

THE KEG ROYALTIES INCOME FUND

FIRST QUARTER REPORT

For the three months ended March 31, 2007

TO OUR UNITHOLDERS

On behalf of the Board of Trustees, I am pleased to present the results of The Keg Royalties Income Fund (the "Fund") for the three months ended March 31, 2007.

RESULTS

The Trustees are delighted to report that The Keg has reached another sales record for the first quarter. The gross sales reported by the 95 Keg restaurants in the Royalty Pool were \$105,239,000, an increase of \$11,282,000 or 12.0% from the comparable quarter of the prior year. Total system sales for The Keg were even more impressive at \$106,960,000 for the quarter, an increase of \$9,920,000 or 10.2% over the comparable quarter of the prior year. These higher system sales reflect the very successful new Keg restaurants which opened during the period from October 3, 2005 through October 2, 2006 and which were added to the Royalty Pool on January 1, 2007, as well as very strong same store sales growth.

The Fund generated earnings of \$3,064,000 or 32.8 cents/Fund unit compared with \$2,651,000 or 30.9 cents/Fund unit during the same quarter of the prior year, an increase of \$413,000. Distributable cash available to pay distributions to public Unitholders increased by \$410,000 to \$3,068,000 or 32.9 cents/Fund unit, from \$2,658,000 or 31.0 cents/Fund unit for the first quarter of the prior year.

DISTRIBUTION INCREASE

On February 6, 2007, the Trustees were pleased to authorize another distribution increase to Unitholders, the fourth distribution increase since the inception of the Fund. The monthly distributions were increased by 2.5% from \$0.0956 per unit to \$0.0980 per unit, beginning with the March 2007 distribution. This equals an annualized distribution of \$1.176 per unit. The Fund's objective is to provide consistent, monthly distributions to Unitholders at the highest sustainable level, and the Fund will continue to review distribution levels on an ongoing basis to fulfill that objective.

FEDERAL GOVERNMENT TAX ON INCOME FUNDS

On October 31, 2006, The Federal Department of Finance announced a new Distribution Tax on publicly traded income trusts. We are very disappointed with the government's sudden about face on its tax treatment of income trusts, and are extremely unhappy with the impact that this has had on our unitholders. That having been said, we are confident that the management of The Keg will remain focused on running great steakhouses and bars, and increasing sales at both new locations and existing restaurants.

OUTLOOK

The Canadian Restaurant and Foodservice Association (CRFA) has projected growth in the full-service restaurant category, the category in which the Keg operates, of 3.6% in 2007. Management of KRL believes that The Keg will continue to outperform the full-service category with respect to same store sales growth.

The Keg remains an industry leader in the full-service restaurant category, showing continued growth in both overall sales and same store sales. Management remains committed to maintaining and improving the legendary high standards that have come to define the brand, including The Keg's high quality menu, knowledgeable service and marketing innovation. The Keg's management team is focused not only on developing new Kegs in new markets where opportunities exist, but also on growing sales in existing Kegs year after year, further strengthening the company's position as a market leader throughout North America.

Sincerely,



C.C. Woodward
Chairman, The Keg Royalties Income Fund
on behalf of the Board of Trustees
April 25, 2007

FINANCIAL HIGHLIGHTS

(\$000's except per unit amounts)	Jan. 1 to Mar. 31, 2007	Jan. 1 to Mar. 31, 2006
Restaurants in the Royalty Pool	95	91
Gross sales reported by restaurants in the Royalty Pool	<u>\$ 105,239</u>	<u>\$ 93,957</u>
Royalty income ⁽¹⁾	\$ 4,260	\$ 3,761
Partnership expenses ⁽²⁾	<u>(102)</u>	<u>(138)</u>
Partnership earnings	4,158	3,623
KRL's interest ⁽³⁾	<u>(1,926)</u>	<u>(1,823)</u>
Equity income ⁽⁴⁾	2,232	1,800
Interest income ⁽⁵⁾	<u>1,061</u>	<u>1,056</u>
Total income	3,293	2,856
Interest and financing expenses ⁽⁶⁾	<u>(229)</u>	<u>(205)</u>
Earnings for the period	<u>\$ 3,064</u>	<u>\$ 2,651</u>
Earnings per Fund unit ⁽⁷⁾	<u>\$.328</u>	<u>\$.309</u>
Distributable cash per Fund unit ⁽⁷⁾⁽⁸⁾	<u>\$.329</u>	<u>\$.310</u>
Distributions declared per Fund unit ⁽⁷⁾	<u>\$.195</u>	<u>\$.187</u>

Notes:

- ⁽¹⁾ The Fund, indirectly through the Partnership, earns royalty income equal to 4% of gross sales of Keg restaurants included in the Royalty Pool.
- ⁽²⁾ The Fund, indirectly through the Partnership, incurs administrative expenses and interest on an operating line of credit, to the extent utilized.
- ⁽³⁾ Represents the interest of KRL in the earnings of the Partnership from the Class A, entitled Class B and Class C Partnership units. The Class A and entitled Class B Partnership units are exchangeable into Fund units on a one-for-one basis.
- ⁽⁴⁾ The Fund directly earns equity income from its investment in the Partnership.
- ⁽⁵⁾ The Fund directly earns interest income on the \$57.0 million Keg Loan, with interest income accruing at 7.5% per annum, payable monthly.
- ⁽⁶⁾ The Fund directly incurs interest expenses on the long-term debt and amortization of deferred financing charges.
- ⁽⁷⁾ All per unit amounts are calculated based on the weighted average number of Fund units outstanding, which are those units held by public unitholders during the respective period. The weighted average number of Fund units outstanding for the three months ended March 31, 2007 and 2006 were 9,327,944 and 8,569,611 respectively.
- ⁽⁸⁾ Distributable cash is not an earnings measure recognized by generally accepted accounting principles ("GAAP") and therefore may not be comparable to similar measures presented by other issuers. Distributable cash per unit is computed as earnings for the period plus non-cash items, divided by the weighted average number of Fund units issued and outstanding.

