agreements.

**The loss of key personnel could have a material impact on Second Cup's operations.**

The success of Second Cup will depend on the efforts of key personnel to retain and attract appropriate franchise partner candidates and locate new café sites in order to continue to successfully grow Second Cup's business

and thereby increase System Sales. The loss of the services of such key personnel could have an adverse effect on the operations of Second Cup. If such key personnel depart Second Cup and subsequently compete with Second Cup or devote significantly more time to other business interests, such activities could have a material adverse effect on Second Cup's ability to conduct its business, maintain existing franchises, generate new franchises and locate new café sites.

**The failure to enforce or maintain, or a successful challenge to, the Second Cup Marks may have an adverse impact on the Second Cup business.**

The ability of Second Cup to maintain or increase its System Sales will depend on its ability to capitalize on the Second Cup brand. A failure to enforce or maintain any of Second Cup's intellectual property rights may result in Second Cup being unable to capitalize on its efforts to utilize its brand equity. In addition, if any Second Cup Marks are ever successfully challenged, this may have an adverse impact on System Sales.

The Fund indirectly owns the Second Cup Marks in Canada. It does not own identical or similar trade-marks relating to the Second Cup business in other jurisdictions. Third parties may use such trade-marks in jurisdictions other than Canada in a manner that diminishes the value of such trade-marks. If this occurs, the value of the Second Cup Marks may suffer and System Sales could decline. Similarly, negative publicity or events associated with such trade-marks in jurisdictions outside of Canada may negatively affect the image and reputation of Second Cup cafés in Canada, resulting in a decline in System Sales.

**Changes in or failure to comply with government regulation could have an adverse effect on Second Cup.**

Second Cup franchise partners will be subject to various federal, provincial and local laws affecting their business. Each Second Cup café is subject to licensing and regulation by a number of governmental authorities, which may regulate among other things, food inspection, health, employee and public safety, zoning, smoking laws and fire prevention. Difficulties in obtaining or failures to obtain the required licences or approvals could delay or prevent the development of a new Second Cup café in a particular area. In addition, changes in laws and regulations to which Second Cup and its franchise partners are currently subject may have an adverse effect on System Sales. The loss of a licence or approval, or a violation of laws, could force the temporary or permanent shut down of a Second Cup café, which could adversely affect System Sales.

**Potential litigation and other complaints could adversely affect System Sales.**

Second Cup franchise partners may be the subject of complaints or litigation from customers alleging food related illness, injuries suffered on the premises or other food quality, health or operational concerns. Adverse publicity resulting from such allegations may adversely affect the Gross Revenue of Second Cup cafés, regardless of whether such allegations are true or whether Second Cup or the Second Cup franchise partner is ultimately held liable. In addition, due to the nature of its business, Second Cup may from time to time be involved in litigation with past and existing franchise partners, suppliers and other third parties. Although historically Second Cup's involvement in such litigation has been rare and has not been material to the operation of the business of Second Cup, litigation is expensive, time consuming and may divert management's attention away from the operation of the business. Management cannot be certain that a substantial claim may not arise that would be material to the operations of Second Cup.

### ***Risk Related to the Structure of the Fund***

#### **The cash distributions to Unitholders are not guaranteed and will depend on the performance of the Second Cup business.**

The cash distributions made to Unitholders are not guaranteed and will be dependent on the performance of the Second Cup business. Second Cup collects royalties, franchise fees and other amounts from Second Cup franchise partners and also generates revenues from its company-owned cafés. In the conduct of its business, Second Cup pays expenses and incurs debt and obligations to third parties. These expenses, debts and obligations could impact the ability of the Fund to pay distributions.

In addition, the growth of the café network is dependant upon investments made by Second Cup to select new locations, enter into new leases and recruit, train and supervise franchises.

#### **The Units do not represent a direct investment in the Second Cup business.**

Securities such as the Units are hybrids in that they share certain attributes common to both equity securities and debt instruments. The Units do not represent a direct investment in the Second Cup business and should not be viewed by investors as units in MarksLP or shares of Second Cup. As holders of Units, Unitholders will not have the statutory rights normally associated with ownership of shares of a corporation including, for example, the right to bring “oppression” or “derivative” actions. The Units represent a fractional interest in the Fund. The price per Unit will be a function of anticipated distributable cash.

#### **Changes to the taxation of income trusts.**

On October 31, 2006, the Federal Government announced proposed changes to income taxes, which were then introduced as part of the 2007 federal budget and received royal assent on June 22, 2007. These changes significantly alter the income tax treatment of most publicly traded income trusts and the distributions from these entities to their unitholders. Under these new tax laws (referred to as the “SIFT Rules”), certain income earned by these entities, known as specified investment flow through entities (each a “SIFT”), will be taxed in a manner similar to income earned by a corporation and distributions or allocations made by these entities to unitholders will be taxed similar to dividends from taxable Canadian corporations. The deemed dividends will be eligible for the new enhanced dividend tax credit if paid or allocated to a resident of Canada. These new tax laws will apply to the Fund commencing 2011.

#### **The Fund may issue additional Units diluting existing Unitholders’ interests.**

The Declaration of Trust authorizes the Fund to issue an unlimited number of Units for such consideration and on such terms and conditions as shall be established by the Fund’s trustees without the approval of any Unitholders. Any subsequent issuances of Units by the Fund may dilute the interests of existing Unitholders.

#### **An investment in Units is subject to certain income tax considerations.**

Although the Fund is of the view, and MarksLP is of the view, that all expenses to be claimed by the Fund or MarksLP in the determination of their respective incomes under the Tax Act will be reasonable and deductible in accordance with the applicable provisions of the Tax Act, there can be no assurance that the Tax Act or the

interpretation of the Tax Act will not change, or that the Canada Revenue Agency will agree with the expenses claimed.

Where Units are issued to Unitholders in lieu of cash distributions, Unitholders will generally be required to include an amount equal to the fair market value of those Units into their taxable income, in circumstances when they do not directly receive a cash distribution.

**There is no assurance of the Units' continued investment eligibility.**

There can be no assurance that the Units will continue to be qualified investments for Deferred Income Plans and registered education savings plans under the Tax Act. The Tax Act imposes penalties for the acquisition or holding of non-qualified or ineligible investments.

**Distribution of securities on redemption of Units or termination of the Fund may result in Unitholders holding illiquid securities.**

Upon a redemption of Units or termination of the Fund, the trustees may distribute MarksLP units held by the Fund or the Fund's other assets directly to the Unitholders, subject to obtaining all required regulatory approvals. There is currently no market for the MarksLP units. In addition, MarksLP units are not freely tradable and are not currently listed on any stock exchange. Securities of MarksLP so distributed may not be qualified investments for trusts governed by Deferred Income Plans and registered education savings plans, depending upon the circumstances at the time.

**The Fund has outstanding indebtedness.**

The Fund will have third-party debt service obligations under the Fund Term Loan and the Fund Operating Loan. See "General Development of the Business — Fund Term Loan and Fund Operating Loan". The degree to which the Fund is leveraged could have important consequences to the holders of the Units, including: (i) a portion of the Fund's cash flow from operations will be dedicated to the payment of the principal and interest on its indebtedness, thereby reducing funds available for distribution to the Fund; and (ii) certain of the Fund's borrowings will be at variable rates of interest, which exposes the Fund to the risk of increased interest rates. The Fund's ability to make scheduled payments of the principal of, or interest on, or to refinance, its indebtedness will depend on the profitability of Second Cup. The Fund Term Loan is due January 2, 2011. The Fund Term Loan and the Fund Operating Loan bear interest at prime rate plus 2.5% or bankers' acceptances plus 3.5%. The Fund has in place an interest rate swap arrangement fixing the interest rate on Fund Term Loan at an estimated effective rate of 6.41%. Current and future borrowings by Second Cup could adversely affect its performance.

The Fund Term Loan and Fund Operating Loan contain numerous restrictive covenants that limit the discretion of the Fund with respect to certain business matters. In certain circumstances, these restrictive covenants may restrict the cash available for distribution to Unitholders.

## **DESCRIPTION OF THE FUND**

### ***Declaration of Trust***

The Fund is an open-ended trust established under the laws of the Province of Ontario pursuant to the Declaration of Trust. The Fund currently qualifies as a mutual fund trust for the purposes of the Tax Act. The following is a summary of the material attributes and characteristics of the Units and certain provisions of the



Declaration of Trust, which does not purport to be complete. Reference is made to the Declaration of Trust for a complete description of the Units and the full text of its provisions. See “Material Contracts”.

### ***Activities of the Fund***

The Declaration of Trust provides that the Fund is restricted to:

- (a) investing in or acquiring or disposing of securities, including those issued by MarksLP and its affiliated entities;
- (b) temporarily holding cash in interest-bearing accounts, short-term government debt or investment grade corporate debt for the purposes of paying the Fund’s expenses, paying amounts payable by the Fund in connection with the redemption of any Units and making distributions to Unitholders;
- (c) issuing Units (or rights, warrants, convertible or exchangeable securities, subscription receipts or options in respect thereof) pursuant to the Declaration of Trust;
- (d) issuing debt securities or borrowing funds (including by way of letters of credit, bank guarantees and bankers’ acceptances);
- (e) guaranteeing (including as guarantor, surety or co-obligor) the payment or performance of any indebtedness, liability or other obligation of MarksLP or its affiliated entities and granting security interests in or otherwise encumbering, pledging (provided that doing so would not affect the redemption rights of Unitholders), mortgaging or charging any or all of the Fund’s assets for those obligations, and where considered appropriate, postponing or subordinating its rights under indebtedness or other obligations;
- (f) issuing or redeeming rights to acquire Units pursuant to any Unitholder rights plan adopted by the Fund;
- (g) redeeming or repurchasing securities of the Fund;
- (h) entering into and performing its obligations under certain agreements listed in the Declaration of Trust; and
- (i) undertaking such other activities, or taking such actions, including investing in securities, as are related to or in connection with the foregoing or as are contemplated by the Declaration of Trust or as may otherwise be approved by the trustees of the Fund from time to time,

provided that the Fund will not undertake any activity, take any action, or make any investment which would result in the Fund not being considered a “mutual fund trust” for purposes of the Tax Act or which would result in the Units being “foreign property” for the purposes of the Tax Act.

