

**ALLIED PROPERTIES REAL ESTATE INVESTMENT TRUST**

**Consolidated Financial Statements**

**For the Years Ended  
December 31, 2008 and 2007**

---

## Management's Responsibility for Financial Reporting

---

The accompanying consolidated financial statements, management's discussion and analysis of results of operations and financial condition and the annual report are the responsibility of the Management of Allied Properties Real Estate Investment Trust (the "REIT"). The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles and where appropriate, include amounts, which are based on best estimates and judgment of Management.

Management has developed and maintains a system of accounting and reporting which provides for the necessary internal controls to ensure that transactions are properly authorized and recorded, assets are safeguarded against unauthorized use or disposition, and liabilities are recognized.

The Board of Trustees (the "Board") is responsible for ensuring that Management fulfills its responsibility for financial reporting and is ultimately responsible for reviewing and approving the consolidated financial statements. The Board carries out this responsibility principally through its Audit Committee (the "Committee"), which is comprised entirely of outside trustees. The Committee reviews the consolidated financial statements with both management and the independent auditors. The Committee reports its findings to the Board, which approves the consolidated financial statements before they are submitted to the Unitholders of the REIT.

BDO Dunwoody LLP (the "Auditors"), the independent auditors of the REIT, have audited the consolidated financial statements of the REIT in accordance with Canadian generally accepted auditing standards to enable them to express to the Unitholders their opinion on the consolidated financial statements. The Auditors had direct and full access to, and meet periodically with the Committee, both with and without Management present.

(signed) "Michael R. Emory"  
Michael R. Emory  
President and Chief Executive Officer

(signed) "Tom Wenner"  
Tom Wenner, CA  
Chief Financial Officer

---

## Auditors' Report

---

### **To the Unitholders of Allied Properties Real Estate Investment Trust**

We have audited the consolidated balance sheets of Allied Properties Real Estate Investment Trust as at December 31, 2008 and 2007 and the consolidated statements of unitholders' equity, earnings and comprehensive income and cash flows for the years then ended. These financial statements are the responsibility of the Trust'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 Trust 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.

(signed) BDO Dunwoody LLP

Chartered Accountants, Licensed Public Accountants

Toronto, Ontario  
March 10, 2009

**ALLIED PROPERTIES REAL ESTATE INVESTMENT TRUST  
CONSOLIDATED BALANCE SHEETS**

(in thousands) December 31	Note	2008	2007
<b>ASSETS</b>			
Rental properties	4	<b>\$807,089</b>	\$693,862
Properties under development		<b>42,463</b>	15,762
Deferred expenses	5	<b>55,826</b>	52,441
Other assets	6	<b>43,223</b>	45,383
Cash		<b>784</b>	1,179
		<b>\$949,385</b>	\$808,627
<b>LIABILITIES</b>			
Mortgages payable	7	<b>\$520,308</b>	\$456,329
Bank indebtedness	7	<b>2,922</b>	32,192
Accounts payable and other liabilities	8	<b>37,068</b>	27,604
Distributions payable		<b>3,436</b>	2,637
		<b>563,734</b>	518,762
<b>UNITHOLDERS' EQUITY</b>	<b>9</b>	<b>385,651</b>	289,865
		<b>\$949,385</b>	\$808,627

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

"Gordon Cunningham"

Gordon Cunningham  
Trustee

"Michael R. Emory"

Michael R. Emory  
Trustee

**ALLIED PROPERTIES REAL ESTATE INVESTMENT TRUST  
CONSOLIDATED STATEMENTS OF UNITHOLDERS' EQUITY**

(in thousands)

