2008 Annual Report

K-BRO LINEN INCOME FUND

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K-Bro Linen Income Fund, through its wholly-owned subsidiary K-Bro Linen Systems Inc., is Canada's largest healthcare and hospitality laundry and linen processor. Our name is known and respected in our industry. With large processing facilities in Toronto, Edmonton, Calgary, Vancouver, Victoria and Québec City, we employ over 1,000 people.

K-Bro provides an extensive value added menu of services that go beyond basic laundry services. These include reusable operating room pack services (KOR Services), resident personal clothing programs, specialty linen purchasing, various textile testing and extensive customer site-based services, including floor-to-floor distribution and linen room management.

We continued to successfully execute our three-part strategic focus in 2008 to:

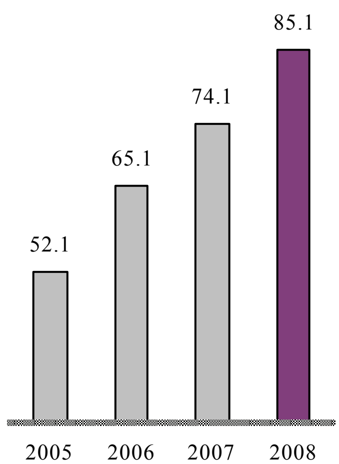
- **Secure and maintain long-term contracts with large healthcare and hospitality customers**
- **Extend core services to new markets**
- **Introduce related services.**

FINANCIAL HIGHLIGHTS

- **Revenues increased by 14.9% and EBITDA (1) by 34.9% in 2008 over 2007.**
- **Distributions of $1.10 per unit were paid in 2008 consistent with the previous two years.**
- **Distributable cash (1) was $11.2 million or $1.66/unit, an increase of $3.5 million over 2007.**
- **K-Bro had a conservative payout ratio (1) of 67.6% for 2008.**
- **The company had a conservative debt to EBITDA (1) ratio of 0.38 at December 31, 2008.**

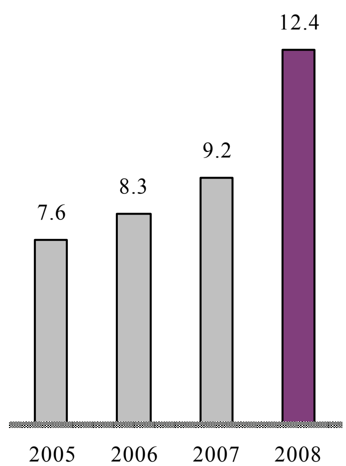
REVENUE

(in millions of Canadian dollars)



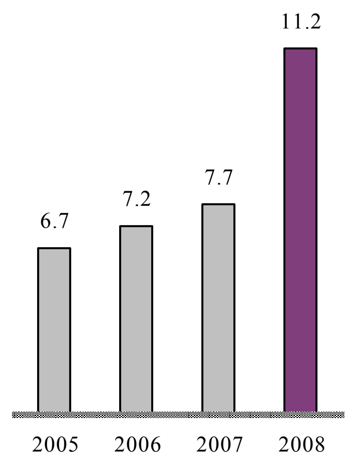
EBITDA (1)

(in millions of Canadian dollars)

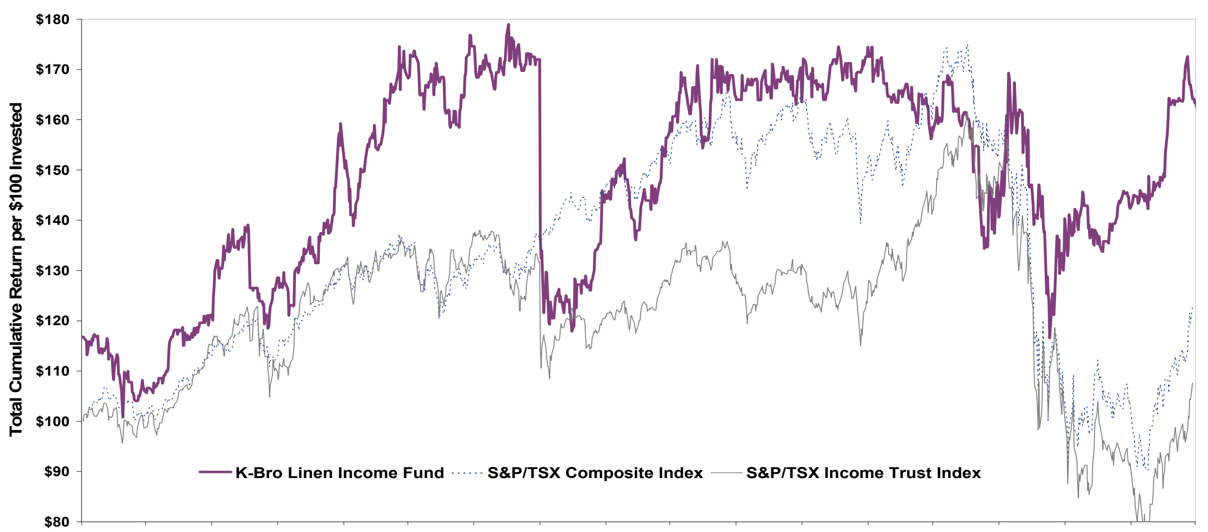


DISTRIBUTABLE CASH (1)

(in millions of Canadian dollars)



TOTAL CUMULATIVE RETURN (February 3, 2005 to May 8, 2009)
K-BRO LINEN INCOME FUND V.S. S&P/TSX COMPOSITE INDEX
VS. S&P/TSX INCOME TRUST INDEX



(1) Please refer to page 27 of Management's Discussion and Analysis for a discussion of this non-GAAP measure.

PRESIDENT'S MESSAGE

I am happy to report that 2008 was a year of continued growth and improved profitability for K-Bro. While we are never satisfied and always strive to improve, I believe we are well positioned to weather the current economic storms and hope to see further strong performance in 2009. We enter 2009 with much of our business from long-term healthcare contracts, good growth prospects and improving profitability, a relatively conservative payout ratio and a strong flexible balance sheet.

K-Bro's revenue grew by 14.9% in 2008 as a result of our Quebec City acquisition, the addition of new customers in our six Canadian markets and volume and price increases from our existing customers. We realized increases in both our healthcare and hospitality business and we're happy with results from all of our facilities. Approximately 76% of our revenue is from large publicly funded healthcare customers under long-term contracts, providing some stability in our business while we are still presented with significant growth opportunities in our markets. Our 34.9% EBITDA growth was primarily due to higher labour productivity, efficiencies from our new Calgary plant as well as our revenue growth, and we continue to focus on all key expense savings going forward. Finally, we have a significant line of credit so that we can quickly respond to attractive growth opportunities.

I believe that we have the strategy, prospects, people, and financial capacity to have a successful 2009 and beyond. At the beginning of 2008, I stated that although I expected to start 2008 slowly, I believed that we would gain momentum throughout the year to end on a successful note with a solid base to profitably grow the company further. K-Bro achieved those goals in 2008 and we look forward to 2009 with continued optimism and enthusiasm and an expectation of further growth in revenue and EBITDA.

I thank you, our employees, our customers and our Board for your continued support.

Linda McCurdy
President and Chief Executive Officer

K-Bro's new 80,000 sq. ft. facility in Calgary was fully operational in April, 2008 with the transitioning of all acute care and long term care volume of the Calgary Health Region as well as that of major Calgary hotels.

Highly automated and energy efficient dryers (above) combined with twin 16 chamber tunnel washers (left) enhance production efficiencies and processing quality to a very high level. Combined with a labour saving materials handling system via overhead monorail, the new plant has the capacity to handle additional volume available now and in the future in a growing southern Alberta market.

WE CAPITALIZED ON GROWTH OPPORTUNITIES IN EXISTING MARKETS

In 2008 we commenced processing under the terms of a further 10-year contract with the Calgary Health Region. The new contract encompassed all the existing acute care volume we processed as well as the long-term care volume previously processed by a competitor. We successfully transitioned into our new state-of-the-art Calgary facility in 2008, which not only allows us to meet the growing demands for services from our existing customers, but also provides us with the capacity to secure additional volumes in the future.

The acquisition of HMR in Quebec City on January 31, 2008 gains us entry into another new and important market.

Primarily servicing the hospitality industry including major hotels and local restaurants, HMR also provides an extensive floor mat rental service which is an extension to K-Bro's traditional service offerings.

WE ACHIEVED GROWTH THROUGH ACQUISITION

We completed the purchase of the business and assets of Buanderie HMR Inc., a leading laundry and linen service provider located in Québec City, Québec, in 2008. HMR has a strong market position in the hospitality and commercial sectors, with excellent brand recognition. This purchase provides K-Bro with an accretive acquisition that will allow us to leverage our healthcare expertise to expand the services provided to the Québec marketplace.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

March 12, 2009

The following management's discussion and analysis is supplemental to, and should be read in conjunction with, the audited consolidated financial statements of K-Bro Linen Income Fund ("the Fund") for the years ended December 31, 2008 and 2007. These financial statements and other documents filed with regulatory authorities can be found on SEDAR at www.sedar.com. The Fund's financial statements are prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). The Fund's reporting currency is the Canadian dollar. The Fund and its subsidiary K-Bro Linen Systems Inc. will collectively be referred to as "K-Bro" in this Management's Discussion and Analysis ("MD&A").

Management is responsible for the information contained in this MD&A and its consistency with information presented to the Audit Committee and Board of Trustees. All information in this document has been reviewed and approved by the Audit Committee and Board of Trustees. This review was performed by management with information available as of March 12, 2009.

In the interest of providing unitholders and potential investors of K-Bro with information regarding future plans and operations, this MD&A contains forward-looking information that represents internal expectations, estimates or beliefs concerning, among other things, future activities or future operating results and various components thereof. The use of any of the words "anticipate", "continue", "expect", "may", "will", "project", "should", "believe", and similar expressions suggesting future outcomes or events are intended to identify forward-looking information. Statements regarding such forward-looking information reflect management's current beliefs and are based on information currently available to management.

These statements are not guarantees of future performance and are based on management's estimates and assumptions that are subject to risks and uncertainties, which could cause K-Bro's actual performance and financial results in future periods to differ materially from the forward-looking information contained in this MD&A. These risks and uncertainties include, among other things, (i) risks associated with acquisitions, including the possibility of undisclosed material liabilities; (ii) K-Bro's competitive environment; (iii) utility and labor costs; (iv) K-Bro's dependence on long-term contracts, (v) increased capital expenditure requirements; (vi) reliance on key personnel; and (vii) the availability of future financing. Material factors or assumptions that were applied in drawing a conclusion or making an estimate set out in the forward-looking information include: (i) volumes and pricing assumptions; (ii) utility costs; (iii) expected contribution from the new Calgary plant; (iv) expected impact of labour cost initiatives; (v) anticipated contribution from the HMR acquisition; and (vi) the level of capital expenditures. Although the forward-looking information contained in this MD&A is based upon what management believes are reasonable assumptions, there can be no assurance that actual results will be consistent with these forward-looking statements. Certain statements regarding forward-looking information included in this MD&A may be considered "financial outlook" for purposes of applicable securities laws, and such financial outlook may not be appropriate for purposes other than this MD&A.

All forward-looking information in this MD&A is qualified by these cautionary statements. Forward-looking information in this MD&A is presented only as of the date made. Except as required by law, K-Bro does not undertake any obligation to publicly revise these forward-looking statements to reflect subsequent events or circumstances.

This MD&A also makes reference to certain non-GAAP measures to assist in assessing the Fund's financial performance. Non-GAAP measures do not have any standard meaning prescribed by GAAP and are therefore unlikely to be comparable to similar measures presented by other issuers. Please see "Non-GAAP Measures" for further discussion.

INTRODUCTION

Core Business

The Fund is a limited purpose trust established under the laws of Alberta pursuant to the Amended and Restated Fund Declaration of Trust dated February 3, 2005. The Fund was created for the purpose of acquiring, directly or indirectly, all of the issued and outstanding securities of K-Bro Linen Systems Inc.

K-Bro is the largest owner and operator of laundry and linen processing facilities in Canada. K-Bro provides a comprehensive range of general linen and operating room linen processing, management and distribution services to healthcare institutions, hotels and other commercial accounts. K-Bro currently has processing facilities in six Canadian cities: Toronto, Edmonton, Calgary, Vancouver, Victoria and Quebec City.

Industry and Market

K-Bro provides laundry and linen services to Canadian healthcare, hospitality and other commercial customers. Typical services offered by K-Bro include the processing, management and distribution of general and operating room linens, including sheets, blankets, towels, surgical gowns and drapes and other linen. Other types of processors in K-Bro's industry in Canada include independent privately-owned facilities (i.e. typically small, single facility companies), public sector central laundries and public and private sector on-premise laundries (known as “OPLs”). Participants in other sectors of the laundry and linen services industry, such as uniform rental companies (which own and launder uniforms worn by their customers' employees) and facilities management companies (which manage public sector central laundries and OPLs), typically do not offer services that significantly overlap with those offered by K-Bro.

Management believes that the healthcare and hospitality sectors of the laundry and linen services industry represent a stable base of annual recurring business with opportunities for growth as additional healthcare beds and funds are made available to meet the needs of an aging demographic.

Industry Characteristics and Trends

Management believes that the industry exhibits the following characteristics and trends:

Stable Industry with Moderate Cyclicality – As evidenced by the stability in the number of approved hospital beds in the healthcare system and hotel rooms in the hospitality industry. Service relationships are typically formalized through contracts in the healthcare sector that are typically long term (from seven to ten years), while contracts in the hospitality sector typically range from two to five years.

Significant Barriers to Entry – Establishing new laundry facilities involves significant up-front investment in equipment, linen, facilities and labour. In addition, customer contracts are typically long-term, making it more difficult for new entrants to access new accounts other than upon the expiry of a contract's term.

Outsourcing and Privatization – There are often advantages to healthcare institutions in outsourcing the processing of healthcare linen to private sector laundry companies such as K-Bro because of the economies of scale and significant management expertise that can be provided on a more comprehensive and cost-effective basis than customers can achieve in operating their own laundry facilities.

Fragmentation – Most Canadian cities have at least one and sometimes several private sector competitors operating in the healthcare and hospitality sectors of the laundry and linen services industry. Management believes that the presence of these operators provides acquisition and consolidation opportunities for larger industry participants with the financial means to complete acquisitions.

Customers and Product Mix

K-Bro's customers include some of the largest healthcare and hospitality institutions in Canada. Healthcare customers include acute care hospitals and long-term care facilities. Most of K-Bro's hospitality customers (typically 250+ rooms) generate between 500,000 and 3,000,000 pounds of linen per year. Most healthcare customers generate between 500,000 pounds of linen per year for a hospital and up to 20,000,000 pounds of linen per year for a healthcare region.

SUMMARY OF RESULTS AND KEY EVENTS FOR THE YEAR

Significant Revenue and EBITDA Growth in 2008

Revenue increased in the fourth quarter of 2008 by 15.1% compared to the fourth quarter of 2007. For the year ended December 31, 2008, revenue increased by 14.9%. Of this 2008 growth, approximately 5.2 percentage points are the result of the acquisition of the assets of Buanderie HMR Inc. ("HMR") located in Quebec City, Quebec which took place on January 31, 2008, 2.8 percentage points are from the addition of new customers part way through 2007 and in 2008, 8.1 percentage points are from growth in existing customers as a result of growing volumes and price increases, and the loss or termination of existing customers accounted for a 1.2 percentage point reduction. Of the 8.1 percentage points of organic growth, approximately half is from price increases and half from volume increases.