As at the date of this Annual Information Form, the Fund does not intend to hold (directly or indirectly) securities of entities other than MarksLP, GP Inc. GP Trust and Second Cup, other than cash equivalents referred to in (b) above.

## ***Description of Units***

The beneficial interests in the Fund are designated as “Units”, which are entitled to the rights and subject to the limitations, restrictions and conditions set out in the Declaration of Trust, the terms of which are summarized below.

An unlimited number of Units may be created and issued pursuant to the Declaration of Trust. Each Unit is transferable and represents an equal undivided beneficial interest in any of the Fund’s distributions, whether of net income, net realized capital gains or other amounts, and in the Fund’s net assets in the event of the Fund’s termination or winding-up.

All Units have equal rights and privileges and are not subject to future calls or assessments. Except as set out under “Redemption Right” below, the Units have no conversion, retraction, redemption or pre-emptive rights.

On December 16, 2004, the *Trust Beneficiaries’ Liabilities Act, 2004* (Ontario) came into force. This statute provides that holders of units of a trust are not, as beneficiaries, liable for any act, default, obligation or liability of the trust if, when the act or default occurs or the liability arises, (i) the trust is a reporting issuer under the Securities Act, and (ii) the trust is governed by the laws of Ontario. The Fund is a reporting issuer under the Securities Act and is governed by the laws of Ontario by virtue of the provisions of its declaration of trust.

No certificates may be issued for fractional Units and fractional Units will not entitle holders to vote in respect of those fractional Units. The Units are not “deposits” within the meaning of the *Canada Deposit Insurance Corporation Act* (Canada) and are not insured under the provisions of such act or any other legislation. Furthermore, the Fund is not a trust company, and accordingly, the Fund is not registered under any trust and loan company legislation as it does not carry on or intend to carry on the business of a trust company.

## ***Issuance of Units***

The Declaration of Trust provides that the Units or rights to acquire Units may be allotted and issued at the times, to the persons, for the consideration and on the terms and conditions that the trustees of the Fund determine. Units may be issued in satisfaction of any non-cash distribution by the Fund to Unitholders on a *pro rata* basis (subject to possible escrow and resale arrangements for non-Canadian residents). The Declaration of Trust also provides that, immediately after any *pro rata* distribution of Units to all Unitholders in satisfaction of any non-cash distribution, the number of outstanding Units will be consolidated such that each Canadian resident Unitholder will hold after the consolidation the same number of Units as the Unitholder held before the non-cash distribution. In this case, each Unit certificate representing a number of Units prior to the non-cash distribution will be deemed to represent the same number of Units after the non-cash distribution and the consolidation. Non-Canadian resident Unitholders will also have their Units consolidated but may be subject to withholding tax.

## ***Trustees***

The Fund may have a minimum of three trustees and a maximum of 10 trustees. The Declaration of Trust prohibits a non-resident of Canada (as that term is defined in the Tax Act) from acting as a trustee. The trustees of the Fund are to supervise the Fund’s activities and manage the Fund’s affairs.

The Fund currently has five trustees, each of whom also serves as a director of Second Cup. See “Trustees, Directors and Management”.

Trustees are to be appointed at each annual meeting of Unitholders to hold office for a term expiring at the close of the next annual meeting. A majority of trustees of the Fund are required at all times to be “independent” within the meaning of Multilateral Instrument 52-110 — *Audit Committees*. Messrs. Guyatt, Rosicki and Ms. Goldberg are considered by the Fund to be “independent” within the meaning of such instrument.

Any one or more of the trustees may resign upon prior written notice and may be removed by a resolution passed by a majority of the Unitholders. Any vacancy created by such removal or resignation must be filled at the same meeting, failing which it may be filled by the remaining trustees of the Fund.

A quorum of trustees, being a majority of trustees then holding office, may fill a vacancy in the board of trustees, except a vacancy resulting from an increase in the maximum number of trustees beyond the limit described below or from a failure of the Unitholders to appoint the minimum number of trustees at a meeting of the Unitholders called for such purpose. In the absence of a quorum of trustees or if the vacancy has arisen from a failure of the Unitholders to appoint the minimum number of trustees at a meeting of the Unitholders called for such purpose, the trustees then holding office will be required to call forthwith a special meeting of the Unitholders to fill the vacancy. If the trustees fail to call such meeting or if there are not any trustees then in office, any Unitholder may call such a special meeting. If a meeting of Unitholders fails to appoint the minimum number of trustees by reason of the disqualification or death of any nominee, the trustees appointed at the meeting may exercise all of the powers of the trustees if the appointed number of trustees constitutes a quorum.

The trustees of the Fund may, between annual meetings of Unitholders, appoint one or more additional trustees to serve until the next annual meeting of Unitholders, but the number of additional trustees will not at any time exceed one third of the number of trustees who held office at the expiration of the immediately preceding annual meeting of Unitholders.

The Declaration of Trust provides that, subject to the terms and conditions thereof, the trustees may, in respect of the assets of the Fund, exercise any and all rights, powers and privileges that could be exercised by a legal and beneficial owner of those assets. The role of the trustees includes, among other things:

- acting for the Fund, voting on the Fund’s behalf and representing the Fund as a Unitholder and noteholder of MarksLP, and as a shareholder of GP Inc., including voting for the election of directors of GP Inc.;
- maintaining records and providing reports to Unitholders;
- supervising the activities of the Fund, including the investments of the Fund; and
- effecting payments of distributions from the Fund to Unitholders.

The trustees will also supervise the application of the Fund’s written corporate disclosure and insider trading policies. These policies will, among other things:

- articulate the legal obligations of the Fund, its affiliates and their respective trustees, directors, officers and employees with respect to confidential information;

- identify spokespersons of the Fund who are authorized to communicate with third parties such as analysts, the media and investors;
- provide guidelines on the disclosure of forward-looking information;
- require advance review of any disclosure of financial information with a view to ensuring that selective disclosure of material information does not occur; and
- establish “black-out” periods immediately prior to and following the disclosure of quarterly and annual financial results during which the Fund, its affiliates and their respective trustees, directors, officers and certain other persons may not purchase or sell Units in the market.

The Declaration of Trust provides that the trustees of the Fund will act honestly and in good faith with a view to the best interests of the Fund and in connection therewith will exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances. The duties and standard of care of the trustees are intended to be similar to, and not any greater than, those imposed on a director of a corporation governed by the *Business Corporations Act* (Ontario). The Declaration of Trust provides that the trustees will be entitled to indemnification from the Fund in respect of the exercise of their powers and the discharge of their duties provided that they acted honestly and in good faith with a view to the best interests of the Fund. In the case of a criminal or administrative action or proceeding that is enforced by a monetary penalty, a trustee will be entitled to indemnification from the Fund provided that he or she had reasonable grounds for believing that his or her conduct was lawful.

The trustees and executive officers of the Fund and its subsidiaries as a group beneficially own, directly or indirectly, or exercise control or direction over, an aggregate of 68,450 units of the Fund, representing 0.7% of the issued and outstanding Units as of March 30, 2010.

### ***Audit Committee***

As required by applicable securities laws, the Fund has established an audit committee to monitor the Fund’s financial reporting, accounting systems and internal controls, and to liaise with the Fund’s external auditors. The audit committee is required to consist of at least three trustees, each of whom must be “independent” within the meaning of Multilateral Instrument 52-110 — *Audit Committees*, subject to the provisions of such instrument. The Chair of the audit committee receives compensation of \$5,000 per year for such role.

#### *Charter of the Audit Committee*

The charter of the audit committee is attached to this Annual Information Form as Schedule A.

#### *Composition of the Audit Committee*

Presently, the audit committee consists of Messrs. Guyatt, Rosicki and Ms. Goldberg and is chaired by Mr. Guyatt. All members of the audit committee are independent and financially literate, as such terms are defined under Multilateral Instrument 52-110 – *Audit Committees*. See “Trustees, Directors and Management” for a summary of the education and experience of each member of the audit committee.

#### *Pre-approval Policies and Procedures*

There have been no recommendations of the audit committee to nominate or compensate an external auditor which have not been adopted by the board of trustees of the Fund. In accordance with the Fund’s audit committee

charter, all non-audit services to be provided to the Fund or any of its affiliates by the external auditors or any of their affiliates are subject to pre-approval by the audit committee. The committee may approve policies and procedures for the pre-approval of non-audit services to be rendered by the external auditors, which policies and procedures (i) shall include reasonable detail with respect to the services covered, (ii) shall require that the committee be informed of each non-audit service and (iii) shall not include delegation of the committee's responsibilities to management of MarksLP.

