

SIR Royalty Income Fund

Consolidated Financial Statements
December 31, 2005 and 2004

January 27, 2006

Auditors' Report

**To the Unitholders of
SIR Royalty Income Fund**

We have audited the consolidated balance sheets of **SIR Royalty Income Fund** as at December 31, 2005 and 2004 and the consolidated statements of earnings, unitholders' equity and cash flows for the year ended December 31, 2005 and the period from August 23, 2004 to December 31, 2004. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Fund as at December 31, 2005 and 2004 and the results of its operations and its cash flows for the year ended December 31, 2005 and the period from August 23, 2004 to December 31, 2004 in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

Chartered Accountants

Hamilton, Ontario

SIR Royalty Income Fund
Consolidated Balance Sheet

	December 31 2005 \$	December 31, 2004 \$ (see note 2)
Assets		
Current assets		
Prepaid expenses and other assets	32,577	97,296
Amounts due from related parties (note 7)	617,962	742,540
	<u>650,539</u>	<u>839,836</u>
Loan receivable from SIR Corp. (note 3)	40,000,000	40,000,000
Investment in SIR Royalty Limited Partnership (note 4)	11,166,671	11,166,671
	<u>51,817,210</u>	<u>52,006,507</u>
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	105,025	104,000
Amounts due to related parties (note 7)	-	228,771
	<u>105,025</u>	<u>332,771</u>
Unitholders' Equity (note 5)	51,712,185	51,673,736
	<u>51,817,210</u>	<u>52,006,507</u>

Approved by the Board of Trustees

(signed) "Peter Fowler" Trustee

(signed) "Peter Luit" Trustee

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

SIR Royalty Income Fund

Consolidated Statement of Earnings

	Year ended December 31, 2005 \$	Period from August 23, 2004 to December 31, 2004 \$ (see note 2)
Investment income		
Distribution income from Partnership (notes 4 and 7)	4,025,112	873,733
Interest income (note 3)	3,000,000	660,959
	<hr/> 7,025,112	<hr/> 1,534,692
Expenses		
General and administrative (note 7)	558,663	147,526
	<hr/> 6,466,449	<hr/> 1,387,166
Net earnings for the period	<hr/> 6,466,449	<hr/> 1,387,166
Basic and diluted earnings per Fund unit (note 6)	<hr/> \$1.21	<hr/> \$0.26

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

SIR Royalty Income Fund
 Consolidated Statement of Unitholders' Equity

	Year ended December 31, 2005 \$	Period from August 23, 2004 to December 31, 2004 \$ (see note 2)
Balance – Beginning of period – as previously reported	48,140,646	-
Change in accounting policy (note 2)	3,533,090	-
Balance – Beginning of period – restated	51,673,736	-
Issuance of Fund units	-	51,166,670
Net earnings for the period	6,466,449	1,387,166
Distributions declared and paid (note 5)	(6,428,000)	(880,100)
Balance – End of period	<u>51,712,185</u>	<u>51,673,736</u>

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

SIR Royalty Income Fund
 Consolidated Statement of Cash Flows

	Year ended December 31, 2005 \$	Period from August 23, 2004 to December 31, 2004 \$ (see note 2)
Cash provided by (used in)		
Operating activities		
Net earnings for the period	6,466,449	1,387,166
Net change in non-cash working capital items	(38,449)	(507,065)
	<u>6,428,000</u>	<u>880,101</u>
Investing activities		
Loan receivable from SIR Corp.	-	(40,000,000)
Investment in SIR Royalty Limited Partnership	-	(11,166,671)
	<u>-</u>	<u>(51,166,671)</u>
Financing activities		
Distributions paid	(6,428,000)	(880,100)
Issuance of Fund units	-	53,566,670
Issuance costs of Fund units	-	(2,400,000)
	<u>(6,428,000)</u>	<u>50,286,570</u>
Change in cash and cash equivalents	<u>-</u>	<u>-</u>
Cash and cash equivalents – Beginning of period	<u>-</u>	<u>-</u>
Cash and cash equivalents – End of period	<u>-</u>	<u>-</u>

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

SIR Royalty Income Fund

Notes to Consolidated Financial Statements

December 31, 2005 and 2004

1 The Fund

SIR Royalty Income Fund is a trust established on August 23, 2004 under the laws of the Province of Ontario.