The weakened economy and a strengthened Canadian dollar for much of the year did not have a significant impact on hospitality revenues in 2008. With the addition of HMR, this sector grew by 21.6% in the fourth quarter of 2008 compared to the fourth quarter of 2007 and by 22.2% for the year ended December 31, 2008 compared to 2007, with all of this growth as a result of the HMR acquisition. There can be no assurance that this trend will continue as the general economic conditions may negatively impact K-Bro's hospitality revenues if tourism or business travel decreases in the future.

EBITDA (see "Non-GAAP Measures") increased in the fourth quarter of 2008 by 76.5% compared to the fourth quarter of 2007. For the year ended December 31, 2008, EBITDA increased by 34.9%. This is the result of:

- The successful startup of the new Calgary plant with increased volumes, price adjustments and operating efficiencies being achieved;
- The positive impact of contractual price adjustments from customers;
- The contribution from the HMR acquisition; and
- The positive impact of the labour initiatives being realized.

Effects of Market Volatility and Uncertainty

K-Bro management feels that it is positioned to withstand the current market volatility and uncertainty given that:

- Approximately 76% of its revenues are from large publicly funded healthcare customers under long-term contracts.
- The impact of the market downturn on the Fund's revenue from hospitality customers, which currently accounts for 24% of total revenue, is mitigated by the fact that the majority of this business is from large downtown, primarily business, hotels. Such hotels are not as dependent on tourism as others and often have commitments several years in advance for meetings and conventions. However, this sector could be negatively impacted by current economic conditions which could impact K-Bro's results if volumes fall or price concessions are required. Management believes this impact may not be material.
- K-Bro's $30 million line of credit is with a major Canadian bank and has a term to February 28, 2011 with an annual option to renew for an additional year. No events of default have occurred and at December 31, 2008, K-Bro had unutilized borrowing capacity under this line of $25.5 million or 85% of the line available.
- K-Bro's payout ratio for the quarter was 66.1% and for the year was 67.6%. The undistributed portion of cashflow provides K-Bro with cashflow from operations to fund growth or cushion it against business downturns.
- K-Bro has fixed a portion of certain potentially volatile components of its cost structure such as natural gas, electricity and interest rates through forward contracts or swaps. With the lowering of commodity prices such as natural gas, K-Bro will benefit as this is a major input cost.

Acquisition of Business and Assets of Buanderie HMR Inc. in Quebec City

On January 31, 2008, K-Bro completed the acquisition of the laundry business, linen, property and equipment of HMR. The business acquisition was accounted for using the purchase method, whereby the purchase consideration was allocated to the estimated fair values of the net assets acquired at January 31, 2008. The purchase price including acquisition costs was $3.9 million.

Of the cash consideration payable to the vendor, $0.5 million was deposited into escrow with an escrow agent. The full amount of the funds held in escrow will be released to the vendor upon the determination that specified earnings before interest, income taxes and amortization were met in the twelve-month period subsequent to the acquisition. Goodwill will correspondingly be increased by the amount released. Management expects the full amount to be paid to the vendor by March 31, 2009.

HMR is a leading laundry and linen service provider located in Quebec City, Quebec. K-Bro believes that HMR has a strong market position in the hospitality and commercial sectors, with excellent brand name recognition. Its large customer base ranges in size from major hotels to family operated restaurants.
The operating results achieved, combined with a low maintenance capital expenditure requirement, resulted in an acquisition that was accretive to the Fund in 2008.

Equity Issuance

On February 6, 2008 the Fund announced it had entered into an agreement to sell 1,362,000 units of the Fund ("Units") at a price of $12.85 per Unit to raise gross proceeds of approximately $17.5 million on a bought deal basis. K-Bro also granted the underwriters an over-allotment option, exercisable in whole or in part for a period of 30 days following closing, to purchase up to an additional 204,300 Units at the same offering price. The offering was made by way of a short form prospectus in all of the provinces of Canada and closed on February 27, 2008 with the issuance of 1,362,000 Units. On March 28, 2008 the underwriters exercised a portion of their over-allotment option and an additional 146,700 Units were issued, which brought the total gross proceeds of the offering to $19.4 million.

The net cash proceeds of the offering of $18.1 million were used to repay indebtedness incurred on the acquisition of the assets of HMR, the retrofit and equipping of the new Calgary plant and for general corporate purposes.

Alberta Labour Costs

Labour costs for plant staff in Alberta as a percentage of plant revenue decreased significantly in the fourth quarter from 54.8% in 2007 to 43.9% in 2008. For the year, these labour costs as a percentage of Alberta plant revenue decreased from 53.7% in 2007 to 46.9% for 2008. Labour cost as a percentage of plant revenue for the year and over the last five quarters is as follows:

	2008					2007	
	Year	Q4	Q3	Q2	Q1	Year	Q4
All plants	47.2%	46.1%	45.9%	46.3%	50.7%	50.4%	51.6%
Alberta	46.9%	43.9%	45.2%	46.1%	53.0%	53.7%	54.8%

This decrease in labour costs is the result of the new, more efficient Calgary plant and further impact of the federal government's Temporary Foreign Worker Program. Staff hired under the Temporary Foreign Worker Program have been deployed as they arrive between Edmonton and Calgary to fill current vacancies, reduce overtime and night shifts, and to fill vacancies due to turnover.

Calgary Health Region Contract and New Calgary Plant

Effective March 1, 2008, K-Bro and the Calgary Health Region have been operating under an interim agreement that reflects the revised pricing and terms of a new ten year contract. The finalized signed new contract was received on March 6, 2009. K-Bro's initial ten-year contract expired February 29, 2008. The new agreement encompasses all the long-term healthcare volume of the region previously processed by a competitor, in addition to the acute care volume that K-Bro has processed in the past.

The transition of volume to the new 80,000 sq. ft. plant was substantially completed by March 31, 2008. No major service issues or disruptions were experienced during this significant undertaking.

The new facility is equipped and retrofitted in order to operate as efficiently as possible in a continuing tight labour market, to be able to meet the growth plans of the Calgary Health Region and to be able to seize other available opportunities in a growing Calgary region. This equipment included the purchase of an additional tunnel washer system that is a twin of the tunnel washer purchased for Calgary in 2006 as well as an overhead materials handling monorail system which did not exist in the previous plant. The total capital cost as of December 31, 2008 is $15.2 million (see "Investing Activities"). This cost was initially funded from the Fund's line of credit, which was paid down as a result of the equity issuance noted previously.

Market Activities and Opportunities

Alberta

Significant healthcare projects in both Calgary and in Edmonton have been previously announced in Alberta and certain projects associated with that growth are underway. This growth in Edmonton includes the Mazankowski Heart Institute, the Lois Hole Hospital for Women and the Centre for Cardiac Services, the Orthopedic Surgery Centre, the Strathcona Community Hospital and the Edmonton Clinic, which are scheduled to open in the 2009 – 2012 timeframe. In Calgary, in addition to various expansions and renovations of existing facilities, the South Health Campus phase one is planned to be completed in the next five years. Alberta's Health minister has said that projects with advanced construction (such as those noted above) will continue; however, Alberta Health's overall $4-billion capital plan is under review by the provincial government because of escalating costs and reduced provincial revenues.

Management believes that the expanded and more efficient new Calgary plant will provide additional opportunities in both the healthcare and hospitality sectors in that marketplace. In Edmonton, additional volume falling under the auspices of Capital Health continues to be added with the commencement of service to Leduc Hospital in January and Devon Hospital in March. Management believes that similar additional facilities may become available in the future.

On May 15, 2008 the Alberta government announced that one provincial government board would replace the nine regional health authority boards. The new Alberta Health Services Board will be responsible for health services delivery for the entire province and will report directly to the Minister of Health and Wellness. Due to its track record and the contractual nature of K-Bro's relationships in Edmonton and Calgary, management does not believe there will be any negative impact on K-Bro's business from this change in structure. However, given this new provincial structure, the Alberta Health Board's timing with respect to addressing K-Bro's contract with the Edmonton Capital Health Region, which expires December 31, 2010, is unknown at this time.

British Columbia

In 2002, the British Columbia provincial government enacted Bill 29, the Health and Social Services Delivery Improvement Act, which, among other things, voided certain provisions of existing collective agreements between public sector healthcare organizations and their employees. The enactment of this legislation provided K-Bro with the opportunity to expand its operations by attracting new healthcare customers in the Vancouver region who wished to outsource their linen processing requirements to private sector laundries. Certain healthcare sector unions, associations of bargaining agents and employees affected by this legislation challenged its constitutionality in B.C. courts and before the Supreme Court of Canada.

On June 8, 2007, the Supreme Court of Canada found that certain sections of the B.C. legislation violated the freedom of association provision in the Canadian Charter of Rights and Freedoms, on the basis that they violated workers' rights to engage in collective bargaining. The court ruled that B.C. health employers retained the right to contract out certain services, but that health care workers have a right to negotiate language in their collective agreements on issues as fundamental to their working lives as contracting out.

On January 25, 2008, the Facilities Bargaining Association reached a settlement agreement regarding the implementation of the Supreme Court decision with the B.C. Government and the Health Employers' Association of B.C. The impact of the decision and the settlement agreement on the Fund is difficult to predict, but management considers the settlement a positive development in that it reduces regulatory uncertainty with respect to the Fund's current Vancouver contracts and may create opportunities for the Fund to attract new healthcare customers in B.C. The settlement agreement was approved by the Hospital Employees' Union on February 22, 2008. Further outsourcing opportunities exist; however, their timing and likelihood is uncertain, especially with a provincial election scheduled for 2009.

On the hospitality front, K-Bro's Vancouver operation commenced processing for four new hotel accounts in 2008 and commenced service for a new group of three hotels in March, 2009.

Quebec

In February 2008, a government task force made recommendations on how best to adequately fund Quebec's health care system. The task force concluded that Quebec must secure the long-term viability of the public health care system by increasing its productivity and adjusting the growth in public health spending to the growth rate of Quebec's economy, while improving access to care and quality of services. As K-Bro has seen in Alberta and British Columbia, such proposals and initiatives have sometimes led to private sector involvement in non-core activities such as laundry and linen services. Although there can be no guarantee that this will be the case in Quebec, K-Bro now has a presence in the Quebec marketplace with a processing facility following the HMR acquisition which may be of benefit should any such opportunities arise.

Ontario

The Ontario market remains very competitive in both the healthcare and hospitality sectors with customers being very price sensitive in the current market downturn. Two hospitality customers were lost to lower priced competitors in 2008; however, K-Bro has been successful in renewing and extending certain major hospitality contracts despite this pressure. Growth in volume from existing customers has offset any losses experienced in 2008.

In March, 2009 K-Bro announced that it was unsuccessful in renewing its healthcare contract with Halton Healthcare as the contract was awarded to another service provider pursuant to a request for proposal process. Management believes that this will not have a material impact on K-Bro's overall results.

Other Future Business Development Opportunities

K-Bro currently has several proposals out and has entered into discussions with potential new healthcare and hospitality customers. In addition, discussions are at various stages with potential acquisition candidates. Neither the timing nor the degree of likelihood of success of any of these proposals or potential acquisitions can be stated with any degree of accuracy at this time. The current state of the economy and capital markets adds a significant component of uncertainty to this growth process with respect to availability and cost of capital as well as the accretiveness of opportunities.

Taxation

On June 12, 2007, Bill C-52, which significantly modifies the income tax rules applicable to certain publicly traded or listed trusts and partnerships, was substantively enacted by the Canadian Federal Government. 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. These rules will be effective with respect to trusts which commence public trading after October 31, 2006. For trusts which were publicly traded or listed prior to November 1, 2006, the application of the rules will be delayed to the earlier or (i) the trust's 2011 taxation year, and (ii) a taxation year of the trust in which the trust exceeds normal growth as determined by reference to the normal growth guidelines, as amended from time to time, unless that excess arose as a result of a prescribed transaction. As currently structured, the Fund will be subject to these new rules, once applicable. There was no future income tax expense or recovery that needed to be recorded by the Fund as a result of this legislation as the Fund has no taxable temporary differences that would exist in 2011. Future income taxes are already recorded by the Fund's wholly-owned subsidiary K-Bro Linen Systems Inc.

Department of Finance (Canada) has table legislative proposals to amend released proposed amendments to the Income Tax Act (Canada) (the "Tax Act") to facilitate the conversion of income trusts into corporations on a tax-deferred basis. These proposed amendments are being evaluated and will be utilized in evaluating the options available to K-Bro in light of the impact of the Bill C-52 tax changes.

ACHIEVEMENT OF KEY PERFORMANCE DRIVERS

K-Bro's key performance drivers focus on growth, profitability, and stability in order to maintain distributions and maximize unitholder value. The following outlines our success in each of these areas:

Category	Specific Indicator	2008	2007
Growth (% increase from prior year)	Revenue	14.9%	13.8%
	EBITDA	34.9%	10.2%
	Distributable cash	45.1%	6.4%
Profitability (actual for the year)	EBITDA	$12,395	$9,188
	EBITDA margin	14.6%	12.4%
	Net income	$4,818	$4,114
Stability	Payout ratio	67.6%	78.5%
	Distributions per Unit	$1.10	$1.10
	Debt to total Capitalization	6.0%	25.6%
	Unutilized line of credit	$25,504	$12,938

OUTLOOK

Management believes that 2009 as a whole will again show a meaningful increase in revenue and EBITDA compared to 2008 with an overall payout ratio (see "Non-GAAP Measures") at a conservative level. Given this outlook, management believes that the current level of cash distributions is sustainable for the Fund in its current structure.

This belief is based on:

- The continued success of the new Calgary plant with increased volumes, price adjustments and operating efficiencies being achieved for twelve months as opposed to only nine months in 2008;
- The anticipated continuing organic growth from existing customers;
- The anticipated positive impact of the labour initiatives that is expected to be realized on an ongoing basis; and
- The reduction in energy costs currently being experienced.

The potential long-term impact of the Federal Government's implementation of its income tax changes (see "Taxation") will continue to unfold as capital markets, investors and the government react to the changes. The Fund, with the assistance of its professional advisers, continues to monitor the possible long-term impact they will have on the Fund and its investors, and what, if any, steps to take in respect of the Fund. However, this legislation is not expected to have an immediate impact on the Fund's tax treatment or distribution policy or the tax treatment of distributions to investors. There can be no assurance that the Fund will be able to undertake any measures to minimize the long-term impact.

RESULTS OF OPERATIONS

(all amounts in this section in $000's except per unit amounts and percentages)

Overall Performance

The fourth quarter of 2008 saw revenue increase by $2,822 or 15.1% over the fourth quarter of 2007 (increases of $11,012 and 14.9% for fiscal 2008 compared to 2007). See the "Summary of Results and Key Events for the Year" and the Revenues section below for an analysis of this change.

EBITDA (see "Non-GAAP Measures") increased in the current quarter by $1,441 (76.5%) over the fourth quarter of 2007 (increases of $3,207 and 34.9% for fiscal 2008 compared to 2007). The positive impact of the additional revenue was aided by operating costs that decreased to 84.6% of revenue in the current quarter compared to 89.9% in 2007 (85.4% of revenue for fiscal 2008 compared to 87.6% in 2007). The causes of this are discussed later under "Operating Expenses".