#### *Audit Fees*

PricewaterhouseCoopers LLP has served as the Fund's auditing firm since the Fund's inception in 2004. Fees paid or payable for the years ended December 26, 2009, December 27, 2008, and December 29, 2007, to PricewaterhouseCoopers LLP are \$229,000, \$77,150, and \$192,000, respectively. These fees are detailed below:

	<b>Year ended December 31, 2009</b>	<b>Year ended December 31, 2008</b>	<b>Year ended December 31, 2007</b>
Audit fees	\$174,000	\$42,000	\$42,000
Audit-related fees	\$4,000	\$9,000	\$8,000
Tax fees	\$51,000	\$26,000	\$30,000
All other fees	\$0	\$0	\$112,000
	<b>\$229,000 <sup>(1)</sup></b>	<b>\$77,000</b>	<b>\$192,000</b>

Note:

(1) The increase in fees in 2009 represents the Second Cup audit fees which the Fund is responsible for, subsequent to its acquisition of Second Cup on June 27, 2009. A portion of the fees (\$42,000) represents a one-time charge, relating to the acquisition of Second Cup.

The nature of each category of fees is described below.

Audit and audit related fees: Audit fees and audit related fees were paid for professional services rendered for the audit of the Fund's annual financial statements, reading of the Fund's quarterly reporting, and for services that are normally provided in connection with the statutory and regulatory filings or engagements.

Tax Fees: Tax fees were paid for professional services rendered for the preparing of the Fund's annual income tax returns and advice associated therewith.

All other fees: Other fees were paid for professional services rendered with respect to assistance with compliance with new accounting standards effective in fiscal years 2007, 2008 and 2009.

#### *Cash Distributions*

The amount of cash to be distributed per month per Unit to the Unitholders of the Fund will be equal to a *pro rata* share of distributions from MarksLP to the Fund, less amounts which are paid, payable, incurred or provided for in such period in connection with:

- the Fund's administrative expenses and other obligations and liabilities;
- amounts which may be paid by the Fund in connection with any cash redemptions of Units;
- satisfaction of the Fund's debt service obligations, if any; and

- such reasonable reserves as may be established by the trustees of the Fund in their sole discretion, which are currently expected to be nominal.

The trustees may authorize increased or decreased distributions in excess of or below the aforementioned distributions from time to time or suspend distributions entirely, as they see fit, in their sole discretion.

The Fund intends to make distributions each month of amounts determined by the trustees in their sole discretion to be available for distribution by the Fund for such month. If declared, distributions in respect of each month are expected to be paid on the last day of the immediately following month to Unitholders of record as of record dates to be specified (except in respect of the month of December, for which the record date will be the last day of December). Substantially all distributions will be considered income of the Unitholder for Canadian tax purposes.

The following table sets forth the month of payment, record date, payment date and distribution per Unit paid by the Fund on the Units for each month of the 2007, 2008 and 2009 fiscal years:

	<u>Period</u>	<u>Record Date</u>	<u>Payment Date</u>	<u>Distribution Per Unit</u>
2007	January 2007	February 26, 2007	February 28, 2007	\$0.0867
	February 2007	March 28, 2007	March 30, 2007	\$0.0910
	March 2007	April 27, 2007	April 30, 2007	\$0.0910
	April 2007	May 29, 2007	May 31, 2007	\$0.0910
	May 2007	June 27, 2007	June 29, 2007	\$0.0910
	June 2007	July 27, 2007	July 31, 2007	\$0.0910
	July 2007	August 29, 2007	August 31, 2007	\$0.0910
	August 2007	September 26, 2007	September 28, 2007	\$0.0910
	September 2007	October 29, 2007	October 31, 2007	\$0.0910
	October 2007	November 28, 2007	November 30, 2007	\$0.0910
	November 2007	December 27, 2007	December 31, 2007	\$0.0910
	December 2007	December 31, 2007	January 31, 2008	\$0.0910
2008	January 2008	February 27, 2008	February 29, 2008	\$0.0910
	February 2008	March 28, 2008	March 31, 2008	\$0.0940
	March 2008	April 29, 2008	April 30, 2008	\$0.0940
	April 2008	May 28, 2008	May 30, 2008	\$0.0940
	May 2008	June 27, 2008	June 30, 2008	\$0.0940
	June 2008	July 29, 2008	July 31, 2008	\$0.0940
	July 2008	August 27, 2008	August 29, 2008	\$0.0940
	August 2008	September 26, 2008	September 30, 2008	\$0.0940
	September 2008	October 29, 2008	October 31, 2008	\$0.0940
	October 2008	November 26, 2008	November 28, 2008	\$0.0940
	November 2008	December 29, 2008	December 31, 2008	\$0.0940
	December 2008	December 31, 2008	January 30, 2009	\$0.0940
2009	January 2009	February 25, 2009	February 27, 2009	\$0.0940
	February 2009	March 27, 2009	March 31, 2009	\$0.0940
	March 2009	April 28, 2009	April 30, 2009	\$0.0767

April 2009	May 27, 2009	May 29, 2009	\$0.0767
May 2009	June 26, 2009	June 30, 2009	\$0.0767
June 2009	July 29, 2009	July 31, 2009	\$0.0767
July 2009	August 28, 2009	August 31, 2009	\$0.0767
August 2009	September 28, 2009	September 30, 2009	\$0.0767
September 2009	October 28, 2009	October 30, 2009	\$0.0767
October 2009	November 26, 2009	November 30, 2009	\$0.0767
November 2009	December 29, 2009	December 31, 2009	\$0.0767
December 2009	December 31, 2009	January 29, 2009	\$0.0767

In addition to monthly distributions, it is provided in the Declaration of Trust that the Fund will make a final year-end distribution each year payable in cash or Units to Unitholders of the Fund of record on December 31, in the amount by which the Fund's income (including net taxable capital gains, if any, but excluding the tax paid or made payable on which may be offset by capital losses carried forward from prior years or is recoverable by the Fund) for the purposes of the Tax Act (plus the non-taxable portion of capital gains, if any) for the year would otherwise exceed distributions already paid or payable to Unitholders of the Fund in that year. The Unitholders will have a legal right to enforce such payment on December 31 of each year. Such year-end distribution is expected to be paid to such Unitholders of the Fund on or before January 31 of the immediately following year. For the year-ended December 31, 2009, no such year-end distribution was required due to significant tax deductions available to the Fund resulting from expenses incurred in connection with the Fund's initial public offering.

To the extent that cash of the Fund is used to redeem Units or is otherwise unavailable to satisfy distributions, the Fund will satisfy distributions to Unitholders in the form of additional Units. Such additional Units are expected to be issued pursuant to available exemptions under applicable securities laws, discretionary exemptions granted by applicable securities regulatory authorities or a prospectus or similar filing.

Unitholders who are non-residents of Canada (as that term is defined in the Tax Act) may be subject to withholding taxes payable in respect of distributions by the Fund, whether such distributions are in the form of cash or additional Units. Non-residents should consult their own tax advisors regarding the tax consequences of investing in the Units. Additional Units otherwise issuable to non-residents of Canada may in certain cases also be escrowed and resold on their behalf.

### ***Redemption Right***

Units are redeemable at any time on demand by their holders. As the Units will only be issued in book-entry form, a Unitholder who wishes to exercise the redemption right will be required to obtain a redemption notice form from the Unitholder's investment dealer, and cause the dealer to deliver the completed redemption notice form to CDS. Upon the Fund's receipt of the redemption notice, all rights to and under the Units tendered for redemption will be surrendered and the holder thereof will be entitled to receive a price per unit (the "Redemption Price") equal to the lesser of:

- 90% of the Market Price (as defined below) of the Units on the principal marketplace on which they are traded during the 10 trading day period immediately preceding the date on which the applicable Units were surrendered for redemption (the "Unit Redemption Date"); and
- 100% of the Closing Market Price (as defined below) of the Units on the principal marketplace on which they are traded on the Unit Redemption Date.

For the purposes of these calculations, the “Market Price” will be the amount equal to the weighted average of all reported trading prices of the Units on the applicable marketplace for each of the trading days on which there was a trade during the specified trading day period; provided that if there was trading in the Units on the applicable marketplace for fewer than five of the trading days during the specified trading day period, the “Market Price” will be the weighted average of the following prices established for each of the trading days during the specified trading period: (a) the average of the last bid and asking prices of the Units for each trading day on which there was no trading and (b) the weighted average reported trading prices of the Units for each trading day that there was trading.

For the purposes of these calculations, the “Closing Market Price” will be: (a) an amount equal to the closing price of the Units on the applicable marketplace if there was a trade on the specified date and the applicable marketplace provides a closing price; (b) an amount equal to the average of the highest and lowest prices of Units on the applicable marketplace if there was trading on the specified date and the applicable marketplace provides only the highest and lowest trading prices of Units on a particular day; or (c) the average of the last bid and last asking prices on the applicable marketplace if there was no trading on the specified date.

The aggregate Redemption Price payable by the Fund in respect of any Units surrendered for redemption during any calendar month will, except in the circumstances described below, be satisfied by way of a cash payment by the Fund. This cash payment will be made no later than the last day of the month following the month in which the Units were tendered for redemption. Unitholders will not be entitled to receive cash upon the redemption of their Units if:

- the total amount payable by the Fund in respect of such Units and all other Units tendered for redemption in the same calendar month exceeds \$50,000 (the “Monthly Limit”), provided that the trustees may, in their sole discretion, waive this limitation in respect of all Units tendered for redemption in any calendar month;
- at the time such Units are tendered for redemption, the outstanding Units are not listed or quoted for trading on the Toronto Stock Exchange or another stock exchange or organized market which the trustees consider to be, in their sole discretion, one which provides representative fair market value prices for the Units; or
- the normal trading of Units is suspended or halted on any stock exchange or organized market on which the Units are listed or quoted for trading on the Unit Redemption Date or for more than five trading days during the 10-day trading period commencing immediately after the Unit Redemption Date.

