# CITADEL

## Group of Funds

**2000 ANNUAL REPORT**

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# MESSAGE TO UNITHOLDERS

**Dear Unitholder,**

The year 2000 was a very successful year for unitholders of the Citadel Group of Funds and it is therefore with great pleasure that I present our Annual Report to you for review. This year we are presenting our report in a combined form, including reports on Citadel Diversified Investment Trust, Citadel S-1 Income Trust Fund and Citadel HYTES Fund.

## Our Commitment

Management of the Citadel Group of Funds is committed to providing its unitholders with quality income products. Within this context, we are also committed to capturing incremental value for our unitholders through capital appreciation.

In 2000, this was accomplished for Citadel Diversified through:

- Effective weighting of our portfolio by our portfolio manager, Bloom Investment Counsel, Inc., throughout the improving income fund market in 2000,
- Effective and significant use of leverage during the first six months of the year, and
- Completion of our properly timed rights offering in June.

For Citadel S-1, this was accomplished through:

- Innovative structuring of Citadel S-1's investment guidelines, designed to ensure that a Standard & Poor's S-1 Stability Rating is awarded to and maintained by the Fund,
- Timing of our Citadel S-1 offering in September 2000, and
- Effective deployment of capital by Bloom Investment Counsel, Inc., in assembling a high quality portfolio of income funds and investment grade debt securities at attractive prices.

In March 2001, we launched the Citadel HYTES Fund offering and closed that offering on April 11, 2001 raising $125,000,000. Citadel HYTES has been structured to provide a high tax-deferred yield of 12.5% per annum. We expect Citadel HYTES Fund to be another top performing income fund in the Citadel Group of Funds and we look forward to reporting to you on that Fund's success in the near future.

For 2001, we will continue to seek ways to enhance unitholder value without impairing our primary focus on maintaining the quality of each of the Funds within the Citadel Group of Funds.

## Outlook for Distributions

Citadel Diversified distributed $1.067 per unit for 2000 tax purposes, slightly more than the $1.05 per unit that we reported last year as being anticipated for 2000. For 2001, we are anticipating another solid year with distributions expected to be between $1.05 and $1.10 per unit.

Citadel S-1 made its first distribution of $0.208 per unit on schedule in December of last year. Citadel S-1 is designed to be the most stable of our income funds. With the Citadel S-1 portfolio now substantially invested, we are confident that distributions for 2001 will be in excess of the fixed annual distribution rate of $2.50 per unit.

Citadel HYTES is scheduled to commence its distributions with the June 30, 2001 record date. Citadel HYTES distributions have been set in advance at $0.26 per unit per month ($3.12 per annum).

Please take the time to review this report in its entirety. We encourage you to discuss any questions you may have with your investment advisor or to call us directly. We thank you for your continued support and confidence.

Citadel Group of Funds
James T. Bruvall, Chief Executive Officer
April 19, 2001

# REPORT OF THE INVESTMENT MANAGER

## Overview

As mentioned in last year's report to unitholders, year 2000 started out well for capital gain seekers in the market, but weak for the income sector. The weakness in the income sector was caused by higher interest rates and money moving out of income oriented investments into capital oriented investments, most particularly technology, media and telecommunication ("TMT") investments. The March 2000 peak for the Toronto Stock Exchange 300 Index ("TSE 300"), which coincided with the peak in the TMT market mania, also coincided with the commencement of a strong revival in the income sector of the market. During the first two months of 2000 the benchmark index for the income fund sector, the Scotia Capital Markets Income Fund Index, declined a sharp 7.2%, but during the following ten months that index rose by an exceptionally strong 42.3%.

Aside from general market psychology and flow of funds, there are two main factors that have a significant influence on income funds: interest rates and commodity prices. Between November 1999 and May 2000, the Bank of Canada rate was increased 1.50% in four increments. During the same period, the prices of crude oil and natural gas were trending upward. It was in this atmosphere of opposing influences that we closed last year's report with the following statement, "We believe that the total return outlook for the rest of this year will be quite rewarding for income trust investors". This outlook was certainly correct!

## Oil & Gas Royalty Trusts

The spot price for West Texas Intermediate crude oil showed little change for year end 2000 compared to year end 1999 (US$26.80 per barrel versus US$26.60 per barrel). Throughout 2000, however, there was tremendous volatility with prices ranging between $23.90 and $37.40 per barrel. The average price for the year was $30.30 per barrel. In contrast, Alberta natural gas prices climbed steadily from about $2.50 per mcf in January to about $7.00 per mcf in October before spiking up to $13.00 per mcf by year end. These higher energy prices provided substantially increased cash flow to the royalty trusts, enabling them to significantly increase their distributions to unitholders. This was achieved despite many trusts withholding 20% to 30% of their cash flow to reduce their debt and improve their balance sheets. Additionally, most royalty trusts were active acquirers of properties and operating companies, which provided growth to their reserves, production, market capitalization and cash flow. Within Citadel Diversified's portfolio, Shiningbank Energy was the top performing royalty trust, and our royalty trust holdings as a group provided total returns (capital growth plus distributions) ranging from 44% to 85%, with the capital growth element ranging from 22% to 60%.

## Real Estate Investment Trusts ("Reits")

Throughout 2000, most Reits kept their distributions unchanged, but managed to decrease their pay out ratios, being the ratio of distributions to cashflow. Most Reits successfully managed their portfolios, adding new holdings, trimming non-core properties, maintaining or improving occupancy rates and improving cash flow during the year. As interest rates started to soften in the latter part of 2000, Reit unit prices started to perform better. The best performers in Citadel Diversified's portfolio were H&R Reit with a total return for the year of 22.8% (12.3% capital) and Cominar with a total return of 23.2% (11.5% capital). RioCan Reit, a trust that improved in quality over the last year, was the only new investment added to our Reit holdings during the year.

## Income Funds

Moves in interest rates and market psychology are two of the main factors which influence the performance of income funds, which is why with few exceptions, income funds had a poor start to the year. Due to the diversity of the businesses involved, the performance of each trust is more dependent on the internal dynamics of each trust. Hence, in any given period of time there is a wide range of market movement within this area. Citadel Diversified's portfolio performance received a significant contribution from Halterm Income Fund. This trust delivered a total return of 89.6% (68.5% capital) for 2000. Koch Pipelines, with improving throughputs and an investment in a new pipeline project, produced a total return of 29.8% (16.3% capital). Superior Propane, following court approval of the ICG merger, delivered a total return of 24.3% (14.2% capital), and TimberWest

which continued to produce good results within a difficult market for lumber and logs delivered a total return of 25.5% (14.2% capital).

Two income trusts, Direct Energy and Western Facilities sold their assets and distributed the capital to the unitholders during the year. Just before year end a third trust held by Citadel Diversified, FACS Record Storage, announced their intention to sell their assets and distribute the proceeds to unitholders. This occurred on its wind up in February 2001.

### Canadian Originated Preferred Securities (COPrS)

The market price of COPrS, as fixed income investments, is influenced by movements in interest rates. Fortunately we were able to purchase the majority of our desired holdings in Citadel S-1 before many of these instruments appreciated above their $25.00 par level when interest rates started to decline towards the end of year. With interest rates projected to remain relatively stable, COPrS prices are also predicted to remain firm throughout the year.

### Citadel Diversified Investment Trust

The year 2000 was very rewarding for Citadel Diversified and its unitholders. On a net asset value basis, inclusive of distributions, Citadel Diversified had a total return of 23.5%. Based on the market price appreciation plus distributions, the total return for the year was 37.2%. These returns do not include any benefit from participation in the Fund's June 2000 rights issue that was highly rewarding for those who participated. By comparison, the total return of the Toronto Stock Exchange 300 Index during this past year was 7.4%.