Selected Annual and Quarterly (Unaudited) Financial Information

The following table provides certain selected consolidated financial and operating data prepared by K-Bro management for the periods indicated:

Fiscal year	2008					2007					2006
	Total	Q4	Q3	Q2	Q1	Total	Q4	Q3	Q2	Q1	Total
Revenue	85,113	21,547	22,063	21,840	19,663	74,101	18,725	19,059	18,560	17,757	65,108
Operating expenses	72,718	18,223	18,466	18,539	17,490	64,913	16,842	16,630	16,050	15,391	56,773
EBITDA[1]	12,395	3,324	3,597	3,301	2,173	9,188	1,883	2,429	2,510	2,366	8,335
EBITDA as a % of revenue	14.6%	15.4%	16.3%	15.1%	11.1%	12.4%	10.1%	12.7%	13.5%	13.3%	12.8%
Amortization	7,203	1,950	1,903	1,896	1,454	5,755	1,408	1,443	1,447	1,457	5,118
Financial charges	687	142	148	140	257	880	318	230	154	178	554
Loss (gain) on disposal of equipment	507	49		458	-	(3)	(28)	-	28	(3)	(4)
Earnings before income taxes	3,998	1,183	1,546	807	462	2,556	185	756	881	734	2,667
Income tax recovery	820	202	64	224	330	1,558	859	262	220	217	1,211
Net earnings	4,818	1,385	1,610	1,031	792	4,114	1,044	1,018	1,101	951	3,878
Net earnings as a % of revenue	5.7%	6.4%	7.3%	4.7%	4.0%	5.6%	5.6%	5.3%	5.9%	5.4%	6.0%
Basic earnings per Unit	0.72	0.21	0.23	0.15	0.13	0.75	0.19	0.19	0.20	0.17	0.74
Diluted earnings per Unit	0.71	0.20	0.23	0.15	0.13	0.75	0.19	0.19	0.20	0.17	0.74
Total assets	85,926	85,926	88,373	89,531	89,568	83,342	83,342	76,384	74,119	74,030	75,074
Total long-term financial liabilities	8,537	8,537	10,862	13,755	8,901	21,948	21,948	18,335	14,576	12,693	14,591
Funds provided by operations	15,455	5,431	5,583	691	3,750	6,942	2,966	207	124	3,645	4,558
Long-term debt, end of period	4,061	4,061	6,219	9,010	4,000	16,627	16,627	12,734	9,510	7,478	9,278
Distributions declared per unit	1.10	0.28	0.27	0.28	0.27	1.10	0.28	0.27	0.28	0.27	1.10

Note: (1) EBITDA is defined as revenue less operating expenses as reflected in the table above (which equates to net earnings before income tax recovery, gain or loss on disposals, financial charges and amortization). See "Non-GAAP Measures".

Revenues

See previous discussion under "Summary of Results and Key Events for the Year" and "Overall Performance". Revenues by sector consist of:

Fiscal year	2008					2007				
	Total	Q4	Q3	Q2	Q1	Total	Q4	Q3	Q2	Q1
Sector										
Healthcare	64,698	16,782	16,226	16,448	15,242	57,393	14,806	14,318	14,261	14,008
Hospitality	20,415	4,765	5,837	5,392	4,421	16,708	3,919	4,741	4,299	3,749
Total	85,113	21,547	22,063	21,840	19,663	74,101	18,725	19,059	18,560	17,757

Operating Expenses

Wages and benefits - The major cause of the quarterly and annual improvement in labor costs is the performance of the Alberta plants as outlined under Alberta Labour Costs on page 12.

Linen - costs as a percentage of revenue have decreased on an annual and quarterly basis as the costs of standard and operating room linen items have remained flat in a competitive global market while revenues have increased.

Utilities – The spike in natural gas rates in the first half of 2008 moderated significantly in the last half of the year. This resulted in the improved quarterly performance as a percentage of revenue (7.3% in 2008 vs 8.2% in 2007) while the 2008 annual total was slightly greater than 2007 as a percentage of revenue (7.8% vs 7.7%).

Delivery – The escalation in delivery costs for the quarter and the year is the result of the addition of delivery costs for HMR, higher fuel costs and additional lease costs to handle the increased volumes.

Occupancy – Of the $626 increase in annual occupancy costs, $432 is attributable to the new and larger Calgary facility which was occupied for nine months, $119 is attributable to vacating the former Calgary plant, and $69 is attributable to the acquired HMR facility and other occupancy cost increases. For the quarter, a reduction in property tax accruals offset other operating increases and resulted in a net decrease of $39 compared to 2007.

Materials and supplies – this includes many different categories, including administrative expenses at the plant level. The year to date increase of $543 and the quarterly increase of $444 is in large part due to increased washfloor chemicals as a result of increased volumes processed. Also impacting this category is the inclusion of recruitment costs under the Temporary Foreign Worker Program of $159 for the year and $117 for the quarter.

Repairs and maintenance – As a percentage of revenue, there was a decrease of 0.1 percentage points for the year and the quarter in repairs and maintenance costs. Of the $688 increase in repairs and maintenance in 2008, $199 is the result of the HMR acquisition and $489 is the result of increased repairs and maintenance as certain equipment ages. For the quarter, HMR accounted for $48 of the $86 increase.

Corporate – costs increased by $538 for the year and $274 for the quarter. An increase in remuneration and performance bonus accruals accounted for $268 of the annual increase ($148 for the quarter) while an increase in the accrual for the Long Term Incentive Plan (see below) accounted for $312 of the annual increase ($110 for the quarter) as a result of significantly exceeding performance targets for the year.

Long Term Incentive Plan

In April 2006, a trust (the "LTIP Trust") was formed to hold Units of the Fund on behalf of the participants of K-Bro's long-term incentive plan (the "LTIP"). K-Bro is neither a trustee nor a direct participant of the LTIP; however, under certain circumstances K-Bro may be the beneficiary of forfeited Units held by the LTIP Trust. Consequently, the LTIP Trust is considered a variable interest entity for accounting purposes and K-Bro has consolidated the LTIP Trust in accordance with the Canadian Institute of Chartered Accountants ("CICA") issued Accounting Guideline AcG-15. For a specific performance year, one-quarter of the Units held by the LTIP Trust vest to the participants of the LTIP thirty days after approval of the audited financial statements by the Trustees upon the participant signing a Participation Agreement and Confirmation and three-quarters will vest on the second anniversary of that date upon continued employment, except in limited circumstances. Compensation expense is recorded by K-Bro in the period earned. Distributions made by the Fund with respect to unvested Units held by the LTIP Trust are paid to LTIP participants. Unvested units held by the LTIP Trust are shown as a reduction of unitholders' equity.

Effects of Inflation

The majority of K-Bro's customer contracts have an annual price adjustment mechanism based on a published price index such as the Consumer Price Index. To the extent that such indices are impacted by inflation, this would be reflected in K-Bro's revenues and net income. K-Bro's operating costs may be affected by general inflation but to a much greater extent are impacted by labour market conditions, textile costs in a global environment and commodity prices impacting the cost of energy.

Amortization of Property and Equipment

Amortization of property and equipment represents the expense related to the appropriate matching of certain of K-Bro's long-term assets to the estimated useful life and period of economic benefit to K-Bro of those assets. Amortization of plant and equipment for the fourth quarter and fiscal year of 2008 has increased from the comparable periods in 2007 primarily due to the capital expense of the new Calgary plant.

Amortization of Intangible Assets

Amortization of intangible assets represents the expense related with matching K-Bro's finite life intangible assets to the estimated useful life and period of economic benefit to K-Bro of those assets. As part of the valuations completed for purposes of the purchase price allocations for the assets of Premier Linen Supply Ltd. in Victoria (acquired on March 31, 2006) and the HMR acquisition by K-Bro, total additional intangible assets were recognized on the balance sheet of K-Bro in the amounts of $3,147 and $850, respectively, representing the value attributable to various contracts held. Amortization expense in the fourth quarter and fiscal year 2008 increased compared to 2007 as a result of the HMR acquisition.

Financial Charges

Financial charges in the current quarter decreased by $175 over 2007 ($193 for the year) as a result of the changing long-term debt balance primarily from the Calgary plant capital expenditures offset by the 2008 equity issuances (see "Liquidity and Capital Resources – Financing Activities").

Income Tax Recovery

Income tax recovery includes current and future income taxes based on taxable income and the temporary timing differences between the tax and accounting bases of assets and liabilities. Income tax recovery reflects the structure as an income trust whereby the Fund's unitholders bear the tax obligations with respect to distributions.

On June 12, 2007, Bill C-52, which significantly modifies the income tax rules applicable to certain publicly traded or listed trusts and partnerships, was substantively enacted by the Canadian Federal Government. 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. These rules will be effective with respect to trusts which commence public trading after October 31, 2006. For trusts which were publicly traded or listed prior to November 1, 2006, the application of the rules will be delayed to the earlier or (i) the trust's 2011 taxation year, and (ii) a taxation year of the trust in which the trust exceeds normal growth as determined by reference to the normal growth guidelines, as amended from time to time, unless that excess arose as a result of a prescribed transaction. As currently structured, the Fund will be subject to these new rules, once applicable. There was no future income tax expense or recovery that needed to be recorded by the Fund as a result of this legislation as the Fund has no taxable temporary differences that would exist in 2011. Future income taxes are already recorded by the Fund's wholly-owned subsidiary K-Bro Linen Systems Inc.

Currently, the Fund is only taxable on amounts that are not distributed to Unitholders. Once the Fund is subject to the new rules (which is not expected to be until 2011) the Fund will be subject to income tax on its earnings regardless of whether amounts are distributed to the Unitholders or not.

LIQUIDITY AND CAPITAL RESOURCES

(all amounts in this section in $000's except per unit amounts and percentages)

Cash Provided by Operating Activities

Cash provided by operating activities was $5,431 in the fourth quarter of 2008, an increase of $2,465 from the funds provided by operating activities in the fourth quarter of 2007. This $2,465 increase is attributable to an increase in cashflow from operations of $1,526 and a decreased working capital requirement of $939 in the quarter compared to the corresponding period in 2007. For fiscal 2008, cash provided by operating activities was $15,455, an increase of $8,513 from the funds provided by operating activities in 2007. This $8,513 increase is attributable to an increase in cashflow from operations of $3,359 augmented by a decreased working capital requirement of $5,154 compared to 2007.

The changes in working capital requirements are the result of: changes in accounts receivable resulting from the timing of receipts from major customers and growth in revenues; changes in linen purchases due to the timing of purchases and business growth; and, changes in accounts payable and prepaids as the result of timing differences in payments.

Financing Activities

On February 27, 2008 and March 28, 2008, the Fund issued additional units and raised proceeds as described under "Summary of Results and Key Events for the Year – Equity Issuance". No equity issuances occurred in 2007.

During the quarter ended December 31, 2008, the Fund declared distributions to unitholders at an annualized rate of $1.10 per unit for a total amount of $1,926 ($1,512 for the 2007 fourth quarter). For the year ended December 31, 2008, the Fund declared distributions to unitholders at an annualized rate of $1.10 per unit for a total amount of $7,554 ($6,046 for 2007). The increase in 2008 is reflective of the increased number of units outstanding as a result of the equity offering on February 27, 2008 and the related over-allotment option exercised on March 28, 2008.

Long-term debt at December 31, 2008 was $4,061 compared with $16,627 at December 31, 2007. The decrease from 2007 is the result of the equity issuance and the decrease in working capital requirements, offset by the purchase of additional strategic capital assets, primarily the Calgary plant.

The existing long-term debt of $4,061 consists of draw downs on a secured, revolving, interest only credit facility (the "Credit Facility") of up to $30,000. The Credit Facility is a two-year committed facility maturing February 28, 2011 and extendable annually for an additional year at the lender's option. It is subject to customary terms and conditions and is also subject to the maintenance of a maximum ratio of funded debt to EBITDA of 2.75 (increased to 3.25 for the two fiscal quarters immediately following an acquisition), and minimum ratios of 1.50 for the defined current ratio and 1.00 for fixed charge coverage. K-Bro has incurred no events of default under the terms of its credit facility agreement.

On June 24, 2005, K-Bro entered into an interest rate swap arrangement whereby the interest rate paid on a notional amount of $4,000 of this debt has been fixed at 5.95% for a period of five years. The floating rate of interest that was swapped for this fixed rate is currently at 3.64%.

Investing Activities

During the current quarter, K-Bro used $180 (2007 – $58) of funds for maintenance capital expenditures and $1,325 (2007 – $4,856) of funds for strategic capital expenditures for a total cash investment of $1,505 (2007 – $4,914) for the quarter. For the year, K-Bro used $490 of funds for maintenance capital expenditures in 2008 (2007 – $604) and $9,255 of funds for strategic capital expenditures (2007 – $7,691) for a total cash investment of $9,745 (2007 – $8,295). Management defines maintenance capital expenditures as additions to, or replacements of, property and equipment to maintain K-Bro's current business operations. K-Bro will be embarking on a computer software upgrade anticipated to commence in the first quarter of 2009. Total estimated costs of this multi-phase project have not been finalized but it is anticipated that approximately $250 could be incurred in Q1 2009 as a maintenance capital expenditure. Management estimates that ongoing annual average maintenance capital expenditures are approximately $850. The modest level of maintenance capital expenditures is due to the long life of the majority of the processing equipment.

Expenditures on parts such as motors, belts and ironer pads are expensed as incurred. These expenditures and an extensive preventative maintenance program performed at each plant by a full complement of qualified maintenance engineers has resulted in a repairs and maintenance expense (including personnel costs) totaling $1,263 in the fourth quarter of 2008 ($1,161 in 2007) which are included in the calculation of EBITDA. For the year ended December 31, 2008, these expenditures were $4,871 in 2008, compared with $4,103 in 2007 with the amount as a percentage of revenue up 0.2 percentage points.

Strategic capital expenditures are defined by management as those expenditures utilized for improvements to, and expansion of, K-Bro's property and equipment to enhance efficiencies and capacity to process incremental volumes. The majority of 2008 strategic capital expenditures relate to the new Calgary plant.

Proceeds from disposal of equipment of $4 were recorded in the fourth quarter and a loss on disposal of $49 was realized. For the year, proceeds from disposal of equipment of $163 were recorded and a loss on disposal of $507 was realized. This was primarily the result of the sale or scrapping of unneeded or technologically obsolete equipment from the former Calgary plant.

Contractual Obligations

At December 31, 2008, payments due under contractual obligations for the next five years and thereafter are as follows:

		Payments Due by Period			
	Total	Less than 1 year	1-3 years	4-5 years	After 5 years
Long-term debt	4,061	-	4,061	-	-
Operating leases and utility commitments	17,613	4,603	5,295	3,743	3,972
Linen purchase obligations	2,196	2,196	-	-	-

The source of funds for these commitments will be from operating cash flow and the undrawn portion of the Credit Facility.

In the current year, the lease on the Toronto facility was extended for three additional years to December 31, 2013 with no material change to the annual cost.

Financial Position

Capital Structure at December 31		
	2008	2007
Long-term debt	4,061	16,627
Unitholders' equity	63,862	48,243
Total capitalization	67,923	64,870
Debt to total capitalization	6.0%	25.6%

For the year ended December 31, 2008, the Fund had a payout ratio (see "Non-GAAP Measures") of 67.6%, a debt to total capitalization of 6.0%, an unused line of credit of $25,504 and has not incurred any events of default under the terms of its credit facility agreement. Based on this, management believes that K-Bro has sufficient liquidity and is able to generate sufficient amounts of cash to meet its planned growth and has access to the equity market, if cost effective, to fund additional growth as acquisition opportunities arise.

