

**NORTHWATER**

NORTHWATER MARKET-NEUTRAL TRUST

ANNUAL INFORMATION FORM

For the fiscal year ended December 31, 2007

As at  
March 31, 2008

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**GENERAL**

The information contained in this Annual Information Form is given as of March 31, 2008. All dollar amounts are stated in Canadian currency unless otherwise indicated.

**NAME, FORMATION AND HISTORY OF THE TRUST:**

Northwater Market-Neutral Trust (the "Trust") is a closed-end investment trust established under the laws of Ontario pursuant to a trust agreement made as of July 18, 1997 and restated on August 17, 1999. The trust agreement was further amended as a result of a special meeting of unitholders held on April 19, 2004. RBC Dexia Investor Services Trust, as successor trustee to The Royal Trust Company, acts as trustee (the "Trustee"). Northwater Fund Management Inc., formerly Newcastle Fund Management Inc., is the manager of the Trust (the "Manager"). The Manager has appointed Northwater Capital Management Inc., formed during 2001 by the amalgamation of Newcastle Capital Management Inc. and NewQuant Capital Inc., as the advisor to the Trust (the "Investment Advisor").

The address of the Trust's principal and head office is Suite 4700, BCE Place, Bay Wellington Tower, 181 Bay Street, P.O. Box 794, Toronto, Ontario, M5J 2T3.

The beneficial interest in the net assets and net income of the Trust is divided into trust units of equal value (the "Units"). Holders of Units are referred to herein as Unitholders.

**Investment Objectives**

The Trust's investment objectives are to: 1) distribute quarterly 2% of the net asset value per unit of the Trust as of the month end proceeding the relevant calendar quarter end (prior to April 19, 2004 - \$0.40 per unit per quarter); 2) steadily grow the net asset value (the "Net Asset Value") per Unit; 3) ensure that the performance of the Trust is substantially independent of the major fixed income and equity markets; and 4) achieve a low volatility, which is expected to be less than that of a mid-term bond portfolio and less than one-half that of major North American stock markets.

**Investment Strategy**

In order to meet its investment objectives, the Trust is invested in a diversified portfolio of hedge funds that are either purely market-neutral or well-hedged with respect to major fixed income and equity markets (the "Hedge Fund Portfolio"). Pursuant to the final prospectus dated July 18, 1997 (the "Prospectus") and in accordance with the Trust Agreement, the Trust is required to invest in at least 10 such funds. The Trust may also make investments that, although they may not be fully hedged, are in markets that, in the Investment Advisor's opinion, have expected returns that have a very low correlation with a mid-term bond portfolio and the major North American stock markets. In addition, to ensure that the Trust achieves relatively low volatility, the Investment Advisor looks for hedge funds that have a low

correlation with one another. The Investment Advisor utilizes a proprietary selection process that it has developed in managing similar portfolios to construct this portfolio of hedge funds.

The Trust focuses its investments on hedge funds that invest in sectors of the capital markets that are relatively inefficient. The Investment Advisor believes that such sectors are poorly researched and imperfectly arbitrated and as such will reward insightful investment analysis. The following are examples of hedged, non-traditional investment strategies that may be included in the Trust:

- Activist
- Asset-backed securities arbitrage
- Capital structure arbitrage
- Convertible bond arbitrage
- Distressed securities
- Energy relative value
- Fixed-income arbitrage
- Market-neutral equity
- Merger arbitrage
- Mortgage-backed security arbitrage
- Re-insurance
- Statistical arbitrage
- Structured finance
- Volatility arbitrage

The Foregoing list is not exhaustive.

Each of the strategies included in the Trust affords a certain amount of risk. However, these strategies exhibit low correlation with one another. It is this low correlation that results in lower overall risk of the Trust. The Investment Advisor believes, based on experience with similar portfolios, that the volatility of investment returns for the Trust will be substantially reduced by the enhanced level of diversification achieved by investing in hedge funds that have a very low level of correlation with one another. As a result, the risk of the Trust, as measured by standard deviation, is expected to be lower than the risk of a mid-term bond fund and less than one-half that of the major North American equity markets.

In order to optimize the Trust's investment performance, the Investment Advisor regularly monitors and reviews the investment strategies of the hedge funds in which the Trust is invested as well as the performance of the managers of each fund. In particular, the Investment Advisor reviews organizational changes made to the hedge funds in which the Trust is invested and changes in policy relative to investment objectives, hedging strategy, degree of diversification, leverage and costs. In addition, the Investment Advisor monitors the hedge fund industry and reviews new investment strategies and new types of hedge funds being offered. Based on the regular application of its proprietary process, the Investment Advisor may from time to time reallocate the Trust's assets among funds with different investment strategies or among different fund managers or invest in hedge funds with new investment strategies.

The Investment Advisor requires that the Trust maintain the level of liquidity reasonably necessary to satisfy its obligations to Unitholders. As many of the hedge funds in which the Trust invests have restrictions that limit the liquidity of the Trust's investment, the Investment Advisor seeks to maintain an appropriate level of liquidity by also investing in hedge funds that have greater liquidity. This involves investing in hedge funds that provide for more frequent redemptions or hedge funds whose shares are listed on an organized market that facilitates secondary trading of such shares.

The Trust has incurred indebtedness to enhance the investment return. The Trust makes use of derivatives to moderate or eliminate foreign currency risk associated with the underlying investments.

### **Proprietary Selection Process**

The Investment Advisor uses its Proprietary Selection Process to advise with respect to the selection and monitoring of potential hedge fund investments to be made by the Hedge Fund Portfolio. The Proprietary Selection Process consists of:

- 1) The development of a multi-faceted set of investment beliefs, which serve as a framework for identifying appropriate market-neutral strategies and the managers that employ those strategies. These investment beliefs have evolved with the Investment Advisor's experience in market-neutral hedge fund investing and in managing complex derivatives strategies.
- 2) The use of an established operational infrastructure necessary for managing complex market-neutral and derivative strategies. The Investment Advisor has built a team of investment professionals and developed robust portfolio and risk management systems and tools essential to managing a sophisticated fund of market-neutral hedge funds.
- 3) A progressive global search for market-neutral strategies consistent with the Investment Advisor's investment beliefs and the Hedge Fund Portfolio's investment criteria of market-neutrality and strong risk-adjusted returns. The Investment Advisor's search focuses on managers who have demonstrated expertise in consistently implementing these strategies.
- 4) A comprehensive quantitative and qualitative assessment of hedge fund managers who employ market-neutral strategies that adhere to the Investment Advisor's investment beliefs and the objectives of the Hedge Fund Portfolio.
- 5) The use of specific quantitative procedures, including screens that attempt to identify consistency and adaptability, market-neutrality, and portfolio fit, which are integral to the Investment Advisor's investment process. Various portfolio construction techniques are used, including mathematical optimization, statistical process control and factor analysis.
- 6) An ongoing qualitative assessment of existing and prospective hedge fund managers. Hedge fund manager reviews involve on-site interviews, monthly portfolio reviews and various industry references. The goal of this process is to fully understand the hedge fund manager's investment strategy and risk management processes. The Investment

Advisor also seeks to ascertain the strength of a hedge fund manager's competitive advantage, its investment team and its business plans.

- 7) The construction of a diversified model portfolio. The model portfolio serves as a target portfolio for the Trust and will be diversified across approximately 14 market-neutral strategies and included 37 hedge funds as at December 31, 2007. This is a dynamic process.
- 8) A comprehensive due diligence process that typically must be completed before the Investment Advisor recommends an investment. This process includes on-site interviews by investment professionals from the Investment Advisor, an all-inclusive strategy and operational due diligence report, a legal review of the offering documentation, an analysis of the hedge fund's financial statements, an assessment of the fees charged by the hedge fund's manager and an examination of any administrative or other costs associated with making the investment. Rigorous monitoring and due diligence continues once a hedge fund is added to the Hedge Fund Portfolio. This process includes regular discussions with the hedge fund manager, multiple on-site interviews each year, continual quantitative and qualitative assessments and monthly justification of the hedge fund's role within the Investment Advisor's model portfolio.

## **Distributions**

The Trust endeavors to pay to Unitholders at the end of each quarter (the "Record Date") cash distributions of 2% of the net asset value per Unit of the Trust as of the month end proceeding the relevant Record Date. The date of declaration of the distribution is referred to as the "Declaration Date".