### Citadel S-1 Income Trust Fund

The inception of Citadel S-1 in early October coincided with a period of generally rising prices for income trusts. Higher commodity prices, the expectation of lower interest rates and the return of money from the TMT segment of the stock market produced a buoyant atmosphere for the income trusts.

Following the selective investment of the funds received, Standard & Poor's confirmed the Fund's S-1 Stability Rating and the Fund's net asset value increased by 4.5% from inception to year end. From a market value perspective, the units closed the year at $26.25 producing a 5.0% capital appreciation and a total return of 6.0%. During this same time period, the TSE 300 Index generated a total negative return of 17.6%.

### Citadel HYTES Fund

On April 11, we closed the Citadel HYTES Fund. We look forward to the challenge of assembling a portfolio over the coming weeks which provides both the targeted yield of over 12.5% per annum and the stability which will help to insure the preservation of capital.

### Outlook

As this current year has progressed, the forecast of lower interest rates has also progressed. To date, the U.S. Federal Reserve Bank has reduced its discount rate by 2.0% in four 0.5% moves, the latest occurring this week. The Bank of Canada has responded, in a less aggressive manner, by lowering its rate by 0.25% in January, 0.5% in March, and 0.25% earlier this week. This has provided a further and ongoing impetus to the rally in the income fund sector with several trusts now trading in single digit yield territory. We believe that this year will provide solid investment returns, but that these will only be achieved by utilizing a selective approach to the sector.

M. Paul Bloom
President, Bloom Investment Counsel, Inc.
April 19, 2001

## ADMINISTRATORS

Each Fund within the Citadel Group of Funds is managed by the same management team and Board of Directors. Citadel Diversified Management Ltd. ("CDML") is the administrator for Citadel Diversified Investment Trust, while Citadel S1 Management Ltd. ("CSML") is the administrator for Citadel S-1 Income Trust Fund. For our newest Fund, Citadel HYTES Fund, the administrator is Citadel TEF Management Ltd ("CTEF"). CDML, CSML and CTEF provide administrative services to their respective Fund and carry out all of the day to day operations of each Fund, other than investment advisory and portfolio management activities. The directors and officers of CDML, CSML and CTEF are as follows:

**Harold P. Milavsky**
Chairman of the Board
Calgary

**Kent J. MacIntyre**
Director
Calgary

**John M. MacLeod**
Director
Calgary

**Paul L. Waitzer**
Director
Toronto

**James T. Bruvall**
Director and Chief Executive Officer
Calgary

**Darren K. Duncan**
Chief Financial Officer
Calgary

## INVESTMENT MANAGER

Bloom Investment Counsel, Inc. ("Bloom") is the investment advisor and portfolio manager for each Fund in the Citadel Group of Funds. Bloom is responsible for implementing each Fund's investment strategy and determines the ongoing commodity, industry and geographic weighting of securities in each Fund's portfolio. In accordance with Bloom's active management philosophy, Bloom continually reviews each Fund's portfolio to ensure that the portfolio meets the investment guidelines of the Fund, while balancing the sometimes divergent goals of delivering income and protecting capital.

Bloom Investment Counsel, Inc. commenced business in 1985 and specializes in the management of segregated investment portfolios for wealthy individuals, their retirement plans, corporations and trusts.

The principal officers and consultants of Bloom which provide investment advisory, research and portfolio management services to the Funds are as follows:

**M. Paul Bloom**
President, Bloom Investment Counsel, Inc.

**Maurice G. Corbett**
Vice-President, Bloom Investment Counsel, Inc.

**Sara Bloom**
Vice-President, Bloom Investment Counsel, Inc.

# CITADEL DIVERSIFIED INVESTMENT TRUST

Citadel Diversified Investment Trust (the "Fund" or "Citadel Diversified") is a closed-end investment trust listed on The Toronto Stock Exchange under the symbol "CTD.un". The Fund has a termination date of December 31, 2007. Citadel Diversified's investment objectives are to provide its unitholders with a high level of monthly distributions and to maximize the net asset value of the Fund over its life. In order to achieve these objectives, the Fund's investment manager, Bloom Investment Counsel, Inc., actively manages a diversified portfolio of oil & gas royalty trusts, real estate investment trusts, income funds and qualified limited partnerships.

Pursuant to the Fund's distribution policy, Citadel Diversified pays monthly cash distributions equal to the cash distributions received in the prior month less estimated expenses and any taxes payable by the Fund. Citadel Diversified paid total monthly distributions for tax purposes during 2000 of $1.067 per unit, which represented a pre-tax yield of 12.6% (11.0% after-tax) based upon the December 31, 2000 closing price of $8.50 per unit. Total distributions paid since Citadel Diversified's inception in September 1997 to April 2001 have been $3.051 per unit, and based on the April 19, 2001 unit price of $9.00, this represents a total compounded rate of return of 10.3% per year on a highly tax-deferred basis.

**Investment Highlights:**

| | Q4 2000 | Q3 2000 | Q2 2000 | Q1 2000 | Q4 1999 |
|---|---|---|---|---|---|
| Net Asset Value per Unit | $ 8.46 | $ 8.34 | $ 7.95 | $ 7.32 | $ 7.70 |
| Market Price per Unit | $ 8.50 | $ 8.35 | $ 7.30 | $ 7.00 | $ 7.10 |
| Trading Premium / (Discount) | 0.5% | 0.1% | (8.2%) | (4.4%) | (7.8%) |
| Quarterly Distributions per Unit | $ 0.301 | $ 0.260 | $ 0.240 | $ 0.266 | $ 0.278 |
| Trailing Yield | 12.6% | 12.5% | 14.3% | 14.8% | 14.1% |
| Market Capitalization ($ millions) | $ 104.4 | $ 102.6 | $ 89.4 | $ 69.2 | $ 70.3 |

| | |
|---|---|
| **Stock Symbol:** | **CTD.un (TSE)** |
| **2000 High / Low:** | **$8.75 - $6.65** |
| **2000 Distribution:** | **$1.067** |
| **2000 Tax-Deferred %:** | **73.9%** |
| **2000 Total Return:** | **37.2%** |

# MANAGEMENT DISCUSSION & ANALYSIS

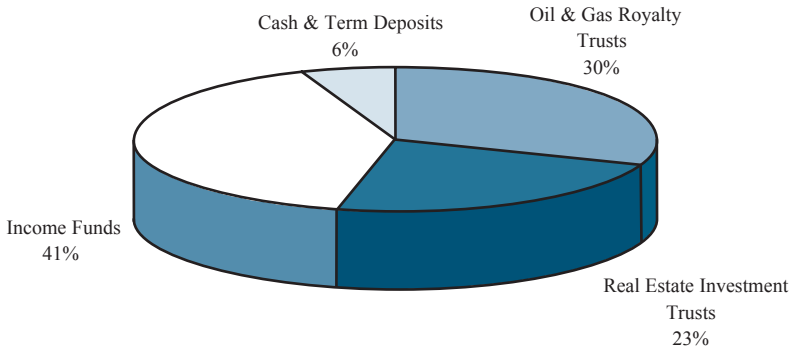
## Investment Activity

Despite the overall weakness in the income fund sector at the beginning of 2000, the sector gradually showed improved market valuations as the year progressed. The Fund capitalized on the improving market by first increasing its debt level to $8.0 million during the first half of the year and then completing a rights offering in June 2000. The Fund used the capital raised to take advantage of the many undervalued trusts in the sector.

