FIRST NATIONAL

FINANCIAL INCOME FUND

ANNUAL REPORT 2006

First National Financial Income Fund (TSX: FN.UN) owns a 19.97% interest in First National Financial LP, a Canadian-based originator, underwriter and servicer of predominantly prime residential (single-family and multi-unit) and commercial mortgages. With more than $24 billion in mortgages under administration, First National is Canada's largest non-bank originator and underwriter of residential mortgages and is among the top three in market share in the growing mortgage broker distribution channel.

www.firstnational.ca

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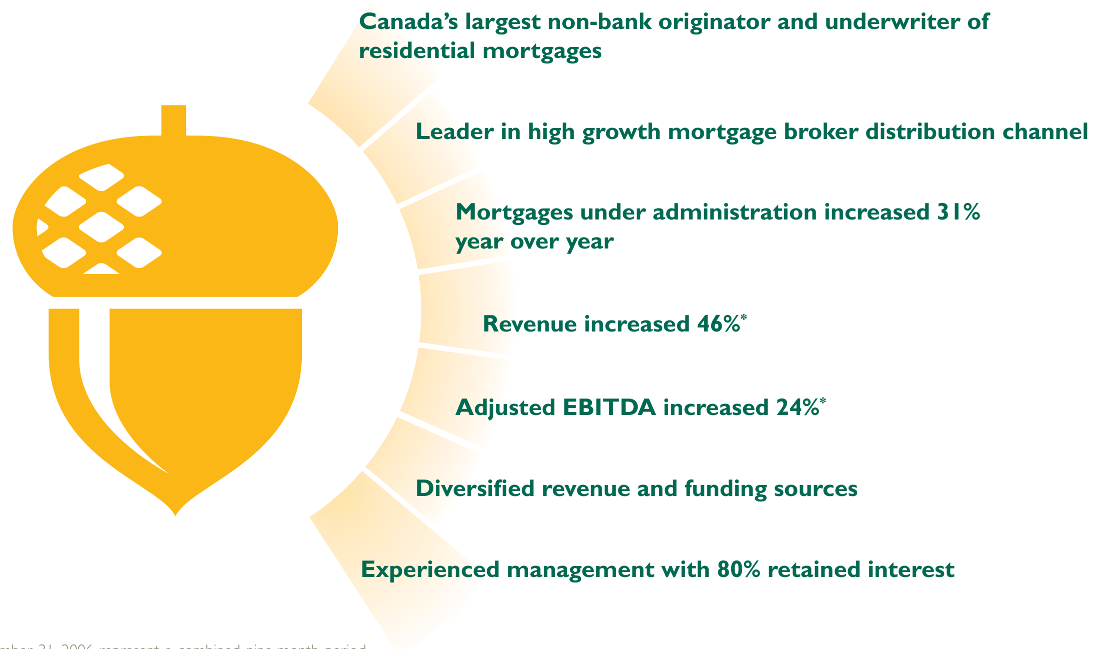
INVESTMENT HIGHLIGHTS

First National's strength is based on our commitment to service, product development, and prudent risk management.

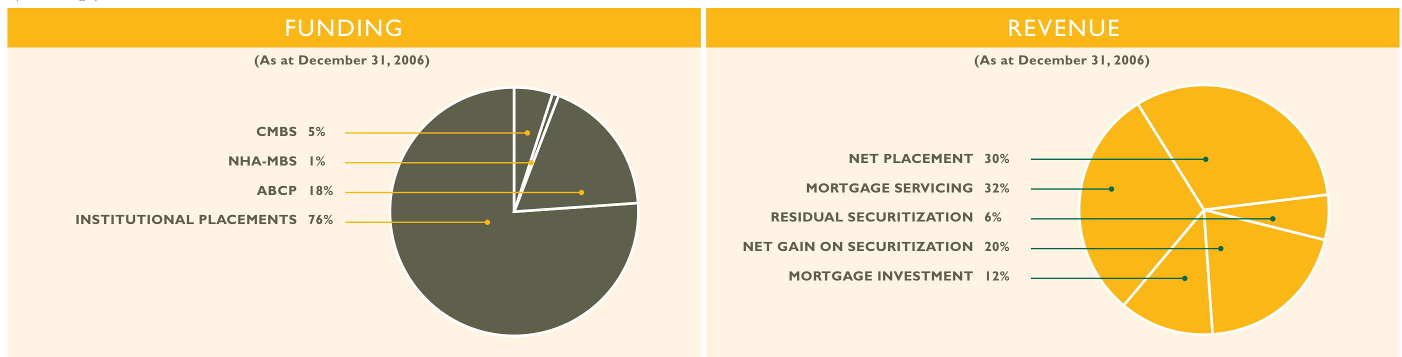
Our long-term growth strategy is focused on four key objectives:

- providing a complete range of mortgage products;
- increasing mortgages under administration;
- lowering costs through efficient processes; and
- maintaining a conservative risk profile.

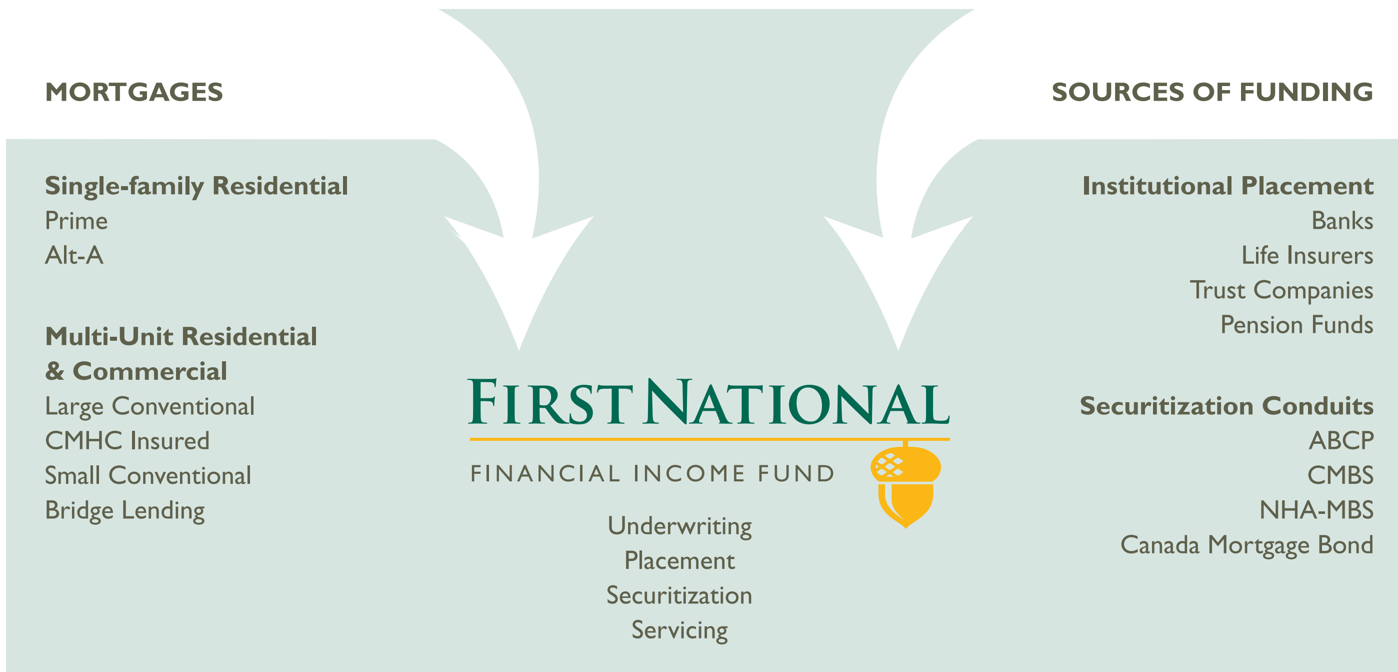
We are achieving this by leveraging our leadership position with mortgage brokers and by continually innovating our products and operations.



* Year-to-date results for the period ended December 31, 2006 represent a combined nine-month period, which includes the activities of First National Financial Income Fund and First National Financial LP (FNLP) from June 15 through December 31, 2006, together with the activities of First National Financial Corporation (FNFC) from April 1 through June 14, 2006.



Our Business Model

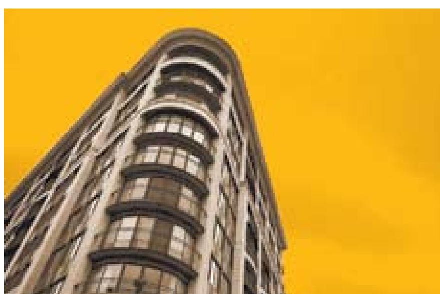


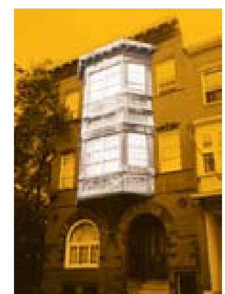
First National's business model is simple: we originate, underwrite and service mortgages.

We offer a full range of mortgage products for both the residential and commercial markets. Our service process offers a complete end-to-end solution for the client. Most of our single-family mortgages are originated through the residential mortgage broker channel while our multi-unit and commercial mortgages are originated through an experienced group of in-house underwriters.

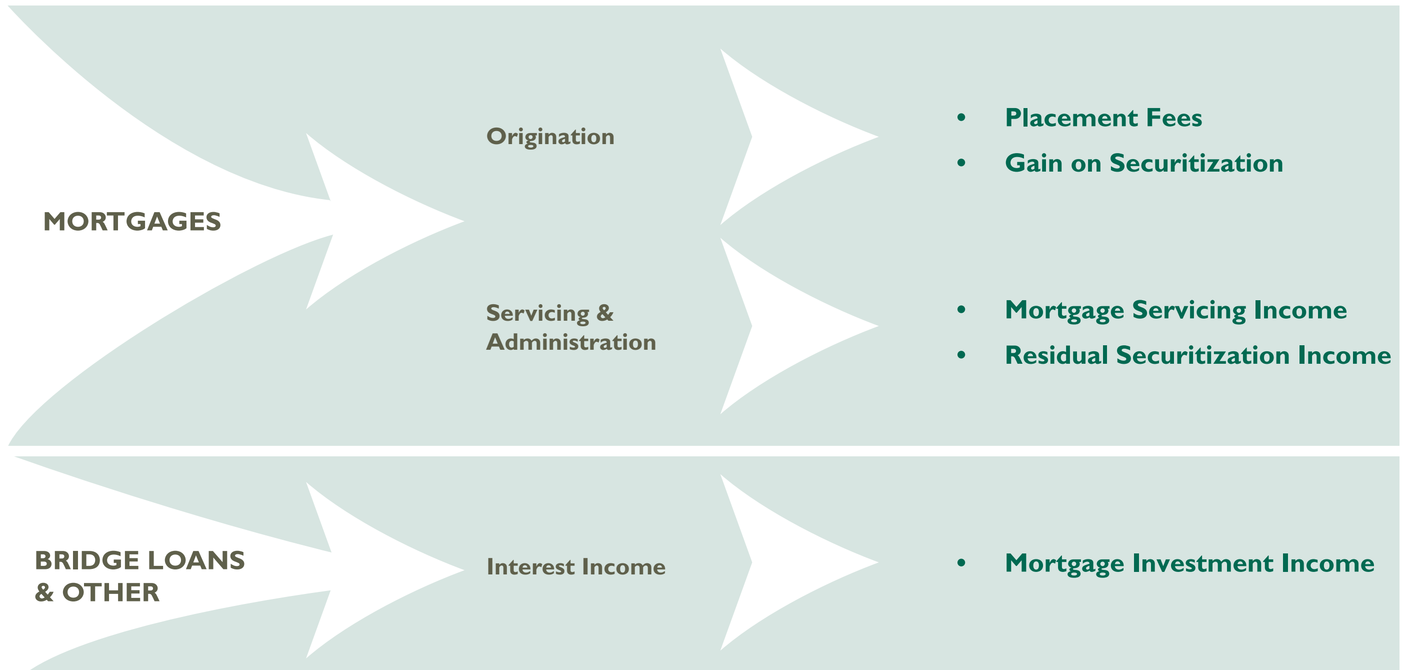
Our mortgages are funded through a diversified mix of both institutional placements and securitization conduits. This gives us flexibility to finance and manage our mortgages in a low risk and cost effective manner.

We service virtually all the mortgages we originate which creates stable, consistent and predictable cash flows.





Our Revenue Model



First National has three revenue sources: origination, servicing & administration, and investment.

Mortgage originations generate revenues at the time they are placed with institutional investors or sold to securitization conduits. This revenue is recorded as either placement fees or gain on securitization. Additional revenue earned on our securitization conduits is recognized as residual securitization income over the term of the mortgage.

Recurring revenue is also earned from servicing our mortgage portfolio.

Another important source is mortgage investment income derived from interest earned on securitization receivables and other mortgage-related assets such as mortgage and loan investments, servicing rights and mortgages accumulated for sale.

LETTER FROM THE PRESIDENT

Fellow Unitholders,

On behalf of management and the Board of Directors, I am pleased to report First National Financial Income Fund's results for fiscal 2006.

The Fund commenced operations upon completion of its initial public offering (IPO) on June 15, 2006 and has a 19.97% indirect interest in First National Financial LP (FNLP).

Moray Tawse and I co-founded First National in 1988 and are very proud of its success. The value of mortgages under administration has grown steadily to more than $24 billion at the end of fiscal 2006 from $835 million in 1997. This represents a 10-year compound annual growth rate of 41%. FNLP is currently Canada's largest non-bank originator and underwriter of residential mortgages and is among the top three in market share in the high-growth mortgage broker distribution channel.

In 2006, we continued to build on our success and enjoyed one of the busiest and most rewarding years in the history of First National.

Key Events of 2006

Our IPO, the most significant event of the year, marked an important step in our strategic evolution. This has created a strong public platform that will provide us with greater opportunities for growth.

In keeping with our strategy of expanding our breadth of mortgage products, FNLP became one of the first Canadian lenders to offer the Canada Mortgage and Housing Corporation (CMHC) insured Interest Only Mortgage, a new mortgage concept that helps qualified homebuyers lower their monthly mortgage payments and improve their cash flow flexibility.

First National's Alt-A product evolution strategy also progressed well in 2006. Alt-A mortgage products are ideal for customers with strong credit histories, who may not be able to verify income in the traditional manner, and those who require more flexible underwriting. We recently completed a multi-city seminar series to build broker awareness for Excalibur, the First National Alt-A mortgage solution, and the opportunities within the Alt-A market. Our marketing efforts have been very well-received, positioning us to capture market share gains in this high growth segment.

We, like you, were surprised by the government's October 31, 2006 announcement regarding proposed tax changes for income trusts. More clarity was provided on this matter in December, and we continue to review the proposed changes to assess their potential impact on the Fund. While we were pleased with the guidance from the government on income trust expansion restrictions, we are still awaiting the passing of the proposed changes into legislation. Until then, we expect to continue to operate as an income trust for the next four years. With a favourable business environment and sound business strategy, we are confident that we can enhance long-term unitholder value.

Evidence of Success

Growth in First National's key metrics provide sound evidence of the strength of our business model.

- Mortgages under administration (MUA) were $24.4 billion as at December 31, 2006, an increase of 31% over 2005.
- Revenue for the nine-month period was up 46% to $156.4 million.*
- Adjusted EBITDA for the nine-month period increased 24% to $51.3 million.*

These excellent results were driven by a combination of successful strategies.

Growth in Single-family Mortgage Origination

Prime single-family residential originations for the nine-month period, which accounted for the majority of the origination volume, were $4.7 billion, up 37% compared to the same period in 2005. This significant growth was primarily due to two factors: the posting of very competitive prime single-family mortgage rates, and our growing market share in the mortgage broker distribution channel. We originate virtually all of our residential mortgages through independent mortgage brokers — the fastest growing distribution channel in Canada.

* Year-to-date results for the period ended December 31, 2006 represent a combined nine-month period, which includes the activities of First National Financial Income Fund and FNLP from June 15 through December 31, 2006, together with the activities of First National Financial Corporation (FNFC) from April 1 through June 14, 2006.

Growth in Higher Margin Mortgage Origination

While our main focus has historically been on the prime single-family mortgage market, First National has been pursuing strategies to increase volumes in both the Alt-A and commercial mortgage backed securities (CMBS) markets by leveraging on existing infrastructure and distribution channels. These markets are typically more profitable than conventional mortgage lending markets and add to economies of scale by further increasing MUA. We have been successful in increasing volume for both of these products this year, originating $432 million of Alt-A mortgages and $285 million of CMBS mortgages, compared to $151 million and $224 million respectively in 2005.

Canada Mortgage Bond: Revenue Enhancing Initiative

Another revenue enhancing initiative involves the Canada Mortgage Bond (CMB). The CMB is an initiative of the Canada Housing Trust, a trust created by CMHC which is designed to offer mortgage backed securities to the investment community in the form of semi-annual interest yielding five year bonds. This agreement has given us access to lower costs of funds on single-family mortgage securitizations.

As a result of this exceptional performance, we have consistently delivered on our commitment to paying stable distributions to unitholders. The Fund's distributable cash for the period June 15 (the IPO date) to December 31, 2006 was $7.9 million or $0.68 per unit. Since the IPO, distributions declared have totalled $6.1 million or $0.52 per unit which translates to a payout ratio of 76%. These monthly distributions represent an annualized distribution of $0.95 per unit, which is consistent with management's expectation at the time of the IPO.

