



## **Connor, Clark & Lunn Real Return Income Fund**

### **Annual Information Form**

No securities regulatory authority has expressed an opinion about these Units and it is an offence to claim otherwise.

March 2011

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## **1 DESCRIPTION OF THE BUSINESS**

### **1.1 NAME AND FORMATION**

The Connor, Clark & Lunn Real Return Income Fund (the “Fund”) is an investment trust established under the laws of the Province of Ontario pursuant to a trust agreement (the “Trust Agreement”), dated as of June 29, 2005, between Connor, Clark & Lunn Capital Markets Inc. (the “Manager” or “CC&L”), as manager of the Fund, and RBC Dexia Investor Services Trust (“RBC Dexia”) (formerly “The Royal Trust Company”), as trustee of the Fund. The principal place of business of the Trust and the registered office of the Manager is 181 University Avenue, Suite 300, Toronto, Ontario M5H 3M7.

### **1.2 STATUS OF CONNOR, CLARK & LUNN REAL RETURN INCOME FUND**

The Fund is not a trust company and accordingly is not registered under the trust company legislation of any jurisdiction, as it does not carry on business as a trust company. Units are not “deposits” within the meaning of the Canada Deposit Insurance Corporation Act (Canada) and are not insured under provisions of that Act or any other legislation. However, the Fund is subject to certain other requirements and restrictions contained in securities legislation, including National Instrument 81-106 —Investment Fund Continuous Disclosure of the Canadian Securities Administrators, which governs the continuous disclosure obligations of investment funds, including the Fund.

### **1.3 ISSUE OF UNITS**

On July 18th, 2005, units of the Fund (“Units”) were issued and began trading on the Toronto Stock Exchange. The Fund does not continuously distribute its Units and does not intend to issue any further Units. The Initial Public Offering (the “Offering”) is summarized in the following table:

- Issue date: July 18, 2005
- Redemption date: July 18, 2015.
- Number of Units issued: 12,384,408.
- Issue price per Unit: \$10.00.
- Total raised: \$123,844,080.
- Expenses of issue: \$6,922,204.
- Net amount raised: \$116,921,876
- Trading symbol: RRB.UN
- Distributions: The Fund intends to provide Unitholders with monthly cash distributions. Cash distributions from the Fund are not fixed and may vary from month to month. The Manager determines and announces at the beginning of each calendar quarter an anticipated monthly distribution amount for each month in that quarter based on prevailing market conditions and the Fund’s estimate of distributable cash flow for the following quarter.

## **2 DESCRIPTION OF THE PORTFOLIO**

### **2.1 THE FUND**

#### **2.1.1 Investment Objectives**

The Fund has the following investment objectives:

- (i) to provide holders of Units (“Unitholders”) with tax efficient monthly cash distributions that are linked to the rate of inflation; and
- (ii) to preserve and enhance the net asset value (the “NAV”) of the Fund.

Cash distributions from the Fund are not fixed and may vary from month to month. The Manager determines and announces at the beginning of each calendar quarter an anticipated monthly distribution amount for each month in that quarter based on prevailing market conditions and the Fund’s estimate of distributable cash flow for the following quarter. For the distribution history of the fund see 3.2 *Monthly Distributions*, below.

Distributions to date have been returns of capital. Future distributions are expected to consist primarily of returns of capital and may

include capital gains and are intended to be tax efficient when compared to units of a trust that depends solely on interest, dividend and/or other investment income to pay distributions.

### **2.1.2 Investment Strategy**

In order to meet its investment objectives, the Fund obtains exposure to the performance of the Portfolio held by Real Return Trust by virtue of forward purchase and sale agreement (the "Forward Agreement") with Bank of Montreal (the "Counterparty"). The Fund does not invest in Real Return Trust. The Fund invested the net proceeds of the Offering in a portfolio of common shares of Canadian public companies (the "Common Share Portfolio"). Under the Forward Agreement, the Fund is entitled to sell securities in the Common Share Portfolio from time to time to fund monthly distributions, redemptions and repurchases of Units and its operating expenses in amounts that reflect the monthly yield or value of Real Return Trust as described in more detail under "Forward Agreement" below. As a result, Unitholders' returns correlate with the net returns realized by Real Return Trust on its investment in the Portfolio. The long-term debt of the Counterparty or any guarantor will be rated at least "A" by Standard & Poor's, a division of The McGraw-Hill Companies, Inc. ("S&P"), or have an equivalent rating from Dominion Bond Rating Service Limited or another "approved credit rating organization" as defined in National Instrument 81-102 Mutual Funds ("NI 81-102").

### **2.1.3 The Forward agreement**

The Fund entered into a Forward Agreement with the Counterparty at the time of closing of the initial public offering of its Units. The Forward Agreement entitles the Fund to deliver the securities in the Common Share Portfolio, or the value of those securities, to the Counterparty on the Termination Date in exchange for the value on that date of the Real Return Trust. Under the Forward Agreement, the Fund is entitled to sell securities in the Common Share Portfolio from time to time to fund monthly distributions, redemptions and repurchases of Units and its operating expenses.

Under the terms of the Forward Agreement, the Fund and the Counterparty have agreed that their settlement obligations under the Forward Agreement with respect to the Common Share Portfolio securities are discharged by physical delivery of the Common Share Portfolio securities by the Fund to the Counterparty against cash payment or, at the election of the Fund, by the making of cash payments between the parties. The amount payable by the Counterparty for physical delivery of the Common Share Portfolio may be more or less than the original aggregate subscription price of the Units. Unless the Fund elects cash settlement of the Forward Agreement, the Counterparty will pay to the Fund on or about the Termination Date, as the purchase price for the Common Share Portfolio, an amount equal to the Canadian dollar equivalent of the redemption proceeds of a corresponding number of units of the Real Return Trust. Prior to the Termination Date, Common Share Portfolio securities or other acceptable securities are pledged to, and may be held by, the Counterparty as security for the obligations of the Fund under the Forward Agreement.

In order to permit the Fund to fund distributions as well as redemptions of Units by Unitholders from time to time, payment for purchases of Units in the market and expenses of the Fund, the terms of the Forward Agreement will provide that the Forward Agreement may be partially settled prior to the Termination Date by the Fund by tendering to the Counterparty securities of the Common Share Portfolio or, at the election of the Fund, in cash.

Under the Forward Agreement, the forward purchase price may be reduced for all dividends and distributions, including extraordinary distributions, declared and paid on the Common Share Portfolio securities paid to the Fund as owner of the Common Share Portfolio. If any dividends or distributions are to be received by the Fund, the Forward Agreement provides that replacement securities as determined by the parties may be substituted for shares in respect of which the dividend or distribution has been declared to preserve the value of the Forward Agreement. Alternatively, the Fund may consider contributing additional securities to the Common Share Portfolio or entering into additional forward, derivative or other transactions. The Forward Agreement have similar provisions designed to avoid adjustments of the amount to be paid on or about the Termination Date which might otherwise be required if the Fund receives consideration as a consequence of a merger transaction involving any of the securities in the Common Share Portfolio.

The Forward Agreement may be terminated prior to the Termination Date in certain circumstances including: (i) at the option of the Fund in its sole discretion; or (ii) by the Counterparty if it is unable to hedge its position or would incur materially increased costs in hedging its position under the Forward Agreement. The Fund intends to exercise its right to partially settle the Forward Agreement prior to the Termination Date in order to permit the Fund to fund monthly distributions, redemptions and repurchases of Units and its operating expenses from time to time.

The Counterparty may choose to enter into transactions in order to hedge its exposure under the terms of the Forward Agreement to the economic performance of Real Return Trust. There is no assurance that the Counterparty maintains a hedge or will do so with respect to the full amount or term of the Forward Agreement. The Fund is exposed to the credit risk associated with the Counterparty

in respect of the Forward Agreement.

#### **2.1.4 Securities Lending**

In order to generate additional returns, the Fund may lend Common Share Portfolio securities to securities borrowers acceptable to the Fund pursuant to the terms of a securities lending agreement between the Fund and any such borrower under which (i) the borrower will pay to the Fund a negotiated securities lending fee and will make compensation payments to the Fund equal to any distributions received by the borrower on the securities borrowed; (ii) the securities loans must qualify as “securities lending arrangements” for the purposes of the Tax Act (as defined under “Canadian Federal Income Tax Considerations”); and (iii) the Fund will receive prescribed collateral security which it may pledge as security under the Forward Agreement.

#### **2.1.5 Investment Restrictions**

The Fund used the net proceeds of the Offering to acquire the Common Share Portfolio. In purchasing and holding the Common Share Portfolio, the Fund is subject to, among other things, the following investment restrictions:

(i) **Investment in Canadian Securities**

In respect of the Common Share Portfolio, the Fund restricts its investments to common shares of Canadian public companies that are “Canadian securities” for the purposes of the Tax Act. The Fund does not make or retain investment that would render the Units “foreign property” for purposes of Part XI of the Tax Act. The Fund does not acquire or retain an investment that is “taxable Canadian property” to the Fund for the purposes of the Tax Act.

(ii) **Concentration**

The Fund restricts its investments in any one issuer to no more than 10% of its total assets at the time of investment in such issuer.

(iii) **Mutual Fund Trust**

The Fund manages its investment and affairs to ensure that it is a “unit trust” and a “mutual fund trust” for purposes of the Tax Act.

(iv) **Foreign Investment Entity**

The Fund will not acquire any interest in a non-resident trust that is not an “exempt foreign trust”, or invest in the securities of any non-resident corporation or trust or other non-resident entity if the Fund would be required to mark its investment in such securities to market in accordance with proposed section 94.2 of the Tax Act or to include any significant amounts in income pursuant to proposed sections 94.1 or 94.3 of the Tax Act, as set forth in the proposed amendments to the Tax Act dealing with foreign investment entities and non-resident trusts contained in a Notice of Ways and Means Motion tabled in the House of Commons on November 9, 2006 (or amendments to such proposals, provisions as enacted into law or successor provisions thereto).