In addition, the Trust distributes annually in respect of each Unit a pro rata share of the taxable net income of the Trust including any amount the Trust is required to include in computing its taxable income as a result of its ownership of an offshore investment property (such net income is included in the per Unit distribution and is paid to Unitholders regardless of the amount of the increase in the Net Asset Value per Unit of the Trust).

Unitholders will be entitled to receive declared distributions if they were Unitholders of record as of 5:00 p.m. (Toronto time) on the relevant Record Date. Distributions will be made within 20 business days after the Record Date (a "Distribution Date").

Holders of Units who are non-residents of Canada are required to pay all withholding taxes payable in respect of any distributions of income by the Trust. The Trust will cause the withholding from the distributions and the remittance to the relevant tax authority of all amounts required by law to be withheld and remitted. Non-residents should consult their tax advisors regarding the tax consequences of investing in Units.

## **Distribution Reinvestment Plan**

If a Unitholder so elects, quarterly distributions will be automatically reinvested in additional Units of the Trust. A Unitholder must elect to receive distributions in additional Units by notifying his or her dealer.

Distributions payable to participants in the Plan (the "Participants") are paid to CIBC Mellon Trust Company in its capacity as agent under the Plan (the "Plan Agent") and applied to purchase Units. Such purchases are either made through the purchase of new Units from the Trust or in the market. If the closing market price plus applicable commissions or brokerage charges (collectively, the "Market Price") of the Units during the first 15 business days following the Record Date is less than the most recent Net Asset Value (as defined below under "Net Asset Value") per Unit as at that date, the Plan Agent will apply the distribution to purchase Units in the market. If the Market Price of the Units during this period is greater than the most recent Net Asset Value per Unit, the Plan Agent will apply the distribution to purchase Units from the Trust through the issue of new whole Units at a price per Unit equal to the greater of (i) Net Asset Value per Unit on the Declaration Date; and (ii) 95% of the weighted average of the trading prices of the Units for the five trading days preceding the Declaration Date.

Purchases in the market are made during the 15 business day period next following the Record Date at such times as the Market Price of the Units is less than the most recent Net Asset Value per Unit. Upon the expiration of such period, the unused part, if any, of the distribution attributable to the Plan Participants is used to purchase Units from the Trust on the basis set forth above. The Units purchased in the market or from the Trust are allocated to the Plan Participants in proportion to their share of the distribution. The Plan Agent furnishes to each Plan Participant a report of the Units purchased for the Plan Participant's account in respect of each distribution and the cumulative total of all Units purchased for that account. The Trust does not issue fractional Units. A Plan Participant's *pro rata* entitlement to Units purchased under the Plan may include a fraction of a Unit in lieu of which a cash payment will be made by the Plan Agent. No certificates representing Units issued or purchased pursuant to the Plan are issued. The Plan Agent's charges for administering the Plan are paid by the Trust. The reinvestment of distributions under the Plan does not relieve Participants of any income tax applicable to such distributions.

Plan Participants may terminate their participation in the Plan at any time by written notice to the Plan Agent through his or her dealer and thereafter distributions payable to such Plan Participants will be made in cash. The Trustee may terminate the Plan, in its sole discretion, upon not less than thirty days' notice to the Plan Participants.

### **Purchases for Cancellation**

Units of listed investment trusts may trade at a discount from net asset value. In recognition of the possibility that the Units may trade at a discount, the terms and conditions attaching to the Units have been designed to attempt to reduce or eliminate a market value discount from Net Asset Value.

To that end, the Trust Agreement provides that if at any time the price at which Unitholders are then offering their Units for sale on the Toronto Stock Exchange (or such other exchange or market on which the Units are then listed) is less than 92.5% of the Net Asset Value per Unit determined as at the close of business on the preceding Valuation Date, then subject to certain exceptions described herein and compliance with any applicable regulatory

requirements, the Trust is obligated to purchase any such Units offered in the market at the then prevailing market price up to a maximum amount in any calendar quarter of 2% of the number of Units outstanding at the beginning of such calendar quarter.

In addition, the Trust has the right (but not the obligation) at any time, exercisable in its sole discretion, to purchase Units in the market whenever Unitholders offer their Units for sale at less than Net Asset Value, subject to any applicable regulatory requirements and limitations. It is expected that these purchases will be made as normal course issuer bids through the facilities and under the rules of the Toronto Stock Exchange (or such other exchange or market on which the Units are then listed).

Notwithstanding the foregoing, purchases will not be effected if: (a) in the opinion of the Manager such transactions, if consummated, could result in the marketability of the Units being severely impaired to the detriment of the Unitholders; (b) in order to fund the purchase, the Trust is not able to liquidate portfolio securities in an orderly manner consistent with the Trust's Investment Strategy or, alternatively, it is not in the best interest of the Unitholders to do so; or (c) there is, in the judgment of the Manager (i) any material legal action or proceeding instituted or threatened challenging such transactions or otherwise materially adversely affecting the Trust, or (ii) a suspension of or limitation on prices for trading securities generally on any exchange on which portfolio securities of the Trust are traded.

Units that have been purchased by the Trust are cancelled thereby reducing the total assets of the Trust but increasing the Net Asset Value per Unit for the Unitholders. If the Trust must liquidate portfolio securities in order to purchase Units, the Trust may realize gains or losses, which gains will be paid or made payable to Unitholders in the year they are realized.

There can be no assurance that purchases of Units by the Trust will result in the Units trading at a price that is equal to the Net Asset Value of the Units. The Trust anticipates that the market price of the Units will in any event vary from Net Asset Value. The market price of the Units will, among other things, be determined by the relative demand for and supply of Units in the market, the Trust's investment performance, the Units' yield and investor perception of the Trust's overall attractiveness as an investment as compared with other investment alternatives. Nevertheless, the fact that the Units may be purchased by the Trust may reduce the potential spread between market price and Net Asset Value that might otherwise exist.

Although it is anticipated that actual Unit purchases generally may have a favourable effect on the market price of the Units, it should be recognized that the acquisition of Units by the Trust will decrease the total assets of the Trust and therefore have the effect of increasing the Trust's expense ratio provided the total expenses do not change.

## **Termination of the Trust**

The Trust will continue until December 31, 2009 (the "Termination Date") and thereupon will terminate and the net assets of the Trust will be distributed to the Unitholders unless an alternative to termination is approved by the Unitholders as described below. Prior to the Termination Date, the Investment Advisor will, to the extent practicable, convert the assets of the Trust to cash.

Not less than 12 months nor more than 18 months prior to the Termination Date, the Manager may present a proposal to Unitholders providing an alternative to the dissolution of the Trust on the Termination Date. Such proposal could include, without limitation: (i) continuing the Trust; or (ii) exchanging the Units for units in one or more mutual funds or closed-end investment funds on or after the Termination Date. A meeting of Unitholders to consider such a proposal must be held at least 12 months prior to the Termination Date in order to give the Manager the opportunity to conduct an orderly liquidation of the assets of the Trust in the event that the Unitholders do not approve the proposal. In order to be implemented, such proposal would require the approval of Unitholders by Extraordinary Resolution (and for any such Extraordinary Resolution a quorum even at an adjourned meeting will consist of two or more Unitholders present in person or by proxy and representing not less than 10% of the Units then outstanding). Any such proposal may be conditional on such matters as the Manager considers are appropriate including, without limitation, obtaining any necessary regulatory approvals.

## **Loan Facility**

The Manager, on behalf of the Trust, has entered into a loan agreement (the "Loan Agreement") with a financial institution (the "Bank") and has a loan facility in place. The loan facility entitles the Trust to borrow funds in Canadian or U.S. dollars. The Loan Agreement contains terms and conditions customary for agreements of this nature.

The Loan Agreement permits the Trust to borrow up to an amount not exceeding 25% of the Net Asset Value of the Trust, for the purpose of purchasing additional investments in accordance with the Investment Objectives. In addition, the Trust may borrow on a temporary basis up to an amount not exceeding 10% of the Net Asset Value of the Trust for the purpose of (i) effecting market purchases of Units; (ii) maintaining liquidity to effect cash distributions; and (iii) settling currency hedging transactions.

The Trust has provided a security interest in its assets in favour of the Bank to secure such borrowings. Indebtedness of the Trust may consist of amounts borrowed under the Loan Agreement. In the event that the total amount borrowed by the Trust exceeds at any time 35% of the Net Asset Value of the Trust or \$22 million, the Manager must take appropriate steps with the Trust's investment portfolio in order that the amount of the indebtedness does not exceed 35% of the Net Asset Value of the Trust or \$22 million, including liquidating certain of the Trust's investments and using the proceeds thereof to reduce the Trust's indebtedness.