	Mar. 31, 2007	Dec. 31, 2006
Total assets	\$ 115,954	\$ 106,500
Total liabilities	14,002	14,863

SUMMARY OF QUARTERLY FINANCIAL RESULTS

	Q1 2007	Q4 2006	Q3 2006	Q2 2006
	(\$000's except per unit amounts)			
Restaurants in the Royalty Pool	95	91	91	91
Gross sales reported by Keg restaurants in the Royalty Pool	<u>\$ 105,329</u>	<u>\$ 98,684</u>	<u>\$ 91,564</u>	<u>\$ 88,266</u>
Royalty income ⁽¹⁾	\$ 4,260	\$ 4,038	\$ 3,734	\$ 3,564
Partnership expenses ⁽²⁾	(102)	(105)	(94)	(120)
Partnership earnings	4,158	3,933	3,640	3,444
KRL's interest ⁽³⁾	(1,926)	(1,876)	(1,880)	(1,726)
Equity income ⁽⁴⁾	2,232	2,057	1,760	1,718
Interest income ⁽⁵⁾	1,061	1,083	1,081	1,069
Total income	3,293	3,140	2,841	2,787
Interest and financing expenses ⁽⁶⁾	(229)	(234)	(235)	(226)
Earnings for the period	<u>\$ 3,064</u>	<u>\$ 2,906</u>	<u>\$ 2,606</u>	<u>\$ 2,561</u>
Earnings per Fund unit ⁽⁷⁾	<u>\$.328</u>	<u>\$.321</u>	<u>\$.288</u>	<u>\$.283</u>
Distributable cash per Fund unit ⁽⁷⁾⁽⁸⁾	<u>\$.329</u>	<u>\$.322</u>	<u>\$.289</u>	<u>\$.284</u>
Distributions declared per Fund unit ⁽⁷⁾	<u>\$.195</u>	<u>\$.382</u>	<u>\$.283</u>	<u>\$.281</u>

	Q1 2006	Q4 2005	Q3 2005	Q2 2005
	(\$000's except per unit amounts)			
Restaurants in the Royalty Pool	91	86	86	86
Gross sales reported by Keg restaurants in the Royalty Pool	<u>\$ 93,957</u>	<u>\$ 85,217</u>	<u>\$ 79,877</u>	<u>\$ 79,433</u>
Royalty income ⁽¹⁾	\$ 3,761	\$ 3,449	\$ 3,227	\$ 3,209
Partnership expenses ⁽²⁾	(138)	(89)	(100)	(136)
Partnership earnings	3,623	3,360	3,127	3,073
KRL's interest ⁽³⁾	(1,823)	(1,756)	(1,756)	(1,718)
Equity income ⁽⁴⁾	1,800	1,604	1,371	1,355
Interest income ⁽⁵⁾	1,056	1,079	1,079	1,067
Total income	2,856	2,683	2,450	2,422
Interest and financing expenses ⁽⁶⁾	(205)	(192)	(177)	(172)
Earnings for the period	<u>\$ 2,651</u>	<u>\$ 2,491</u>	<u>\$ 2,273</u>	<u>\$ 2,250</u>
Earnings per Fund unit ⁽⁷⁾	<u>\$.309</u>	<u>\$.296</u>	<u>\$.271</u>	<u>\$.276</u>
Distributable cash per Fund unit ⁽⁷⁾⁽⁸⁾	<u>\$.310</u>	<u>\$.297</u>	<u>\$.272</u>	<u>\$.277</u>
Distributions declared per Fund unit ⁽⁷⁾	<u>\$.187</u>	<u>\$.367</u>	<u>\$.272</u>	<u>\$.270</u>

MANAGEMENT DISCUSSION AND ANALYSIS

**For the Three Months Ended March 31, 2007
As of April 25, 2007**

OVERVIEW

On May 31, 2002, The Keg Royalties Income Fund (the “Fund”), through its subsidiary The Keg Rights Limited Partnership (the “Partnership”), purchased The Keg trademarks and related property (collectively, the “Keg Rights”) from Keg Restaurants Ltd. (“KRL”). The Partnership, in turn, granted KRL an exclusive licence to use the Keg Rights for a term of 99 years pursuant to a licence and royalty agreement, which obligates KRL to make monthly royalty payments to the Partnership.

During 2005, the Partnership was determined to be a variable interest entity in accordance with the criteria established in the new Canadian Institute of Chartered Accountants’ Guideline, Consolidation of Variable Interest Entities (“AcG-15”). As a result of this guideline, the Fund accounts for its investment in the Partnership on an equity basis and KRL consolidates the Partnership. Readers are advised that this is an accounting basis of presentation only and that earnings and distributable cash attributable to Fund unitholders are not impacted nor does this impact the contractual obligations between the Fund, and the Partnership, and KRL. The consolidated financial statements of the Fund therefore include the accounts of the Fund, its wholly-owned subsidiary The Keg Holdings Trust (“KHT”) and its 90% owned subsidiary The Keg GP Ltd. (“KGP”) (collectively, the “Companies”). KGP is the managing general partner of the Partnership. All residual ownership of the Companies is either directly or indirectly controlled by KRL.

The Fund earns equity income from its investment in the Partnership and interest income on a \$57.0 million loan to KRL (the “Keg Loan”). The Fund’s equity income from the Partnership is calculated as the royalty income less the Partnership’s operating expenses less earnings attributable to KRL. The Fund’s interest income on the Keg Loan is calculated at 7.5% per annum, payable monthly.

The Fund, indirectly through the Partnership, earns royalty income equal to 4% of gross sales of Keg restaurants included in a specific royalty pool (the “Royalty Pool”).

The Fund, indirectly through the Partnership, incurs administrative expenses and interest expense on the operating line of credit, to the extent utilized (the “Partnership Expenses”). See “Liquidity and Capital Resources – Operating Line of Credit”.

KRL’s interest in the earnings of the Partnership is from its ownership of Class A, entitled Class B and Class C Partnership units. The Class A and entitled Class B Partnership units are exchangeable into Fund units on a one-for-one basis in certain circumstances. On July 4, 2005 KRL exchanged 250,000 Class B units of the Partnership for an equal amount of Fund units, increasing the number of issued and outstanding Fund units to 8,403,500 and on July 6, 2005, sold these 250,000 Fund units through the facilities of the Toronto Stock Exchange. On March 9, 2006 KRL exchanged 650,000 Class B units of the Partnership for an equal amount of Fund units, increasing the number of issued and outstanding Fund units to 9,053,500 and on March 14, 2006, sold these 650,000 Fund units through the facilities of the Toronto Stock Exchange. On February 22, 2007 KRL exchanged 650,000 Class B units of the Partnership for an equal amount of Fund units, increasing the number of issued and outstanding Fund units to 9,703,500 and on February 23, 2007, sold these 650,000 Fund units through the facilities of the Toronto Stock Exchange. As of March 31, 2007, KRL owned 2,436,784 of the entitled exchangeable units of the Partnership or the equivalent of 20.07% of the Fund units on a fully diluted basis.

OVERVIEW (CONTINUED)

The Fund's operating expenses are limited to interest on the term loan and amortization of deferred financing charges. See "Liquidity and Capital Resources – Term Loan".

THE ROYALTY POOL

Annually, on January 1st, the Royalty Pool is adjusted to include the gross sales from new Keg restaurants that have opened on or before October 2nd of the prior year, less gross sales from any Keg restaurants that have permanently closed during the preceding calendar year. In return for adding these net sales to the Royalty Pool, KRL receives the right to indirectly acquire additional Fund units (the "Additional Entitlement"). The Additional Entitlement is determined based on 92.5% of the estimated royalty revenue added to the Royalty Pool, divided by the yield of the Fund units. KRL receives 80% of the estimated Additional Entitlement initially, with the balance received on December 31st of each year when the actual full year performance of the new restaurants is known with certainty.

Readers should note that the number of restaurants added to the Royalty Pool each year may differ from the number of restaurant openings and closings reported by KRL on an annual basis, as the periods for which they are reported differ slightly.