DISTRIBUTIONS FOR THE YEAR

Fiscal year		2008		2007	
Period	Payment Date	Per Unit Distribution	Distribution Amount ($)	Per Unit Distribution	Distribution Amount ($)
Fund Units					
First quarter		$0.27501	$1,754,774	$0.27501	$1,491,617
Second quarter		$0.27501	$1,906,524	$0.27501	$1,491,617
Third quarter		$0.27501	$1,906,524	$0.27501	$1,491,617
October	November 14	$0.09167	$635,508	$0.09167	$497,205
November	December 15	$0.09167	$635,508	$0.09167	$497,205
December	January 15	$0.09167	$635,508	$0.09167	$497,204
Fourth quarter		$0.27501	$1,906,524	$0.27501	$1,491,614
Year to date		$1.10004	$7,474,346	$1.10004	$5,966,465
Exchangeable Shares					
First quarter		$0.27501	$19,913	$0.27501	$19,913
Second quarter		$0.27501	$19,914	$0.27501	$19,913
Third quarter		$0.27501	$19,913	$0.27501	$19,913
October	November 14	$0.09167	$6,638	$0.09167	$6,639
November	December 15	$0.09167	$6,638	$0.09167	$6,639
December	January 15	$0.09167	$6,638	$0.09167	$6,638
Fourth quarter		$0.27501	$19,914	$0.27501	$19,916
Year to date		$1.10004	$79,654	$1.10004	$79,655
Total Distributions		**$1.10004**	**$7,554,000**	**$1.10004**	**$6,046,120**

For the year ended December 31, 2008, the Fund distributed $1.10 per unit compared with Distributable Cash (see "Non-GAAP Measures") per unit of $1.66. The actual payout ratio was 67.6%.

The Fund's policy is to make distributions to unitholders of its available cash to the maximum extent possible consistent with good business practices considering requirements for capital expenditures, working capital, growth capital and other reserves considered advisable by the Trustees of the Fund. All such distributions are discretionary. Distributions are declared payable each month in equal amounts to the Fund unitholders and exchangeable shareholders on the last business day of each month and are paid by the 15th of the following month.

DISTRIBUTABLE CASH (see "Non-GAAP Measures")

(all amounts in this section in $000's except per unit amounts and percentages)

The Fund's source of cash for distributions is cash provided by operating activities. Distributable cash, reconciled to cash provided by operating activities as calculated under GAAP, is presented as follows:

Fiscal year[(1)]	2008					2007				
	Total	Q4	Q3	Q2	Q1	Total	Q4	Q3	Q2	Q1
Per consolidated financial statements:										
Cash provided by operating activities	$15,455	$5,431	$5,583	$691	$3,750	$6,942	$2,966	$207	$124	$3,645
Add (deduct):										
Net changes in non-cash working capital items[(2)]	(3,788)	(2,337)	(2,108)	2,491	(1,834)	1,366	(1,398)	1,991	2,231	(1,458)
Maintenance capital expenditures[(3)]	(490)	(180)	(68)	(172)	(70)	(604)	(58)	(150)	(170)	(226)
Distributable cash	**$11,177**	**$2,914**	**$3,407**	**$3,010**	**$1,846**	**$7,704**	**$1,510**	**$2,048**	**$2,185**	**$1,961**
Distributable cash per weighted average diluted Units outstanding	**$1.66**	**$0.43**	**$0.49**	**$0.43**	**$0.31**	**$1.40**	**$0.26**	**$0.38**	**$0.40**	**$0.36**
Distributions declared[(4)]	$7,554	$1,927	$1,926	$1,926	$1,775	$6,046	$1,511	$1,512	$1,511	$1,512
Distributions declared per unit (see "Non-GAAP Measures")	**$1.10**	**$0.27**	**$0.28**	**$0.28**	**$0.27**	**$1.10**	**$0.27**	**$0.28**	**$0.28**	**$0.27**
Payout ratio (see "Non-GAAP Measures")[(4)]	**67.6%**	**66.1%**	**56.5%**	**64.0%**	**96.2%**	**78.5%**	**100.0%**	**73.8%**	**69.2%**	**77.1%**
Weighted average units outstanding during the period – Basic	6,719	6,969	6,969	6,961	5,972	5,464	5,459	5,459	5,465	5,476
Weighted average units outstanding during the period – Diluted	6,747	6,998	6,996	6,985	5,997	5,498	5,493	5,493	5,498	5,488
12-month trailing										
Distributable cash		11,177	9,773	8,414	7,589		7,704	8,225	7,906	7,676
Distributions		7,554	7,138	6,724	6,309		6,046	6,046	6,046	6,047
Payout ratio		67.6%	73.0%	79.9%	83.1%		78.5%	73.5%	76.5%	78.8%
Cumulative since IPO February 3, 2005										
Distributable cash		32,288	29,374	25,967	22,957		21,111	19,601	17,553	15,368
Distributions		23,572	21,645	19,719	17,793		16,018	14,507	12,995	11,484
Payout ratio		73.0%	73.7%	75.9%	77.5%		75.9%	74.0%	74.0%	74.7%

1. Following the revised Staff Notice 52-306 issued by the Canadian Securities Administrators on distributable cash presentation, we adopted their recommendations retroactive to February 3, 2005 in order to disclose comparable results.
2. Net changes in non-cash working capital is excluded from the calculation as management believes it would introduce significant cash flow variability and affect underlying cash flow from operating activities. Significant variability can be caused by such things as the timing of receipts (which individually are large because of the nature of K-Bro's customer base and timing may vary due to the timing of customer approval, vacations of customer personnel, etc.) and the timing of disbursements (such as the payment of large volume rebates done once annually). As well, large increases in working capital are generally required when contracts with new customers are signed as linen is purchased and accounts receivable increase. Management feels that this amount should be excluded from the distributable cash figure which is used as the basis for determining the distributions to be paid.
3. Maintenance capital expenditure is discussed under "Investing Activities".
4. The level of distributions paid compared to distributable cash is reviewed periodically to take into account the current and prospective performance of the business and other items considered to be prudent.

OUTSTANDING UNITS

At December 31, 2008, the Fund had 6,932,562 Fund Units outstanding and 72,411 Special Trust Units outstanding (unchanged from September 30, 2008). The basic and the diluted weighted average number of units outstanding for fiscal 2008 were 6,719,305 and 6,747,522 respectively (5,464,487 and 5,498,318 respectively for 2007).

In accordance with the LTIP agreement and in conjunction with the performance of the Fund in the prior fiscal year, the Compensation, Nominating and Corporate Governance Committee of the Trustees of the Fund in 2008 approved LTIP compensation of $0.3 million (2007 – $0.3 million) and approved the funding and transfer of $0.3 million (2007 – $0.3 million) of cash to the LTIP Trust in March 2008 and April 2007 respectively in order to fund the purchase of Units by the LTIP Trust. In March 2008, the LTIP Trust purchased 24,751 Units of the Fund (2007 – 22,647). As at December 31, 2008, 38,961 Units held by the LTIP Trust have vested (December 31, 2007 – 12,436). The basic net earnings per unit calculation exclude the unvested units held by the LTIP Trust.

RELATED PARTY TRANSACTION

The Fund has incurred expenses in the normal course of business for advisory consulting services provided by Matthew Hills, a Trustee, relating to acquisitions. The amounts charged are recorded at their exchange amounts and are subject to normal trade terms. For the year ended December 31, 2008, the Fund incurred such fees totaling $74,000 (2007 - $46,000). Of the total 2008 amount, $23,000 is included in costs related to the HMR acquisition and $51,000 is included in corporate expenses.

CRITICAL ACCOUNTING ESTIMATES

The preparation of the financial statements, in conformity with GAAP, requires management of K-Bro to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Management regularly evaluates these estimates and assumptions which are based on past experience and other factors that are deemed reasonable under the circumstances. This involves varying degrees of judgment and uncertainty and, therefore, amounts currently reported in the financial statements could differ in the future.

Linen in Service

Linen in service is recorded at cost. Operating room linen is amortized on a straight-line method over an estimated service life of 24 months. General linen is amortized based on usage which results in an estimated service life of the linen equal to 24 months. Based on past experience, management believes that a service life of 24 months is representative of the average service life of linen and would not expect a material deviation to the balance of linen in service or linen expense.

Revenue and Volume Rebates

Revenue from linen management and laundry services is largely based on written service agreements whereby K-Bro has agreed to collect, launder, deliver and replenish linens. K-Bro recognizes revenue in the period in which the services are provided. Volume rebates, where applicable, are recorded based on annualized expected volumes when it is determined that they are likely to be met. Based on past experience, management believes that volumes utilized for any estimates are reasonable and would not expect a material deviation to the balance of accrued liabilities or revenue.

Property, Plant and Equipment

Property, plant and equipment are recorded at cost. Amortization is provided over the estimated useful lives of the assets, based on past experience, on a declining basis using the following annual rates:

Building	5%
Laundry equipment	15%
Office and delivery equipment	20%
Computers and software	30%
Leasehold improvements	straight line over the initial lease period
Asset under development	at applicable rates and methods when put into service

The carrying value of property, plant and equipment is evaluated whenever significant circumstances indicate impairment in value is likely. The carrying value of property, plant and equipment and amortization expense is affected by these estimates.

Goodwill

Goodwill is not amortized and K-Bro assesses goodwill for impairment on an annual basis, or more frequently if changes in circumstances indicate a potential impairment. Any potential impairment is identified by comparing the fair value of the business to its carrying value. If the fair value exceeds its carrying value, goodwill is considered not to be impaired. If the carrying value exceeds its fair value, a more detailed goodwill impairment assessment would have to be undertaken. Any resulting impairment would be charged to earnings in the period in which the impairment is identified and would affect the carrying value of goodwill but such charges do not result in a cash outflow and would not affect K-Bro's liquidity. No impairment was incurred upon completion of management's 2008 and 2007 assessments. The possible impact of the Bill C-52 tax changes has been taken into account in K-Bro's review for impairment of goodwill.

Intangible Assets

Intangible assets with a finite life which relate to contracts K-Bro has with certain customers are recorded at cost and are amortized over the remaining life of the contract plus one renewal period. Impairment is evaluated if there are significant changes in circumstances affecting the carrying value of intangible assets by comparing the fair value of the finite life intangible asset with its carrying value. Management has determined that no such significant change has occurred in 2008 or 2007 that would impact the carrying value of intangible assets.

NON-GAAP MEASURES

EBITDA

We report on our EBITDA (Earnings before interest, taxes, depreciation and amortization) because it is a key measure used by management to evaluate performance. EBITDA is utilized in measuring compliance with debt covenants and in making decisions relating to distributions to unitholders. We believe EBITDA assists investors in assessing our performance on a consistent basis as it is an indication of our capacity to generate income from operations before taking into account management's financing decisions and costs of consuming tangible and intangible capital assets, which vary according to their vintage, technological currency and management's estimate their useful life. Accordingly, EBITDA comprises revenues less operating costs before: financing costs, capital asset amortization, disposal and impairment charges, and income taxes.

EBITDA is not a calculation based on GAAP and is not considered an alternative to net earnings in measuring K-Bro's performance. EBITDA does not have a standardized meaning and is therefore not likely to be comparable with similar measures used by other issuers. For reconciliation with GAAP, please refer to "Selected Annual and Quarterly Information". EBITDA should not be used as an exclusive measure of cash flow since it does not account for the impact of working capital changes, capital expenditures, debt changes and other sources and uses of cash, which are disclosed in the consolidated statements of cash flows.

Distributable Cash

Distributable cash is a non-GAAP measure generally used by Canadian income trusts as an indicator of financial performance but it should not be seen as a measurement of liquidity or a substitute for comparable metrics prepared in accordance with GAAP. Management believes that this measure is commonly used by investors, management and other stakeholders to evaluate the ongoing performance of K-Bro. For reconciliation with GAAP, please refer to the "Distributable Cash" section.

Cash Distributions per Unit and Payout Ratios

We report on cash distributions per unit and payout ratios (actual cash distribution divided by distributable cash) because they are believed to be key measures used by investors to value K-Bro, assess its performance and provide an indication of the sustainability of distributions. Cash distributions per unit and the payout ratio depend on the amount of distributable cash generated and the Fund's distribution policy.

The Fund's policy is to make distributions to unitholders of its available cash to the maximum extent possible consistent with good business practices considering requirements for capital expenditures, working capital, growth capital and other reserves considered advisable by the Trustees of the Fund. Distributions are declared payable each month to the Fund unitholders and exchangeable shareholders on the last business day of each month and are paid by the 15th of the following month. All distributions are discretionary. We periodically review cash distributions taking into account our current and prospective performance.

CHANGES IN ACCOUNTING POLICIES INCLUDING INITIAL ADOPTION

The CICA has issued three new accounting standards:

(i) Capital disclosures

The CICA issued a new accounting standard, Section 1535 "Capital Disclosures", which requires the disclosure of both qualitative and quantitative information that provides users of financial statements with information to evaluate the entity's objectives, policies and processes for managing capital. This new section was adopted by the Fund beginning January 1, 2008. The adoption of this standard did not have an impact on the consolidated financial statements other than with respect to note disclosure.

The Fund views its capital as the combination of its indebtedness and equity balances. In general, the overall capital of the Fund is evaluated and determined in the context of its financial objectives and its strategic plan.

With respect to its level of indebtedness, the Fund determines the appropriate level in the context of its cash flow and overall business risks. The Fund has historically generated cash flow in excess of distributions and has used such excess to fund maintenance capital expenditures, working capital and other reserves considered advisable by the Trustees of the Fund. Growth capital for strategic capital expenditures and acquisitions has generally been funded from indebtedness and equity. As well, the Fund will review its level of indebtedness in the context of the change in taxation impacting the Fund commencing in 2011.

The Fund's indebtedness is subject to a number of covenants and restrictions including the requirement to meet certain financial ratios and financial condition tests. One such ratio is the Total Funded Debt / EBITDA Ratio as defined in the Credit Facility. The maximum ratio allowed for a 12-month trailing period is 2.75, which is increased to 3.25 for the two quarters immediately following an acquisition. For the year ended December 31, 2008, this ratio was calculated at 0.38 (year ended December 31, 2007 – 1.86). Management also uses this ratio as a key indicator in managing the Fund's capital.

With respect to its equity, the current level of capital is considered adequate in the context of current operations and the present strategic plan of the Fund. Any major acquisitions or expansions may be financed in part with additional equity. The Fund will also review its level of equity in the context of the change in taxation impacting the Fund commencing 2011.

(ii) Financial instruments-disclosure and Financial instruments-presentation

Two new accounting standards were issued by the CICA, Section 3862 "Financial Instruments-Disclosures", and Section 3863 "Financial Instruments – Presentation". These sections replaced Section 3861 "Financial Instruments – Disclosure and Presentation". The objective of Section 3862 is to provide users with information to evaluate the significance of the financial instruments on the entity's financial position and performance, the nature and extent of risks arising from financial instruments, and how the entity manages those risks. The provisions of Section 3863 deal with the classification of financial instruments, related interest, dividends, losses and gains and the circumstances in which financial assets and financial liabilities are offset. These new sections were adopted by the Fund beginning January 1, 2008. The adoption of this standard did not have an impact on the consolidated financial statement other than with respect to note disclosure.

(iii) Inventories

In June 2007, the CICA issued a new accounting standard – Section 3031 "Inventories" which replaced the existing standard for inventories, Section 3030. The new Section was adopted by the Fund beginning January 1, 2008. Application of the new Section did not have an impact on the financial statements.

Future changes in accounting policies are:

(i) Goodwill and intangible assets

In February 2008, the CICA issued a new accounting standard – Section 3064 "Goodwill and intangible assets" which replaces the existing standard for goodwill and other intangible assets in Section 3062 and research and development costs in Section 3450. The new Section is effective for the Fund beginning January 1, 2009. It establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented enterprises. Standards concerning goodwill are unchanged from the standards included in the previous Section 3062. In accordance with this new policy, deferred charges at December 31, 2008 of $133 will be written off retrospectively against equity in 2009 with restatement of comparative amounts.