On October 1, 2004, SIR Royalty Income Fund (the "Fund") filed a final prospectus for a public offering of units of the Fund. The net proceeds of the offering to the Fund of \$51,166,670 were used by the Fund to acquire, directly, certain bank debt of SIR Corp. (the "SIR loan") and indirectly, through SIR Holdings Trust (the "Trust"), all of the Ordinary LP units of SIR Royalty Limited Partnership (the "Partnership"). The Partnership owns the Canadian trademarks (the "SIR Rights") formerly owned or licensed by SIR Corp. ("SIR") or its subsidiaries and used in connection with the operation of the majority of SIR's restaurants in Canada (the "SIR restaurants"). The Partnership has granted SIR a 99-year license to use the SIR Rights in most of Canada in consideration for a royalty, payable by SIR to the Partnership, equal to 6% of the revenue of the restaurants included in the royalty pool (the "License and Royalty Agreement"). The Fund, indirectly, participates in the revenue generated under the License and Royalty Agreement through its investment in the Partnership (note 4).

2 Summary of significant accounting policies

These consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles and include the accounts of the Fund and its subsidiaries, namely the Trust and SIR GP Inc. All intercompany accounts and transactions have been eliminated.

Use of estimates

The preparation of these financial statements requires management to make estimates and assumptions that affect income and expenses during the reporting periods, in addition to the reported amounts of assets and liabilities and disclosure of contingent liabilities at the date of the financial statements. Actual results could differ materially from those estimates in the near term.

Seasonality

The full service restaurant sector of the Canadian foodservice industry in which SIR operates experiences seasonal fluctuations in revenues. Favourable summer weather generally results in increased revenue during SIR's fourth quarter (ending the last Sunday in August) when patios can be open. Additionally, certain holidays and observances also affect dining patterns both favourably and unfavourably. Accordingly, distribution income recognized by the Fund will vary in conjunction with the seasonality in revenue experienced by SIR.

Cash and cash equivalents

Cash is defined as cash and short-term investments with original maturities of three months or less.

SIR Royalty Income Fund

Notes to Consolidated Financial Statements

December 31, 2005 and 2004

Earnings per Fund unit

The earnings per Fund unit are based on the weighted average number of Fund units outstanding during the period. Diluted earnings per Fund unit are calculated to reflect the dilutive effect, if any, of SIR exercising its right to exchange its Class A GP units of the Partnership into Fund units at the beginning of the period.

Distributions

Distributions to unitholders are intended to be made monthly in arrears and are recorded when declared by the Trustees of the Fund.

Financial instruments

The Fund's financial instruments consist of cash and cash equivalents, loan receivable from SIR, investment in the Partnership, accounts payable and accrued liabilities and amounts due to and from related parties. Unless otherwise noted, it is management's opinion that the Fund is not exposed to significant interest or credit risks arising from these financial instruments. Management estimates that the fair values of these financial instruments approximate their carrying values due to their short-term maturity except for the loan receivable from SIR and the investment in the Partnership. The fair values of the loan receivable from SIR and the investment in the Partnership could only be determined through the valuation of the assets. As a result, the determination of the fair value is not practicable within the constraints of timeliness and cost.

Income taxes

The Fund is a unit trust for income tax purposes. As such, the Fund is only taxable on income not distributed to unitholders. As substantially all taxable income is allocated to unitholders, no provision for income taxes has been made for earnings of the Fund. The Fund's subsidiaries also are not required to pay tax, and accordingly, no provision for income taxes has been made for the earnings of the Fund's subsidiaries.

Investment and loan receivable

The investment in SIR Royalty Limited Partnership is recorded at cost and written down to its estimated realizable amount when there is an impairment. Distribution income from the Partnership is recorded when distributions are declared by the Partnership. To date, had the Fund used the equity method to account for the investment in the Partnership there would not have been any impact on net earnings for the period or the balance of the Fund's investment in the Partnership. The loan receivable from SIR Corp. is reviewed for impairment. If an impairment is identified the loan would be reduced to its estimated realizable amount measured by the present value of expected future cash flows. The accrual of interest would be suspended if collection becomes doubtful. At December 31, 2005 there is no impairment of the investment or loan receivable.