The net proceeds of $16.9 million from the rights offering were used to fully repay the Fund's loan facility of $8.0 million, with the balance invested across the spectrum of oil & gas royalty trusts, real estate investment trusts and various income funds. At year end and presently, Citadel Diversified carries no debt, but may borrow up to 25% of the total asset value of the Fund if the investment manager sees opportunities to use debt to enhance the Fund's net asset value.

As at December 31, 2000, the Fund's portfolio (based on market values) is shown in the chart below.

## Fund Portfolio




## Financial Results

Citadel Diversified's total income for 2000 continued to show strong growth with a 22% increase over 1999. Total income rose from $10.3 million in 1999 to $12.5 million in 2000, as a result of improved distribution income from its portfolio and the additional capital invested from the rights offering during the last half of 2000. Administrative and investment manager fees increased to $1.6 million in 2000 from $1.2 million in 1999 as a result of a higher average net asset value enjoyed by the Fund during the past year. These fees represent 1.5% of the net asset value of the Fund and are payable in units. General and administrative costs, along with debt servicing costs, in 2000 remained fairly consistent with those incurred in 1999.

Net investment income and net investment income per unit also improved significantly from $8.5 million and $0.86 per unit in 1999 to $10.3 million and $0.93 per unit in 2000 respectively. This improvement translated into an increase in distributions reported for tax purposes from $1.000 in 1999 to $1.067 in 2000. Distributions were 73.9% tax-deferred in 2000 compared to 82.8% in 1999. This increase in taxability occurred as a result of an increase in the taxability of distributions from the issuers within the Fund's portfolio.

Improved market valuations of the underlying portfolio were reflected in the Fund’s net asset value per unit, which ended the year at $8.46 per unit compared to $7.70 per unit at year end 1999. The improved net asset value, combined with the positive operating results, provided an impetus for a significant rise in the Fund’s

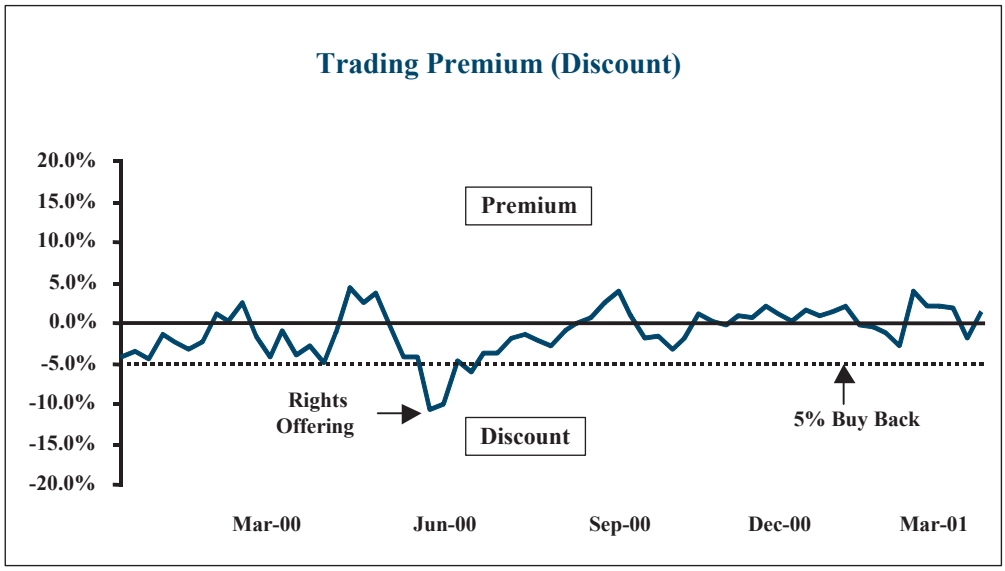
market price. Citadel Diversified's market price rose from $7.10 per unit at December 31, 1999 to $8.50 per unit at December 31, 2000, representing a total unitholder return (inclusive of distributions) of 37.2% for 2000. Comparatively, the Scotia Capital Markets composite index provided a total return of 32.1%, while the TSE 300 index recorded a 7.4% total return.

### Trading Premium / Discount to Net Asset Value

During 2000, the Fund repurchased for cancellation 274,700 units (1999 – 292,300 units) under the mandatory repurchase program. Of the total repurchased in 2000, 94% of the units were repurchased during Citadel Diversified's discounted rights offering, as the Fund's unit price experienced some market weakness.

Under the mandatory repurchase program, the Fund is obligated to repurchase units offered for sale at a discount to net asset value of greater than 5%. Citadel Diversified's average discount to net asset value during 2000 was 1.46%. At December 31, 2000 Citadel Diversified's net asset value and market price were $8.46 per unit and $8.50 per unit respectively, reflecting a slight premium to net asset value.

The mandatory repurchase program continues to provide unitholders liquidity while maintaining a narrow discount to net asset value, as the graph below demonstrates. The only exception to this occurred during Citadel Diversified's discounted rights offering in June 2000, where the market price came under some temporary weakness before rebounding back to normal narrow discount levels.




### Rights Offering

On May 29, 2000, Citadel Diversified announced a rights offering whereby each unitholder of record on June 7, 2000 was issued a right to subscribe for trust units. Four rights entitled the unitholder to purchase one trust unit at a price of $7.00 per trust unit.

The rights offering, which closed on June 30, 2000, was fully subscribed, resulting in the issuance of an additional 2.5 million units for gross proceeds of $17.3 million. The proceeds of the offering were used to repay indebtedness outstanding under the Fund's loan facility and enhance the Fund's existing portfolio.

## Outlook for 2001

Year 2000 was an extremely positive period for the income trust sector as the shift in investor attitudes created renewed demand for income yielding products such as Citadel Diversified. Continued strong commodity prices and stable to declining interest rates provided great fundamentals for the income trust sector. Although Canada will undoubtedly feel the effects of a slowing economy, we feel that distributions from Citadel Diversified's portfolio should remain strong in 2001. Citadel Diversified's net asset value has continued to climb, from $8.46 at year end to $9.21 as at April 19, 2001.

Based upon the Fund's current portfolio and analysts' estimates of distributions from the portfolio, Citadel Diversified's fiscal 2001 distributions are estimated to be in the $1.05 - $1.10 range per unit with approximately 65% - 70% of those distributions being tax deferred. Using Citadel Diversified's market price of $9.00 per unit as at April 19, 2001, the forecast distributions generate a highly diversified tax advantaged yield of approximately 12%.

## MANAGEMENT'S RESPONSIBILITY STATEMENT

The financial statements of Citadel Diversified Investment Trust have been prepared by Citadel Diversified Management Ltd ("CDML") and approved by the Board of Directors of CDML. CDML is responsible for the information and representations contained in these financial statements and the other sections of the annual report.

CDML maintains appropriate procedures to ensure that relevant and reliable financial information is produced. These statements have been prepared in accordance with accounting principles generally accepted in Canada and include certain amounts that are based on estimates and judgements. The significant accounting policies applicable to the Fund are described in Note 2 to the financial statements.

The Board of Directors of CDML is responsible for ensuring that management fulfills its responsibilities for financial reporting and has reviewed and approved these financial statements. The Board carries out this responsibility through the Audit Committee, which is comprised of the independent directors of the Board.

CDML, with the approval of its Board of Directors, has appointed the external audit firm of PricewaterhouseCoopers LLP. They have audited the financial statements in accordance with Canadian generally accepted auditing standards to enable them to express to unitholders their opinion on the financial statements. The auditors have full and unrestricted access to the Audit Committee to discuss their findings.

James T. Bruvall
Chief Executive Officer
Citadel Diversified Management Ltd.

Darren K. Duncan
Chief Financial Officer
Citadel Diversified Management Ltd.

