

## CONSOLIDATED STATEMENTS OF INCOME, COMPREHENSIVE INCOME AND UNDISTRIBUTED INCOME

## CONSOLIDATED STATEMENTS OF CASH FLOWS

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## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## CORPORATE INFORMATION

	For the Nine Months Ended September 30,	
	2009	2008
	(Unaudited)	
<b>Revenue</b>		
IOC royalties	\$ 51,016,686	\$ 117,170,887
IOC commissions	947,045	1,164,218
Interest and other income	134,831	88,942
	<u>52,098,562</u>	<u>118,424,047</u>
<b>Expenses</b>		
Newfoundland royalty taxes	10,203,337	23,434,177
Amortization of royalty and commission interests	3,373,768	3,815,050
Administrative expenses (note 2)	1,346,269	1,266,865
Interest expense	342,479	497,175
	<u>15,265,853</u>	<u>29,013,267</u>
<b>Income before equity earnings and income taxes</b>	36,832,709	89,410,780
<b>Equity earnings in IOC</b>	17,305,381	84,726,196
<b>Income before income taxes</b>	54,138,090	174,136,976
<b>Provision for (recovery of) income taxes</b>		
Current	5,966,202	23,841,695
Future	230,000	(40,000)
	<u>6,196,202</u>	<u>23,801,695</u>
<b>Net income and comprehensive income for the period</b>	47,941,888	150,335,281
<b>Undistributed income, beginning of period</b>	84,370,152	63,053,439
<b>Distributions to unitholders</b>	(48,000,000)	(139,200,000)
<b>Undistributed income, end of period</b>	\$ 84,312,040	\$ 74,188,720
<b>Net income per unit</b>	\$ 1.50	\$ 4.70

	For the Three Months Ended September 30,	
	2009	2008
	(Unaudited)	
<b>Net inflow (outflow) of cash related to the following activities</b>		
<b>Operating</b>		
Net income for the period	\$ 13,629,876	\$ 65,638,121
Items not affecting cash:		
Equity earnings in IOC	(3,261,695)	(34,190,307)
Future income taxes	(1,110,000)	(6,730,000)
Amortization of royalty and commission interests	1,332,629	1,424,051
Amortization of deferred charges	20,666	31,251
Common share dividend received from IOC	8,200,096	77,923,564
Change in amounts receivable, accounts payable and income taxes payable/recoverable	(961,659)	18,075,891
Cash flow from operating activities	<u>17,849,913</u>	<u>122,172,571</u>
<b>Financing</b>		
Distributions paid to unitholders	(16,000,000)	(32,000,000)
Repayment of long-term debt	—	(5,405,519)
	<u>(16,000,000)</u>	<u>(37,405,519)</u>
<b>Increase in cash and cash equivalents during the period</b>	1,849,913	84,767,052
<b>Cash and cash equivalents, beginning of period</b>	8,999,039	108,881
<b>Cash and cash equivalents, end of period</b>	\$ 10,848,952	\$ 84,875,933
<b>Cash income taxes paid</b>	\$ 4,849,155	\$ 1,896,000
<b>Cash interest paid</b>	\$ 93,493	\$ 64,480

	For the Nine Months Ended September 30,	
	2009	2008
	(Unaudited)	
<b>Net inflow (outflow) of cash related to the following activities</b>		
<b>Operating</b>		
Net income for the period	\$ 47,941,888	\$ 150,335,281
Items not affecting cash:		
Equity earnings in IOC	(17,305,381)	(84,726,196)
Future income taxes	230,000	(40,000)
Amortization of royalty and commission interests	3,373,768	3,815,050
Amortization of deferred charges	62,000	93,753
Common share dividend received from IOC	8,200,096	77,923,564
Change in amounts receivable, accounts payable and income taxes payable/recoverable	(11,448,989)	(542,625)
Cash flow from operating activities	<u>31,053,382</u>	<u>146,858,827</u>
<b>Financing</b>		
Distributions paid to unitholders	(48,000,000)	(60,800,000)
Repayment of long-term debt	—	(1,334,150)
	<u>(48,000,000)</u>	<u>(62,134,150)</u>
<b>Increase (decrease) in cash and cash equivalents during the period</b>	(16,946,618)	84,724,677
<b>Cash and cash equivalents, beginning of period</b>	27,795,570	151,256
<b>Cash and cash equivalents, end of period</b>	\$ 10,848,952	\$ 84,875,933
<b>Cash income taxes paid</b>	\$ 32,943,452	\$ 4,056,000
<b>Cash interest paid</b>	\$ 280,480	\$ 317,062

### 1. Basis of Presentation

The financial statements have not been reviewed in accordance with section 7050 of the CICA Handbook, Auditor Review of the Interim Financial Statements, by the Fund's Auditor.