In the event of a default by the Trust under the Loan Agreement, the Loan Agreement provides that the Bank's recourse will be limited solely to the assets of the Trust.

**INVESTMENT RESTRICTIONS:**

The activities of the Fund are subject to certain investment restrictions contained in its constating documents. For purposes of the restrictions listed below, all percentage limitations apply only immediately after a transaction and any subsequent change in any applicable percentage resulting from changing values will not require elimination of any security from the Hedge Fund Portfolio (except for the restriction in paragraph 4, which must be complied with at all times and which may necessitate the selling of and reinvesting in securities from time to time). These investment restrictions provide, among other things, the following:

1. **Sole Undertaking.** The Trust will not engage in any undertaking other than the investment of the Trust's assets in accordance with the Investment Objectives and the Investment Strategy.
2. **Fixed Price.** The Trust will not purchase any security that by its terms requires the Trust to make a contribution in addition to the payment of the purchase price, other than a permitted derivative pursuant to a transaction described below (see "Limit on Derivatives" below), provided that this restriction shall not apply to the purchase of securities that are paid for on an installment basis where the total purchase price and the amount of all such installments is fixed at the time the first installment is paid.
3. **No Material Interest.** The Trust will not purchase securities from, sell securities to, or otherwise contract for the acquisition and disposition of securities with the Investment Advisor or any of its respective affiliates, any officer, director or shareholder of any of them, any person, trust, firm or corporation managed by the Investment Advisor or any of its respective affiliates or any firm or corporation in which any officer, director or shareholder of the Investment Advisor may have a material interest (which, for these purposes, includes beneficial ownership of more than 10% of the voting securities of such entity) unless, with respect to any purchase or sale of securities, any such transaction is effected through normal market facilities and the purchase price approximates the prevailing market price.
4. **Unit Trust Qualification.** The Investment Advisor will manage the assets of the Trust so as to ensure that the Trust qualifies as a "unit trust" within the meaning of the *Income Tax Act* (Canada) (the "Tax Act"). As a result:
  - (i) at least 80% of the property of the Trust at all times must consist of any combination of shares, bonds, marketable securities, cash, notes or other similar obligations, or other investments permitted to be held by "unit trusts", as defined by the Tax Act from time to time;
  - (ii) at least 95% of its income for each year must be derived from, or from the disposition of, investments described in (i) above; and

- (iii) at no time may more than 10% of its property consist of shares, bonds or securities of any one corporation or debtor other than Her Majesty in Right of Canada or a province or a Canadian municipality.
5. **Limit on Derivatives.** The Trust will not purchase or sell derivatives other than for the purpose of off-setting or reducing foreign currency risk associated with an investment or group of investments. The Trust may use futures, forwards or options for currency hedging purposes.
  6. **Restriction on Underwriting.** The Trust will not act as an underwriter except to the extent that the Trust may be deemed to be an underwriter in connection with the sale of securities in its investment portfolio.
  7. **No Commodities.** The Trust will not purchase or sell physical commodities with the intention to make or take physical delivery.
  8. **Related Party Transactions.** The Trust shall not knowingly make an investment in any class of securities of any issuer, other than those issued or guaranteed by Canadian governments,
    - (a) for which the Investment Advisor (a related party of the Trust) or any associate or affiliate of the Investment Advisor (individually a "manager") has acted as an underwriter in the distribution of such class of securities (except as a member of a selling group distributing 5% or less of the securities underwritten) for a period of at least 60 days following the conclusion of the distribution of the underwritten securities to the public; or
    - (b) of which any partner, director, officer or employee of a manager or any partner, director, officer or employee of any affiliate or associate of such manager is an officer or director, provided that this prohibition will not apply where any such person does not:
      - (i) participate in the formulation of investment decisions made on behalf of the Trust;
      - (ii) have access to the investment decision-making process of the Trust prior to the implementation of investment decisions made on behalf of the Trust; and
      - (iii) influence (other than through research, statistical and other reports generally available to clients) the investment decisions made on behalf of the Trust; or
    - (c) in which a manager or any partner, director, officer or employee of a manager had a material interest (which for these purposes includes beneficial ownership of more than 10% of the voting securities of the issuer).

9. **Limit on Indebtedness.** The Trust may borrow up to an amount not exceeding 25% of the Net Asset Value (as defined under "Net Asset Value") of the Trust, for the purpose of purchasing additional investments in accordance with the Investment Objectives. In addition, the Trust may borrow on a temporary basis up to an amount not exceeding 10% of the Net Asset Value of the Trust for the purpose of (i) effecting market purchases of Units; (ii) maintaining liquidity to effect cash distributions; and (iii) settling currency hedging transactions.
10. **Restriction on Experience of Underlying Fund Managers.** The Trust will not purchase securities of any underlying hedge fund unless either: (i) the hedge fund has been in operation for at least two years or (ii) the manager of the hedge fund has been engaged in the hedge fund management business for at least two years.
11. **Liquidity of Investment on Termination of the Trust.** The Trust will not invest in securities that by their terms will not be redeemable prior to the termination of the Trust.

#### **DESCRIPTION OF THE UNITS OFFERED BY THE TRUST:**

The Trust is a closed-end investment trust created pursuant to the Trust Agreement and governed by the laws of the Province of Ontario. The Trust was authorized to issue transferable units of beneficial interest on initial public offering. Each Unit represents an equal, undivided interest in the net assets of the Trust.

Each Unit entitles the holder to the same rights and obligations as a holder of any other Unit and no Unitholder is entitled to any privilege, priority or preference in relation to any other Unitholders. Each Unitholder is entitled to one vote for each Unit held and is entitled to participate equally with respect to any and all distributions made by the Trust, including distributions of net income and net realized capital gains. On termination, the Unitholders of record holding outstanding Units are entitled to receive all of the assets of the Trust remaining after payment of all debts, liabilities and liquidation expenses of the Trust.

#### **Meetings of Unitholders**

The Trustee may, at any time, convene a meeting of the Unitholders and is required to convene a meeting on receipt of a request in writing of the Manager or of Unitholders holding, in aggregate, 10% or more of the Units outstanding.

Any matter to be considered at a meeting of Unitholders, other than certain matters requiring the approval of Unitholders by extraordinary resolution (an "Extraordinary Resolution") as discussed below, requires the approval of Unitholders by a resolution passed by holders of not less than 50% of the Units voting thereon at a meeting duly convened for the consideration of such matter. A quorum for any meeting convened to consider such matter consists of two or more Unitholders present in person or by proxy and representing not less than 10% of the Units outstanding. If a quorum is not present at a meeting within 30 minutes after the time fixed for the meeting, the meeting, if convened pursuant to a request of Unitholders, will be cancelled, but otherwise will be adjourned to another day, not less than 10 days nor more than 21 days later, selected by the Manager and notice will be given to the Unitholders of such

adjourned meeting. The Unitholders present at any adjourned meeting will constitute a quorum. Each Unitholder is entitled to one vote per Unit held.

Notwithstanding the foregoing, certain matters will require the approval of Unitholders by Extraordinary Resolution. An Extraordinary Resolution is a resolution passed by holders of not less than 66 <sup>2</sup>/<sub>3</sub>% of the Units voting thereon at a meeting duly convened for the consideration of such matter. A quorum for any meeting convened to consider a matter requiring the approval of Unitholders by Extraordinary Resolution consists of two or more Unitholders present in person or by proxy and representing not less than 50% of the Units then outstanding except, in the case of a meeting convened to extend the term of the Trust which will require the approval of Unitholders by Extraordinary Resolution consisting of two or more Unitholders present in person or by proxy representing not less than 10% of the Units then outstanding. See "Termination of the Trust".

### **Acts Requiring Unitholder Approval**

The Trust Agreement may be amended with the consent of the Unitholders given by Extraordinary Resolution. However, unless all of the Unitholders consent thereto, no amendment can be made to the Trust Agreement that would have the effect of reducing the interest in the Trust of the Unitholders, increasing the liability of any Unitholder or changing the right of a Unitholder to vote at any meeting. No amendment can be made to the Trust Agreement that would have the effect of reducing the fees payable to the Manager or the terms for terminating the Manager unless the Manager, in its sole discretion, consents.