Outlook

Based on the strength of our fundamentals and the current market conditions, we are optimistic about the year ahead. The Canadian economy as a whole, the principal driver of the single-family residential housing market, continues to show strength despite some weakness in Ontario.

From an interest rate perspective, housing continues to be affordable by historical standards. We see numerous opportunities arising in Western Canada due to the strong regional economy. The mortgage broker market should continue to grow rapidly as the distribution channel of choice in the mortgage industry.

Growth Strategy

Moray Tawse and I have retained an 80% interest in FNLP and, along with you, we are committed to its long-term growth and success.

There are four primary goals that form the basis for our growth strategy:

- providing a complete range of mortgage products;
- increasing mortgages under administration;
- lowering costs through efficient processes; and
- maintaining a conservative risk profile.

To realize these goals, we will leverage our leadership position with mortgage brokers and continue to innovate our operations and products to create efficiencies. One particular growth initiative for 2007 is the launch of single-family mortgages in Quebec.

Acknowledgements

I would like to recognize all the key players in First National's success this year. To our employees, I thank you for your ongoing commitment. I acknowledge my fellow board members for providing valued guidance and dedication to our unitholders. I extend gratitude to our mortgage brokers and customers for your support and feedback, which helps us develop innovative products to serve your evolving needs.

Finally, I offer a sincere thank you to our unitholders for entrusting us with your investment. We look forward to earning your trust again in the years ahead.

Yours truly,

Stephen Smith
President and Chairman

CORPORATE GOVERNANCE

Board of Directors 2006

BACK ROW: Stanley Beck, Robert Mitchell, Stephen Smith, Robert Courteau, John Harris
FRONT ROW: John Brough, Moray Tawse, Duncan Jackman

First National believes that investor trust and confidence comes from straightforward and transparent governance from its Board of Directors.

To properly guide the Fund towards ongoing success, management and the Board are committed to the highest standards of integrity. As such, the Board of Directors' role is clear and focused: to serve the long-term interests of our unitholders.

Policies

The Board has adopted several policies which reflect best practices in governance and disclosure. These include a Disclosure Policy, a Code of Business Conduct, a Whistleblower Policy and an Insider Trading Policy.

As a newly listed public company, the Board continues to develop and implement appropriate governance policies and practices.

Committees

Upon the closing of First National's IPO, the Board of Directors created an Audit Committee and a Compensation, Governance and Nominating Committee to further the effective functioning of the Fund's corporate governance strategy.

Audit Committee

The Audit Committee's responsibilities include:

- the oversight and supervision of the audit of the Fund's financial statements;
- the management of the relationship with the auditor of the Fund's financial statements;
- the oversight and supervision of the accounting and financial reporting practices and procedures of the Fund;
- the oversight and supervision of the adequacy of the Fund's internal accounting controls and procedures; and
- the oversight and supervision of the quality and integrity of the Fund's financial statements.

All of the Audit Committee members are independent directors and deemed financially literate for the purposes of the Canadian Securities Administrators' Multilateral Instrument 52–110 — Audit Committees.

Committee Members: John Brough (Chair), Duncan Jackman and Robert Mitchell

Compensation, Governance and Nominating Committee

The Compensation, Governance and Nominating Committee's responsibilities include:

- annually reviewing the President's goals and objectives for the coming year and providing an appraisal of the President's performance;
- making recommendations concerning compensation of the Fund's senior executive officers and the remuneration of the Board of Directors;
- developing the Fund's approach to corporate governance issues and compliance with applicable laws, regulations, rules, policies and orders with respect to such issues;
- advising the Board of Directors on filling director vacancies;
- periodically reviewing the composition and effectiveness of the directors and the contributions of individual directors; and
- adopting and periodically reviewing and updating the Fund's written disclosure policy.

All of the Compensation, Governance and Nominating Committee members are independent directors for the purposes of the Canadian Securities Administrators' Multilateral Instrument 58 – 101 — Disclosure of Corporate Governance Practices.

Committee Members: Stanley Beck (Chair), Robert Courteau and John Harris

BOARD MEMBERS

Stephen Smith, Chairman, is President and Co-Founder of First National. Mr. Smith has been an innovator in the development and utilization of various securitization techniques to finance mortgage assets and is a regular speaker at securitization and financial services conferences. Mr. Smith holds a Master of Science (Economics) from the London School of Economics and Political Science, a Bachelor of Science (Honours) in Electrical Engineering from Queen's University, and is a member of the Association of Professional Engineers of Ontario. He is also Vice-Chairman of the Greater Toronto Transit Authority (Go Transit).

Moray Tawse is Vice President, Mortgage Investments. He directs the operations of all commercial mortgage origination activities and is Co-Founder of First National. Mr. Tawse is one of Canada's leading experts on commercial real estate and is often called upon to deliver keynote addresses at national real estate symposiums. Prior to co-founding First National, Mr. Tawse was Manager of Mortgages for the Guaranty Trust Company of Canada from 1983 until 1988.

Stanley Beck, Q.C. has been President of Granville Arbitrations Limited (an arbitration and mediation firm) for more than five years. He was previously a Professor of Law and Dean at Osgoode Hall Law School in Toronto. From 1985 to 1990, Mr. Beck served as Chairman of the Ontario Securities Commission. Mr. Beck acts as a consultant on securities and corporate matters. In addition, Mr. Beck is the chairman of 407 International Inc. and GMP Capital Trust and serves on the board as a director of Scotia Utility Corp., Scotia NewGrowth Corp., Canadian Tire Bank Inc., Hollinger Inc. and Hollinger International.

John Brough is President of both Wittington Properties Limited (Canada) and Torwest, Inc. (United States) real estate investment companies. He has held these positions since 1998. From 1974 until 1996, he was with Markborough Properties Inc., where he was Senior Vice President and Chief Financial Officer from 1986 until 1996. From 1996 to 1998, Mr. Brough was Executive Vice President and Chief Financial Officer of iStar Internet, Inc. Mr. Brough is a director of Kinross Gold Corporation, Silver Wheaton Corp., Livingstone International Inc. and Rockwater Capital Corp. Mr. Brough holds a Bachelor of Arts (Political Science and Economics) from the University of Toronto and is a Chartered Accountant.

The Board of Directors consists of eight members, six of whom are independent.

Robert Courteau is the President and Managing Director of SAP Canada (an enterprise software company) and is responsible for all of SAP's business activities in Canada. Prior to joining SAP Canada in January 2004, Mr. Courteau served as the Executive Vice President responsible for Canadian sales and consulting services for EDS Corporation. Mr. Courteau graduated from Concordia University with a Bachelor of Commerce degree.

John Harris is the Chairman and Chief Executive Officer of Harris Steel Group Inc. Employed by Harris Steel Inc. since 1974, Mr. Harris was appointed President and Chief Operating Officer of Harris Steel Group Inc. in 1994 and was named Chairman and Chief Executive Officer in 2005. Mr. Harris has a Bachelor of Arts degree from Trent University and a Master of Business Administration degree from the University of Toronto.

Duncan Jackman has been the Chairman and Chief Executive Officer of E-L Financial Corporation Limited (an insurance holding company) since 2003 and the Chairman and Chief Executive Officer of both Economic Investment Corporation (a closed end investment trust) and United Corporations Limited (a closed end investment trust) since 2001. Prior to this, Mr. Jackman held a variety of positions, including portfolio manager at Cassels Blaikie and investment analyst at RBC Dominion Securities. Mr. Jackman holds a Bachelor of Arts (Honours) in Literature from McGill University.

Robert Mitchell has been President of Dixon Mitchell Investment Counsel Inc., a Vancouver-based investment management company since 2000. Prior to that, Mr. Mitchell was Vice President, Investments at Seaboard Life Insurance Company. Mr. Mitchell is a director and chairman of the audit committee for Discovery Parks Holdings Ltd., trustee for Discovery Parks Trust. Discovery Parks Trust was established to support the high technology and research industries in British Columbia through the development of its real estate assets. Mr. Mitchell has a Master of Business Administration from the University of Western Ontario, a Bachelor of Commerce (Finance) from the University of Calgary, and is a CFA charterholder.

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following management's discussion and analysis of financial condition and results of operations is prepared as of February 28, 2007. This discussion should be read in conjunction with the consolidated financial statements of First National Financial Income Fund (the "Fund") and First National Financial LP ("FNLP") as at and for the nine-months ended December 31, 2006 (as applicable) and the notes thereto. This discussion should also be read in conjunction with the audited financial statements and notes thereto of First National Financial Corporation (as predecessor to First National LP – "FNFC") for the year ended March 31, 2006. The consolidated financial statements of the Fund and FNLP have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP").

The Fund earns income from its 19.97% interest in FNLP. The Fund accounts for its investment in FNLP using the equity method and therefore does not consolidate the results of operations of FNLP. As a result, financial statements with accompanying notes thereon have been presented for both the Fund and FNLP. In addition, the following management's discussion and analysis ("MD&A") presents a discussion of the financial condition and results of operations for both the Fund and FNLP.

Information for the nine-month period ended December 31, 2006 for FNLP includes information from FNLP and its predecessor, FNFC. Historical comparative information refers to FNFC.

This MD&A contains forward-looking statements. Please see "Forward-Looking Statements" for a discussion of the risks, uncertainties and assumptions relating to these statements. The selected financial information and discussion below also refers to certain measures to assist in assessing financial performance. These "non-GAAP measures" such as "EBITDA", "Adjusted Net Income", "Distributable Cash", and "Distributable Cash per Unit" should not be construed as alternatives to net income or loss or other comparable measures determined in accordance with GAAP as an indicator of performance or as a measure of liquidity and cash flow. Non-GAAP measures do not have standard meanings prescribed by GAAP and therefore may not be comparable to similar measures presented by other issuers.

The Fund is entirely dependent upon the operations and financial condition of FNLP. The earnings and cash flows of FNLP are affected by certain risks. For a description of those risks, please refer to the "Risk and Uncertainties Affecting the Business" section.

Unless otherwise noted, monetary amounts are in thousands of Canadian dollars.

Additional information relating to the Fund and FNLP is available on the Fund's profile on the System for Electronic Data Analysis and Retrieval ("SEDAR") website at ***www.sedar.com.***

General Description Of The Fund And First National Financial LP

Pursuant to an underwriting agreement dated June 6, 2006 and initial public offering ("IPO"), the Fund sold 10,600,000 units of the Fund ("Fund Units", "Units", or "Unit"), at a price of $10.00 per Unit for proceeds totaling $106 million. The proceeds of the offering were used to partially fund the indirect acquisition (through the Fund's wholly-owned subsidiary, First National Financial Operating Trust) by the Fund of a 17.94% interest in First National Financial LP ("FNLP"). The underwriters were also granted an over-allotment option to purchase 1,200,000 Units at $10.00 per Unit. The option was exercised in full on July 11, 2006. Accordingly, the Fund indirectly holds a 19.97% interest in FNLP and First National Financial Corporation holds an 80.03% controlling interest in FNLP.

Concurrent with the initial public offering and as part of the acquisition agreement between FNLP and FNFC on June 15, 2006, FNLP purchased all of FNFC's assets and assumed its liabilities, except for future income tax liabilities, which are payable by FNFC. The consideration for this purchase was:

- the issuance of 48,486,316 exchangeable Class B LP units to FNFC
- an acquisition promissory note of $10.94 million, which has been accounted for as a distribution in FNLP's financial statements;
- a working capital note in the amount of $6.4 million, representing the difference between the net assets, except future income tax liabilities, of FNFC as at March 31, 2006 and the net assets transferred to FNLP as at June 14, 2006. The issuance of this note has also been accounted for as a distribution in FNLP's financial statements.

First National Financial Income Fund

The Fund is an unincorporated, open-ended trust established under the laws of the Province of Ontario on April 19, 2006, pursuant to a Declaration of Trust. The Fund has been established to acquire and hold, through a newly constituted wholly owned trust, First National Financial Operating Trust (the "Trust"), investments in the outstanding limited partnership units of FNLP. Each unitholder participates pro rata in any distribution from the Fund. Income tax obligations related to the distributions of the Fund are the obligations of the unitholders.

The Fund effectively commenced operations through its indirect investment in FNLP on June 15, 2006, and the income reported by the Fund commenced on that date.

Selected Quarterly Information

Quarterly Results (in $000s except per unit amounts)

	Net Income Revenue	Net Income for the period	($/Unit)	Total Assets
2006				
Fourth Quarter	$ 1,602	$ 1,596	0.14	$ 110,417
Third Quarter	$ 1,825	$ 1,819	0.16	$ 111,617
Second Quarter	$ 488	$ 487	0.05	$ 100,128

Investments

At December 31, 2006 the Fund has an investment in 11,800,000 units (19.97%) of First National Financial LP at a cost of $111.6 million. Under Canadian GAAP, the Fund is required to account for this investment using the equity method. During the period June 15, 2006 to December 31, 2006, the Fund's earnings from FNLP were $3.9 million and the carrying value of this investment at December 31, 2006 was $109.5 million. During the period from October 1, 2006 to December 31, 2006, the Fund's earnings from FNLP were $1.6 million.

Expenses

Trust administration expenses include trustees' fees and travel costs.

Distributions

The initial public offering described above closed on June 15, 2006. The Fund made its first distribution of $0.11875 per Unit, representing a monthly distribution of $0.07917 per Unit plus the stub period of June 15, 2006 to June 30, 2006, on August 15, 2006. Beginning on September 15, 2006, the Fund made monthly distributions of $0.07917 per unit on or around the 15th of each month. On December 14, 2006, the Fund declared its sixth distribution in the amount of $0.07917 per unit payable January 15, 2007. These distributions of approximately $6.1 million are equivalent to the distributions that the Fund receives from FNLP. Consistent with management's expectation at the time of the IPO, these distributions represent an annualized distribution rate of $0.95 per unit. As shown in the following table, the Fund's payout ratio based on distributable cash is approximately 76% since the IPO.

Statement of Distributable Cash

(in $000s except per unit amounts)

	For the three-months ended December 31, 2006	For the Period June 15 to December 31, 2006
First National Financial LP		
Net Income	18,038	40,148
Amortization	290	589
EBITDA [(1)]	18,328	40,737
Maintenance Capital Expenditures	124	341
Distributable Cash from First National Financial LP	18,204	40,396
First National Financial Income Fund		
Weighted Average Share of Distributable Cash from First National Financial LP	3,635	7,957
Trust Administration Expenses	6	13
Distributable Cash from First National Financial Income Fund [(2)]	3,629	7,944
Distributable Cash per Unit ($/Unit) [(2)]	0.31	0.68
Distributions Declared	2,803	6,072
Distributions Declared per Unit ($/Unit)	0.24	0.52

[(1)] EBITDA is a non-GAAP measure that represents earnings generated to fund capital investment, meet financial obligations and fund distributions. It is considered a key measure as it demonstrates the ability of the business to meet its capital and financing commitments.

[(2)] Distributable cash and distributable cash per unit are non-GAAP measures generally used by Canadian open-ended trusts as an indicator of financial performance. They are considered key measures as they demonstrate the cash available for distributions to unit holders.

Income Taxes

The Fund is a mutual fund trust for income tax purposes. As such, the Fund is only taxed on any amount not allocated to unitholders. The Fund intends to distribute substantially all of its taxable income to its unitholders and the Fund intends to comply with the provisions of the Income Tax Act (Canada) that permit, amongst other items, the deduction of distributions to unitholders from the Fund's taxable income.

Outstanding Securities of the Fund

At December 31, 2006 and at February 28, 2007, the Fund had 11,800,000 units outstanding.

First National Financial Corporation holds 47,286,316 exchangeable Class B LP units of FNLP, each of which is exchangeable into one Fund Unit at no cost at any time at the option of First National Financial Corporation, and each of which carries a Special Voting Right that entitles the holder to receive notice of, attend and vote at all meetings of unitholders of the Fund.

Critical Accounting Estimates

Management makes estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the Consolidated Financial Statements, and revenues and expenses during the reporting period. Management reviews these estimates on an ongoing basis, including those related to securitization accounting. Changes in facts and circumstances may result in revised estimates and actual results may differ from these estimates.

Business Risks

The Fund is entirely dependent upon the operations and financial condition of FNLP. The earnings and cash flows of FNLP are affected by certain risks. For a description of those risks, please refer to the Risk and Uncertainties Affecting the Business section in the First National Financial LP portion of this analysis.

Guarantee

The Fund's wholly-owned subsidiary, First National Financial Operating Trust has provided guarantees to and subordinated their rights to receive payments from FNLP in respect of FNLP's bank credit facility.

First National Financial LP

Basis of Presentation

The financial statements of First National Financial LP ("FNLP" or the "Company") are prepared in accordance with Canadian Generally Accepted Accounting Principles ("GAAP").

FNLP is considered to be a continuation of First National Financial Corporation's ("FNFC's" or the "Company's") business following the continuity of interest method of accounting. Under the continuity of interest method of accounting, FNLP's acquisition of the FNFC business is recorded at the net book value of FNFC's business assets and liabilities on June 14, 2006 and the equity of FNLP represents the equity of the FNFC business at that date.

