

# ANNUAL REPORT



FIRST PREMIUM U.S. INCOME TRUST



# FIRST PREMIUM U.S. INCOME TRUST

## INVESTMENT OBJECTIVES

First Premium U.S. Income Trust was launched in February 1997 with similar objectives to First Premium Income Trust. Those objectives are to provide unitholders of the Trust with a stable stream of quarterly distributions of at least 0.50 (\$2.00 annually) per unit while returning the original issue price of the units (\$25.00 per unit) to unitholders upon termination of the Trust.

## INVESTMENT STRATEGY

The Trust intends to achieve its investment objectives by investing the net proceeds from this offering in a diversified portfolio consisting primarily of common shares issued by corporations that rank in the top 50 of the Standard & Poor's 100 Index on the basis of market capitalization. To generate additional returns above the dividend income generated by the portfolio, the Trust will engage in a program of covered call option writing in respect of all or part of the securities in the portfolio.

## DISTRIBUTION HISTORY

<b>Date</b>	<b>Regular</b>	<b>Special</b>	<b>Total</b>
June 1997	\$ 0.83	-	\$ 0.83
September 1997	0.50	-	0.50
December 1997	0.50	\$ 0.75	1.25
<b>Total 1997</b>	<b>\$ 1.83</b>	<b>\$ 0.75</b>	<b>\$ 2.58</b>

## TEN LARGEST HOLDINGS

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SOUTHERN COMPANY
FORD MOTOR COMPANY
AT&T CORP.
GENERAL ELECTRIC COMPANY
WALT DISNEY COMPANY
HEWLETT-PACKARD COMPANY
DOW CHEMICAL COMPANY
IBM CORPORATION
BANKAMERICA CORPORATION
BELL ATLANTIC CORPORATION

# MESSAGE TO UNITHOLDERS

**F**irst Premium U.S. Income Trust (the "Trust") was launched in February 1997 to provide investors with an attractive alternative to fixed income vehicles. The Trust's objective is to provide a quarterly distribution based on net income and realized capital gains in the Trust during the year to yield 8% on the initial offering price of \$25.00.

The Trust has performed well since its inception and this has been reflected by the total distributions of \$2.58 for 1997. This represents \$0.75 over the target distribution composed of a special distribution paid on December 31, 1997. Based on the initial price of \$25.00, the 1997 distributions represent a total

distribution of 11% (annualized) for 1997 or 3% above the annual target yield of 8%.

This special distribution was the result of continuing growth throughout 1997 in the U.S. equity markets. Favorable price performance and increased price volatility both have had positive effects on the performance of the Trust.

As well, the unit price (listed as FPU.UN on the Toronto Stock Exchange and Montreal Exchange) has performed well throughout 1997 reaching a high of \$25.95.

We would like to take this opportunity to thank each of the Trust's unitholders for all their support in 1997.

John P. Mulvihill

*President & CEO*

Mulvihill Capital Management Inc.

Donald Biggs

*Vice President, Structured Finance*

Mulvihill Capital Management Inc.



# AUDITORS' REPORT

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To the Unitholders of the  
First Premium U.S. Income Trust

We have audited the statement of net assets and the schedule of investments of First Premium U.S. Income Trust as at December 31, 1997 and the statements of financial operations, changes in net assets and gain on sale of investments for the period then ended. These financial statements are the responsibility of the Trustee. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with 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 the Trustee, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position and the investments of the Trust as at December 31, 1997, and the results of its operations and changes in its net assets for the period then ended in accordance with generally accepted accounting principles.