(ii) Business combinations

Section 1582 "Business combinations" will be applicable to business combinations for which the acquisition date is on or after the Fund's interim and fiscal year beginning January 1, 2011. Early adoption is permitted. The section improves the relevance, reliability and comparability of the information that a reporting entity provides in its financial statements about a business combination and it effects. The Fund has not yet determined the impact of the adoption of this new Section on the consolidated financial statements.

(iii) Consolidated financial statements

Section 1601 "Consolidated financial statements" will be applicable to financial statements relating to the Fund's interim and fiscal year beginning on or after January 1, 2011. Early adoption is permitted. This section establishes standards for the preparation of consolidated financial statements. The Fund has not yet determined the impact of the adoption of this new Section on the consolidated financial statements.

(iv) Non-controlling interests

Section 1602 "Non-controlling interests" will be applicable to financial statements relating to the Fund's interim and fiscal year beginning on or after January 1, 2011. Early adoption is permitted. This section establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. The Fund has not yet determined the impact of the adoption of this new Section on the consolidated financial statements.

(v) International Financial Reporting Standards

The Accounting Standards Board of Canada has announced that accounting standards in Canada, as used by public companies, will be converged to International Financial Reporting Standards ("IFRS") effective January 1, 2011. The changeover date is for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011.

IFRS uses a conceptual framework similar to Canadian GAAP but there are significant differences in recognition, measurement and disclosure requirements. As a result, the Fund has established a changeover plan to convert to these new standards according to the timetable set with these new rules. An implementation plan has been created and will be executed primarily with internal resources. The Fund will complete the scoping and diagnostic phase in the first quarter of 2009 and will then move to the impact analysis and design phase. The Fund's preliminary analysis of IFRS in comparison to Canadian GAAP has identified a number of differences. At this time, the impact on our future financial position and results of operations is not reasonably determinable or estimable. The Fund will continually review and adjust the changeover plan to ensure the implementation process properly addresses the key elements of the plan.

Key activities, milestones/deadlines and status are as follows:

Key Activity	Milestones/Deadlines	Status
Financial Statement Preparation: ▪ Identify differences between IFRS and Canadian GAAP accounting policies ▪ Selection of IFRS policies ▪ Select choices under IFRS 1 ▪ Develop financial statement format ▪ Quantify effects of change in initial IFRS1 disclosures and 2010 financial statements	Senior Management sign-off and audit committee review for all items by fourth quarter, 2009.	Analysis of issues currently underway.
Staffing: Define and introduce appropriate level of IFRS expertise for each of the following: ▪ Accounting staff ▪ Senior executives and Board, including Audit Committee	Appropriate level of expertise to be in place by second quarter 2009.	Resource assessment underway.
Infrastructure: Ensure information technology is fully compliant for IFRS as follows: ▪ Capability of system to produce dual financial statements (Canadian GAAP and IFRS) during the transition years ▪ Programs upgrades/changes ▪ Gathering disclosure data ▪ Budget/forecast monitoring process	Ready for parallel processing of 2010 general ledgers and for planning/monitoring process.	Process to begin second quarter 2009 in conjunction with financial systems software upgrade.
Business Policy Assessment: Financial Covenants ▪ Identify impact of IFRS on financial covenants ▪ Complete any required renegotiations/changes	Renegotiations to be completed by third quarter 2010.	Process of identifying metrics affected by conversion to IFRS currently underway.

Business Policy Assessment: Compensation Arrangements ▪ Identify impact on compensation arrangements ▪ Make any required changes	Fourth quarter 2010.	Process of identifying metrics affected by conversion to IFRS currently underway.
Business Policy Assessment: Customer and Supplier Contracts ▪ Evaluate impact of IFRS on current customer or supplier contracts.	Complete review by first quarter 2010.	Process of identifying IFRS consequences in process.
Control Environment: ICFR ▪ For all accounting policy changes identified, assess ICFR design and effectiveness implications. ▪ Implement changes where appropriate.	Fourth quarter 2009.	To be reviewed in conjunction with accounting policies.
Control Environment: DC&P ▪ For all accounting policy changes identified, assess DC&P design and effectiveness implications. ▪ Implement changes where appropriate.	See ICFR deadlines above. Publish impact of conversion on Key Performance Indicators in third quarter, 2010 MD&A. Publish material changes in policies and expectations by January 10, 2011. Publish revised 2010 results and MD&A by March 31, 2011.	To be reviewed in conjunction with accounting policies.

FINANCIAL INSTRUMENTS

K-Bro's financial instruments at December 31, 2008 consist of accounts receivable, accounts payable and accrued liabilities, distribution payable to unitholders, long-term debt and an interest rate swap agreement. The Fund does not enter into financial instruments for trading or speculative purposes. Financial assets are either classified as available for sale, held to maturity, trading or loans and receivables. Financial liabilities are recorded at amortized cost. Initially, all financial assets and financial liabilities must be recorded on the balance sheet at fair value. Subsequent measurement is determined by the classification of each financial asset and liability. Unrealized gains and losses on financial assets that are held as available for sale are recorded in other comprehensive income until realized, at which time they are recorded in the consolidated statement of earnings. All derivatives, including embedded derivatives that must be separately accounted for, are recorded at fair value in the consolidated balance sheet. Transaction costs related to financial instruments are generally capitalized and then amortized over the expected life of the financial instrument using the effective yield method.

Derivative financial instruments are utilized by K-Bro to manage cashflow risk against the volatility in interest rates on its long-term debt and foreign exchange rates on its equipment purchase commitments. K-Bro does not utilize derivative financial instruments for trading or speculative purposes. K-Bro has floating interest rate debt that gives rise to risks that its earnings and cash flows may be adversely impacted by fluctuations in interest rates. In order to manage these risks, K-Bro may enter into interest rate swaps, forward contracts or option contracts. K-Bro has entered into an interest rate swap arrangement as described under "Financing Activities".

It is K-Bro's policy to document all relationships between hedging instruments and hedged items, as well as its risk management objectives and strategy for undertaking various hedge transactions. This process includes linking all derivatives to specific assets and liabilities on the balance sheet or to specific firm commitments or forecasted transactions. K-Bro also assesses, both at the hedge inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are effective in offsetting changes in fair value or cash flows of hedged items. K-Bro's interest rate swaps, forward contracts or option contracts are designated as hedges when the underlying risks of the hedged and hedging instruments offset to manage K-Bro's exposure. Gains or losses relating to such contracts are accounted for as discussed above.

CRITICAL RISKS AND UNCERTAINTIES

Effects of Market Volatility and Uncertainty

See "Summary of Results and Key Events for the Year – Effects of Market Volatility and Uncertainty".

Alberta Labour Market

Alberta continues to have one of the lowest unemployment rates in Canada. With continuing high employment and competition in the workplace, K-Bro is faced with a very competitive market for workers and the inability to recruit and retain sufficient workers to process increasing volumes of business could have an adverse impact on the operations. K-Bro has taken steps on many fronts including utilizing the Temporary Foreign Worker program, adjusting wage levels, reviewing benefits and working conditions to address this situation but there can be no assurance that these will be successful. Continuance of the federally legislated Temporary Foreign Worker program in its current form is an important factor in this process but there can be no assurance of this continuance given the national unemployment rate.

Competitive Environment

K-Bro experiences competition in its markets from its public and private sector competitors. The principal elements of competition include quality, service and price. While many competitors are independent and privately-owned, certain of K-Bro's competitors are public sector entities and may have greater financial and other resources. There can be no assurance that these competitors will not substantially increase the resources devoted to the development and marketing, including discounting, of products and services that compete with those offered by K-Bro.

In addition to competition provided by its laundry processor competitors, K-Bro also competes against suppliers of single-use disposable linens, particularly in its K-Bro Operating Room ("KOR") business of providing reusable surgical packs. Management estimates that suppliers of disposable packs currently control 80% of the overall operating room linen market in Canada.

It is believed that these risks are managed primarily by entering into long-term contacts where possible, providing a comprehensive program of services that are difficult to replace, adhering to the highest possible quality and service standards and providing a cost effective service through the economies of large scale processing plants and purchasing power.

Utility Costs

K-Bro's operations utilize natural gas, electricity and water that comprise approximately 9% of its operating expenses. K-Bro's energy costs are affected by various market factors including the availability of supplies of particular forms of energy, energy prices and local and national regulatory decisions. There can be no assurance that K-Bro will be protected against substantial changes in the price or availability of energy sources. K-Bro has entered into fixed price natural gas and electricity contracts with remaining terms of up to 2 years to fix the price on a significant portion of its natural gas and electricity requirements over this time period. Upon expiration of the contracts, K-Bro will be subject to prevailing market rates. K-Bro reviews its requirements and the forward pricing regularly to determine if it's feasible and desirable to lock in additional volumes or years.

K-Bro's Calgary and Edmonton facilities currently benefit from a natural gas rebate program sponsored by the Alberta provincial government. The winter rebate program runs from October through March, when gas prices are traditionally highest. During the program, when the price of gas on most Albertans' monthly bills is over $5.50/GJ, rebates are issued. The rebate program was originally set to terminate March 31, 2006 but was extended for a further three years to March 31, 2009. There can be no assurance that the program will be renewed upon its expiry. If the rebate program is not renewed and natural gas prices continue at their present levels, K-Bro's financial results could be negatively impacted.

Credit Facility Imposes Numerous Covenants and Encumbers Assets

Covenants in the Credit Facility include, among others, ones that limit the ability of K-Bro to incur additional debt, make liens, dispose of assets, consolidate, merge or acquire other businesses, pay dividends or make other distributions (including on the common shares of K-Bro Linen Systems Inc. and the promissory notes of K-Bro Linen Systems Inc. held by the Fund), and amend material contracts. These covenants restrict numerous aspects of the business of K-Bro. Moreover, financial performance covenants require K-Bro, among other things, to maintain up to a maximum total debt-to-EBITDA ratio, no less than a minimum ratio of current assets to current liabilities and up to a maximum total fixed charge coverage ratio. The failure to comply with the terms of the Credit Facility would, after the expiration of available cure periods, entitle the bank to accelerate all amounts outstanding under the Credit Facility, and upon such acceleration, the bank would be entitled to begin enforcement procedures against the assets of K-Bro Linen Systems Inc. or the Fund, including accounts receivable, inventory and equipment. The bank would then be repaid from the proceeds of such enforcement proceedings, using all available assets. Only after such repayment and the payment of any other secured and unsecured creditors would the holders of Units receive any proceeds from the liquidation of K-Bro's assets. K-Bro's ability to satisfy the restrictive covenants may be affected by events beyond its control. K-Bro monitors its compliance on an ongoing basis, including prospectively. K-Bro has incurred no events of default under the terms of its credit facility agreement.

Income Tax Matters

On June 12, 2007, Bill C-52, which significantly modifies the income tax rules applicable to certain publicly traded or listed trusts and partnerships, was substantively enacted by the Canadian Federal Government. 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. These rules will be effective with respect to trusts which commence public trading after October 31, 2006. For trusts which were publicly traded or listed prior to November 1, 2006, the application of the rules will be delayed to the earlier or (i) the trust's 2011 taxation year, and (ii) a taxation year of the trust in which the trust exceeds normal growth as determined by reference to the normal growth guidelines, as amended from time to time, unless that excess arose as a result of a prescribed transaction.

On December 15, 2006, the Department of Finance (Canada) released the normal growth guidelines for income trusts and other flow-through entities that qualify for the four-year transitional relief. The guidance, as amended from time to time, establishes objective tests with respect to how much an income trust is permitted to grow without jeopardizing its transitional relief. If the limits described in the normal growth guidelines are exceeded, the Fund may lose its transitional relief and thereby become immediately subject to the new rules.

The Department of Finance (Canada) has tabled legislative proposals to amend the Income Tax Act (Canada) to facilitate the conversion of income trusts into corporations on a tax-deferred basis (the "Conversion Rules"). The Conversion Rules provide income trusts with tax efficient structuring options to convert to corporate form in advance of their 2011 taxation year at which time most income trusts would become subject to a new entity level tax based on corporate income tax rates. Management is reviewing the Conversion Rules to assess their implication to the Fund. There can be no assurances that the proposed amendments will be enacted as proposed or at all.

The Fund is considering these legislative changes and their possible impact to the Fund. The new rules (including the normal growth guidelines) 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 new rules apply to the Fund, the distributable cash of the Fund may be materially reduced.

Capital Investment

Laundry equipment can, with proper ongoing maintenance, remain useful for long periods of time. For example, the useful life of a tunnel washer can extend beyond 20 years. K-Bro's maintenance capital expenditures have historically been modest. Management currently expects that for the foreseeable future, the normalized level of capital expenditures required to maintain K-Bro's laundry processing operations will be approximately $850,000 per year. In 2009, K-Bro will be commencing a project to upgrade its management information systems which will increase this anticipated annual amount for 2009 and 2010.

K-Bro also funds capital expenditures necessary for growth or that result in efficiencies that provide high returns in terms of anticipated increased revenues or lower costs. The amount of these strategic capital expenditures have fluctuated over the past several years as K-Bro has selectively pursued growth opportunities through the purchase of (i) new equipment to increase capacity; (ii) equipment with an anticipated high payback from a reduction in labour and utility costs; and (iii) the purchase or construction of new laundry facilities.

The timing and amount of capital expenditures by K-Bro will indirectly affect the amount of cash available for distribution to Unitholders. Distributions may be reduced, or even eliminated, at times when K-Bro deems it necessary to make significant capital or other expenditures.

Acquisitions and Integration of Acquired Businesses

K-Bro's long-term growth strategy depends, in part, on its ability to acquire and successfully integrate and operate additional businesses. There can be no assurances that K-Bro can successfully integrate this new volume or successfully identify, negotiate, complete and integrate any future acquisitions. However, the size and scope of K-Bro's operations, the experience and reputation of its management team and its financial capacity may alleviate this risk.

Environmental Matters

K-Bro's facilities are subject to federal, provincial and municipal laws and regulations relating to the protection of the environment and worker health and safety including those governing water waste discharges, management, recycling and disposal of hazardous materials and waste, cleanup of contamination, and worker exposure to hazardous materials. K-Bro is attentive to the environmental concerns surrounding and the environmental laws regulating the disposal of its waste materials and has through the years continued to make significant investments in properly handling and disposing of these materials. K-Bro does not use toxic materials or produce hazardous waste in its laundry facilities. All waste water is discharged through the municipal sewer system in compliance with applicable regulations. Each plant's waste water is regularly tested by the relevant municipal authorities to ensure compliance with local by-laws. Compliance with environmental laws and regulations has not and is not expected to give rise, in the aggregate, to any material adverse financial or operational effects upon K-Bro's business. Environmental laws and regulations and their interpretation, however, have changed rapidly over the years and may continue to do so in the future.

CONTROLS AND PROCEDURES

In order to ensure that information with regard to reports filed or submitted under securities legislation present fairly in all material respects the financial information of K-Bro, management, including the President and Chief Executive Officer and the Vice-President and Chief Financial Officer, are responsible for establishing and maintaining disclosure controls and procedures, as well as internal control over financial reporting.

Disclosure Controls and Procedures

The Fund’s disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed by the Fund is recorded, processed, summarized and reported within the time periods specified under Canadian securities laws, and include controls and procedures that are designed to ensure that information is accumulated and communicated to management, including the President and Chief Executive Officer and the Vice-President and Chief Financial Officer, to allow timely decisions regarding required disclosure.