For years ended December 31, 2007 and 2008

	Notes	Cumulative Capital	Cumulative Issue Costs	Cumulative Net Income	Cumulative Distributions	Contributed Surplus	Total
Unitholders' equity, December 31, 2006		\$259,866	(\$13,980)	\$23,410	(\$53,592)	\$ -	\$215,704
Net income		-	-	5,810	-	-	5,810
Distributions		-	-	-	(29,763)	-	(29,763)
Public offering		100,119	(4,578)	-	-	-	95,541
Distribution reinvestment plan		1,904	-	-	-	-	1,904
Unit option plan – options exercised	11	130	-	-	-	-	130
Contributed surplus unit option plan	11	-	-	-	-	36	36
Long-Term incentive plan	12	505	(2)	-	-	-	503
Unitholders' equity, December 31, 2007		\$362,524	\$(18,560)	\$29,220	(\$83,355)	\$36	\$289,865
<b>Net income</b>		\$ -	\$ -	<b>\$12,512</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$12,512</b>
<b>Distributions</b>		-	-	-	<b>(38,667)</b>	-	<b>(38,667)</b>
<b>Public offering</b>		<b>120,738</b>	<b>(5,562)</b>	-	-	-	<b>115,176</b>
<b>Distribution reinvestment plan</b>		<b>5,512</b>	-	-	-	-	<b>5,512</b>
<b>Unit option plan options exercised</b>	11	<b>425</b>	-	-	-	-	<b>425</b>
<b>Contributed surplus, unit option plan</b>		-	-	-	-	<b>489</b>	<b>489</b>
<b>Long-Term incentive plan</b>	12	<b>339</b>	-	-	-	-	<b>339</b>
Unitholders' equity, December 31, 2008		\$489,538	(\$24,122)	\$41,732	(\$122,022)	\$525	\$385,651

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

**ALLIED PROPERTIES REAL ESTATE INVESTMENT TRUST  
CONSOLIDATED STATEMENTS OF EARNINGS AND COMPREHENSIVE INCOME**

(in thousands, except unit and per unit amounts)

For the Years Ended December 31	2008	2007
<hr/>		
<b>Revenues</b>		
Rental properties	\$131,808	\$105,998
Real estate services	663	909
	<hr/>	
	<b>132,471</b>	106,907
<hr/>		
<b>Expenses</b>		
Rental property operating	52,387	41,777
Real estate services	336	510
Financing	26,166	22,414
Trust	3,506	2,713
Amortization of rental properties	16,135	13,026
Amortization of deferred expenses	20,023	19,674
Amortization of other assets	1,406	983
	<hr/>	
	<b>119,959</b>	101,097
<hr/>		
<b>Net income and comprehensive income for the year</b>	<b>\$12,512</b>	\$5,810
<hr/>		
<b>Net income per unit</b>		
Basic	\$0.43	\$0.25
Fully diluted	\$0.42	\$0.24
<hr/>		
Weighted average number of units (Note 10)		
Basic	29,214,389	23,348,712
Fully diluted	29,602,531	23,756,519
<hr/>		

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

**ALLIED PROPERTIES REAL ESTATE INVESTMENT TRUST**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

(in thousands)

For the Years Ended December 31	Notes	2008	2007
<b>CASH PROVIDED BY (USED IN):</b>			
<b>Operating activities</b>			
Net income		\$12,512	\$5,810
Items not affecting cash			
Amortization of rental properties		16,135	13,026
Amortization of office equipment		257	47
Amortization of deferred expenses		20,023	19,674
Amortization of tenant improvements		1,149	937
Step rent adjustments (revenue)		(1,224)	(1,487)
Step rent adjustments (expenses)		232	155
Mark to market rent adjustments		2,060	3,206
Amortization, premium on assumed mortgages		(164)	(327)
Changes in other non-cash financing expenses		547	318
Compensation expense, unit option plan		489	36
Interest benefit granted under long-term incentive plan		-	6
		52,016	41,401
Change in other non-cash operating items		375	(24,706)
<b>Cash from operating activities</b>		<b>52,391</b>	<b>16,695</b>
<b>Investing activities</b>			
Rental properties acquired, net of non-cash consideration	2 (a)	(103,394)	(150,980)
Properties under development acquired	2 (a)	(24,153)	-
Capital expenditures, rental properties and other assets		(9,422)	(6,717)
Capital expenditures, properties under development		(6,196)	(975)
Tenant improvements and leasing cost		(4,181)	(4,753)
Tenant inducements		(501)	(40)
Recoverable expenses		(109)	(87)
<b>Cash used in investing activities</b>		<b>(147,956)</b>	<b>(163,552)</b>
<b>Financing Activities</b>			
Repayment of mortgages payable		(17,666)	(33,535)
Proceeds from new mortgages payable		58,522	77,074
Distributions		(32,356)	(27,268)
Proceeds of public offering (net of issue costs)		115,176	95,541
Proceeds from exercise of unit options		425	130
Proceeds from units issued under the LTIP (net of issue costs)	12	339	497
Net increase (decrease) in bank indebtedness		(29,270)	32,192
<b>Cash provided by financing activities</b>		<b>95,170</b>	<b>144,631</b>
<b>Increase (decrease) in cash and cash equivalents</b>		<b>(395)</b>	<b>(2,226)</b>
<b>Cash and cash equivalents, beginning of year</b>		<b>1,179</b>	<b>3,405</b>
<b>Cash and cash equivalents, end of year</b>		<b>784</b>	<b>\$1,179</b>
<b>Other cash flow information</b>			
Interest paid		\$27,587	\$22,428