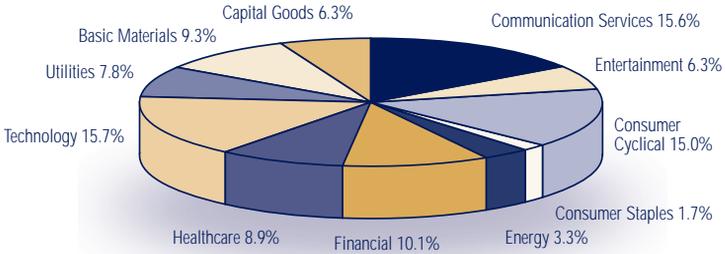
*Deloitte + Touche*

Chartered Accountants

Toronto, Ontario  
March 6, 1998

## ASSET MIX

December 31, 1997



## TRADING HISTORY



## COMMENTARY

As of December 31, 1997 the net assets of the Trust were \$320.70 million or \$25.10 per unit as compared to the initial unit value of \$23.71 at the issue date of February 3, 1997 (after deduction of Agents fees and Underwriting expenses). In addition to the underlying asset growth, cash distributions of \$2.58 were made during 1997 comprised of \$1.83 in regular distributions and \$0.75 in special distributions. Accordingly, the annualized cash yield on this product was 11.4%, based on the initial issue price of \$25.

This strong performance was attributable to rising equity markets and high price volatility

in the underlying securities. The latter enabled the Trust to generate high levels of premium income from its covered call option writing program.

The Trust remains well positioned for 1998 and management believes that the income orientation of this product renders it an attractive vehicle for the current investment climate. The Trust's conservative strategy of enhancing income by way of covered call writing will also reduce downside risk in the event of a market correction.



# FIRST PREMIUM U.S. INCOME TRUST

## STATEMENT OF FINANCIAL OPERATIONS

Period ended December 31, 1997

<b>Income</b>	
Dividends	\$ 4,649,267
Interest	4,840,179
	<u>9,489,446</u>
<b>Expenses (Note 5)</b>	
Management fees	5,254,551
Withholding tax	473,927
Goods and services tax	383,172
Custodian and other fees	219,327
	<u>6,330,977</u>
<b>Net investment income</b>	<u>3,158,469</u>
<b>Gain on sale of investments and options</b>	34,306,732
<b>Unrealized appreciation of investments</b>	<u>15,695,046</u>
<b>Net gain on investments</b>	<u>50,001,778</u>
<b>Total results of financial operations</b>	<u>\$ 53,160,247</u>
<b>Net investment income per unit</b>	\$0.2363
<b>Net gain on investments per unit</b>	<u>3.7413</u>
<b>Total results of financial operations per unit</b>	
(based on the weighted average number of units outstanding during the period of 13,364,832)	<u>\$ 3.9776</u>

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## STATEMENT OF NET ASSETS

December 31, 1997

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### Assets

Investments at market value (average cost - \$177,214,099)	\$ 191,709,072
Short-term notes (average cost - \$143,400,298)	144,600,371
Cash	107,491
Dividends receivable	511,960
Due from brokers	248,603
	<u>337,177,497</u>

### Liabilities

Accrued liabilities	717,559
Redemptions payable	15,755,671
	<u>16,473,230</u>

**Net Assets, represented by Unitholders' Equity** \$ 320,704,267

**Number of Units outstanding (Note 4)** 12,778,282

**Net Asset Value per Unit** \$ 25.0976

On behalf of the Trustee,  
The Royal Trust Company



Trustee



Trustee



# FIRST PREMIUM U.S. INCOME TRUST

## STATEMENT OF GAIN ON SALE OF INVESTMENTS

Period ended December 31, 1997

<b>Proceeds from sale of investments</b>	<u>\$ 520,977,455</u>
<b>Cost of investments sold</b>	
Cost of investments, beginning of period	-
Cost of investments purchased	<u>663,884,822</u>
	<u>663,884,822</u>
Cost of investments, end of period	<u>(177,214,099)</u>
	<u>486,670,723</u>
<b>Gain on sale of investments</b>	<u>\$ 34,306,732</u>

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## STATEMENT OF CHANGES IN NET ASSETS

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Period ended December 31, 1997

### **Unit transactions**

Proceeds from units issued, net of issue costs	\$ 317,742,145
Amount paid for units redeemed	(15,895,498)
Proceeds from reinvestment of distributions	282,775
	<u>\$ 302,129,422</u>