The consolidated statements of income and cash flows for the nine-months ended December 31, 2006 reflect the activities of the FNFC business from April 1, 2006 to June 14, 2006 and the activities of FNLP for the period June 15, 2006 to December 31, 2006. The comparative figures represent the historic activities of FNFC.

Executive Summary

The recent quarter and year-to-date performance is fully consistent with management's expectations. The Company continues to have growth in mortgages under administration from increasing mortgage origination volumes, especially in the prime single-family and Alt–A markets.

Highlights

- Mortgages under administration grew to $24.4 billion at December 31, 2006 from $22.7 billion at September 30, 2006, an increase of 7.5%; the growth from December 31, 2005, when mortgages under administration were $18.6 billion, was 31.2%;
- Revenue for the nine-months ended December 31, 2006 grew by 46% over the comparative period;
- Adjusted EBITDA increased by 24% for the nine-month period ended December 31, 2006 in comparison to the same period in the prior year. This increase has resulted from higher volumes experienced in many aspects of the company's business including placement fees on higher origination volumes, servicing income derived from the larger portfolio of mortgages under administration, and gains on securitization earned from higher Alt-A and commercial mortgage origination.

Selected Annual Financial Information for the Company's fiscal year ends
(in $000s except per unit amounts)

	December 31, 2006 [(1)]	March 31, 2006	March 31, 2006
For the Period			
Income Statement Highlights			
Revenue	156,427	144,643	102,226
Brokerage fees	(67,891)	(47,915)	(37,971)
Other operating expenses	(37,007)	(37,796)	(36,298)
EBITDA [(2)]	51,529	58,932	27,957
Amortization of capital assets	(803)	(895)	(708)
Interest paid to shareholders	–	(1,711)	(1,695)
Provision for income taxes	(3,312)	(19,994)	(9,290)
Net Income	47,414	36,332	16,264
Distributions declared	30,406	–	–
Per Unit Highlights			
Net Income per unit [(3)]	0.80	0.61	0.28
Distributions declared per unit	0.51	N/A	N/A
At Period End			
Balance Sheet Highlights			
Total assets	528,116	279,751	253,190
Total long-term financial liabilities	–	–	13,700

(in $000s except where noted)	December 31, 2006 [(1)]	March 31, 2006	March 31, 2005
Reconciliation of EBITDA to Adjusted EBITDA			
EBITDA[(2)]	51,529	58,932	27,957
Historic management compensation expenses [(4)]	917	700	8,500
Revised management compensation [(5)]	(1,125)	(1,500)	(1,500)
Adjusted EBITDA [(2)]	51,321	58,132	34,957

[(1)] December 31, 2006 figures are for the nine-month period ended December 31, 2006.

[(2)] EBITDA and Adjusted EBITDA are not recognized earnings measures under GAAP and do not have standardized meanings prescribed by GAAP. Therefore, EBITDA and Adjusted EBITDA may not be comparable to similar measures presented by other issuers. Investors are cautioned that EBITDA should not be construed as an alternative to net income or loss determined in accordance with GAAP as indicators of the Company's performance or as an alternative to cash flows from operating, investing and financing activities as a measure of liquidity and cash flows.

[(3)] Per unit amounts calculated as if the Company converted to a partnership on April 1, 2004 and issued 59,086,316 partnership units so that these measures are comparable among the periods show. Prior to June 15, 2006, the Company had two shares outstanding.

[(4)] Management compensation for each of the two senior management executives while FNFC operated as a private company.

[(5)] Normalized compensation for each of the two senior management executives consistent with compensation policies that have been implemented on closing of the IPO.

Vision

The Company provides mortgage financing solutions to virtually the entire mortgage market in Canada. By offering a full range of mortgage products with a focus on customer service and superior technology, the Company views itself as one of the leading "non-bank" mortgage lenders in the industry. Growth has been achieved while maintaining a relatively conservative risk profile. The Company sees itself levering on these strengths to continue to lead the "non-bank" mortgage lending industry in Canada, managing risk appropriately.

Strategy

The Company's strategy is built on four cornerstones: providing a full range of mortgage products; growing assets under administration; employing leading edge technology to lower costs and rationalize business processes; and maintaining a conservative risk profile. An important consequence of the Company's strategy is the direct relationship with the mortgage borrower. Although the Company places most of its originations with third parties, FNLP is perceived by all of its borrowers as the mortgage lender. This is a critical distinction. It allows the Company to communicate with each borrower directly throughout the term of the related mortgage and negotiate new transactions and pursue marketing initiatives. Management believes this strategy will provide long-term profitability and branding for the Company.

Key Performance Drivers

The Company's success is driven by the following factors:

- Growth in portfolio of mortgages under administration;
- Growth in origination of higher margin mortgages; and
- Lowering the costs of operations through the innovation of systems and technology.

Growth in Portfolio of Mortgages under Administration

Management considers the growth in mortgages under administration a key element of the Company's performance. The portfolio grows in two ways: through mortgages originated by the Company and mortgage servicing portfolios purchased from third parties. Mortgage originations not only drive placement fee and gain on securitization revenues, but perhaps more importantly, longer term values such as servicing fees, mortgage administration fees, renewal opportunities and a customer base for marketing initiatives. For the nine-months ended December 31, 2006, mortgages under administration grew to $24.4 billion from $19.6 billion as at March 31, 2006, an annualized rate of increase of 33%. During the current quarter, mortgages under administration grew to $24.4 billion from $22.7 billion as at September 30, 2006. This is an annualized increase of 30%. This growth is primarily organic, created from new originations of $6.0 billion in the nine-month period net of normal run-off. This compares favorably with the nine-month period ended December 31, 2005 when originations totaled $4.7 billion. For the nine-months ended December 31, 2006, non-originated servicing business increased mortgages under administration by $1.3 billion.

Growth in Origination of Higher Margin Mortgages

While the Company's main focus is on the Prime single-family mortgage market, during 2006 FNLP has launched strategies to increase volumes in both the Alt-A and CMBS markets by leveraging on existing infrastructure and distribution channels. Alt-A describes single-family residential mortgages that are originated using broader underwriting criteria than those applied in originating prime mortgages. Alt-A borrowers are generally considered "A" quality borrowers in terms of their credit histories, but do not qualify for a prime mortgage because of non-conformities, such as the degree of income disclosure and verification required. These markets are relatively more profitable than conventional mortgage lending markets and add to economies of scale in the Company's operations by further increasing mortgages under administration. The Company has been successful in increasing volume for both of these products. For the nine-month period ended December 31, 2006, the Company originated $432 million of Alt-A mortgages and $285 million of CMBS mortgages. These volumes contrast the prior year's comparative period ended December 31, 2005 when the Company originated $151 million of Alt-A mortgages and $224 million of CMBS mortgages. For the current quarter the comparative volumes are $155 million versus $55 million for Alt-A and $115 million versus $123 million for CMBS. At December 31, 2006, the Company's securitized Alt-A mortgages under administration totaled $569 million.

Lowering Costs of Operations through Innovation of Systems and Technology

The Company has always used technology to provide for efficient and effective operations. This is particularly true for its MERLIN underwriting system, Canada's only web-based real time broker information system. By creating a paperless, 24/7 available commitment management platform for mortgage brokers, the Company has reached a place among the top three ranked lenders in market share in the broker channel. This has translated into increased single-family origination volumes and higher closing ratios (the percentage of mortgage commitments that the Company issues that actually become closed mortgages). The nine-months ended December 31, 2006 showed single-family origination volumes of $4.7 billion, which compares to $3.4 billion for the same period ended on December 31, 2005.

Canada Mortgage Bond as a New Funding Source

The Canada Mortgage Bond ("CMB") is an initiative introduced by Canada Mortgage and Housing Corporation whereby the Canada Housing Trust issues securities to investors in the form of semi-annual interest yielding five year bonds the proceeds of which are used to buy NHA mortgage backed securities. In the quarter ended September 30, 2006, the Company entered into an agreement with a Canadian bank which allowed the Company to indirectly sell a portion of the Company's single-family mortgage origination into the September issue of the CMB. Pursuant to the same agreement, the Company indirectly sold a smaller amount into the December 2006 CMB issue. Because of the similarities to a traditional Government of Canada bond (both have five year

unamortizing terms with a government guarantee), the CMB trades in the capital markets at only a modest premium to the yields on Government of Canada bonds. For the Company, this agreement has given the Company access to lower costs of funds on single-family mortgage securitizations.

First National Mortgage Trust as Special Purpose Vehicle

In another initiative to increase gain on securitization revenue, the Company created a special purpose vehicle, First National Mortgage Trust, in March 2006 for the purpose of financing its mortgages through the issuance of R-1(High) and R-1(Mid) rated ABCP directly in the Canadian public debt markets. The Company uses both this vehicle and bank sponsored conduits to access the CP markets; however the cost of funding through First National Mortgage Trust is considerably cheaper. The amount of commercial paper notes issued by this trust grew from Nil at March 31, 2006 to over $478 million as at December 31, 2006.

Key Performance Indicators

The principal indicators used to measure the Fund's performance are:

- Earnings before income taxes, depreciation and amortization after normalizing management compensation while the Company was a private entity ("Adjusted EBITDA")
- Distributable cash.

Adjusted EBITDA is not a recognized measure under Canadian generally accepted accounting principles ("GAAP"). However, management believes that Adjusted EBITDA is a useful measure to provide investors with an indication of cash available for distribution prior to capital expenditures and income taxes. Adjusted EBITDA should not be construed as an alternative to net earnings determined in accordance with GAAP or to cash flows from operating, investing and financing activities. The Fund's method of calculating Adjusted EBITDA may differ from other issuers and, accordingly, Adjusted EBITDA may not be comparable to measures used by other issuers. Management believes that the cash generation performance of the operations is better monitored by Adjusted EBITDA and provides a better comparative to the operations of the Company while it was a private entity.

Distributable cash is not a defined term under GAAP. It is determined by the Fund as earnings before income taxes adjusted for non-cash expenses, including depreciation and amortization, and reduced by maintenance capital expenditures and current income taxes. Management believes that net cash generated by the Fund prior to distribution is an important measure for investors to monitor. Some consider this measure to be more important than actual cash distributions. Any distribution in excess of the distributable cash means a depletion of the cash reserve, while any distribution below the distributable cash means that the reserves are being built for future investments, to serve as a buffer for operations over economic cycles or to reimburse outstanding debt.

(in $000s except where noted)	Three-months ended		Nine-months ended	
	December 31, 2006	December 31, 2005	December 31, 2006	December 31, 2005
For the Period				
Revenue	49,551	34,899	156,427	107,140
Net income	18,038	8,080	47,414	25,848
Adjusted EBITDA [(1)]	18,328	13,014	51,321	41,295
Less:				
Public company expenses	–	250	250	750
Maintenance capital expenditures	124	117	539	462
Distributable cash [(2)]	18,204	12,647	50,532	40,083
At Period end				
Total assets	528,116	393,016	528,116	393,016
Mortgages under administration	24,359,481	18,607,866	24,359,481	18,607,866

[(1)] This Non-GAAP measure adjusts income before income taxes by adding back expenses for management compensation and interest expense on shareholder loans which consist primarily of distributions to shareholders while First National operated as a private company. This measure also includes a deduction of $1,500,000 for normalized compensation for each of the two senior management executives based on compensation policies that will take effect on closing of the initial public offering.

[(2)] This Non-GAAP measure adjusts Adjusted EBITDA by deducting public company expenses and maintenance capital expenditures. The comparative figures assume the Company incurred public company expenses in the prior period as described in the initial public offering prospectus.

Reconciliation of distributable cash to cash provided by (used in) operations

(in $000s except where noted)	Three-months ended		Nine-months ended	
	December 31, 2006	December 31, 2005	December 31, 2006	December 31, 2005
For the Period				
Cash provided by (used in) operating activities	37,222	51,516	(36,086)	23,372
Add:				
Provision for income taxes - current	–	3,862	4,239	9,108
Interest on shareholder loans	–	432	–	1,300
Funding of increase in securitization receivable [(1)]	10,752	870	20,100	12,411
Net change in non-cash working capital balances related to operations [(2)]	(29,491)	(43,480)	63,778	(3,928)
Less:				
Normalized management compensation	–	50	208	550
Amortization of purchased mortgage servicing rights	155	136	502	418
Public company expenses [(3)]	N/A	250	250	750
Maintenance capital expenditures	124	117	539	462
Distributable cash [(4)]	18,204	12,647	50,532	40,083

[(1)]Funding of the increase in securitization receivable represents the difference between gains on securitization recorded on the sale of mortgages to securitization vehicles in a period and the cash received from prior periods' securitizations.

[(2)]The Company's working capital balances consist of: "Accounts receivable and sundry", "Mortgages accumulated for sale", Accounts payable and accrued liabilities", "Management bonuses payable", "Shareholder loan", and "Current taxes payable". "Mortgages accumulated for sale" represents mortgages held temporarily until settlement, usually for a period not exceeding seven days, with institutional investors or securitization vehicles.

[(3)]For the quarter and nine-months ended December 31, 2005, these figures are pro-forma amounts to provide a suitable comparative to the current quarter's actual figures.

[(4)]This Non-GAAP measure adjusts Adjusted EBITDA by deducting public company expenses and maintenance capital expenditures. The comparative figures assume the Company incurred public company expenses in the prior period as described in the initial public offering prospectus.

Revenues and Funding Sources

Mortgage Origination

The Company derives a significant amount of its revenue from mortgage origination activities. The majority of mortgages originated are funded by either placement with institutional investors or sale to securitization conduits, in each case with retained servicing. Depending upon market conditions, either an institutional placement or a securitization conduit may be the most cost-effective means for the Company to fund individual mortgages. In general, originations are allocated from one funding source to another depending on market conditions and strategic considerations related to maintaining diversified funding sources. The Company retains servicing rights on virtually all of the mortgages it originates, which provides the Company with servicing fees to complement revenue earned through originations. For the nine-months ended December 31, 2006, origination volume grew from $4.7 billion to $6.0 billion or 28% over the same period in the prior year. For the quarter ended December 31, 2006, origination volume grew from $1.6 billion to $1.7 billion or 6% over the same quarter in the prior year.

Placement Fees and Gain on Securitization

The Company recognizes revenue at the time that the mortgage is placed with the institutional investor or sold to the securitization conduit. Cash amounts received in excess of the mortgage principal at the time of sale are recognized in revenue as "Placement fees". The present value of additional amounts (excess spread) expected to be received over the remaining life of the mortgages sold (net of servicing and other costs) are recognized as a "Gain on securitization".

The excess spread on a mortgage is the difference between the interest rate on the mortgage and the yield earned by the investor after accounting for all anticipated prepayment provisions, servicing obligations and other costs. For Alt-A and small conventional multi-unit residential and commercial mortgages, the excess spread also includes assumptions for credit losses.

Upon the recognition of the "Gain on securitization", the Company establishes a "Securitization receivable" which is amortized as spread income is received by the Company. In addition, the Company is also required to establish a "servicing liability", which represents the future cost of servicing the securitized mortgages. As spread income is received by the Company, both the securitization receivable and the servicing liability are amortized accordingly. Residual securitization income consists of two components, the difference between a) the spread income received over time and the spread income assumed in the Company's derivation of securitization receivable at the time of sale; and b) the amortization of the servicing liability. The excess is attributable to better than expected cash flows being earned by the securitization than those anticipated when gain on sale assumptions regarding prepayments, cost of funds, and credit losses are originally forecasted.

For all institutional placements and loans securitized through NHA-MBS and CMBS, the Company earns "Placement fees". In addition, under certain circumstances, additional revenue from institutional placements and NHA-MBS may be recognized as a "Gain on securitization". Revenues based on these originations are equal to either (1) the present value of the excess spread, or (2) an origination fee based of the outstanding principal amount of the mortgage. This revenue is received in cash at the time of placement. Of the Company's $6.0 billion of originations for the nine-months ended December 31, 2006, $4.5 billion was placed with institutional investors, $87 million was sold under the NHA-MBS program and $285 million was originated for sale to CMBS conduits.

All loans securitized through the Company's ABCP program are recognized as a "Gain on securitization", as is a portion of the spread earned from NHA-MBS. Of the Company's $6.0 billion of originations for the quarter ended December 31, 2006, $1.1 million was sold to ABCP conduits, generating "Gain on securitization" revenue. The Company also acquires other significant amounts of mortgages for sale to its ABCP programs from other institutions. For the nine-months ended December 31, 2006, the Company acquired approximately $675 million of such mortgages.

In the past several years, the Company has experienced significant growth in mortgages funded through its ABCP securitization programs. As a result, revenue from "Gain on securitization" has increased accordingly. Since cash flows received from securitized assets are received over the life of the mortgage, and the revenue is recognized upon origination, there will be a timing difference between the recognition of revenue and the receipt of cash. This is not unlike most companies that record the revenue from sales at the time that goods are sold or shipped and set up a receivable until the cash is actually received. The financial effect of the timing difference between the recognition of revenue and the receipt of cash is effectively equal to the "Gain on securitization" less "Amortization of securitization receivable" (net of "Amortization of servicing liability") in any given year. For the fiscal year ended March 31, 2006, the timing difference required working capital funding of approximately $10.6 million. For the nine-months ended December 31, 2006, the volume of mortgages funded through ABCP programs has increased and the Company funded approximately $10.6 million in upfront fees to support purchases of mortgages from institutions. This timing difference required working capital funding of approximately $20.1 million. To the extent that gains on securitization do not increase for a number of years, the effects of the timing difference would be neutralized as new securitization receivables would be offset by collections of existing securitization receivables.

