



# AVENIR DIVERSIFIED INCOME TRUST

## A Report to Unit Holders

April 13, 2004

### 2003 Financial Highlights

For the periods ended	Three months ended Dec 31		Year Ended Dec 31 <sup>1</sup>	
	2003	2002	2003	2002
<b>FINANCIAL</b>				
Gross Revenue	\$2,079,584	\$112,911	\$5,219,610	\$187,211
Net Revenue	\$1,730,350	\$112,911	\$4,455,418	\$187,211
Cash Flow From Operations <sup>2</sup>	\$853,418	\$174,780	\$2,362,525	(\$70,889)
Cash Flow Per Unit <sup>2</sup> - Basic	\$0.02	\$0.02	\$0.08	(\$0.01)
Distributions	\$725,892	---	\$1,853,871	---
Distributions Per Unit - Basic	\$0.018	---	\$0.045	---
Distribution Payout Ratio	---	---	78%	---
% of Distributions Taxed as Income	---	---	68%	---
Net Earnings (loss)	(\$116,403)	\$174,780	\$519,180	(\$70,889)
Net Earnings (loss) Per Basic Unit	(\$0.00)	\$0.02	\$0.02	(\$0.01)
Total Assets	\$21,301,243	\$2,028,316	\$21,301,243	\$2,028,316
Net Debt	\$4,241,206	---	\$4,241,206	---
Wtd. Avg. Common Shares Outstanding	41,503,282	8,000,000	27,621,558	7,342,468
Common Shares Outstanding at YE	41,503,282	8,000,000	41,503,282	8,000,000
<b>OPERATING</b>				
Production (6:1)				
Oil and NGL's – bbls per day	299	---	239	---
Gas – mcf per day	2,009	---	767	---
Total Boe per day	634	---	367	---
Average Pricing				
Oil & NGL (\$/Bbl) before hedging	\$33.95	---	\$36.19	---
Oil & NGL (\$/Bbl) after hedging	\$32.21	---	\$35.08	---
Natural Gas (\$/mcf)	\$5.34	---	\$5.97	---
Average Price Per Boe before hedging	\$33.55	---	\$36.35	---
Average Price Per Boe after hedging	\$32.73	---	\$35.62	---
Gross Reserves (Proved plus Probable 6:1)				
Natural Gas (Mmcf)	---	---	4375.5	---
Oil & NGL (Mbbbl)	---	---	730.0	---

<sup>1</sup> Trust was created January 16, 2003. 2002 comparatives are those of 928719 Alberta Ltd.

<sup>2</sup> Cash flow from operations and cash flow per unit are not recognized measures under Canadian generally accepted accounting principles (GAAP). Cash flow from operations is calculated by taking net earnings and adding back non-cash balances such as depletion and depreciation, site restoration and abandonment, gain on sale of investments, compensation expense and unsuccessful acquisition and re-organizational costs. Management believes that cash flow is a useful supplemental measure to analyze operating performance and provide an indication of the results generated by the Trust's principal business activities. Avenir Diversified Income Trust's method of calculating these measures may differ from other companies, and accordingly, they may not be comparable to measures used by other companies.

### Forward Looking Statements

Except for historical financial information contained herein, the matters discussed in this document may be considered forward-looking statements. Such statements include declarations regarding management's intent, belief or current expectations. Prospective investors are cautioned that any such forward-looking statements are not guarantees of future performance and involve a number of risks and uncertainties; actual results could differ materially from those indicated by such forward-looking statements. Among the important factors that could cause actual results to differ materially from those indicated by such forward-looking statements are: (i) that the information is of a preliminary nature and may be subject to further adjustment, (ii) the possible unavailability of financing, (iii) risks related to the exploration and development of oil and gas properties, (iv) the impact of price fluctuations and the demand and pricing for oil and natural gas, (v) the seasonal nature of the business, (vi) start-up risks, (vii) general operating risks, (viii) dependence on third parties, (ix) changes in government regulation, (x) the effects of competition, (xi) dependence on senior management, (xii) financial condition of real estate tenants and financial services counter arts, (xiii) impact of

*the Canadian economic conditions or the demand for real estate leasing opportunities, (xiv) fluctuations in currency exchange rates and interest rates.*

## **Financial Review**

2003 was a very successful first year for the Avenir Diversified Income Trust. From the Trust's inception in January 2003 to the year-ended December 31, 2003, the Trust delivered a 61% return to unit holders, including \$0.18 per unit capital appreciation and \$0.063 per unit in distributions paid. Distributions were increased twice for a total of 30% representing a 78% cash flow payout ratio for the year.

It was a year of growth. The market capitalization of the Trust grew from approximately \$4 million to \$24.0 million by the end of December 2003. The units outstanding increased through two private placement financings, one that closed in January and February 2003 at a price of \$0.40 per unit for proceeds of \$4.5 million and the second, which closed in September 2003 at a price of \$0.50 per unit for proceeds of \$8.0 million. In addition, two acquisitions were completed from the issuance of units through treasury, Outback Energy Ltd. and 728409 Alberta Ltd.

The Trust's strategy is to have three distinct business units: Oil and Gas, Financial Services, and Real Estate. The Trust combines the stability of cash flows from both real estate and financial services with a more volatile cash flow stream from oil and gas production. The Trust's first real estate assets were not purchased until March of 2004.

Cash flow from operations increased in the fourth quarter to \$853,418 or \$0.02 per unit up 70% over the third quarter. The increase in cash flow was due primarily to the natural gas acquisitions made in the late third and early fourth quarters. For the year ended December 31, 2003 the cash flow from operations totaled \$2,362,525 or \$0.08 per unit.

The Trust recorded a net loss of \$116,403 for the fourth quarter and earnings of \$519,180 or \$0.02 per unit for the year ended December 31, 2003. The fourth quarter earnings were reduced by \$119,868 as a result of the early adoption of the stock based compensation rules that come into effect January 1, 2004. In addition, higher year end audit, accounting legal and reserve evaluation costs associated with the Trust's first year of operation negatively impacted fourth quarter earnings and cash flow. The Trust distributed \$725,892 or \$0.018 per unit to unitholders in the fourth quarter and distributed \$1,853,871 for the year ended December 31, 2003. The year end distribution payout ratio of 78% was in line with the Trust's target ratio. Of the distributions paid, 68% of the amount was classified as taxable income and 32% was tax deferred (return of capital).