<b>Total results from financial operations</b>	<u>53,160,247</u>
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### **Distributions to Unitholders (Note 6)**

From net realized gain on sale of investments	(33,873,136)
Non-taxable distribution	(712,266)
	<u>(34,585,402)</u>

<b>Changes in net assets during the period</b>	<u>320,704,267</u>
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<b>Net assets, beginning of period</b>	<u>-</u>
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<b>Net assets, end of period</b>	<u>\$ 320,704,267</u>
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# FIRST PREMIUM U.S. INCOME TRUST

## SCHEDULE OF INVESTMENTS (cont'd)

December 31, 1997

Par Value/ Number of Shares		Average Cost	Market Value	% of Total
	<b>Energy</b>			
55,000	Schlumberger Limited	6,999,787	6,336,224	
	<b>Total Energy</b>	<b>6,999,787</b>	<b>6,336,224</b>	<b>3.3%</b>
	<b>Entertainment</b>			
85,000	Walt Disney Company	10,272,914	12,050,364	
	<b>Total Entertainment</b>	<b>10,272,914</b>	<b>12,050,364</b>	<b>6.3%</b>
	<b>Financial Services</b>			
100,000	BankAmerica Corporation	9,253,892	10,447,078	
75,000	First Chicago NBD Corporation	7,371,813	8,962,305	
	<b>Total Financial Services</b>	<b>16,625,705</b>	<b>19,409,383</b>	<b>10.1%</b>
	<b>Healthcare</b>			
50,000	Bristol-Myers Squibb Company	6,116,511	6,770,923	
110,000	Johnson & Johnson	9,472,814	10,370,156	
	<b>Total Healthcare</b>	<b>15,589,325</b>	<b>17,141,079</b>	<b>8.9%</b>
	<b>Technology</b>			
116,250	Cisco Systems Inc.	8,376,742	9,274,912	
119,500	Hewlett-Packard Company	10,272,952	10,688,577	
70,000	International Business Machines Corporation	9,579,893	10,474,805	
	<b>Total Technology</b>	<b>28,229,587</b>	<b>30,438,294</b>	<b>15.9%</b>
	<b>Utilities</b>			
405,000	Southern Company	13,424,909	14,997,102	
	<b>Total Utilities</b>	<b>13,424,909</b>	<b>14,997,102</b>	<b>7.8%</b>
	<b>Total U.S. Equities</b>	<b>177,462,702</b>	<b>192,082,502</b>	<b>100.2%</b>
	<b>Covered Calls</b>			
(500)	Chrysler Corporation	(47,217)	(67,083)	
(250)	Cisco Systems Inc.	(70,327)	(105,097)	
(250)	Dow Chemical Company	(48,294)	(120,750)	
(250)	First Chicago NBD Corporation	(43,447)	(44,722)	
(250)	Hewlett-Packard Company	(39,318)	(35,778)	
	<b>Total Covered Calls</b>	<b>(248,603)</b>	<b>(373,430)</b>	<b>(0.2)%</b>
	<b>Total Investments</b>	<b>\$ 177,214,099</b>	<b>\$ 191,709,072</b>	<b>100.0%</b>