Mortgage Servicing and Administration

The Company services virtually all mortgages generated through its mortgage origination activities on behalf of a wide range of institutional investors. Mortgage servicing and administration is a key component of the Company's overall business strategy and a significant source of continuing income and cash flow. In addition to pure servicing revenues, fees related to mortgage administration are earned by the Company throughout the mortgage term. Another aspect of servicing is the administration of funds held in trust including: borrower's property tax escrow, reserve escrows, and mortgage payments. As acknowledged in the Company's agreements, any interest earned on these funds accrues to the Company as partial compensation for administration services. The Company has negotiated favorable interest rates on these funds with the chartered bank which maintains the deposit account and earns significant interest revenue.

In addition to the interest income earned on securitization receivables, the Company also earns interest income on mortgage related assets, including mortgages accumulated for sale, mortgage and loan investments and purchased mortgage servicing rights.

Results of Operations

The following table sets forth information on the volume of mortgages originated by First National and the mortgages under administration for the periods indicated:

(in $ millions)	Quarter ended		Nine-months ended	
	December 31, 2006	December 31, 2005	December 31, 2006	December 31, 2005
Mortgage Originations By Asset Class				
Single-family residential	1,138	1,076	4,669	3,406
Multi-unit residential and commercial	580	551	1,306	1,250
Total originations	1,718	1,627	5,975	4,656
Funding of Mortgage Originations by Source				
Institutional investors	1,161	1,148	4,518	2,938
CMBS	115	123	285	224
NHA-MBS	22	40	87	148
ABCP and Company internal resources	420	316	1,085	1,346
Total	1,718	1,627	5,975	4,656
Mortgages Under Administration				
Single-family residential	14,145	10,157	14,145	10,157
Multi-unit residential and commercial	10,214	8,451	10,214	8,451
Total	24,359	18,608	24,359	18,608

The Company experienced steady growth in the nine-month period ended December 31, 2006. Total mortgage origination increased from $4.7 billion in the nine-month period of 2005 to $6.0 billion for the period ended December 31, 2006, representing an increase of 28%. Total mortgage origination for the three-month period ended December 31 increased from $1.63 billion in the corresponding quarter of 2005 to $1.72 billion for the quarter ended in 2006, representing an increase of 6%. Overall the 28% growth reflects the Company's growing market share in the single-family residential mortgage broker channel and competitive rates posted in Q3 of this year. For the quarter, the year over year origination growth was slower relative to the significant growth in originations experienced in the third quarter. Total revenues for the nine-months ended December 31, 2006 compared to the same period ended December 31, 2005, increased by 46% from $107 million to $156 million. Total revenues for the fourth quarter were $50 million compared to the $35 million for the corresponding period in the prior year, representing an increase of 43%. This growth results primarily from increased origination volume as well as securitization activities. The Company purchased and securitized $675 million of insured single-family mortgages in the nine-month period and recorded gains on securitization of $12.4 million as well as significant increases in Alt-A securitization gains due to increased origination. Mortgage servicing revenue has also increased due to the substantial increase in the mortgages under administration between 2005 and 2006.

The timing of revenues recognized on CMBS securitization also had a small impact. These revenues are recognized at the time CMBS mortgages are sold into securitization vehicles. In the nine-months ended December 31, 2005, the Company went to market with two pools of mortgages and recorded placement fee revenues of $6.2 million regarding CMBS mortgages. For the nine-months ended December 31, 2006, the company securitized one normal sized pool as well as contributing $23 million of CMBS mortgages to a Merrill Lynch issue and recognized $3.0 million of revenue in placement fees. This decrease is also reflective of tighter spreads in the CMBS market. At December 31, 2006, First National has $173 million under administration awaiting CMBS placement in early 2007.

Placement Fee Revenue

Comparing the nine-months ended December 31, 2006 to the same period ended December 31, 2005, placement fee revenue increased by 46%, to $73.1 million from $50.0 million. This is largely due to the growth of mortgages originated for institutional placement which increased by 53% period over period. The timing of CMBS securitization as described above offset this growth by approximately 6%.

Gain on Securitization Revenue

Gain on securitization revenue increased by 49%, to $37.8 million from $25.4 million. The increase is primarily due to two securitizations, through the Company's commercial paper conduit. In the current

quarter, the Company purchased two portfolios totaling $265 million of single-family mortgages which were securitized for a gain of $5.0 million. Second, as a consequence of a securitization of the Company's mortgages indirectly through the CMB distribution channel, the Company recorded gains on securitization of $7.4 million. Although the volume of mortgages originated for ABCP conduits has decreased from the nine-month period ended December 31, 2005 to the current period by 19%, gain on securitization revenue has not been affected greatly. This is a result of the significant growth in Alt-A origination which is securitized by the Company. Alt-A securitization is more profitable than the securitization of prime mortgages. In the nine-months ended December 31, 2006, the company securitized $432.6 million of Alt-A mortgages. In the comparable period of the prior year, the securitized volume was $152.3 million, an increase of 184% accounting for a $7.5 million increase in gain on securitization revenue.

Mortgage Servicing Revenue

Mortgage servicing income increased by 51%, to $29.2 million from $19.3 million which is primarily due to the growth in the portfolio of mortgages under administration which grew by 31% from period to period, in particular the residential component which grew by 39%. The higher servicing rates associated with residential and a greater portion of origination being placed as opposed to securitized for much of the year, has also lead to revenue increases for mortgage servicing. Another aspect of this revenue is interest earned on funds held in trust. These funds are administered by the Company and include borrowers' property tax escrow. This income was $7.0 million for the 2006 nine-month end and $3.6 million for the 2005 comparative. The dramatic increase is due to the increase in short-term interest rates and the amount of funds held in trust. At December 31, 2006 the amount of funds held in trust were $289 million (2005 - $236 million) and the average 30 day Canadian Deposit Offer Rate ("CDOR"), which is a benchmark for short-term interest rates increased from 3.15% for the 2005 quarter end to 4.33% for the December 31, 2006 quarter end, an increase of 37.5%.

Mortgage Investment Income Revenue

Mortgage investment income increased by 34%, to $11.4 million from $8.5 million. This increase is due to increased investment in mortgage assets held on balance sheet, including mortgages accumulated for sale, securitization receivable, mortgage and loan investments and purchased mortgage servicing rights. Together these assets, excluding mortgages accumulated for sale which turnover daily, have increased by 42% from March 31, 2006 to December 31, 2006. While short-term interest rates have risen (prime lending rate averaged 5.93% for the nine-months ended December 2006 and was 4.44% for the comparative period), this variable only affects mortgage and loan investments interest revenue. In comparison, residential five year posted mortgage rates remained steady, fluctuating between 5.90% on April 11, 2005 to 6.00% on December 12, 2006. These increases are offset by lower rates earned on securitization receivables. The average discount rates implicit in the securitization receivables have decreased as mortgages securitized at 10% rates in the periods prior to April 1, 2005 run off. These have been replaced by new assets being discounted at 7%.

Residual Securitization Income Revenue

Residual securitization income increased by 28%, to $5.0 million from $3.9 million. The primary source of this revenue is the amortization of the servicing liability, which represents the servicing portion of the spread received from securitization conduits. It also includes the excess cash flows received over the expected cash flows received from securitization vehicles. The increase from the prior year's quarter is a function of the growth of the securitization receivable which grew by 44% from the comparative quarter. The growth has been offset by a reduction of gains related to "lock-in" transactions. This revenue is earned when borrowers elect to change the terms of their mortgage from floating rate to fixed rate. The December 2005 period featured a significant amount of lock-in revenue as the Company sold these mortgages to institutional investors at going placement fee rates. Because of the conservatism of the Company's assumptions in recording the securitization receivable associated with these mortgages, the placement fees normally exceeded the carrying value of the securitization revenue. In the current nine-month period ended December 31, 2006 quarter, there has been a significant reduction in such lock-in transactions due in part to the stability of short-term interest rates such that borrowers do not have the same incentive to change their mortgage terms.

Brokerage Fees Expense

Brokerage fees expense increased by 78%, to $67.9 million from $38.2 million. The increase is due primarily to the increased single-family residential origination between the periods of 37%. As virtually all single-family mortgage originations are sourced through brokers these percentage changes should be comparable. Additional increases are attributable to $10.6 million of costs incurred to purchase $675 million of mortgages for securitization as described previously in the gain on securitization section above. These expenses accounted for 28% of the increase over and above origination volumes. The remaining increase of 13% pertains to three factors: increased volume bonus costs, the increase of Alt-A volume which has higher broker fees and new insurance costs to support the Company's home warranty program launched in September 2005. Because of the Company's success in single-family origination, more brokers qualify for the Company's volume bonus incentives this period than in the comparative period. Alt-A origination requires higher broker fees due to the increased credit adjudication information needed from brokers. Because Alt-A volume increased by 184% between the periods, this had an effect on overall brokerage fees expense.

Salaries and Benefits Expense

Salaries and benefits expense increased by 31%, to $21.3 million from $16.2 million. To support the increase in mortgage origination and servicing a larger mortgage portfolio under administration, the Company has added to its head count. As at December 31, 2006 the Company had 352 employees and 292 as at December 31, 2005. The 30% overall

increase in salaries is consistent with the increase in mortgages under administration of 30%. The Company also introduced an RRSP matching program in March 2006 which accounted for approximately 3% of the increase. Management salaries are paid to the two senior executives who are indirectly the Class B LP unitholders. The current period's expense includes an increase to this expense as a result of the revised compensation arrangement executed on closing of the initial public offering.

Interest Expense

Interest expense increased by 89%, to $7.0 million from $3.7 million. This has been primarily driven by rising interest rates and increased use of the Company's credit facility for commercial mortgage investments and CMBS warehousing. As described in the "Liquidity and cash resources" section of this analysis, the Company warehouses a portion of the mortgages it originates prior to settlement with the ultimate investor. The Company uses the credit facility with its banking syndicate to fund the mortgages in this period. First National's average investment in commercial mortgages and CMBS warehoused mortgages for the quarter ended December 31, 2006 increased by 62% from the comparative period's amount. As described above regarding mortgage investment income, short-term interest rates also increased about 33% between comparative quarters. Interest on shareholders' loans is $nil in the current quarter as the related shareholder loans were repaid prior to March 31, 2006.

Other Operating Expense

Other operating expense increased by 18%, to $8.6 million from $7.3 million. The increase in these expenses is primarily due to the increase in the amount of mortgages under administration of 30% from period end to period end. The increase trails this growth, evidencing the economies of scale built into the Company's business model. A large amount of these costs are fixed and do not increase in the same proportion as revenues.

Provision for Income Taxes

Because the Company converted to a limited partnership from a corporation, the income before income taxes earned subsequent to the conversion date of June 15, 2006 does not attract tax at the partnership level. Accordingly, there is no provision for income taxes for the period June 15 through December 31, 2006.

Net Income

Net income increased by 87%, to $47.4 million from $25.3 million, primarily as a result of the change in the taxability of the income of the Company as described above and the growth of mortgages under administration which has driven servicing income and Alt A origination which has lead to higher gains on securitization.

Adjusted EBITDA

Adjusted EBITDA increased by 24%, to $51.3 million from $41.3 million. The increase was largely due to the increase of mortgages under administration of 31% and increased Alt A origination.

Operating Segment Review

The Company aggregates its business from two segments for financial reporting purposes: (i) Residential (which includes single-family residential mortgages) and (ii) Commercial (which includes multi-unit and commercial mortgages), as summarized below.

(in $000s except percent amounts)	Operating Business Segments			
	Residential		Commercial	
Nine-months ended	**December 31, 2006**	**December 31, 2005**	**December 31, 2006**	**December 31, 2005**
Originations	4,669,000	3,406,000	1,306,000	1,250,000
Percentage change	*37.1%*		*4.5%*	
Revenue	119,040	79,569	37,387	27,571
Percentage change	*49.6%*		*35.6%*	
Income before income taxes	29,073	23,762	22,570	16,161
Percentage change	*22.4%*		*39.7%*	
Period ended	**December 31, 2006**	**December 31, 2005**	**December 31, 2006**	**December 31, 2005**
Identifiable assets	188,001	107,402	340,115	172,349
Mortgages under administration	14,145,311	10,670,000	10,214,170	8,953,000

Residential Segment

Residential revenues have increased by 49.6% from the prior nine-month period primarily due to the 37.1% increase in origination of single-family mortgages. These revenues have also been bolstered by growth in mortgage servicing revenue which has been increased through the growth of the residential mortgage portfolio and higher amounts of interest earned on fund held in trust. Income before income taxes increased by 20.4% to reflect the growth in Alt-A origination and mortgage servicing. Because prime single-family mortgage origination is not a high margin business, the increase of revenues shown above does not generate bottom line profitability in the period of origination.

Identifiable assets have increased due to increased single-family origination volumes which affect mortgages accumulated for sale, mortgage and loan investments and securities purchased under resale agreements and owned. These securities are used by the Company to hedge outstanding Alt-A fixed mortgage rate commitments in the residential sector.

Commercial Segment

Commercial revenues have increased by 35.6% from the prior nine-month period due primarily to the increase in securitization of small multi-family and commercial loans offset by the timing of the recognition of CMBS placement fees. The Company increased origination of smaller commercial mortgages in the current period and recorded greater gains on their securitization. For CMBS, in the nine-months ended December 31, 2006, the Company earned placement fees of $3.0 million from CMBS securitizations. In the comparative period in 2005 the Company earned $6.2 million from CMBS securitizations. Higher short-term interest rates have also led to increased interest income on trust funds and mortgage investment income. The growth in the mortgage portfolio under administration has driven mortgage servicing revenues higher. Income before income taxes grew at a higher rate due to the high margin nature of commercial origination.

Identifiable assets for the commercial sector increased primarily due to the CMBS securitization timing. Not only did the Company have $30 million more CMBS mortgages accumulated for sale at the end of December 2006 than March 2006, but because of hedging requirements, the Company had $96 million more securities held for resale for its CMBS program at the end of December compared to March 2006.

Review of Fourth Quarter Results

Revenue in the fourth quarter increased from the prior year's comparative quarter due to increased growth of originations and in particular, Alt-A and small commercial loan originations on which the Company earns higher gains on securitization. The current year's quarterly revenue has also benefited from the growth in the portfolio of mortgages under administration during the year which has caused 38% increases in mortgage servicing income, mortgage investment income, and residual securitization income. Net income and distributable cash for the fourth quarter increased by $9.9 million from the same period in 2005 due to increased revenues and the change in taxability of the Company.

Liquidity and Capital Resources

The Company's liquidity strategy has been to use bank credit to fund working capital requirements and to use cash flow from operations to fund longer term assets, providing a relatively low leveraged balance sheet. The Company's credit facilities are typically drawn to fund: (1) mortgages accumulated for sale, (2) securitization receivables, and (3) mortgage and loan investments. The Company entered into a credit facility on closing of the initial public offering which provides for a total of $200 million in financing. Subsequent to December 31, 2006, this facility was increased to $250 million.

At December 31, 2006, outstanding bank indebtedness was $169.6 million (March 31, 2006 – $60.6 million) of which $90.7 million (March 31, 2006 – $44.7 million) was drawn to fund mortgages accumulated for sale. At December 31, 2006, the Company's other interest-yielding assets included: (1) securitization receivables of $78.0 million (March 31, 2006 – $54.1 million) and (2) mortgage and loan investments of $53.2 million (March 31, 2006 – $36.8 million). The difference between bank indebtedness and mortgages accumulated for sale, which the Company considers a proxy for true leverage, has grown between March and December 2006 and now stands at $78.9 million. This represents a debt to equity ratio of 0.82 to 1 which the Company believes is still at a conservative level. This ratio has increased as the Company has taken advantage of opportunities to purchase mortgages for securitization, in particular its CMB initiative started in September. As these investments return cash, it will be used to pay down the bank indebtedness.

The Company funds a portion of its mortgage originations with institutional placements and sales to securitization vehicles on the same day as the advance of the related mortgage. The remaining originations, primarily residential, are funded by the Company on behalf of institutional investors or securitization vehicles on the day of the advance of the mortgage. On specified days, typically weekly, the Company aggregates all mortgages "warehoused" to date for an institutional investor and transacts a settlement with that institutional investor. A similar process occurs for sales to securitization vehicles, although the Company can dictate the date of sale into the vehicle at its discretion. The Company uses a portion of the committed credit facility with the banking syndicate to fund the mortgages during this "warehouse" period. The credit facility is designed to be able to fund the highest balance of warehoused mortgages in a month and is normally only partially drawn.

The Company also invests in short-term mortgages, usually six to eighteen months, to bridge existing borrowers in the interim period between long-term financing solutions. The banking syndicate has provided credit facilities to partially fund these investments. The syndicate has also provided credit to finance a portion of the Company's securitization receivables and other miscellaneous long term financing needs.

Capital Expenditures

First National's business is not a capital intensive business. Historically, capital expenditures have included technology software and hardware, facility improvements and office furniture. In the nine-months ended

December 31, 2006, the Company purchased new computers, office equipment and leaseholds to support the growth of its single-family residential business, in particular the outfitting of new premises for its Calgary residential sales office.