## **Operations Review**

Operationally, the Oil and Gas business unit had a busy year growing through acquisition and development with production increasing from 246 barrels of oil equivalent per day (boe/d) at the end of the first quarter to 634 boe/d at the end of the fourth quarter. Operating costs were reduced by 21% from \$9.51 per boe in the first quarter to \$7.48 per boe in the fourth quarter as the Trust targeted acquisitions with lower cost structures. The Trust drilled five wells in 2003: three oil wells, one gas well and a water disposal well and farmed out two oil wells in southeast Saskatchewan at no cost to the Trust. The financial services business unit grew from \$1.2 million in financial services contracts to \$3.2 million by the end of the year, which includes a \$2 million debenture in December 2003. The Trust recently announced its first real estate acquisition, which closed on March 31, 2004. With assets in all three business units, the diversification strategy of the Trust is taking form and the Trust is committed to continue growth in each segment.

## **Reserves Summary**

The Trust's oil and gas reserves as at December 31, 2003 were evaluated by McDaniel & Associates Ltd. McDaniel was appointed by the Board of Directors of Avenir in 2003 as the new independent reserves evaluators for all of Avenir's oil and gas properties. Their evaluation report is prepared in accordance with National Instrument ("NI") 51-101, the new standards of disclosure for oil and gas activities as mandated by the Canadian Securities Administrators for year-ends beginning with December 31, 2003.

NI 51-101 replaces the former National Policy 2-B ("NP 2-B") and requires a higher degree of confidence in the assignment of oil and gas reserves. Under NI 51-101, proved reserves are defined to have a 90%

probability that the actual reserves recovered will equal or exceed the assigned estimates compared to the previous definition of “reasonable certainty” as stipulated by NP 2-B. Also, under NI 51-101, probable reserves are defined to have a 50% probability that the actual reserves recovered will equal or exceed the assigned estimates compared to the previous definition of “likelihood of existence” in NP 2-B. Because of the more stringent requirements under NI 51-101, the industry has adopted the interpretation that the new proved plus probable (P-50) reserves represent the most “realistic” estimates of remaining recoverable reserves. The following reserves information also adopts the general industry practice of comparing the new P-50 reserves to the previous proved plus risk adjusted (50%) probable reserves, commonly referred to as “established reserves”, under NP 2-B.

Under McDaniel’s NI 51-101 evaluation, technical revisions caused proved plus probable reserves for Avenir’s light and medium crude oil, natural gas liquids and natural gas properties to increase by 12.5%, on a combined basis, compared to the prior year.

The following tables summarize certain information with regard to Avenir’s oil and gas reserves as evaluated by McDaniel as at December 31, 2003.

## Oil and Gas Reserves

### Forecast Prices and Costs As at December 31, 2003

	Light and Medium Crude Oil		Heavy Oil		Natural Gas Liquids	
	Gross <sup>(1)</sup>	Net <sup>(2)</sup>	Gross <sup>(1)</sup>	Net <sup>(2)</sup>	Gross <sup>(1)</sup>	Net <sup>(2)</sup>
	(Mbbbls)		(Mbbbls)		(Mbbbls)	
Proved						
Developed Producing	528.0	484.8	0.0	0.0	31.5	23.2
Developed Non-Producing	0.0	0.0	0.0	0.0	3.0	2.1
Undeveloped	0.0	0.0	0.0	0.0	0.0	0.0
Total Proved	528.0	484.8	0.0	0.0	34.5	25.3
Probable	159.2	141.1	0.0	0.0	8.3	6.1
Total Proved Plus Probable	687.2	625.9	0.0	0.0	42.8	31.4

	Natural Gas		Oil Equivalent	
	Gross <sup>(1)</sup>	Net <sup>(2)</sup>	Gross <sup>(1)</sup>	Net <sup>(2)</sup>
	(Mmcf)		(MBoe)	
Proved				
Developed Producing	3410.8	2908.3	1128.0	992.7
Developed Non-Producing	74.4	59.0	15.4	12.0
Undeveloped	83.1	70.1	13.8	11.7
Total Proved	3568.3	3037.3	1157.3	1016.4
Probable	807.2	693.2	302.0	262.7
Total Proved Plus Probable	4375.5	3730.5	1459.3	1279.0

#### Notes:

(1) “Gross” reserves include working interest reserves only and are before royalty deductions. Gross reserves do not include 33.6 Mboes of royalty interest reserves.

(2) “Net” reserves include working interest after royalty deductions plus royalty interest reserves.

(3) Oil equivalent amounts have been calculated using a conversion rate of six thousand cubic feet of natural gas to one barrel of oil.

## Reserves Life Index

	Q4/2003	Reserves Life Index (RLI)	
	Production	Total Proved	Proved Plus Probable
Crude Oil (bbl/d)	299	5.7	7.7
Natural Gas (mcf/d)	2009	4.4	5.4
Oil Equivalent (boe/d)	634	5.0	6.4

Note: Reserve Life index is calculated by dividing the Company interest reserve the estimated annual production of the corresponding product category.

## Net Present Value of Reserves

It should not be assumed that the estimates of future net revenues presented in the tables below represent the fair market value of the reserves. There is no assurance that the constant prices and costs assumptions and forecast prices and costs assumptions will be attained and variances could be material.