The total number of Keg restaurants included in the Royalty Pool has increased from the 80 Keg restaurants in existence on March 31, 2002, to 91 as of December 31, 2006. Twenty-one new Keg restaurants that opened during the period from April 1, 2002 through October 2, 2005, with annual gross sales of \$97.5 million, have been added to the Royalty Pool. Ten permanently closed Keg restaurants with annual sales of \$24.8 million have been removed from the Royalty Pool. This has resulted in a net increase in Royalty Pool sales of \$72.7 million annually and KRL receiving a cumulative Additional Entitlement equivalent to 2,489,280 Fund units as of December 31, 2006.

On January 1, 2007, six new Keg restaurants that opened during the period from October 3, 2005 through October 2, 2006 were added to the Royalty Pool. The gross sales of these six new restaurants have been estimated at \$28.0 million annually. Two permanently closed Keg restaurants with annual sales of \$5.7 million were removed from the Royalty Pool, resulting in an estimated net increase in Royalty Pool sales of \$22.3 million annually. The total number of restaurants in the Royalty Pool increased to 95. The yield of the Fund units was determined to be 8.52% calculated using a weighted average unit price of \$13.10.

As a result of the contribution of the additional net sales to the Royalty Pool, and assuming 100% of the estimated Additional Entitlement is received, KRL's Additional Entitlement will be equivalent to 739,449 Fund units, being 6.02% of the Fund units on a fully diluted basis. On January 1, 2007, KRL received 80% of this entitlement representing the equivalent of 591,559 Fund units, being 4.87% of the Fund units on a fully diluted basis. KRL will also receive a proportionate increase in monthly distributions from the Partnership. Including the initial portion of the Additional Entitlement described above, KRL will have the right to exchange its units in the capital of the Partnership for 2,436,784 Fund units (after giving effect to the sale of 650,000 Fund units on February 23, 2007), representing 20.07% of the Fund units on a fully diluted basis. The balance of the Additional Entitlement will be adjusted to be effective January 1, 2007 once the actual performance of the new restaurants has been confirmed. If KRL were to receive 100% of the estimated Additional Entitlement for 2007, it would have the right to exchange its Partnership units for 2,584,674 Fund units (after giving effect to the sale of 650,000 Fund units on February 23, 2007), representing 21.03% of the Fund units on a fully diluted basis.

OWNERSHIP OF THE FUND

The ownership of the Fund on a fully diluted basis is as follows:

	March 31, 2007 ⁽¹⁾		March 31, 2006	
	<u>#</u>	<u>%</u>	<u>#</u>	<u>%</u>
Fund units held by public unitholders ⁽²⁾	9,703,500	79.93	9,053,500	79.73
Exchangeable Partnership units held by KRL: ⁽³⁾				
Class A units ⁽⁴⁾	905,944	7.46	905,944	7.98
Class B units ⁽⁵⁾	<u>1,530,840</u>	<u>12.61</u>	<u>1,395,982</u>	<u>12.29</u>
Total Exchangeable Partnership units ⁽⁶⁾	<u>2,436,784</u>	<u>20.07</u>	<u>2,301,926</u>	<u>20.27</u>
Total Fund and Exchangeable Partnership units	<u>12,140,284</u>	<u>100.00</u>	<u>11,355,426</u>	<u>100.00</u>

Notes:

⁽¹⁾ Information is current as of March 31, 2007.

⁽²⁾ On March 9, 2006, KRL exchanged 650,000 Class B units of the Partnership for an equal amount of Fund units, increasing the number of issued and outstanding Fund units to 9,053,500 and on March 14, 2006, sold these 650,000 Fund units through the facilities of the Toronto Stock Exchange. On February 22, 2007, KRL exchanged 650,000 Class B units of the Partnership for an equal amount of Fund units, increasing the number of issued and outstanding Fund units to 9,703,500 and on February 23, 2007, sold these 650,000 Fund units through the facilities of the Toronto Stock Exchange. The weighted average number of Fund units outstanding for the three months ended March 31, 2007 and 2006 were 9,327,944 and 8,569,611 respectively.

⁽³⁾ Exchangeable into Fund units on a one-for-one basis. Class D Partnership units are also exchangeable into Fund units on a one-for-one basis, but may only be issued after all Class B units have become fully entitled. As at March 31, 2007, no Class D Partnership units have been issued.

⁽⁴⁾ Represents KRL's initial 10% effective ownership of the Fund, prior to the entitlement to Class B units.

⁽⁵⁾ KRL is the registered holder of 1,826,700 Class B units as of the date hereof, although only a portion of such are entitled to proportionate distributions from the Partnership, which as at March 31, 2007 comprised 1,530,840 Class B units and as at March 31, 2006 comprised 1,395,982 Class B units. This cumulative entitlement is as a result of adding net sales to the Royalty Pool on an annual basis. Also included in these figures is 80% of the Additional Entitlement estimated at the beginning of each year, pursuant to which KRL receives a proportionate increase in monthly distributions from the partnership. The remaining 20% of KRL's Additional Entitlement to Class B units is adjusted retroactively to January 1st of each year once the actual sales performance of the new restaurants has been confirmed. KRL is not entitled to proportionate monthly distributions from the Partnership on the remaining 20% of KRL's Additional Entitlement until such time as the Additional Entitlement is adjusted retroactively at the end of each year.

⁽⁶⁾ Represents KRL's total effective ownership of the Fund as of March 31, 2007 and 2006. KRL's average effective ownership, based on the weighted average number of Fund and exchangeable units held by KRL during the respective period, was 23.17% during the three-month period ended March 31, 2007 and 24.53% during the three-month period ended March 31, 2006.

SYSTEM SALES

While the Fund's income is indirectly based on a royalty of 4% of sales of Keg restaurants in the Royalty Pool, the total system sales of The Keg chain are of interest to the Fund and its unitholders as the total system sales best reflect the chain's overall performance. The following table sets out The Keg's total system sales for the periods indicated below:

(\$000's)	13 weeks ended Apr. 1, 2007	13 weeks ended Apr. 2, 2006
Corporate Keg restaurants	\$ 54,445	\$ 48,969
Franchised Keg restaurants ⁽¹⁾	<u>52,515</u>	<u>48,071</u>
Total system sales	<u>\$ 106,960</u>	<u>\$ 97,040</u>

Notes:

⁽¹⁾ The amount of system sales for the franchised Keg restaurants is the amount of gross sales reported to KRL by franchised Keg restaurants without independent audit and includes the gross sales of a joint venture restaurant located in Coquitlam, British Columbia.

System sales for the 13 weeks ended April 1, 2007 were \$106.9 million compared to \$97.0 million for the 13 weeks ended April 2, 2006, an increase of \$9.9 million or 10.2%. During the 13 weeks ended April 1, 2007, one new corporate restaurant was opened, and one corporate and one franchised restaurant were relocated. During the 13 weeks ended April 2, 2006, two new franchised restaurants were opened and one franchised restaurant was closed. As of April 1, 2007, there were a total of 96 Keg restaurants as compared with 93 restaurants at April 2, 2006.