Not all disclosures required by Canadian generally accepted accounting principles for annual financial statements have been presented and, accordingly, these interim financial statements should be read in conjunction with the most recently prepared annual financial statements for the year ended December 31, 2008.

These interim financial statements follow the same accounting policies and method of application as the most recent annual financial statements for the year ended December 31, 2008.

### Seasonality

The results of operations and operating cash flows of the Fund vary considerably from quarter to quarter. The operations of the Fund are dependent on the royalty and commission revenues from IOC, whose production and revenues are not constant throughout the year, being lower during the winter months when the St. Lawrence Seaway is closed.

### 2. Unit appreciation rights

In 2005, the Fund adopted a unit appreciation rights plan which granted 50,000 units to each of its six trustees, all as more fully described in the annual financial statements. Since the grant date, 297,500 unit appreciation rights have been exercised.

Compensation expense is not recognized when rights are issued, but is accrued as an expense over the period that the rights vest. The unit appreciation rights are marked to market each quarter to the extent the unit price exceeds \$23.00. Compensation expense/(recovery) of \$98,500 (2008 - \$(621,135)) for the three months ended September 30, 2009 and \$482,500 (2008 - \$255,490) for the nine months ended September 30, 2009 have been recorded in administrative expenses in connection with the unit appreciation rights.

During the quarter, Trustees exercised unit appreciation rights in respect of 10,500 units at a market value of \$40.00 resulting in a total payment of \$178,500.

### 3. Capital Management

The Fund's capital consists of the unitholders' equity and a long-term debt facility. The Trustees are responsible for managing the investments and affairs of the Fund, including the receipt of revenues and the payment of distributions to the unitholders. The Fund makes cash distributions of the net income to the maximum extent possible, subject to the maintenance of appropriate levels of working capital.

### 4. Financial Instruments

The Fund derives dividends and royalty income from IOC denominated in US dollars. From time to time the Fund may enter into financial agreements with banks and other financial institutions to reduce the underlying risks associated with this foreign currency denominated income. As at September 30, 2009, there were no foreign exchange contracts outstanding.

### Principal Office

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### Trustees

**Bruce C. Bone**  
Chairman and  
Chief Executive Officer,  
Labrador Iron Ore  
Royalty Income Fund

**William J. Corcoran** <sup>(1)(2)</sup>  
Vice-Chairman,  
Jarislowsky Fraser Limited

**James C. McCartney**  
Company Director;  
Counsel, McCarthy Tétrault LLP

**Paul H. Palmer** <sup>(2)</sup>  
Company Director

**Alan R. Thomas**  
Company Director

**Donald J. Worth** <sup>(2)</sup>  
Company Director

(1) Lead Trustee  
(2) Member of Audit, Nominating  
and Compensation Committees

### Officers

**Bruce C. Bone**  
Chairman and  
Chief Executive Officer

**James C. McCartney**  
Vice-Chairman & Secretary

**Alan R. Thomas**  
Chief Financial Officer

### Registrar & Transfer Agent

Computershare  
Investor Services Inc.  
100 University Avenue  
Toronto, Ontario  
M5J 2Y1

### Legal Counsel

McCarthy Tétrault LLP  
Toronto, Ontario

### Auditors

Deloitte & Touche LLP  
Toronto, Ontario

### Stock Exchange Listing

The Toronto  
Stock Exchange

### Symbol

LIF.UN

### Website

www.labradorironore.com

## Labrador Iron Ore Royalty Income Fund



## THIRD QUARTER REPORT

# TO THE UNITHOLDERS OF LABRADOR IRON ORE ROYALTY INCOME FUND

Royalty income for the third quarter of 2009 amounted to \$15.51 million as compared to \$43.20 million for the third quarter of 2008. The Fund's cash flow from operating activities after adjustments for changes in amounts receivable, accounts payable and income taxes payable/recoverable (adjusted cash flow) for the third quarter was \$18.81 million or \$0.59 per unit as compared to \$104.10 million or \$3.25 per unit for the same period in 2008. Net income was \$13.63 million or \$0.43 per unit compared to \$65.64 million or \$2.05 per unit for the same period in 2008.