If a Unitholder is not entitled to receive cash upon the redemption of Units as a result of the last two limitations above, the redemption price will be equal to the fair market value of the Units as determined by the trustees in their sole discretion, and the redemption price for each Unit tendered for redemption will, subject to obtaining all applicable regulatory approvals, be paid and satisfied by way of a distribution *in specie* by the Fund of securities of any subsidiary of the Fund. The aggregate fair market value of the securities of any subsidiary of the Fund being distributed shall be equal to the product of the redemption price per Unit payable by the Fund and the number of Units tendered.

If a Unitholder is not entitled to receive cash upon the redemption of Units as a result of the first limitation described above, the Unitholder will receive a cash payment equal to such Unitholder’s *pro rata* share of the Monthly Limit based on the aggregate number of Units tendered for redemption in the applicable calendar month and, subject to obtaining all applicable regulatory approvals, the balance in securities of any subsidiary of the Fund determined in accordance with the procedures described above.



It is anticipated that the redemption right described above will not be the primary mechanism for Unitholders to dispose of their Units. Securities of any subsidiary of the Fund which may be distributed *in specie* to Unitholders in connection with a redemption will not be listed on any stock exchange, no market is expected to develop for those notes and they may be subject to an indefinite “hold period” or other resale restrictions under applicable securities laws. Securities of any subsidiary of the Fund so distributed may be qualified investments for Deferred Income Plans and registered education savings plans, depending upon the circumstances at the time.

The Fund will be allowed, from time to time, to purchase Units for cancellation in accordance with applicable securities laws and the rules prescribed under applicable stock exchanges or regulatory policies.

### ***Meetings of Unitholders***

Each Unit entitles the holder thereof to one vote at all meetings of the Unitholders. Meetings of Unitholders will be called and held annually for (i) the election of trustees; (ii) the appointment of auditors of the Fund for the ensuing year, (iii) generally, any other matter that requires a resolution of Unitholders and (iv) transacting such other business as the trustees may determine or as may be properly brought before the meeting. The Declaration of Trust provides that the Unitholders will be entitled to pass resolutions that will bind the Fund only with respect to (and that such actions may not occur without the passing of such resolutions):

- the election or removal of trustees of the Fund;
- the appointment or removal of the auditors of the Fund;
- the appointment of an inspector to investigate the performance by the trustees of their responsibilities and duties;
- the approval of amendments to the Declaration of Trust (except as described under “Amendments to the Declaration of Trust” below);
- the sale, lease or exchange of all or substantially all of the Fund’s assets, except in conjunction with an internal reorganization or an *in specie* redemption of Units by the Fund;
- any amalgamation, arrangement, other merger or capital reorganization of the Fund with any other entity, except in conjunction with an internal reorganization;
- the exercise of certain voting rights attached to the securities of any subsidiary of the Fund held directly or indirectly by the Fund;
- the termination, winding-up or dissolution of the Fund prior to the end of its term; and
- such other business as the trustees may determine or as may be properly brought before a meeting.

A resolution appointing or removing the trustees or the auditors of the Fund must be passed by a simple majority of the votes cast by the Unitholders. All other matters must be approved by a Unitholders’ Special Resolution.

A meeting of Unitholders may be convened at any time and for any purpose by the trustees and must be convened if requisitioned by the holders of not less than 10% of the Units then outstanding by a written requisition. A requisition must state in reasonable detail the business proposed to be transacted at the meeting.

Unitholders may attend and vote at all meetings of Unitholders of the Fund either in person or by proxy and a proxy holder need not be a Unitholder. Two persons present in person or represented by proxy and representing in the aggregate at least 10% of the votes attached to all outstanding Units will constitute a quorum for the transaction of business at all such meetings. The Declaration of Trust contains provisions as to the notice required and other procedures with respect to the calling and holding of meetings of Unitholders. If no quorum is present, the meeting may (unless it was a requisitioned meeting) be adjourned to a date that is not less than seven days later by notice given by news release and at the adjourned meeting all those Unitholders of the Fund present will constitute a quorum.

### ***Limitation on Non-Resident Ownership***

In order for the Fund to maintain its status as a mutual fund trust under the Tax Act, the Fund must not be established or maintained primarily for the benefit of non-residents of Canada within the meaning of the Tax Act and pursuant to certain proposed amendments to the Tax Act, not more than 50% of the fair market value of the Units may be held by non-residents of Canada and/or partnerships (other than Canadian partnerships as defined in the Tax Act). Accordingly, the Declaration of Trust provides that at no time may non-residents of Canada and/or partnerships other than Canadian partnerships be the beneficial owners of more than 40% of the Units. The trustees may require declarations as to the jurisdictions in which beneficial owners of Units are resident or as to their status as Canadian partnerships.

If the trustees become aware that the beneficial owners of 40% of the Units then outstanding are or may be non-residents and/or partnerships other than Canadian partnerships or that such a situation is imminent, the trustees may direct the transfer agent and registrar to make a public announcement thereof and will not accept a subscription for Units from or issue or register a transfer of Units to any person unless the person provides a declaration that he or she is not a non-resident or a partnership other than a Canadian partnership. If, notwithstanding the foregoing, the trustees determine that more than 40% of the Units are held by non-residents and/or partnerships other than Canadian partnerships, they may direct the transfer agent of the Units to send a notice to such holders of Units, chosen in inverse order to the order of acquisition or registration or in such manner as the trustee may consider equitable and practicable, requiring them to sell their Units or a portion thereof within a specified period determined by the trustees. If the Unitholders receiving such notice have not sold the specified number of Units or provided the trustees with satisfactory evidence that they are not non-residents or a partnership other than a Canadian partnership within such period, the trustees may direct the transfer agent to sell such Units on behalf of such Unitholders, and in the interim, the voting and distribution rights attached to such Units will be suspended. Upon such sale, the affected holders will cease to be holders of the Units and their rights will be limited to receiving the net proceeds of such sale.

On September 16, 2004, the Minister of Finance (Canada) released draft amendments to the Tax Act relating to the circumstances under which the ownership of units of a trust by non-resident persons and partnerships other than Canadian partnerships would cause the trust to lose its status as a mutual fund trust. Under the draft amendments, a trust would lose its status as a mutual fund trust if the aggregate fair market value of all units issued by the trust held by one or more non-resident persons or partnerships that are not Canadian partnerships is more than 50% of the aggregate fair market value of all the units issued by the trust. The draft amendments do not currently provide any means of rectifying a loss of mutual fund trust status such that if, at any time, the Fund were to lose its mutual fund trust status as a result of the application of the draft amendments, the Fund would permanently cease to be a mutual fund trust. The December 6, 2004 Notice of Ways and Means Motion to implement the tax proposals contained in the 2004 Federal Budget does not contain this proposal and the Department of Finance indicated in a concurrent release that further discussions would be pursued with the private sector in this regard. Depending on the final form of the draft amendments as enacted, it may be necessary to amend the Declaration of Trust to take into account these new restrictions. This amendment may be made without Unitholder approval.

### ***Amendments to the Declaration of Trust***

The Declaration of Trust may be amended or altered from time to time by a Unitholders' Special Resolution. The trustees of the Fund may, without the approval of the Unitholders, make certain amendments to the Declaration of Trust, including amendments:

- for the purpose of ensuring continuing compliance with applicable laws, regulations, requirements or policies of any governmental authority having jurisdiction over the trustees or over the assets of the Fund or its subsidiary entities, or any stock exchange or other organized market on which the Units are listed or quoted for trading;
- which, in the opinion of the trustees, provide additional benefits or protection for Unitholders of the Fund;
- to remove any conflicts or inconsistencies in the Declaration of Trust or to make minor corrections which, in the opinion of the trustees, are necessary or desirable and not prejudicial to the Unitholders of the Fund;
- which, in the opinion of the trustees, are necessary or desirable as a result of changes in Canadian taxation laws or policies of any governmental authority having jurisdiction over the trustees or the Fund; and
- for the purpose of ensuring that the Fund continues to qualify as a mutual fund trust and the Units do not constitute "foreign property", in each case, under the Tax Act.

### ***Term of the Fund***

The Fund has been established for an indefinite term. However, Unitholders may, by a Unitholders' Special Resolution, require the trustees to commence to wind up the affairs of the Fund.

The Declaration of Trust provides that, upon being required to commence to wind up the affairs of the Fund, the trustees will give notice thereof to Unitholders, which notice will designate the time or times at which Unitholders must surrender their Units for cancellation and the date at which the register of Units will be closed. After the date the register is closed, the trustees will proceed to wind up the affairs of the Fund as soon as may be reasonably practicable and, for such purpose, will, subject to any direction to the contrary in respect of a termination authorized by a resolution of the Unitholders, sell and convert into money all of the assets comprising the Fund, including if applicable the MarksLP Note and MarksLP partnership units, and all of the other assets of the Fund in one transaction or in a series of transactions at public or private sales and do all other acts appropriate to liquidate the Fund. After paying, retiring, discharging or making provision for the payment, retirement or discharge of all of the Fund's known liabilities and obligations and providing for indemnity against any other outstanding liabilities and obligations, the trustees will distribute the remaining part of the proceeds of the sale of the assets comprising the Fund, together with any cash forming part of the assets of the Fund, among the Unitholders in accordance with their *pro rata* interests, against delivery of Units. If the trustees are unable to sell all or any of the assets which comprise part of the Fund by the date set for termination, they may distribute such assets *in specie* directly to the Unitholders in accordance with their *pro rata* interests, subject to obtaining all required regulatory approvals.