The Keg's same store sales (sales of restaurants that operated during the entire 13-week period of both the current year and the prior year) increased by 8.1% in Canada and by 3.8% in the United States. After translating the sales of the U.S. restaurants into their Canadian dollar equivalent, consolidated same store sales for the comparable 13-week period increased by 7.6%. The average exchange rate moved from 1.16 in KRL's second quarter of fiscal 2006 to 1.17 in KRL's second quarter of fiscal 2007, slightly increasing the Canadian dollar equivalent of the U.S. restaurant sales.

OPERATING RESULTS

GROSS SALES

Gross sales reported by the restaurants in the Royalty Pool increased from \$93,957,000 to \$105,239,000 for the comparable quarter. The increase of \$11,282,000 or 12.0% reflects both the addition of net new sales to the Royalty Pool at the beginning of the year and the same store sales increases discussed previously.

ROYALTY INCOME

Royalty income earned by the Partnership increased by \$499,000 from \$3,761,000 in the first quarter of 2006 to \$4,260,000 in the first quarter of 2007, as a result of the increase in gross sales for the reasons explained previously.

PARTNERSHIP EXPENSES

Expenses incurred by the Partnership for the three months ended March 31, 2007 were \$102,000 and included general and administrative expenses of \$104,000 and interest income on the surplus cash balances of \$2,000. The decrease of \$36,000 over the comparable quarter in 2006 was due to a decrease in general and administrative expenses of \$35,000 due to the timing of certain expenditures associated with the publication of the annual report and an increase in interest income of \$1,000 due to greater cash balances on hand during the quarter.

KRL'S INTEREST

KRL's interest in the earnings of the Partnership from the Class A, entitled Class B and Class C Partnership units increased from \$1,823,000 for the three months ended March 31, 2006 to \$1,926,000 for the three months ended March 31, 2007. The increase of \$103,000 was primarily due to the increase in Partnership earnings as a result of the increased royalty income. This was partially offset by a decrease in KRL's average effective ownership interest in the Partnership from 24.53% during the three-month period ended March 31, 2006 to 23.17% during the three-month period ended March 31, 2007. The change in the average effective ownership of the Partnership during the period was a result of the sale of 650,000 Fund units owned by KRL on March 14, 2006, the 2007 Additional Entitlement, and the sale of an additional 650,000 Fund units owned by KRL on February 23, 2007.

EQUITY INCOME

The Fund's equity income from its investment in the Partnership increased from \$1,800,000 during the first quarter of 2006 to \$2,232,000 during the first quarter of 2007. The increase of \$432,000 is due to the net impact of the increase in royalty income of \$499,000, the decrease in Partnership expenses of \$36,000, and the increase in KRL's interest in the earnings of the Partnership of \$103,000.

INTEREST INCOME

Interest income earned by the Fund for the quarter was \$1,061,000 and included interest income on the Keg Loan of \$1,054,000 and other interest income of \$7,000.

INTEREST AND FINANCING EXPENSES

Interest and financing expenses incurred by the Fund were \$229,000 for the three months ended March 31, 2007 and included interest on the long-term debt of \$224,000 and amortization of deferred financing charges of \$5,000. Interest costs increased by \$26,000 in the quarter as a result of an increase in the average interest rate on the long-term debt from 5.75% in the first quarter of 2006 to 6.50% in the first quarter of 2007. Amortization of deferred financing charges decreased by \$2,000 for the quarter.

NET EARNINGS AND COMPREHENSIVE INCOME

Net earnings increased by \$413,000 from \$2,651,000 (30.9 cents/Fund unit) in the first quarter of 2006 to \$3,064,000 (32.8 cents/Fund unit) in the first quarter of 2007.

DISTRIBUTABLE CASH

Cash available for distribution to Fund unitholders increased by \$410,000 from \$2,658,000 (31.0 cents/Fund unit) to \$3,068,000 (32.9 cents/Fund unit) during the quarter. Distributions of 19.5 cents per Fund unit were declared in the first quarter of 2006 and 18.7 cents per Fund unit in the first quarter of 2007. The difference between the Fund's earnings and distributable cash is due to non-cash items included in the Fund's operating expenses.

LIQUIDITY AND CAPITAL RESOURCES

It is the Fund's policy to distribute all available cash on a monthly basis in order to provide consistent returns to unitholders and to maximize those returns. Any increase in distributions in the future will be implemented in such a manner so as to maintain uniform monthly distributions.

TERM LOAN

The Keg Holdings Trust, a subsidiary of the Fund, has a \$14 million non-revolving term loan facility, which bears interest at bank prime plus 0.50% per annum. The facility was originally arranged during the IPO to partially finance the purchase of the Keg Rights from KRL, and to provide term debt as part of the capital structure. On September 26, 2006, this facility was refinanced, and the maturity date extended to April 3, 2011. Certain conditions must be maintained for the term loan to be in good standing, all of which have been met.

OPERATING LINE OF CREDIT

The Partnership, a subsidiary of the Fund, has a \$1 million operating line of credit, which bears interest at bank prime plus 0.25% per annum. This facility is used primarily to bridge timing differences between the receipt of the royalty payments and distributions on the Partnership securities. This operating line is also available for general working capital purposes, or if required, to help finance periodic differences between receipt of the royalty payment, (which may vary due to small seasonal variations in the gross sales of those restaurants in the Royalty Pool), and distributions to unitholders.

CONTROLS AND PROCEDURES

Disclosure controls and procedures are designed to provide reasonable assurance that relevant information is gathered and reported to Senior Management, including the Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO") of The Keg GP Ltd., managing general partner of the Partnership and administrator of the Fund, on a timely basis so that the appropriate decisions can be made regarding public disclosure. As of March 31, 2007, an evaluation of the effectiveness of the Fund's disclosure controls and procedures, as defined under Multilateral Instrument 52-109 ("MI 52-109") issued by the Canadian Securities Administrators, was carried out under the supervision of and with the participation of management, including the CEO and CFO. Based on that evaluation, the CEO and CFO concluded that the design and operation of these disclosure controls and procedures were effective.

As of March 31, 2007, under the supervision of and with the participation of management, including the CEO and CFO, internal controls over financial reporting have been designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP.

CRITICAL ACCOUNTING ESTIMATES

The Fund's only critical accounting estimate is the valuation of its investment in the Partnership. As the Partnership's only significant assets are intangible assets consisting of the Keg Rights, the valuation of the Fund's investment is based primarily upon the valuation of intangible assets in the Partnership. The Keg Rights are not amortized as they have an indefinite life. The Keg GP Ltd., as the general partner of the Partnership and administrator of the Fund, reviews the carrying values of the intangible assets in the Partnership and the Fund's investment at least annually, taking into consideration any events or circumstances which may have impaired the carrying values of these items. If permanent declines in the carrying amounts are determined, these items are written down to their estimated net recoverable amount. The Keg GP Ltd. believes that there have been no declines in either the carrying value of the intangible assets in the Partnership or in the carrying value of the Fund's investment in the Partnership as of March 31, 2007.