## AUDITORS' REPORT TO UNITHOLDERS

**To the Unitholders of Citadel Diversified Investment Trust**

We have audited the statement of net assets of Citadel Diversified Investment Trust as at December 31, 2000 and 1999, the statement of investments as at December 31, 2000 and the statements of operations and changes in net assets for the years ended December 31, 2000 and December 31, 1999. These financial statements are the responsibility of management of the Fund's manager. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, these financial statements present fairly, in all material respects, the net assets of the Fund as at December 31, 2000 and 1999, its investments as at December 31, 2000 and the results of its operations and the changes in its nets assets for the years ended December 31, 2000 and 1999 in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers

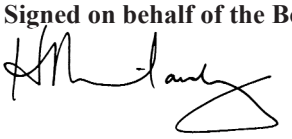
**PricewaterhouseCoopers LLP**
Chartered Accountants
Calgary, Alberta
March 23, 2001

# Citadel Diversified Investment Trust

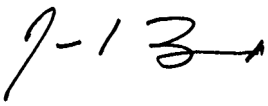
***Statement of Net Assets***

| | As at December 31, 2000 | (Restated – note 3) As at December 31, 1999 |
|---|---|---|
| **Assets** | | |
| Investments, at market (cost: 2000 – $96,292,143; 1999 - $88,951,616) | $ 96,641,036 | $ 78,912,490 |
| Cash and term deposits | 5,871,783 | 1,424,599 |
| Prepaid expenses (note 5) | 1,106,390 | 1,179,774 |
| Accounts receivable | 605,774 | - |
| Distributions receivable | 827,137 | 698,613 |
| | 105,052,120 | 82,215,476 |
| **Liabilities** | | |
| Accounts payable and accrued liabilities (note 5) | 58,886 | 91,870 |
| Distributions payable (note 3) | 1,092,678 | 910,643 |
| Loan payable (note 8) | - | 5,000,000 |
| | 1,151,564 | 6,002,513 |
| **Net Assets representing Unitholders' Equity** | **$ 103,900,556** | **$ 76,212,963** |
| **Units outstanding** (note 4) | **12,277,284** | **9,898,291** |
| **Net asset value per unit – basic** | **$ 8.46** | **$ 7.70** |

**Signed on behalf of the Board,**



Harold P. Milavsky
Chairman of the Board



James T. Bruvall
Director and Chief Executive Officer

# Citadel Diversified Investment Trust

***Statement of Operations***

| | Year Ended December 31, 2000 | Year Ended December 31, 1999 |
|---|---|---|
| **Income** | | |
| Interest and other income | $ 12,346,189 | $ 9,916,139 |
| Dividend income | 141,064 | 341,150 |
| | 12,487,253 | 10,257,289 |
| **Expenses** | | |
| Administrative and investment manager fees (note 5) | 1,642,410 | 1,188,121 |
| General and administration costs | 403,587 | 433,441 |
| Interest expense | 186,956 | 181,456 |
| | 2,232,953 | 1,803,018 |
| **Net investment income** | **10,254,300** | **8,454,271** |
| **Net realized gain (loss) on sale of investments** (note 6) | **2,454,833** | **(856,013)** |
| **Net change in unrealized gain on investments** | **10,388,019** | **1,270,527** |
| **Total results of operations** | **$ 23,097,152** | **$ 8,868,785** |
| **Results of operations per unit** (1) | | |
| Net investment income | $ 0.93 | $ 0.86 |
| Net realized gain (loss) on sale of investments | 0.22 | (0.09) |
| Net change in unrealized gain on investments | 0.94 | 0.13 |
| | $ 2.09 | $ 0.90 |

(1) Based on the weighted average number of units outstanding during the period.

# Citadel Diversified Investment Trust

***Statement of Changes in Net Assets***

| | Year Ended December 31, 2000 | (Restated – note 3) Year Ended December 31, 1999 |
|---|---|---|
| **Net Assets – beginning of year** | **$ 76,212,963** | **$ 76,556,831** |
| Operations: | | |
| Net investment income | 10,254,300 | 8,454,271 |
| Net realized gain (loss) on sale of investments | 2,454,833 | (856,013) |
| Net change in unrealized gain on investments | 10,388,019 | 1,270,527 |
| | 23,097,152 | 8,868,785 |
| Unitholder Transactions: | | |
| Proceeds from issuance of trust units, net | 18,452,490 | 2,585,108 |
| Repurchase of units | (2,045,864) | (2,158,016) |
| | 16,406,626 | 427,092 |
| Distributions to Unitholders: | | |
| From net investment income (note 7) | (11,816,185) | (9,639,745) |
| Net Increase (Decrease) in Net Assets | 27,687,593 | (343,868) |
| **Net Assets – end of year** | **$ 103,900,556** | **$ 76,212,963** |
| **Distributions per unit** | **$ 1.05** | **$ 0.98** |

# Citadel Diversified Investment Trust

***Statement of Investments***

| Number of Units | | As at December 31, 2000 Cost | Market | % of Portfolio |
|---|---|---|---|---|
| | **Income Funds** | | | |
| 400,000 | Algonquin Power Income Fund | $ 3,828,500 | $ 4,040,000 | |
| 358,000 | Associated Freezers Income Trust | 3,888,757 | 2,810,300 | |
| 189,000 | FACS Record Storage Income Fund | 1,828,236 | 1,493,100 | |
| 350,000 | Fort Chicago Energy Partners L.P. | 2,929,017 | 2,975,000 | |
| 450,000 | Halterm Income Fund | 2,762,875 | 3,487,500 | |
| 587,500 | Koch Pipelines Canada L.P. | 3,347,000 | 3,348,750 | |
| 278,000 | Luscar Coal Income Fund | 1,218,532 | 525,420 | |
| 415,000 | North West Company Fund | 5,224,654 | 4,793,250 | |
| 330,000 | Oceanex Income Fund | 3,115,113 | 3,003,000 | |
| 215,000 | Pacifica Papers Inc. | 2,150,000 | 1,935,000 | |
| 205,000 | PRT Forest Regeneration | 2,023,764 | 1,793,750 | |
| 625,000 | Rogers Sugar Income Fund | 4,917,990 | 2,750,000 | |
| 364,800 | Superior Propane Income Fund | 5,266,294 | 5,709,120 | |
| 275,000 | Timberwest Forest Corp. | 2,261,250 | 2,983,750 | |
| | | 44,761,982 | 41,647,940 | 43.1% |
| | **Oil & Gas Royalty Trusts** | | | |
| 500,000 | ARC Energy Trust | 4,014,582 | 5,650,000 | |
| 820,750 | Enermark Income Fund | 3,532,088 | 3,619,508 | |
| 231,000 | Enermark Income Fund Warrants | 57,750 | 57,750 | |
| 150,000 | Enerplus Resource Fund | 2,657,625 | 3,435,000 | |
| 350,000 | NAL Oil and Gas Trust | 3,048,072 | 3,027,500 | |
| 216,100 | Pengrowth Energy Trust | 3,779,433 | 4,149,120 | |
| 350,000 | PrimeWest Energy Trust | 2,452,946 | 3,132,500 | |
| 275,000 | Shiningbank Energy Income Fund | 2,731,858 | 4,675,000 | |
| 574,704 | Vanguard Oil Corporation | 68,964 | 71,838 | |
| 400,000 | Viking Energy Royalty Trust | 2,466,160 | 3,420,000 | |
| | | 24,809,478 | 31,238,216 | 32.3% |
| | **Real Estate Investment Trusts** | | | |
| 300,000 | Cdn Hotel Income Property Reit | 3,548,879 | 2,625,000 | |
| 350,000 | Cominar Reit | 3,422,700 | 3,552,500 | |
| 220,000 | CPL Long Term Care Reit | 3,827,550 | 2,893,000 | |
| 488,400 | H&R Reit | 5,545,701 | 5,787,540 | |
| 494,800 | Morguard Reit | 4,932,953 | 4,106,840 | |
| 275,000 | Riocan Reit | 2,475,000 | 2,585,000 | |
| 350,000 | Royal Host Reit | 2,967,900 | 2,205,000 | |
| | | 26,720,683 | 23,754,880 | 24.6% |
| | **Total** | **$ 96,292,143** | **$ 96,641,036** | **100.0%** |

# Citadel Diversified Investment Trust

Notes to Financial Statements December 31, 2000 and 1999

## 1. Structure of the Fund

Citadel Diversified Investment Trust (the "Fund" or "Citadel Diversified") is a closed-end investment trust established under the laws of Ontario pursuant to a Declaration of Trust dated as of July 11, 1997. The Fund commenced operations on September 16, 1997, when it completed an issue of 9,900,000 units at $10.00 per unit through an initial public offering. The Fund shall continue until December 31, 2007 or such earlier or later date as the unitholders may determine in accordance with the provisions of the Declaration of Trust.