### ***Take-over Bids***

The Declaration of Trust contains provisions to the effect that, if a take-over bid is made for all of the issued and outstanding Units, and not less than 90% of the Units on a fully-diluted basis (including any Units issuable upon

the exchange of any securities exchangeable into Units but not including any Units held at the date of the take-over bid by or on behalf of the offeror or associates or affiliates of the offeror) are taken up and paid for by the offeror, the offeror will be entitled to acquire the Units held by Unitholders and holders of securities exchangeable for Units who did not accept the take-over bid on the terms offered by the offeror.

### ***Exercise of Certain Voting Rights Attached to Certain Securities***

The Declaration of Trust provides that the Fund will not vote any securities held by it or permit any subsidiary of the Fund to vote any securities held by it, to authorize, among other things:

- any sale, lease or other disposition of all or substantially all of the direct or indirect assets of any subsidiary of the Fund except in conjunction with an internal reorganization or a permitted charge, pledge or lien or pursuant to any guarantee of any subsidiary of the Fund;
- any amalgamation, arrangement or other merger of any subsidiary of the Fund with any other entity except in conjunction with an internal reorganization or in conjunction with the acquisition by any subsidiary of the Fund of the securities or assets of another entity;
- any material amendment to the constituting documents of any subsidiary of the Fund to change the authorized share capital in a way which would reasonably be expected to be prejudicial to the Fund,

without the authorization of the Unitholders by a Unitholders' Special Resolution.

### ***Information and Reports***

The Fund will furnish to Unitholders, in accordance with and subject to applicable securities laws, such consolidated financial statements (including quarterly and annual consolidated financial statements) and other reports as are from time to time required by applicable law, including prescribed forms needed for the completion of Unitholders' tax returns under the Tax Act and equivalent provincial legislation.

Prior to each meeting of the Unitholders of the Fund, the trustees will provide the Unitholders with notice of the meeting and all such information as is required by applicable law and the Declaration of Trust to be provided to such holders.

### ***Book-Entry Only System***

Registration of interests in and transfers of the Units will be made only through a book-based system (the "Book-Entry Only System") administered by CDS. At Closing, the Fund delivered to CDS certificates evidencing the aggregate number of Units subscribed for under the initial public offering. Pursuant to the Book-Entry Only System, Units must be purchased, transferred and surrendered for redemption through a CDS Participant. All rights of beneficial Unitholders must be exercised through, and all payments or other property to which such Unitholder is entitled will be made or delivered by, CDS or the CDS Participant through which the Unitholder holds such Units. Upon purchase of any Units, the Unitholders will receive only a customer confirmation from the registered dealer which is a CDS Participant and from or through which the Units are purchased.

References in this Annual Information Form to a “Unitholder” means, unless the context otherwise requires, the owner of the beneficial interest in such Units.

The ability of a beneficial owner of Units to pledge those Units or otherwise take action with respect to the Unitholder’s interest in those Units (other than through a CDS Participant) may be limited due to the lack of a physical certificate.

The Fund has the option to terminate registration of the Units through the Book-Entry Only System, in which case certificates for the Units in fully registered form would be issued to beneficial owners of Units or their nominees.

The Fund, the trustees of the Fund and the transfer agent and registrar for the Units will not have any liability for (a) records maintained by CDS relating to the beneficial interests in the Units or the book-entry accounts maintained by CDS; (b) maintaining, supervising or reviewing any records relating to those beneficial interests; or (c) any advice or representation made or given by CDS and made or given with respect to the rules and regulations of CDS, or any action taken or not taken by CDS or the CDS participants.

### ***Fund Administration***

Except as expressly prohibited by law, the trustees may grant or delegate certain of their authority to effect the actual administration of their duties under the Declaration of Trust. The trustees may grant broad discretion to a third party to administer and manage the Fund’s day-to-day operations and to make executive decisions which conform to the general policies and principles set forth in the Declaration of Trust or otherwise established by the trustees from time to time. Effective April 11, 2007, the Fund and GP Inc. entered into the Administration Agreement whereby GP Inc. agreed to provide or arranged for the provision of services required in the Fund’s administration.

## **GOVERNANCE OF MARKSLP**

### ***Capital of MarksLP***

The capital of MarksLP consists of the aggregate of all sums of money or other property contributed by the partners of MarksLP and which is not returned to them. The interests of the partners are divided into and represented by an unlimited number of general partnership units designated as “GP Units” and an unlimited number of limited partnership units designated as “LP Units”. Each MarksLP units will represent an interest in MarksLP having the preferences, rights, restrictions, conditions and limitations as provided in the Limited Partnership Agreement as follows: (a) the holders of MarksLP units will have the right to receive allocations as provided for in the Limited Partnership Agreement; (b) the holders of MarksLP units will have the right to share in returns of capital and to share in cash and any other distributions to partners of MarksLP and to receive the remaining property of MarksLP on dissolution or winding up as provided for in the Limited Partnership Agreement; and (c) the holders of MarksLP units will have the right to receive notice of and to attend any meetings of partners of MarksLP and will be entitled to vote as set out in the Limited Partnership Agreement.

### ***Distribution Policy***

It is a policy of the board of directors of GP Inc., in its capacity as the sole trustee of GP Trust, in its capacity as the general partner of MarksLP to distribute all of MarksLP’s available cash, subject to applicable law after:

- satisfaction of its debt service obligations, including principal and interest and other expense obligations;
- provisions for its administrative expenses and other obligations and liabilities (including taxes, if any);
- making any principal repayments in respect of the MarksLP Note considered advisable by the board of directors of GP Inc., with the consent of the Fund; and
- such reasonable working capital reserves as may be considered appropriate by its board of directors.

## **TRUSTEES, DIRECTORS AND MANAGEMENT**

### ***Trustees and Directors of the Fund, Second Cup and GP Inc.***

The trustees of the Fund are James Anas, Bryna Goldberg, Raymond Guyatt, Edward McDermott and Michael Rosicki. Each of the trustees is also a director of Second Cup. The directors of GP Inc. are James Anas and Stacey Mowbray.

<u>Name</u>	<u>Position</u>
James Anas, ..... <i>Burlington, Ontario</i>	Fund Trustee, Second Cup Director, and GP Inc. Director
Bryna Goldberg <sup>(1) (2) (5)</sup> ..... <i>Toronto, Ontario</i>	Fund Trustee and Second Cup Director
Raymond Guyatt <sup>(1) (4)</sup> ..... <i>Westmount, Quebec</i>	Fund Trustee and Second Cup Director
Edward McDermott <sup>(2)</sup> ..... <i>Markham, Ontario</i>	Fund Trustee and Second Cup Director
Stacey Mowbray, ..... <i>Toronto, Ontario</i>	GP Inc. Director
Michael Rosicki <sup>(1) (2) (3)</sup> ..... <i>Oakville, Ontario</i>	Fund Trustee and Second Cup Director

Notes:

- <sup>(1)</sup> Member of Audit Committee
- <sup>(2)</sup> Member of Governance/ Human Resources/ Compensation Committee
- <sup>(3)</sup> Chair of Board of Trustees
- <sup>(4)</sup> Chair of Audit Committee
- <sup>(5)</sup> Chair of Governance/ Human Resources/ Compensation Committee

The following is a summary biography of each of the trustees and directors of the Fund, Second Cup and GP Inc.:

*James S. Anas*

Mr. Anas held the position of Chairman of Second Cup from April 1, 2009 to June 27, 2009, and has held the position of Vice-Chairman of the Board of Directors since June 27, 2009. Mr. Anas has held the position of Chairman of S.C. Coffee Co. since April 2009, following his tenure as Executive Vice-Chairman from 2008 to April 2009 and previously as President and Chief Executive Officer from 2001 to 2008. Previously, Mr. Anas held the position of President and Chief Executive Officer and director of the national franchisor, and formerly TSX listed, Jumbo Entertainment Inc. from 1993 to 2001. Mr. Anas is currently on the Board of Directors of Guardian Capital Group Limited, a TSX listed financial services company.

*Bryna Goldberg*

Bryna Goldberg is a retired business executive. Until her retirement in 2007, Ms. Goldberg was Executive Vice President, Legal Affairs, General Counsel and Secretary of Shoppers Drug Mart Inc., where she was employed for over 20 years. She played a key role in transitioning Shoppers to a new ownership structure including through a leveraged buy-out transaction and subsequent initial public offering. Ms. Goldberg is a lawyer and a member of the Law Society of Upper Canada.

*Raymond Guyatt*

Raymond Guyatt is a retired executive. From 1987 to 2000, Mr. Guyatt was the Executive Vice President and Chief Financial Officer of Imasco Limited. He was also a director of both Imasco and CT Financial Services from 1990 to 2000. Mr. Guyatt was a director of Mackenzie Financial Corporation from 2002 to 2005 and was Chairman of the Innovation Council of the Canadian Institute of Chartered Accountants from 2001 to 2003. Mr. Guyatt is a Chartered Accountant and a member of the Institute of Chartered Accountants of Ontario.