CHANGE IN ACCOUNTING POLICY

Effective the commencement of its 2007 fiscal year, the Fund has adopted the Canadian Institute of Chartered Accountants (CICA) Handbook Section 1530, Comprehensive Income, Section 3251, Equity, Section 3855, Financial Instruments - Recognition and Measurement, Section 3861, Financial Instruments - Disclosure and Presentation, and Section 3865, Hedges. These new Handbook sections, which apply to fiscal years beginning on or after October 1, 2006, provide comprehensive requirements for the recognition and measurement of financial instruments, as well as standards on when and how hedge accounting may be applied. All financial assets and derivative financial instruments, except for those financial assets classified as held-to-maturity or loans and receivables, are measured at their fair values. Financial liabilities are measured at their fair values when they are classified as held for trading purposes. Otherwise, they are measured at amortized cost. Handbook Section 1530 also establishes standards for reporting and displaying comprehensive income.

The Fund has reviewed the impact of these new standards and determined that they do not have a significant impact on the consolidated financial statements in the current or prior quarters.

The Fund classifies its amount due KRL and the Partnership and the note receivable from KRL as loans and receivables which are carried at amortized cost. The Fund's interest and distributions payable and term loan are also carried at amortized cost. The requirement of the Fund to settle its note receivable from KRL in exchange for Class C Partnership units represents a derivative instrument. The Fund has reviewed the net impact of this potential exchange requirement on its cash flows and has determined there is no significant value applicable to this feature.

Amendments to CICA 1540, Cash Flow Statements, require entities to disclose total cash distributions on financial instruments classified as equity in accordance with a contractual agreement and the extent to which total cash distributions are non-discretionary. This disclosure requirement is effective for interim and annual financial statements for fiscal periods ending on or after March 31, 2007. The determination to declare and make payable distributions from the Fund are at the discretion of the board of Trustees of the Fund and, until declared payable by the Board of Trustees of the Fund, the Fund has no contractual requirement to pay cash distributions to unitholders' of the Fund. During the three month period ended March 31, 2007, \$2.2 million (three months ended March 31, 2006 - \$1.8 million) in cash distributions were declared payable by the Board of Trustees of the Fund and paid to unitholders.

FINANCIAL INSTRUMENTS

The Fund's financial instruments consist of cash, accounts receivable, note receivable, accounts payable and accrued liabilities, and the term loan. Due to the interrelationship between the note receivable from KRL and the Class C Partnership units held by KRL, it is not practicable to estimate the fair value of the note receivable with sufficient reliability. The Keg GP Ltd., as the general partner and administrator of the Fund, estimates that the fair value of these financial instruments approximate their carrying values. It is The Keg GP Ltd.'s opinion that the Fund is not exposed to significant interest rate or credit risk arising from these financial instruments.

OUTLOOK

Management of KRL has advised the Trustees that it intends to continue to focus on growing same store sales and to continue to expand the number of corporate and franchised restaurants in Canada and the United States. KRL management has also advised the Trustees that it believes that the strong same store sales growth KRL has delivered in the past will continue to be realized in the future through a combination of increased guest counts and increased guest average cheque. Advertising and promotions programs will continue to focus on food taste, quality and excellent service in a friendly atmosphere. Management of KRL has further advised the Trustees that it believes that continued Canadian market expansion will be leveraged by KRL's leading market position and national presence. Corporate market expansion in the United States will continue to focus on three target markets, specifically Phoenix, Arizona; Denver, Colorado; and Dallas, Texas. KRL management has advised the Trustees that it intends to aggressively pursue franchising opportunities in the United States.

KRL continues to refurbish, and in some cases, relocate existing Keg restaurants in order to better serve its guests and to protect and enhance the strong leadership position The Keg brand has enjoyed for over thirty-five years.

Management of KRL has advised the Trustees that it has revised the number of restaurants it expects to open in 2007, due to late turnover of the sites by landlords as a result of delays in both municipal approvals and site construction. Management of KRL has advised that it currently expects to add two new corporate and two new franchised restaurants, and to relocate two corporate and one franchised restaurant during 2007. Management of KRL has further advised the Trustees that it intends to open 30 new restaurants over the next ten years.

RISKS AND UNCERTAINTIES

The Fund continues to recognize certain risks and uncertainties associated with the ordinary course of business, including those associated with the business and operations of KRL, upon which the Fund relies solely for its income.

THE RESTAURANT INDUSTRY

The performance of the Fund is directly dependent upon the royalty and interest payments received from KRL. The amount of the royalty is dependent upon restaurant sales, which is subject to a number of factors that affect the restaurant industry generally, and the casual dining segment of the industry in particular. The casual dining segment of the restaurant industry is intensely competitive with respect to price, service, location and food quality. There are many well-established competitors, particularly in the United States with substantially greater financial and other resources than KRL. Competitors include national and regional chains, as well as individually owned restaurants. Recently, competition has increased in the mid-price, full-service, casual dining segment in which Keg restaurants operate. If KRL and the Keg franchisees are unable to successfully compete in the casual dining segment of the restaurant industry, sales may be adversely affected, the amount of the royalty reduced and the ability of KRL to pay the royalty or interest on the Keg Loan may be impaired. The restaurant business is also affected by changes in demographic trends, traffic patterns, and the type, number, and location of competing restaurants. In addition, factors such as inflation, increased food, labour and benefits costs, government regulations, smoking by-laws and the availability of experienced management and hourly employees may adversely affect the restaurant industry in general and therefore potentially KRL and its franchisees. Changing consumer preferences, discretionary spending patterns and factors affecting the availability of beef could force KRL to modify its restaurant content and menu and could result in a reduction of restaurant sales. Accordingly, this could impact the amount of the royalty and financial condition of KRL.

Consumer preferences could be affected by health concerns about the consumption of beef, the primary item served at Keg restaurants, and specific events such as the outbreak of “mad cow disease” could reduce the available supply of beef or significantly raise the price of beef. KRL’s success also depends on numerous factors affecting discretionary consumer spending including economic conditions, disposable consumer income and consumer confidence. Adverse changes in these factors could reduce guest traffic or impose practical limits on pricing, either of which could reduce restaurant sales and operating income, which could adversely affect the royalty and the ability of KRL to pay the royalty, the make-whole payment or interest on the Keg Loan.

AVAILABILITY AND QUALITY OF RAW MATERIALS

Management of KRL has advised the Trustees that it continues to monitor the situation regarding the cases of BSE found in North America during the past two years. The widespread testing of herds confirms these are isolated cases; the risk to human health appears to be negligible. Most importantly to The Keg, there has been no significant negative consumer reaction to beef in North America and there has not been a material impact on its restaurant traffic. KRL management has further advised the Trustees that KRL has maintained an uninterrupted supply of quality beef that meets its demanding specifications despite the border closures and the unfortunate impact on cattle producers. Management of KRL has advised the Trustees that it expects the demand for beef to remain strong among consumers and its supply to continue uninterrupted.