The Fund may also hold cash, and may invest excess cash in cash equivalents.

## **2.2 THE REAL RETURN TRUST**

Real Return Trust invests, on a leveraged basis, in a portfolio (the “Portfolio”) in accordance with the following:

- (i) **Real Return Bonds:** at least 80% of the Portfolio is invested in real return bonds issued by governments with AAA credit ratings such as the United States, the United Kingdom, Canada, France, Sweden and Australia. At least 70% of the Portfolio will be invested in U.S. Treasury Inflation Protected Securities (“TIPS”). In addition, up to 20% of the Portfolio may be invested in AAA-rated real return bonds issued by governments other than the United States; and
- (ii) **Other Portfolio Investments:** in order to diversify the Portfolio, improve net asset value stability and increase expected returns, up to 20% of the Portfolio is invested in a mix of assets which may include mortgage-backed and other asset-backed securities, corporate debt securities, bank loans, emerging markets debt securities, and commodity index investments. No more than 10% of the Portfolio may be invested in any one of these asset classes with the exception of mortgage-backed securities, in respect of which up to 20% of the Portfolio may be invested.

The combination of these investments is targeted to create a portfolio that has a dollar weighted average credit rating of AA+ on the Portfolio assets. In order to enhance returns the Manager may employ leverage in the Portfolio with a debt-to-equity ratio of up to

2:1. It is also intended that at least 90% of foreign currency exposure be hedged back to Canadian dollars at all times.

### **2.2.1 Investment Restrictions of the Real Return Trust**

The investment activities of Real Return Trust are to be conducted in accordance with, among other things, the following investment restrictions:

**(a) Investments**

Real Return Trust invests in the Portfolio. Real Return Trust may also hold cash or cash equivalents.

**(b) Composition of Portfolio**

- (a) at least 80% of the Portfolio is invested in real return bonds issued by governments with AAA credit ratings such as the United States, the United Kingdom, Canada, France, Sweden and Australia;
- (b) at least 70% of the Portfolio is invested in TIPS; and
- (c) no more than 20% of the Portfolio may be invested in mortgage-backed securities, asset-backed securities, corporate debt securities, bank loans, emerging markets debt securities, and commodity index investments and no more than 10% of the Portfolio may be invested in each such asset class, except for mortgage-backed securities in respect of which no more than 20% of the Portfolio may be invested.

**(c) Leverage.**

Real Return Trust's debt to equity ratio may not exceed 2:1. If at any time Real Return Trust's debt-to-equity ratio exceeds 2:1, the Investment Advisor will, in a timely manner, take all commercially reasonable steps as are necessary to reduce Real Return Trust's debt-to-equity ratio to 2:1 or less.

**(d) Weighted Average Credit Rating**

The dollar weighted average credit rating on the Portfolio assets will not fall below AA-.

**(e) Foreign Issuers**

Real Return Trust does not invest in securities of any foreign issuer if distributions to Real Return Trust from such issuer are subject to any foreign taxes or foreign withholding taxes that would not be recoverable by it or in respect of which it would not be entitled to receive a compensatory "gross-up" payment.

### **2.2.2 Real Return Bonds**

Real Return Trust invests a minimum of 80% of the Portfolio in real return bonds of sovereign issuers. While at least 70% of the Portfolio is invested in U.S. real return bonds, in order to provide additional diversification to the Portfolio and to take advantage of different real rates of return in various countries, Real Return Trust also invests in non-U.S. real return bonds. U.S. real return bonds, or TIPS, were first offered in 1997 in the United States.

### **2.2.3 Other Portfolio Investments**

In order to diversify the Portfolio, improve net asset value stability and increase expected returns, the Investment Advisor may invest up to 20% of the Portfolio in a basket of non-real return assets. The basket is intended to enhance the Investment Advisor's ability to adjust Portfolio characteristics such as effective duration, yield curve exposure and credit exposure in response to changing market conditions. Within the 20% maximum, up to 10% of the Portfolio may be invested in any of: bank loans, asset-backed securities, corporate debt securities, emerging markets debt securities or commodity index investments, and up to 20% may be invested in mortgage-backed securities. The Investment Advisor invests in each of the asset classes that may comprise the basket both in its diversified mandates and as stand-alone pools.

#### **2.2.3.1 Mortgage-Backed Securities**

Real Return Trust may invest up to 20% of the Portfolio in mortgage-backed securities. Mortgage-related securities are debt instruments that provide periodic payments consisting of interest and/or principal that are derived from or related to payments of interest and/or principal on underlying mortgages. Additional payments on mortgage-backed securities may be made out of unscheduled prepayments of principal resulting from the sale of the underlying property, refinancing or foreclosure, net of fees or costs that may be incurred.

### 2.2.3.2 *Asset-Backed Securities*

Real Return Trust may invest up to 10% of the Portfolio in asset-backed securities. Asset-backed securities are debt instruments that are backed by financial assets. Typically these assets consist of receivables other than mortgage loans, such as credit card receivables, auto loans, manufactured-housing contracts and home-equity loans. Asset-backed securities differ from most other kinds of debt instruments in that their creditworthiness (which is at the AAA level for more than 90% of outstanding issues) derives from sources other than the paying ability of the originator of the underlying assets.

### 2.2.3.3 *Corporate Debt Securities*

Real Return Trust may invest up to 10% of the Portfolio in corporate debt securities, including high yield debt securities. The investment return of corporate debt securities reflects interest on the security and changes in the market value of the security. The market value of corporate debt securities generally may be expected to rise and fall inversely with interest rates, and may also be affected by the credit rating of the corporation, the corporation's performance, perceptions of the corporation in the marketplace and general market liquidity. The value of the intermediate and longer-term corporate debt securities in which Real Return Trust generally will invest normally fluctuates more in response to changes in interest rates than does the value of shorter-term corporate debt securities. There is a risk that the issuers of corporate debt securities may not be able to meet their obligations on interest or principal payments at the time called for by a debt security.

### 2.2.3.4 *Bank Loans*

This asset class consists primarily of adjustable rate senior secured loans ("Senior Loans") selected by the Investment Advisor. Senior Loans are made by banks to corporations, partnerships and other business entities (the "Borrowers") that operate in various industries and geographical regions. In general, Senior Loans hold the most senior position in the capital structure of a Borrower, are typically secured with specific collateral, have a claim on the assets and/or shares of the Borrower that is senior to that held by subordinated debtholders and shareholders of the Borrower, and typically obligate the Borrower to abide by more numerous and restrictive covenants than bonds.

### 2.2.3.5 *Emerging Markets Debt Securities*

Emerging market countries, broadly defined, are those making efforts to improve their economy by developing open-market economies. The debt is issued by governments, government-sponsored entities and corporate issuers in these emerging market countries. Emerging markets debt has historically shown a low correlation to U.S. Treasury securities and may provide investors an attractive alternative to further diversify their investment portfolios.

### 2.2.3.6 *Commodity Index Investments*

Commodity exposure, if any, is comprised of two components: a commodity-based total return swap and a short-term bond portfolio. The swap is used to track the price movements of the Dow Jones-AIG Commodity Total Return index ("DJ-AIG Index") and the bond portfolio adds value above the returns provided by the swap. For the swap component, the commodity exposure is obtained by entering into a total return swap in which the Real Return Trust receives the total return of the DJ-AIG Index and pays an amount equal to the return on 3-month U.S. treasury bills. The notional value of the total return swap is equal to the value of the portfolio at inception. Choices are available as to the term of the swap contract. The foundation for the bond portfolio component of commodity exposure is the Investment Advisor's extensive and successful track record managing short-duration bond portfolios, dating back to 1988. Its Enhanced Cash Strategy, managed against a 3-month LIBOR benchmark, is used for the bond component of commodity exposure. The team managing these portfolios has been in place since 1991.

## 2.2.4 *Leverage Strategy*

The Real Return Trust is entitled to employ leverage at a debt-to-equity ratio of up to 2:1. If at any time Real Return Trust's debt-to-equity ratio exceeds 2:1 (the "leverage cap"), the Investment Advisor will, in a timely manner, take all commercially reasonable steps as are necessary to reduce Real Return Trust's debt-to-equity ratio to 2:1 or less. Real Return Trust has used, and intends to use, primarily short-term borrowings, in accordance with its investment objectives and restrictions, to finance the acquisition of the Portfolio and it intends to pledge the Portfolio to secure such borrowings.

A repurchase agreement, although structured as a sale and purchase obligation, operates as a financing (i.e., borrowing) under which Real Return Trust pledges TIPS as collateral to secure a loan with the Repurchase Agreement counterparty (BMO). Repurchase

agreements take the form of a sale of the pledged collateral to a lender at an agreed upon price in return for such lender's simultaneous agreement to resell the same TIPS back to the borrower at a future date (i.e., the maturity of the borrowing) at a higher price. The difference between the sale and repurchase price is the cost, or interest expense, of borrowing under the repurchase agreement. Real Return Trust retains beneficial ownership of the TIPS, while the lender maintains custody of such collateral. At the maturity of a Repurchase Agreement, Real Return Trust will be required to repay the loan and concurrently receive back its pledged collateral from the lender or, with the consent of the lender, Real Return Trust may renew such agreement at the then prevailing financing rate.

### **2.2.5 Derivatives**

Real Return Trust may, but is not required to, use a variety of derivative instruments for risk management purposes only. Generally, derivatives are financial contracts whose value depends upon, or is derived from, the value of an underlying asset, reference rate or index, and often may relate to individual debt instruments, interest rates, commodities and related indexes. Examples of derivative instruments that Real Return Trust may use include options contracts, futures contracts, options on futures contracts, warrants and swaps. Real Return Trust's use of derivative instruments involves risks different from, or possibly greater than, the risks associated with investment directly in securities and other more traditional investments. The use of derivative instruments is managed by the Investment Advisor subject to the Manager's approval.