### Summary of Net Present Value of Future Net Revenue As at December 31, 2003 Forecast Prices and Costs

	Before Income Taxes Discounted at (%/year)			
	0%	5%	10%	15%
	(\$mms)	(\$mms)	(\$mms)	(\$mms)
Proved Developed Producing	18.03	15.59	13.83	12.50
Developed Non-Producing	0.32	0.20	0.14	0.11
Undeveloped	0.16	0.15	0.14	0.13
Total Proved	18.51	15.94	14.11	12.74
Probable	4.95	3.48	2.63	2.08
Total Proved Plus Probable	23.46	19.41	16.74	14.82

## McDaniel January 1, 2004 Escalating Price Forecast

The escalating crude oil and natural gas pricing, inflation factors and the exchange rate utilized in the McDaniel Report are as follows:

Year	WTI Cushing US\$/Bbl	Edmonton Par Price C\$/Bbl	Hardisty Heavy 12 API C\$/Bbl	AECO C-Spot C\$/Mmbtu	Inflation Rate %/Yr	Exchange Rate \$/US/\$Cdn
2004	29.00	37.70	22.70	5.84	2.0	0.750
2005	26.50	34.30	21.55	5.50	2.0	0.750
2006	25.50	33.00	21.56	5.16	2.0	0.750
2007	25.00	32.30	20.63	4.97	2.0	0.750
2008	25.00	32.30	20.39	4.81	2.0	0.750
2009	25.50	32.90	20.76	4.85	2.0	0.750
2010	26.00	33.50	21.11	4.88	2.0	0.750

## McDaniel January 1, 2004 Constant Price Forecast

The constant crude oil and natural gas benchmark references pricing and the exchange rate utilized in the McDaniel Report are as follows:

Year	OIL				NATURAL GAS LIQUIDS		EXCHANGE RATE <sup>(1)</sup> (\$US/\$Cdn)
	WTI Cushing Oklahoma (\$US/bbl)	Edmonton Par Price 40° API (\$Cdn/bbl)	Hardisty Heavy 12° API (\$Cdn/bbl)	Cromer Medium 29.3° API (\$Cdn/bbl)	NATURAL GAS AECO Gas Price (\$Cdn/MMBtu)	FOB Field Gate (\$Cdn/BBL)	
Historical <sup>(2)</sup>							
2003	32.78	39.76	22.75	34.25	5.87	31.50	0.80

Notes:

- The exchange rate used to generate the benchmark reference prices in this table.
- As at December 31.

### Reserves Reconciliation Table AS AT DECEMBER 31, 2003 Constant Prices and Costs

	Light and Medium Crude		Heavy Crude	Total	Net	Net Natural	Oil Equiv.
	Net Crude Oil	Net Crude Oil	Net Crude Oil	Net Crude Oil	Net NGL's	Net Gas	Oil Equiv. 2003
	(Mbbbl)	(Mbbbl)	(Mbbbl)	(Mbbbl)	(Mbbbl)	MMcf	(Mbbbl)
<b>Proved Producing</b>							
Opening Balance: December 31, 2002 <sup>(1)</sup>	465.3	0.0	465.3	8.6	396.8	540.0	
Extensions	4.4	0.0	4.4	0.0	101.0	21.3	
Improved Recovery	0.0	0.0	0.0	0.0	0.0	0.0	
Technical Revisions	0.0	0.0	0.0	3.9	29.4	8.8	
Discoveries	0.0	0.0	0.0	0.0	0.0	0.0	
Acquisitions	111.3	0.0	111.3	14.9	2696.0	575.5	
Dispositions	-22.1	0.0	-22.1	-0.8	-100.4	-39.6	
Economic Factors	0.0	0.0	0.0	0.0	0.0	0.0	
Production	-68.9	0.0	-68.9	-3.4	-214.6	-108.1	
Closing Balance: December 31, 2003	490.0	0.0	490.0	23.2	2908.2	997.9	
<b>Total Proved</b>							
Opening Balance: December 31, 2002	465.3	0.0	465.3	8.6	396.8	540.0	
Extensions	4.4	0.0	4.4	0.0	101.0	21.3	
Improved Recovery	0.0	0.0	0.0	0.0	0.0	0.0	
Technical Revisions	0.0	0.0	0.0	3.8	30.1	8.8	
Discoveries	0.0	0.0	0.0	0.0	0.0	0.0	
Acquisitions	111.3	0.0	111.3	17.1	2941.0	618.6	
Dispositions	-22.1	0.0	-22.1	-0.8	-217.0	-59.0	
Economic Factors	0.0	0.0	0.0	0.0	0.0	0.0	
Production	-68.9	0.0	-68.9	-3.4	-214.6	-108.1	
Closing Balance: December 31, 2003	490.0	0.0	490.0	25.3	3037.3	1021.5	
<b>Proved Plus Probable</b>							
Opening Balance: December 31, 2002	528.3	0.0	528.3	9.4	439.4	610.8	
Extensions	6.6	0.0	6.6	0.0	109.5	24.8	
Improved Recovery	0.0	0.0	0.0	0.0	0.0	0.0	
Technical Revisions	56.9	0.0	56.9	4.5	174.8	90.5	
Discoveries	0.0	0.0	0.0	0.0	0.0	0.0	
Acquisitions	130.7	0.0	130.7	21.6	3445.0	726.5	
Dispositions	-22.1	0.0	-22.1	-0.7	-222.8	-59.8	
Economic Factors	0.0	0.0	0.0	0.0	0.0	0.0	
Production	-68.9	0.0	-68.9	-3.4	-214.6	-108.1	
Closing Balance: December 31, 2003	631.4	0.0	631.4	31.4	3731.3	1284.7	

Notes:

1. The evaluation as at December 31, 2002 was prepared using National Policy 2-B reserves definitions. Under those definitions, probable reserves were adjusted by a factor to account for the risk associated with their recovery. The Corporation previously applied a risk factor of 50% in reporting probable reserves. Under current NI 51-101 reserves definitions, estimates are prepared such that the full proved plus probable reserves are estimated to be recoverable (proved plus probable reserves are effectively a "best estimate"). The above reconciliation reflects current probable reserves versus previous risk adjusted (50%) probable reserves reported by the Corporation.

## A Discussion of Operational and Financial Results

MANAGEMENT'S DISCUSSION AND ANALYSIS should be read in conjunction with the audited annual consolidated financial statements for the year ended December 31, 2003.