As of December 31, 2008, an evaluation of the effectiveness of our disclosure controls and procedures as defined in Multilateral Instrument 52-109 was performed under the supervision of the President and Chief Executive Officer and the Vice President and Chief Financial Officer who attested that the design and operation of these disclosure controls and procedures were effective, as at December 31, 2008. K-Bro’s management can therefore provide reasonable assurance that material information relating to the Fund is reported to it in a timely manner so that it can provide investors with complete and reliable information.

Management also concluded that during the three and twelve months ended December 31, 2008, no changes were made to internal controls over financial reporting that would have materially affected, or would be reasonably considered to materially affect, these controls.

Internal Controls over Financial Reporting

Management is responsible for establishing and maintaining adequate internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP. The President and Chief Executive Officer and the Chief Financial Officer assessed, or caused an assessment under their direct supervision of the design and operating effectiveness of K-Bro's internal controls over financial reporting as at December 31, 2008, and based on that assessment determined that K-Bro's internal controls over financial reporting were appropriately designed and were operating effectively in accordance with the COSO framework, published by the Committee of Sponsoring Organizations of the Treadway Commission.

No changes were made in the Fund's design of internal controls over financial reporting during the three and twelve months ended December 31, 2008, that have materially affected, or are reasonably likely to materially affect, K-Bro's internal controls over financial reporting.

A control system, no matter how well conceived and operated, can provide only reasonable, and not absolute, assurance that the objectives of the control system are met. As a result of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues, including instance of fraud, if any, have been detected. These inherent limitations include, amongst other items: (i) that managements' assumptions and judgments could ultimately prove to be incorrect under varying conditions and circumstances; or, (ii) the impact of isolated errors.

Additionally, controls may be circumvented by the unauthorized acts of individuals, by collusion of two or more people, or by management override. The design of any system of controls is also based, in part, upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential (future) conditions.

VISION

Management believes that K-Bro has the capability to deliver results and can achieve its vision of continuing to grow profitably in existing and new markets by capitalizing on its strengths and competitive advantages which include:

> **Long-Term Contracts** – K-Bro's contracts with its healthcare customers typically range from seven to ten years. Contracts in the hospitality sector typically range from two to five years. K-Bro is the exclusive provider of laundry and linen services to most of its customers. Management believes that these long standing relationships, customer knowledge, quality services and value added services may bode well when contract renewals are due such as the contract with Alberta Health Services in Edmonton due to expire December 31, 2010.
>
> **Strong Institutional Customer Base** – K-Bro's customers include a number of leading hospitals, health authorities, continuing care facilities and hotels in Canada. Healthcare customers include: Alberta Health Services (which encompasses the Calgary Health Region and Capital Health in Edmonton); The Hospital For Sick Children, Mount Sinai Hospital and St. Michael's Hospital in Toronto; and, Vancouver Coastal Health and Fraser Health (the central healthcare organizations for the greater Vancouver region). K-Bro's hospitality customers include major hotels from such well known groups as Fairmont, Westin, Delta and Hyatt. This customer base provides a strong reference list for entry into new markets or expanding services in existing markets.

Modest Maintenance Capital Expenditure Requirements – Laundry equipment can, with proper ongoing maintenance, remain operative for long periods of time. For example, the useful life of a high capacity, energy efficient tunnel washer can extend beyond 20 years. This allows for competitive pricing for existing and new customers, as well as margin improvement as additional volumes are processed without additional capital expenditure. The longevity of equipment is enhanced by having a full complement of qualified maintenance engineers at each plant performing a comprehensive on-going preventative maintenance program.

National Brand-Name Recognition and Strong Reputation – K-Bro is the largest owner and operator of laundry and linen processing plants in Canada and the only service provider with a large operation in several of Canada's largest cities. Management believes that K-Bro's size and presence in multiple markets provide it with enhanced credibility when competing for new accounts in existing markets. As well, opportunity for growth in new markets through acquisitions or new builds is also enhanced. Management believes that this reputation is also enhanced through well established “green programs’ including: an extensive reusable operating room linen program (K-Bro’s “KOR” program); effective energy use and re-use through direct fired water heaters, heat exchangers and efficient tunnel washer systems; plastic recycling programs; and, replacement of chlorine bleach with more environmentally friendly hydrogen peroxide where feasible.

Experienced Management Team and Effective Organizational Structure – The general managers at K-Bro's six laundry facilities have each been in the industry from 14 to 20 years, and four began their careers at K-Bro in other positions before being promoted to their current positions. When combined with the CEO and the CFO, the group of eight senior managers has an average of 17 years of industry experience and an average age of 46. This provides an effective combination of youth and experience which bodes well for the future success of K-Bro in achieving its vision.

K-Bro’s organizational structure has been developed to enable the general managers of its plants to focus on growth and operations in their individual markets, while enabling aggressive business development and tight management controls through K-Bro's separate corporate team.

Scalable Business Model – Each of K-Bro's plants is highly automated and has a cost structure with a significant fixed cost component. This allows the Company to generate economies of scale as volumes increase. Maintenance capital expenditures are incurred as necessary to maintain productive capacity in each plant. Strategic capital expenditures are incurred as necessary to enhance productive capacity as dictated by growth from existing or new customers. See Liquidity and Capital Resources—Investing Activities. Productive capacity can also be increased in each plant through longer operating hours; however, adequate consideration must be given to downtime for preventative maintenance as well as the availability of productive labor to perform efficiently in an expanded day.

Effective Financing Strategy – K-Bro maintains a conservative financing strategy to ensure the availability of lines of credit to fund growth as necessary. For major acquisitions or strategic capital expenditures, the equity markets will be accessed when available and it is prudent to do so. Payout ratios are kept at a prudent level giving consideration to business conditions and maintenance capital expenditures.

STRATEGY

K-Bro maintains the following three-part strategic focus:

Secure and Maintain Long-Term Contracts with Large Healthcare and Hospitality Customers – K-Bro's core service is providing high quality laundry and linen services at competitive prices to large healthcare and hospitality customers under long-term contracts. K-Bro's contracts in the healthcare sector typically range from seven to ten years in length. Contracts in the hospitality sector typically range from two to five years.

Extend Core Services To New Markets – Management has demonstrated its ability to successfully expand K-Bro's business into new markets from its established base in Edmonton and Toronto. K-Bro entered the Calgary market in 1998, the Vancouver market in 2003, the Victoria market in 2006 and the Quebec market in 2008. These new markets have contributed significantly to K-Bro's growth. Management believes that new outsourcing opportunities will continue to arise in the near to medium-term and that K-Bro is well-positioned for continued growth, particularly as healthcare and hospitality institutions continue to increase their focus on core services and confront pressures for capital and cost savings.

Management may in the future expand its core services to new markets either through acquisitions or by establishing new facilities. Its choice of areas for expansion will depend on the availability of suitable acquisition candidates, the volume of healthcare linen to be processed and the policies of applicable governments.

Introduce Related Services – In addition to focusing on its core services, K-Bro also attempts to capitalize on attractive business opportunities by introducing closely-related services that enable it to provide more complete solutions to the K-Bro's healthcare customers. These related service offerings include K-Bro Operating Room Services ("KOR") and on-site services. For three major hospitals in Toronto, K-Bro has introduced the sterilization of operating room linen packs to its menu of services.

FINANCIAL STATEMENTS

MANAGEMENT'S REPORT

Management is responsible for the integrity and objectivity of the financial information presented in this Annual Report. The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles. The financial information presented elsewhere in this annual report is consistent with that shown in the accompanying consolidated financial statements.

Management maintains a system of internal controls to provide reasonable assurance at to the reliability of financial information and the safeguarding of assets. The consolidated financial statements include amounts that are based on the best estimates of management.

The Board of trustees is responsible for ensuring management fulfills its responsibilities for financial reporting and internal control. The Board carries out this responsibility principally through its Audit Committee. The Audit Committee, which consists solely of non-management trustees, reviews the consolidated financial statements and recommends them to the Board for approval. The fund's auditors PricewaterhouseCoopers LLP have full and unrestricted access to the Audit Committee and meet periodically with them (and separately, in the absence of management) to discuss audit, financial reporting and related matters.

Linda McCurdy	Doug Thomson, FCA
President and Chief Executive Officer	Vice President and Chief Financial Officer

AUDITORS' REPORT

March 12, 2009

To the Unitholders of K-Bro Linen Income Fund

We have audited the consolidated balance sheets of **K-Bro Linen Income Fund** as at December 31, 2008 and 2007 and the consolidated statements of earnings and deficit, comprehensive income and cash flows for the years then ended. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Fund as at December 31, 2008 and 2007 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

Chartered Accountants

Edmonton, Canada

K-Bro Linen Income Fund

Consolidated Balance Sheets

	As at December 31, 2008 $	2007 $
Assets		
Current assets		
Accounts receivable	**8,669,939**	9,141,721
Linen in service	**7,755,839**	8,560,077
Prepaid expenses and deposits	**623,953**	837,212
Future income taxes (note 10)	**426,032**	-
	17,475,763	18,539,010
Restricted escrow funds (note 3)	**540,500**	-
Deferred charges (note 4)	**132,631**	-
Property, plant and equipment (note 5)	**36,024,039**	31,864,330
Intangible assets (note 6)	**16,073,218**	17,373,196
Goodwill (note 3)	**15,679,750**	15,565,799
	85,925,901	83,342,335
Liabilities and Unitholders' Equity		
Current liabilities		
Accounts payable and accrued liabilities	**12,884,895**	12,540,726
Distribution payable to unitholders	**642,146**	503,843
Future income taxes (note 10)	**-**	106,603
	13,527,041	13,151,172
Long-term debt (note 7)	**4,061,285**	16,627,107
Unamortized lease inducements (note 9)	**520,144**	576,376
Future income taxes (note 10)	**3,955,645**	4,744,968
	22,064,115	35,099,623
Contingencies and commitments (note 11)		
Unitholders' Equity		
Exchangeable shares (note 12b)	**724,110**	724,110
Fund units (note 12b)	**70,675,516**	52,210,472
Fund units held in trust by LTIP (note 13)	**(457,079)**	(533,603)
Contributed surplus (note 12c)	**340,728**	413,671
Deficit	**(7,309,749)**	(4,573,837)
Accumulated other comprehensive (loss) income (note 12d)	**(111,740)**	1,899
	63,861,786	48,242,712
	85,925,901	83,342,335

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

Approved on behalf of the Fund

Ross Smith
Trustee

Matthew Hills
Trustee

K-Bro Linen Income Fund

Consolidated Statements of Earnings and Deficit

	Year ended December 31,	
	2008	2007
	$	$
Revenue	85,113,294	74,100,941
Expenses		
Wages and benefits	40,142,329	37,334,778
Linen	10,238,433	9,396,962
Utilities	6,626,307	5,728,452
Delivery	3,643,869	2,780,344
Occupancy costs	3,032,291	2,405,533
Repairs and maintenance	3,008,801	2,227,415
Materials and supplies	2,914,738	2,465,795
Corporate	3,111,187	2,573,468
	72,717,955	64,912,747
Earnings before the undernoted	12,395,339	9,188,194
Other income (expenses)		
Amortization of property, plant and equipment	(5,053,611)	(3,684,034)
Amortization of intangible assets	(2,149,978)	(2,071,184)
Financial charges (note 8)	(686,731)	(879,747)
(Loss) gain on disposal of property, plant and equipment	(506,668)	2,838
	(8,396,988)	(6,632,127)
Earnings before income taxes	3,998,351	2,556,067
Income tax recovery (note 10)	819,737	1,558,114
Net earnings for the year	4,818,088	4,114,181
Deficit – beginning of year	(4,573,837)	(2,641,898)
Distributions to unitholders (note 14)	(7,554,000)	(6,046,120)
Deficit– end of year	(7,309,749)	(4,573,837)
	$	$
Net earnings per unit		
Basic	0.72	0.75
Diluted	0.71	0.75
	#	#
Weighted average number of units outstanding (note 12e)		
Basic	6,719,305	5,464,487
Diluted	6,747,522	5,498,318

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

K-Bro Linen Income Fund

Consolidated Statements of Comprehensive Income

	Year ended December 31,	
	2008	**2007**
	$	**$**
Net earnings for the year	**4,818,088**	4,114,181
Other comprehensive loss		
Unrealized loss on derivative instruments designated as cash flow hedges, net of future income taxes of $50,340 (2007 – $13,156)	**(113.639)**	(26,186)
Other comprehensive loss for the year	**(113,639)**	(26,186)
Comprehensive income for the year	**4,704,449**	4,087,995

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

K-Bro Linen Income Fund

Consolidated Statements of Cash Flows

	Year ended December 31,	
	2008	**2007**
	$	**$**
Cash provided by (used in)		
Operating activities		
Net earnings for the year	**4,818,088**	4,114,181
Items not affecting cash		
Amortization of property, plant and equipment	**5,053,611**	3,684,034
Amortization of intangible assets	**2,149,978**	2,071,184
Amortization of lease inducements	**(42,174)**	-
Loss (gain) on disposal of property, plant and equipment	**506,668**	(2,838)
Future income taxes	**(819,737)**	(1,558,114)
	11,666,434	8,308,447
Net change in non-cash working capital items (note 15)	**3,788,404**	(1,366,321)
Cash provided by operating activities	**15,454,838**	6,942,126
Financing activities		
Fund units issued – net of issue costs	**18,092,544**	-
Distributions paid to unitholders	**(7,415,697)**	(6,046,120)
(Decrease) increase in long term debt revolving line of credit	**(12,565,822)**	7,348,678
Cash (used) provided by financing activities	**(1,888,975)**	1,302,558
Investing activities		
Purchase of property, plant and equipment	**(9,744,642)**	(8,294,811)
Business acquisition (note 3)	**(3,311,349)**	-
Escrow funds (note 3)	**(540,500)**	-
Deferred charges (note 4)	**(132,631)**	-
Proceeds from disposal of equipment	**163,259**	50,127
Cash used in investing activities	**(13,565,863)**	(8,244,684)
Change in cash	**-**	-
Cash – beginning of year	**-**	-
Cash – end of year	**-**	-
Supplementary cash flow information		
Interest paid	**533,361**	820,751
Non-cash financing and investing activities		
Equipment purchases included in accounts payable and accrued liabilities	**1,082,763**	3,091,099
Distribution included in distribution payable	**138,303**	-
Leasehold improvements included in lease inducements	**-**	576,376

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

1 Business description

K-Bro Linen Income Fund (the "Fund") is a limited purpose trust established under the laws of Alberta pursuant to the Amended and Restated Fund Declaration of Trust dated February 3, 2005. The Fund was created for the purpose of acquiring, directly or indirectly, all of the issued and outstanding securities of K-Bro Linen Systems Inc. K-Bro Linen Systems Inc. provides a range of services to healthcare institutions, hotels and other commercial accounts. These services include the processing, management and distribution of linen.