*Edward T. McDermott*

Edward McDermott was a senior partner at Osler, Hoskin & Harcourt LLP from 1974 to 2009 when he retired from active practice. Mr. McDermott's legal practice involved advising numerous public and private corporations with particular emphasis on matters involving labour relations and employment law as well as general business issues. He is currently associated with ADR Chambers where he carries on an Alternate Dispute Resolution practice as a mediator and arbitrator. Mr. McDermott has served in a number of leadership positions in the community including as the President of York Downs Golf Club and Chair of Holy Trinity School. He is a member of the Law Society of Upper Canada.

*Michael Rosicki*

Michael Rosicki is the President of Wexford Group Inc. From 1999 to 2004, Mr. Rosicki was Chairman and Chief Executive Officer of Parmalat North America. From 1997 to 1999, Mr. Rosicki was with Mattel, where he began as President of Mattel Canada Inc. and later became President, Mattel Europe, Canada, Middle East, and Africa. Prior to that, he was with Nestlé Canada Inc. for 12 years, where he held progressively senior management positions culminating in his role as President of the company's Foods Group. Mr. Rosicki is a director of Metro Inc. and Santa

Maria Foods Inc. He has held senior positions with various industry and charitable associations, including past member of the Board of the Hospital for Sick Children's Foundation (SickKids Foundation), past Chairman and co-founder of Kids Help Phone, past Chairman of the Food Products Manufacturers of Canada and past President of the Ontario Grocery Industry Foundation

*Stacey Mowbray*

A summary of Ms. Mowbray's biography can be found below under "Management".

***Management***

The names and municipalities of residence of the persons who are the executive officers of Second Cup are as follows:

<u>Name</u>	<u>Position with Second Cup</u>
Stacey Mowbray ..... <i>Toronto, Ontario</i>	President and Chief Executive Officer
Robert Masson ..... <i>Richmond Hill, Ontario</i>	Chief Financial Officer
Steven Tsambaleros ..... <i>Toronto, Ontario</i>	Chief Operating Officer
Ian M. Baskerville, ..... <i>Milton, Ontario</i>	Vice-President, Legal Affairs and Secretary
Rita Toporowski ..... <i>Oakville, Ontario</i>	Vice-President, Corporate Planning and Development
Kimberly Clark ..... <i>Toronto, Ontario</i>	Vice-President, Marketing
Wayne C. Vanderhorst ..... <i>Grimsby, Ontario</i>	Vice-President, Franchise Development

The following is a summary biography of each of the members of the senior management team of Second Cup:

*Stacey Mowbray — President and Chief Executive Officer*

Prior to joining Second Cup, Ms. Mowbray held positions in Molson Canada as Chief Marketing Officer, Cara Operations as President of the Milestone's chain and as SVP Branding and Marketing, Pepsi Canada as Vice President of Marketing and the Weston group where she started her career in sales and marketing over 20 years ago. Ms. Mowbray has a Masters Business Degree from York University and a Bachelor of Business



Administration from Wilfrid Laurier University. She has been a director of Second Cup since early 2007 and has been a board member of several industry associations over her career.

*Robert Masson — Chief Financial Officer*

Mr. Masson has held various finance and accounting related positions over the last 14 years and is a designated Chartered Accountant with the Institute of Chartered Accountants of Ontario. Mr. Masson holds a Bachelor of Commerce degree from the University of Kwa-Zulu Natal in South Africa. From 1995 to 1998 Mr. Masson was employed as an auditor with Ernst & Young. From 1999 to 2006, Mr. Masson held positions with various companies including Deloitte & Touche and IBM Canada. From 2006 to January 2009 Mr. Masson was VP Finance with Manchu Wok Canada Inc. In February 2009, Mr. Masson was appointed Chief Financial Officer of Second Cup and the Fund.

*Steven Tsambalieros — Chief Operating Officer*

Mr. Tsambalieros joined Second Cup as Global Chief Operating Officer in July 2008. Prior to joining Second Cup, he was President and Chief Executive Officer of Chrisco Canada from 2007 until July 2008, President and Chief Operating Officer of Swiss Chalet Restaurants from 1998 to 2007, Chief Operating Officer for Cara Airline Terminal Restaurants from 1996 to 1998 and multi-unit franchise operator of Harvey's and Swiss Chalet restaurants from 1983 to 1996.

*Ian Baskerville — Vice-President, Legal Affairs and Secretary*

Mr. Baskerville has been Vice President, Legal Affairs since November 2006. Prior to joining Second Cup, Mr. Baskerville was Legal Counsel for Cara Operations Limited from 2003 to November 2006. From 2000 to 2003, Mr. Baskerville specialized in mergers and acquisitions as a lawyer at Cassels Brock & Blackwell LLP. Mr. Baskerville obtained a Bachelor of Arts degree from the University of Victoria and a Bachelor of Laws degree from the University of Western Ontario. Mr. Baskerville is a member of the Law Society of Upper Canada.

*Rita Toporowski — Vice-President, Corporate Planning & Development*

Ms Toporowski joined Second Cup as Vice President Corporate Planning & Development in June 2009. Prior to that, Ms. Toporowski was Vice President Corporate Planning & Development for S.C. Coffee Co. from July 2007 to June 2009. Before joining S.C. Coffee Co., she was with Air Canada for over 16 years in numerous senior level positions including Senior Director Six Sigma.

*Kimberly Clark — Vice-President, Marketing*

Ms. Clark joined Second Cup as Vice President, Marketing in September 2009. Prior to joining Second Cup, Ms. Clark was Vice President, Marketing for E1 Entertainment L.P. from September 2008 to September 2009. From October 2007 to September 2008, Ms. Clark held the position of Principal at Marrkit Consulting. Ms. Clark was employed as Vice President, Marketing at Blockbuster Canada Co. from May 2004 to October 2007.

*Wayne C. Vanderhorst – Vice-President, Franchise Development*

Mr. Vanderhorst joined Second Cup in September 2007 as Vice President, Franchise Development. Prior to joining Second Cup, Mr. Vanderhorst was employed with Mr. Lube Canada LP as Vice President, Real Estate & Development from August 2005 to September 2007 and was previously with Dairy Queen Canada Inc. for over 16 years in numerous positions including Director of Real Estate & Leasing.

As of March 30, 2010, the senior management team of Second Cup held 28,460 Units, representing approximately 0.3 % of the Fund’s issued and outstanding Units.

### ***Insider Reporting***

Based upon an analysis of the structure of the Fund and applicable law, the following individuals are “insiders” of the Fund and, as such, will have reporting obligations as insiders under the securities laws of the various provinces and territories of Canada, including the obligation to file “insider trading reports” under those laws:

- the trustees and senior officers of the Fund; and
- the directors and senior officers of GP Inc. and Second Cup.

## **MARKET FOR SECURITIES**

### ***Trading Price and Volume***

The outstanding Units of the Fund are listed and posted for trading on the TSX under the symbol “SCU.UN”. The following table shows the price range and average daily volume traded on the TSX for each month of 2009.

<b>Month</b>	<b>Trading Price Range</b>	<b>Average Trading Volume</b>
January 2009	\$4.76 - \$6.21	13,600
February 2009	\$4.90 - \$5.79	9,100
March 2009	\$4.46 - \$5.31	10,700
April 2009	\$5.00 - \$5.60	9,800
May 2009	\$4.85 - \$5.42	40,400
June 2009	\$4.52 - \$5.50	20,800
July 2009	\$4.61 - \$5.00	5,700
August 2009	\$4.80 - \$5.25	11,900
September 2009	\$4.91 - \$5.78	14,500
October 2009	\$5.45 - \$7.28	11,800
November 2009	\$5.75 - \$6.49	16,200
December 2009	\$5.86 - \$6.38	22,500

## **LEGAL PROCEEDINGS**

Neither the Fund nor any of its affiliates are involved in any litigation or proceedings which, if determined adversely, would be material to the Fund, and no such proceedings are known to the Fund to be contemplated. See “Risk Factors” and note 16 to the consolidated financial statements of Second Cup for the year ended December 26, 2009.

## **INTERESTS OF MANAGEMENT AND OTHERS IN MATERIAL TRANSACTIONS**

On June 27, 2009, the Fund through MarksLP acquired all of the issued and outstanding shares of Second Cup. See “General Development of the Business – Establishment of the Fund”.

## **TRANSFER AGENT AND REGISTRAR**

The transfer agent and registrar for the Units is Computershare Investor Services Inc, 100 University Avenue, Toronto, Ontario.

## **MATERIAL CONTRACTS**

The material contracts relating to the Fund are as follows:

- (a) the purchase agreement referred to under “Acquisition of Second Cup”
- (b) the Declaration of Trust referred to under “Description of the Fund”;
- (c) the loan agreement in respect of each of the Fund Term Loan and the Fund Operating Loan; and
- (d) the Administration Agreement referred to under “Description of the Fund”.

Copies of the foregoing documents may be examined during normal business hours at the Fund’s offices at 6303 Airport Road, 2<sup>nd</sup> Floor, Mississauga, Ontario L4V 1R8.

## **EXPERTS**

The Fund’s auditors are PricewaterhouseCoopers LLP, Chartered Accountants, who have prepared an independent auditors’ report dated March 17, 2010 in respect of the Fund’s consolidated financial statements with accompanying notes as at and for the years ended December 31, 2009, 2008, and 2007. PricewaterhouseCoopers LLP has advised that they are independent with respect to the Corporation within the meaning of the Rules of Professional Conduct of the Institute of Chartered Accountants of Ontario.