Except for historical financial information contained herein, the matters discussed in this document may be considered forward-looking statements. Such statements include declarations regarding management's intent, belief or current expectations. Prospective investors are cautioned that any such forward-looking statements are not guarantees of future performance and involve a number of risks and uncertainties; actual results could differ materially from those indicated by such forward-looking statements. Among the important factors that could cause actual results to differ materially from those indicated by such forward-looking statements are: (i) that the information is of a preliminary nature and may be subject to further adjustment, (ii) the possible unavailability of financing, (iii) risks related to the exploration and development of oil and gas properties, (iv) the impact of price fluctuations and the demand and pricing for oil and natural gas, (v) the seasonal nature of the business, (vi) start-up risks, (vii) general operating risks, (viii) dependence on third parties, (ix) changes in government regulation, (x) the effects of competition, (xi) dependence on senior management, (xii) financial condition of real estate tenants and financial services counter parts, (xiii) impact of the Canadian economic conditions or the demand for real estate leasing opportunities, (xiv) fluctuations in currency exchange rates and interest rates.

The Trust's strategy is comprised of having three distinct business units: Oil and Gas, Financial Services, and Real Estate. These three units combine the stability of cash flows from both real estate and financial services with a more volatile cash flow stream from oil and gas production. These 2003 results do not include any contribution from the real estate business unit as the Trust's first real estate transaction was not concluded until March 31, 2004.

## Significant Events

- **January 2003 Creation of Avenir Diversified Income Trust ("Avenir" or the "Trust")**  
The Trust was created on January 16, 2003 through a plan of arrangement with Onward Energy Ltd. Since inception, the Trust's unique strategy has been to have three distinct business units: Oil and Gas, Financial Services, and Real Estate. In connection with the Arrangement, the Trust also completed a private placement of an aggregate of 11,325,551 Trust Units at \$0.40 per unit, which closed in a series of two allocations. Proceeds from the private placement were used for the purchase of assets from Response Energy Ltd. and Aventura Energy Ltd., as well as an additional \$600,000 financial services contract with a cash-advance company.
- **May 2003 Acquisition of Outback Energy Ltd. ("Outback")**  
Pursuant to an acquisition agreement dated May 21, 2003, the Trust closed the acquisition of Outback Energy Inc., a junior private oil and gas company, in the second quarter. This acquisition added approximately 50 boe/d. In conjunction with the transaction, the Trust issued 2,333,358 units and assumed approximately \$465,000 in debt and working capital deficiency.
- **September 2003 \$8.0 million Private Placement**  
On September 24, 2003, the Trust closed an \$8,000,000. There were a total of 16,000,000 units issued from treasury, at a price of \$0.50 per unit. Subsequent to the quarter, approximately \$6.2 million of the proceeds from the financing were used for the purchase of 215 boe/d of natural gas assets in late October. The remaining funds from the financing were invested in a portfolio of trust units until the funds were deployed for an investment in the financial services business unit.

- September 2003 Acquisition of 728409 Alberta Ltd. ("728409")**  
 On September 24, 2003 the Trust acquired all of the issued and outstanding common shares of 728409, thereby acquiring approximately 90 boe/d of natural gas. Under the terms of the agreement, the Trust issued an aggregate of 2,000,000 Trust Units from treasury at a price of \$0.50 per unit and \$1,282,829 in cash to shareholders of 728409 as consideration.
- October 2003 Purchase of Natural Gas Assets**  
 The Trust also announced an agreement in September to purchase certain gas assets from a major oil and gas producer. This transaction, which closed on October 24, 2003, added approximately 215 boe/d of natural gas production. This transaction was funded by the proceeds of the September financing as described above.
- December 2003 Issuance of \$2 million Subordinated Debenture with Rentcash Inc. ("Rentcash")**  
 On December 5, 2003 the Trust entered into a subordinated debenture agreement with Rentcash Inc., a publicly listed company traded on the TSXV under the symbol "RCS". The debenture yields a monthly coupon equivalent to a 12% annualized yield, plus associated fees equating to an annualized 4% return.
- Western Spirit Investments Ltd. ("Western Spirit")**  
 On January 21, 2004 the Trust announced that it had entered into its first real estate agreement pursuant to which the Trust would acquire Western Spirit under a plan of arrangement. Western Spirit was a public real estate investment company with a portfolio consisting of five properties with approximately 433,000 square feet of leasable area. The properties are located in Toronto, London (Ontario), Calgary and Edmonton. Through this transaction, shareholders of Western Spirit received, at their election, \$3,000,000 in cash and approximately 5,000,000 trust units of Avenir. The Trust also assumed all of Western Spirit's outstanding debt, including mortgages, of approximately \$16.38 million as at December 31, 2003. The Trust also issued to each Western Spirit shareholder one performance right for each Western Spirit share, each right entitling the holder to acquire 0.05 of a trust unit, for no additional consideration, provided that, at any time on or prior to January 21, 2005, either a signed lease agreement is in place for that portion of the area in Western Spirit's Harris Building, which is currently vacant, or the Trust should sell the Harris Building for not less than \$8.5 million.

### **Revenue and Production**

Oil and gas revenues (net of royalties) were \$1,558,709 for the fourth quarter of 2003, up 96% from the third quarter attributable in most part to the acquisition of 728409 and the natural gas asset purchase in late October. Gross revenue from petroleum and natural gas sales were \$1,907,943 for the fourth quarter up from \$930,905 in the third quarter. The average price received for crude oil and natural gas liquids during the fourth quarter of 2003 was \$32.21 per barrel, up slightly from the previous quarter and \$5.34 per mcf for natural gas, down 27% from the third quarter average of \$6.77 per mcf due to a decline in the overall commodity price. In 2003, the Trust had a hedging program in place for oil with 85 barrels per day hedged at US\$28.00 WTI per barrel for the period April 2003 to March 2004; 33 barrels per day hedged at US\$27.45 WTI per barrel for the period July 2003 to September 2004; 85 barrels per day hedged at US\$27.70 WTI per barrel for the period April 2004 to June 2004; and 100 barrels per day hedged at US\$27.78 WTI per barrel for the period July 1, 2004 to June 01, 2005.

For the year ended December 31, 2003, oil and gas revenues (net of royalties) were \$3,796,376. Gross revenues totaled \$4,560,568 with the average price per boe being \$35.08. As a result of its hedging program to ensure stability of distributions, the Trust recorded a hedging loss of \$47,659 for the fourth quarter of 2003 and \$92,949 for the year ended December 31, 2003.