FLUCTUATIONS IN FOREIGN EXCHANGE RATES

KRL presently has 17 restaurants located in the United States, 16 of which are corporately owned through its wholly owned subsidiaries, and one of which is franchised. Keg restaurants located in the United States generate sales in United States dollars, which must be translated into their Canadian dollar equivalent for Fund reporting purposes. Fluctuations in foreign exchange rates will affect the Canadian dollar equivalent of the sales of the restaurants located in the United States, which will affect the amount of the royalty.

TAX STATUS

On October 31, 2006, the Department of Finance (Canada) announced the "Tax Fairness Plan" whereby the income tax rules applicable to publicly traded trusts and partnerships will be significantly modified. In particular, certain income of (and distributions made by) these entities will be taxed in a manner similar to income earned by (and distributions made by) a corporation. The application of these rules will be delayed to the 2011 taxation year with respect to trusts that were publicly traded prior to November 1, 2006 (although the announcement suggested that this transitional relief could be lost under certain circumstances, including the "undue expansion" of an income trust). On December 15, 2006, the Department of Finance (Canada) released guidance for income trusts and other flow-through entities that qualify for the four-year transitional relief. The guidance establishes objective tests with respect to how much an income trust is permitted to grow without jeopardizing its transitional relief. In general, the Fund will be permitted to issue new equity over the next four years equal to its market capitalization as of the end of trading on October 31, 2006 (subject to certain annual limits). Market capitalization, for these purposes, is to be measured in terms of the value of the Fund's issued and outstanding publicly traded units. If these limits are exceeded, the Fund may lose its transitional relief and thereby become immediately subject to the proposed rules. On December 21, 2006, the Department of Finance issued for public comment the draft legislation to implement these proposals. On March 29, 2007 the federal government tabled a bill in the House of Commons to implement the new tax on distributions from publicly traded trusts and partnerships. There is no assurance that the draft legislation will be enacted in the manner proposed or at all.

The Fund is considering these announcements and the possible impact of the proposed rules to the Fund. The proposed rules (including the guidance released on December 15, 2006) may adversely affect the marketability of the Fund's units and the ability of the Fund to undertake financings and acquisitions, and, at such time as the proposed rules apply to the Fund, the distributable cash of the Fund may be significantly reduced.

FORWARD LOOKING INFORMATION

The information provided in this report includes forward-looking statements with respect to business plans, activities and events anticipated by the Fund and the Fund's future results. Although the Fund believes the assumptions underlying such statements to be reasonable, any of the assumptions may prove to be inaccurate and, as a result, the forward-looking information may prove to be incorrect. The forward-looking information contained in this document is current only as of the date of this document. There should not be an expectation that such information will in all circumstances be updated, supplemented or revised whether as a result of new information, changing circumstances, future events or otherwise.

ADDITIONAL INFORMATION

Additional information about the Fund including the Fund's most recent annual information form is available on SEDAR at www.sedar.com.

UNITHOLDER INFORMATION

CORPORATE HEAD OFFICE

The Keg Royalties Income Fund
10100 Shellbridge Way
Richmond, BC V6X 2W7

BOARD OF TRUSTEES

C. C. Woodward
George Killy
George Tidball

BOARD OF DIRECTORS AND OFFICERS OF THE KEG GP LTD., THE GENERAL PARTNER OF THE KEG RIGHTS LIMITED PARTNERSHIP

C. C. Woodward*
Chairman and Director
David Aisenstat
President and Director
Neil Maclean
Secretary, Treasurer and Director
George Killy*
Director
George Tidball*
Director

* Audit Committee and Governance Committee Member

REGISTRAR AND TRANSFER AGENT

Computershare Trust Company of Canada

STOCK EXCHANGE LISTING

Toronto Stock Exchange: KEG.UN

INVESTOR ENQUIRIES

Karyn Byrne
Investor Relations Manager
Telephone: (416) 646-4960
Facsimile: (416) 695-2401
E-mail: karynb@kegrestaurants.com
Website: www.kegincomefund.com

THE KEG ROYALTIES INCOME FUND

CONSOLIDATED
FINANCIAL STATEMENTS
For the three months ended March 31, 2007 and 2006

CONSOLIDATED BALANCE SHEETS

(Expressed in thousands of dollars)

	March 31, 2007 (unaudited)	December 31, 2006
ASSETS		
Current assets:		
Cash	\$ 935	\$ 562
Due from Keg Restaurants Ltd. (note 5)	363	363
Due from The Keg Rights Limited Partnership (note 6)	<u>262</u>	<u>1,216</u>
	1,560	2,141
Note receivable from Keg Restaurants Ltd.	57,000	57,000
Investment in The Keg Rights Limited Partnership (note 3)	<u>57,394</u>	<u>47,359</u>
	<u>\$ 115,954</u>	<u>\$ 106,500</u>
LIABILITIES AND UNITHOLDERS' EQUITY		
Current liabilities:		
Interest payable on term loan	\$ 77	\$ 77
Distributions payable to Fund unitholders	<u>-</u>	<u>866</u>
	77	943
Term loan, net of \$75 deferred financing charges (December 31, 2006 - \$80)	13,925	13,920
Unitholders' equity:		
Capital contributions (note 7(a))	100,014	90,946
Retained earnings	<u>1,938</u>	<u>691</u>
	<u>101,952</u>	<u>91,637</u>
	<u>\$ 115,954</u>	<u>\$ 106,500</u>

See accompanying notes to consolidated financial statements.

Approved on behalf of the Board of Trustees

"C.C. Woodward"
C.C. Woodward, Trustee

"George Tidball"
George Tidball, Trustee

CONSOLIDATED STATEMENTS OF EARNINGS AND COMPREHENSIVE INCOME

(Expressed in thousands of dollars, except unit and per unit amounts - unaudited)

	January 1 to March 31, <u>2007</u>	January 1 to March 31, <u>2006</u>
Gross sales reported by Keg restaurants in the Royalty Pool (note 3)	\$ <u>105,239</u>	\$ <u>93,957</u>
Revenue:		
Equity income (note 3)	\$ 2,232	\$ 1,800
Interest income	<u>1,061</u>	<u>1,056</u>
	3,293	2,856
Expenses:		
Interest and financing fees	224	199
Amortization of deferred financing charges	<u>5</u>	<u>6</u>
	<u>229</u>	<u>205</u>
Net earnings and comprehensive income for the period	\$ <u>3,064</u>	\$ <u>2,651</u>
Weighted average units outstanding (note 7(a))	<u>9,327,944</u>	<u>8,569,611</u>
Basic and diluted earnings per unit	\$ <u>0.33</u>	\$ <u>0.31</u>

CONSOLIDATED STATEMENTS OF RETAINED EARNINGS

(Expressed in thousands of dollars - unaudited)