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

**ALLIED PROPERTIES REAL ESTATE INVESTMENT TRUST**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(In thousands of dollars except per unit and unit amounts)  
December 31, 2008 and December 31, 2007

**1. The Trust**

Allied Properties Real Estate Investment Trust (the "REIT") is an unincorporated closed-end real estate investment trust created pursuant to the Declaration of Trust dated October 25, 2002, subsequently amended and restated on February 6, 2003 and on May 14, 2008. The REIT is governed by the laws of the Province of Ontario and began operations on February 19, 2003. The units of the Trust are traded on the Toronto Stock Exchange.

**2. Acquisitions**

**Rental Properties and Properties Under Development**

Net assets with respect to rental properties and properties under development acquired were as follows (using the purchase method of accounting):

For the Years Ended December 31	2008	2007
Rental properties	\$116,323	\$272,688
Properties under development	24,153	-
Other assets	86	2,784
Fair value of in-place leases and tenant relationships	20,877	34,756
Fair value of above-market leases	771	15,551
Fair value of below-market leases	(10,224)	(4,382)
Mortgages payable	(22,741)	(150,154)
Accounts payable and accrued liabilities	(1,698)	(20,263)
Cash consideration paid for the net assets acquired	\$127,547	\$150,980

The REIT allocates the purchase price of an acquisition on a preliminary basis, to the identified assets and liabilities acquired based on their estimated fair values at the time of acquisition. The purchase-price allocations are considered preliminary until the REIT has obtained the necessary information to complete its allocations.

**3. Summary of Significant Accounting Policies**

**(a) Basis of Presentation**

The REIT's consolidated financial statements have been prepared in accordance with Canadian Generally Accepted Accounting Principles ("GAAP").

**(b) Basis of Consolidation**

The REIT's consolidated financial statements include the accounts of the REIT and its wholly owned subsidiaries.

**(c) Use of Estimates**

The preparation of financial statements in conformity with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting periods. Actual results could differ from those estimates. Significant estimates and assumptions include those related to the valuation of above and below market leases, in place leases and tenant relationships.

**(d) Cash and Cash Equivalents**

Cash and cash equivalents include cash on hand, balances with banks and short-term deposits with original maturities of three months or less.

**(e) Rental Properties**

Rental properties include land, buildings, improvements and acquisition costs that are capitalized as part of the cost of rental properties.

Rental properties are stated at cost less accumulated amortization. Amortization on buildings is recorded on the straight-line basis over the useful life of the buildings, estimated at 40 years.

Upon the acquisition of rental properties, the REIT evaluates all in-place tenant lease agreements to determine if the leases are at, below or above market rates. If a lease is determined to be above or below market rates, a corresponding asset or liability is recorded and amortized into income over the life of the lease. Also at the time of acquisition, an asset representing the fair value of the costs of the leasing commissions and tenant inducements that the REIT would have otherwise incurred if it had originated each lease agreement acquired is recorded and amortized over the lease's remaining life. Furthermore, an asset representing the fair value, if any, of the relationship with a tenant is created upon the acquisition of the property, and amortized over the remaining term of the tenant's lease.

**(f) Properties Under Development**

Properties under development are stated at cost. Cost includes the cost of acquisition, including asset of liabilities for above and below market rent, fair value of leasing commissions and tenant inducements and the fair value of relationship with tenants, other direct cost, realty tax, other operating expense and applicable financing expense during the development period, less the amount of operating revenue during the development period. The principal factors in determining when the redevelopment-period ends are (i) the achievement of positive cash flow after applicable interest expense and (ii) the passage of a predetermined period of time. Other criteria may be considered in determining when a redevelopment-period ends if warranted by circumstances relating to the relevant property under development.

**(g) Computer, Office Equipment and Leasehold Improvements**

Amortization on computer, office equipment and leasehold improvements is recorded on a straight-line basis over estimated useful lives of three to five years.

**(h) Impairment of Long-Lived Assets**

The impairment of an asset is recognized if the carrying amount of the asset exceeds the aggregated undiscounted future cash flows expected from use of the asset and the eventual disposal of the asset. The impairment recognized is measured as the amount by which the carrying amount of the asset exceeds its fair value.