Notwithstanding the foregoing, the Manager is entitled, without the consent of the Unitholders, to make certain amendments to the Trust Agreement that are for the purpose of adding any provisions that, in the opinion of the Manager, are for the protection or benefit of the Unitholders or the Trust, for the purpose of curing an ambiguity or for the purpose of supplementing any provision that may be defective or inconsistent with another provision, including without limitation, for the purpose of ensuring that the Trust Agreement and this prospectus are not inconsistent. The Manager must disclose such change in the next regularly scheduled report to Unitholders. Such amendments may be made only if they will not materially adversely affect the interest of any Unitholder or the Trustee.

### **Reporting to Unitholders**

The Trust's fiscal year is the calendar year. A copy of the Trust's December 31, 2007 audited annual financial statements and an annual report will be mailed by the Manager to each Unitholder by March 28, 2008. In accordance with the provisions of National Instrument 81-106, the annual financial statements and annual reports of the Trust are required to be mailed to each Unitholder within 90 days following the end of the fiscal year. Within 60 days following June 30 of each year, an unaudited semi-annual report prepared in accordance with applicable regulatory requirements will be mailed to unitholders.

In addition, the Manager shall, on or before February 28<sup>th</sup> of each year, cause to be forwarded to each Unitholder of record on any Record Date of the preceding year information in a

suitable form to enable the Unitholder to comply with his or her income tax reporting obligations relating to his or her interest in the Trust.

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

**VALUATION OF PORTFOLIO SECURITIES AND CALCULATION OF NET ASSET VALUE:**

The Manager, as of the last business day of each month (each, a "Valuation Date"), calculates the value of the Trust's assets as set forth below.

The net asset value of the Trust (the "Net Asset Value") is calculated by the Manager on each Valuation Date by subtracting the aggregate amount of the Trust's liabilities from the aggregate value of the Trust's assets (the "Total Assets"). The Total Assets are valued as follows:

- (i) the value of cash, receivables, prepaid expenses, dividends and interest declared or accrued and not yet received, is deemed to be the face value unless the Manager considers otherwise;
- (ii) the value of futures, options, or securities traded on a public exchange is the settlement price as published by the clearing house of the exchange;
- (iii) the value of over-the-counter options shall be the current market price thereof and the value of forward contracts shall be the gain or loss that would be realized if on such date the forward contracts were "closed out";
- (iv) the value of treasury bills and other money market instruments is the bid price for such instruments at the Toronto closing time on the Valuation Date;
- (v) the value of any unit or share of a private investment fund is the definitive net asset value reported by the administrator or fund manager of such fund on the Valuation Date or, if not available, the most recent provisional net asset value reported by the administrator or fund manager;
- (vi) the value of all other property of the Trust, and any property for which a third party valuation is not available, is the value as the Manager determines in its reasonable discretion most accurately reflects its fair value; and
- (vii) the value of any asset of the Trust measured in a foreign currency is valued at the rate of exchange current on the Valuation Date as determined by the Manager.

Some hedge funds in which the Trust is invested provide a weekly value, the balance provide a monthly value. Hedge fund managers conventionally communicate the net asset value per share within 10 business days after the month end. The Trust does not invest in hedge funds that will not commit to these terms.

The process of valuing investments for which no published market exists is based on inherent uncertainties and the resulting values may differ from values that would have been used had a ready market existed for the investments and may differ from the prices at which the investments may be sold.

In valuing the liabilities of the Trust, the following are included: bills, amounts owing under the loan facility, accounts payable, fees and administrative expenses payable, contractual obligations for the payment of money or property, allowances for tax or contingencies and all other liabilities of the Trust of any kind and nature. The value of the liabilities of the Trust is determined as follows:

- (i) the value of all liabilities and contractual obligations is the value determined by the Manager to most accurately reflect fair value; and
- (ii) liabilities and contractual obligations payable in a foreign currency are valued at the rate of exchange current on the Valuation Date as determined by the Manager.

The value of any security or property to which, in the opinion of the Manager, the above principles cannot be applied (whether because no price or yield equivalent quotations are available as above provided, or for any other reason) shall be the fair value thereof determined in good faith in such manner as the Manager from time to time adopts.

The Net Asset Value per Unit is the amount obtained by dividing the Net Asset Value as of a particular date by the total number of Units outstanding on that date. The Trust makes available to the financial press for publication in the next available weekend edition of a national newspaper the Net Asset Value per Unit as of the last business day of the previous month on the 15<sup>th</sup> business day of the month. At any time, a Unitholder may call 1-888-429-8774 or e-mail at [mpt@northwatercapital.com](mailto:mpt@northwatercapital.com) to obtain the most recently published Net Asset Value per Unit.

### **PURCHASES OF UNITS:**

The Units are listed and posted for trading on the Toronto Stock Exchange under the symbol NMN.UN.

**RESPONSIBILITY FOR FUND OPERATIONS:****The Manager**

Pursuant to the Management Agreement, Northwater Fund Management Inc. (the "Manager") has exclusive authority to manage the operations and affairs of the Trust, to make all decisions regarding the business of the Trust and has authority to contract on behalf of the Trust. The Manager may, pursuant to the terms of the Trust Agreement, delegate its powers to third parties at no additional cost to the Trust where, in the discretion of the Manager, it would be in the best interests of the Trust to do so. The Manager is required to exercise its powers and discharge its duties honestly, in good faith and in the best interests of the Trust and to exercise the care, diligence and skill of a prudent and qualified manager. Among other restrictions imposed on the Manager, it may not dissolve the Trust or wind up the Trust's affairs except in accordance with the provisions of the Trust Agreement.

The Manager's duties include, without limitation: maintaining accounting records for the Trust; authorizing the payment of operating expenses incurred on behalf of the Trust; calculating the amount of distributions by the Trust; preparing financial statements, income tax returns and financial and accounting information as required by the Trust; ensuring that the Unitholders are provided with financial statements and other reports as required from time to time by applicable law; ensuring that the Trust complies with regulatory requirements; preparing the Trust's reports to Unitholders and to the Canadian securities regulatory authorities; providing the Trustee with certain information and reports; 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 that are not furnished by the Trust's custodian or transfer agent.

The Management Agreement entitles the Manager, in payment for the services noted above, to receive a monthly management fee equal to one twelfth of 1.25% of the Net Asset Value of the Trust at month end calculated and paid monthly in arrears; The Manager is entitled to be reimbursed for all expenses and liabilities properly incurred by it in connection with the activities of the Trust.

The Management Agreement, unless terminated as described below, will continue in effect until the termination of the Trust. The Trust may terminate the Management Agreement: (i) in the event that the Manager is in breach or default of the provisions thereof and, if capable of being cured, such breach or default has not been cured within 20 business days' notice of such breach or default to the Manager, (ii) if the Manager becomes bankrupt or insolvent, (iii) if any of the licenses or registrations necessary for the Investment Advisor to perform its duties under the Investment Management Agreement are no longer in full force and effect, or (iv) at any time upon six months' prior written notice following the approval of the Unitholders of such termination by Extraordinary Resolution.

In the event of the termination of the Management Agreement by the Trust as described in (iv) above, the Manager will be entitled to a termination payment in an amount equal to the annual fees, paid or payable to the Manager in the most recently completed 12-month period.

The Manager is currently also manager of two other closed-end investment trusts, Northwater Five-Year Market-Neutral Trust and Northwater Top 75 Income Trusts <sup>Plus</sup>.

### **The Investment Advisor**

Northwater Capital Management Inc. (the "Investment Advisor"), an affiliate of the Manager, has been retained by the Manager to provide investment advisory and portfolio management services to the Manager for the benefit of the Trust pursuant to an investment management agreement (the "Investment Management Agreement") dated as of July 18, 1997 and amended November 28, 1997 and further amended April 19, 2004.

The Investment Advisor, a leader in financial innovation since January 1989, offers customized portfolio solutions to the global investment community by providing stable, diversified alpha and precise, low-cost market exposure.

Utilizing its expertise in constructing market-neutral portfolios that seek to generate consistent returns in both normal and extreme markets, the Investment Advisor delivers a source of alpha that can be tailored to meet an investor's active risk budget. In addition, the firm's established indexing capability allows access to the global equity and fixed income markets to complement an investor's unique asset/liability profile. The Investment Advisor's structuring technology then combines these two components in a portable alpha framework that seeks to achieve an investor's return/risk objectives in an efficient, cost-effective manner.