SIR Royalty Income Fund

Notes to Consolidated Financial Statements

December 31, 2005 and 2004

Changes in accounting policy

Consolidation of Variable Interest Entities ("VIEs"), Accounting Guideline – 15

Effective January 1, 2005, the Fund adopted Accounting Guideline – 15 ("AcG-15") of the Canadian Institute of Chartered Accountants ("CICA"), Consolidation of Variable Interest Entities ("VIEs") which requires the consolidation of VIEs by the primary beneficiary. A VIE is an entity where (a) its equity investment at risk is insufficient to permit the entity to finance its activities without additional subordinated support from others and/or where certain essential characteristics of a controlling financial interest are not met, and (b) it does not meet specified exemption criteria. The primary beneficiary is the enterprise that will absorb or receive the majority of the VIE's expected losses, expected residual returns, or both.

The Fund has determined that the Partnership is a VIE and that SIR, under AcG-15, is the primary beneficiary of the Partnership. Therefore the Fund will no longer consolidate the Partnership which it had done previously based on the former consolidation guidelines. The prior year results have been restated to exclude the balances and transactions of the Partnership and to record the Fund's investment in the Partnership at cost. The effect of this change in accounting policy on the consolidated balance sheet as at December 31, 2004 was as follows:

	Balance as previously reported	Adjustment	Balance as restated
	\$	\$	\$
Current assets	1,038,941	(199,105)	839,836
Loan receivable from SIR Corp.	40,000,000	-	40,000,000
Intangible assets	53,585,422	(53,585,422)	-
Investment in SIR Royalty Limited Partnership	-	11,166,671	11,166,671
Current liabilities	531,865	(199,094)	332,771
Non-controlling interest	45,951,852	(45,951,852)	-
Unitholders' equity	48,140,646	3,533,090	51,673,736

The change in accounting policy has had no impact on the consolidated net earnings for the period from August 23, 2004 to December 31, 2004.

The Partnership agreed to pay \$3,533,090 of the cost of the public offering of the Fund and the issuance of the Ordinary LP units of the Partnership and accordingly, upon adoption of AcG-15, unitholders' equity increased by an equivalent amount.

SIR Royalty Income Fund

Notes to Consolidated Financial Statements

December 31, 2005 and 2004

Recently issued accounting pronouncements

Financial Instruments – Recognition and Measurement, Handbook Section 3855

Section 3855 prescribes when a financial asset, financial liability, or non-financial derivative is to be recognized on the balance sheet and at what amount – in certain instances using fair value and in others using cost-based measures. It also specifies how financial instrument gains and losses are to be presented.

Section 3855 applies to interim and annual financial statements relating to fiscal years beginning on or after October 1, 2006. Earlier adoption is permitted only as of the beginning of a fiscal year ending on or after December 31, 2004. The Fund plans to adopt this standard for its 2007 fiscal year. Transitional provisions for this Section are complex and vary based on the type of financial instrument under consideration.

The Fund is currently evaluating the effect of this standard.

Comprehensive Income, Handbook Section 1530

Section 1530 introduces a new requirement to temporarily present certain gains and losses outside net income.

Section 1530 applies to interim and annual financial statements relating to fiscal years beginning on or after October 1, 2006. Earlier adoption is permitted only as of the beginning of a fiscal year ending on or after December 31, 2004. The Fund plans to adopt this standard for its 2007 fiscal year. Financial statements of prior periods are required to be restated for certain comprehensive income items. In addition, an enterprise is encouraged, but not required, to present reclassification adjustments in comparative financial statements provided for earlier periods.

The Fund is currently evaluating the effect of this standard.

Hedges – Handbook Section 3865

Section 3865 establishes standards for when and how hedge accounting may be applied. Hedge accounting is optional. This Section applies for interim and annual financial statements relating to fiscal years beginning on or after October 1, 2006. Retroactive application is not permitted. Earlier adoption is permitted only as of the beginning of a fiscal year that ends on or after December 31, 2004.