Royalty income for the quarter was substantially below the 2008 quarter due to the 2009 benchmark price reduction for pellets of 48.3% and concentrates of 29.75% as compared to 2008 benchmark prices, and the lower volume of sales. Cash flow from operations was affected by the reduced royalty revenue and the reduction in the dividend from Iron Ore Company of Canada (IOC) which was \$8.2 million compared to the \$77.9 million received in the 2008 third quarter. Net income was affected by these factors as well as substantially lower equity earnings from IOC. The retroactive effect of the price settlements which occurred during the quarter (retroactive to January 1) had been provided for in previous quarters.

The world recession which started last year continued to cause the demand for iron ore, especially pellets, to be reduced from the previous year. As a result IOC, which had previously idled some pellet machines, shut down its Carol Lake operations in Labrador City from July 7 to August 10, 2009 in order to balance inventories with demand. Shipments from IOC's terminal in Sept-Îles continued during this period. With the revival of pellet demand in traditional markets, IOC resumed full pellet production subsequent to the summer shut down.

Equity earnings from IOC amounted to \$3.26 million (\$0.10 per unit) as compared to \$34.19 million (\$1.07 per unit) in 2008. IOC earnings were negatively affected by reduced sales volume and lower prices for concentrates and pellets as compared to 2008.

On September 30, 2009 the Fund received a dividend from IOC totaling US\$7.5 million equating to CDN\$8.2 million or \$0.26 per unit.

Results for the three months and nine months ended September 30, 2009 are summarized below:

	3 Months Ended Sept. 30, 2009	3 Months Ended Sept. 30, 2008	9 Months Ended Sept. 30, 2009	9 Months Ended Sept. 30, 2008
	(Unaudited)			
Revenue (in millions)	\$15.84	\$43.72	\$52.10	\$118.42
Adjusted cash flow (in millions)	\$18.81	\$104.10	\$42.50	\$147.40
Adjusted cash flow per unit	\$ 0.59	\$ 3.25	\$ 1.33	\$ 4.60
Net income (in millions)	\$13.63	\$65.64	\$47.94	\$150.34
Net income per unit	\$ 0.43	\$ 2.05	\$ 1.50	\$ 4.70

"Adjusted cash flow" (defined as cash flow from operating activities as shown on the attached financial statements adjusted for changes in amounts receivable, accounts payable and income taxes payable/recoverable) is not a recognized measure under Canadian GAAP. The Trustees believe that adjusted cash flow is a useful analytical measure as it better reflects cash available for distributions to Unitholders.

A summary of IOC's sales in millions of tonnes is as follows:

	3 Months Ended Sept. 30, 2009	3 Months Ended Sept. 30, 2008	9 Months Ended Sept. 30, 2009	9 Months Ended Sept. 30, 2008	Year Ended Dec. 31, 2008
Pellets	2.08	3.29	5.70	9.86	12.30
Concentrates	1.17	1.15	3.92	1.97	2.76
Total	3.25	4.44	9.62	11.83	15.06

During the quarter iron ore markets for concentrates and pellets continued to firm with the result that IOC, which is now back to operating at full capacity, expects to be able to sell all its production for the balance of the year. The prices on the spot market have firmed and are now comparable to benchmark prices. 2009 will be disappointing when compared to last year but the outlook for 2010 appears more promising.

Respectfully submitted on behalf of the Trustees of Labrador Iron Ore Royalty Income Fund,



Bruce C. Bone  
Chairman and Chief Executive Officer  
October 29, 2009

## MANAGEMENT'S DISCUSSION AND ANALYSIS

The following discussion and analysis should be read in conjunction with the Management's Discussion and Analysis section of the Fund's 2008 Annual Report and the interim financial statements and notes contained in this report. Although management believes that expectations reflected in forward-looking statements are reasonable, such statements involve risk and uncertainties including the factors discussed in the Fund's 2008 Annual Report.

The Fund's revenues are entirely dependent on the operations of Iron Ore Company of Canada (IOC) as its principal assets relate to the operations of IOC and its principal source of revenue is the 7% royalty it receives on all sales of iron ore products by IOC. In addition to the volume of iron ore sold, the Fund's royalty revenue is affected by the price of iron ore and the Canadian – U.S. dollar exchange rate.

The sales of IOC are usually 15% – 20% of the annual volume in the first quarter, with the balance spread fairly evenly throughout the other three quarters. The current state of the market may cause 2009 sales to deviate from this pattern. Because of the size of individual shipments some quarters may be affected by the timing of the loading of ships that can be delayed from one quarter to the next.

Royalty income for the third quarter of 2009 amounted to \$15.51 million as compared to \$43.20 million for the third quarter of 2008. The Fund's cash flow from operating activities after adjustments for changes in amounts receivable, accounts payable and income taxes payable/recoverable (adjusted cash flow) for the third quarter was \$18.81 million or \$0.59 per unit as compared to \$104.10 million or \$3.25 per unit for the same period in 2008. Net income was \$13.63 million or \$0.43 per unit compared to \$65.64 million or \$2.05 per unit for the same period in 2008.