With over a ten year track record in fund of hedge funds, the Investment Advisor has steadily grown assets under management to approximately CDN \$14.1 billion total, including USD \$4.8 billion invested in hedge funds as at December 31, 2007. The Investment Advisor has focused on developing, delivering and continuously improving its market-neutral fund of hedge fund portfolios since launching its first such portfolio in 1994.

The Investment Advisor advises institutional clients in Canada, the United States, the United Kingdom and other parts of Europe and Australia. The firm has offices in Toronto, New York and Chicago.

The Investment Advisor is engaged in a wide range of investment management, investment advisory and other business activities. The services of the Investment Advisor under the Investment Management Agreement are not exclusive and nothing in the Investment Management Agreement prevents the Investment Advisor or any of its affiliates from providing similar services to other investment funds and other clients (whether or not their investment objectives, strategies and restrictions are similar to those of the Trust) or from engaging in other activities. The Investment Advisor's investment decisions for the Trust will be made independently of those made for its other clients and independently of its own

investments. However, the Investment Advisor may make the same investment for the Trust and for one or more of its other clients. If the Trust and one or more of the other clients of the Investment Advisor is engaged in the purchase or sale of the same security, the Investment Advisor will seek to effect the transactions on an equitable basis.

The Investment Management Agreement, unless terminated as described below, will continue until the termination of the Trust. The Manager in certain circumstances may, and the Manager upon the direction of the Unitholders authorized by an Extraordinary Resolution will, terminate the Investment Management Agreement upon six months' prior written notice. In the event of the termination of the Investment Management Agreement as a result of the passing of a resolution by the Unitholders as described above, no payments need be made by the Manager to the Investment Advisor or by the Investment Advisor to the Manager, except for amounts owing as of the date of termination. The Investment Advisor may terminate the Investment Management Agreement upon at least 20 business days' written notice given by the Investment Advisor to the Manager if the Manager is in breach or default of any material provision of the Investment Management Agreement and, if capable of being cured, the breach or default has not been cured within twenty business days of written notice of such breach or default given by the Investment Advisor to the Manager. In the event of such termination, no payments need be made by the Manager to the Investment Advisor or by the Investment Advisor to the Manager, except for amounts owing as of the date of termination.

In the Investment Management Agreement, the Investment Advisor covenants to act at all times on a basis that is fair and reasonable to the Manager, to act honestly and in good faith with a view to the best interests of the Manager and, in connection therewith, shall exercise the degree of care, diligence and skill that a reasonably prudent portfolio manager would exercise in comparable circumstances. The Investment Management Agreement provides that the Investment Advisor will not be liable in any way for any default, failure or defect in any of the securities comprising the investment portfolio of the Trust if it has exercised the degree of care, diligence and skill set forth above. The Investment Advisor will incur liability, however, in cases of willful misconduct, bad faith, gross negligence or disregard of its duties or the standard of care, diligence and skill set forth above.

In the event that the Investment Management Agreement is terminated as provided above, the Manager will appoint a successor investment Investment Advisor to carry out the activities of the Investment Advisor until a meeting of the Unitholders is held to confirm such appointment.

The Investment Advisor will receive a portion of the fee payable by the Trust to the Manager in consideration of the Investment Advisor's services to the Trust.

### **The Trustee**

RBC Dexia Investor Services Trust, as successor trustee of The Royal Trust Company, acts as Trustee. The address of the Trustee is P.O. Box 7500, Royal Trust Tower, Toronto, Ontario, M5W 1P9.

The Trustee or any successor trustee may resign upon 90 days written notice to Unitholders and to the Manager or may be removed with the approval of a majority of the votes cast at a

meeting of Unitholders called for such purpose with two or more persons present in person or by proxy representing not less than 10% of the Units then outstanding. Any such resignation or removal shall become effective only on the appointment of a successor trustee. If, after the resignation of the Trustee, no successor has been appointed within 90 days, the Trustee, the Manager or any Unitholder may apply to a court of competent jurisdiction for the appointment of a successor trustee.

The Trust Agreement provides that the Trustee will not be liable in carrying out its duties under the Trust Agreement except in cases of willful misconduct, bad faith, negligence or disregard of its obligations and duties that are not delegated to the Manager under the Trust Agreement or in cases where the Trustee fails to act honestly and in good faith with a view to the best interests of the Unitholders 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 in respect of certain liabilities incurred by it in carrying out its duties.

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

### **Custodian**

The Canada Trust Company ("Canada Trust") was appointed as custodian of the securities comprising the investment portfolio of the Trust pursuant to an agreement made as of July 18, 1997. Since its appointment as custodian, Canada Trust sold its pension and institutional trust business to CIBC Mellon Trust Company. CIBC Mellon acted as custodian to the Trust as a result of this transaction from March 1, 1999 to August 17, 1999. On August 17, 1999 The Royal Trust Company was appointed custodian to the Trust.

### **Registrar and Transfer Agent**

CIBC Mellon Trust Company acts as transfer agent and registrar for the Trust at 320 University Avenue, 5th Floor Toronto, Ontario, M5H 4A6. In addition to performing registrar and transfer agency services, CIBC Mellon Trust Company provides certain record-keeping, Unitholder reporting and general administrative services pursuant to the registrar and transfer agency agreement made as of July 18, 1997.

### **Auditors**

The auditors of the Trust are PricewaterhouseCoopers LLP, Suite 3000, Box 82, Royal Trust Tower, Toronto Dominion Centre, Toronto, Ontario, M5K 1E6.

## 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 as follows:

<u>Name and Municipality</u>	<u>Position with the Manager</u>	<u>Principal Occupation</u>
DAVID G. PATTERSON, MBA Toronto, Ontario	Chairman, Chief Executive Officer and Director	Chairman and Chief Executive Officer, Northwater Capital Management Inc.
BENITA M. WARMBOLD, CA Scarborough, Ontario	Managing Director, Chief Financial Officer and Director	Managing Director and Chief Financial Officer, Northwater Capital Management Inc.
DANIEL C.R. MILLS, CFA Mississauga, Ontario	Managing Director, Chief Investment Officer and Director	Managing Director and Chief Investment Officer, Northwater Capital Management Inc.
JAMES D. SINCLAIR, LL.B. Unionville, Ontario	Vice-President, Secretary and Director	Vice-President and Chief Legal Officer, Northwater Capital Management Inc.
DAVID S. FINCH, CFA Toronto, Ontario	Vice-President and Director	Managing Director, Northwater Capital Management Inc.
EVE N. JEDRZEJEWSKA, CA, C.F.A. Toronto, Ontario	Vice-President	Vice-President, Northwater Capital Management Inc.
SHAUNA L. CASSIDY, CFA Toronto, Ontario	Vice-President	Vice-President, Northwater Capital Management Inc.
JIENAN WANG, CFA Toronto, Ontario	Vice-President	Vice-President, Northwater Capital Management Inc.

All of the directors and officers of the Manager have held their current offices or other executive offices with the above companies or their affiliates for at least five years.

## Officers and Directors of the Investment Advisor

The name, municipality of residence, position with the Investment Advisor and principal occupation of each of the directors and officers of the Investment Advisor are as follows:

<b><u>Name and Municipality</u></b>	<b><u>Position with the Investment Advisor</u></b>	<b><u>Principal Occupation</u></b>
DAVID G. PATTERSON, MBA Toronto, Ontario	Chairman, Chief Executive Officer and Director	Chairman and Chief Executive Officer
PAUL W. ROBSON, MBA, CFA. Mississauga, Ontario	Managing Director, President	Managing Director, President
BENITA M. WARMBOLD, CA Scarborough, Ontario	Managing Director, Chief Financial Officer and Director	Managing Director and Chief Financial Officer
DANIEL C.R. MILLS, CFA. Mississauga, Ontario	Managing Director and Chief Investment Officer	Managing Director and Chief Investment Officer
DAVID S. FINCH, CFA Toronto, Ontario	Managing Director	Managing Director
DENNIS G. COOK, C.M.C., C.H.R.P. Toronto, Ontario	Executive Vice-President	Executive Vice-President
JAMES D. SINCLAIR, LL.B. Unionville, Ontario	Vice-President, Chief Legal Officer and Chief Compliance Officer	Vice-President, Chief Legal Officer and Chief Compliance Officer
HEATHER L. BROUGHTON, MBA, CFA Toronto, Ontario	Vice-President	Vice-President
SHAUNA L. CASSIDY, CFA Toronto, Ontario	Vice-President	Vice-President
JOANNA CHRZANOWSKI, CA Mississauga, Ontario	Vice-President	Vice-President
A. MICHAEL DERZKO New York, New York	Vice-President	Vice-President
STEPHEN M. FOOTE, CFA OAKVILLE, Ontario	Vice-President	Vice-President
R. ANDREW HARRISON New York, New York	Vice-President	Vice-President
SCOTT C. HENSHAW, MEC., MBA, CFA Toronto, Ontario	Vice-President	Vice-President