### **2.2.6 Currency Hedging**

Real Return Trust hedges against currency risk initially in the amount of the U.S. dollar currency exposure of the Portfolio at inception. To the extent that the net asset value of the Real Return Trust in U.S. dollar terms increases or decreases, the net asset value will be underhedged or overhedged unless the Manager adjusts the hedge. Distributions on the Units are not hedged and changes in the exchange rates may have a positive or negative effect on such distributions.

## **3 UNITHOLDERS' EQUITY**

### **3.1 DESCRIPTION OF UNITHOLDERS' EQUITY**

The Fund is authorized to issue an unlimited number of transferable, redeemable units of one class (the "Units"), each of which represents an equal, undivided interest in the net assets of the Fund.

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

All Units have equal rights and privileges. Each whole Unit is entitled to one vote at all meetings of Unitholders and is entitled to participate equally with respect to any and all distributions made by the Fund, including distributions of net income and net realized capital gains, and distributions upon the termination of the Fund. Units are issued only as fully paid and are non-assessable.

The Trust Agreement provides that the Fund will not issue additional Units following completion of the original Offering, except: (i) for net proceeds per Unit of not less than 100% of NAV per Unit, (ii) by way of Unit distributions, or (iii) with the approval of Unitholders by Extraordinary Resolution. Immediately after a pro rata distribution of Units to all Unitholders in satisfaction of any non-cash distribution, the number of outstanding Units will be consolidated such that each Unitholder will hold, after the consolidation, the same number of Units as the Unitholder held before the non-cash distribution. Subject to the foregoing, the Fund may also allot and issue other securities at such time or times, and in such manner, as the Trustee in its sole discretion shall determine.

Subject to applicable law, the Fund may at any time or times purchase Units for cancellation at prices not exceeding the most recently calculated NAV per Unit.

### **3.2 MONTHLY DISTRIBUTIONS**

The Fund provides Unitholders with tax efficient monthly cash distributions. Cash distributions from the Fund are not fixed and may vary from month to month. The Manager determines and announces at the beginning of each calendar quarter an Anticipated

Distribution for each month in that quarter based on prevailing market conditions and the Fund's estimate of distributable cash flow for the following quarter.

Distributions are expected to always consist primarily of returns of capital and may include capital gains and are intended to be tax efficient when compared to units of a trust that depends solely on interest, dividend and/or other investment income to pay distributions.

The Fund may also, at the discretion of the Manager, make special distributions in cash or in Units at any time in addition to monthly cash distributions. To the extent that the Fund makes a distribution in Units, the number of outstanding Units of the Fund will be consolidated such that each Unitholder of the Fund will hold after the consolidation the same number of Units of the Fund as it held before the distribution of additional Units (except in the case of non-resident Unitholders, where withholding is required).

Monthly cash distributions of the Fund are derived from the proceeds of disposition of Common Share Portfolio securities. These proceeds are received by the Fund from the Counterparty under the Forward Agreement.

Cash distributions are payable to Unitholders of record at 5:00 p.m. (Toronto time) on the last business day of each month. All cash distributions are paid by cheque to The Canadian Depository for Securities Limited ("CDS") or paid in such other manner as may be agreed to by the Trustee.

If, in any year after such distributions, there remains in the Fund additional net income or net realized capital gains, the Fund intends, after December 15 but on or before December 31 of that year, to distribute such portion of the net income and net realized capital gains as is necessary to ensure that the Fund will not be liable for income tax under the Tax Act.

Each Unitholder will be mailed annually, no later than March 31<sup>st</sup>, information necessary to enable such Unitholder to complete an income tax return with respect to amounts paid or payable by the Fund in respect of the preceding taxation year of the Fund.

The Fund has made all its scheduled distributions to date. During the year ended December 31, 2010, the Fund met its targeted monthly distribution and paid total distributions of \$1,010,871, or \$0.25 per Unit (\$1,337,749, or \$0.27 per Unit during the year ended December 31, 2009).

### **3.3 ANNUAL REDEMPTIONS**

#### **3.3.1 Annual Redemption of Units**

Units may be redeemed on the last business day of August in each year (the "Redemption Date"), subject to the Fund's right to suspend redemptions, for a redemption price per Unit equal to the NAV per Unit less any costs of funding the redemption and the Unitholder will receive payment on or before the fifteenth day following the Redemption Date. Notice of Redemption must be provided between July 15th and the 20th Business Day before the Redemption Date. Redeeming Unitholders will be entitled to receive a redemption price per Unit equal to the NAV per Unit determined as of the Redemption Date, less any expenses incurred by the Fund to partially settle the Forward Agreement in order to fund such redemption. Any unpaid distribution payable on or before the Redemption Date in respect of Units tendered for redemption on such Redemption Date will also be paid on the same day as the redemption proceeds are paid. The NAV per Unit will vary depending on a number of market factors, including interest rates, volatility in the equity markets and changes in the amount that the Fund is entitled to receive under the Forward Agreement as a result of changes in the market price of the Portfolio securities. If the Fund is extended beyond the Termination Date, Unitholders may redeem their Units on the Termination Date for the NAV as of that date.

During August 2010 the fund had its annual Redemption Date and \$7,607,375 was paid to redeem 979,321 units at August 31, 2010 (\$6,339,840 was paid to redeem 822,481 units at August 31, 2009) Transactional NAV per unit price minus the costs of funding the redemption including all brokerage fees, commissions and other costs incurred in liquidating the securities held in the Portfolio.

#### **3.3.2 Exercise of Redemption Right**

An owner of Units who desires to exercise redemption privileges thereunder must do so by causing a participant in The Canadian Depository for Securities Limited a ("CDS Participant") to deliver to CDS (at its office in the City of Toronto) on behalf of the owner a written notice (the "Redemption Notice") of the owner's intention to redeem Units. An owner who desires to redeem Units should ensure that the CDS Participant is provided with notice of his or her intention to exercise his or her redemption privilege sufficiently in advance of the relevant notice date so as to permit the CDS Participant to deliver notice to CDS and so as to permit CDS to deliver notice to the registrar and transfer agent of the Fund in advance of the required time. The form of Redemption Notice

is available from a CDS Participant or the registrar and transfer agent. Any expense associated with the preparation and delivery of Redemption Notices will be for the account of the owner exercising the redemption privilege.

Except as provided under “Suspension of Redemptions”, by causing a CDS Participant to deliver to CDS a notice of the owner’s intention to redeem Units, an owner shall be deemed to have irrevocably surrendered his or her Units for redemption and appointed such CDS Participant to act as his or her exclusive settlement agent with respect to the exercise of the redemption privilege and the receipt of payment in connection with the settlement of obligations arising from such exercise.

Any Redemption Notice delivered by a CDS Participant regarding an owner’s intent to redeem which CDS determines to be incomplete, not in proper form or not duly executed shall for all purposes be void and of no effect and the redemption privilege to which it relates shall be considered for all purposes not to have been exercised thereby. A failure by a CDS Participant to exercise redemption privileges or to give effect to the settlement thereof in accordance with the owner’s instructions will not give rise to any obligations or liability on the part of the Fund to the CDS Participant or to the owner.

### **3.3.3 Suspension of Redemptions**

The Manager may direct the Trustee to suspend the redemption of Units or payment of redemption proceeds: (i) during any period when normal trading is suspended on a stock exchange or other market on which securities owned by the Fund are listed and traded, if these securities represent more than 50% by value or underlying market exposure of the total assets of the Fund, without allowance for liabilities, and if these securities are not traded on any other exchange that represents a reasonably practical alternative for the Fund; or (ii) with the prior permission of the securities regulatory authorities where required, for any period not exceeding 30 days during which the Manager determines that conditions exist which render impractical the sale of assets of the Fund or which impair the ability of the Trustee to determine the value of the assets of the Fund. The suspension may apply to all requests for redemption received prior to the suspension but as to which payment has not been made, as well as to all requests received while the suspension is in effect. All Unitholders making such requests shall be advised by the Manager of the suspension and that the redemption will be effected at a price determined on the first business day following the termination of the suspension. All such Unitholders shall have and shall be advised that they have the right to withdraw their requests for redemption. The suspension shall terminate in any event on the first day on which the condition-giving rise to the suspension has ceased to exist, provided that no other condition under which a suspension is authorized then exists. To the extent not inconsistent with official rules and regulations promulgated by any government body having jurisdiction over the Fund, any declaration of suspension made by the Manager shall be conclusive.

### **3.4 MANDATORY MARKET PURCHASE PROGRAM**

To enhance liquidity and to provide market support for the Units, the Fund has a mandatory market purchase program under which the Fund is, subject to the following exceptions and to compliance with any applicable regulatory requirements, obligated to purchase any Units offered in the market at the then prevailing market price if, at any time, the price at which Units are then offered for sale and the most recent closing price of the Units on the TSX are each less than 95% of the latest determined NAV per Unit. The maximum number of Units to be purchased by the Fund pursuant to such mandatory market purchase program in any calendar quarter is 1.25% of the number of Units outstanding at the beginning of such calendar quarter.

In addition, the Fund is not obligated to make such purchases, if among other things, (i) the Manager reasonably believes that the Fund would be required to make an additional distribution in respect of the year to Unitholders of record on the last Valuation Date (as defined under “Calculation of Net Asset Value”) in December of a year in order that the Fund will generally not be liable to pay income tax after the making of such purchase, (ii) in the opinion of the Manager, the Fund lacks the cash, debt capacity or other resources to make such purchases, or (iii) in the opinion of the Manager, such purchases would adversely affect the ongoing activities of the Fund or the remaining Unitholders. In addition, the Fund will have the right (but not the obligation), exercisable in its sole discretion, at any time to purchase additional Units in the market, subject to any applicable regulatory requirements and limitations.