	January 1 to March 31, <u>2007</u>	January 1 to March 31, <u>2006</u>
Retained earnings, beginning of period.....	\$ 691	\$ 139
Net earnings	3,064	2,651
Distributions declared to Fund unitholders	<u>(1,817)</u>	<u>(1,603)</u>
Retained earnings, end of period.....	\$ <u>1,938</u>	\$ <u>1,187</u>

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Expressed in thousands of dollars - unaudited)

	January 1 to March 31, 2007	January 1 to March 31, 2006
Cash provided by (used for):		
OPERATIONS:		
Net earnings for the period	\$ 3,064	\$ 2,651
Items not involving cash:		
Amortization of deferred financing charges	5	6
Equity income (note 3)	(2,232)	(1,800)
Distributions from The Keg Rights Limited Partnership	1,264	1,022
Change in non-cash operating working capital (note 8(a))	954	449
	3,055	2,328
FINANCING:		
Distributions paid to Fund unitholders	(2,682)	(2,374)
Increase (decrease) in cash.....	373	(46)
Cash, beginning of period	562	185
Cash, end of period	\$ 935	\$ 139

See note 8(b) for supplementary cash flow information.

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Tabular amounts expressed in thousands of dollars - unaudited)

For the three months ended March 31, 2007 and 2006

1. BASIS OF PRESENTATION:

The Keg Royalties Income Fund (the "Fund") prepares its interim consolidated financial statements in accordance with Canadian generally accepted accounting principles on a basis consistent with those used and described in the annual consolidated financial statements for the year ended December 31, 2006. The disclosures contained in these interim consolidated financial statements do not include all the requirements of Canadian generally accepted accounting principles for annual financial statements.

These interim consolidated financial statements should be read in conjunction with the annual consolidated financial statements for the year ended December 31, 2006.

2. CHANGE IN ACCOUNTING POLICY:

- (a) Effective the commencement of its 2007 fiscal year, the Fund has adopted the Canadian Institute of Chartered Accountants (CICA) Handbook Section 1530, Comprehensive Income, Section 3251, Equity, Section 3855, Financial Instruments - Recognition and Measurement, Section 3861, Financial Instruments - Disclosure and Presentation, and Section 3865, Hedges. These new Handbook sections, which apply to fiscal years beginning on or after October 1, 2006, provide comprehensive requirements for the recognition and measurement of financial instruments, as well as standards on when and how hedge accounting may be applied. All financial assets and derivative financial instruments, except for those financial assets classified as held-to-maturity or loans and receivables, are measured at their fair values. Financial liabilities are measured at their fair values when they are classified as held for trading purposes. Otherwise, they are measured at amortized cost. Handbook Section 1530 also establishes standards for reporting and displaying comprehensive income.

The Fund has reviewed the impact of these new standards and determined that they do not have a significant impact on the consolidated financial statements in the current or prior quarters.

The Fund classifies its amount due from Keg Restaurants Ltd. ("KRL") and The Keg Rights Limited Partnership (the "Partnership") and the note receivable from KRL as loans and receivables which are carried at amortized cost. The Fund's interest and distributions payable and term loan are also carried at amortized cost. The requirement of the Fund to settle its note receivable from KRL in exchange for Class C Partnership units represents a derivative instrument. The Fund has reviewed the net impact of this potential exchange requirement on its cash flows and has determined there is no significant value applicable to this feature.

- (b) Amendments to CICA 1540, Cash Flow Statements, require entities to disclose total cash distributions on financial instruments classified as equity in accordance with a contractual agreement and the extent to which total cash distributions are non-discretionary. This disclosure requirement is effective for interim and annual financial statements for fiscal periods ending on or after March 31, 2007. The determination to declare and make payable distributions from the Fund are at the discretion of the board of Trustees of the Fund and, until declared payable by the Board of Trustees of the Fund, the Fund has no contractual requirement to pay cash distributions to unitholders' of the Fund. During the three month period ended March 31, 2007, \$2.2 million (three months ended March 31, 2006 - \$1.8 million) in cash distributions were declared payable by the Board of Trustees of the Fund and paid to unitholders.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Tabular amounts expressed in thousands of dollars - unaudited)

For the three months ended March 31, 2007 and 2006

3. EQUITY INVESTMENT:

	March 31, <u>2007</u>	December 31, <u>2006</u>
Investment in the Partnership, at cost	\$ 56,669	\$ 47,601
Accumulated equity earnings less distributions received, beginning of period	(243)	(238)
Equity income in the Partnership	2,232	7,335
Distributions from the Partnership	<u>(1,264)</u>	<u>(7,339)</u>
Equity investment in the Partnership	<u>\$ 57,394</u>	<u>\$ 47,359</u>

The Partnership owns the trademarks, trade names, operating procedures and systems and other intellectual property (collectively, the “Keg Rights”) used in connection with the operation of Keg steakhouse restaurants and bars.

The Fund, through its ownership of The Keg Holdings Trust (“KHT”), holds all of the issued and outstanding Limited Partnership units (“LP units”), 900,000 Class B units and 99% of the General Partnership units (“GP units”) of the Partnership through its 90% interest in The Keg GP Ltd.

Summarized financial information of the Partnership is as follows:

	March 31, <u>2007</u>	December 31, <u>2006</u>
Current assets	\$ 1,895	\$ 2,097
Long-term assets, being Keg Rights	<u>134,067</u>	<u>129,297</u>
Total assets	<u>\$ 135,962</u>	<u>\$ 131,394</u>
Current liabilities	\$ 539	\$ 2,385
Partners’ equity	<u>135,423</u>	<u>129,009</u>
Total liabilities and equity	<u>\$ 135,962</u>	<u>\$ 131,394</u>

	January 1 to March 31, <u>2007</u>	January 1 to March 31, <u>2006</u>
System sales reported by Keg restaurants in the Royalty Pool	<u>\$ 105,239</u>	<u>\$ 93,957</u>
Royalty income at 4% of system sales reported above	\$ 4,210	\$ 3,758
Make-whole payment, based on 4% of lost system sales	<u>50</u>	<u>3</u>
Total royalty income	4,260	3,761
Expenses	<u>(102)</u>	<u>(138)</u>
Net earnings of the Partnership for the period	4,158	3,623
KRL’s interest in the net earnings of the Partnership.....	<u>(1,926)</u>	<u>(1,823)</u>
Equity income for the period	<u>\$ 2,232</u>	<u>\$ 1,800</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Tabular amounts expressed in thousands of dollars, except unit and per unit amounts - unaudited)

For the three months ended March 31, 2007 and 2006

3. EQUITY INVESTMENT (CONTINUED):

The gross sales reported by the 95 Keg restaurants on which KRL pays a royalty to the Partnership (the "Royalty Pool") are from January 1 to March 31, 2007 (January 1 to March 31, 2006 – 91 Keg restaurants).

On January 1, 2007, six new Keg restaurants that opened during the period from October 3, 2005 to October 2, 2006 were added to the Royalty Pool. The gross sales of these six new restaurants have been estimated at \$28.0 million annually. Two permanently closed Keg restaurants with annual sales of \$5.7 million have been removed from the Royalty Pool, resulting in an estimated net increase in Royalty Pool sales of \$22.3 million annually.