**(i) Mortgages Payable**

Mortgages payable consists of the legal liabilities owing pursuant to loans secured by mortgages and premiums and discounts recognized on loans assumed on acquisition of properties, netted against the transaction cost, and the effective interest method of amortization is applied to the premiums, discounts and transaction costs.

**(j) Distribution Reinvestment Plan (DRIP)**

The REIT has instituted a DRIP whereby Canadian unitholders may elect to have their distributions automatically reinvested in additional units. Unitholders who so elect will receive a further distribution of units equal in value to 5% of each distribution that was reinvested. No commissions, service charges or brokerage fees are payable by participants in connection with the DRIP. Effective June 18, 2007, the REIT temporarily suspended the DRIP. Effective December 20, 2007 the REIT reinstated the DRIP.

**(k) Revenue Recognition**

Rental revenue includes rents from tenants under leases, property tax and operating cost recoveries, parking income and incidental income. Rental revenue with respect to rents from tenants under lease is recognized ratably over the term of the lease. Real estate services revenue is recorded on an accrual basis as services are provided.

**(l) Unit-based Compensation Plan**

The REIT accounts for employee unit-based options by measuring the compensation cost for options granted on or after January 1, 2002 under the fair value-based method using a Black-Scholes option pricing model. The REIT accounts for loans granted under the long-term incentive plan that do not meet the conditions for recognition as an asset, as a reduction of equity.

**(m) Per Unit Calculations**

Basic net income per unit is calculated by dividing net income by the weighted average number of units outstanding for the year, excluding those units issued under the Long Term Incentive Plan, which are not fully paid up. The calculations of net income per unit on a diluted basis consider the potential exercise of outstanding unit purchase options, if dilutive, and are calculated using the treasury stock method. The calculation of net income per unit on a diluted basis includes those units issued under the Long Term Incentive Plan, which are not fully paid up.

**(n) Contracts and Customer Relationships**

Contracts and customer relationships included in deferred expenses consists of the values assigned to property management clients upon initial acquisition and are amortized on a straight-line basis over their estimated useful lives of 10 years.

**(o) Leasing Costs and Tenant Improvements**

Leasing costs include costs associated with leasing activities such as commissions. These costs are amortized on a straight-line basis over the terms of the leases to which they relate.

The REIT may provide funding to tenants through allowances. In accounting for a tenant allowance, the REIT determines whether the allowance is for funding the construction of improvements and the ownership of such improvements. In those circumstances where the REIT is considered the owner of the improvements, the REIT capitalizes the amount of the allowance as a tenant improvement and amortizes it over the shorter of the useful life of the improvement and the lease term. If the REIT provides an allowance that does not represent a payment for funding improvements, or in the event the REIT is not considered the owner of the improvement, the allowance would be considered a lease incentive and would be deferred and amortized over the lease term as a reduction of revenue. Determination of the accounting treatment of a tenant allowance is made on a case-by-case basis.

**(p) Financial Instruments**

Financial assets and liabilities are classified into one of the following five categories: held-for-trading; held-to-maturity; loans and receivables; available-for-sale financial assets; and other financial liabilities. Financial instruments are initially measured at fair value. Subsequent measurement and recognition of the changes in fair value of financial instruments depends upon their initial classifications, as follows:

Held-for-trading financial assets: measured at fair value with subsequent changes in fair value recognized in current period net income;

Held-to-maturity assets, loans and receivables and other financial liabilities: initially measured at fair value and subsequently measured at amortized cost with changes recognized in current period net income;

Available-for-sale financial assets: measured at fair value with subsequent gains and losses included in other comprehensive income until the asset is removed from the balance sheets or when there is an unrealized loss that is considered other than temporary; and

Derivative financial instruments: classified as held-for-trading financial instruments and measured at fair value, with subsequent changes in fair value recognized in current period income.

The REIT designated its cash as held-for-trading, its accounts receivable as loans and receivables, and its bank indebtedness, accounts payable and other liabilities, distributions payable and mortgages payable as other financial liabilities. The REIT had no held-to-maturity or available-for-sale financial assets during the years ended December 31, 2008 and December 31, 2007.

**(q) Change in Accounting Policies**

Effective January 1, 2008, the REIT adopted the new standards of the Canadian Institute of Chartered Accountants ("CICA") comprising CICA Handbook Sections 1535, Capital Disclosures; Section 3862, Financial Instruments – Disclosures; and Section 3863, Financial Instruments – Presentation.