## **ADDITIONAL INFORMATION**

Additional information relating to the Fund may be obtained on request from the administrative office of the Fund at 6303 Airport Road, 2<sup>nd</sup> Floor, Mississauga, Ontario, L4V 1R8 or may be found at the Fund’s website at [www.secondcupincomefund.com](http://www.secondcupincomefund.com) or on SEDAR at [www.sedar.com](http://www.sedar.com). Additional information, including with respect to trustees’ remuneration and indebtedness and principal holders of the units of the Fund will be contained in the Fund’s information circular for its 2009 annual meeting of Unitholders.

Additional financial information is provided in the consolidated financial statements and notes to the consolidated financial statements of the Fund and Management’s Discussion and Analysis for 2009.

## Schedule A – Charter of the Audit Committee

The term “**Fund**” herein shall refer to Second Cup Income Fund and the term “**Board**” shall refer to the Board of Trustees of the Fund. “**Second Cup Group**” means, collectively, the Fund, Second Cup Trade-Marks Limited Partnership (“**MarksLP**”), Second Cup GP Inc. (“**GP Inc.**”), Second Cup GP Trust and The Second Cup Ltd. The term “**Management**” herein shall refer to senior management of GP Inc.

### PURPOSE

The Audit Committee (the “**Committee**”) is a standing committee appointed by the Board to assist the Board in fulfilling its oversight responsibilities with respect to financial reporting including responsibility to:

- oversee the work of the Fund’s external auditors engaged for the purpose of preparing or issuing an auditor’s report or performing other audit, review or attest services for the Fund;<sup>1</sup>
- oversee the integrity of the Fund’s financial statements and financial reporting process, including the audit process and the Fund’s internal accounting controls and procedures and compliance with related legal and regulatory requirements;
- oversee the work of the Fund’s internal auditors;
- oversee the qualifications and independence of the external auditors;
- oversee the work of the Fund’s financial management and external auditors in these areas;<sup>2</sup> and
- provide an open avenue of communication between the external auditors, the Board and Management.<sup>3</sup>

In addition, the Committee will review and/or approve any other matter specifically delegated to the Committee by the Board, including a quarterly review to ensure the Fund is meeting its financial covenants with its lender.

The function of the Committee is oversight. It is not the duty or responsibility of the Committee or its members (i) to plan or conduct audits, (ii) to determine that the Fund’s financial statements are complete and accurate and are in accordance with generally accepted accounting principles or (iii) to conduct other types of auditing or accounting reviews or similar procedures or investigations. The Committee and its Chair are members of the Board, appointed to the Committee to provide broad oversight of the financial, risk and control related activities of the Fund and are specifically not accountable or responsible for the day to day operation or performance of such activities.

GP Inc., as administrator of the Fund, is responsible for the preparation, presentation and integrity of the Fund’s financial statements. Management is also responsible for maintaining appropriate accounting and financial reporting principles and policies and systems of risk assessment and internal controls and procedures designed to provide reasonable assurance that assets are safeguarded and transactions are properly authorized, recorded and

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<sup>1</sup> Multilateral Instrument 52-110 (“MI 52-110”) s.2.3(3)

<sup>2</sup> MI 52-110 s.2.3(3)

<sup>3</sup> MI 52-110 s.4.1(c)

reported and to assure the effectiveness and efficiency of operations, the reliability of financial reporting and compliance with accounting standards and applicable laws and regulations.

The external auditors are responsible for planning and carrying out an audit of the Fund's annual financial statements in accordance with generally accepted auditing standards to provide reasonable assurance that, among other things, such financial statements are in accordance with generally accepted accounting principles.

## **AUDIT RESPONSIBILITIES OF THE COMMITTEE**

### **Selection and Oversight of the External Auditors**

1. The external auditors are ultimately accountable to the Committee and the Board as the representatives of the Unitholders of the Fund and shall report directly to the Committee and the Committee shall so instruct the external auditors.<sup>4</sup> The Committee shall evaluate the performance of the external auditors and make recommendations to the Board on the reappointment or appointment of the external auditors of the Fund to be proposed in the Fund's proxy circular for Unitholder approval and shall have authority to terminate the external auditors.<sup>5</sup> If a change in external auditors is proposed, the Committee shall review the reasons for the change and any other significant issues related to the change, including the response of the incumbent auditors, and enquire on the qualifications of the proposed auditors before making its recommendation to the Board.<sup>6</sup> The Board is responsible for selecting the external auditor to be proposed in the Fund's proxy circular for Unitholder approval and appointment.
2. The Committee shall review and recommend to the Board for approval the terms of engagement and the compensation to be paid by the Fund to the external auditors with respect to the conduct of the annual audit.<sup>7</sup>
3. The Committee shall review the independence of the external auditors and shall make recommendations to the Board on appropriate actions to be taken which the Committee deems necessary to protect and enhance the independence of the external auditors. In connection with such review, the Committee shall:
  - (a) actively engage in a dialogue with the external auditors about all relationships or services that may impact the objectivity and independence of the external auditors;<sup>8</sup>
  - (b) require that the external auditors submit to it on a periodic basis, and at least annually, a formal written statement delineating all relationships between the Fund and Second Cup Group, on the one hand, and the external auditors and their affiliates on the other hand;<sup>9</sup>

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<sup>4</sup> MI 52-110 s.2.2

<sup>5</sup> MI 52-110 s.2.3(2)(a)

<sup>6</sup> National Instrument 51-102 s.4.11

<sup>7</sup> MI 52-110 s.2.3(2)(b)

<sup>8</sup> PCAOB Ethics and Independence Rule 3526 – Communication with Audit Committees Concerning Independence

<sup>9</sup> CICA Handbook Section 5751.12, .25 - .29 and .32

- (c) require that (i) both the lead audit partner and the partner responsible for performing a second review respecting the audit be rotated at least every five years and be subject to a five year time out and (ii) all other partners on the audit engagement team who provide more than 10 hours of audit, review or attest services with respect to the Fund's consolidated financial statements or who serve as the lead partner in connection with any audit or review related to financial statements of a subsidiary whose assets or revenues constitute at least 20% of the consolidated assets or revenues of the Fund be rotated at least every seven years and be subject to a two year time out;<sup>10</sup>
  - (d) consider whether there should be a regular rotation of the external audit firm itself; and
  - (e) consider the auditor independence standards promulgated by applicable auditing regulatory and professional bodies.
4. The Committee shall prohibit the external auditor and its subsidiaries from providing certain non-audit services to the Fund. All non-audit services to be provided to the Fund or any of its affiliates by the external auditors or any of their affiliates shall be subject to pre-approval by the Committee.<sup>11</sup> The Committee may approve policies and procedures for the pre-approval of non-audit services to be rendered by the external auditors, which policies and procedures (i) shall include reasonable detail with respect to the services covered, (ii) shall require that the Committee be informed of each non-audit service and (iii) shall not include delegation of the Committee's responsibilities to management of GP Inc.<sup>12</sup>
  5. The Committee shall establish and monitor clear policies for the hiring by Second Cup Group of partners, employees and former partners and employees of the external auditors.<sup>13</sup>
  6. The Committee shall require the external auditors to provide to the Committee, and the Committee shall review and discuss with the external auditors, all reports which the external auditors are required to provide to the Committee or the Board under rules, policies or practices of professional or regulatory bodies applicable to the external auditors, and any other reports which the Committee may require. Such reports shall include:
    - (a) a description of the external auditors' internal quality-control procedures, any material issues raised by the most recent internal quality-control review, or peer review, of the external auditors, or by any inquiry or investigation by governmental or professional authorities, within the preceding five years, respecting one or more independent audits carried out by the external auditors, and any steps taken to deal with any such issues;<sup>14</sup> and
    - (b) a report describing (i) all critical accounting policies and practices used in the preparation of the Fund's financial statements, (ii) all alternative treatments of financial information within generally accepted accounting principles related to material items that have been discussed with Management, ramifications of the use of such alternative disclosures and treatments, and the treatment preferred by the external auditors (iii) other material written communication between

<sup>10</sup> CICA (Proposed) Independence Standards s.204.4(20)

<sup>11</sup> MI 52-110 ss.2.3(4), 2.4 and 2.5

<sup>12</sup> MI 52-110, s.2.6

<sup>13</sup> Independence Standards Board Independence Standard No. 3; MI 52-110 s.2.3(8)

<sup>14</sup> CICA Handbook Section 5751.31

the external auditors and Management, such as any management letter or schedule of unadjusted differences; and (iv) disagreements between Management and/or the internal auditors and the external auditors regarding financial reporting.

7. The Committee is responsible for resolving disagreements between Management and the external auditors regarding financial reporting.<sup>15</sup>

#### **Oversight of Internal Audit Function**

8. The Committee shall determine the appropriate internal audit function for the Fund and oversee its processes, reports and the terms of compensation for any individuals engaged in such function, if any.

#### **Oversight and Monitoring of Audits**

9. The Committee shall review with the external auditors and Management the audit function generally, the objectives, staffing, locations, co-ordination, reliance upon Management, any internal audit and general audit approach and scope of proposed audits of the financial statements of the Fund, the overall audit plans, the responsibilities of Management and the external auditors, the audit procedures to be used and the timing and estimated budgets of the audits.<sup>16</sup>
10. The Committee shall discuss with the external auditors any difficulties or disputes that arise with Management or any internal auditors during the course of the audit and the adequacy of Management's responses in correcting audit-related deficiencies.<sup>17</sup>
11. The Committee shall review with Management the results of any internal and all external audits.
12. The Committee shall take such other reasonable steps as it may deem necessary to satisfy itself that the audit was conducted in a manner consistent with all applicable legal requirements and auditing standards of applicable professional or regulatory bodies.