# SCHEDULE OF INVESTMENTS

December 31, 1997

<u>Par Value/ Number of Shares</u>		<u>Average Cost</u>	<u>Market Value</u>	<u>% of Total</u>
<b>Short-term Notes</b>				
	<b>Domestic</b>			
91,300,000	Bank of Canada Treasury Bill January 8, 1998	\$ 90,553,536	\$ 91,236,090	63.1%
	<b>U.S. Dollar Denominated</b>			
3,550,000	Bank of Canada Treasury Bill January 5, 1998	4,843,208	5,076,184	
16,350,000	Bank of Canada Treasury Bill January 14, 1998	23,167,711	23,346,077	
200,000	Bank of Canada Treasury Bill February 3, 1998	276,110	284,782	
6,665,000	Bank of Canada Treasury Bill February 5, 1998	9,390,004	9,487,509	
10,600,000	Royal Bank TDR January 2, 1998	15,169,729	15,169,729	
		52,846,762	53,364,281	36.9%
	<b>Total Short-term Notes</b>	<b>\$ 143,400,298</b>	<b>\$ 144,600,371</b>	<b>100.0%</b>
<b>Investments</b>				
<b>U.S. Equities</b>				
	<b>Basic Materials</b>			
72,500	Dow Chemical Company	\$ 10,305,038	\$ 10,531,154	
120,000	Monsanto Company	7,518,273	7,212,777	
	<b>Total Basic Materials</b>	<b>17,823,311</b>	<b>17,743,931</b>	<b>9.3%</b>
	<b>Capital Goods</b>			
115,000	General Electric Company	12,285,320	12,075,856	
	<b>Total Capital Goods</b>	<b>12,285,320</b>	<b>12,075,856</b>	<b>6.3%</b>
	<b>Communication Services</b>			
55,000	Ameritech Corporation	6,466,219	6,336,224	
150,000	AT&T Corp.	8,650,871	13,148,291	
80,000	Bell Atlantic Corporation	9,699,009	10,418,456	
	<b>Total Communication Services</b>	<b>24,816,099</b>	<b>29,902,971</b>	<b>15.6%</b>
	<b>Consumer Cyclical</b>			
156,200	Chrysler Corporation	7,384,514	7,865,773	
200,000	Ford Motor Company	13,448,369	13,935,400	
122,500	Wal-Mart Stores Inc.	7,110,434	6,913,810	
	<b>Total Consumer Cyclical</b>	<b>27,943,317</b>	<b>28,714,983</b>	<b>15.0%</b>
	<b>Consumer Staples</b>			
45,000	H. J. Heinz Company	3,452,428	3,272,315	
	<b>Total Consumer Staples</b>	<b>3,452,428</b>	<b>3,272,315</b>	<b>1.7%</b>

# FIRST PREMIUM U.S. INCOME TRUST

## NOTES TO THE FINANCIAL STATEMENTS (cont'd)

deferred credits in investments so long as the options are outstanding. Any difference resulting from revaluation is included in unrealized appreciation or depreciation on investments.

Dividend income is recorded on the ex-dividend date.

### *Foreign currency translation*

Assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the prevailing rate of exchange on each valuation date. Purchases and sales of investments, and income derived from investments, are translated at the rate of exchange prevailing on the respective dates of such transactions.

### **4. Unitholders' Equity**

The Trust is authorized to issue an unlimited number of transferable, redeemable trust units of one class, each of which represents an equal, undivided interest in the net assets of the Trust.

All units have equal voting rights and privileges. Each whole unit is entitled to one vote at all meetings of unitholders and is entitled to participate equally with respect to any and all distributions made by the Trust. Fractional units are not entitled to voting privileges.

Units may be surrendered at any time for redemption but will be redeemed only on the monthly valuation date. Unitholders whose units are redeemed on a December 31 valuation date will be entitled to receive a redemption price per unit equal to the net asset value per unit. Unitholders whose units are redeemed on any other valuation date will be entitled to receive a redemption price per unit equal to the net asset value per unit less the lesser of (i) 4% of such net asset value per unit

and (ii) \$1.00. Under the terms of a Recirculation Agreement, the Trust may, but is not obligated to, require the Recirculation Agent to use its best efforts to find purchasers for any units tendered for redemption.

On January 22, 1997, the Trust issued 12,500,000 units at \$25.00 per unit for total gross cash proceeds of \$312,500,000. On February 28, 1997, the Trust issued 900,000 units at \$25.00 per unit for total gross proceeds of \$22,500,000. Costs of \$17,257,855 were incurred in connection with these offerings and the establishment of the Trust.