Pursuant to this obligation, during the year ended on December 31, 2010 the Fund did not purchase any units for cancellation (500 units at a cost of \$3,687 during the year ended on December 31, 2009).

### **3.5 MEETINGS OF UNITHOLDERS**

A meeting of Unitholders may be convened by the Manager by a written requisition specifying the purpose of the meeting and must be convened if requisitioned by Unitholders holding not less than 10% of the Units then outstanding by a written requisition specifying the purpose of the meeting. Not less than 21 days’ and not more than 50 days’ notice will be given of any meeting of Unitholders. The quorum at any such meeting is two Unitholders present in person or by proxy except for the purpose of any meeting called to consider item (d) below under “Acts Requiring Unitholder Approval” in which case the quorum shall be Unitholders

holding 15% of the outstanding Units. If no quorum is present at such meeting when called, the meeting, if called on the requisition of Unitholders or for the purpose of item (d), will be terminated and otherwise will be adjourned for not less than 10 days and at the adjourned meeting the Unitholders then present in person or represented by proxy will form the necessary quorum. At any meeting of Unitholders, each Unitholder will be entitled to one vote for each whole Unit registered in the Unitholder's name.

The Fund does not intend to hold annual meetings of Unitholders.

### **3.6 ACTS REQUIRING UNITHOLDER APPROVAL**

Pursuant to the Trust Agreement, the following matters require the approval of Unitholders by resolution passed by at least 66<sup>2/3</sup>% of the votes cast at a meeting called and held for such purpose (an "Extraordinary Resolution"), other than items (c), (f) and (j), which require approval of Unitholders by a simple majority vote at a meeting called and held for such purpose (an "Ordinary Resolution"):

- (a) a change in the investment objectives of the Fund as described in this document;
- (b) a change in the investment restrictions of the Fund as described in this document;
- (c) any change in the basis of calculating fees or other expenses that are charged to the Fund which could result in an increase in charges to the Fund other than a fee or expense charged by a person or company that is at arm's length to the Fund;
- (d) a change of the manager of the Fund, other than a change resulting in an affiliate of such person assuming such position;
- (e) except as described under "Management of the Fund— The Trustee", a change in the trustee of the Fund, other than a change resulting in an affiliate of such person assuming such position;
- (f) a change in the auditors of the Fund;
- (g) a reorganization with, or transfer of assets to, a mutual fund trust, if
  - (i) the Fund ceases to continue after the reorganization or transfer of assets; and
  - (ii) the transaction results in Unitholders becoming securityholders in the mutual fund trust;
- (h) a reorganization with, or acquisition of assets of, a mutual fund trust, if
  - (i) the Fund continues after the reorganization or acquisition of assets;
  - (ii) the transaction results in the securityholders of the mutual fund trust becoming unitholders of the Fund; and
  - (iii) the transaction would be a significant change to the Fund;
- (i) a termination of the Fund prior to the Termination Date;
- (j) an extension of the Fund beyond the Termination Date as described under "Termination of the Fund";
- (k) an amendment, modification or variation in the provisions or rights attaching to the Units;
- (l) the issuance of additional Units, other than: (i) for net proceeds equal to or greater than 100% of the NAV per Unit; or (ii) by way of Unit distribution; and
- (m) a reduction in the frequency of calculating the NAV per Unit.

The Manager may, without the approval of or notice to Unitholders, amend the Trust Agreement for certain limited purposes specified therein, including to:

- (a) remove any conflicts or other inconsistencies which may exist between any terms of the Trust Agreement and any provisions of any law or regulation applicable to or affecting the Fund;
- (b) make any change or correction in the Trust Agreement which is of a typographical nature or is required to cure or

correct any ambiguity or defective or inconsistent provision, clerical omission, mistake or manifest error contained therein;

- (c) bring the Trust Agreement into conformity with applicable laws, rules and policies of securities regulatory authorities or with current practice within the securities industry, provided that any such amendment does not adversely affect the rights, privileges or interests of the Unitholders;
- (d) maintain, or permit the Trustee to take such steps as may be desirable or necessary to maintain, the status of the Fund as a “mutual fund trust” for the purposes of the Tax Act; or
- (e) provide added protection to Unitholders.

Except for changes to the Trust Agreement which require the approval of Unitholders or changes described above which do not require approval of or prior notice to Unitholders, the Trust Agreement may be amended from time to time by CC&L upon not less than 30 days’ prior written notice to Unitholders.

### **3.7 FINANCIAL REPORTING TO UNITHOLDERS**

The Fund delivers to Unitholders semi-annual unaudited and annual audited financial statements of the Fund and Real Return Trust. The financial statements for Real Return Trust shall include a statement of investments held by Real Return Trust at the date of the financial statements.

### **3.8 TERMINATION OF THE FUND**

The Fund will terminate on July 18, 2015 (the “Termination Date”), whereupon the Forward Agreement will be settled, any non-cash assets of the Fund will be liquidated, and the net assets of the Fund will be distributed to Unitholders unless Unitholders determine to continue the Fund by a majority of the votes cast at a meeting of Unitholders called for such purpose. Immediately prior to the Termination Date, the Trustee will, to the extent possible, convert the assets of the Fund to cash and after paying or making adequate provision for all of the Fund’s liabilities, distribute the net assets of the Fund to Unitholders as soon as practicable after the Termination Date. If a meeting of Unitholders is to be held to extend the Fund, it must be held at least 30 days prior to the then scheduled Termination Date. The Manager, may, in its discretion, terminate the Fund without the approval of Unitholders if, in the opinion of the Manager, the Net Asset Value of the Fund is reduced as the result of redemptions or otherwise so that it is no longer economically feasible to continue the Fund and it would be in the best interests of the Unitholders to terminate the Fund. After paying outstanding liabilities, the Fund will distribute its remaining assets pro rata to Unitholders.

If the term of the Fund is extended beyond the Termination Date, Unitholders may redeem their Units on the Termination Date for the NAV per Unit as of that date.

### **3.9 NON-RESIDENT UNITHOLDERS**

At no time may (i) non-residents of Canada, (ii) partnerships that are not Canadian partnerships or (iii) a combination of non-residents of Canada and such partnerships (all as defined in the Tax Act) be the beneficial owners of a majority of the Units, and the Trustee shall inform the registrar and transfer agent of the Fund of this restriction. The Trustee may require declarations as to the jurisdictions in which a beneficial owner of Units is resident and, if a partnership, its status as a Canadian partnership. If the Trustee becomes aware, as a result of requiring such declarations as to beneficial ownership or otherwise, that the beneficial owners of 40% or more of the Units then outstanding are, or may be, non-residents and/or partnerships that are not Canadian partnerships, or that such a situation is imminent, the Trustee may make a public announcement thereof. If the Trustee determines that more than 40% of the Units are beneficially held by non-residents and/or partnerships that are not Canadian partnerships, the Trustee may send a notice to such non-resident Unitholders and partnerships, chosen in inverse order to the order of acquisition or in such manner as the Trustee may consider equitable and practicable, requiring them to sell their Units or a portion thereof within a specified period of not less than 30 days. If the Unitholders receiving such notice have not sold the specified number of Units or provided the Trustee with satisfactory evidence that they are not non-residents or partnerships other than Canadian partnerships within such period, the Trustee may on behalf of such Unitholders sell such Units and, in the interim, shall suspend the voting and distribution rights attached to such Units. Upon such sale, the affected holders shall cease to be beneficial holders of Units and their rights shall be limited to receiving the net proceeds of sale of such Units.

Notwithstanding the foregoing, the Trustee may determine not to take any of the actions described above if the Trustee has been advised by legal counsel that the failure to take any of such actions would not adversely impact the status of the Fund as a mutual

fund trust for purposes of the Tax Act or, alternatively, may take such other action or actions as may be necessary to maintain the status of the Fund as a mutual fund trust for purposes of the Tax Act.

### **3.10 BOOK-ENTRY ONLY SYSTEM**

Registration of interests in, and transfers of, the Units is made only through the book-entry only system of CDS. On the date of closing of the Offering, the Fund delivered to CDS certificates evidencing the aggregate Units subscribed for under the Offering. Units must be purchased, transferred and surrendered for retraction only through a CDS Participant. All rights of an owner of Units must be exercised through, and all payments or other property to which such owner is entitled will be made or delivered by, CDS or the CDS Participant through which the owner holds such Units.

Real Return Trust, the Fund, the Manager, the Investment Advisor and the Agents do not have any liability for (i) records maintained by CDS relating to the beneficial interests in the Units or the book entry accounts maintained by CDS; (ii) maintaining, supervising or reviewing any records relating to such beneficial ownership interests; or (iii) any advice or representation made or given by CDS and made or given with respect to the rules and regulations of CDS or any action taken by CDS or at the direction of the CDS Participants.

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

The Fund has the option to terminate registration of the Units through the book-entry only system in which case certificates for Units in fully registered form will be issued to beneficial owners of such Units or to their nominees.

## **4 VALUATION**

### **4.1 CALCULATION OF NET ASSET VALUE**

The NAV on a particular date is equal to the aggregate value of the assets of the Fund less the aggregate value of the liabilities of the Fund, including any income, net realized capital gains or other amounts payable to Unitholders on or before such date expressed in Canadian dollars at the applicable exchange rate on such date. The NAV per Unit on any day is obtained by dividing the NAV of the Fund on such day by the number of Units then outstanding.

The NAV per Unit is calculated as of 4:00 p.m. (Toronto time) on the following days (each, a "Valuation Date"): (i) each Friday during the year (or, if a Friday is not a business day, then on the business day following such Friday); and (ii) each Redemption Date. If the Fund elects to change year-end to December 15 year-end for tax purposes as permitted by the Tax Act, the NAV per Unit will also be calculated on December 15.