Going forward, the Company expects maintenance capital expenditures will be approximately $1,000,000 annually and primarily relate to technology software and hardware maintenance. Maintenance capital expenditures are expected to be funded from operating cash flow.

Critical Accounting Policies and Estimates

FNLP prepares its financial statements in accordance with GAAP, which requires management to make estimates, judgements and assumptions that management believes are reasonable based upon the information available. These estimates, judgements and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Management bases its estimates on historical experience and other assumptions, which it believes to be reasonable under the circumstances. Management also evaluates its estimates on an ongoing basis.

The significant accounting policies of First National are described in Note 2 to the audited financial statements. The policies which First National believes are the most critical to aid in fully understanding and evaluating its reported financial results include the determination of the gain on securitization revenue.

The Company uses estimates in valuing its gain or loss on the sale of its mortgages to special purpose entities ("Trusts") through securitizations. Under GAAP, valuing a gain on sale requires the use of estimates to determine the fair value of the retained interest (derived from the present value of expected future net cash flows) in the mortgages. The retained interest is reflected on the Company's balance sheet as securitization receivable.

On a quarterly basis, the Company reviews the estimates used to ensure their appropriateness and monitors the performance statistics of the relevant mortgage portfolios to adjust and improve these estimates. The estimates used reflect the expected performance of the mortgage portfolio over the life of the mortgages. The assumptions underlying the estimates used for the nine-months and quarter ended December 31, 2006 continue to be consistent with those used for the year ended March 31, 2006.

The key assumptions used in the valuation of gain on sale are prepayment rates, the annual expected credit losses, and the discount rate used to present value future expected residual cash flows. The annual rate of unscheduled principal payments is determined by reviewing portfolio prepayment experience on a monthly basis. The Company uses a rate of 16% for residential adjustable mortgages, 13% for residential fixed rate mortgages and 32% for commercial floating rate mortgages. The Company assumes there is no prepayment on commercial fixed rate mortgages. Credit losses are also reviewed on a monthly basis, in the context of the type of mortgages securitized. For the largest portion of the Company's securitizations, the mortgages are either insured or low ratio mortgages for which the Company does not provide for the event of a credit loss. For the securitization of Alt-A mortgages, the Company uses a credit loss rate of 0.35% per annum which is greater than the rate experienced by theCompany to-date, but which management feels is an appropriate estimate of losses that will average over the life of mortgages being securitized. For the securitization of small multi-unit residential and commercial mortgages, the Company uses a credit loss rate of 0.25% per annum which is greater than the rate experienced by the Company to-date, but which management feels is an appropriate estimate of losses that will average over the life of mortgages being securitized.

Changes During 2006: Consolidation of Variable Interest Entities

Effective April 1, 2005, the Company adopted the recommendations of CICA Accounting Guideline 15 — Consolidation of Variable Interest Entities ("AcG-15"). The adoption of AcG-15 has had no effect on the financial statements of the Company for the nine-months and quarter ended December 31, 2006 and the comparatives presented therein.

Future Changes: Financial Instruments, Hedges and Comprehensive Income

The CICA has issued three new accounting standards — Financial Instruments — Recognition and Measurement, Hedges, and Comprehensive Income. These standards are effective for the Company beginning with the first quarter of the 2007 fiscal year. The principal impacts of the standards are detailed below:

- Comprehensive income will be a new component of shareholders' equity and a new statement entitled Statement of Comprehensive Income will be added to the Company's primary financial statements.
- Financial assets and liabilities will be required to be classified as available for sale, held to maturity, trading or loans and receivables. Such classification may affect their carrying value and timing of recognition of unrecognized gains and losses.
- For fair value hedges, where the Company is hedging changes in the fair value of assets and liabilities or firm commitments, the change in the value of derivatives and hedged items will be recorded through income. Adoption is not expected to have a significant impact on the financial statements of the Company since the new standard is in harmony with CICA Accounting Guideline 13 – Hedging Relationships ("Acg-13"), which the standard replaces and which the Company has previously adopted.

Summary of Contractual Obligations

The Company's long-term obligations include, among other things, its five year operating lease for its head office, and its obligations for the ongoing servicing of mortgages sold to Trusts and mortgages related to servicing rights purchased. The Company sells it mortgages to Trusts and purchases servicing rights on a fully-serviced basis, and is responsible for the collection of the principal and interest payments on behalf of the Trusts, including the management and collection of mortgages in arrears.

(in $000s)	Payments Due By Period				
	Total	0-1 Years	1-3 Years	4-5 Years	After 5 Years
Lease Obligations	9,082	2,104	3,947	3,031	–
Servicing Liability	15,038	4,967	7,746	2,160	165
Total Contractual Obligations	24,120	7,071	11,693	5,191	165

Guarantees

First National Financial Operating Trust (the "Trust") and First National Financial GP Corporation (FNLP's general partner, the "GP") have entered into postponement of claim and guarantees with respect to FNLP's borrowings under its credit facility. The guarantee is supported by first ranking security over all the present and future assets of the Trust, including a first ranking pledge of all securities held by the Trust in FNLP and the GP.

Financial Instruments

The Company uses bond forwards (consisting of bonds sold short and bonds purchased under resale agreements) to manage interest rate exposure between the time a mortgage rate is committed to borrowers and the time the mortgage is sold to the Trusts and the underlying cost of funding is fixed. As interest rates change, the value of these interest rate derivatives varies inversely with the value of the mortgage contract. As interest rates increase, a gain will be recorded on the hedge which will be offset by the loss on the sale of the mortgage to the Trusts as the mortgage rate committed to the borrower is fixed at the point of commitment. For residential mortgages, primarily mortgages for the Alt-A program, only a portion of the mortgage commitments issued by the Company eventually fund. The Company must assign a probability of funding to each mortgage in the pipeline and estimate how that probability changes as mortgages move through the various stages of the pipeline. The amount that is actually hedged is the expected value of mortgage fundings within the next 60 days (60 days being the standard maximum rate hold period available). For the period ended December 31, 2006, the Company had entered into $29.0 million in notional value forward bond sales. The current contracts were purchased in the period November 1, 2006 to December 18, 2006. The mark-to-market value of the hedges as at December 31, 2006 was insignificantly different from the carrying value to the Company.

For multi-unit residential and commercial mortgages, the Company assumes all mortgages committed will fund and hedges each mortgage individually. This includes mortgages committed for the CMBS program as well as mortgages for sale to the Company's own securitization vehicles. As at December 31, 2006, the Company had entered into $198.0 million in notional value forward bond sales. The current contracts were purchased during the period from November 24, 2005 to December 28, 2006. The mark-to-market value of the hedges as at December 31, 2006 was a $0.9 million loss to the Company.

The Company is considering using a derivative based hedging program comprising bond futures instead of the current practice of selling bonds short and offsetting with resale agreements. This will ease the administration of the hedging program and consequently, reduce the amount of hedging securities disclosed on the balance sheet.

The Company has also entered into interest rate swaps to immunize the Company's exposure to changing interest rates related to cash flows receivable from servicing rights. When the Company bids for servicing rights, particularly from CMBS issuances, it estimates the interest to be earned from receiving mortgage payments and holding them in trust until payable to the ultimate investor/ transfer agent. This estimate requires the Company to use current short-term interest rates as a proxy for rates over a long term period (typically ten years for CMBS). In order to lock in this rate and ensure the purchase price for the rights is not impaired in the future, the Company enters into interest rate swaps to remove the variability of changing short-term interest rates. As at December 31, 2006, the notional value of these swaps is $5.7 million and the mark-to market value of the swaps was $0.1 million in favour of the Company. The amortizing swaps mature between April 2015 and October 2016.

Related Party Transactions

Concurrent with the initial public offering and as part of the acquisition agreement between FNLP and FNFC on June 15, 2006, FNLP incurred a working capital note payable in the amount of $6,339, representing the difference between the net assets of FNFC as at March 31, 2006 and the net assets transferred to FNLP as at June 14, 2006. The issuance of this non-interest bearing note has been accounted for as a distribution in FNLP's financial statements. This note was paid in full prior to August 31, 2006 by FNLP to FNFC.

Risk and Uncertainties Affecting the Business

The business, financial condition and results of operations of the Company are subject to a number of risks and uncertainties, and are affected by a number of factors outside the control of management of the Company including: reliance on sources of funding, concentration of institutional investors, reliance on independent mortgage brokers, changes in interest rates, repurchase obligations and breach of representations and warranties on mortgage sales, risk of servicer termination events and trigger events, cash collateral and retained interest, reliance on multi-unit residential and commercial mortgages,

general economic conditions, government regulation, competition, reliance on mortgage insurers, reliance on key personnel, conduct and compensation of independent mortgage brokers, failure or unavailability of computer and data processing systems and software, insufficient insurance coverage, change in or loss of ratings, impact of natural disasters and other events, environmental liability, alt-a mortgages employ broad underwriting criteria and ability to sustain performance and growth. In addition, risks associated with the structure of the Fund include those related to the dependence on FNLP, leverage and restrictive covenants, cash distributions which are not guaranteed and will fluctuate with FNLP's performance, the nature of Units, distribution of securities on redemption or termination of the Fund, restrictions on potential growth, unitholder liability, undiversified and illiquid holding in the Trust, the market price of Units, dilution of existing unitholders and FNLP unitholders, statutory remedies, control of the Company and contractual restrictions and income tax matters. Risk and risk exposure are managed through a combination of insurance, a system of internal controls, and sound operating practices. For a more complete discussion of the risks affecting the Fund's business, reference should be made to the prospectus of the Fund dated June 7, 2006.

Income Tax Matters

On December 21, 2006, the Department of Finance (Canada) released draft legislation to implement proposals originally announced on October 31, 2006 pertaining to the taxation of certain income distributed by publicly traded trusts and the tax treatment of such distributions to unitholders (the SIFT Proposals). If the SIFT Proposals are enacted as currently proposed, commencing in January 2011 (provided the Fund experiences only normal growth and no undue expansion before then) the Fund will be liable for tax at a rate comparable to the combined federal and provincial corporate tax rate on all or a significant portion of its income distributed to unitholders, and unitholders will receive Fund income distributions as taxable dividends. There can be no assurance that the final rules will not differ from the current draft legislation.

If the SIFT Proposals are enacted as announced the Fund will be required to account for future income taxes under the asset and liability method, whereby future income tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Future income tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on future income tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Future income tax assets are recorded in the consolidated financial statements to the extent that realization of such benefits is more likely than not.

If enacted as proposed, the SIFT Proposals will apply a tax at the trust level on distributions of certain income from publicly traded trusts at rate of tax comparable to the combined federal and provincial corporate tax and to treat such distributions as dividends to unitholders. Generally, existing trusts will have a four-year transition period and will not be subject to the new rules until 2011. However, assuming the SIFT Proposals are ultimately enacted in the form proposed, the implementation of such proposals would be expected to result in adverse tax consequences to the Fund and certain unitholders, may impact the future level of distributions made by the Fund, and may reduce the value of Fund units and hence the cost to the Fund of raising capital in the public capital markets.

Further, the Department of Finance (Canada) has indicated that, while there is no intention to prevent normal growth of existing trusts during the transition period, any undue expansion of a particular trust could result in loss of the benefit of the transitional period. On December 15, 2006, the Department of Finance (Canada) issued guidelines with respect to what will be considered normal growth in this context. While the Fund does not intend to raise capital in excess of the safe harbour limits outlined in these guidelines, there is a risk that the adverse tax consequences resulting from the SIFT Proposals could be realized sooner than 2011.

Management's Annual Report on Disclosure Controls and Procedures and Internal Control over Financial Reporting

Disclosure Controls and Procedures

Disclosure controls and procedures are designed to provide reasonable assurance that all relevant information is gathered and reported to senior management, including the President & Chief Executive Officer (CEO) and the Chief Financial Officer (CFO), on a timely basis so that appropriate decisions can be made regarding public disclosure.

An evaluation of the effectiveness of the design and operation of First National's disclosure controls and procedures was conducted as of December 31, 2006, by and under the supervision of First National's management, including the CEO and the CFO. Based on this evaluation, the CEO and the CFO have concluded that the Company's disclosure controls and procedures, as defined in Canada by Multilateral Instrument 52-109, Certification of Disclosure in Issuers' Annual and Interim Filings, are effective to ensure that information required to be disclosed in reports that the Company files or submits under Canadian securities legislation is recorded, processed, summarized and reported within the time periods specified in those rules and forms.

Internal Control over Financial Reporting

Internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with Canadian generally accepted accounting principles. Management is responsible for establishing and maintaining adequate internal control over financial reporting for First National Financial LP and First National Financial Income Fund.

First National's management, including the CEO and the CFO, has evaluated the effectiveness of the internal control over financial reporting using the framework and criteria established in Internal Control – Integrated Framework, issued by the Committee of Sponsoring

Organizations of the Treadway Commission. Based on this evaluation, management has concluded that internal control over financial reporting was effective as of December 31, 2006.

Changes in Internal Control over Financial Reporting

There were no changes in internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, First National's internal control over financial reporting.

Forward-Looking Statements

Forward-looking statements are included in this MD&A. In some cases, forward-looking information can be identified by the use of terms such as "may", "will, "should", "expect", "plan", "anticipate", "believe", "intend", "estimate", "predict", "potential", "continue" or other similar expressions concerning matters that are not historical facts. Forward-looking information may relate to management's future outlook and anticipated events or results, and may include statements or information regarding the future financial position, business strategy and strategic goals, product development activities, projected costs and capital expenditures, financial results, risk management strategies, hedging activities, geographic expansion, licensing plans, taxes and other plans and objectives of or involving the Company. Particularly, information regarding growth objectives, any increase in mortgages under administration, future use of securitization vehicles, industry trends and future revenues is forward-looking information. Forward-looking information is based on certain factors and assumptions regarding, among other things, interest rate changes and responses to such changes, the demand for institutionally placed and securitized mortgages, the status of the applicable regulatory regime and the use of mortgage brokers for single-family residential mortgages. These forward-looking statements should not be read as guarantees of future performance or results, and will not necessarily be accurate indications of whether or not, or the times by which, those results will be achieved. While management considers these assumptions to be reasonable based on information currently available to it, they may prove to be incorrect. Forward looking-information is subject to certain factors, including risks and uncertainties, which could cause actual results to differ materially from what management currently expects. These factors include reliance on sources of funding, concentration of institutional investors, reliance on independent mortgage brokers' and changes in interest rates under "Risk and Uncertainties Affecting the Business". In evaluating these statements, the reader should specifically consider various factors, including the risks outlined under "Risk and Uncertainties Affecting the Business", which may cause actual events or results to differ materially from any forward-looking statement. The forward-looking statements contained in this discussion represent management's expectations as of February 28, 2007, and are subject to change after such date. However, management and the Fund disclaim any intention or obligation to update or revise any forward-looking statements whether as a result of new information, future events or otherwise, except as required under applicable securities regulations.

Outlook

The Company achieved excellent financial results in the nine-month period ended December 31, 2006 and the outlook for the next fiscal year is favourable. Nonetheless, market conditions can change quickly, making future conditions difficult to predict.

After a period of rising interest rates, rates have been stable for the past six months, such that housing continues to be affordable by historical standards. The economy, which is the principal driver of the single-family residential housing market, continues to be strong across the country, particularly in Western Canada. In addition, the mortgage broker distribution channel continues to grow.

Although more difficult to predict, management anticipates overall commercial mortgage originations for the next fiscal year, including all classes of commercial lending and bridge loans, will exceed the levels of the previous year. Originations destined for CMBS conduits are also likely to exceed prior year levels.

Mortgage assets under administration are expected to grow strongly in fiscal 2007 with double-digit growth anticipated. The Company's own originations, third party institutional mortgage growth and increases in CMBS master servicing will all contribute to increases in mortgage assets under administration.

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

The accompanying consolidated financial statements of First National Financial Income Fund for the period from June 15, 2006 to December 31, 2006 and the financial statements of First National Financial LP for the period April 1, 2006 to December 31, 2006 and all information in this annual report are the responsibility of management.

The financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles. The preparation of these financial statements requires management to make estimates and assumptions that affect certain reported amounts which management believes are reasonable.

The Audit Committee of the Board of Directors has reviewed in detail the financial statements with management and the independent auditor. The Board of Directors has approved the financial statements on the recommendation of the Audit Committee.

Ernst & Young LLP, an independent auditing firm, has audited First National Financial Income Fund's 2006 consolidated financial statements and First National Financial LP's 2006 financial statements in accordance with Canadian generally accepted auditing standards and has provided independent audit opinions. The auditors have full and unrestricted access to the Audit Committee to discuss the results of their audits.

Stephen J. R. Smith
President & Chairman

Robert A. Inglis
Vice President, Finance

AUDITORS' REPORT

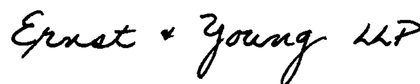
To the Unitholders of

First National Financial Income Fund

We have audited the consolidated balance sheet of **First National Financial Income Fund** as at December 31, 2006 and the consolidated statements of income and unitholders' equity and cash flows for the period from April 19, 2006, the date of Declaration of Trust, to December 31, 2006. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Fund as at December 31, 2006 and the results of its operations and its cash flows for the period from April 19, 2006, the date of Declaration of Trust, to December 31, 2006 in accordance with Canadian generally accepted accounting principles.