#### **Oversight and Review of Accounting Principles and Practices<sup>18</sup>**

13. The Committee shall, as it deems necessary, oversee, review and discuss with Management, the external auditors and any internal auditors:
  - (a) the quality, appropriateness and acceptability of the Fund's accounting principles and practices used in its financial reporting, changes in the Fund's accounting principles or practices and the application of particular accounting principles and disclosure practices by Management to new transactions or events;

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<sup>15</sup> MI 52-110 s.2.3(3)

<sup>16</sup> CICA Handbook Section 5751.14; MI 52-110 s.2.3(3)

<sup>17</sup> CICA Handbook Section 5751.23

<sup>18</sup> CICA Handbook Section 5751.17, .20, .21 and .22

- (b) all significant financial reporting issues and judgments made in connection with the preparation of the Fund’s financial statements, including the effects of alternative methods within generally accepted accounting principles on the financial statements and any “second opinions” sought by Management from an independent auditor with respect to the accounting treatment of a particular item;
  - (c) disagreements between Management and the external auditors or any internal auditors regarding the application of any accounting principles or practices;
  - (d) any material change to the Fund’s auditing and accounting principles and practices as recommended by Management, the external auditors or any internal auditors or which may result from proposed changes to applicable generally accepted accounting principles;
  - (e) the effect of regulatory and accounting initiatives on the Fund’s financial statements and other financial disclosures;
  - (f) any reserves, accruals, provisions, estimates or management programs and policies, including factors that affect asset and liability carrying values and the timing of revenue and expense recognition, that may have a material effect upon the financial statements of the Fund;
  - (g) the use of special purpose entities and the business purpose and economic effect of off-balance sheet transactions, arrangements, obligations, guarantees and other relationships of Second Cup Group and their impact on the reported financial results of the Fund;
  - (h) any legal matter, claim or contingency that could have a significant impact on the financial statements, the Fund’s compliance policies and any material reports, inquiries or other correspondence received from regulators or governmental agencies and the manner in which any such legal matter, claim or contingency has been disclosed in the Fund’s financial statements;
  - (i) the treatment for financial reporting purposes of any significant transactions which are not a normal part of the Fund’s operations;
  - (j) the use of any “pro forma” or “adjusted” information not in accordance with generally accepted accounting principles;<sup>19</sup> and
  - (k) Management’s determination of goodwill impairment, if any, as required by applicable accounting standards.
14. The Committee will review and resolve disagreements between Management and the external auditors regarding financial reporting<sup>20</sup> or the application of any accounting principles or practices.

**Oversight and Monitoring of Internal Controls**

15. The Committee shall, as it deems necessary, exercise oversight of, review and discuss with Management and the external auditors:

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<sup>19</sup> CSA Notice 52-306

<sup>20</sup> MI 52-110 s.2.3(3)



- (a) the adequacy and effectiveness of the Fund’s internal accounting and financial controls based on recommendations of Management and the external auditors for the improvement of accounting practices and internal controls;<sup>21</sup>
- (b) any material weaknesses in the internal control environment, including with respect to computerized information system controls and security; and
- (c) Management’s compliance with the Fund’s processes, procedures and internal controls.

**Communications with Others**

- 16. The Committee shall establish and monitor procedures for the receipt and treatment of complaints received by the Fund regarding accounting, internal accounting controls or audit matters and the anonymous submission of concerns regarding questionable accounting or auditing matters and review periodically with Management, and senior finance officers of Second Cup Group responsible for any internal audit function, these procedures and any significant complaints received.<sup>22</sup>

**Oversight and Monitoring of the Fund’s Financial Disclosures**

- 17. The Committee shall:

- (a) review with the external auditors and Management and recommend to the Board for approval the audited financial statements and the notes and Management’s Discussion and Analysis accompanying such financial statements, the Fund’s annual report, the financial information of the Fund contained in any prospectus or information circular or other disclosure documents or regulatory filings of the Fund;<sup>23</sup> and
- (b) review with the external auditors and Management and approve each set of interim financial statements and the notes and Management’s Discussion and Analysis accompanying such financial statements and any other disclosure documents or regulatory filings of the Fund containing or accompanying financial information of the Fund.<sup>24</sup>

Such reviews shall be conducted prior to the release of any summary of the financial results or the filing of such reports with applicable regulators.

- 18. The Committee shall review all financial statements and material change reports prepared for the Fund
- 19. The Committee shall review such additional information regarding the business of MarksLP as the Fund may reasonably request to comply with any continuous disclosure or other disclosure requirements.

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<sup>21</sup> CICA Handbook Section 5751.16

<sup>22</sup> MI 52-110 s.2.3(7)

<sup>23</sup> National Instrument 51-102 ss.4.5(1) and 5.5(1); MI 52-110 ss.2.3(5) and 5.1

<sup>24</sup> National Instrument 51-102 ss. 4.5(2), (3) and 5.5(2) and (3); MI 52-110 s.2.3(5)

20. Prior to their distribution and filing, the Committee shall review and discuss earnings press releases, as well as financial information provided to analysts and ratings agencies. The Chair of the Committee may perform this review function, on behalf of the Committee, as is required. Such discussions may, in the discretion of the Committee, be done generally (i.e., by discussing the types of information to be disclosed and the type of presentation to be made) and the Committee need not discuss in advance each instance in which the Fund discloses financial information if it has reviewed and approved the Fund's policies and procedures with respect to such matters.<sup>25</sup>
21. The Committee shall meet with Management to review and assess the process and systems in place for the review of public disclosure documents that contain audited and unaudited financial information and their effectiveness.<sup>26</sup>
22. As part of the process by which the Committee shall satisfy itself as to the reliability of public disclosure documents that contain audited and unaudited financial information, the Committee shall require each of (i) the President or Chief Executive Officer and (ii) the Chief Financial Officer of the applicable member of the Second Cup Group to provide a certificate addressed to the Committee certifying in respect of each annual and quarterly report the matters such officers are required to certify in connection with the filing of such reports under applicable securities laws.<sup>27</sup> The Committee shall oversee the inclusion of such a certificate in respect of each annual and quarterly financial statement that MarksLP provides to the Fund as a supplement to the Fund's financial statement filings.
23. The Committee shall review the disclosure with respect to its pre-approval of audit and non-audit services provided by the external auditors.

#### **Oversight of Finance Matters**

24. The Committee shall meet periodically with Management to review and discuss the Fund's major financial risk exposures and the policy steps Management has taken to monitor and control such exposures.
25. The Committee shall meet periodically with the Secretary of GP Inc. to review issues arising out of compliance activities, as well as assess contingent legal and regulatory risks.
26. The Committee shall receive and review the financial statements, material charge reports and other financial information of members of Second Cup Group and any auditor recommendations concerning such entities as they relate to the ownership, licensing, maintenance and control of the Second Cup Marks.

#### **Committee Reporting**

27. As required by applicable laws or regulations or stock exchange requirements, the Committee shall review and approve the information required to be reported to Unitholders and others in its Annual Information

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<sup>25</sup> National Instrument 51-102 s.11.4 and MI 52-110 s.2.3(5); National Policy 51-201 s. 6.4

<sup>26</sup> MI 52-110 s.2.3(6)

<sup>27</sup> Multilateral Instrument 52-109, Parts 2 and 3

Form, and for such purposes, each member of the Committee shall provide information respecting that member's education and experience that relate to his or her responsibilities as a Committee member.<sup>28</sup>

### **Insider Trading**

28. The Committee shall prepare and revise as necessary a policy on insider trading respecting the Fund's securities. Such policy shall impose trading black-outs, policies and procedures respecting trades in the Fund's securities.
29. The Committee shall periodically review Management's systems and practices for ensuring that all trustees, directors, officers and other reporting insiders of the Fund who are required to do so file insider reports in connection with any trade of securities of the Fund or any derivative transaction which results in the effective disposition of the individual's economic interest in a security of the Fund within the shortest period of time in which such reports are required to be filed.

### **Additional Responsibilities**

30. Each new member of the Committee shall receive such training as may be approved by the Chair of the Committee. Training should cover the requirements and obligations of audit committees, issues of accounting principles, auditing standards, risk management and ethical compliance. Each Committee member should attend refresher training as may be deemed appropriate from time to time.
31. The Committee shall review and/or approve any other matter specifically delegated to the Committee by the Board and undertake on behalf of the Board such other activities as may be necessary or desirable to assist the Board in fulfilling its oversight responsibilities with respect to financial reporting.

### **THE CHARTER**

The Committee shall review and reassess the adequacy of this Charter at least annually and otherwise as it deems appropriate and recommend changes to the Board. The performance of the Committee shall be evaluated with reference to this Charter annually.<sup>29</sup>

The Committee shall ensure that this Charter or a summary of it which has been approved by the Committee is disclosed in accordance with all applicable securities laws or regulatory requirements in the annual proxy circular or annual report of the Fund.

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<sup>28</sup> MI 52-110 s.5.1; Form 52-110F and Companion Policy 52-110CP s. 4.2

<sup>29</sup> National Policy 58-201 s.3.18(a)