Royalty income for the quarter was substantially below the 2008 quarter due to the 2009 benchmark price reduction for pellets of 48.3% and concentrates of 29.75% as compared to 2008 benchmark prices, and the lower volume of sales. Cash flow from operations was affected by the reduced royalty revenue and the reduction in the dividend from Iron Ore Company of Canada (IOC) which was \$8.2 million compared to the \$77.9 million received in the 2008 third quarter. Net income was affected by these factors as well as substantially lower equity earnings from IOC. The retroactive effect of the price settlements which occurred during the quarter (retroactive to January 1) had been provided for in previous quarters.

The world recession which started last year caused the demand for iron ore, especially pellets, to be reduced from the previous year. As a result IOC, which had previously idled some pellet machines, shut down its Carol Lake operations in Labrador City from July 7 to August 10, 2009 in order to balance inventories with demand. Shipments from IOC's terminal in Sept-Îles continued during this period.

Equity earnings from IOC amounted to \$3.26 million (\$0.10 per unit) as compared to \$34.19 million (\$1.07 per unit) in 2008. IOC earnings were negatively affected by reduced sales volume and lower prices for concentrates and pellets as compared to 2008.

The nine months results were affected by the same factors as the quarter and reflect the lower volume and lower pricing. Because of particularly weak pellet demand, IOC idled a portion of its pellet plant during the first half of the year in order to have more concentrate available for sale in spot markets. With the revival of the pellet market, IOC resumed full pellet production subsequent to the summer shut down.

The following table sets out quarterly revenue, net income and cash flow data for 2009, 2008 and 2007.

	Revenue	Net Income	Net Income per Unit	Adjusted Cash Flow(1)	Adjusted Cash Flow per Unit(1)	Distributions Declared per Unit
(in millions except per Unit information)						
<b>2009</b>						
First Quarter	\$16.6	\$16.5	\$0.52	\$11.1	\$0.35	\$0.50
Second Quarter	\$19.7	\$17.8	\$0.55	\$12.6	\$0.39	\$0.50
Third Quarter	\$15.8	\$13.6	\$0.43	\$18.8 <sup>(2)</sup>	\$0.59	\$0.50
<b>2008</b>						
First Quarter	\$16.6	\$10.8	\$0.34	\$10.4	\$0.32	\$0.35
Second Quarter	\$58.1	\$73.9	\$2.31	\$32.9	\$1.03	\$1.00
Third Quarter	\$43.7	\$65.6	\$2.05	\$104.1 <sup>(3)</sup>	\$3.25	\$3.00
Fourth Quarter	\$45.0	\$26.2	\$0.82	\$27.5	\$0.86	\$0.50
<b>2007</b>						
First Quarter	\$13.1	\$10.7	\$0.34	\$ 8.7	\$0.27	\$0.35
Second Quarter	\$15.7	\$15.2	\$0.47	\$ 9.5	\$0.30	\$0.35
Third Quarter	\$20.1	\$23.0	\$0.72	\$30.8 <sup>(4)</sup>	\$0.96	\$0.70
Fourth Quarter	\$18.7	\$32.0	\$1.00	\$11.5	\$0.36	\$0.55
<b>Notes:</b>	(1) <i>Adjusted cash flow</i> (see below)		(2) <i>Includes an \$8.2 million IOC dividend</i>			
	(3) <i>Includes a \$77.9 million IOC dividend</i>		(4) <i>Includes an \$18.8 million IOC dividend</i>			

## Standardized Cash Flow and Adjusted Cash Flow

For the Fund, standardized cash flow is the same as cash flow from operating activities as recorded in the Fund's cash flow statements as the Fund does not incur capital expenditures or have any restrictions on distributions. Standardized cash flow per unit was \$0.56 for the quarter (2008 - \$3.82). Cumulative standardized cash flow from inception of the trust is \$23.21 per unit and total cash distributions since inception are \$22.43 per unit, for a payout ratio of 97%.

"Adjusted cash flow" is defined as cash flow from operating activities as shown on the attached financial statements adjusted for changes in amounts receivable, accounts payable and income taxes payable/recoverable. It is not a recognized measure under Canadian GAAP. The Trustees believe that adjusted cash flow is a useful analytical measure as it better reflects cash available for distributions to Unitholders.

The chart below reconciles cash flow from operating activities to adjusted cash flow.