Toronto, Canada
February 27, 2007

Chartered Accountants

CONSOLIDATED BALANCE SHEET

(in $000s of dollars, as at December 31, 2006)

		2006
ASSETS		
Distributions receivable	$	934
Investment in First National Financial LP *[note 4]*		109,483
		110,417
LIABILITIES AND EQUITY		
Liabilities		
Distributions payable		934
Accounts payable and accrued liabilities		13
Total liabilities		947
Equity		
Unitholders' equity		109,470
	$	110,417

See accompanying notes

Approved by the Trustees:

Trustee
John Brough

Trustee
Robert Mitchell

CONSOLIDATED STATEMENT OF INCOME AND UNITHOLDERS' EQUITY

(in $000s of dollars, period from April 19 to December 31, 2006)

REVENUE	
Equity income from investment in First National Financial LP	$ 3,915
EXPENSES	
Trust administration expenses	13
Net income for period	3,902
Unitholders' equity, beginning of the period	–
Unitholders' equity, initial amount	1
Redemption	(1)
Issued pursuant to initial public offering on June 15, 2006	99,640
Issued pursuant to over-allotment option	12,000
Distributions *[note 5]*	(6,072)
Unitholders' equity, end of period	109,470
Average number of units outstanding during the period	11,643,216
Earnings per unit/share	
Basic	$ 0.34

See accompanying notes

CONSOLIDATED STATEMENT OF CASH FLOWS

(in $000s of dollars, period from April 19 to December 31, 2006)

OPERATING ACTIVITIES	
Net income for the period	$ 3,902
Add (deduct) items not affecting cash	
Equity income from investment in First National Financial LP	(3,915)
Distributions received from First National Financial LP	5,138
	5,125
Net change in non-cash working capital balances	
related to operations	13
Cash provided by operating activities	5,138
INVESTING ACTIVITIES	
Investment in First National Financial LP	(111,640)
Cash used in investing activities	(111,640)
FINANCING ACTIVITIES	
Issuance of Fund Units	111,640
Distributions paid	(5,138)
Cash provided by financing activities	$ 106,502
Net change in cash during the period and cash equivalents end of period	–

See accompanying notes

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(December 31, 2006, in $000s of dollars, except per unit amounts)

1. Organization And Business Of The Fund

First National Financial Income Fund (the "Fund") is an unincorporated, open-ended trust established under the laws of the Province of Ontario on April 19, 2006, pursuant to a Declaration of Trust. The Fund was established to acquire and hold, through a newly constituted wholly owned trust, First National Financial Operating Trust (the "Trust"), investments in the outstanding limited partnership units of First National Financial LP ("FNLP"). Pursuant to an underwriting agreement dated June 6, 2006 and initial public offering dated June 15, 2006, the Fund sold 10,600,000 units of the Fund ["Fund Units", "Units" or "Unit"], at a price of $10.00 per Unit for proceeds totalling $106,000. The proceeds of the offering, net of underwriters fees of $6,360, were used to partially fund the indirect acquisition [through the Trust] by the Fund of a 17.94% interest in FNLP, through the issuance of 10,600,000 Class A LP Units by FNLP.

Concurrent with the initial public offering and as part of the acquisition agreement between the Fund, FNLP and First National Financial Corporation ["FNFC" or the "predecessor"], on June 15, 2006, FNLP purchased all of FNFC's assets and assumed its liabilities, except for income tax liabilities. The consideration for this purchase was:

- the issuance of 48,486,316 exchangeable Class B LP Units;
- an acquisition promissory note of $97,140, of which $10,940 has been accounted for as a distribution in FNLP's financial statements;
- a working capital note in the amount of $6,339, representing the difference between the net assets of FNFC as at March 31, 2006, excluding tax liabilities, and the net assets transferred to FNLP as at June 14, 2006. The issuance of this note has also been accounted for as a distribution in FNLP's financial statements.

The exchangeable Class B LP units retained by FNFC are exchangeable on a one-for-one basis for units of the Fund at any time at the option of FNFC. FNLP is managed by First National Financial GP Corporation, the general partner, which holds a 0.01% interest in FNLP. The Fund initially owned 17.94% of the shares of First National Financial GP Corporation and FNFC wholly owned the remaining 82.06%. The ownership of the general partner will change pro rata as the exchangeable Class B LP units are exchanged for units in the Fund.

On July 11, 2006, the underwriters exercised an over-allotment option to purchase 1,200,000 Units of the Fund at $10.00 per Unit from FNFC. Accordingly, as at December 31, 2006, the Fund indirectly holds a 19.97% interest in FNLP and FNFC holds an 80.03% controlling interest in FNLP.

The Class A LP unitholders and the exchangeable Class B LP unitholders of FNLP are entitled to one vote for each unit held at all meetings of holders of the LP Units and have economic rights that are equivalent in all material respects, except that exchangeable Class B LP units are exchangeable, directly or indirectly, on a one-for-one basis [subject to customary anti-dilution provisions] for Fund Units at the option of the holder at any time. Additionally, exchangeable Class B LP units have special voting rights that entitle the holder to receive notice of, attend and to vote at all meetings of unitholders of the Fund.

The Fund effectively commenced operations through its indirect investment in FNLP on June 15, 2006. The excess of the Fund's cost of its investments in units of FNLP over the carrying value of the underlying net assets has been assigned to goodwill and finite life intangible assets. Income reported by the Fund commenced on the acquisition date.

Pursuant to the Limited Partnership Agreement between FNLP, the Trust and FNFC dated June 15, 2006, a subsidiary of FNFC, First National Financial GP Corporation, as general partner of FNLP, has full power and exclusive authority to employ all persons necessary for the conduct of the partnership, to enter into an agreement and to incur any obligation related to the affairs of the partnership and is entitled to full reimbursement of all costs and expenses incurred on behalf of the partnership. As general and administrative costs incurred by First National Financial GP Corporation are on behalf of the partnership, these costs have been reflected in the financial statements of FNLP.

2. Basis Of Presentation And Significant Accounting Policies

Basis of presentation

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles.

These consolidated financial statements should be read in conjunction with the audited March 31, 2006 financial statements of FNFC included in the Fund's initial public offering prospectus dated June 6, 2006.

Income taxes

The Fund qualifies as a "mutual fund trust" as defined in the Income Tax Act (Canada) ["the Tax Act"], including its establishment and maintenance as a Trust for the benefit of Canadian residents. Consequently, these consolidated financial statements do not reflect any provision for income taxes as the Fund intends to distribute to its unitholders substantially all of its taxable income and the Fund intends to comply with the provisions of the Tax Act that permit, amongst other items, the deduction of distributions to unitholders, from the Fund's taxable income.

On October 31, 2006, the Minister of Finance (Canada) announced proposed tax legislation rendering income trusts taxable commencing in 2011. In the event the Fund becomes a taxable entity, income taxes payable will reduce net earnings and will affect distributable cash by an equivalent amount.

Investments in FNLP and First National Financial GP Corporation

The Fund accounts for its investments in FNLP and First National Financial GP Corporation using the equity method. Under this method, the cost of the investment is increased by the Fund's proportionate share of FNLP's earnings and reduced by any distribution paid to the Fund by FNLP and amortization of the portion of the purchase price discrepancy, consisting of intangible assets.

Excess of purchase price over the carrying values of assets

The excess of the Fund's cost of its investment in units over the carrying value of the underlying net assets has been allocated to servicing rights, FNLP's broker and borrower relationships and goodwill. The excess related to servicing rights is being amortized over the average term of the related mortgages and the excess related to broker and borrower relationships over the estimated useful term of 5 and 10 years of the relationships. The goodwill component of the purchase price discrepancy will not be amortized The value of the assets will be tested annually for impairment.

3. Fund Units

The Fund may issue an unlimited number of Units for consideration and on the terms and conditions as determined by the Fund's trustees. Each Fund Unit is transferable and represents an equal undivided beneficial interest in any distribution from the Fund. All Fund Units are of the same class and have equal rights and privileges.

In connection with the initial public offering, the Fund issued 10,600,000 Fund Units on June 15, 2006 for $10 per Unit. On July 11, 2006, subject to the over-allotment option, the Fund issued 1,200,000 additional Fund Units for $10.00 per Unit.

Under the terms of the Exchange, Voting and Registration Rights Agreement dated June 15, 2006, the exchangeable Class B LP units held by FNFC are exchangeable for Fund Units on a one-for-one basis. After exercise of the over-allotment options, the Fund has reserved 47,286,316 Units for the exchange of the exchangeable Class B LP units.

Fund Units are redeemable at any time on demand by the unitholder. The redemption price per Unit is equal to the lesser of:

- 90% of the weighted average trading price per Unit during the last 10 days on the principal exchange on which the Units are listed; or
- An amount equal to:
  - the closing price of the Units on the date on which the Units were tendered for redemption on the principal stock exchange on which the Units are listed, if there was a trade on the specified date and the applicable market or exchange provides a closing price; or
  - the average of the highest and lowest prices of the Units on the date on which the Units were tendered for redemption on the principal stock exchange on which the Units are listed, if there was trading on the date on which the Units were tendered for redemption and the exchange or other market provides only the highest and lowest trade prices of the Units traded on a particular day; or
  - the average of the last bid and ask prices quoted in respect of the Units on the principal stock exchange on which the Units are listed if there was no trading on the date on which the Units were tendered for redemption.

4. Investment In First National Financial LP

Investment in First National Financial LP consists of the following:

Initial investment, June 15, 2006	$ 99,640
Additional purchase pursuant to over-allotment option	12,000
Equity in earnings of First National Financial LP	
since initial investment	7,915
Amortization of purchase price discrepancy	(4,000)
Distributions received	(6,072)
	$ 109,483

5. Distributions To Unitholders

The Fund is entirely dependent on distributions from FNLP to make its own distributions. The Fund pays monthly distributions to its unitholders of record on the last business day of each month approximately 15 days after the end of each month. The table below outlines the cumulative distributions to unitholders:

Period ended	Per unit	Amount
Distributions paid		
July 31, 2006[1]	$ 0.11875	$ 1,401.3
August 31, 2006	0.07917	934.2
September 30, 2006	0.07917	934.2
October 31, 2006	0.07917	934.2
November 30, 2006	0.07917	934.2
Distributions payable		
December 31, 2006	0.07917	934.2
Total distributions	$ 0.51460	$ 6,072.3

[1] Distribution for unitholders of record on this date was for the period June 15, 2006 to July 31, 2006.

6. Guarantee

The Fund's wholly-owned subsidiary, First National Financial Operating Trust, has provided guarantees to and subordinated its rights to receive payments from FNLP in respect of FNLP's bank credit facility that had an outstanding amount at December 31, 2006 of $116,900 and an authorized limit of $200,000.

AUDITORS' REPORT

To the Partners of

First National Financial LP

We have audited the balance sheets of First National Financial LP as at December 31, 2006 and March 31, 2006 and the statements of income, cash flows and changes in equity for the nine-month period ended December 31, 2006 and the year ended March 31, 2006. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2006 and March 31, 2006 and the results of its operations and its cash flows for the nine-month period ended December 31, 2006 and the year ended March 31, 2006 in accordance with Canadian generally accepted accounting principles.

Ernst & Young LLP

Toronto, Canada

February 27, 2007 Chartered Accountants

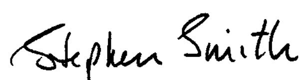
BALANCE SHEETS

(in $000s of dollars)

	As at December 31, 2006	As at March 31, 2006
ASSETS		
Accounts receivable and sundry	**$ 16,846**	$ 10,315
Mortgages accumulated for sale	**90,669**	44,688
Securitization receivable *[note 3]*	**77,949**	54,126
Cash collateral and short-term notes held by securitization trusts *[note 3]*	**45,489**	23,389
Mortgage and loan investments *[note 4]*	**53,230**	36,771
Purchased mortgage servicing rights *[note 5]*	**7,267**	6,378
Securities purchased under resale agreements and owned *[note 11]*	**232,952**	100,603
Capital assets, net *[note 6]*	**3,714**	3,481
Total assets	**528,116**	279,751
LIABILITIES AND EQUITY		
Liabilities		
Bank indebtedness *[note 7]*	**$ 169,638**	$ 60,558
Accounts payable and accrued liabilities	**14,487**	8,593
Income taxes payable *[note 9]*	–	12,482
Future income tax liabilities *[note 9]*	–	17,882
Servicing liability *[note 3]*	**15,038**	11,315
Securities sold under repurchase agreements and sold short *[note 11]*	**232,952**	100,603
Total liabilities	**432,115**	211,433
Commitments and guarantees *[note 10]*		
Equity		
GP units *[note 1]*	**$ 59**	$ –
Class A LP units *[note 1]*	**109,140**	–
Exchangeable Class B LP units *[note 1]*	**(22,940)**	–
Shareholders' equity — predecessor *[note 1]*	–	68,318
Retained earnings	**9,742**	–
Total equity	**96,001**	68,318
Total liabilities and equity	**$ 528,116**	$ 279,751

See accompanying notes

On behalf of the Board:



Director
Stephen Smith

Director
Moray Tawse

STATEMENTS OF INCOME

(in $000s of dollars, except earnings per share/unit)

	Nine-month period ended December 31, 2006	Year ended March 31, 2006
REVENUE		
Placement fees	$ **73,069**	$ 67,108
Gains on securitization *[note 3]*	**37,804**	29,998
Mortgage investment income	**11,444**	12,578
Mortgage servicing income	**29,154**	27,401
Residual securitization income	**4,956**	7,558
	156,427	144,643
EXPENSES		
Brokerage fees	$ **67,891**	$ 47,915
Salaries and benefits	**21,317**	22,914
Interest	**7,022**	5,260
Interest on shareholders' loans	–	1,711
Management salaries	**917**	700
Other operating	**8,554**	9,817
	105,701	88,317
Income before income taxes	**50,726**	56,326
Provision for (recovery of) income taxes *[note 9]*		
Current	$ **4,239**	$ 14,950
Future	**(927)**	5,044
	3,312	19,994
Net income for the period	$ **47,414**	$ 36,332
Earnings per unit/share *[note 16]*		
Basic	**0.80**	0.61

See accompanying notes

STATEMENTS OF CASH FLOWS

(in $000s of dollars)

	Nine-month period ended December 31, 2006	Year ended March 31, 2006
OPERATING ACTIVITIES		
Net income for the period	$ 47,414	$ 36,332
Add (deduct) items not affecting cash		
Gains on securitization	(37,804)	(29,998)
Amortization of securitization receivable	21,839	23,141
Amortization of purchased mortgage servicing rights	502	574
Amortization of capital assets	803	895
Amortization of servicing liability	(4,135)	(3,797)
Future income taxes	(927)	5,044
	27,692	32,191
Net change in non-cash working capital balances related to operations *[note 12]*	(63,778)	3,574
Cash provided by (used in) operating activities	(36,086)	35,765
INVESTING ACTIVITIES		
Additions to capital assets	$ (1,036)	$ (1,699)
Acquisition FNFC business	(97,140)	–
Investment in cash collateral and short-term notes, net	(22,100)	(7,685)
Investment in mortgage and loan investments	(46,428)	(59,687)
Repayment of mortgage and loan investments	29,969	49,965
Investment in purchased mortgage servicing rights	(1,391)	(3,454)
Cash used in investing activities	$ (138,126)	$ (22,560)
FINANCING ACTIVITIES		
Repayment in shareholders' loans	–	(13,700)
Issuance of Class A LP Units *[note 1]*	109,140	–
Issuance of GP Units *[note 1]*	59	–
Distributions paid	(25,728)	–
Exercise of over-allotment option	(12,000)	–
Distribution related to working capital adjustment	(6,339)	–
Securities purchased under resale agreements and owned	(132,349)	9,992
Securities sold under repurchase agreements and sold short	132,349	(9,992)
Cash provided by (used in) financing activities	65,132	(13,700)
Net increase in bank indebtedness during the period	(109,080)	(495)
Bank indebtedness, beginning of period	(60,558)	(60,063)
Bank indebtedness, end of period	(169,638)	(60,558)
Supplemental cash flow information		
Income taxes paid	$ 15,794	$ 3,004
Interest paid	7,022	6,971

See accompanying notes

STATEMENTS OF CHANGES IN EQUITY

(in $000s of dollars)

	Number of Units	Nine-month period ended December 31, 2006	Year ended March 31, 2006
GP units			
Balance, beginning of period	–	$ –	$ –
Issued upon formation *[note 1]*	59,092	59	–
Balance, end of period	59,092	59	–
Class A LP units			
Balance, beginning of period		–	–
Issued upon acquisition of FNFC business *[note 1]*	10,600,000	97,140	–
Issued upon exercise of over-allotment option *[note 1]*	1,200,000	12,000	–
Balance, end of period	11,800,000	$ 109,140	$ –
Exchangeable Class B LP units			
Balance, beginning of period		–	–
Transfer of excess of purchase price over net book value to exchangeable Class B LP Units upon acquisition of FNFC business *[note 1]*	48,486,316	(10,940)	–
Repurchased upon exercise of over-allotment option *[note 1]*	(1,200,000)	(12,000)	–
Balance, end of period	47,286,316	$ (22,940)	$ –
Shareholders' equity — predecessor			
Balance, beginning of period	2	68,318	31,986
Net income for the period *[note 18]*		7,266	36,332
Distribution related to working capital adjustment		(6,339)	–
Paid to FNFC on acquisition of FNFC business *[note 18]*		(97,140)	–
Future income tax liabilities applicable to predecessor not assumed by the partnership on acquisition *[note 1]*		16,955	–
Transfer of excess of purchase price over net book value to exchangeable Class B LP Units upon acquisition of FNFC business *[note 1]*	(2)	10,940	–
Balance, end of period	–	$ –	$ 68,318
Retained earnings			
Balance, beginning of period		–	–
Net income for the period *[note 18]*		40,148	–
Less distributions declared		(30,406)	–
Balance, end of period		$ 9,742	$ –
Equity		$ 96,001	$ 68,318

See accompanying notes

NOTES TO FINANCIAL STATEMENTS

(December 31, 2006, in $000s of dollars)

1. General Organization And Business Of First National Financial LP

First National Financial LP [the "Company" or "FNLP"], a limited partnership established under the laws of Ontario, is a Canadian-based originator, underwriter and servicer of predominantly prime single-family residential and multi-unit residential and commercial mortgages.