<b><u>Name and Municipality</u></b>	<b><u>Position with the Investment Advisor</u></b>	<b><u>Principal Occupation</u></b>
CRAIG H. HIPPERN, CA, C.P.A. Mississauga, Ontario	Vice-President	Vice-President
ADRIAN HUSSEY, MBA, CFA Toronto, Ontario	Vice-President	Vice-President
EVE N. JEDRZEJEWSKA, CA, CFA Toronto, Ontario	Vice-President	Vice-President
MOHAMED S. KHAKI, A.S.A., CFA Toronto, Ontario	Vice-President	Vice-President
FRANCES KORDYBACK, CA Toronto, Ontario	Vice-President	Vice-President
ROBERT J. KULPERGER, J.D., Darrien, Connecticut	Vice-President	Vice-President
DANIEL S. LAWEE, MBA, CFA Toronto, Ontario	Vice-President	Vice-President
HOWARD M.H. LEE, M.Sc. Toronto, Ontario	Vice-President	Vice-President
IRENE C. MARKUS, LL.B. Toronto, Ontario	Vice-President	Vice-President
DAVID MARLEAU, F.S.A., F.C.I.A. Toronto, Ontario	Vice-President	Vice-President
SUSAN L. NAYLOR, CA Burlington, Ontario	Vice-President	Vice-President
HARRY R.L. PATTERSON, CFA Toronto, Ontario	Vice-President	Vice-President
JONATHAN PIURKO, LL.B Toronto, Ontario	Vice-President	Vice-President

<b><u>Name and Municipality</u></b>	<b><u>Position with the Investment Advisor</u></b>	<b><u>Principal Occupation</u></b>
NEIL SIMONS, PH.D, MMF Unionville, Ontario	Vice-President	Vice-President
MARK STEFFLER, CA Toronto, Ontario	Vice-President	Vice-President
JHENAN J. WANG, M.A., CFA Toronto, Ontario	Vice-President	Vice-President
KAI WANG, MBA, CFA Toronto, Ontario	Vice-President	Vice-President
XIANG ZHANG, MMF, CFA Toronto, Ontario	Vice-President	Vice-President

All of the directors and officers of the Investment Advisor have held their current offices or other executive offices with the above companies or their affiliates for at least five years except for: Ms. Chrzanowski who between July 2002 and January 2005 was Senior Financial Consultant with The Canada Life Assurance Company, and prior July 2005 was Associate with the Investment Advisor; Mr. Cook who between March 2002 and June 2003 was Vice President with the Investment Advisor, and prior to February 2002 was Director, Deloitte & Touche LLP; Mr. Derzko who prior to February 2004 was Associate with the Investment Advisor; Mr. Finch who prior to May 2002 was Vice President, ING Investment Management Inc.; Mr. Foote who prior to March 2005 was Senior Consultant, Mercer Investment Consulting; Mr. Harrison who prior to February 2006 was Associate with Celtic House Venture Partners; Mr. Henshaw who between October 2003 and February 2004 was Associate with the Investment Advisor, and prior to October 2003 was Associate Director, UBS Securities Canada Inc.; Mr. Khaki who prior to June 2003 was Senior Consultant, Frank Russell Canada Limited; Ms. Kordyback who between January 2003 and December 2004 was Managing Director, CCFL Parklea Capital Inc., and prior to December 2002 was Partner, Plaxton & Co. Limited; Mr. Kulperger who prior to October 2006 was Director, Credit Suisse; Mr. Lawee who between August 2002 and February 2004 was Associate with the Investment Advisor, and prior to August 2002 was Vice President, Foreign Exchange, TD Securities; Ms. Markus who between August 2000 and July 2004 was Vice-President, J.P. Morgan Securities Inc.; Mr. Marleau who prior to July 2003 was Assistant Portfolio Manager, ING Investment Management, Inc.; Mr. H. Patterson who between January 2001 and February 2004 was Associate with the Investment Advisor, and prior to January 2001 was Business Analyst, Geophysical Applications; Mr. Piurko who between September 2004 and July 2005 was Associate with the Investment Advisor and prior to September 2004 was an Associate at Blake, Cassels & Graydon LLP; Mr. Simons who prior to Prior to 2006, Mr. Simons was Senior Manager, Enterprise Market Risk Reporting and Analysis; Mr. Steffler who prior to September 2006 was Senior Manager, Finance, Royal and Sun Alliance between March 2004 and September 2006 and prior to March 2004 was as Senior Consultant, Treasury for Canada Life; and prior to March 2003, Assistant Controller, First Capital Realty Inc.; and Mr. Zhang who between August 2003 and July 2005 was Associate with the Investment Advisor, and prior to

August 2003 was Senior Investment Analyst and Assistant Portfolio Manager at MFC Global Investment Management Corporation.

**POTENTIAL CONFLICTS OF INTEREST:**

The Manager, the Investment Advisor, their respective directors and officers and their respective affiliates and associates may engage in the promotion, management or investment management of, or may render advice to, any other account, fund, corporation, partnership or trust that invests primarily in funds of market-neutral hedge fund securities. The Investment Advisor may have a conflict of interest in rendering advice to the Trust because the benefit the Investment Advisor and its principals may receive from managing some other accounts may exceed the benefit from managing the Trust's account, and, therefore, may provide an incentive to favour such other accounts.

Although none of the directors or officers of the Manager or the Investment Advisor will devote his or her full time to the business and affairs of the Trust or the Manager, each will devote as much time as is necessary to supervise the management of (in the case of the directors) or to manage (in the case of officers) the business and affairs of the Manager and the Trust. Although officers, directors, members and professional staff of the Investment Advisor will devote as much time to the Trust as the Investment Advisor deems appropriate to perform its duties in accordance with the Investment Advisory Agreement, the staff of the Investment Advisor may have conflicts in allocating its time and services among the Hedge Fund Portfolio and the other portfolios of the Investment Advisor.

Neither the Investment Advisor nor any of its affiliates is under any obligation to offer investment opportunities of which they become aware to the Trust or to inform the Trust of any investment before offering any investments to other funds or accounts that the Investment Advisor and/or its affiliates manage or advise. Furthermore, the Investment Advisor and/or its affiliates may make an investment on their own behalf or on behalf of any account that they manage or advise without offering the investment opportunity or making any investment on behalf of the Trust.

In addition, the Investment Advisor and/or its affiliates, in connection with their other business activities, may acquire material non-public confidential information that may restrict the Investment Advisor from purchasing assets or selling assets for itself or its clients (including the Trust) or otherwise using such information for the benefit of its clients or itself. As a result of investments for other clients, the Investment Advisor may be unable for legal, regulatory or other reasons to effect a particular transaction on behalf of the Trust that it would otherwise effect.

**FUND GOVERNANCE:**

In accordance with the terms of National Instrument 81-107 Independent Review Committee for Investment Funds, the Trust was required, not later than November 1, 2007, to appoint an independent review committee to review any conflict of interest matters referred to the Independent Review Committee by the Manager. The independent review committee (“IRC”) was officially appointed as of November 1, 2007 and the initial members of the IRC are: Jeffrey D. Francoz (Chair), Ann Marshall and Peter Vesely. All members of the IRC are independent of the Manager, the Investment Advisor and the Trust.

For the period prior to November 1, 2007, the advisory board appointed (the “Trust Advisory Board”) by the Manager consisted of two members (Jeffrey D. Francoz and Ann Marshall). Both members of the Trust Advisory Board are independent of the Manager, the Investment Advisor and the Trust.

The Trust Advisory Board provided independent advice to the Manager in connection with its role as manager of the Trust, including with respect to conflicts of interest, potential conflicts of interest and related party transactions identified by the Manager. In addition, the Trust Advisory Board received and reviewed periodic reports about the investment of the Trust’s assets. The Manager reported to the Trust Advisory Board on a quarterly basis, including with respect to compliance with the investment guidelines and restrictions of the Trust.