	3 Months Ended Sept. 30, 2009	3 Months Ended Sept. 30, 2008	9 Months Ended Sept. 30, 2009	9 Months Ended Sept. 30, 2008
Standardized cash flow from operating activities	\$ 17,849,913	\$ 122,172,571	\$ 31,053,382	\$ 146,858,827
Excluding: changes in amounts receivable, accounts payable and income taxes payable/recoverable	961,659	(18,075,891)	11,448,989	542,625
Adjusted cash flow	\$ 18,811,572	\$ 104,096,680	\$ 42,502,371	\$ 147,401,452
Adjusted cash flow per unit	\$ 0.59	\$ 3.25	\$ 1.33	\$ 4.61

## Liquidity

The Fund has a \$50 million revolving credit facility with a term ending September 18, 2012 with provision for annual one-year extensions. No amounts are currently drawn under this facility leaving \$50 million available to provide for any capital required by IOC or other Fund requirements. IOC has suspended its previously announced expansion plans and intends to fund capital expenditures from internally generated funds.

## Transition to International Financial Reporting Standards ("IFRS")

As indicated in the 2008 annual report, the Canadian Accounting Standards Board will require all Canadian publically accountable enterprises, including the Fund, to adopt International Financial Reporting Standards (IFRS) for the years beginning January 1, 2011. Management has developed a project plan for the conversion to IFRS for the Fund. The project is progressing as planned, and to date there are no changes to the disclosure outlined in the December 31, 2008 MD&A in the 2008 annual report.

## Outlook

During the quarter iron ore markets for concentrates and pellets continued to firm with the result that IOC, which is now back to operating at full capacity, expects to be able to sell all its production for the balance of the year. The prices on the spot market have firmed and are now comparable to benchmark prices. 2009 will be disappointing when compared to last year but the outlook for 2010 appears more promising.



Bruce C. Bone  
Chairman and Chief Executive Officer  
Toronto, Ontario  
October 29, 2009

# CONSOLIDATED BALANCE SHEETS

	As at	
	September 30, 2009	December 31, 2008
	(Unaudited)	
<b>Assets</b>		
Current		
Cash and cash equivalents	\$ 10,848,952	\$ 27,795,570
Amounts receivable	17,120,621	36,476,337
Income taxes recoverable	1,335,358	—
	29,304,931	64,271,907
Deferred charges	330,666	392,666
Iron Ore Company of Canada ("IOC"), royalty and commission interests	298,824,331	302,198,099
Investment in IOC	196,557,418	187,452,133
	\$ 525,017,346	\$ 554,314,805
<b>Liabilities and Unitholders' Equity</b>		
Current		
Accounts payable	3,657,159	7,484,614
Income taxes payable	—	25,641,892
Distributions payable to unitholders	16,000,000	16,000,000
	19,657,159	49,126,506
Future income tax liability	103,340,000	103,110,000
	122,997,159	152,236,506
Unitholders' equity		
Trust units	317,708,147	317,708,147
Undistributed income	84,312,040	84,370,152
	\$ 525,017,346	\$ 554,314,805

# CONSOLIDATED STATEMENTS OF INCOME, COMPREHENSIVE INCOME AND UNDISTRIBUTED INCOME

	For the Three Months Ended September 30,	
	2009	2008
	(Unaudited)	
<b>Revenue</b>		
IOC royalties	\$ 15,514,566	\$ 43,200,281
IOC commissions	320,284	437,089
Interest and other income	4,363	84,604
	15,839,213	43,721,974
<b>Expenses</b>		
Newfoundland royalty taxes	3,102,913	8,640,056
Amortization of royalty and commission interests	1,332,629	1,424,051
Administrative expenses (note 2)	447,476	(267,623)
Interest expense	115,187	144,614
	4,998,205	9,941,098
<b>Income before equity earnings and income taxes</b>	10,841,008	33,780,876
<b>Equity earnings in IOC</b>	3,261,695	34,190,307
<b>Income before income taxes</b>	14,102,703	67,971,183
<b>Provision for (recovery of) income taxes</b>		
Current	1,582,827	9,063,062
Future	(1,110,000)	(6,730,000)
	472,827	2,333,062
<b>Net income and comprehensive income for the period</b>	13,629,876	65,638,121
<b>Undistributed income, beginning of period</b>	86,682,164	104,550,599
<b>Distributions to unitholders</b>	(16,000,000)	(96,000,000)
<b>Undistributed income, end of period</b>	\$ 84,312,040	\$ 74,188,720
<b>Net income per unit</b>	\$ 0.43	\$ 2.05