As a Canada Mortgage and Housing Corporation approved lender, the Company is active in the single-family residential and commercial mortgage markets. As at December 31, 2006, the Company had mortgages under administration of $24,359,481 [March 31, 2006 – $19,622,960] and cash held in trust of $287,382 [March 31, 2006 – $236,392]. Mortgages under administration are serviced for financial institutions such as insurance companies, pension funds, mutual funds, trust companies, credit unions and special purpose entities [including trusts], also referred to as securitization vehicles. As at December 31, 2006, the Company administered 83,098 mortgages [March 31, 2006 – 66,846] for 106 institutional investors [March 31, 2006 – 105] with an average remaining term to maturity of 60 months [March 31, 2006 – 61 months].

First National Financial Income Fund [the "Fund"] owns an indirect interest in FNLP of 19.97% and First National Financial Corporation ["FNFC" or the "predecessor"] holds indirectly the controlling interest of 80.03%. The Fund is an unincorporated, open-ended trust established under the laws of the Province of Ontario on April 19, 2006, pursuant to a Declaration of Trust. The Fund was established to acquire and hold, through a newly constituted wholly-owned trust, First National Financial Operating Trust [the "Trust"], investments in the outstanding limited partnership units of FNLP. Pursuant to an underwriting agreement dated June 6, 2006 and an initial public offering dated June 15, 2006 and the exercise of an over-allotment option by the underwriters on July 11, 2006, in aggregate the Fund sold 11,800,000 units of the Fund ["Fund Units", "Units" or "Unit"] at a price of $10.00 per Unit for proceeds totalling $118,000. The proceeds of the offering, net of underwriters fees of $6,360 and other offering costs of $2,500 were used to partially fund the indirect acquisition [through the Trust] of FNLP by the Fund through the issuance of Class A LP Units by FNLP.

Concurrent with the initial public offering and as part of the acquisition agreement between the Fund, FNLP and FNFC, FNLP purchased all of FNFC's assets and assumed its liabilities, except for income tax liabilities. The consideration for this purchase was:

- the issuance of 48,486,316 Class B exchangeable partnership units;
- an acquisition promissory note of $97,140, of which $10,940 has been accounted for as a distribution in FNLP's financial statements;
- a working capital note of $6,339, representing the difference between the net assets of FNFC as at March 31, 2006, excluding future income tax liabilities, and the net assets transferred to FNLP as at June 14, 2006. The issuance of this note has also been accounted for as a distribution in FNLP's financial statements.

FNLP is considered to be a continuation of FNFC business following the continuity of interest method of accounting. Under the continuity of interest method of accounting, FNLP's acquisition of the FNFC business is recorded at the net book value of FNFC business assets and liabilities on June 14, 2006 and the equity of FNLP represents the equity of the FNFC business at that date.

Pursuant to the Limited Partnership Agreement between FNLP, the Trust and FNFC dated June 15, 2006, First National Financial GP Corporation, as general partner, has full power and exclusive authority to employ all persons necessary for the conduct of the partnership, to enter into an agreement and to incur any obligation related to the affairs of the partnership and is entitled to full reimbursement of all costs and expenses incurred on behalf of the partnership. As general and administrative costs incurred by First National Financial GP Corporation are on behalf of the partnership, these costs have been reflected in the financial statements of FNLP.

On August 17, 2006, the acquisition promissory note and the working capital note were paid in full.

2. Significant Accounting Policies

Use of estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, including contingencies, at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results may differ from those estimates. Major areas requiring use of estimates by management are the securitization receivable and the fair values of financial assets and liabilities.

Change in fiscal year end

Upon the reorganization of the Company going public, the shareholders/partners changed the Company's fiscal year end from March 31 to December 31. Consequently, the comparative numbers are as at and for the year ended March 31, 2006.

Revenue recognition

The Company earns revenue from placement, securitization and servicing activities related to its mortgage business. The majority of originated mortgages are funded either by placement of mortgages with institutional investors or the sale of mortgages to securitization conduits. The Company retains servicing rights on substantially all of the mortgages it originates, providing the Company with servicing fees.

Placement fees are earned by the Company for its origination and underwriting activities on a completed transaction basis when the mortgage is with the institutional investor or securitized. Amounts collected in excess of the mortgage principal are recognized as placement fees.

Securitization revenue consists of gain on securitization and residual securitization income. The Company complies with The Canadian Institute of Chartered Accountants' ["CICA"] Accounting Guideline 12, "Transfers of Receivables". Accordingly, gains on securitization are recognized in income at such time as the Company transfers mortgages to securitization vehicles and surrenders control whereby the transferred assets have been isolated presumptively beyond the reach of the Company and its creditors, even in bankruptcy or other receivership. When the Company securitizes mortgages, it generally retains a residual interest, presented in the balance sheet as securitization receivable, and the rights and obligations associated with servicing the mortgages. The measurement of gains or losses recognized on the sale of mortgages depends in part on the previous carrying amount of the transferred mortgages, as allocated between the assets sold and the interests that are retained by the Company as the seller, based on the relative fair value of the assets and the retained interest at the date of transfer. To obtain fair values, quoted market prices are used where available. Since quoted prices are generally not available for retained interests, the Company estimates fair value based on the net present value of future expected cash flows, calculated using management's best estimates of key assumptions related to expected credit loss experience, prepayment rates and discount rates commensurate with the risks involved.

Residual securitization income represents the difference between the actual cash flows received on securitized mortgages and the assumed cash flows, recognized in income as received. Further, subsequent to securitization, the fair value of retained interests is measured quarterly and compared to the securitization receivable at the balance sheet date. Should the securitization receivable exceed the fair value of the retained interests determined by reference to underlying remaining expected cash flows, an impairment charge is included in residual securitization income to reduce the carrying value of the securitization receivable.

The Company services substantially all of the mortgages that it originates whether the mortgage is placed with institutional investors or transferred to a securitization vehicle. In addition, mortgages are serviced on behalf of third-party institutional investors and securitization structures. Servicing revenue is recognized in income on an accrual basis and is collected on a monthly basis from institutional investors. For securitized mortgages, the Company retains the rights and obligations to service mortgages and records a liability for future servicing and a reduction of gain on securitization at the time of transfer. Servicing income related to securitized mortgages is accreted to income over the life of the servicing obligation and included in residual securitization income. Interest income earned by the Company related to servicing activities is classified as mortgage servicing income.

In addition to the foregoing sources of revenue, the Company earns interest income which is recorded on an accrual basis from its interest bearing assets including securitization receivable, mortgage and loan investments and mortgages accumulated for sale. Prior to placement or transfer, funded mortgages are presented in the balance sheet as mortgages accumulated for sale which are typically held for a period of less than 180 days and are carried at cost.

Brokerage fees

Brokerage fees incurred to originate mortgages are deferred and amortized to income over the term of the underlying mortgage. Upon placement or securitization of the related mortgages, brokerage fees are recorded as an expense.

Mortgage and loan investments

Mortgage and loan investments are carried at outstanding principal balances adjusted for unamortized premiums or discounts and are net of specific provisions for credit losses, if any.

Mortgage and loan investments are recognized as being impaired when the Company is no longer reasonably assured of the timely collection of the full amount of principal and interest. An allowance for loan losses is established only for mortgages and loans that are known to be uncollectible.

Mortgages accumulated for sale

Mortgages accumulated for sale are mortgages funded on behalf of the Company's investors. These mortgages are carried at cost and held for terms of less than 90 days.

Purchased mortgage servicing rights

The Company purchases the rights to service mortgages from third parties. Purchased mortgage servicing rights are initially recorded at cost and charged to income over the life of the underlying mortgage servicing obligation. The fair value of such rights is determined on a periodic basis to assess the continued recoverability of the unamortized cost in relation to estimated future cash flows associated with the underlying serviced assets. Any loss arising from an excess of the unamortized cost over the fair value is immediately recorded as a charge to income.

Other financial instruments

To meet the criteria for hedge accounting, a financial instrument must be effective at reducing the risk associated with the exposure being hedged, and must be designated at the inception of the instrument. Accordingly, changes in the market value of the instrument must substantially offset the changes in the market value of the underlying hedged item, both at inception of the hedge and throughout the hedge period. If the hedging relationship is found to no longer be effective, the derivative is reclassified as a trading item and is marked to market. Upon reclassification to trading, any gain or loss associated with the derivative would be amortized over the remaining term of the hedged instrument.

When applying hedge accounting the Company complies with Accounting Guideline 13 ["AcG 13"], "Hedging Relationships", as issued and amended by the CICA. AcG 13 addresses the identification, designation, documentation and effectiveness of hedging relationships for the purpose of applying hedge accounting. AcG-13 establishes certain conditions for applying hedge accounting and the discontinuance of hedge accounting. The Emerging Issues Committee abstract [EIC] 128, "Accounting for Trading, Speculative or Non-Hedging Derivative Financial Instruments", requires that any derivative financial instrument not designated within an AcG-13-compliant hedging relationship be measured at fair value with changes in fair value recorded in current income. The Company applies hedge accounting for its hedging related to commercial mortgage securitization.

Bonds sold short and bonds purchased under resale agreements

Bonds sold short consist of the short sale of a bond. Bonds purchased under resale agreements consist of the purchase of a bond with the commitment by the Company to resell the bond to the original seller at a specified price. The Company uses combinations of bonds sold short and bonds purchased under resale agreements to create synthetic forward interest rate contracts that it uses to hedge the mortgage commitments and on balance sheet mortgages of the Company. Accordingly bonds sold short are carried at the proceeds from sale plus accrued interest less accrued coupon. The accrued coupon on bonds sold short is recorded as interest expense. Bonds purchased under resale agreements are carried at cost plus accrued interest, which approximates market value. The difference between the cost of the purchase and the predetermined proceeds to be received on a resale agreement is recorded over the term of the hedged mortgages as an offset to interest expense. Transactions are recorded on a settlement date basis.

Bonds owned and bonds sold under repurchase agreements

The Company purchases bonds and enters into bond repurchase agreements to close out hedging positions when mortgages are sold to special purpose entities or securitization vehicles.

These transactions are accounted for in a similar manner as the transactions described for bonds sold short and bonds purchased under resale agreements.

Income taxes

These financial statements are those of the partnership and do not reflect the assets, liabilities, revenues and expenses of its partners. FNLP is a partnership carrying on business in Canada, and consequently, is not directly subject to federal or provincial income taxes. The income or loss for income tax purposes of the partnership is required to be allocated to FNLP's partners. Accordingly, the tax provision recorded represents income taxes accrued on earnings while FNFC operated the Company's business from April 1, 2006 to June 14, 2006.

Cash and cash equivalents

Cash and cash equivalents consist of cash balances with banks and bank indebtedness.

Capital assets

Capital assets are recorded at cost, less accumulated amortization, at the following annual rates and bases:

Computer equipment	30% declining balance
Office equipment	20% declining balance
Leasehold improvements	straight-line over the term of the lease
Computer software	30% declining balance except for computer licence, which is straight-line over 10 years

Variable interest entities

The partnership adopted CICA Accounting Guideline 15 ["AcG-15"], "Consolidation of Variable Interest Entities" in the current year. AcG-15 provides a framework for identifying a variable interest entity ["VIE"] and requires a primary beneficiary to consolidate a VIE. A primary beneficiary is the enterprise that absorbs the majority of the VIE's expected losses or receives a majority of the VIE's residual returns, or both. The Company has interests in VIEs that are not consolidated because the Company is not considered the primary beneficiary.

Future changes: financial instruments, hedges and comprehensive income

The CICA has issued three new accounting standards - "Financial Instruments — Recognition and Measurement", "Hedges" and "Comprehensive Income". These standards are effective for the Company beginning with the first quarter of fiscal 2007. The principal impacts of the standards are detailed below:

Comprehensive income will be a new component of equity and a new statement entitled statement of comprehensive income will be added to the Company's primary financial statements.

Financial assets and liabilities will be required to be classified as available for sale, held to maturity, trading or loans and receivables. Such classification may affect their carrying value and timing of recognition of unrecognized gains and losses.

For fair value hedges, where the Company is hedging changes in the fair value of assets and liabilities or firm commitments, the change in the value of derivatives and hedged items will be recorded through income.

3. Securitization

The Company securitizes residential and commercial mortgage loans. In all of those securitizations, the Company retains servicing responsibilities and subordinate interests. In approximately 26% [March 31, 2006 – 46%] of current-period securitizations, the Company securitized fixed-term mortgage loans through the NHA-MBS program and with institutional investors and received a

fixed servicing fee for its servicing responsibilities. The remaining 74% [March 31, 2006 – 54%] of those securitizations consisted of sales of fixed and floating rate mortgages to special purpose entities. In these cases, the Company does not receive an explicit servicing fee; instead, the Company receives subordinated interests consisting of rights to future cash flows arising after the investors in the special purpose entities have received the return for which they contracted, and provides credit enhancement to the special purpose entity in the form of cash collateral accounts and short-term notes. The investors and the special purpose entities have no recourse to the Company's other assets for failure of debtors to pay when due. The Company's retained interests are subject to credit, prepayment and interest rate risks on the transferred receivables.

During the nine-month period ended December 31, 2006, the Company securitized $2,152,161 [year ended March 31, 2006 – $1,892,484] of mortgage loans to special purpose entities, recognizing gains on securitization of $37,379 [year ended March 31, 2006 – $27,940]. The Company also recognized gains on securitization of $425 [year ended March 31, 2006 – $2,058], in addition to placement fees, from the placement with institutional investors of $762,534 mortgage loans during the period [year ended March 31, 2006 – $1,167,232].

The liability for implicit servicing on securitization was $15,038 as at December 31, 2006 [March 31, 2006 – $11,315]. In the absence of quoted market rates for servicing securitized assets, management has estimated, based on industry expertise, that the fair market value of this liability approximates its carrying value. Amortization of the servicing liability during the period ended December 31, 2006 amounted to $4,135 [year ended March 31, 2006 – $3,797] and is included in residual securitization income.

As part of the securitization activities the Company is required to provide cash collateral and invest in subordinate short-term notes for credit enhancement purposes as required by the rating agency. Credit exposure to securitized mortgages is limited to the securitization receivable, cash collateral and amounts invested in the notes. The securitization receivable is paid to the Company by the special purpose entity over the term of the mortgages, as monthly net spread income. The full amount of the cash collateral and the notes held by the securitization trusts, and accrued interest thereon, is also recorded as a receivable and the Company anticipates full recovery of these amounts. As at December 31, 2006, the cash collateral was $37,726 [March 31, 2006 – $20,698] and the subordinate short-term notes were $7,763 [March 31, 2006 – $2,691].

The key weighted average assumptions used in determining the securitization gains were as follows:

	December 31, 2006	March 31, 2006
Prepayment rate	% 12.1	% 12.0
Discount rate	6.8	6.8

There was no credit loss assumption used for insured mortgages as no loss is expected. For uninsured mortgages, the expected weighted average credit loss assumption used was 0.33% [March 31, 2006 – 0.32%].