Upon the formation and inception of the IRC, the primary task assigned to the IRC under National Instrument 81-107 is to review and report on conflict of interest matters as such term is defined in the Instrument. The IRC’s mandate will continue to include all of the functions and responsibilities of the Trust Advisory Board as well as incorporating all of the requirements of National Instrument 81-107.

Members of the Trust Advisory Board and, going forward, the IRC, will act honestly and in good faith in the best interests of the Trust and the Unitholders and in connection with that duty will exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.

**FEES AND OTHER EXPENSES:**

The Manager is responsible for the ongoing business of the Trust and monitoring the investment portfolio of the Trust. In consideration for these and other services and pursuant to the terms of the Trust Agreement and the Management Agreement, the Trust will pay to the Manager a monthly management fee equal to one-twelfth of 1.25% of the Net Asset Value at month end, paid monthly in arrears, plus applicable taxes. The Manager pays a portion of the foregoing fee to the Investment Advisor in consideration of the Investment Advisor’s services to the Trust.

The Trust pays for all expenses incurred in connection with the operation and administration of the Trust. These expenses include, without limitation: mailing and printing expenses for periodic reports to Unitholders; fees payable to the Trustee for acting as trustee of the Trust; fees payable to the Custodian (as hereinafter defined) for acting as custodian of the assets of the Trust; fees payable to the registrar and transfer agent for performing certain financial, record-keeping, Unitholder reporting and general administrative services; fees payable to the auditors, valuers, and legal advisors of the Trust; debt service fees (including set-up and commitment fees); ongoing regulatory filing fees and listing and other fees; any reasonable out-of-pocket expenses incurred by the Manager or its agents in connection with their ongoing obligations to the Trust; and any expenditures that may be incurred upon the termination of the Trust.

The Trustee will be entitled to receive an annual fee equal to 0.015% of the Net Asset Value calculated and paid quarterly in arrears.

### **INCOME TAX CONSIDERATIONS:**

This summary is applicable to a Unitholder who is an individual (other than a trust) and who, for the purposes of the *Income Tax Act* (Canada) (the "Tax Act") is resident in Canada, deals at arm's length with and is not affiliated with the Trust and holds Units as capital property. Generally, Units will be considered to be capital property to a holder provided that the holder does not hold the Units in the course of carrying on a business of buying and selling securities and has not acquired them in one or more transactions considered to be an adventure in the nature of trade. Certain persons who might not otherwise be considered to hold their Units as capital property may, in certain circumstances, be entitled to have them treated as capital property by making the election permitted by subsection 39(4) of the Tax Act.

The Trust currently qualifies as a "mutual fund trust" under the Tax Act. Investors are encouraged to refer to the disclosure under the heading "Canadian Federal Income Tax Considerations" in the Trust's prospectus for a more complete discussion of tax considerations.

There can be no assurance that Canadian federal income tax laws respecting the treatment of mutual fund trusts will not be changed in a manner that adversely affects the Unitholders. If the Trust ceases to qualify as a "mutual fund trust" under the Tax Act, the income tax considerations may be materially and adversely different in certain respects.

### **MATERIAL CONTRACTS:**

Material contracts that have been entered into by the Trust since its formation, other than contracts entered into in the ordinary course of business, are as follows:

1. The Trust Agreement between the Trustee and the Manager referred to under "Management of the Trust";

2. The Management Agreement between the Manager on behalf of the Trust and the Manager referred to under "Management of the Trust - the Manager";
3. The custody agreement (the "Custody Agreement") made among the Manager on behalf of the Trust, the Manager and The Royal Trust Company (the "Custodian") referred to under "Trustee and Custodian";
4. The registrar and transfer agency agreement among the Manager on behalf of the Trust, and CIBC Mellon Trust Company referred to under "Registrar and Transfer Agent"; and
5. The Loan Agreement among the Manager on behalf of the Trust and the Bank referred to under "Loan Facility".

**LEGAL AND ADMINISTRATIVE PROCEEDINGS:**

Neither the Manager nor the Investment Advisor are aware of any legal or administrative proceedings involving the Trust.

**OTHER MATERIAL INFORMATION:**

The following summary of financial information has been derived from the financial statements of the Trust. This information should be read in conjunction with the Financial Statements specifically incorporated herein by reference. There have been no changes in accounting policies and no changes in the investment strategy of the Trust. The Trust commenced operations on July 30, 1997.

Distribution History:

<b>YEAR</b>	<b>TYPE</b>	<b>PER UNIT</b>	<b>TOTAL</b>
2007	Return of capital	\$ 0.81181	\$ 5,386,622
	Other income	<u>1.18819</u>	<u>7,883,975</u>
		\$ 2.00000	\$ 13,270,597
2006	Return of capital	\$ 1.10	\$ 5,393,646
	Other income	<u>0.04</u>	<u>198,716</u>
		\$1.14	\$ 5,592,362
2005	Return of capital	\$0.80052	\$ 4,186,458
	Other income	<u>0.35948</u>	<u>1,880,049</u>
		\$1.16000	\$6,066,507
2004	Return of capital	\$ 0.00592	\$ 31,011
	Other income	<u>1.84054</u>	<u>9,648,774</u>
		\$ 1.84646	\$ 9,676,785
2003	Return of capital	\$ 0.04317	\$ 226,142
	Other income	4.21072	22,053,863
	Realized gain	<u>0.82611</u>	<u>4,326,795</u>
		\$5.08000	\$26,606,800

2002	Return of capital	\$1.08	\$5,909,697
2001	Return of capital	\$2.17	\$12,475,419
2000	Return of capital	\$2.89	\$17,757,559
1999	Return of capital	\$0.57	\$3,663,823
1998	Return of capital	\$0.69	\$5,909,858
1997	Not applicable	Nil	Nil

**For a full discussion of the Trust's distribution policy, please see page 4.**

(All figures in Canadian dollars)	<u>For the year ended December 31, 2007</u>	<u>For the six-month period ended June 30, 2007</u>	<u>For the year ended December 31, 2006</u>	<u>For the six-month period ended June 30, 2006</u>
Total income	249,623	99,333	252,333	156,933
Net income (loss) from operations	2,099,086	4,328,248	6,495,505	3,332,840
Net income (loss) per unit *	0.45	0.91	1.32	0.66
Total assets	80,635,456	85,777,830	85,856,477	87,795,003
Bank loan	12,578,644	14,851,075	16,289,420	16,173,949
Net assets and unitholders' equity	53,777,617	69,019,328	67,650,955	69,353,324

\* based on average number of Units outstanding for the period

(All figures in Canadian dollars)	For the year ended	For the quarter ended		
	<u>December 31, 2005</u>	<u>September 30, 2005</u>	<u>June 30, 2005</u>	<u>March 31, 2005</u>
Total income	201,021	52,135	24,525	44,469
Net income (loss) from operations	1,530,794	509,576	(312,070)	699,880
Net income (loss) per unit *	0.29	0.10	(0.06)	0.13
Total assets	89,016,701	91,094,700	93,212,261	94,569,354
Bank loan	15,660,346	15,656,492	16,533,967	16,306,879
Net assets and unitholders' equity	71,507,578	73,675,156	74,689,564	76,525,618

\* based on average number of Units outstanding for the period

(All figures in Canadian dollars)	For the year ended	For the quarter ended		
	<u>December 31, 2004</u>	<u>September 30, 2004</u>	<u>June 30, 2004</u>	<u>March 31, 2004</u>
Total income	149,523	30,634	26,039	42,953
Net income (loss) from operations	4,029,286	50,586	(47,108)	2,364,469
Net income (loss) per unit *	0.77	0.01	(0.01)	0.45
Total assets	98,317,028	99,183,137	101,736,588	103,076,594
Bank loan	16,192,417	17,033,524	18,064,648	17,659,069
Net assets and unitholders' equity	77,232,421	80,262,974	81,837,344	85,190,909

\* based on average number of Units outstanding for the period

(All figures in Canadian dollars)	For the year ended	For the quarter ended		
	<u>December 31, 2003</u>	<u>September 30, 2003</u>	<u>June 30, 2003</u>	<u>March 31, 2003</u>
Total income	115,487	17,598	30,919	48,296
Net income from operations	9,420,485	966,906	3,877,018	2,485,108
Net income per unit *	1.80	0.18	0.74	0.47
Total assets	121,323,496	121,634,550	123,989,597	126,019,043
Bank loan	19,225,073	21,412,039	21,517,747	23,489,409
Net assets and unitholders' equity	82,788,506	99,918,895	99,161,491	98,531,760