The total assets of the Fund consist of the aggregate value of the assets of the Common Share Portfolio, the Forward Agreement and any net other assets held by the Fund. Since the value of the Fund's rights and obligations under the Forward Agreement is determined by reference to the value of units of the Real Return Trust, the Fund's NAV is linked to the value of Real Return Trust. The total assets of Real Return Trust consist of the aggregate value of the Portfolio.

In determining the NAV of the Fund, at any time the Trustee takes into account the following:

- (a) the value of the Forward Agreement shall be the gain or loss with respect thereto that would be realized if, at that time, the Forward Agreement were to be closed out in accordance with its terms;
- (b) the value of any cash on hand or on deposit, prepaid expenses, cash distributions declared and interest accrued and not yet received, shall be deemed to be the face amount thereof, unless the Trustee determines that any such asset is not worth the face amount thereof, in which event the value thereof shall be deemed to be such value as the Trustee determines to be the fair value thereof;
- (c) TIPS, bonds, debentures, mortgage-backed securities, asset-backed securities, emerging market debt securities, bank loans and commodity index investments shall be valued by taking the bid price at 4:00 p.m. on the Valuation Date;
- (d) any security that is listed or dealt in on a stock exchange shall be valued at the sale price applicable to a board lot last reported at 4:00 p.m. on the Valuation Date on the principal stock exchange on which such security is traded, or, if no sale price is available at that time, the last closing price quoted for the security, but if bid and ask quotes are available, at

the average of the latest bid and asked price rather than at the last quoted closing price;

- (e) any security purchased, the purchase price of which has not been paid, shall be included for valuation purposes as a security held, and the purchase price, including brokers' commissions and other expenses, shall be treated as a liability of the Fund;
- (f) any security sold but not delivered, pending receipt of the proceeds, shall be valued at the net sale price;
- (g) Restricted Securities (as that term is defined in NI 81-102) shall be valued at the lesser of:
  - (i) the value thereof based on reported quotations of such Restricted Securities in common use; and
  - (ii) that percentage of the market value of securities of the class or series of a class of which the Restricted Securities form part that are not Restricted Securities equal to the percentage that the Fund's acquisition cost was of the market value of such securities at the time of acquisition, but taking into account, if appropriate, the amount of time remaining until the Restricted Securities will cease to be Restricted Securities;
- (h) if any date on which NAV is determined is not a U.S. business day, then the property of the Fund will be valued as if such date was the preceding U.S. business day;
- (i) if any investment cannot be valued under the foregoing rules or if the foregoing rules are at any time considered by the Trustee to be inappropriate under the circumstances, then notwithstanding the foregoing rules, the Trustee shall make such valuation as it considers fair and reasonable;
- (j) the value of all assets of the Fund quoted or valued in terms of foreign currency, the value of all funds on deposit and contractual obligations payable to the Fund in foreign currency and the value of all liabilities and contractual obligations payable by the Fund in foreign currency shall be determined using the applicable rate of exchange current at, or as nearly as practicable to, the applicable date on which NAV is determined; and
- (k) estimated operating expenses of the Fund shall be accrued to the date as of which the NAV is being determined.

## **4.2 AUDIT OF FINANCIAL STATEMENTS**

The annual financial statements of the Fund and the Real Return Trust shall be audited by the Fund's auditors in accordance with Canadian generally accepted auditing principles. The auditors will be asked to report on the fair presentation of the annual financial statements in accordance with Canadian generally accepted accounting principles.

## **5 MANAGEMENT OF THE FUND**

### **5.1 THE MANAGER**

Connor, Clark & Lunn Capital Markets Inc. performs management services for the Company pursuant to a management agreement (the "Management Agreement") dated September 24, 2004. The Manager is entitled to receive fees as compensation for management services rendered to the Company. See "Fees and Expenses".

The Manager is part of the Connor, Clark & Lunn Financial Group, which also includes Connor, Clark & Lunn Investment Management Ltd., Connor, Clark & Lunn Private Capital Ltd., Baker Gilmore & Associates Inc., PCJ Investment Counsel Ltd., Scheer Rowlett & Associates Investment Management Ltd., New Star Canada Inc., Connor, Clark & Lunn Infrastructure Ltd, Banyan Capital Partners Management Partnership, Global Alpha Capital Management Ltd., Gyrus Investment Management Inc. and Crestpoint Real Estate Investments Ltd.(collectively, the "CC&L Group"). The CC&L Group offers professional management of financial assets for pension plan sponsors, capital accumulation plans, corporations, foundations, mutual funds and individual investors.

The Manager also acts as manager or investment advisor for the following investment funds: Connor, Clark & Lunn 2009 Flow-Through Limited Partnership, Connor, Clark & Lunn 2010 Flow-Through Limited Partnership, Connor, Connor, Clark & Lunn Conservative Income and Growth Fund, CANADIAN Financials & Utilities Split Corp., Focused Global Trends Fund, Connor, Clark & Lunn Global Financials Fund II, Connor, Clark & Lunn Natural Resources Class, Connor, Clark & Lunn Balanced Portfolio Class, Build America Investment Grade Bond Fund, Canadian Banc Capital Securities Trust, North American Financials Capital Securities

Trust, HBanc Capital Securities Trust, Australian Banc Capital Securities Trust, Macquarie Emerging Markets Infrastructure Income Fund and Australian Banc Income Fund.

### ***5.1.1 Duties and Services to be provided by the Manager***

Pursuant to the Trust Agreement, the Manager has exclusive authority to manage the operations and affairs of the Fund, to make all decisions regarding the business of the Fund and to bind the Fund. The Manager may delegate certain of its powers to third parties where, in the discretion of the Manager, it would be in the best interests of the Fund to do so.

The Manager's duties include: maintaining accounting records for the Fund; authorizing the payment of operating expenses incurred on behalf of the Fund; preparing financial statements, income tax returns and financial and accounting information as required by the Fund; ensuring that Unitholders are provided with financial statements and other reports as are required from time to time by applicable law; ensuring that the Fund complies with regulatory requirements, including its continuous disclosure requirements under applicable securities laws; preparing the Fund's reports to Unitholders and to the Canadian securities regulators; providing the custodian with information and reports necessary for the custodian to fulfill its fiduciary responsibilities; administering the retraction and redemption of Units; administering the Forward Agreement including partial or early settlement thereof; arranging for any payment required on or about the Redemption Date; dealing and communicating with Unitholders; and negotiating contracts with third party providers of services, including, but not limited to, custodians, transfer agents, auditors and printers. The Manager provides office facilities and personnel to carry out these services, together with clerical services, which are not furnished by the custodian, valuation agent or transfer agent of the Fund.

The Manager is also responsible for selecting the Common Share Portfolio held by the Fund. In addition, the Manager monitors the Fund's investment strategy to ensure compliance with the Investment Guidelines.

The Fund entered into the custodial agreement and the registrar, transfer agency and distribution agency agreement, all as referred to under "Material Contracts". Such agreements do not in any way release the Manager from compliance with its obligations to the Fund under the Trust Agreement. The Fund may terminate each of the foregoing agreements upon notice.

### ***5.1.2 Accounting and Reporting***

The Fund's fiscal year is the calendar year. The Manager ensures that the Fund complies with all applicable reporting and administrative requirements.

The Manager keeps adequate books and records reflecting the activities of the Fund. A Unitholder or his or her duly authorized representative have the right to examine the books and records of the Fund during normal business hours at the offices of the Manager. Notwithstanding the foregoing, subject to applicable law, a Unitholder shall not have access to any information, which, in the opinion of the Manager, should be kept confidential in the interests of the Fund.

### ***5.1.3 Officers and Directors of the Manager***

The name, municipality of residence, position with the Manager and principal occupation of each of the directors and officers of the Manager are set out below:

<b>Name and Municipality</b>	<b>Position with the Manager</b>	<b>Principal Occupation</b>
W. Neil Murdoch Oakville, Ontario	Director, President and Chief Executive Officer	Director, President and Chief Executive Officer, Connor, Clark & Lunn Capital Markets Inc.
Michael W. Freund Toronto, Ontario	Director and Chairman	Managing Partner, Connor, Clark & Lunn Financial Group
Darren N. Cabral Toronto, Ontario	Director and Vice-President	Vice-President, Connor, Clark & Lunn Capital Markets Inc.

**W. Neil Murdoch:** CFA; BComm, McGill University; LLB, University of Toronto; Master of Management, Kellogg Graduate School of Management, Northwestern University. Mr. Murdoch joined Connor, Clark & Lunn Capital Markets Inc. in December 2003. Prior thereto, Mr. Murdoch was Executive Vice President and Portfolio Manager at AIC Group of Funds.

**Michael W. Freund:** B.Bus.Sci., University of Capetown. Mr. Freund has held various management positions within the CC&L Group of companies since 1997. Mr. Freund's current principal occupation is managing partner of the Connor, Clark & Lunn Financial Group.

**Darren N. Cabral:** CFA; BA (Hons.), York University; MBA, Schulich School of Business, York University. Mr. Cabral joined Connor, Clark & Lunn Capital Markets Inc. in May 2007. Prior thereto, Mr. Cabral held various positions with affiliates of Middlefield Group Limited from September 2001 to April 2007, including Executive Director of Research at Middlefield Capital Corporation and Managing Director of Middlefield International Limited.

## **5.2 THE ADVISORY BOARD**

The Fund established an advisory board (the "Advisory Board") consisting of at least two members appointed by the Manager each of whom is independent of the Manager, the Investment Advisor, and each of their affiliates, and free from any interest and any business or other relationship which could, or could be reasonably perceived to, materially interfere with the exercise of an Advisory Board member's judgment. The Advisory Board provides independent advice to the Manager to assist the Manager in performing its services under the Trust Agreement or Real Return Trust Agreement, as applicable, including with respect to conflicts of interest or potential conflicts of interest or related party transactions identified by the Manager. The members of the Advisory Board are required to act honestly and in good faith in the best interests of the Fund, the Unitholders, and the Real Return Trust, as the case may be, and in connection with that duty exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.