The royalty payment from KRL to the Partnership is four percent of system sales for such period reported by Keg restaurants in the Royalty Pool plus a make-whole payment, if required by a restaurant closure, based on four percent of lost system sales. System sales for any period and for any Keg restaurant located in Canada and the United States, as defined in the Licence and Royalty Agreement, means the gross sales by such Keg restaurants for such period. The make-whole payment is based on three restaurant closures for the period from January 1 to March 31, 2007 (January 1 to March 31, 2006 – one restaurant closure).

4. UNITHOLDER DISTRIBUTIONS:

	January 1 to March 31, <u>2007</u>	January 1 to March 31, <u>2006</u>
Distributions declared to Fund unitholders	\$ <u>1,816</u>	\$ <u>1,603</u>
Weighted average Fund units outstanding (note 7(a)).....	<u>9,327,944</u>	<u>8,569,611</u>
Weighted average distributions declared per unit	\$ <u>0.19</u>	\$ <u>0.19</u>

Annually, two distributions are expected to be declared during the first quarter, three distributions in each of the second and third quarters and four distributions in the fourth quarter. This is done to ensure that the distribution based on December KRL Royalty Pool system sales, which is paid the following month in January, is recorded in the period it was earned for income tax purposes.

5. DUE FROM KEG RESTAURANTS LTD.:

	March 31, <u>2007</u>	December 31, <u>2006</u>
Interest on note receivable from Keg Restaurants Ltd.	\$ <u>363</u>	\$ <u>363</u>

The above amounts were received when due from KRL subsequent to the end of the above periods to facilitate the following month's distribution to Fund unitholders.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Tabular amounts expressed in thousands of dollars - unaudited)

For the three months ended March 31, 2007 and 2006

6. DUE FROM THE KEG RIGHTS LIMITED PARTNERSHIP:

The amounts due from the Partnership are working capital items owing to the Fund or its subsidiaries and are in the normal course of operations.

7. UNITHOLDERS' EQUITY:

(a) Fund units:

On May 31, 2002, the Fund issued 8,153,500 Fund units at \$10.00 per unit pursuant to a public underwriting. Expenses of the offering amounted to \$2,150,000 and were charged to unitholders' equity.

On July 4, 2005, the Fund issued 250,000 Fund units to KRL in exchange for 250,000 Class B units. The fair value of these units was approximately \$13.25 which resulted in an additional \$3,312,500 recorded as unitholders' equity. Thereafter, on July 6, 2005, KRL sold these 250,000 Fund units through the facilities of the Toronto Stock Exchange.

On March 9, 2006, the Fund issued 650,000 Fund units to KRL in exchange for 650,000 Class B units. The fair value of these units was approximately \$12.69 which resulted in an additional \$8,248,500 recorded as unitholders' equity. Thereafter, on March 14, 2006, KRL sold these 650,000 Fund units through the facilities of the Toronto Stock Exchange.

On February 22, 2007, the Fund issued 650,000 Fund units to KRL in exchange for 650,000 Class B units. The fair value of these units was approximately \$13.95 which resulted in an additional \$9,067,500 recorded as unitholders' equity. Thereafter, on February 23, 2007, KRL sold these 650,000 Fund units through the facilities of the Toronto Stock Exchange.

The declaration of trust of the Fund provides that an unlimited number of Fund units may be issued. Each Fund unit is transferable and represents an equal undivided beneficial interest in any distributions of the Fund and in the net assets of the Fund. All units have equal rights and privileges. Each Fund unit entitles the holder thereof to participate equally in the allocations and distributions and to one vote at all meetings of Fund unitholders for each whole Fund unit held. The Fund units issued are not subject to future calls or assessments.

Fund units are redeemable at any time at the option of the holder at a price based on market value as defined in the trust agreement, subject to a maximum of \$50,000 in cash redemptions by the Fund in any one month. The limitation may be waived at the discretion of the Trustees of the Fund. Redemption in excess of these amounts, assuming no waiving of the limitation, shall be paid by way of a pro-rata distribution of Partnership securities held by the Fund.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Tabular amounts expressed in thousands of dollars, except unit amounts - unaudited)

For the three months ended March 31, 2007 and 2006

7. UNITHOLDERS' EQUITY (CONTINUED):

(b) Exchangeable Partnership units:

	March 31, <u>2007</u>	December 31, <u>2006</u>
Class A Partnership units (i)	905,944	905,944
Class B Partnership units (ii)	<u>1,530,840</u>	<u>1,589,280</u>
	<u>2,436,784</u>	<u>2,495,224</u>

Pursuant to the declaration of trust, the holders (other than the Fund or its subsidiaries) of the Class A units and Class B units of the Partnership are entitled to vote in all votes of Fund unitholders as if they were holders of the number of Fund units they would receive if Class A units and entitled Class B units were exchanged into Fund units as of the record date of such votes, and will be treated in all respects as Fund unitholders for the purpose of any such votes.

- (i) The Class A units are entitled to a preferential proportionate distribution equal to the distribution on the Class C Partnership units, multiplied by the number of Class A units divided by the number of LP units issued and outstanding. KHT holds all of the 8,153,500 LP units issued and outstanding at March 31, 2007. In addition, the Class A units receive a residual distribution proportionately with the Class B units, LP units and GP units relative to the aggregate number of each class issued and outstanding (or in the case of the Class B units, the number issued and outstanding multiplied by the Class B current distribution entitlement). Class A units are exchangeable for Fund units on the basis of one Fund unit for one Class A unit.
- (ii) The Class B units are entitled to a preferential proportionate distribution and a residual distribution based on the incremental royalty paid to the Partnership from new Keg restaurants. The distribution entitlements of the Class B units are adjusted annually on January 1. Class B units held by KRL are exchangeable for Fund units based upon a defined calculation that itself is based on system sales from new restaurants. As at March 31, 2007, 1,530,840 (December 31, 2006 – 1,589,280) Class B units held by KRL receive a distribution entitlement.

In addition to these exchangeable Class B units, KRL also holds 295,860 (December 31, 2006 – 887,420) Class B units which are not yet entitled to receive distributions and are not exchangeable for Fund units.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Tabular amounts expressed in thousands of dollars - unaudited)

For the three months ended March 31, 2007 and 2006

8. SUPPLEMENTARY CASH FLOW INFORMATION:

	January 1 to March 31, <u>2007</u>	January 1 to March 31, <u>2006</u>
(a) Change in non-cash operating working capital:		
Due from The Keg Rights Limited Partnership	\$ 954	\$ 443
Interest payable on term loan	<u>-</u>	<u>6</u>
	<u>\$ 954</u>	<u>\$ 449</u>
(b) Supplementary information:		
Interest received	\$ 1,061	\$ 1,056
Interest paid	224	193
Non-cash transactions:		
Issuance of Fund units to acquire additional interest in the Partnership ..	9,068	8,249