Average daily production volumes for the quarter ending December 31, 2003 were 634 boe/d, up 108%, compared to 304 boe/d in the in the third quarter. Fourth quarter production consisted of 299 bbls/d of crude oil and natural gas liquids and 2,009 mcf/d of natural gas (compared to 241 bbls/day and 378 mcf/d for the third quarter respectively). The 24% increase in oil and liquids production came mostly from new infill development drilling in Southern Alberta. The 431% increase in natural gas production was the result of the natural gas purchases in late September and October.

## Netbacks

	Three months ended				Twelve months
	Mar 31	Jun 30	Sep 30	Dec 31	Dec 31,
	\$/boe	\$/boe	\$/boe	\$/boe	\$/boe
Gross revenue after hedging	46.74	36.31	33.67	32.73	35.62
Royalties	7.62	5.81	4.96	5.99	5.97
Operating costs	9.51	8.46	7.76	7.48	8.01
Operating netback	29.61	22.05	20.95	19.26	21.64

## Royalties

The Trusts royalty costs net of ARTC for the quarter ending December 31, 2003 were \$349,234, up 156% over the third quarter; however, on a boe basis, royalty costs averaged \$5.99 per boe in the period, which is up 21% over the third quarter's cost of \$4.96 per boe. The royalty costs net of ARTC for the year totaled \$764,192 or \$5.97 per boe. The Trust's royalty rate of 16.42% is low by industry standards, even though most of the Trust's properties do not receive ARTC.

## Operating Expenses

The Trusts operating costs for the quarter ending December 31, 2003 were \$436,153, up 94% over the third quarter; however, on a boe basis, operating costs averaged \$7.48 per boe in the period, which is down 4% over the third quarter's cost of \$7.76 per boe. The operating expenses for the year totaled \$1,025,986 or \$8.01 per boe. The operating costs were higher as a result of the third and fourth quarter natural gas acquisitions. The Trust continues to focus on means of reducing overall operating costs and believes they will decline on a comparative basis for 2004 as they did over the course of 2003.

## Financial Services

Since inception the Trust has held two cash advance contracts, fully collateralized, with a 10-year term callable at the Trust's option. These contracts pay a fixed fee over the life of the contract. The Trust recognized income of \$84,204 relating to the financial services contracts in the fourth quarter of 2003 and total revenues on these contracts for the year ended December 31, 2003 of \$298,404. The Rentcash subordinated debenture, which closed in December 2003, will have monthly payments beginning January 2004.

## Gain (Loss) on Short-Term Investments

At inception, the Trust held a portfolio investment of 100,000 units in an oil and gas trust. The units were sold on June 30, 2003 and a gain of \$75,190 was recognized and the capital was redeployed. On July 26, 2003 the Trust purchased units of three publicly trading energy trusts. Total cost of the acquisitions was \$1,088,111. On September 25, 2003, in order to partially deploy funds prior to closing long-term investments, the Trust purchased a diverse basket of publicly traded income trusts at a cost of \$1,959,579. Income earned on these investments in the fourth quarter amounted to \$31,423 and \$226,975 for the year ended December 31, 2003. All of these short-term investments in units were sold during the fourth quarter of 2003 to finance activities in line with the Trust's business plan and a gain of \$53,319 was realized.

## General and Administrative Expenses

General and administrative expenses were \$430,460 (\$310,592 not including the change for early adopting the stock based compensation plan) in the fourth quarter 2003, up from the third quarter of \$140,542. In the fourth quarter the Trust incurred additional staffing costs associated with the doubling of the Trust's production, as well, costs increased with the Trust's early adoption of the new stock-based compensation rules. On a year to date basis, general and administration costs for oil and gas was \$569,916 or \$4.44 per boe and the corporate trust and financial services general and administration costs amount to \$298,998 (including compensation expense of \$119,868 due to the early adoption of the compensation rules). In addition, as this was the Trust's first year in operation, the year's accounting, audit, legal and reserve evaluation costs were higher for this initial year end and required reporting.

## Interest Expense

Interest expense was \$64,020 for the fourth quarter with bank debt of \$4,505,000 at year end. Bank debt increased substantially from the third quarter, as a portion of the previously described natural gas

acquisitions, were funded by debt. The quarterly expense included banking fees associated with increasing the Trust's revolving line to \$5.2 million from \$3.1 million.

### Depletion, Depreciation and Amortization

Provision for depletion and depreciation was \$736,909 for the quarter ending December 31, 2003, with the Trust's depletion and depreciation rate at \$12.64/boe up slightly from \$11.84/boe in the third quarter. This increase reflects the increasing cost per boe of acquisitions in the current market.

### Future Site Restoration and Abandonment Costs

Total estimated future site restoration costs relating to the oil and gas properties owned by the Trust is \$1,539,600, with the total provision recorded to date at \$567,156.

### Income Taxes

The Trust did not provide for income taxes as it expects that all taxable income will be passed to unit holders in the form of distributions. The Trust did record a capital tax expense of \$12,848 associated with the holding of the oil and gas assets.

### Cash Flow and Earnings

Cash flow from operations was \$853,418 or \$0.02 per unit for the fourth quarter up 60%, compared to \$532,540 in the third quarter or \$0.01 per unit. The increase in cash flow was primarily the natural gas acquisitions made in the third and early in the fourth quarter. The impact of the December financial services investment will not be realized until 2004.