The Manager reports to the Advisory Board on the operation and performance of the Fund and the Real Return Trust, as applicable, on a quarterly basis, including with respect to compliance with applicable investment restrictions and material contracts as amended from time to time.

The Manager is required under the Trust Agreement and Real Return Trust Agreement, as applicable, to notify each member of the Advisory Board in writing of any conflicts of interest, potential conflicts of interest or related party transactions concerning the Manager, the Fund, or the Real Return Trust, as applicable (other than any such conflicts of interest, potential conflicts of interest or related party transactions relating to matters with respect to which the approval of Unitholders is required under the Trust Agreement or the unitholders under the Real Return Trust Agreement) and to consult with the Advisory Board in respect of any such conflicts of interest, potential conflicts of interest or related party transactions.

In the event of a dispute between the Advisory Board and the Manager with respect to a conflict of interest, potential conflict of interest or related party transaction, upon written direction of the Advisory Board, the Manager will call a meeting of Unitholders or limited partners, as applicable, to consider the conflict of interest, potential conflict of interest or related party transaction.

The Fund's annual report to Unitholders and the Real Return Trust's annual report to its unitholders each includes a report by the Advisory Board summarizing any recommendations made by the Advisory Board (if any), including recommendations made and not followed by the Manager, as applicable, and any other matter that the Advisory Board determines to be appropriate in the circumstances. All fees and expenses of the Advisory Board incurred in connection with its duties with respect to the Fund or Real

Return Trust are paid by the Fund. The Advisory Board have the authority to retain, at the expense of the Fund, independent counsel or other advisors if the Advisory Board deems it appropriate to do so.

The members of the Advisory Board are indemnified by the Fund or Real Return Trust, as the case may be, except in cases of willful misconduct, bad faith, negligence or breach of their standard of care. The Advisory Board members are not responsible for the investments made by the Fund, or for the performance of the Fund. The members of the Advisory Board may serve in a similar capacity in respect of other entities managed by the Manager.

The following is a brief description of the backgrounds of the members of the Advisory Board:

**Frank Santangeli** has worked in the financial services industry since 1960. Positions he has held include Vice President of Sunlife of Canada, President and Chief Executive Officer of Finsco Investment Management Corporation, and Vice President of Imasco Financial Corporation. He has also served as Chairman of The Investment Funds Institute of Canada.

**Selwyn Kletz** is Chairman of Guardian Timing Services Inc. He was previously President, North America of Asset Management Investment Company PLC, a British based company engaged in the business of investing in investment counseling companies, having served as President and CEO of AMIC Canada Limited since its inception. He was previously a Managing Director of CIBC Wood Gundy Securities Inc. where he managed the Global Equity Research Department and served as a member of the Equity Management Committee and the Investment Committee of the merchant banking arm. Earlier in his career, Mr. Kletz founded and managed MYW Financial Management (since incorporated into Scotia Investment Management Limited), Laurim Capital Management Inc. and Laurentian Investment Management (Canada) Inc. Mr. Kletz has more than 30 years of experience in the investment business.

The members of the Advisory Board of the Fund receive remuneration for their services as advisors. All fees and expenses of the Advisory Board incurred in connection with its duties with respect to the Fund and Real Return Trust are paid by the Fund and Real Return Trust, respectively. The Advisory Boards' fees paid during the year ended December 31, 2010 were \$21,406 (\$21,341 during the year ended December 31, 2009) on a consolidation basis. The Advisory Board members are not responsible for investments made by the Trust or for the performance of the Trust.

### **5.3 *MANAGER'S RIGHTS AND OBLIGATIONS UNDER THE TRUST AGREEMENT***

Pursuant to the Trust Agreement, the Manager shall exercise the powers and discharge the duties of its office honestly, in good faith and in the best interests of Unitholders, and in connection therewith, shall exercise the degree of care, diligence and skill that a reasonably prudent manager would exercise in similar circumstances.

The Manager may resign as manager of the Fund upon 60 days' notice to the Unitholders and the Fund or upon such lesser notice period as the Fund may accept. If the Manager resigns it may appoint its successor but, unless its successor is an affiliate of the Manager, its successor must be approved by Unitholders. If the Manager is in material default of its obligations under the Trust Agreement and such default has not been cured within 20 Business Days (any day on which commercial banks are open for business in Toronto, Ontario hereinafter referred to as a "Business Day") after notice of same has been given to the Manager, the Fund shall give notice thereof to Unitholders and the Unitholders may remove the Manager and appoint a successor manager of the Fund.

The Manager is entitled to fees for its services under the Trust Agreement as described under "Fees and Expenses" and is reimbursed for all reasonable costs and expenses incurred by the Manager on behalf of the Fund. In addition, the Manager and each of its directors, officers, employees and agents are indemnified by the Fund for all liabilities, costs and expenses incurred in connection with any action, suit or proceeding that is proposed or commenced or other claim that is made against the Manager or any of its officers, directors, employees or agents in the exercise of its duties as manager, except those resulting from the Manager's willful misconduct, bad faith or negligence.

### **5.4 *THE TRUSTEE***

RBC Dexia is the trustee of the Fund under the Trust Agreement and, as such, is responsible for certain aspects of the day-to-day administration of the Fund as described in the Trust Agreement, including calculating NAV, net income and net realized capital gains of the Fund and executing instruments on behalf of the Fund.

The Trustee may resign upon 60 days' notice to Unitholders. The Trustee may be removed with the approval of a simple majority vote cast at a meeting of Unitholders called for such purpose or by the Manager, if the Trustee has committed certain events of bankruptcy or insolvency or is in material breach or default of its obligations under the Trust Agreement which breach has not been cured within 30 days after notice thereof has been given to the Trustee. Any such resignation or removal shall become effective only

upon the acceptance of appointment by a successor. If the Trustee resigns, its successor may be appointed by the Manager. The successor must be approved by Unitholders if the Trustee is removed by Unitholders. If no successor has been appointed within 60 days, the Trustee or any Unitholder may apply to a court of competent jurisdiction for the appointment of a successor.

The Trust Agreement provides that the Trustee shall not be liable in carrying out its duties under the Trust Agreement except where it is in breach of its obligations under the Trust Agreement or where the Trustee fails to act honestly and in good faith, and in the best interests of Unitholders to the extent required by laws applicable to corporate trustees, or to exercise the degree of care, diligence and skill that a reasonably prudent trustee would exercise in comparable circumstances. In addition, the Trust Agreement contains other customary provisions limiting the liability of the Trustee and indemnifying the Trustee, or any of its officers, directors, employees or agents, in respect of certain liabilities incurred by it in carrying out its duties.

The Trustee is entitled to receive fees from the Fund as described under ‘‘Fees and Expenses— Operating Expenses’’. The Trustee is entitled to be reimbursed for all expenses and liabilities which are properly incurred by the Trustee in connection with the activities of the Fund.

The Trustee is also the trustee of Real Return Trust pursuant to Real Return Trust Agreement described under the ‘‘management of Real Return Trust’’. The rights and responsibilities of the Trustee under Real Return Trust Agreement are substantially equivalent to the rights and responsibilities of the Trustee under the Trust Agreement described above.

## **5.5 THE CUSTODIAN**

RBC Dexia acts as custodian (the ‘‘Fund Custodian’’) of the assets of the Fund pursuant to the Trust Agreement. However, the Fund Custodian does not have custody of the Common Share Portfolio, which is pledged by the Fund to the Counterparty under the Forward Agreement.

## **6 MANAGEMENT OF REAL RETURN TRUST**

### **6.1 THE MANAGER**

The Manager of the fund continues as manager of Real Return Trust until terminated in accordance with the terms of Real Return Trust Agreement. The terms of its appointment are the same as the Trust Agreement. See ‘‘Management of the Fund— Trust Agreement’’.

### **6.2 THE INVESTMENT ADVISOR**

Western Asset acts as Investment Advisor to Real Return Trust pursuant to an agreement (the ‘‘Investment Advisory Agreement’’) entered into between the Investment Advisor, the Manager and Real Return Trust on June 1, 2005.

The fund is managed by a broad team of portfolio managers, sector specialists and other investment professionals. The investment professionals involved in developing and implementing investment strategies for a fund depend on the asset classes in which the fund invests. Senior portfolio managers are responsible for the development of investment strategy and oversight for each fund and coordination of other relevant investment team members. These portfolio managers work together with the broader Western Asset investment management team on portfolio structure, duration weighting and term structure decisions.

The portfolio managers responsible for day-to-day portfolio management, development of investment strategy, oversight and coordination of this fund are S. Kenneth Leech, Peter Stutz, Stephen A. Walsh and Paul Wynn.

The name and municipality of residence of each of the Investment Advisor’s investment management personnel involved with Real Return Trust and their principal occupations are as follows:

<b>Name and Municipality</b>	<b>Position with the Investment Advisor</b>	<b>Principal Occupation</b>
S. Kenneth Leech Pasadena, California	Chief Investment Officer Emeritus	Chief Investment Officer Emeritus, Western Asset
Peter Stutz Pasadena, California	Portfolio Manager/Research Analyst	Portfolio Manager/Research Analyst, Western Asset

<b>Name and Municipality</b>	<b>Position with the Investment Advisor</b>	<b>Principal Occupation</b>
Stephen A. Walsh Pasadena, California	Chief Investment Officer	Chief Investment Officer, Western Asset
Paul Wynn Pasadena, California	Portfolio Manager	Portfolio Manager, Western Asset

**Mr. Leech** joined Western Asset in 1990 and currently holds the title of Chief Investment Officer Emeritus. Prior thereto, Mr. Leech was a Portfolio Manager at Greenwich Capital Markets. Mr. Leech received his Bachelor of Arts, Bachelor of Science and Masters in Business Administration degrees from the Wharton School of the University of Pennsylvania.