2 Significant accounting policies

These consolidated financial statements have been prepared by management in accordance with accounting principles generally accepted in Canada. The precise determination of many assets and liabilities is dependent upon future events. Accordingly, the preparation of financial statements for a reporting period necessarily involves the use of estimates and approximations which have been made using careful judgment. Actual results could differ from those estimates. These consolidated financial statements have, in management's opinion, been properly prepared within reasonable limits of materiality and within the framework of the accounting policies summarized below.

a) Basis of presentation

These consolidated financial statements include the Fund, its wholly owned subsidiary K-Bro Linen Systems Inc. and the LTIP Trust, a variable interest entity (note 13). All material intercompany balances and transactions have been eliminated upon consolidation. These consolidated financial statements are for the years ended December 31, 2008 and 2007.

b) Linen in service

Linen in service is recorded at cost. Operating room linen is amortized using the straight-line method over the estimated service life of 24 months. General linen is amortized based on usage which results in an estimated average service life of 24 months.

c) Revenue recognition

Revenue from linen management and laundry services is largely based on written service agreements whereby the Fund agrees to collect, launder, deliver and replenish linens. The Fund recognizes revenue in the period in which the services are provided.

d) Property, plant and equipment

Property, plant and equipment are recorded at cost. Amortization is provided over the estimated useful life of the asset using the following annual rates and methods:

Building	5% declining balance
Laundry equipment	15% declining balance
Office and delivery equipment	20% declining balance
Computers and software	30% declining balance
Leasehold improvements	Straight-line over the initial lease period
Asset under development	At applicable rates and methods when put into service

e) Intangible assets

Intangible assets with a finite life, which relate to contracts the Fund has with certain customers, are recorded at cost and are amortized using the straight-line method over the remaining life of the contract plus one renewal period, ranging from 13 months to 169 months.

f) Impairment of long-lived assets

The Fund assesses impairment of its long-lived assets (property, plant and equipment and finite life intangible assets) when events or changes in circumstances cause the carrying value of an asset to exceed the total undiscounted cash flows expected from its use and eventual disposition. An impairment loss, if any, is determined as the excess of the carrying value of the asset over its fair value.

g) Future income taxes

The Fund is a mutual fund trust for income tax purposes. As such, the Fund is currently only taxable on any amount not distributed to unitholders and income tax liabilities relating to distributions of the Fund are taxed in the hands of the unitholders. As substantially all taxable income is distributed to the unitholders, no provision for current income taxes on earnings of the Fund is made in the financial statements. On June 11, 2007, the Canadian federal government substantively enacted legislation whereby the income tax rules applicable to publicly traded trusts was significantly modified. In particular, income earned by a trust will be taxed in a manner similar to income earned and distributed by a corporation. The legislation is effective for the 2007 taxation year, but the application of the rules is delayed to the 2011 taxation year with respect to trusts that were publicly traded prior to November 1, 2006 within certain guidelines. For the Fund, only temporary differences expected to reverse after January 1, 2011 are taken into account in the determination of the provision for income taxes.

The incorporated subsidiary of the Fund calculates income taxes using the liability method of accounting. Temporary differences arising from the difference between the tax basis of an asset or liability and its carrying amount on the balance sheet are used to calculate future income tax liabilities or assets. Future income tax liabilities or assets are calculated using substantively enacted tax rates applicable to the period that the temporary differences are expected to reverse. Future income tax assets are only recognized to the extent that, in the opinion of management, they will more likely than not be utilized. The effect on future income tax assets or liabilities is recognized in income in the period that the change occurs.

Income tax obligations relating to distributions of the Fund are the obligations of the unitholders and, accordingly, no provision for income taxes has been made in respect of the assets and liabilities of the Fund. The enactment of the new legislation did not have a significant impact on the Fund's consolidated financial statements.

h) Goodwill

Goodwill represents the excess of the cost of business acquisitions over the fair value of net identifiable assets acquired. Goodwill is not amortized but is tested for impairment annually or more frequently if changes in circumstances indicate a potential impairment. Goodwill will be written down when the carrying value exceeds the fair value. Management has determined that there was no goodwill impairment at December 31, 2008 or 2007.

i) Volume rebates

Certain customers receive a rebate based on specified annual processing volumes. A volume rebate liability is recognized at the time it is expected that the customer will meet the specified annual volume levels.

j) Financial instruments

The Fund has made the following classifications:

- Cash and temporary investments will be classified as financial assets held for trading and measured at fair value. Gains and losses related to periodical revaluation are recorded in net income.

- Accounts receivable are classified as loans and receivables and are initially measured at fair value and subsequent periodical revaluations are recorded at amortized cost using the effective interest rate method.

- Accounts payable and accrued liabilities, distribution payable and long-term debt are classified as other liabilities and are initially measured at fair value and subsequent periodical revaluations are recorded at amortized cost using the effective interest rate method.

Initially, all financial assets and financial liabilities must be recorded on the balance sheet at fair value. Subsequent measurement is determined by the classification of each financial asset and liability. Unrealized gains and losses on financial assets that are held as available for sale are recorded in other comprehensive income until realized, at which time they will be recorded in the consolidated statement of earnings. All derivatives, including embedded derivatives that must be separately accounted for, are recorded at fair value in the consolidated balance sheet. Transaction costs related to financial instruments are generally capitalized and then amortized over the expected life of the financial instrument using the effective yield method.

k) Adoption of new accounting policies

(i) Capital disclosures

On January 1, 2008, the Fund adopted Section 1535 of the Canadian Institute of Chartered Accountants' ("CICA") Handbook, "Capital Disclosures." This Section requires the disclosure of both qualitative and quantitative information that provides users of financial statements with information to evaluate the entity's objectives, policies and processes for managing capital. The adoption of this standard did not have an impact on the consolidated financial statements as the standard relates to note disclosure as per Note 17.

(ii) Financial instruments-disclosure and Financial instruments-presentation

On January 1, 2008, the Fund adopted Section 3862 "Financial Instruments– Disclosure" and Section 3863 "Financial Instruments – Presentation" of the CICA Handbook. These sections replace Section 3861 "Financial Instruments – Disclosure and Presentation." The objective of Section 3862 is to provide users with information to evaluate the significance of the financial instruments on the entity's financial position and performance, the nature and extent of risks arising from financial instruments, and how the entity manages those risks. The provisions of Section 3863 deal with the classification of financial instruments, related interest, dividends, losses and gains and the circumstances in which financial assets and financial liabilities are offset. The adoption of these standards did not have an impact on the consolidated financial statements as the standards relate to note disclosure as per Note 16.

(iii) Inventories

On January 1, 2008, the Fund adopted Section 3031 of the CICA Handbook, "Inventories." This Section replaces the previous standard for inventories, Section 3030. Adoption of this standard had no impact on the consolidated financial statements.

l) Future changes in accounting policies

(i) Goodwill and intangible assets

In February 2008, the CICA issued a new accounting standard – Section 3064 "Goodwill and intangible assets" which replaces the existing standard for goodwill and other intangible assets in Section 3062 and research and development costs in Section 3450. The new Section is effective for the Fund beginning January 1, 2009; however, earlier adoption is encouraged. It establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented enterprises. Standards concerning goodwill are unchanged from the standards included in the previous Section 3062. In accordance with this new policy, deferred charges at December 31, 2008 of $132,631 will be written off retrospectively against equity in 2009 with restatement of comparative amounts.

(ii) International Financial Reporting Standards

The Accounting Standards Board of Canada has announced that accounting standards in Canada, as used by public companies, will be converged to International Financial Reporting Standards ("IFRS") effective January 1, 2011. The Fund will convert to these new standards according to the timetable set with these new rules. The changeover date is for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011.

IFRS uses a conceptual framework similar to Canadian GAAP but there are significant differences in recognition, measurement and disclosure requirements. As a result, the Fund has established a changeover plant to convert to these new standards according to the timetable set with these new rules. An implementation plan has been created and will be executed primarily with internal resources. The Fund will complete the scoping and diagnostic phase in the first quarter of 2009 and will then move to the impact analysis and design phase. The Fund's preliminary analysis of IFRS in comparison to Canadian GAAP has identified a number of differences. At this time, the impact on our future financial position and results of operations is not reasonably determinable or estimable. The Fund will continually review and adjust the changeover plan to ensure the implementation process properly addresses the key elements of the plan.

(iii) Business combinations

Section 1582 "Business combinations" will be applicable to business combinations for which the acquisition date is on or after the Fund's interim and fiscal year beginning January 1, 2011. Early adoption is permitted. The section improves the relevance, reliability and comparability of the information that a reporting entity provides in its financial statements about a business combination and it effects. The Fund has not yet determined the impact of the adoption of this new Section on the consolidated financial statements.

(iv) Consolidated financial statements

Section 1601 "Consolidated financial statements" will be applicable to financial statements relating to the Fund's interim and fiscal year beginning on or after January 1, 2011. Early adoption is permitted. This section establishes standards for the preparation of consolidated financial statements. The Fund has not yet determined the impact of the adoption of this new Section on the consolidated financial statements.

(v) Non-controlling interests

Section 1602 "Non-controlling interests" will be applicable to financial statements relating to the Fund's interim and fiscal year beginning on or after January 1, 2011. Early adoption is permitted. This section establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. The Fund has not yet determined the impact of the adoption of this new Section on the consolidated financial statements.

3 Business acquisition

On January 31, 2008, the Fund completed the acquisition of the laundry business, linen, property and equipment of Buanderie HMR Inc. located in Quebec City, Quebec. The business acquisition has been accounted for using the purchase method, whereby the purchase consideration was allocated to the fair values of the net assets acquired at January 31, 2008. The allocation is based on management's best estimate of the fair value of net assets acquired.

The purchase price allocated to the net assets acquired, based on their estimated fair values, is as follows:

	$
Consideration	
Purchase price including acquisition costs	**3,851,849**
Less	
Restricted escrow funds	**(540,500)**
Net cash consideration	**3,311,349**
Net assets acquired	
Net working capital	**62,397**
Linen	**125,000**
Property, plant and equipment	**2,160,000**
Intangible assets	**850,000**
Goodwill	**113,952**
	3,311,349

Of the cash consideration payable to the vendor, $540,500 was deposited into escrow with an escrow agent. The full amount of the funds held in escrow will be released to the vendor in 2009 upon the determination that specified earnings before interest, income taxes and amortization were met in the twelve-month period subsequent to the acquisition. Goodwill will be correspondingly increased by the amount released. Management expects that the full amount will be paid to the vendor by March 31, 2009.

4 Deferred charges

Deferred charges relate to net expenditures during the pre-operating period of the new Calgary plant, which are being amortized on a straight-line basis over the ten-year period of the associated lease. These charges will be written off in 2009 as per Note 2l(i).

5 Property, plant and equipment

			2008
	Cost **$**	**Accumulated amortization** **$**	**Net** **$**
Land	**70,000**	**-**	**70,000**
Building	**550,013**	**25,209**	**524,804**
Equipment			
Laundry[(1)]	**34,865,253**	**10,047,651**	**24,817,602**
Office	**644,938**	**147,653**	**497,285**
Delivery	**467,656**	**204,865**	**262,791**
Computers and software	**1,293,542**	**616,283**	**677,259**
Leasehold improvements	**10,985,452**	**1,811,154**	**9,174,298**
	48,876,854	**12,852,815**	**36,024,039**

(1) Of this total, $1,082,763 is included in accounts payable.

			2007
	Cost **$**	**Accumulated amortization** **$**	**Net** **$**
Equipment			
Laundry	25,740,872	6,925,484	18,815,388
Office	219,308	86,151	133,157
Delivery	433,578	158,466	275,112
Computers and software	845,624	420,855	424,769
Leasehold improvements	3,413,524	1,261,552	2,151,972
Asset under development-new Calgary plant[(2)]	10,063,932	-	10,063,932
	40,716,838	8,852,508	31,864,330

(2) Of this total, $3,091,099 is included in accounts payable and $576,376 is included in unamortized lease inducements.

6 Intangible assets

			2008
	Cost $	Accumulated amortization $	Net $
Finite life intangible assets			
Healthcare contracts	15,700,000	4,418,441	11,281,559
Operating room contracts	3,500,000	1,912,790	1,587,210
Hospitality contracts	4,697,000	1,492,551	3,204,449
	23,897,000	7,823,782	16,073,218

			2007
	Cost $	Accumulated amortization $	Net $
Finite life intangible assets			
Healthcare contracts	15,700,000	3,290,328	12,409,672
Operating room contracts	3,500,000	1,424,418	2,075,582
Hospitality contracts	3,847,000	959,058	2,887,942
	23,047,000	5,673,804	17,373,196

7 Long-term debt

K-Bro Linen Systems Inc. has a revolving credit facility of up to $30,000,000 of which $4,496,285 is drawn (including letters of credit totalling $435,000 per note 11(a)). The facility is a two-year committed facility maturing February 28, 2010. It is extendable annually for another year at the lender's option and subsequent to December 31, 2008 it was extended to February 28, 2011. Interest payments only are due during the term of the facility.

A general security agreement over all assets, a mortgage against all leasehold interests and real property, insurance policies and an assignment of material agreements have been pledged as collateral.

Drawings under the revolving credit facility are available by way of Bankers' Acceptances, Canadian prime rate loans, letters of credit or standby letters of guarantee. Drawings under the revolving credit facility bear interest at a floating rate, plus an applicable margin based on certain financial performance ratios. At December 31, 2008 for Bankers' Acceptances the margin varied from 2.00% to 3.00% and for Canadian prime rate loans, the margin varied from 0.50% to 1.50%. Subsequent to December 31, 2008, these margins in each case were increased by 0.50%.

The balance consists of:

	2008 $	2007 $
Bankers' Acceptances, 3.64% (2007 – 7.10%)	**4,000,000**	4,000,000
Prime rate loan, 4.00% (2007 – 7.00%)	**61,285**	12,627,107
	4,061,285	16,627,107

8 Financial charges

	Year ended December 31, 2008 $	2007 $
Interest on long-term debt	**533,361**	820,751
Other charges	**153,370**	58,996
	686,731	879,747

9 Unamortized lease inducements

Lease inducements are received from certain of the Fund's landlords, primarily in the form of leasehold improvements and rent-free periods. Lease inducements are recorded as a liability when credited or received and will be amortized on a straight-line basis as a reduction of rent expense over the term of the related lease. For lease contracts with escalating lease payments, total rent expense for the lease term is expensed on a straight-line basis over the lease term. The difference between rent expensed and amounts paid will be recorded as an increase or reduction in deferred lease inducements.

The Fund entered into a ten-year lease for a new facility in Calgary in 2007 which included certain lease inducements. These inducements totalling $585,748 include leasehold improvements and a rent-free period. Accumulated amortization at December 31, 2008 is $65,604 (December 31, 2007 – $9,372). Of this accumulated amortization at December 31, 2008, $23,430 (December 31, 2007 – $9,372) was capitalized during the pre-opening period to leasehold improvements.

10 Income taxes

A reconciliation of the expected income tax recovery (expense) to the actual income tax recovery (expense) is as follows:

	Year ended December 31, 2008 $	2007 $
Canadian statutory rates (federal and provincial)	**30.7%**	33.4%
Expected expense for income taxes	**(1,227,094)**	(853,726)
Change resulting from:		
Non-deductible items	**(42,471)**	(24,235)
Impact of substantively enacted rates and other	**(110,671)**	559,529
Income of the Fund allocated to unitholders	**2,199,973**	1,876,546
Actual provision for income tax recovery	**819,737**	1,558,114

Future income tax assets (liabilities) are attributable to the following items:

	Year ended December 31, 2008 $	2007 $
Linen in service	**172,119**	(299,969)
Accounts payable and accrued liabilities	**253,913**	193,366
Current future income tax asset (liability)	**426,032**	(106,603)
Property and equipment	**(725,530)**	(1,022,216)
Intangible assets and goodwill	**(3,767,294)**	(4,304,982)
Offering costs and other	**537,179**	582,230
Long-term future income tax liability	**(3,955,645)**	(4,744,968)
Future income tax liability, net	**(3,529,613)**	(4,851,571)

The benefit of deductible temporary differences of $300,000 (2007 – $600,000) relating to offering costs borne directly by the Fund have not been recorded. The amount of goodwill deductible for tax purposes is $3,321,984 (2007 – $3,208,033).