Following are the unit transactions for the period:

	<u>1997</u>
Units outstanding, beginning of period	-
Units issued for cash	13,400,000
Units redeemed	(633,375)
Units issued on reinvestment of distributions	11,657
Units outstanding, end of period	<u>12,778,282</u>

### **5. Management Fees And Expenses**

The Trust is responsible for all ongoing trustee, manager, legal, accounting and audit fees as well as all other expenses incurred by the Trustee and the Manager in the ordinary course of business relating to the Trust's operations. The Trust is also responsible for commissions and other costs of portfolio transactions and any extraordinary expenses of the Trust which may be incurred from time to time.

Fees are payable to the Manager under the terms of the trustee agreement and to the

## NOTES TO THE FINANCIAL STATEMENTS

### 1. Establishment of the Trust

First Premium U.S. Income Trust (the "Trust") is an investment trust established under the laws of the Province of Ontario on January 22, 1997. The Trust began operations on February 4, 1997 and will terminate on January 1, 2007 and its net assets will be distributed to unitholders unless unitholders determine to continue the Trust by a majority vote at a meeting called for such purpose.

The manager of the Trust is Mulvihill Fund Services Inc. (the "Manager") and the Trust's investment manager is Mulvihill Capital Management Inc. (the "Investment Manager"). The Royal Trust Company (the "Trustee") is the trustee and acts as custodian of the assets of the Trust.

### 2. Investment Objectives of the Trust

The Trust intends to achieve its investment objectives by investing in a diversified portfolio consisting primarily of common shares issued by corporations that rank in the top 50 of the Standard & Poor's 100 Index on the basis of market capitalization. The securities comprising the portfolio may also include instalment receipts for common shares and securities convertible into or exchangeable for common shares.

To generate additional returns above the dividend income earned on the portfolio, the Trust will from time to time write covered call options in respect of all or some of the securities in the portfolio. Additionally, the Trust may purchase call options with the effect of closing out existing call options written by the Trust and may also purchase put options to preserve the value of the portfolio where appropriate. The Trust may enter

into trades to close out positions in such permitted derivatives.

From time to time, the portfolio may include debt securities having a remaining term to maturity of less than one year issued or guaranteed by the government of Canada or a province or the government of the United States or short term commercial paper with a minimum specified credit rating.

### 3. Summary of Significant Accounting Policies

#### *Valuation of investments*

Investments are recorded at their market value at the end of the period, determined as follows:

Shares or other securities for which market quotations are readily available are valued at the closing sale price or, if there is no sale price, the average of the closing bid and ask prices. Shares or other securities for which market quotations are not readily available are valued at fair market value as determined by management.

Options are valued at an amount equal to the current market value of an option which would have the effect of closing the position.

Treasury bills are valued at quoted market values.

#### *Investment transactions and income*

Investment transactions are accounted for on a trade date basis. Realized gains and losses on the sale of investments and unrealized appreciation or depreciation of investments are determined on an average cost basis.

Option fees paid or received are reflected as



# MULVIHILL CAPITAL MANAGEMENT INC.

Mulvihill Capital Management Inc. is a leading Canadian investment counsellor responsible for the care of institutional and personal assets. The company manages corporate, pension, insurance, endowment, trust and mutual funds under a wide variety of investment mandates. Founded in 1985 as CT Investment Counsel Inc., the investment arm of Canada Trust, the company emerged in 1995 as an independent Company operated by a cohesive team of senior managers and owners who have been together for more than a decade. The Company's scale and independent structure allow them to provide clients with a uniquely customized approach to asset management.

First Premium U.S. Income Trust is managed by Mulvihill Capital's structured finance group. This area of Mulvihill Capital concentrates exclusively on creating and managing products tailored to meet very specific investment objectives. Assets are generally managed to meet specific absolute return levels rather than taking on the additional risk of targeting relative returns. This methodology allows Mulvihill Capital to make investment decisions that meet the client's needs rather than to make investments to rival the competition.

Mulvihill Capital's personal asset management division, Mulvihill Wealth Management, offers a comprehensive specialized approach tailored to clients' personal strategies. This not only relieves the client's burden of day-to-day investment decisions but also provides financial peace of

mind for today and tomorrow. The Company's personalized service and customized reporting assure that its powerful team of professionals is always working toward your current objectives and that you are fully aware of the progress you are making.