## 2. Significant accounting policies

These financial statements, prepared in accordance with Canadian generally accepted accounting principles, include estimates and assumptions by management that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the period.

### (a) Valuation of investments

Investments are stated at market values based on closing market quotations. Average cost is used to compute realized and unrealized gains or losses on investments. Investment transactions are recorded on the trade date.

### (b) Canadian income taxes

The Fund qualified as a unit trust within the meaning of the Income Tax Act (Canada). Provided the Fund distributes to its unitholders its net income for tax purposes, the Fund will not generally be liable for income tax under Part 1 of the Income Tax Act (Canada).

### (c) Dividend, interest and other income

Dividend income is recorded on the ex-dividend date and interest and other income are recognized as earned.

## 3. Distribution payable

The accrual for distributions payable as at December 31, 1999 has been restated to reflect distributions declared by the Fund, as compared to an accrual based on distributions received or receivable from the Fund's portfolio. As a result of the retroactive restatement, distributions payable at December 31, 1999 has been reduced by $1,197,693 (1998 - $967,794) with the offsetting increase to Net Assets. There is no impact to the Statement of Operations.

## 4. Unitholders' contribution

The purchase price of the units issued pertaining to the initial public offering was payable in two instalments, the initial instalment of $6.00 per unit payable on the closing date and the final instalment of $4.00 per unit payable on September 16, 1998. On September 16, 1998 proceeds of $40.1 million were received from all outstanding instalment receipt units.

Pursuant to the initial public offering and over allotment provision, each unit was comprised of one non-redeemable trust unit and one trust unit purchase warrant which entitled the unitholder to acquire one trust unit at any time between September 16, 1998 and September 16, 1999 at an exercise price of $8.50. The trust unit was ascribed a value of $9.40 and the warrant a value of $0.60, less the discount relating to the final instalment.

# Citadel Diversified Investment Trust

Notes to Financial Statements December 31, 2000 and 1999

## 4. Unitholders' contribution (continued)

**Authorized –**

The authorized capital of the Fund consists of an unlimited number of trust units which are transferable non-redeemable units of beneficial interest.

| **Issued and issuable –** | **2000** | | **1999** | |
|---|---|---|---|---|
| | **Number** | **Amount** | **Number** | **Amount** |
| Trust units – beginning of year | 9,898,291 | $ 98,660,203 | 9,875,451 | $ 92,260,040 |
| Reclass of expired warrants | - | - | - | 5,973,071 |
| Issued for cash: | | | | |
| Exercise of warrants, net | - | - | 118,952 | 966,557 |
| Exercise of rights, net | 2,472,848 | 16,906,265 | - | - |
| Issued for services (note 5) | 180,845 | 1,546,225 | 196,188 | 1,618,551 |
| Repurchase of units | (274,700) | (2,045,864) | (292,300) | (2,158,016) |
| Trust units – end of year | 12,277,284 | $115,066,829 | 9,898,291 | $ 98,660,203 |

On June 30, 2000, Citadel Diversified completed a fully subscribed rights offering. Under the terms of the rights offering a total of 2,472,848 trust units were issued at an exercise price of $7.00 per unit, resulting in gross proceeds of $17.3 million.

Effective July 23, 1999, the unitholders of the Fund passed a resolution that amended the mandatory repurchase program such that units offered for sale at a discount to net asset value of greater than 5% (previously 10%) are repurchased for cancellation. This program is subject to a maximum of 1.25% of the total number of units outstanding at the beginning of each calendar quarter. During 2000, Citadel Diversified repurchased 274,700 trust units (1999 – 292,300 trust units) under this repurchase program.

In December 1999, Citadel Diversified received approval from The Toronto Stock Exchange to undertake a normal course issuer bid for the period December 8, 1999 to December 7, 2000. Under the terms of the issuer bid, the Fund could have purchased up to 471,547 trust units, representing 5% of the public float, on the open market through the facilities of The Toronto Stock Exchange. As at December 31, 2000, no trust units had been purchased under the issuer bid.

## 5. Administrative and Investment Manager Fees

Citadel Diversified Management Ltd. ("CDML") is the administrator for the Fund. Pursuant to the administrative services agreement, the administration and investment management fees are based upon 1.5% of the average weekly net asset value of the Fund, payable in units and subject to annual adjustment. On September 16, 1998, CDML was issued 80,937 units in respect of the six months of services for the period from March 16, 1999 to September 16, 1999. On September 16, 2000 an additional 173,536 units (1999 - 188,613 units) were issued to CDML in respect of the next twelve months of services. As at December 31, 2000, the Fund recorded an expense of $1,642,410 (1999 - $1,188,121) in respect of the units earned during the year. The amounts issued to CDML in 2000 and 1999 are included in units issued for services as shown in note 4. As at December 31, 2000 included in accounts payable were amounts owed to CDML of $58,886 (1999 - $91,870).

# Citadel Diversified Investment Trust

Notes to Financial Statements December 31, 2000 and 1999

## 6. Investments

The net realized gain (loss) on the sale of investments was determined as follows:

| | 2000 | 1999 |
|---|---|---|
| Proceeds on sale of securities | $ 23,663,759 | $ 15,579,183 |
| Less cost of securities sold: | | |
| Investments at cost – beginning of year | 88,951,616 | 77,104,922 |
| Investments purchased during year | 28,549,453 | 28,281,890 |
| Investments at cost – end of year | (96,292,143) | (88,951,616) |
| Cost of investments disposed of during period | 21,208,926 | 16,435,196 |
| Net realized gain (loss) on sale of investments | $ 2,454,833 | $ (856,013) |

## 7. Cash distributions

The Fund is required to distribute monthly cash distributions equal to the cash distributions received by the Fund less estimated expenses and any taxes payable.

| | 2000 | (Restated - note 3) 1999 |
|---|---|---|
| Net investment income for the year | $ 10,254,300 | $ 8,454,271 |
| Add back (deduct) amounts not affecting cash: | | |
| Fees paid by issuance of units | 1,704,903 | 1,250,616 |
| Excess cash not distributed in period | (143,018) | (65,142) |
| Cash distributions | $ 11,816,185 | $ 9,639,745 |
| Cash distributions per unit | $ 1.05 | $ 0.98 |

## 8. Loan payable

The Fund maintains a revolving credit facility with a Canadian chartered bank for up to a maximum amount of $25,000,000 of which no amount was drawn as at December 31, 2000 (1999 – $5,000,000). Borrowings are collateralized by a demand debenture in the amount of $55,000,000 which provides a first floating charge over the Fund's assets. The credit facility bears interest at the bank's prime lending rate or at rates slightly below prime if incurred by way of bankers' acceptances. The credit facility is a revolving facility that will revolve until September 15, 2001 and for a further 364 days at the option of the bank. If the revolving facility is converted to a term loan by the bank, the Fund will be required to repay the loan within one year.