The Fund plans to adopt this standard for its 2007 fiscal year. The Fund has no arrangements for hedging, and the adoption of this standard is not expected to have any impact on the Fund at this time.

SIR Royalty Income Fund

Notes to Consolidated Financial Statements
December 31, 2005 and 2004

3 Loan receivable from SIR Corp.

The SIR loan bears interest at 7.5% per annum, is due October 12, 2044 and is collateralized by a general security agreement covering substantially all of the assets of SIR and its subsidiaries in Canada. Interest income of \$3,000,000 was earned during the year ended December 31, 2005 (period from August 23, 2004 to December 31, 2004 - \$660,959).

SIR has the right to require the Fund to, indirectly, purchase the Class C GP units of the Partnership and assume a portion of the SIR loan as consideration for the acquisition of the Class C GP units.

4 Investment in SIR Royalty Limited Partnership

On October 12, 2004, the Fund, indirectly through the Trust, acquired all of the Ordinary LP units of the Partnership. The holders of the Ordinary LP and Class A GP units are entitled to receive a pro rata share of distributions of the Partnership. The holder of the Ordinary LP units have the right to receive distributions in priority to the initial 595,185 Class A GP units. The subordination on the distributions on the Class A GP units of the Partnership ends on the date that both of the following conditions have been satisfied:

- a) Revenue of the SIR restaurants subject to the License and Royalty Agreement has not been less than \$127.4 million for each of two consecutive years commencing with SIR's fiscal year ending August 28, 2005; and
- b) Average monthly distributions of \$0.10 per Fund unit have been paid by the Fund and average quarterly cash distributions of at least \$0.30 have been paid by the Partnership to the Class A GP unitholders, in each case for the immediately preceding twelve month period.

The subordination on the distributions on the initial Class A GP units of the Partnership is expected to continue until at least August 26, 2007.

The distributions from the Partnership primarily comprise revenue earned by the Partnership under the License and Royalty Agreement (note 1) less certain general and administrative expenses. Distributions for the year ended December 31, 2005 amount to \$4,025,112 (period from August 23, 2004 to December 31, 2004 - \$873,733).

SIR Royalty Income Fund

Notes to Consolidated Financial Statements
December 31, 2005 and 2004

5 Fund units

An unlimited number of Fund units may be issued pursuant to the declaration of trust. Fund units are redeemable by the holder at a price equal to the lesser of 90% of the market price of a unit during the 10 consecutive trading day period ending on the trading day immediately prior to the date on which the units were surrendered for redemption and an amount based on the closing price on the redemption date, subject to certain restrictions. Each holder of units of the Fund participates pro rata in any distributions from the Fund. Income tax obligations related to the distributions by the Fund are obligations of the unitholders. The Fund issued one unit on August 23, 2004 for cash proceeds of \$10. Upon completion of the initial public offering, the initial unit was redeemed for \$10.

On October 12, 2004, the Fund issued 5,356,667 units for cash proceeds of \$51,166,670, net of unit issuance costs of \$2,400,000. As at December 31, 2005 and December 31, 2004, there are 5,356,667 units issued and outstanding. Each unit is entitled to one vote at any meeting of unitholders.

During the year ended December 31, 2005, the Fund declared distributions of \$1.20 per unit (period from August 23, 2004 to December 31, 2004 - \$0.16 per unit). Subsequent to December 31, 2005, the Fund declared a distribution of \$0.10 per unit for the month of December 2005.

6 Earnings per Fund unit

Basic earnings per Fund unit is computed by dividing net earnings by the weighted average number of Fund units outstanding during the period.

Subject to the subordination provisions of the Class A GP units, SIR has the right to convert the Class A GP units of the Partnership into units of the Fund. Diluted earnings per Fund unit is calculated using the weighted average number of Fund units outstanding adjusted to include the effect of the conversion of the Class A GP units of the Partnership into Fund units.