**Mr. Stutz** has been a Portfolio Manager/Research Analyst of Western Asset since 1997. Prior thereto, Mr. Stutz was a Portfolio Manager at Pacific Telesis Group. He received his Bachelor of Science degree from the University of Illinois and Masters of Business Administration degree from the University of Chicago. Mr. Stutz also holds the Chartered Financial Analyst designation.

**Mr. Walsh** joined Western Asset in 1991 and currently holds the title of Chief Investment Officer. Prior thereto, Mr. Walsh was a Portfolio Manager at Security Pacific Investment Managers, Inc. He received his Bachelor of Science degree from the University of Colorado at Boulder.

**Mr. Wynn** has been a Portfolio Manager of Western Asset since 1992. Prior thereto, he was a Portfolio Manager at Morgan Grenfell. Mr. Wynn received his Bachelor of Science degree from Keele University.

#### **6.2.1 Services provided by the Investment Advisor**

Decisions as to the active management of, and the evaluation of risks associated with, the Portfolio held by Real Return Trust are made by the Investment Advisor in accordance with and subject to the Investment Advisory Agreement and the investment restrictions applicable to Real Return Trust.

The Manager and the Investment Advisor are responsible for ensuring that the provisions of the Investment Advisory Agreement are consistent with the investment guidelines and restrictions relating to Real Return Trust and that such investment guidelines and restrictions comply with applicable Canadian federal and provincial laws. The Manager and the Investment Advisor are also responsible for analyzing all provisions of applicable Canadian federal and provincial laws and interpretation of such laws (and any changes thereto) referred to in the investment restrictions relating to Real Return Trust. See “Investment Restrictions of Real Return Trust”.

#### **6.2.2 Investment Advisory Agreement**

The services provided by the Investment Advisor pursuant to the Investment Advisory Agreement include making investment decisions for Real Return Trust with regard to the Portfolio, including advising Real Return Trust on negotiating credit terms, in accordance with the investment objectives, strategies and restrictions of Real Return Trust.

Under the Investment Advisory Agreement, the Investment Advisor is required to discharge its duties in a manner that is fair and reasonable to Real Return Trust, to act honestly and in good faith with a view to the best interests of Real Return Trust and the unitholders of Real Return Trust and, in connection therewith, to exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in like circumstances (“Standard of Care”). The Investment Advisory Agreement provides that the Investment Advisor shall not be liable in any way for any default, failure or defect in any of the securities of Real Return Trust if it has satisfied the duties and standard of care, diligence and skill set forth above.

CC&L has responsibility for the investment advice given or the portfolio management services provided by the Investment Advisor and is responsible to Real Return Trust and the Fund for any loss that arises out of the failure of the Investment Advisor to discharge its obligations under the Investment Advisory Agreement in accordance with the standard of care, diligence and skill set forth above. There may be difficulty in enforcing any legal rights against the Investment Advisor because it is resident outside Canada and all or a substantial portion of its assets are situated outside Canada.

The Investment Advisory Agreement may be terminated by the Manager and Real Return Trust or by the Investment Advisor by providing the other parties to the Investment Advisory Agreement with no less than 60 days' written notice of such termination.

The Investment Advisor is entitled to fees for its services under the Investment Advisory Agreement, which are paid by the Manager out of its management fee, and is reimbursed for all reasonable costs and expenses incurred by the Investment Advisor on behalf of Real Return Trust. In addition, the Investment Advisor and each of its directors, officers, employees and agents is indemnified by Real Return Trust for all liabilities, costs and expenses incurred in connection with any action, suit or proceeding that is proposed or commenced or other claim that is made against the Investment Advisor or any of its officers, directors, employees or agents in the exercise of its duties as Investment Advisor, if they do not result from the Investment Advisor's willful misconduct, bad faith, negligence or breach of its Standard of Care as set forth in the Investment Advisory Agreement.

### **6.2.3 The Custodian**

RBC Dexia acts as custodian (the "Real Return Trust Custodian") of the assets of Real Return Trust pursuant to the Real Return Trust Agreement between Real Return Trust and the Real Return Trust Custodian. The Real Return Trust Custodian, or an affiliate of the Real Return Trust Custodian, is also carrying out certain aspects of the day-to-day administration of Real Return Trust, including calculating NAV, net income and net realized capital gains of Real Return Trust and maintaining the books and records of Real Return Trust.

## **7 INDEPENDENT REVIEW COMMITTEE**

National Instrument 81-107 Independent Review Committee for Investment Funds ("NI 81-107") which came into force on November 1, 2006 requires all publicly offered investment funds to establish an Independent Review Committee to whom the Manager must refer all conflict of interest matters for review or approval. NI 81-107 imposes obligations upon the Manager to establish written policies and procedures for dealing with conflict of interest matters maintain records in respect of these matters and provide assistance to the Independent Review Committee in carrying out its functions. The Independent Review Committee must be comprised of a minimum of three independent members and is subject to requirements to conduct regular assessments and provide reports to the Manager and to Limited Partners in respect of its functions. The members of the Independent Review Committee are Fred Lazar, Frank Santangeli and Joseph Wright. The Independent Review Committee acts as a review committee for a number of investment funds managed by the Manager.

The principal occupations and biographies of the IRC members are set out below.

**Fred Lazar** is a Professor of Economics at York University's Schulich School of Business. In addition to a distinguished academic career, Mr. Lazar has served as a senior advisor to the governments of Canada and Ontario and to a number of national and international companies.

**Frank Santangeli** has worked in the financial services industry since 1960. Positions he has held include Vice-President of Sunlife Canada, President and Chief Executive Officer of Finsco Investment Management Corporation, and Vice President of Imasco Financial Corporation. He has also served as Chairman of The Investment Funds Institute of Canada.

**Joseph Wright** currently serves on the board of directors of several public companies and private organizations, including Loblaw Companies Limited and BFI Canada Income Fund. His former positions include the Chief Executive Officer of Swiss Bank Corporation (Canada) and Vice-Chairman and Director of Burns Fry Limited.

The Independent Review Committee fees paid during the year ended December 31, 2010 were \$986 (\$2,508 paid during the year ended December 31, 2009).

## **8 CONFLICT OF INTEREST**

The management and administrative services provided by the Manager to the Fund pursuant to the Trust Agreement (and to Real Return Trust pursuant to the Real Return Trust Agreement) are not exclusive and nothing in the Trust Agreement prevents CC&L from providing similar management services to other investment funds and clients (whether or not their investment objectives and policies are similar to those of the Fund or Real Return Trust) or from engaging in other activities. Investment decisions for Real Return Trust are made independently of those made for other clients and independently of investments of the Manager. On occasion, however, the Manager may manage the same investment for Real Return Trust and for one or more of its other clients. If Real Return Trust and one or more of the other clients of the Manager are engaged in the purchase or sale of the same security, the transactions will be effected on an equitable basis.

The investment management services provided by the Investment Advisor to Real Return Trust under the Investment Advisory Agreement are not exclusive and nothing in the Investment Advisory Agreement prevents the Investment Advisor from providing similar services for its own account or to other investment funds and other clients (whether or not their investment objectives and policies are similar to those of Real Return Trust) or from engaging in other activities. Investments in securities purchased by the Investment Advisor on behalf of Real Return Trust and other investment funds or trusts for which the Investment Advisor provides investment management services are allocated to Real Return Trust and such other investment funds or trusts on a pro rata basis according to the size of the order and the applicable investment restrictions and policies of Real Return Trust and the other investment funds or trusts.

The Trust Agreement acknowledges that the Trustee may provide services to the Fund in other capacities, provided that the terms of any such arrangements are no less favorable to the Fund than those which would be obtained from parties which are at arm's length for comparable services. The Trustee may act as trustee of, and provide services to, other investment funds or trusts.

## **9 PORTFOLIO TRANSACTIONS AND BROKERAGE**

The Manager and the Investment advisor are responsible for selecting members of securities exchanges, brokers and investment dealers for the execution of transactions in respect of the Trust's investments and, when applicable, the negotiation of commissions in connection therewith. The Trust is responsible to pay those commissions.

## **10 CUSTODIAN**

The Trustee acts as the custodian of the assets of the Trust and is responsible for processing redemptions, calculating NAV, net income and net realized capital gains of the Trust and maintaining the books and records of the Trust. See "The Trustee".

## **11 AUDITORS**

The auditors of the Trust are PricewaterhouseCoopers LLP. The principal office of the auditor's is located at The Royal Trust Tower, Suite 3000, 77 King Street West, Toronto, Ontario M5K 1G8.

## **12 REGISTRAR, TRANSFER AGENT AND DISTRIBUTION AGENT**

The registrar, transfer agent and distribution agent is Computershare Investor Services Inc. The principal office of the registrar and the place where the securities register for the Units is kept is located at 8th Floor, 100 University Avenue, Toronto, Ontario M5J 2Y1.

## **13 FEES AND EXPENSES**

### ***13.1 INITIAL FEES AND EXPENSES***

The expenses of the Offering (including the costs of creating and organizing the Trust, the costs of printing and preparing the prospectus, legal expenses, marketing and advertising expenses and other reasonable out-of-pocket expenses) incurred by the Trust and the Agents and other incidental expenses, which were \$730,000 were paid out of the gross proceeds of the Offering. In addition, the Agents' fees, which were \$6,192,204, were paid to the Agents from the gross proceeds of the Offering.

### ***13.2 MANAGEMENT FEES***

The breakdown of the management fees between the Fund and Real Return Trust is as follows:

- (i) As compensation for management services rendered to the Fund, the Manager is entitled to receive an annual management fee in an amount equal to 0.30% per annum of the NAV of the Fund, to be calculated and payable monthly in arrears, plus applicable taxes.
- (ii) As compensation for management services rendered to Real Return Trust, the Manager is entitled to receive an annual management fee in an amount equal to 0.90% of the net asset value of Real Return Trust calculated and payable monthly in arrears, plus applicable taxes.