## 9. Income taxes

As all taxable income was allocated to the unitholders in 2000 and 1999, no provision for income taxes has been made in these financial statements.

## 10. Financial Instruments

The fair values of the Fund's financial instruments which are comprised of cash and term deposits, accounts receivable, distributions receivable, accounts payable and accrued liabilities, distributions payable and loan payable approximate their carrying amount due to the short-term maturity of these instruments.

## CITADEL S-1 INCOME TRUST FUND

Citadel S-1 Income Trust Fund (the "Fund" or "Citadel S-1") is a closed-end investment trust which became listed on October 6, 2000 on The Toronto Stock Exchange under the symbol "SDL.un". The Fund has a life of approximately 10 years with a termination date of December 31, 2010. Citadel S-1's investment objectives are to provide its unitholders with a high level of monthly distributions while maintaining an S-1 stability rating and to maximize the net asset value of the Fund over its life. In order to achieve these objectives, the Fund's investment manager, Bloom Investment Counsel, Inc., actively manages a diversified portfolio of Canadian income funds, Canadian and U.S. high yielding investment grade debt and income yielding equity securities.

Pursuant to the Fund's distribution policy, Citadel S-1 pays fixed monthly cash distributions of $0.208 per trust unit. With the recent closing of the Fund on October 6, 2000, only the December 31, 2000 distribution of $0.208 per unit was paid in respect of the fiscal year ending December 31, 2000. Total distributions paid since Citadel S-1's inception in October 2000 have been $0.832 per unit and based on the April 19, 2001 unit price of $25.75, this represents a total compounded return of 12.1% per year.

**Investment Highlights:**

| | Q4 2000 |
|---|---|
| Net Asset Value per Unit | $ 24.32 |
| Market Price per Unit | $ 26.25 |
| Trading Premium | 7.9% |
| Quarterly Distributions per Unit (1) | $ 0.208 |
| Market Capitalization ($ millions) | $ 54.2 |

(1) Only one distribution paid during 2000.

| | |
|---|---|
| **Stock Symbol:** | **SDL.un (TSE)** |
| **2000 High / Low:** | **$27.00 - $24.95** |
| **2000 Distributions:** | **$0.208** |
| **2000 Tax-Deferred %:** | **78.9%** |
| **2000 Total Return:** | **6.0%** |

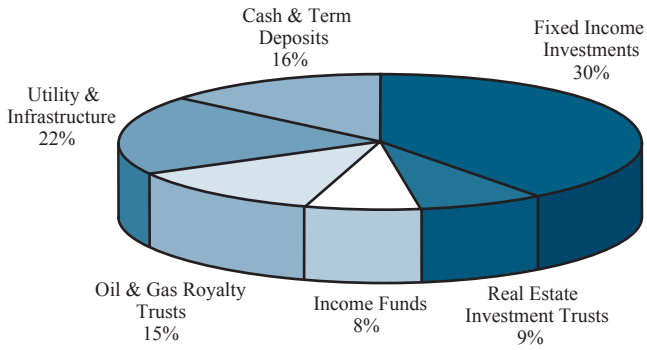
# MANAGEMENT DISCUSSION & ANALYSIS

## Investment Activity

Upon closing of Citadel S-1's initial public offering on October 6, 2000, net proceeds after agents' fees and issue costs of $47.4 million were available for investment. These funds were prudently and selectively deployed into Canadian originated preferred securities, various income funds, real estate investment trusts and oil & gas royalty trusts, all in accordance with the investment guidelines of the Fund, which were established to meet the strict guidelines of the S-1 stability rating. On January 24, 2001 Standard & Poor's (previously Canadian Bond Rating Service) affirmed the Fund's S-1 Stability Rating.

At December 31, 2000 Citadel S-1 had deployed 84% of the initial net proceeds, leaving $8.1 million in cash available for investment. The chart below reflects the Fund's portfolio (based on market values) as at year end.

## Fund Portfolio




## Financial Results

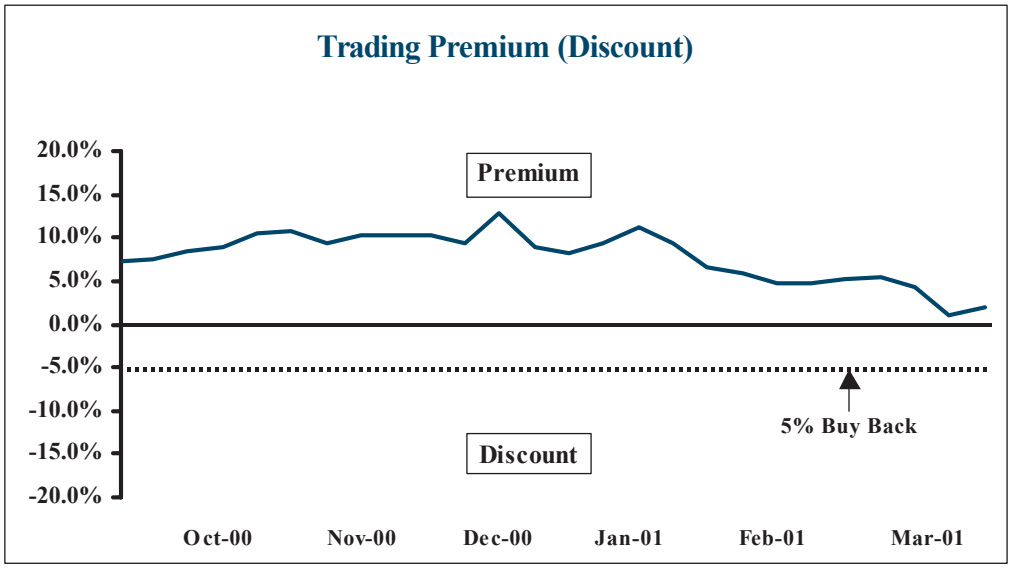
Citadel S-1's total income for the stub period of October 6, 2000 to December 31, 2000 was $1.3 million, which after deducting total expenses of $0.2 million, resulted in net investment income of $1.1 million.

During 2000, the Fund paid distributions of $0.4 million or $0.208 per unit. The Fund expects to continue making fixed monthly distributions of $0.208 per unit out of cash flow derived from its portfolio. The December 31, 2000 record date distribution was 78.9% tax-deferred, with the expectation that future distributions will be approximately 50% tax-deferred.

Trading activity in Citadel S-1's units has been light, but demand for the units has remained very strong since inception as reflected in Citadel S-1's market price. Since inception, Citadel S-1's market price has consistently traded well above the initial offering price of $25.00. As at December 31, 2000, the net asset value was $24.32 per unit while the market price was $26.25. Continued strong commodity prices and stable to lower interest rates has aided in the appreciation of the Fund's net asset value, which presently sits at $25.19 per unit as at April 19, 2001.

### Trading Premium / Discount to Net Asset Value

The units of Citadel S-1 have performed very well in the market place. As can be seen in the chart shown below, Citadel S-1 units have consistently traded at a premium to both issue price and net asset value.




### S-1 Stability Rating

Standard & Poor's provides a rating scale to assist investors in understanding the risk profile of an investment in an income fund. Standard & Poor's Stability Ratings characterize the stability of the cash distribution stream of an income fund in terms of variability and sustainability in the medium to longer term. The rating continuum ranges from S-1 at the highest to S-7 at the lowest.