For the year ended December 31, 2003 the cash flow from operations was \$2,362,525 or \$0.08 per unit. The Trust recorded a net loss of \$116,403 for the fourth quarter and net earnings of \$519,180 or \$0.02 per unit for the year ended December 31, 2003. The fourth quarter loss was attributable to the early adoption of the stock-based compensation rules and additional general and administration costs associated with the Trust's first yearend and resulting reporting requirements. The Trust distributed \$725,892 or \$0.02 per unit, to unitholders in the fourth quarter and has distributed \$1,853,871 for the year ended December 31, 2003. The year to date distribution payout ratio was in line with the Trust's target ratio ending the year at 78%. Of the distributions paid, 68% of the amount was classified as taxable income and 32% was tax deferred (return of capital). Cash distributions declared per Trust unit issued and outstanding:

Period covered	Date of Distribution	Per Unit \$
January 16, 2003 to February 28, 2003	03/14/2003	0.00675
March 1, 2003 to March 31, 2003	04/15/2003	0.00525
April 1, 2003 to April 30, 2003	05/15/2003	0.00525
May 1, 2003 to May 31, 2003	06/15/2003	0.00525
June 1, 2003 to June 30, 2003	07/15/2003	0.00525
July 1, 2003 to July 31, 2003	08/15/2003	0.00583
August 1, 2003 to August 31, 2003	09/15/2003	0.00583
September 1, 2003 to September 30, 2003	10/15/2003	0.00583
October 1, 2003 to October 31, 2003	11/15/2003	0.00583
November 1, 2003 to November 30, 2003	12/15/2003	0.00583
December 1, 2003 to December 31, 2003	01/15/2004	0.00583

As at December 31, 2003 the Trust had distributions owing of \$241,964 (2002 - \$nil).

### Quarterly Information

Historical quarterly information, prepared by the Trust in accordance with GAAP, is as follows:

	Fiscal 2003 Three months ended			
	Mar 31	Jun 30	Sep 30	Dec 31
	\$	\$	\$	\$
Gross Revenue	989,004	1,068,917	1,082,105	2,079,584
Net revenue	848,135	931,230	945,703	1,730,350
Net income (loss)	320,710	98,706	216,167	(116,403)
Net income (loss) per unit basic and diluted	0.02	0.00	0.01	(0.00)

## Capital expenditures

	Year End Dec 31, 2003 \$
Land	3,984
Geological and geophysical	12,328
Drilling	450,972
Production equipment and facilities	187,665
Other	75,937
<b>Development expenditures</b>	<b>730,886</b>
Corporate acquisitions	6,263,909
Property acquisitions	9,480,647
Proceeds received on property dispositions	(65,000)
Other	13,472
<b>Net capital expenditures</b>	<b>16,423,914</b>
<b>Property, plant and equipment December 31, 2003</b>	<b>14,915,876</b>

## Liquidity and Debt

The Trust's net debt position of \$4,241,206 at December 31, 2003 is a result of bank indebtedness of \$4,505,000 and positive working capital of \$263,794. The Trust has a revolving demand facility with up to \$5,200,000 bearing interest at bank prime plus one percent. The Trust also has an acquisition and development line of \$2,000,000, bearing interest at bank prime plus one and one-half percent, to fund additional oil and gas acquisitions and a bridge demand facility of \$3,000,000 bearing interest at bank prime plus two percent, to fund real estate acquisitions. As at December 31, 2003 there was \$4,505,000 outstanding on the revolving demand facility. The bridge facility was subsequently drawn on March 31, 2004 to fund the acquisition of Western Spirit.

## Contractual Obligations

The contracts outstanding with respect to the physical deliveries of oil and gas at December 31, 2003 are as follows:

A physical fixed price swap for the period April 1, 2004 to October 31, 2004 on 700 GJ/day of gas at a price of \$5.91 per GJ.

A physical fixed price swap for the period November 1, 2004 to October 31, 2005 on 700 GJ/day of gas at a price of \$5.94 per GJ.

The Trust also has a capital lease on gas compression equipment, which is repayable in monthly installments of \$5,537 including interest at a fixed interest rate of 8% per annum. The lease matures on June 6, 2005 and is collateralized by specific equipment purchased.

## Share Capital

Trust Units	Number of Units	Amount \$
<b>Balance December 31, 2002</b>	<b>—</b>	<b>—</b>
Units issued on 928719 corporate purchase	7,650,000	1,325,182
Units issued on Onward Trust conversion	2,194,373	877,749
Units from Special Warrants financing January 16, 2003	10,158,801	4,063,520
Units financing February 27, 2003	1,166,750	466,700
Units issued on Outback Acquisition	2,333,358	1,050,011
Units issued on private placement	16,000,000	8,000,000
Units issued on 728409 Acquisition	2,000,000	1,000,000
Trust unit issue costs	—	(931,220)
<b>Balance December 31, 2003</b>	<b>41,503,282</b>	<b>15,851,942</b>

For the year ended December 31, 2003 the Trust had a weighted average of 27,621,558 trust units outstanding and the diluted per unit amount was calculated assuming the exercise of outstanding in-the-

money options resulting in 28,182,317. The Trust's weighted average unit price at year end was \$0.511. As at April 1, 2004 the total units outstanding for the Trust were 46,490,779 (which includes the 4,987,497 issued in the Western Spirit transaction).

### **Related Party Transactions**

The Trust's two financial services contracts are with 19695 Yukon Inc., an affiliate of a financial services provider, which is related to a member of the Trust's Board of Directors. These contracts provide funding to a cash advance company providing cash advance, cheque cashing and payday loan services.

In addition, the Trust paid \$85,654 during the year ended December 31, 2003 for corporate administrative and financial services provided by Avenir Capital Corporation, a major unitholder of the Trust.

### **Risks and Uncertainties**

The business of developing and producing oil and natural gas reserves is inherently risky. There is risk that the sale of the Trust's reserves may be delayed indefinitely due to process constraints, lack of pipeline capacity or lack of markets. The price the Trust receives for its oil and gas reserves fluctuates continuously and for the most part is beyond its control. The Trust is also subject to the risks associated with owning oil and gas properties, including environmental risks such as the pollution of air, land and water. In all areas of the Trust business, it competes against entities that have greater technical and financial resources. The Trust's growth is dependent upon external sources of financing which may not be available on acceptable terms.

The Trust mitigates these risks by contracting professional services when required. The Trust diversifies its oil and gas market portfolio among various marketers and aggregators and among a variety of contracts with respect to pricing and term. Finally, all levels of the Trust's operations are adequately insured.

The Trust's existing Financial Services Contracts are with affiliates of a financial services provider and with a chain of cash advance stores. The stated return on the Financial Services Contracts is subject to a degree of credit risk and risk of not realizing on collateral in the event of default. The Trust is afforded full collateral on a customer's pay cheque or other security on the transaction entered into by the cash advance stores. As each transaction is generally between \$100 and \$300, the impact of default on any one transaction is quite small when spread over a number of customers. As with respect to all financial instruments, the Trust could be exposed to losses if a counter party fails to perform in accordance with the terms of the contracts.