11 Contingencies and commitments

a) Contingencies

Letters of credit

The Fund has outstanding letters of credit issued as part of normal business operations in the amounts of $185,000 (2007 – $185,000) expiring January 21, 2010 and $250,000 (2007 – $250,000) expiring January 24, 2010.

b) Commitments

Operating leases and utility commitments

Minimum lease payments for operating leases on buildings and equipment and estimated natural gas and electricity commitments for the next five years are as follows:

	$
2009	**4,602,991**
2010	**3,242,505**
2011	**2,052,890**
2012	**1,971,456**
2013	**1,771,144**
Subsequent	**3,971,850**

Linen purchase commitments

At December 31, 2008, the Fund was committed to linen expenditure obligations in the amount of $2,196,023 (December 31, 2007 – $2,741,266).

Equipment purchase commitments

The Fund has commitments to purchase equipment totalling $nil at December 31, 2008 (December 31, 2007 – $126,000).

12 Unitholders' equity

a) Authorized

The declaration of trust provides that an unlimited number of units and an unlimited number of Special Trust Units may be issued.

b) Issued and outstanding

On February 27, 2008 the Fund completed the issuance of 1,362,000 Units at a price of $12.85 per Unit. Net proceeds to the Fund after commission and expenses, net of tax, were $16.7 million. The underwriters were also granted an over-allotment option, exercisable in whole or in part for a period of 30 days following closing, to purchase up to an additional 204,300 units at the same offering price. On March 28, 2008, the over-allotment option was exercised in part and 146,700 additional Units were issued at a price of $12.85 per Unit. Net proceeds to the Fund after commission and expenses, net of tax, were $1.8 million.

Fund Units	#	$
Balance at December 31, 2007 and 2006	5,423,862	52,210,472
Issued on February 27, 2008 at $12.85 per Unit	1,362,000	17,501,700
Offering costs – net of future tax recovery of $341,000		(842,959)
Issued on March 28, 2008 at $12.85 per Unit	146,700	1,885,095
Offering costs – net of future tax recovery of $31,500		(78,792)
	1,508,700	18,465,044
Balance at December 31, 2008	**6,932,562**	**70,675,516**

Exchangeable shares	#	$
Balance at December 31, 2008 and 2007	**72,411**	**724,110**
Total Fund Units and Exchangeable shares issued	**7,004,973**	

The exchangeable shares were issued by the Fund's subsidiary to certain members of management and are exchangeable on a one-to-one basis for Fund Units. The risks and privileges of these shares are the same as for Fund Units. The exchangeable shares of the Fund's subsidiary are synonymous with the Special Trust Units of the Fund.

c) Contributed surplus

	Year ended December 31, 2008 $	2007 $
Balance, beginning of year	**413,671**	184,635
Net stock based compensation recorded	**319,628**	302,294
Issuance of vested Units to participants	**(392,571)**	(73,258)
Balance, end of year	**340,728**	413,671

d) Accumulated other comprehensive (loss) income

	Year ended December 31, 2008 $	2007 $
Balance, beginning of year, as previously reported	**1,899**	-
Financial instruments – recognition and measurement	**-**	28,085
Restated balance, beginning of year	**1,899**	28,085
Other comprehensive loss during the year	**(113,639)**	(26,186)
Balance, end of year	**(111,740)**	1,899

e) Weighted average number of units outstanding

	Year ended December 31, 2008 #	2007 #
Weighted average unit calculation		
Basic		
Units – opening	**5,496,273**	5,496,273
Weighted average units issued during the year	**1,262,115**	-
Weighted average unvested units purchased for LTIP	**(39,083)**	(31,786)
Weighted average units for the year	**6,719,305**	5,464,487
Diluted		
Basic weighted average units	**6,719,305**	5,464,487
Dilutive effect of LTIP units	**28,217**	33,831
	6,747,522	5,498,318

13 Long Term Incentive Plan

In April, 2006, a trust (the "LTIP Trust") was formed to hold Units of the Fund on behalf of the participants of the Fund's long-term incentive plan (the "LTIP"). The Fund is neither a trustee nor a direct participant of the LTIP; however, under certain circumstances the Fund may be the beneficiary of forfeited Units held by the LTIP Trust. Consequently, the LTIP Trust is considered a variable interest entity for accounting purposes and the Fund has consolidated the LTIP Trust in accordance with the CICA issued Accounting Guideline AcG-15. For a specific performance year, one-quarter of the Units held by the LTIP Trust vest to the participants of the LTIP thirty days after approval of the audited financial statements by the Trustees upon the participant signing a Participation Agreement and Confirmation and three-quarters will vest on the second anniversary of that date upon continued employment, except in limited circumstances. Compensation expense is recorded by the Fund in the period earned. Distributions made by the Fund with respect to unvested Units held by the LTIP Trust are paid to LTIP participants. Unvested units held by the LTIP Trust are shown as a reduction of unitholders' equity.

In accordance with the LTIP agreement and in conjunction with the performance of the Fund in the prior fiscal year, the Compensation, Nominating and Corporate Governance Committee of the Trustees of the Fund in 2008 approved LTIP compensation of $0.3 million (2007 – $0.3 million) and approved the funding and transfer of $0.3 million (2007 – $0.3 million) of cash to the LTIP Trust in March 2008 and April 2007 respectively in order to fund the purchase of Units by the LTIP Trust. In March 2008, the LTIP Trust purchased 24,751 Units of the Fund (2007 – 22,647). As at December 31, 2008, 38,961 Units held by the LTIP Trust have vested (December 31, 2007 – 12,436).

The basic net earnings per unit calculation exclude the unvested units held by the LTIP Trust.

14 Distributions to unitholders

The Fund's policy is to make distributions to unitholders of its available cash to the maximum extent possible consistent with good business practice considering requirements for capital expenditures, working capital, growth capital and other reserves considered advisable by the Trustees of the Fund. All such distributions are discretionary. Distributions are declared payable each month to the Fund unitholders and exchangeable shareholders on the last business day of each month and are paid by the 15th day of the following month.

During the year ended December 31, 2008, the Fund declared total distributions to Unitholders and Exchangeable Unitholders of $7,554,000 (2007 – $6,046,120) or $1.10 per unit (2007 – $1.10).

15 Net change in non-cash working capital items

	Year ended December 31, 2008	2007
Cash provided (used) by changes in	**$**	**$**
Accounts receivable	**719,182**	(1,700,543)
Linen in service	**929,238**	(66,776)
Prepaid expenses and deposits	**188,696**	(316,792)
Accounts payable and accrued liabilities	**1,951,288**	717,790
	3,788,404	(1,366,321)

16 Financial instruments

Fair value

The Fund's financial instruments at December 31, 2008 consist of accounts receivable, accounts payable and accrued liabilities, distribution payable to unitholders, long-term debt, and an interest rate swap agreement. The carrying value of accounts receivable, accounts payable and accrued liabilities, and distribution payable to unitholders approximate fair value due to the immediate or short-term maturity of these financial instruments. The fair value of the Fund's long-term debt is estimated based on market prices for same or similar instruments and approximates carrying value. The interest rate swap agreement is a derivative designated as an effective hedge and is measured at fair value with subsequent changes in fair value being charged to other comprehensive income.

Financial risk management

The Fund's activities are exposed to a variety of financial risks: price risk, credit risk and liquidity risk. The Fund's overall risk management program focuses on the unpredictability of financial and economic markets and seeks to minimize potential adverse effects on the Fund's financial performance. Risk management is carried out by financial management in conjunction with overall Fund governance.

Price risk

There are three types of price risk:

Currency risk – Foreign currency risk arises from the fluctuations in foreign exchange rates and the degree of volatility of these rates relative to the Canadian dollar. The Fund is not significantly exposed to foreign currency risk as all revenues are received in Canadian dollars and minimal expenses are incurred in foreign currencies. For large capital expenditure commitments denominated in a foreign currency, the Fund will enter into foreign exchange forward contracts if considered prudent to mitigate this risk. At December 31, 2008, no foreign exchange forward option contracts were outstanding. Based on the Fund's US dollar liability for equipment purchases at December 31, 2008, a 1% change in the Canadian-US dollar foreign exchange rate would result in a $7,500 change in the amount recorded in property, plant and equipment.

Interest rate risk – The Fund is subject to interest rate risk as its credit facility bears interest at rates that depend on certain financial ratios of the Fund and vary in accordance with market interest rates. On June 24, 2005, the Fund entered into an interest rate swap arrangement whereby the interest rate paid on a notional amount of $4 million of this debt has been fixed at 5.95% for a period of five years. The floating rate of interest that was swapped for this fixed rate is currently at 3.64%. Based on the outstanding balance on the Fund's revolving credit facility for which the interest rate has not been fixed at December 31, 2008, a 1% fluctuation in the Canadian prime rate would result in a negligible change in annual interest expense. Management does not believe that the impact of interest rate fluctuations will be significant.

Other price risk – The Fund's exposure to other price risk is limited since there are no significant financial instruments which fluctuate as a result of changes in market prices.

Credit risk

The Fund's financial assets that are exposed to credit risk consist primarily of accounts receivable and an interest rate swap agreement. The Fund, in the normal course of business, is exposed to credit risk from its customers. The Fund is exposed to credit loss in the event of non-performance by counterparties to the interest rate swap. Management believes that the risks associated with concentrations of credit risk with respect to accounts receivable and the interest rate swap are limited due to the nature of the customers and the swap counterparty serviced by the Fund and the generally short payment terms and frequent settlement of swap differences.

The following outlines the details of the aging of the Fund's receivables and related allowance for doubtful accounts:

	2008 $
Current	6,701,444
Past due amounts:	
1 – 30 days	1,851,171
Greater than 30 days	160,028
Less: allowance for doubtful accounts	(42,704)
Accounts receivable, net	8,669,939

Liquidity risk

The Fund has long-term debt with a maturity date of February 28, 2010 (see note 7). Subsequent to December 31, 2008 this maturity date was extended to February 28, 2011. The degree to which the Fund is leveraged may reduce its ability to obtain additional financing for working capital and to finance investments to maintain and grow the current levels of cash flows from operations. The Fund may be unable to extend the maturity date of the credit facility.

Management, to reduce liquidity risk, has historically renewed the terms of the credit facility in advance of its maturity dates and the Fund has maintained financial ratios that management believes are conservative compared to financial covenants applicable to the credit facility. A significant portion of the available facility remains undrawn.

Management measures liquidity risk through comparisons of current financial ratios with financial covenants contained in the credit facility.

Hedge accounting

Where derivatives are held for risk management purposes or when transactions meet the criteria, including documentation requirements, specified in the CICA Handbook Section 3865, hedge accounting is applied to the risks being hedged. When hedge accounting is not applied, the change in the fair value of the derivative is recognized in earnings.

The Fund applied hedge accounting on the interest rate swap agreement outstanding at December 31, 2008.

17 Capital management

The Fund views its capital resources as the aggregate of its debt, unitholders' equity, internally generated funds, amounts available under credit facilities and cash on hand. In general, the overall capital of the Fund is evaluated and determined in the context of its financial objectives and its strategic plan.

With respect to its level of indebtedness, the Fund determines the appropriate level in the context of its cash flow and overall business risks. The Fund has historically generated cash flow in excess of distributions and has used such excess to fund capital expenditures, working capital, growth capital and other reserves considered advisable by the Trustees of the Fund. The Fund would consider increasing its level of indebtedness relative to cash flow to assist in the financing of an acquisition or expansion. As well, the Fund will review its level of indebtedness in the context of the change in taxation impacting the Fund commencing 2011.

The Fund's indebtedness is subject to a number of covenants and restrictions including the requirement to meet certain financial ratios and financial condition tests which are subject to an appropriate cure period if necessary. One such ratio is the Total Funded Debt / EBITDA Ratio as defined in the credit facility (see note 7). The maximum ratio allowed for a 12-month trailing period is 2.75, which is increased to 3.25 for the two quarters immediately following an acquisition. For the twelve months ended December 31, 2008, this ratio was calculated at 0.38 (twelve months ended December 31, 2007 – 1.86). Management also uses this ratio as a key indicator in managing the Fund's capital. EBITDA is defined in the credit facility as net earnings plus interest expense, income taxes, and amortization expense. For the purpose of the calculation of the Fund's financial ratios under the credit facility, EBITDA is calculated on a rolling four quarter basis.

With respect to its equity, the current level of capital is considered adequate in the context of current operations and the present strategic plan of the Fund. Any major acquisitions or expansions may be financed in part with additional equity. The Fund will also review its level of equity in the context of the change in taxation impacting the Fund commencing 2011.

The Fund's capital resources, comprised of long-term debt, unitholders' equity and amounts available under its committed revolving credit facility, totalled \$93.4 million at December 31, 2008 (2007 – \$77.8 million). Available liquidity as at December 31, 2008 consisting of unused committed revolving credit facility was \$25.5 million (2007 – \$12.9 million). The Fund has incurred no events of default under the terms of its credit facility agreement.

18 Segmented information

The Fund provides laundry and linen services to the healthcare and hospitality sectors through six operating segments in Vancouver, Victoria, Calgary, Edmonton, Toronto and Quebec City. The services offered and the economic characteristics associated with these segments are similar, therefore these segments have been aggregated into one reportable segment which operates exclusively in Canada. The results of the Quebec City operation acquired (see note 3) are reported commencing February 1, 2008.

Total revenue derived from the healthcare and hospitality sectors are as follows:

	Year ended December 31, 2008	
	$	**%**
Healthcare	**64,698,218**	**76.0**
Hospitality	**20,415,076**	**24.0**
Total	**85,113,294**	**100.0**

	Year ended December 31, 2007	
	$	**%**
Healthcare	57,393,080	77.5
Hospitality	16,707,861	22.5
Total	74,100,941	100.0

In Edmonton, the Fund is the significant supplier of laundry and linen services to the entity which manages all major healthcare facilities in the region. This contract expires on December 31, 2010. In Calgary, the major customer is contractually committed to February 28, 2018 and in Vancouver the major customer is contractually committed to January 15, 2013.

For the year ended December 31, 2008, the Fund has recorded revenue of $49.4 million (year ended December 31, 2007 – $42.8 million) from these three major customers, representing 58% (2007 – 58%) of total revenue.

19 Related party transaction

The Fund has incurred expenses in the normal course of business for advisory consulting services provided by a Trustee relating to acquisitions. The amounts charged are recorded at their exchange amounts and are subject to normal trade terms. For the year ended December 31, 2008, the Fund incurred such fees totalling $74,000 (2007 – $46,000). Of the total 2008 amount, $23,000 is included in acquisition costs related to the assets of Buanderie HMR Inc. (see note 3) and $51,000 is included in Corporate expenses.

CORPORATE INFORMATION

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Stock Exchange and Symbol
Toronto Stock Exchange
Trading Symbol KBL.UN

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Matthew Hills
Steven Matyas
Linda McCurdy
Michael Percy

Audit Committee
Ross Smith (Chair)
Steven Matyas
Michael Percy

Compensation, Nominating and Corporate Governance Committee
Matthew Hills (Chair)(1)
Steven Matyas(1)
Michael Percy
Ross Smith

(1) Effective May 12, 2009, Mr. Matyas was appointed Chair of the Committee

Legal Counsel
Goodmans LLP
McLennan Ross LLP

Officers
Linda McCurdy
President and CEO

Sean Curtis, Senior Vice President
and General Manager, Edmonton

Doug Thomson, FCA, Vice President
and Chief Financial Officer

Jerry Ostrzyzek, Vice President Eastern Operations
and General Manager, Toronto

Ron Graham, General Manager, Vancouver

Jeff Gannon, General Manager, Calgary

Annual General Meeting
The Annual General Meeting of the Unitholders will be held at the Sheraton Centre Hotel, Peel Room, in Toronto on Thursday, June 11, 2009 at 2 o'clock in the afternoon. All Unitholders are cordially invited to attend.

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