Prior to establishing the Fund, the Administrator (Citadel S1 Management Ltd.) retained and worked with Standard & Poor's to establish investment guidelines which, if met, would result in the Fund achieving and maintaining an S-1 stability rating over the life of the Fund. These investment guidelines became the investment guidelines of Citadel S-1, as set out in its Declaration of Trust. Upon the Fund's net proceeds being substantially invested, Standard & Poor's reviewed the Fund's portfolio and affirmed the Fund's S-1 rating on January 24, 2001.

### Outlook for 2001

The first few months of Citadel S-1's existence have been extremely positive, as the declining interest environment has elevated the underlying portfolio's market values. Capital appreciation on Citadel S-1 units up until year end was 5%, combined with the ongoing yield of 10%, has given unitholders a very attractive total return over the period. Given the current market environment of decreasing interest rates, 2001 looks very bright for Citadel S-1.

Based upon the Fund's current portfolio and analysts' estimates of distributions from the portfolio, Citadel S-1's fiscal 2001 distributions are estimated to be in excess of $2.50 per unit with approximately 50% of those distributions being tax deferred.

## MANAGEMENT'S RESPONSIBILITY STATEMENT

The financial statements of Citadel S-1 Income Trust Fund have been prepared by Citadel S1 Management Ltd ("CSML") and approved by the Board of Directors of CSML. CSML is responsible for the information and representations contained in these financial statements and the other sections of the annual report.

CSML maintains appropriate procedures to ensure that relevant and reliable financial information is produced. These statements have been prepared in accordance with accounting principles generally accepted in Canada and include certain amounts that are based on estimates and judgements. The significant accounting policies applicable to the Fund are described in Note 2 to the financial statements.

The Board of Directors of CSML is responsible for ensuring that management fulfills its responsibilities for financial reporting and has reviewed and approved these financial statements. The Board carries out this responsibility through the Audit Committee, which is comprised of the independent directors of the Board.

CSML, with the approval of its Board of Directors, has appointed the external audit firm of PricewaterhouseCoopers LLP. They have audited the financial statements in accordance with Canadian generally accepted auditing standards to enable them to express to unitholders their opinion on the financial statements. The auditors have full and unrestricted access to the Audit Committee to discuss their findings.

James T. Bruvall
Chief Executive Officer
Citadel S1 Management Ltd.

Darren K. Duncan
Chief Financial Officer
Citadel S1 Management Ltd.

## AUDITORS' REPORT TO UNITHOLDERS

**To the Unitholders of Citadel S-1 Income Trust Fund**

We have audited the statements of net assets and investments of Citadel S-1 Income Trust Fund as at December 31, 2000, and the statements of operations and changes in net assets for the period August 11, 2000, the date of Declaration of Trust, to December 31, 2000. These financial statements are the responsibility of management of the Fund's manager. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, these financial statements present fairly, in all material respects, the net assets and investments of the Fund as at December 31, 2000 and the results of its operations and the changes in its net assets for the period August 11, 2000, the date of Declaration of Trust, to December 31, 2000 in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers

**PricewaterhouseCoopers LLP**
Chartered Accountants
Calgary, Alberta
March 23, 2001

# Citadel S-1 Income Trust Fund

***Statement of Net Assets***

| | As at December 31, 2000 |
|---|---|
| **Assets** | |
| Investments, at market (cost: 2000 – $39,963,127) | $ 41,396,605 |
| Cash and term deposits | 8,112,158 |
| Prepaid expenses (note 4) | 480,469 |
| Distributions receivable | 684,575 |
| | 50,673,807 |
| **Liabilities** | |
| Accounts payable and accrued liabilities (note 4) | 85,475 |
| Distributions payable | 429,080 |
| | 514,555 |
| **Net Assets representing Unitholders' Equity** | **$ 50,159,252** |
| **Units outstanding** (note 3) | **2,062,885** |
| **Net asset value per unit - basic** | **$ 24.32** |

**Signed on behalf of the Board,**

Harold P. Milavsky
Chairman of the Board

James T. Bruvall
Director and Chief Executive Officer

# Citadel S-1 Income Trust Fund

***Statement of Operations***

| | For the Period August 11, 2000 to December 31, 2000 |
|---|---|
| **Income** | |
| Interest and other income | $ 1,329,591 |
| | 1,329,591 |
| **Expenses** | |
| Administrative and investment manager fees (note 4) | 154,648 |
| General and administration costs | 86,823 |
| | 241,471 |
| **Net investment income** | **1,088,120** |
| **Net change in unrealized gain on investments** | **1,433,478** |
| **Total results of operations** | **$ 2,521,598** |
| **Results of operations per unit** (1) | |
| Net investment income | $ 0.54 |
| Net change in unrealized gain on investments | 0.71 |
| | $ 1.25 |

(1) Based on the weighted average number of units outstanding during the period.

# Citadel S-1 Income Trust Fund

***Statement of Changes in Net Assets***

| | For the Period August 11, 2000 to December 31, 2000 |
|---|---|
| **Net Assets – beginning of period** | **$ -** |
| Operations: | |
| Net investment income | 1,088,120 |
| Net change in unrealized gain on investments | 1,433,478 |
| | 2,521,598 |
| Unitholder Transactions: | |
| Proceeds from issuance of trust units, net | 48,066,734 |
| Distributions to Unitholders: | |
| From net investment income (note 5) | (429,080) |
| **Net Assets – end of period** | **$ 50,159,252** |
| **Distributions per unit** | **$ 0.21** |

# Citadel S-1 Income Trust Fund

***Statement of Investments***

| Number of Units | | As at December 31, 2000 Cost | Market | % of Portfolio |
|---|---|---|---|---|
| | **Fixed Income Investments** | | | |
| 27,800 | Alberta Energy Co. Ltd. 8.50% | $ 698,920 | $ 717,240 | |
| 41,000 | Enbridge Inc. 7.60% Preferreds | 1,000,400 | 1,035,250 | |
| 18,000 | Enbridge Inc. 8.00% Preferreds | 451,800 | 459,000 | |
| 180,000 | Magna Int'l Inc. Series A 8.65% | 4,489,750 | 4,482,000 | |
| 130,000 | Shaw Communications 8.875% | 3,152,500 | 3,165,500 | |
| 40,000 | Suncor Energy Inc. 9.05% | 1,055,200 | 1,084,000 | |
| 145,000 | Transalta Corporation 8.15% | 3,620,250 | 3,784,500 | |
| | | 14,468,820 | 14,727,490 | 35.6% |
| | **Oil & Gas Royalty Trusts** | | | |
| 140,000 | ARC Energy Trust | $ 1,578,994 | $ 1,582,000 | |
| 580,000 | Enermark Income Fund | 2,575,450 | 2,557,800 | |
| 125,000 | Pengrowth Energy Trust | 2,370,707 | 2,400,000 | |
| 45,000 | Shiningbank Energy Income Fund | 623,250 | 765,000 | |
| | | 7,148,401 | 7,304,800 | 17.6% |
| | **Real Estate Investment Trusts** | | | |
| 160,000 | Cdn Hotel Income Property Reit | $ 1,479,496 | $ 1,400,000 | |
| 340,000 | Riocan Reit | 3,049,693 | 3,196,000 | |
| | | 4,529,189 | 4,596,000 | 11.1% |
| | **Income Funds** | | | |
| 95,000 | NorthWest Company Fund | $ 942,250 | $ 1,097,250 | |
| 150,000 | Rogers Sugar Income Fund | 733,033 | 660,000 | |
| 145,000 | Superior Propane Income Fund | 2,061,913 | 2,269,250 | |
| | | 3,737,196 | 4,026,500 | 9.8% |
| | **Utility & Infrastructure** | | | |
| 90,000 | Fort Chicago Energy Partners L.P. | $ 802,000 | $ 765,000 | |
| 151,000 | KMS Power Income Fund | 1,233,057 | 1,321,250 | |
| 310,000 | Koch Pipelines Canada L.P. | 1,690,525 | 1,767,000 | |
| 246,500 | Northland Power Income Fund | 2,005,840 | 2,181,525 | |
| 300,000 | Pembina Pipelines Income Fund | 2,340,000 | 2,625,000 | |
| 100,300 | Transalta Power L.P. | 647,786 | 682,040 | |
| 24,400 | TransCanada Power L.P. | 646,734 | 671,000 | |
| 180,000 | Westshore Terminals Fund | 713,579 | 729,000 | |
| | | 10,079,521 | 10,741,815 | 25.9% |
| | **Total** | **$ 39,963,127** | **$ 41,396,605** | **100.0%** |