SIR Royalty Income Fund

Notes to Consolidated Financial Statements

December 31, 2005 and 2004

The following table reconciles the basic and diluted weighted average number of Fund units outstanding and basic and diluted earnings per Fund unit:

	Basic earnings per Fund unit	Adjustments for conversion of Class A GP units	Diluted earnings per Fund unit
Net earnings for the year ended December 31, 2005	\$6,466,449	\$718,494	\$7,184,943
Earnings per Fund unit for the year ended December 31, 2005	\$1.21		\$1.21
Net earnings for the period from August 23, 2004 to December 31, 2004	\$1,387,166	\$170,520	\$1,557,686
Net earnings per unit for the period from August 23, 2004 to December 31, 2004	\$0.26		\$0.26
Weighted average number of Fund units outstanding for the year ended December 31, 2005 and the period from August 23, 2004 to December 31, 2004	5,356,667	595,185	5,951,852

7 Related party transactions and balances

During the year ended December 31, 2005, the Fund received distribution income of \$4,025,112 from the Partnership (period from August 23, 2004 to December 31, 2004 - \$873,733). The Fund, indirectly through the Trust, is entitled to receive a pro rata share of all residual distributions. The Fund's distribution income is dependent upon the revenue generated by SIR for the restaurants subject to the License and Royalty Agreement. Under the terms of the License and Royalty Agreement, SIR may be required to pay a make-whole payment in respect of the reduction in revenue for restaurants closed during a reporting period. SIR is not required to pay any make-whole payment in respect of a closed restaurant following the date on which the number of restaurants in the royalty pool is equal to or greater than 68 or following October 12, 2019, whichever occurs first. On January 1 of each year (the adjustment date), following December 31, 2005, the restaurants subject to the License and Royalty Agreement are adjusted for new restaurants opened in the previous fiscal year. At each adjustment date, SIR will be entitled to convert its Class B GP units of the Partnership to Class A GP units of the Partnership based on a conversion formula defined in the License and Royalty Agreement.

On January 1, 2006, two new SIR Restaurants were added to the Royalty Pooled Restaurants in accordance with the License and Royalty Agreement. As consideration for the additional royalty associated with the addition of two new restaurants, SIR converted 438,820 Class B GP units of the Partnership into 438,820 Class A GP units of the Partnership.

SIR Royalty Income Fund

Notes to Consolidated Financial Statements

December 31, 2005 and 2004

The Partnership has entered into an arrangement with the Fund and the Trust whereby the Partnership will provide or arrange for the provision of services required in the administration of the Fund and the Trust. The Partnership has arranged for these services to be provided by SIR GP Inc. in its capacity as the Managing General Partner, or SIR as General Partner, of the Partnership. SIR, on behalf of SIR GP Inc., also provides services to the Partnership for its administration. For the year ended December 31, 2005, the Partnership provided these services to the Fund and the Trust for consideration of \$24,000 (period from August 23, 2004 to December 31, 2004 - \$5,288), which was the amount of consideration agreed to by the related parties.