Cash flows received from securitization vehicles for the nine-month period ended December 31, 2006 and the year ended March 31, 2006 are as follows:

	Nine-month period ended December 31, 2006	Year ended March 31, 2006
Proceeds from new securitizations	$ 2,887,222	$ 3,043,980
Receipts on securitization receivable	24,591	30,699

The Company uses various assumptions to value the securitization receivable [excluding cash collateral and subordinate short-term notes held by the securitization trusts], which are set out below in the table, including the rate of unscheduled prepayments. Accordingly, the securitization receivable is subject to measurement uncertainty. The effect of variations between actual experience and assumptions will be recorded in future statements of income. Key economic weighted average assumptions and the sensitivity of the current carrying value of residual cash flows to immediate 10% and 20% adverse changes in those assumptions are as follows:

	December 31, 2006			
	Commercial mortgage loans		Residential mortgage loans	
	Fixed rate	Adjustable	Fixed rate	Adjustable
Carrying value of retained interests	$18,628	$ 2,550	$ 23,110	$ 33,661
Average life [in months] [1]	38	14	35	34
Prepayment speed assumption [annual rate]	0.9%	31.7%	12.6%	16.5%
Impact on fair value of 10% adverse change	$ 14	$ 82	$ 644	$ 896
Impact on fair value of 20% adverse change	$ 27	$ 161	$ 1,266	$ 1,759
Residual cash flows discount rate [annual]	6.0%	8.0%	7.0%	7.0%
Impact on fair value of 10% adverse change	$ 282	$ 19	$ 275	$ 360
Impact on fair value of 20% adverse change	$ 556	$ 37	$ 545	$ 713
Expected credit losses	0.07%	0.07%	0.24%	0.05%
Impact on fair value of 10% adverse change	$ 107	$ 13	$ 366	$ 111
Impact on fair value of 20% adverse change	$ 214	$ 26	$ 732	$ 221

	March 31, 2006			
	Commercial mortgage loans		Residential mortgage loans	
	Fixed rate	Adjustable	Fixed rate	Adjustable
Carrying value of retained interests	$16,041	$ 3,574	$ 4,298	$ 30,213
Average life [in months] [1]	40	16	36	33
Prepayment speed assumption [annual rate]	0.04%	34.5%	12.6%	16%
Impact on fair value of 10% adverse change	$ 3	$ 192	$ 75	$ 733
Impact on fair value of 20% adverse change	$ 6	$ 369	$ 138	$ 1,439
Residual cash flows discount rate [annual]	6.88%	8.2%	7.2%	8.2%
Impact on fair value of 10% adverse change	$ 249	$ 30	$ 48	$ 384
Impact on fair value of 20% adverse change	$ 493	$ 59	$ 95	$ 760
Expected credit losses	0.05%	0.06%	0.3%	0.04%
Impact on fair value of 10% adverse change	$ 58	$ 15	$ 83	$ 71
Impact on fair value of 20% adverse change	$ 115	$ 30	$ 166	$ 143

(1) The weighted average life of prepayable assets in periods [for example, months or years] can be calculated by multiplying the principal collections expected in each future period by the number of periods until that future period, summing those products, and dividing the sum by the initial principal balance.

These sensitivities are hypothetical and should be used with caution. As the figures indicate, changes in carrying value based on a 10% or 20% variation in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. Also, in this table, the effect of a variation in a particular assumption on the fair value of the retained interest is calculated without changing any other assumption; in reality, changes in one factor may result in changes in another [for example, increases in market interest rates may result in lower prepayments and increased credit losses], which might magnify or counteract the sensitivities.

The Company estimates that the expected cash flows of the securitization receivable will be as follows:

2007	$ 25,738
2008	21,381
2009	18,753
2010	8,172
2011	3,017
Thereafter	888
	$ 77,949

Mortgages under administration are serviced as follows:

	December 31, 2006	March 31, 2006
Institutional investors	**$ 15,116,636**	$ 12,206,363
Securitization vehicles	**5,309,532**	4,459,951
CMBS conduits	**3,933,313**	2,956,646
	$ 24,359,481	$ 19,622,960

The Company's exposure to credit losses is limited to mortgages under administration totalling $1,026,876 [March 31, 2006 – $518,029]. The Company incurred actual credit losses, net of recoveries, of $185 during the nine-month period ended December 31, 2006 [year ended March 31, 2006 – $265].

4. Mortgage And Loan Investments

As at December 31, 2006, mortgage and loan investments consist primarily of commercial first and second mortgages held for various terms up to 19 years. Due to the short-term, floating rate and bridging nature of most of these mortgages, management believes that fair value approximates carrying value.

The contractual repricing on the table below is based on the earlier of contractual repricing or maturity dates.

	December 31, 2006					March 31, 2006
	Within 1 year	Over 1 to 3 years	Over 3 to 5 years	Over 5 years	Book value	Book value
Residential	$ 3,417	$ –	$ –	$ 14	$ 3,431	$ 4,951
Commercial	46,823	2,183	172	621	49,799	31,820
	$ 50,240	$ 2,183	$ 172	$ 635	$ 53,230	$ 36,771

The Company has not experienced any credit losses or impairment on these items in the nine-month period ended December 31, 2006 or in the year ended March 31, 2006.

The maturity profile of mortgage and loan investments is as follows:

2007	$ 46,512
2008	5,575
2009	336
2010	–
2011	172
Thereafter	635
	$ 53,230

5. Purchased Mortgage Servicing Rights

As at period end, the balance consists of the following components:

	December 31, 2006			**March 31, 2006**		
	Cost	Accumulated amortization	Net Book Value	Cost	Accumulated amortization	Net Book Value
Third-party commercial mortgage servicing rights	**$ 3,614**	**$ 1,445**	**$ 2,169**	**$ 3,614**	**$ 1,157**	**$ 2,457**
CMBS primary and master servicing rights	**5,492**	**394**	**5,098**	**4,101**	**180**	**3,921**
	$ 9,106	**$ 1,839**	**$ 7,267**	**$ 7,715**	**$ 1,337**	**$ 6,378**

During the nine-month period ended December 31, 2006, the Company purchased servicing rights valued at $1,391 [year ended March 31, 2006 – $3,454]. Amortization charged to income for the nine-month period ended December 31, 2006 was $502 [year ended March 31, 2006 – $574].

During the nine-month period ended December 31, 2006 and the year ended March 31, 2006, management determined that the estimated fair market value of this asset at any time was not less than the Company's unamortized cost; accordingly, no write downs were recorded during the periods.

6. Capital Assets

Capital assets consist of the following:

	December 31, 2006			**March 31, 2006**		
	Cost	Accumulated amortization	Net Book Value	Cost	Accumulated amortization	Net Book Value
Computer equipment	**$ 2,790**	**$ 1,453**	**$ 1,337**	**$ 2,740**	**$ 1,530**	**$ 1,210**
Office equipment	**2,392**	**1,272**	**1,120**	**2,048**	**1,105**	**943**
Leasehold improvements	**1,293**	**721**	**572**	**1,166**	**542**	**624**
Computer software	**1,198**	**513**	**685**	**1,082**	**378**	**704**
	$ 7,673	**$ 3,959**	**$ 3,714**	**$ 7,036**	**$ 3,555**	**$ 3,481**

7. Bank Indebtedness

Bank indebtedness includes a one year revolving line of credit of $200,000 [March 31, 2006 – $150,000], of which $163,900 [March 31, 2006 – $56,100] was drawn at December 31, 2006 and against which the following have been pledged as collateral:

a) a general security agreement over all assets, other than real property, of the Company; and

b) a general assignment of all mortgages owned by the Company.

The revolving line of credit bears variable rate interest based on prime or bankers' acceptance rates.

8. Swap Contracts

Swaps are over-the-counter contracts in which two counterparties exchange a series of cash flows based on agreed upon rates to a notional amount. The Company uses interest rate swaps to manage interest rate exposure relating to variability of interest earned on Commercial Mortgage Backed Securities ["CMBS"] payments held in trust as the master servicer. The swap agreements that the Company entered into are interest rate swaps where two counterparties exchange a series of payments based on different interest rates applied to a notional amount in a single currency.

The following table presents the notional amounts and fair value of swap contracts as at December 31, 2006 and March 31, 2006 by remaining term to maturity:

	December 31, 2006			
	3 to 5 years	>5 years	Total notional amount	Fair value
Interest rate swap contracts	$ –	$ 5,665	$ 5,665	$ 81

	March 31, 2006			
	3 to 5 years	>5 years	Total notional amount	Fair value
Interest rate swap contracts	$ –	$ 4,056	$ 4,056	$ (42)

9. Income Taxes

Reconciliation of income taxes consists of the following:

	Nine-month period ended December 31, 2006	Year ended March 31, 2006
Income before income taxes [while a taxable entity]	**$ 10,578**	$ 56,326
Statutory income tax rate	**35.64%**	35.87%
Income taxes at statutory rate	**3,770**	20,204
Increase (decrease) resulting from		
Effect of future tax rate changes	**(477)**	(322)
Other non-deductible amounts for tax purposes	**19**	112
	$ 3,312	$ 19,994

Future income taxes

Future income taxes reflect the net tax effect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Future income tax liabilities are comprised of the following:

	December 31, 2006	March 31, 2006
Purchased mortgage servicing rights	$ –	$ 2,296
Retained interest in securitized assets and related benefits	–	19,485
Servicing liability	–	(4,073)
Other temporary differences	–	174
Total future income tax liabilities	$ –	$ 17,882

10. Commitments And Guarantees

As at December 31, 2006, the Company has the following operating lease commitments for its office premises:

2007	$ 2,104
2008	2,066
2009	1,882
2010	1,912
2011	1,119
	$ 9,083

Outstanding commitments for future advances on mortgages with terms of one to 10 years amounted to $1,346,659 as at December 31, 2006 [March 31, 2006 – $1,457,279]. The commitments generally remain open for a period of up to 90 days. These commitments have credit and interest rate risk profiles similar to those mortgages which are currently under administration. Certain of these commitments will expire before being drawn down. Therefore, these amounts do not represent the Company's future cash requirements.

In the normal course of business, the Company enters into a variety of guarantees. Guarantees include contracts where the Company may be required to make payments to a party, based on changes in the value of an asset or liability that the party holds. In addition, contracts under which the Company may be required to make payments if a third party fails to perform under the terms of the contract [such as mortgage servicing contracts] are considered guarantees. The Company has determined that the estimated potential loss from these guarantees is insignificant.

11. Securities Owned And Sold Short Under Resale And Repurchase Agreements

The Company's outstanding securities transactions under resale and repurchase agreements have a remaining term to maturity of less than one month.

12. Net Change In Non-cash Working Capital Balances Related To Operations

Net change in non-cash working capital balances related to operations consists of the following:

	Nine-month period ended December 31, 2006	Year ended March 31, 2006
Accounts receivable and sundry	**$ (6,531)**	$ (3,117)
Mortgages accumulated for sale, net	**(45,981)**	2,017
Accounts payable and accrued liabilities	**5,894**	2,873
Management bonus payable	**–**	(8,000)
Distributions payable	**(4,678)**	–
Shareholders' loans	**–**	(2,144)
Income taxes payable	**(12,482)**	11,945
	$ (63,778)	$ 3,574

13. Financial Instruments

Fair value

The estimated fair value of the securitization receivable is determined using a discounted cash flow calculation and the market interest rates currently charged for CMBS with similar terms and credit risks.

The carrying values of accounts receivable and sundry, mortgages accumulated for sale and accounts payable and accrued liabilities are assumed to approximate their fair values due to their short-term nature or underlying interest rate repricing. Any assets that are not financial instruments have been excluded from the estimate of fair values.

Market risk

Market risk refers to the risk that a change in the level of one or more of market prices, interest rates, indices, volatilities, correlations or other market factors, such as liquidity, will result in losses. As certain financial instruments and investments held are recognized at fair value or net recoverable amount, these changes could affect reported earnings as they occur. The Company manages market risk on a divisional level and on an individual product basis.

Credit risk

The Company incurs credit risk when entering into, settling and financing various transactions. Credit risk arises from the potential that investors or counterparties fail to satisfy their obligations. Credit risk is managed by dealing with counterparties the Company believes to be creditworthy and by actively monitoring credit and margin exposure and the financial health of the counterparties.

Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect the value of financial instruments. The Company manages interest rate risk by entering into hedging activities.

14. Related Party Transaction

During the period, the Company loaned a total of nil [year ended March 31, 2006 – $3,942] by way of a promissory note, bearing interest at prime rate, to a company wholly owned by a shareholder of the Company. No amounts were outstanding in the note at March 31, 2006 or at any time subsequent to that date.

15. Information About Major Customers

Placement fees and mortgage servicing income from two Canadian chartered banks represent approximately 37% of the Company's total revenue. During the nine-month period ended December 31, 2006, the Company placed 54% of all mortgages it originated with two institutional investors, who are Canadian chartered banks.

16. Earnings Per Unit

Earnings per unit are calculated as follows:

	Nine-month period ended December 31, 2006	Year ended March 31, 2006
Net income available to unitholders	**$ 47,414**	$ 36,332
Number of unitholders [Class A and B]	**59,086**	59,086
Basic earnings per unit [1]	**$ 0.80**	$ 0.61

[1] For comparative purposes, the number of units reflects the reorganization of capital as if it had occurred on April 1, 2005.

17. Earnings By Business Segment

The Company operates principally in two segments, being Residential and Commercial. These segments are organized by mortgage type and contain revenues and expenses related to origination, underwriting, securitization and servicing activities. Expenses not allocated to segments relate to compensation paid to senior management. Identifiable assets are those used in the operations of the segments.

	Nine-month period ended December 31, 2006		
	Residential	Commercial	Total
REVENUE			
Placement, securitization and servicing	$ 113,982	$ 31,001	$ 144,983
Mortgage investment income	5,058	6,386	11,444
	119,040	37,387	156,427
EXPENSES			
Amortization	619	184	803
Interest	2,948	4,074	7,022
Other operating	86,400	10,559	96,959
Corporate non allocated expenses	–	–	917
	89,967	14,817	105,701
Income before income taxes	29,073	22,570	50,726
Identifiable assets	188,001	340,115	528,116
Capital expenditures	$ 898	$ 138	$ 1,036

	Year ended March 31, 2006		
	Residential	Commercial	Total
REVENUE			
Placement, securitization and servicing	$ 92,676	$ 39,389	$ 132,065
Mortgage investment income	4,699	7,879	12,578
	97,375	47,268	144,643
EXPENSES			
Amortization	647	248	895
Interest on shareholders' loans	855	856	1,711
Other interest	2,530	2,730	5,260
Other operating expenses	66,917	12,834	79,751
Corporate non allocated expenses	–	–	700
	70,949	16,668	88,317
Income before income taxes	26,426	30,600	56,326
Identifiable assets	107,402	172,349	279,751
Capital expenditures	$ 1,399	$ 300	$ 1,699

18. Results Of FNLP

To provide information to the Fund's unitholders, management has prepared the following statements of income and cash flows, which reflect the activities of FNLP for the nine-month period ended December 31, 2006. The tables below show the results of the FNFC business prior to June 15, 2006 and the results of FNLP subsequent to June 14, 2006:

Statements of income	April 1, 2006 to June 14, 2006 [unaudited]	June 15, 2006 to December 31, 2006 [unaudited]	Nine-month period ended December 31, 2006
REVENUE			
Placement fees	$ 18,923	$ 54,146	$ 73,069
Gain on securitization	4,349	33,455	37,804
Mortgage investment income	2,783	8,661	11,444
Mortgage servicing income	7,475	21,679	29,154
Residual securitization income	1,209	3,747	4,956
	34,739	121,688	156,427
EXPENSES			
Brokerage fees	14,837	53,054	67,891
Salaries and benefits	5,637	15,680	21,317
Interest	1,435	5,587	7,022
Management salaries	105	812	917
Other operating	2,147	6,407	8,554
	24,161	81,540	105,701
Income before income taxes	10,578	40,148	50,726
Provision for (recovery of) income taxes			
Current	4,239	–	4,239
Future	(927)	–	(927)
	3,312	–	3,312
Net income for the period	$ 7,266	$ 40,148	$ 47,414

Statements of Cash Flows	April 1, 2006 to June 14, 2006 [unaudited]	June 15, 2006 to December 31, 2006 [unaudited]	Nine-month period ended December 31, 2006
OPERATING ACTIVITIES			
Net income for the period	$ 7,266	$ 40,148	$ 47,414
Add (deduct) items not affecting cash			
Gain on securitization	(4,349)	(33,455)	(37,804)
Amortization of securitization receivable	7,665	14,174	21,839
Amortization of purchased mortgage servicing rights	125	377	502
Amortization of capital assets	214	589	803
Amortization of servicing liability	(1,516)	(2,619)	(4,135)
Future income taxes	(927)	—	(927)
	8,478	19,214	27,692
Net change in non-cash working capital balances related to operations	(68,644)	4,866	(63,778)
Cash provided by (used in) operating activities	(60,166)	24,080	(36,086)
INVESTING ACTIVITIES			
Additions to capital assets	(418)	(618)	(1,036)
Investment in cash collateral and subordinate short-term notes	(3,057)	(19,043)	(22,100)
Investment in mortgage and loan investments	(13,811)	(32,617)	(46,428)
Repayment of mortgage and loan investments	3,338	26,631	29,969
Acquisition of FNFC business	—	(97,140)	(97,140)
Investment in purchased mortgage servicing rights	—	(1,391)	(1,391)
Cash used in investing activities	$ (13,948)	$ (124,178)	$ (138,126)
FINANCING ACTIVITIES			
Issuance of Class A LP Units	—	109,140	109,140
Issuance of GP Units	—	59	59
Distribution related to working capital adjustment	—	(6,339)	(6,339)
Distribution paid	—	(25,728)	(25,728)
Exercise over-allotment option	—	(12,000)	(12,000)
Securities purchased under resale agreements and owned	(71,750)	(60,599)	(132,349)
Securities sold under repurchase agreements and sold short	71,750	60,599	132,349
Cash provided by financing activities	—	65,132	65,132
Net increase in bank indebtedness during the period	(74,114)	(34,966)	(109,080)
Bank indebtedness, beginning of period	(60,558)	—	(60,558)
Bank indebtedness, end of period	$ (134,672)	$ (34,966)	$ (169,638)

19. Comparative Financial Statements

The comparative financial statements have been reclassified from statements previously presented to conform to the presentation of the December 31, 2006 financial statements.

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