### **Critical Accounting Estimates**

The MD&A is based on the Trust's consolidated financial statements, which have been prepared in accordance with GAAP. The application of GAAP requires management to make estimates, judgments and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities, if any, at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. The Trust bases its estimates on historical experience and various other assumptions that are believed to be reasonable under the circumstances. Actual results could differ from these estimates under different assumptions or conditions.

The following is a discussion of the critical accounting estimates that are inherent in the preparation of the Company's consolidated financial statements and notes thereto.

### **Reserve Estimates**

Estimates of the Trust's reserves in its consolidated financial statements are prepared in accordance with guidelines established by the Alberta Securities Commission. Reserve engineering is a subjective process of estimating underground accumulations of petroleum and natural gas that cannot be measured in an exact manner. The process relies on interpretations of available geological, geophysical, engineering and production data. The accuracy of a reserve estimate is a function of the quality and quantity of available data, the interpretation of that data, the accuracy of various mandated economic assumptions and the judgment of the persons preparing the estimate.

The Trust's reserve information is based on estimates prepared by its independent petroleum consultants. Estimates prepared by others may be different than these estimates. Because these estimates depend on many assumptions, all of which may differ from actual results, reserve estimates may be different from the quantities of petroleum and natural gas that are ultimately recovered. In addition, the results of drilling, testing and production after the date of an estimate may justify revisions to the estimate.

The present value of future net revenues should not be assumed to be the current market value of the Trust's estimated reserves. Actual future prices, costs and reserves may be materially higher or lower than the prices, costs and reserves used for the future net revenue calculations.

The estimates of reserves impact depletion, dry hole and site restoration expenses. If reserve estimates decline, the rate at which the Trust records depletion and site restoration expenses increases, reducing net earnings. In addition, changes in reserve estimates may impact the outcome of the Trust's assessment of its petroleum and natural gas properties for impairment.

#### **Future Site Restoration and Abandonment Costs**

Future site restoration and abandonment costs are provided for using the unit of production method based on the estimated net proved reserves. Costs are estimated each year by management in consultation with the Trust's independent reservoir engineers based on current regulations, costs, technology, and industry standards. Such costs are included in income and are accumulated in the provision account based on proven reserve estimates and current production levels. When expenditures are made to restore a property, the accrued provision is charged with these expenditures.

Beginning in 2004, the Trust will adopt the Canadian Institute of Chartered Accountants ("CICA") Handbook section 3110 – Asset Retirement Obligation, which will result in changes in accounting for site restoration and abandonment costs. See "Recent Accounting Pronouncements" section.

#### **Income Taxes**

The Trust's operating entity is a taxable entity under the Income Tax Act of Canada and is taxable only on income that is not distributed or distributable to the unitholders. As the Trust distributes all of its taxable income to the unitholders pursuant to the Trust Indenture and meets the requirements of the Income Tax Act of Canada applicable to the Trust, no provision for income taxes have been made.

### **Recent Accounting Pronouncements and Impact of the Trust**

#### **Impairment of Long-Lived Assets**

The CICA recently issued Handbook Section 3063 – Impairment of Long-Lived Assets, which will impact the Trust's Financial Services and Real Estate segments. This new section establishes standards for the recognition, measurement and disclosure of the impairment of long-lived assets by profit-oriented enterprises. The section is effective for fiscal years beginning on or after April 1, 2003. This section will require a new calculation of impairment based on undiscounted future cash flows. As the Trust's oil and gas segment follows the full cost method and this new section is not applicable for full cost, the Trust will be required to follow the new CICA accounting guideline 16, Oil & Gas Accounting - Full Costs. This new guideline is designed to ensure consistency with the Impairment of Long-Lived Assets section, described above for, for the oil and gas industry. This guideline is applicable to fiscal years beginning on or after January 1, 2004. The Trust anticipates the adoption of these pronouncements will not have a material effect on its consolidated financial statements.

#### **Variable Interest Entities**

The CICA recently issued Accounting Guideline 15 – Consolidation of Variable Interest Entities. The guideline requires the consolidation of entities in which an enterprise absorbs a majority of the entity's expected losses, receives a majority of the entity's expected residual returns, or both, as a result of ownership, contractual or other financial interests in the equity. (The guideline applies to annual and interim periods beginning on or after November 1, 2004, except for certain disclosure requirements. Entities should provide disclosures about variable interest entities in which they hold significant interests for periods beginning on or after January 1, 2004). The Trust does not expect the implementation of this guideline to have a material impact on its financial statements.

### **Asset Retirement Obligation**

The CICA recently issued Handbook Section 3110 – Asset Retirement Obligation, which addresses statutory, regulatory, contractual and other legal obligations associated with the retirement of a long-lived asset that results from its acquisition, construction, development or normal operation. The asset retirement obligations are initially measured at fair value at the time the obligation is incurred with a corresponding amount capitalized as part of the asset's carrying value and depreciated over the asset's useful life using a systematic and rational allocation method. The impact of this has not yet been determined.

### **Stock-Based Compensation and Other Stock-Based Payments**

In October 2003, the CICA amended Handbook Section 3870 to require recognition of expense, based on the fair value method, for all employee stock-based compensation transactions for fiscal years beginning on or after January 1, 2004.

The recommendations of the Section should also be applied to the following awards that were outstanding at the start of the fiscal year beginning on or after January 1, 2002 in which adoption of this Section was initially applied: awards that call for settlement in cash or other assets and stock appreciation rights that call for settlement by the issuance of equity instruments. The award should be accounted for as a new award, and not using modification accounting. The cumulative amount that would have been recognized in prior years had this section been applied, less any amount previously recognized, should be recorded as the effect of a change in accounting policy and charged to opening retained earnings for the fiscal year in which this section is initially applied, without restatement of prior periods.

The Trust early adopted with respect to this requirement and has used the intrinsic method of accounting for stock options for fiscal 2003. The intrinsic method will be applied prospectively, whereby compensation costs will be recognized for all options granted on or after January 1, 2003. Adoption of this accounting policy has resulted in an expense of \$119,868 being recorded in the Trusts consolidated financial statements for the year ended December 31, 2003.