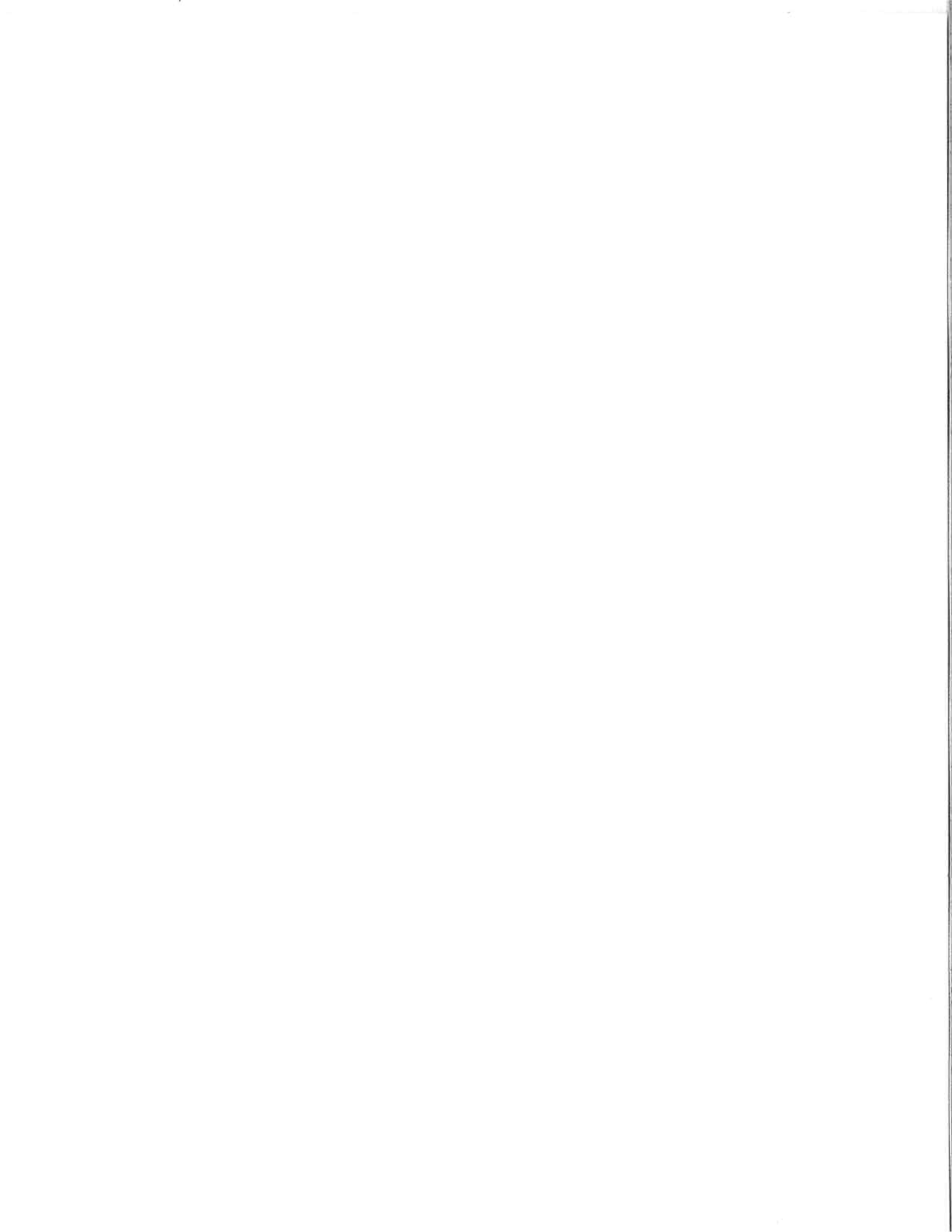
Amounts due from (to) related parties consist of:

	December 31, 2005	December 31, 2004
	\$	\$
Distribution receivable	890,917	873,733
Advances payable	(503,243)	(131,193)
Amounts receivable from SIR Royalty Limited Partnership	<u>387,674</u>	<u>742,540</u>
Interest receivable	250,000	250,000
Advances payable	(19,712)	(478,771)
Amounts receivable from (payable to) SIR Corp.	<u>230,288</u>	<u>(228,771)</u>
Amounts due from (to) related parties – net	<u>617,962</u>	<u>513,769</u>

Amounts due to (from) related parties are non-interest bearing and due on demand. All advances were conducted as part of the normal course of business operations.

8 Economic dependence

The Fund's income is derived from interest income on the SIR loan and distributions from the Partnership and accordingly, the Fund is economically dependent upon SIR.



SIR Royalty Limited Partnership

Financial Statements
December 31, 2005 and 2004

January 27, 2006

Auditors' Report

To the Partners of SIR Royalty Limited Partnership

We have audited the balance sheets of **SIR Royalty Limited Partnership** as at December 31, 2005 and 2004 and the statements of earnings, partners' interest and cash flows for the year ended December 31, 2005 and the period from May 13, 2004 to December 31, 2004. These financial statements are the responsibility of the Partnership's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Partnership as at December 31, 2005 and 2004 and the results of its operations and its cash flows for the year ended December 31, 2005 and the period from May 13, 2004 to December 31, 2004 in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

Chartered Accountants

Hamilton, Ontario