The total management fees charged to the Funds during the year ended December 31, 2010 were \$107,774 (119,004 during the year

ended December 31, 2009). The total management fees charged to the Fund and the Real Return Trust during the year ended December 31, 2010 were \$378,931 (428,185 during the year ended December 31, 2009).

The Manager, in its capacity as manager of Real Return Trust, is responsible for payment of the investment management fees of the Investment Advisor.

### **13.3 OPERATING EXPENSES**

The Fund pays for all expenses incurred in connection with the operation and administration of the Fund. These expenses include, without limitation:

- (a) mailing and printing expenses for periodic reports to Unitholders;
- (b) fees payable to the Trustee for acting as trustee (except when the Manager is the Trustee);
- (c) fees payable to the Counterparty under the Forward Agreement;
- (d) commissions and the costs of portfolio transactions in respect of the Common Share Portfolio;
- (e) fees payable to the Fund Custodian;
- (f) fees payable to the auditors and legal advisors of the Fund;
- (g) regulatory filing, stock exchange and licensing fees;
- (h) fees and expenses of the Advisory Board incurred in connection with its duties with respect to the Fund;
- (i) fees payable to the members of the Independent Review Committee; and
- (j) expenditures incurred upon the termination of the Fund.

Such expenses also include expenses of any action, suit or other proceedings in relation to which CC&L or the Trustee is entitled to indemnity by the Fund. Real Return Trust pays all ordinary expenses incurred in connection with the operation and administration of Real Return Trust. The aggregate amount of these fees and expenses paid during the year ended December 31, 2010 was \$185,953 (\$216,459 for the year ended December 31, 2009) on a consolidation basis, excluding any fees and interest under the Repurchase Agreements or other borrowings. The Fund pays to the Counterparty a fee under the Forward Agreement of approximately 0.50% per annum of the net asset value of Real Return Trust. Such fee includes any hedging costs incurred by the Counterparty. Forward fees paid during the year ended December 31, 2010 were \$164,805 (\$189,567 for the year ended December 31, 2009).

### **13.4 SERVICE FEE**

The Manager pays to registered dealers a servicing fee (the "Service Fee") equal to 0.30% annually of the NAV per Unit for each Unit held by clients of the registered dealer (calculated and paid at the end of each calendar quarter). Service fees paid during the year ended December 31, 2010 was \$89,742 (\$109,237 for the year ended December 31, 2009).

## **14 CANADIAN FEDERAL INCOME TAX CONSIDERATIONS**

**This summary is not exhaustive of all possible Canadian federal income tax considerations applicable to an investment in Units and does not describe the income tax consequences relating to the deductibility of interest on money borrowed to acquire Units. Moreover, the income and other tax consequences of acquiring, holding or disposing of Units will vary depending on an investor's particular circumstances including the province or territory in which the investor resides or carries on business. Accordingly, this summary is of a general nature only and is not intended to be legal or tax advice to any investor. Investors should consult their own tax advisors for advice with respect to the income tax consequences of an investment in Units, based on their particular circumstances.**

### **14.1 TAXATION OF THE FUND**

The Fund is subject to tax under Part I of the Tax Act for a taxation year on the amount of its income for the year computed for tax

purposes (including net taxable capital gains) less the portion thereof paid or payable to Unitholders in the year that it claims as a deduction. Provided the net income and net realized capital gains of the Fund are paid or payable to Unitholders in each year, and provided the Fund deducts, in computing its income, the full amount available for deduction in each year, the Fund is not generally liable for income tax under Part I of the Tax Act.

The Fund does not realize any income, gain or loss as a result of entering into the Forward Agreement. Provided that the Common Share Portfolio continues to consist of Canadian securities within the meaning of the Tax Act and the Fund elects in accordance with the Tax Act to have each of its Canadian securities treated as capital property, gains or losses realized by the Fund on the sale of Canadian securities are taxed as capital gains or capital losses. If the obligations of the Fund and the Counterparty under the Forward Agreement are settled by making cash payments, a payment made or received by the Fund may be treated as an income outlay or receipt, as applicable. When the Fund delivers securities in the Common Share Portfolio to the Counterparty in satisfaction of its obligations under the Forward Agreement and receives a payment from the Counterparty equal to the price stipulated in the Forward Agreement, the Fund realizes capital gains (or capital losses) equal to the amount by which such purchase price (less reasonable costs of disposition) exceeds (or is less than) the aggregate adjusted cost base of such securities.

In computing its income for tax purposes, the Fund may deduct reasonable administrative, interest and other expenses incurred by it for the purpose of earning income and generally may deduct over a five-year period the expenses incurred by it to issue Units pursuant to the Offering and not reimbursed.

#### ***14.2 TAXATION OF UNITHOLDERS***

Returns of capital distributed by the Fund to Unitholders are generally not subject to tax but will reduce the adjusted cost base of the Preferred Shares to the Unitholder. The amount of any capital gains dividend received by a Unitholder will be considered to be a capital gain of the Unitholder from the disposition of capital property in the taxation year of the Unitholder in which the capital gains dividend is received. Unitholders are not expected to receive distributions other than returns of capital and, in certain circumstances, capital gains dividends. A disposition of a Preferred Share held as capital property may result in a capital gain or a capital loss to the Unitholder thereof. A redemption or retraction of Preferred Shares is considered to be a disposition for these purposes.

#### ***14.3 HOLDING UNITS***

A Unitholder is generally required to include in computing income for a taxation year, the Unitholder's share of the net income of the Fund (including the taxable portion of any net capital gains) that is paid or becomes payable to the Unitholder in the taxation year, whether or not reinvested in additional Units. Where an appropriate designation is made by the Fund, the portion of (a) any net taxable capital gains of the Fund, and (b) any taxable dividends received by the Fund on shares of taxable Canadian corporations, that is paid or becomes payable to a Unitholder shall retain its character in the hands of the Unitholder. Thus, where an amount is designated to a Unitholder as taxable dividends from taxable Canadian corporations, the normal gross-up and dividend tax credit rules will apply.

The non-taxable portion of any net capital gains of the Fund that is paid or becomes payable to a Unitholder in a year will not be included in computing the Unitholder's income for the year and will not reduce the adjusted cost base of the Units of the Unitholder. Any other amount in excess of a Unitholder's share of the net income of the Fund (including any net capital gains) for a taxation year that is paid or becomes payable to the Unitholder in the year will not generally be included in computing the Unitholder's income for the year. However, the payment by the Fund of such excess amount will reduce the adjusted cost base of the Units of the Unitholder. To the extent that the adjusted cost base of a Unit would otherwise be less than zero, the negative amount will be deemed to be a capital gain realized by the Unitholder from the disposition of the Unit and the Unitholder's adjusted cost base will be increased by the amount of such deemed capital gain.

#### ***14.4 DISPOSITION OF UNITS***

Upon a disposition or deemed disposition by a Unitholder of a Unit, whether on a sale, redemption, repurchase or otherwise, a capital gain (or capital loss) will be realized by the Unitholder to the extent that the proceeds of disposition, net of any reasonable costs of disposition, exceed (or are less than) the adjusted cost base of the Unit to the Unitholder immediately before the disposition. For the purposes of determining the adjusted cost base to a Unitholder of Units, the cost of any newly acquired Units will be averaged with the adjusted cost base of all Units owned by the Unitholder as capital property immediately before such acquisition. The cost of additional Units acquired as a distribution of income (including capital gains) will be equal to the amount of the distribution. A consolidation of Units following a distribution paid in the form of additional Units will not be regarded as a disposition of Units and will not affect the aggregate adjusted cost base to a Unitholder of Units.

Generally, one-half of any capital gain (a “taxable capital gain”) realized by a Unitholder in a taxation year must be included in computing the income of the Unitholder for the year and one-half of any capital loss (an “allowable capital loss”) realized by a Unitholder in a taxation year may be deducted from taxable capital gains realized by the Unitholder in the year in accordance with the rules in the Tax Act. Allowable capital losses for a taxation year in excess of taxable capital gains for that year generally may be carried back and deducted in any of the three preceding taxation years or carried forward and deducted in any subsequent taxation year, against taxable capital gains realized in those years, including taxable capital gains realized on the disposition of Units or amounts designated by the Fund to a Unitholder as taxable capital gains.

#### ***14.5 ALTERNATIVE MINIMUM TAX***

Amounts designated as taxable dividends from taxable Canadian corporations and net realized capital gains paid or payable to a Unitholder by the Fund or realized on the disposition of Units may give rise to a liability for alternative minimum tax.

### **15 MATERIAL CONTRACTS**

The following contracts that have been entered into by the Fund can reasonably be regarded as material to the unitholders:

- (a) the Trust Agreement of the Fund described under “Management of the Fund–The Trustee”;
- (b) the Forward Agreement described under “The Fund–The Forward Agreement”;
- (c) the Registrar and Transfer Agency Agreement between the Fund, the Manager and Computershare Investor Services Inc.; and
- (d) the Agency Agreement.

Copies of the contracts referred to above may be inspected during normal business hours at the offices of the Manager at 181 University Ave, Toronto, Ontario and are available on [www.sedar.com](http://www.sedar.com).

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### **Connor, Clark & Lunn Real Return Income Fund**

Additional information about Connor, Clark & Lunn Real Return Income Fund is available in the financial statements. You can get copy of the financial statements, including a statement of portfolio transactions, at no charge by contacting the Manager by:

- Mail: Connor, Clark & Lunn Capital Markets Inc.  
181 University Avenue  
Suite 300  
Toronto, ON  
M5H 3M7  
[www.cclcapitalmarkets.com](http://www.cclcapitalmarkets.com)
- Phone: 416 862-2020
- E-mail: [dcabral@cclgroup.com](mailto:dcabral@cclgroup.com)