# Citadel S-1 Income Trust Fund

Notes to Financial Statements December 31, 2000

## 1. Structure of the Fund

Citadel S-1 Income Trust Fund (the "Fund" or "Citadel S-1") is a closed-end investment trust established under the laws of Alberta pursuant to a Declaration of Trust dated as of August 11, 2000. The Fund commenced operations on October 6, 2000, when it completed an issue of 1,850,000 units at $25.00 per unit through an initial public offering. The Fund shall continue until December 31, 2010 or such earlier or later date as the unitholders may determine in accordance with the provisions of the Declaration of Trust.

## 2. Significant accounting policies

These financial statements, prepared in accordance with Canadian generally accepted accounting principles, include estimates and assumptions by management that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the period.

### (a) Valuation of investments

Investments are stated at market values based on closing market quotations. Average cost is used to compute realized and unrealized gains or losses on investments. Investment transactions are recorded on the trade date.

### (b) Canadian income taxes

The Fund qualified as a unit trust within the meaning of the Income Tax Act (Canada). Provided the Fund distributes to its unitholders its net income for tax purposes, the Fund will not generally be liable for income tax under Part 1 of the Income Tax Act (Canada).

### (c) Dividend, interest and other income

Dividend income is recorded on the ex-dividend date and interest and other income are recognized as earned.

## 3. Unitholders' contribution

The trust units issued as part of the initial public offering were payable on October 6, 2000 at a price of $25.00 per unit.

**Authorized –**

The authorized capital of the Fund consists of an unlimited number of trust units which are transferable non-redeemable units of beneficial interest.

| | 2000 | |
|---|---|---|
| **Issued and issuable -** | **Number** | **Amount** |
| Trust units – beginning of period | - | $ - |
| Issued for cash: | | |
| Initial public offering | 1,850,000 | 46,250,000 |
| Over-allotment provision | 187,260 | 4,681,500 |
| Issued for services (note 4): | 25,625 | 640,625 |
| Trust units – end of period | 2,062,885 | $ 51,572,125 |

# Citadel S-1 Income Trust Fund

Notes to Financial Statements December 31, 2000

**3. Unitholders' contribution (continued)**

The Fund has a mandatory repurchase program such that units offered for sale at a discount to net asset value of greater than 5% are repurchased for cancellation, subject to a maximum of 1.25% of the total number of units outstanding at the beginning of each calendar quarter. During 2000, Citadel S-1 repurchased no trust units under this repurchase program.

**4. Administrative and investment manager fees**

Citadel S1 Management Ltd. ("CSML") is the administrator for the Fund. Pursuant to the administrative services agreement, the administration and investment management fees are based upon 1.25% of the average weekly net asset value of the Fund, payable in units and subject to annual adjustment. On October 6, 2000, CSML and Bloom Investment Counsel, Inc. were issued 12,719 and 10,406 units respectively in respect of the next twelve months of services. As at December 31, 2000, the Fund recorded an expense of $154,648 in respect of the units earned during the period. As at December 31, 2000 included in accounts payable were amounts owed to CSML of $85,475.

**5. Cash distributions**

The Fund pays out fixed monthly cash distributions of $0.208 per unit based upon cash distributions received by the Fund less estimated expenses and any taxes payable.

| | 2000 |
|---|---|
| Net investment income for the period | $ 1,088,120 |
| Addback (deduct) amounts not affecting cash: | |
| Fees paid by issuance of units | 170,273 |
| Excess cash not distributed in period | (829,313) |
| Cash distributions | $ 429,080 |
| Cash distributions per unit | $ 0.21 |

**6. Income taxes**

As all taxable income was allocated to the unitholders in 2000, no provision for income taxes has been made in these financial statements.

**7. Financial Instruments**

The fair values of the Fund's financial instruments which are comprised of cash and term deposits, distributions receivable, accounts payable and accrued liabilities and distributions payable approximate their carrying amount due to the short-term maturity of these instruments.

## CITADEL HYTES FUND

Citadel HYTES Fund (the "Fund" or "Citadel HYTES") is a closed-end investment trust listed on The Toronto Stock Exchange under the symbol "CHF.un". The Fund has a life of approximately 5 years with a termination date of December 31, 2006. Citadel HYTES's investment objectives are to provide its unitholders with stable, sustainable and predominantly tax-deferred distributions and to return the invested capital at the end of the Fund's life. In order to achieve these objectives, the Fund's investment manager, Bloom Investment Counsel, Inc., actively manages a diversified portfolio of oil & gas royalty trusts, real estate investment trusts, income funds, qualified limited partnerships, Canadian high yielding investment grade debt and income yielding equity securities.

Pursuant to the Fund's distribution policy, Citadel HYTES will pay fixed monthly cash distributions of $0.26 per trust unit, representing an annualized yield of 12.5% based upon the issue price of $25.00 per unit. The Citadel HYTES initial public offering closed on April 11, 2001, raising gross proceeds of $125 million. The investment manager anticipates that it will take upwards of three months to prudently deploy the net proceeds of the offering. The first distribution is therefore expected to be declared in June 2001 and monthly thereafter.

As at April 19, 2001, Citadel HYTES had deployed approximately $25.0 million of the initial net proceeds. Early trading activity in Citadel HYTES units has been quite strong, with trading being at or above the $25.00 issue price.

**Stock Symbol: CHF.un (TSE)**

## *Administrators*

**Citadel Diversified Management Ltd.**
**Citadel S1 Management Ltd.**
**Citadel TEF Management Ltd.**
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Calgary, Alberta T2P 3E6
Telephone: (403) 261-9674
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Website: www.citadelfunds.com
Email: info@citadelfunds.com

## *Investment Manager*

**Bloom Investment Counsel, Inc.**
Suite 1710, 150 York Street
Toronto, Ontario
M5H 3S5

## *Trustee (CTD.un & SDL.un)*

**The Trust Company of Bank of Montreal**
20th Floor, First Canadian Place
Toronto, Ontario
M5X 1A1

## *Trustee (CHF.un)*

**Montreal Trust Company of Canada**
710 Western Gas Tower
530 – 8th Avenue S.W.
Calgary, Alberta
T2P 3S8

## *Custodian*

**CIBC Mellon Global Securities Services Company**
320 Bay Street, 6th Floor
Toronto, Ontario
M5H 4A6

## *Legal Counsel*

**Stikeman Elliott**
4300 Bankers Hall West
888 – 3rd Street S.W.
Calgary, Alberta
T2P 5C5

## *Auditors*

**PricewaterhouseCoopers LLP**
1200, 425 – 1st Street S.W.
Calgary, Alberta
T2P 3V7

## *Stock Exchange Listings*

**The Toronto Stock Exchange**
Citadel Diversified Investment Trust units: CTD.un
Citadel S-1 Income Trust Fund units: SDL.un
Citadel HYTES Fund units: CHF.un

CITADEL

Group of Funds

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