Mulvihill's reputation has been built on its ability to provide customized portfolios that meet the stated needs of its clients. The First Premium investments are prime examples of that customized approach to asset management.

Other Premium Income products within the Mulvihill Group include Premium Income Corporation, First Premium Income Trust, First Premium Oil & Gas Income Trust and MCM Split Share Corp. These Funds are Unit Trusts and have traded on the Toronto Stock Exchange and the Montreal Exchange as follows over the past year:

	<b>High</b>	<b>Low</b>
Premium Income Corporation PIC.A (Class A)	\$17.25	\$10.00
Premium Income Corporation PIC.P.R.A (Preferred)	\$16.30	\$14.90
First Premium Income Trust FPI.UN	\$30.50	\$24.90
First Premium Oil & Gas Income Trust FPG.UN	\$13.00	\$8.50

Investment Manager under the terms of an investment management agreement. The fees are payable at annual rates of 0.10% and 1.65%, respectively, of the Trust's net asset value calculated and payable monthly, plus applicable taxes.

Charges to the Trust for the period, excluding taxes, were as follows:

	<b>1997</b>
Expenses	\$ 5,473,878
Expenses as a percent of average net assets	1.82%*

(\*annualized)

Average net assets are calculated to be the average of the net assets determined at each valuation date of the Trust.

## 6. Distributions

The Trust endeavours to make quarterly distributions of net income and net realized capital gains and option premiums to unitholders on the last day of March, June, September and December in each year.

Unitholders may elect to reinvest distributions received from the Trust in additional units.

Distributions for the period were as follows:

	<b>1997</b>
<i>Distribution per unit:</i>	
Net realized capital gains	\$ 2.5269
Non-taxable distribution	0.0531
	<b>\$ 2.5800</b>

The non-taxable distribution received by unitholders reduces the adjusted cost base of the unit for tax purposes.

## 7. Income Taxes

The Trust is a "mutual fund trust" as defined in the Income Tax Act (Canada) (the "Act"). The Trust is subject to tax in each taxation year under Part I of the Act on the amount of its income for the year, including net realized taxable capital gains, less the portion thereof that it claims in respect of the amount paid or payable to unitholders in the year. Income tax paid by the Trust on any net realized capital gains not paid or payable to unitholders is recoverable by the Trust to the extent and in the circumstances provided in the Act.

Given the investment and distribution policies of the Trust and taking into account expenses, the Trust does not expect to bear any appreciable non-refundable income tax.

No amount is payable on account of income taxes in 1997.

## 8. Risk Management

The Trust may hedge its foreign currency exposure through the use of permitted derivatives such as clearing corporation options, futures contracts, options on futures, over-the-counter options and forward contracts. No investments in such permitted derivative instruments were entered into in the period.

## 9. Commission Charges

Total commissions paid in connection with portfolio transactions were \$936,497.

## 10. Statement of Portfolio Transactions

The Trust will provide, without charge, a Statement of Portfolio Transactions (unaudited) upon written request by any unitholder to the Trust at 121 King Street West, Suite 2600, Toronto, Ontario, M5H 3T9.

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**First Premium U.S. Income Trust**

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**Board of Advisors**

John P. Mulvihill  
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Mulvihill Capital Management Inc.

David N. Middleton  
Vice President, Finance & CFO  
Mulvihill Capital Management Inc.

Robert W. Korthals  
Corporate Director

R. John Lawrence  
Chairman  
Lawrence & Company

C. Edward Medland  
President  
Beauwood Investments Inc.

**Auditors**

Deloitte & Touche  
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**Units Listed**

Toronto Stock Exchange and  
Montreal Exchange  
trading under FPU.UN

**Transfer Agent**

Montreal Trust  
151 Front Street, 8th Floor  
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M5J 2N1

**Trustee**

Royal Trust  
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# FIRST PREMIUM U.S. INCOME TRUST



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