## **2004 OUTLOOK**

With the first year of operation complete, the Trust looks forward to 2004 without the costs and complexities associated with setting up the Trust in 2003.

The start to 2004 resulted in the Trust continuing the rounding out of its business plan, by adding real estate assets to the portfolio in March. Looking ahead, the Trust will concentrate on the further build out of each business unit, ensuring the stability of distributions and the growth in distributions per unit.

For additional information on the Trust, please go to the company's profile on SEDAR at [www.sedar.com](http://www.sedar.com) or the Trust's website at [www.avenirtrust.com](http://www.avenirtrust.com).

Submitted on behalf of the Board of Directors by:

William M. Gallacher  
President & CEO

Gary Dundas  
Vice President Finance & CFO

## Avenir Diversified Income Trust

### CONSOLIDATED BALANCE SHEETS

As at December 31,

	2003 \$	2002 \$
<b>ASSETS</b>		
<b>Current</b>		
Cash and cash equivalents	256,872	82,497
Accounts receivable and prepaid expenses	1,799,803	335,819
Short-term investments	—	1,010,000
	<b>2,056,675</b>	<b>1,428,316</b>
<b>Capital assets</b>		
<b>Financial services contracts</b>	<b>14,915,876</b>	—
<b>Goodwill</b>	<b>3,241,963</b>	600,000
	<b>1,086,729</b>	—
	<b>21,301,243</b>	<b>2,028,316</b>
<b>LIABILITIES AND UNITHOLDERS' EQUITY</b>		
<b>Current</b>		
Bank indebtedness	4,505,000	602,859
Accounts payable and accrued liabilities	1,489,755	588,829
Distributions payable	241,964	—
Current portion of capital lease obligations	61,162	—
	<b>6,297,881</b>	<b>1,191,688</b>
<b>Capital lease obligations</b>	<b>32,459</b>	—
<b>Provision for future site restoration and abandonment</b>	<b>567,156</b>	—
<b>Commitments</b>		
<b>Shareholders'/Unitholders' equity</b>		
Shareholder capital	—	1,070,000
Unitholder capital	15,851,942	—
Contributed surplus	119,868	—
Accumulated earnings/(deficit)	285,808	(233,372)
Accumulated cash distributions	(1,853,871)	—
	<b>14,403,747</b>	<b>836,628</b>
	<b>21,301,243</b>	<b>2,028,316</b>

**Avenir Diversified Income Trust**

**CONSOLIDATED STATEMENTS OF  
OPERATIONS AND ACCUMULATED EARNINGS/(DEFICIT)**

For the year ended December 31,

	<b>2003</b>	<b>2002</b>
	<b>\$</b>	<b>\$</b>
<b>REVENUE</b>		
Oil and gas	4,560,568	—
Royalties net of ARTC	(764,192)	—
	3,796,376	—
Financial services fees	298,404	44,100
Investment income	226,975	143,111
Interest and other income	5,154	—
Gain on sale of short-term investments	128,509	—
	4,455,418	187,211
<b>EXPENSES</b>		
Oil and gas operating	1,025,986	—
General and administrative	868,914	249,515
Unsuccessful acquisition and re-organizational costs	233,057	—
Bank fees and interest	176,504	8,585
Capital tax	12,848	—
Depletion and depreciation	1,508,038	—
Site restoration	110,891	—
	3,936,238	258,100
Income (loss) before income tax	519,180	(70,889)
Income tax expense	—	—
Net income (loss) for the year	519,180	(70,889)
Accumulated earnings/(deficit), beginning of year	(233,372)	(162,483)
Accumulated earnings/(deficit), end of year	285,808	(233,372)
Net income (loss) per unit/share basic and diluted	0.02	(0.01)

## Avenir Diversified Income Trust

### CONSOLIDATED STATEMENTS OF CASH FLOWS

For the year ended December 31,

	2003 \$	2002 \$
<b>OPERATING ACTIVITIES</b>		
Net income (loss) for the year	519,180	(70,889)
Add (deduct) non-cash items		
Depletion and depreciation	1,508,038	—
Non-cash general and administrative	119,868	—
Site restoration	110,891	—
Gain on sale of short-term investments	(128,509)	—
Unsuccessful acquisition and re-organizational costs	233,057	—
Funds from (used in) operations	2,362,525	(70,889)
Change in non-cash working capital	(506,904)	32,869
Cash provided by operating activities	1,855,621	(38,020)
<b>FINANCING ACTIVITIES</b>		
Issue of trust units/shares	12,530,220	—
Trust unit issue costs	(931,220)	—
Distribution to unitholders	(1,611,907)	—
Change in bank indebtedness	3,642,141	602,859
Repayments of capital lease obligations	(14,544)	—
Change in non-cash working capital	(2,386)	156,818
Cash provided by financing activities	13,612,304	759,677
<b>INVESTING ACTIVITIES</b>		
Purchase and conversion of Onward Energy Inc.	(1,643,458)	—
Purchase of Outback Energy Inc.	(141,592)	—
Purchase of 728409 Alberta ltd.	(1,319,863)	—
Oil and gas property acquisitions	(9,480,647)	—
Oil and gas property disposals	65,000	—
Purchase of financial services contract	(2,641,963)	(600,000)
Oil and gas development expenditures	(730,886)	—
Purchase of other assets	(17,377)	—
Sale of other assets	3,905	—
Sale of short-term investments	4,186,199	—
Purchase of short-term investments	(3,047,690)	—
Unsuccessful acquisition and re-organizational costs	(233,057)	—
Changes in non-cash working capital	(292,121)	(39,160)
Cash used in investing activities	(15,293,550)	(639,160)
<b>Increase in cash and cash equivalents during the year</b>	<b>174,375</b>	<b>82,497</b>
Cash and cash equivalents, beginning of year	82,497	—
<b>Cash and cash equivalents, end of year</b>	<b>256,872</b>	<b>82,497</b>
<b>Cash interest paid</b>	<b>144,359</b>	<b>5,812</b>