\* based on average number of Units outstanding for the period

(All figures in Canadian dollars)	For the year ended	For the quarter ended		
	<u>December 31, 2002</u>	<u>September 30, 2002</u>	<u>June 30, 2002</u>	<u>March 31, 2002</u>
Total income	192,052	48,097	55,663	40,083
Net income from operations	7,993,620	276,921	1,282,671	2,400,940
Net income per unit *	1.45	0.05	0.23	0.42
Total assets	129,555,734	127,962,810	132,727,842	135,113,967
Bank loan	25,254,941	25,354,035	25,799,831	27,069,220
Net assets and unitholders' equity	101,834,209	102,103,773	104,192,349	107,577,815

\* based on average number of Units outstanding for the period

(All figures in Canadian dollars)	For the year ended	For the quarter ended		
	<u>December 31, 2001</u>	<u>September 30, 2001</u>	<u>June 30, 2001</u>	<u>March 31, 2001</u>
Total income	281,679	30,707	130,945	84,556
Net income from operations	10,841,484	3,298,413	2,249,793	6,940,328
Net income per unit *	1.89	0.58	0.39	1.20
Total assets	132,907,382	140,214,910	138,975,513	149,970,603
Bank loan	27,055,187	30,345,340	26,859,775	33,660,325
Net assets and unitholders' equity	105,773,541	107,425,839	107,206,533	110,826,845

\* based on average number of Units outstanding for the period

(All figures in Canadian dollars)	For the year ended	For the quarter ended		
	<u>December 31, 2000</u>	<u>September 30, 2000</u>	<u>June 30, 2000</u>	<u>March 31, 2000</u>
Total income	812,441	129,478	307,627	295,956
Net income from operations	14,955,071	3,992,978	3,791,506	6,290,890
Net income per unit *	2.45	0.66	0.62	1.00
Total assets	142,728,561	149,217,522	156,462,961	156,152,032
Bank loan	29,511,017	30,548,932	34,425,772	30,001,072
Net assets and unitholders' equity	111,140,383	114,137,600	116,450,964	119,961,941

\* based on average number of Units outstanding for the period

(All figures in Canadian dollars)	For the year ended	For the quarter ended		
	<u>December 31, 1999</u>	<u>September 30, 1999</u>	<u>June 30, 1999</u>	<u>March 31, 1999</u>
Total income	2,185,438	496,220	629,543	487,732
Net income from operations	16,260,295	2,292,592	5,860,975	4,430,671
Net income per unit *	2.42	0.35	0.87	0.62
Total assets	155,145,153	156,666,680	155,690,082	153,968,419
Bank loan	29,300,058	32,497,832	31,057,978	31,968,349
Net assets and unitholders' equity	121,925,046	124,048,356	124,432,871	121,851,048

\* based on average number of Units outstanding for the period

(All figures in Canadian dollars)	For the year ended	For the quarter ended		
	<u>December 31, 1998</u>	<u>September 30, 1998</u>	<u>June 30, 1998</u>	<u>March 31, 1998</u>
Total income	3,188,333	633,563	1,076,842	631,380
Net income from operations	(17,264,732)	(21,544,848)	(1,717,077)	4,037,377
Net income per unit *	(2.11)	(2.67)	(0.20)	0.46
Total assets	153,254,621	171,511,456	201,582,198	215,682,917
Bank loan	30,129,151	44,024,705	41,582,287	44,945,326
Net assets and unitholders' equity	123,031,606	126,169,715	156,513,387	167,517,044

\* based on average number of Units outstanding for the period

(All figures in Canadian dollars)	For the Period from July 30, 1997 (date of commencement of operation) to	
	<u>December 31, 1997</u>	<u>September 30, 1997</u>
Total income	380,635	79,089
Net income from operations	1,853,576	2,657,233
Net income per unit*	0.21	0.30
Total assets	206,023,611	195,293,312
Bank loan	39,002,517	27,292,815
Net assets and unitholders' equity	166,674,246	167,495,233

\* based on average number of Units outstanding for the period

The monthly Net Asset Value per Unit for the Trust was as follows:

Net Asset Value Per Unit (since inception)

(in Canadian dollars)

	Jan. 31 <sup>st</sup>	Feb. 28 <sup>th</sup>	Mar. 31 <sup>st</sup>	Apr. 30 <sup>th</sup>	May 31 <sup>st</sup>	June 30 <sup>th</sup>	July 31 <sup>st</sup>	Aug. 31 <sup>st</sup>	Sept. 30 <sup>th</sup>	Oct. 31 <sup>st</sup>	Nov. 30 <sup>th</sup>	Dec. 31 <sup>st</sup>
2007	14.33	14.49	14.36	14.49	14.68	14.46	14.35	13.88	13.63	13.89	13.77	11.76
2006	14.10	14.20	14.09	14.26	14.27	14.02	14.08	14.20	13.85	14.05	14.22	14.15
2005	14.75	14.87	14.56	14.48	14.39	14.21	14.34	14.35	14.02	13.96	14.03	13.88
2004	16.11	16.27	16.26	16.15	15.63	15.61	15.51	15.60	15.31	15.37	15.48	14.73
2003	19.50	19.54	18.81	19.12	19.41	18.93	18.80	18.83	19.08	19.24	19.41	15.81
2002	18.88	18.86	18.95	19.12	19.27	18.72	18.66	18.87	18.72	18.99	19.24	19.05
2001	19.38	19.71	19.14	19.35	19.63	18.70	18.89	19.20	18.88	18.94	18.55	18.59
2000	19.35	19.76	19.08	19.42	19.67	18.90	19.30	19.52	18.91	19.15	19.10	18.81
1999	17.07	17.15	17.45	17.99	18.29	18.46	18.76	18.73	18.88	19.09	19.36	18.97
1998	18.98	19.11	19.15	19.33	19.16	18.62	18.64	16.44	16.08	15.93	16.47	16.63
1997							18.79	18.78	19.09	18.64	18.71	19.00

## **Risk Factors**

An investment in Units of the Trust involves certain risks. Investors should consider the risk factors as set out in the prospectus of the Trust before purchasing Units.

## **EXEMPTIONS AND APPROVALS:**

Pursuant to an order dated October 11, 2005 under the securities legislation of each of British Columbia, Alberta, Saskatchewan, Manitoba, Ontario, Quebec, New Brunswick, Nova Scotia, Newfoundland and Labrador, Yukon, Northwest Territories and Nunavut (collectively, the “Jurisdictions”), the local securities regulatory authority in each of the Jurisdictions granted an exemption to the Trust from certain provisions of National Instrument 81-106 Investment Fund Continuous Disclosure (“NI 81-106”).

Generally, the Trust has received exemptive relief from the following provisions of NI 81-106:

- (a) the requirement in paragraph 3.5(1)1 of NI 81-106 to include in the statement of investment portfolio for the Trust the name of the issuer of each portfolio asset; and
- (b) with respect to the preparation of both management reports of fund performance under Part 4 of NI 81-106 and quarterly portfolio disclosure under Part 6 of NI 81-106, both required to be prepared in accordance with Form 81-

106F1 or parts thereof (the Summary of Investment Portfolio), the requirement in Item 5(2)(b), Part B of Form 81-106F1 to disclose the names of the top 25 positions held by the Trust.

The relief requested has been granted subject to various conditions imposed by the regulators in the Jurisdictions. The Trust complies with the interim and annual disclosure requirements imposed on it by the regulators pursuant to the exemptive relief order granted to the Trust.

**ADDITIONAL INFORMATION:**

The Annual Report, including Management's Discussion and Analysis and the audited financial statements of the Northwater Market-Neutral Trust for the year ended December 31, 2007 and the notes thereto (collectively referred to as the "Financial Statements") are hereby incorporated by reference. Copies of the Annual Report, including the Financial Statements of the Trust, may be obtained upon request from the Secretary of the Manager, James D. Sinclair, at the offices of the Trust. In addition, you can get a copy of the Trust's financial statements, including a statement of portfolio transactions, at no cost by calling toll-free 1-800-422-1867. The financial statements and other information about the Trust, such as information circulars and material contracts, are also available at [www.sedar.com](http://www.sedar.com) and certain information is available on the Investment Advisor's Internet site at [www.northwatercapital.com](http://www.northwatercapital.com).