Section 1535 requires disclosure of the REIT's objectives, policies and processes for managing capital, quantitative data about what the REIT considers as capital, disclosure of any externally imposed capital requirements and if it has not complied, the consequences of such non-compliance.

Section 3862 and 3863 replaces the existing Section 3861, Financial Instruments – Disclosure and Presentation to revise and enhance disclosure requirements but did not change existing presentation requirements. These new sections require disclosure about the nature and extent of risks arising from the financial instruments and how the REIT manages those risks.

The adoption of these new standards resulted in additional disclosure in the consolidated financial statements (see note 14) but do not affect the REIT's consolidated financial position, results of operations or cash flows.

**(r) Comparative Amounts**

The comparative amounts presented in the consolidated financial statements have been reclassified to conform to the current year's presentation.

**(s) Future Changes to Accounting Policies**

In February 2008, the CICA issued new accounting standard, Section 3064, Goodwill and Intangible Assets, replacing Section 3062, Goodwill and Other Intangible Assets and Section 3450, Research Development Costs, which clarifies that costs can be capitalized only when they relate to an item that meets the definition of an asset. The CICA also amended Section 1000 – Financial Statement Concepts, to provide consistency with the new standard. These changes will be effective for the REIT's fiscal year beginning January 1, 2009, and will be applied retroactively with restatement of the comparative period and will not have a significant impact on the REIT's consolidated financial statements.

In February 2008, the Accounting Standards Board ("AcSB") of the CICA confirmed that Canadian GAAP for publicly accountable enterprises will be converged with International Financial Reporting Standards ("IFRS") effective in the calendar year 2011. The conversion to IFRS will be required for the REIT for interim and annual financial statements beginning on January 1, 2011, with comparative IFRS information. The REIT continues to assess the potential impact of IFRS to its consolidated financial statements.

#### 4. Rental Properties and Properties Under Development

As at December 31, 2008	Cost	Accumulated Amortization	Net Carrying Amount
Buildings, improvements and other costs	\$690,568	\$47,858	\$642,710
Land	164,379	-	164,379
	<b>\$854,947</b>	<b>\$47,858</b>	<b>\$807,089</b>

  

As at December 31, 2007	Cost	Accumulated Amortization	Net Carrying Amount
Buildings, improvements and other costs	\$590,619	\$31,723	\$558,896
Land	134,966	-	134,966
	<b>\$725,585</b>	<b>\$31,723</b>	<b>\$693,862</b>

Included in properties under development is interest capitalized in the year of \$1,858 (2007 - \$661).

#### 5. Deferred Expenses

Deferred expenses consist of costs incurred by the REIT, net of accumulated amortization of \$56,486 (December 31, 2007 - \$35,890), with respect to leasing costs incurred, the fair value attributed to in-place leases acquired, the fair value attributed to customer relationships with respect to rental property acquisitions and amounts recorded on the acquisition of the property manager – contracts and customer relationships. Amortization is recorded on a straight-line basis over the remaining term of the respective leases to which the costs or fair value relate.

As at December 31, 2008	Cost	Accumulated Amortization	Net Carrying Amount
Leasing costs	\$8,184	\$2,083	\$6,101
Tenant inducements	742	246	496
Leasing costs and tenant relationships on rental properties acquired	101,144	52,719	48,425
Amounts recorded on the acquisition of the property manager – contracts and customer relationships	959	336	623
Recoverable expenditures	372	191	181
	<b>\$111,401</b>	<b>\$55,575</b>	<b>\$55,826</b>

  

As at December 31, 2007	Cost	Accumulated Amortization	Net Carrying Amount
Leasing costs	\$6,373	\$1,308	\$5,065
Tenant inducements	248	75	173
Leasing costs and tenant relationships on rental properties acquired	80,488	34,186	46,302
Amounts recorded on the acquisition of the property manager – contracts and customer relationships	959	240	719
Recoverable expenditures	263	81	182
	<b>\$88,331</b>	<b>\$35,890</b>	<b>\$52,441</b>

#### 6. Other Assets

Other assets consist of:

December 31	2008	2007
Above-market rents of leases acquired through rental property acquisitions net of accumulated amortization of \$12,760 (December 31, 2007 - \$7,576)	<b>\$12,604</b>	\$16,990
Accounts receivable and deposits for property acquisitions	<b>16,376</b>	15,632
Tenant improvements, net of accumulated amortization of \$2,439 (December 31, 2007 - \$1,870)	<b>5,854</b>	5,027
Prepaid expenses	<b>605</b>	1,041
Escrow accounts held by mortgagees	<b>7,051</b>	6,543
Computer and office equipment, net of accumulated amortization of \$243 (December 31, 2007 - \$87)	<b>656</b>	120
Leasehold improvements, net of accumulated amortization of \$5 (December 31, 2007 - \$8)	<b>77</b>	30
	<b>\$43,223</b>	<b>\$45,383</b>

## 7. Mortgages Payable and Bank Indebtedness

Substantially all of the REIT's assets have been pledged as security under the related mortgages and other security agreements. Effective interest rates on the mortgages payable are between 5.1% and 8.1% (contractual 4.37% and 8.10%).

Mortgages payable at December 31, 2008 are due as follows:

	Principal Repayments	Balance due at Maturity	Total
Year ended December 31, 2009	\$13,029	\$15,209	\$28,238
Year ended December 31, 2010	13,433	5,978	19,411
Year ended December 31, 2011	13,965	14,868	28,833
Year ended December 31, 2012	13,780	36,805	50,585
Year ended December 31, 2013	13,992	21,997	35,989
Thereafter	21,766	338,734	360,500
	<b>\$89,965</b>	<b>\$433,591</b>	<b>\$523,556</b>
Net discount on assumed mortgages (net of amortization of \$1,305)			(196)
Deferred financing costs (net of amortization of \$1,199)			(3,052)
			<b>\$520,308</b>

Mortgages payable at December 31, 2007 are due as follows:

	Principal Repayments	Balance due at Maturity	Total
Year ended December 31, 2008	\$11,153	\$6,486	\$17,639
Year ended December 31, 2009	11,346	14,022	25,368
Year ended December 31, 2010	11,673	4,478	16,151
Year ended December 31, 2011	12,106	8,496	20,602
Year ended December 31, 2012	12,253	12,317	24,570
Thereafter	41,939	312,463	354,402
	<b>\$100,470</b>	<b>\$358,262</b>	<b>\$458,732</b>
Net premium on assumed mortgages (net of accumulated amortization of \$1,142)			499
Deferred financing costs (net of accumulated amortization of \$694)			(2,902)
			<b>\$456,329</b>

The REIT has a \$70,000 revolving credit facility with a Canadian chartered bank, which matures August 31, 2010 and bears interest at bank prime rate. Security for the facility consists of first and second mortgage charges on seven rental properties and security agreements covering assignment of rents and personal property with respect to the seven properties. The credit facility has a number of covenants which were met as at December 31, 2008.

At December 31, 2008 the amount outstanding under the credit facility was \$2,922 (December 31, 2007 \$32,192).

## 8. Accounts Payable and Other Liabilities

Accounts payable and other liabilities consist of:

December 31	2008	2007
General operating payables and tenant deposits	\$21,314	\$19,274
Below market rents of leases acquired through rental property acquisition – net of amortization of \$7,121 (December 31, 2007 - \$3,997)	13,363	6,264
Accrued interest	2,391	2,066
	<b>\$37,068</b>	<b>\$27,604</b>

## 9. Unitholders' Equity

The REIT is authorized to issue an unlimited number of trust units, each of which represents a unitholder's proportionate undivided beneficial interest in the REIT. No unitholder has or is deemed to have any right of ownership in any of the assets of the REIT.

The number of units issued and outstanding are as follows:

	<b>Units</b>
Units outstanding, December 31, 2006	20,130,313
Units issued pursuant to offering on April 2, 2007	4,825,000
Units issued pursuant to the Long Term Incentive Plan (Note 12)	51,500
Units issued under the Distribution Reinvestment Plan	89,895
Units issued pursuant to Unit Option Plan (Note 11)	13,000
<hr/>	
Units outstanding, December 31, 2007	25,109,708
<hr/>	
<b>Units issued pursuant to offering on January 3, 2008</b>	<b>2,900,000</b>
<b>Units issued pursuant to offering on July 2, 2008</b>	<b>2,850,000</b>
<b>Units issued under the Distribution Reinvestment Plan</b>	<b>333,462</b>
<b>Units issued under the Unit Option Plan (Note 11)</b>	<b>42,500</b>
<hr/>	
<b>Units outstanding, December 31, 2008</b>	<b>31,235,670</b>

## 10. Weighted Average Units

The weighted average units outstanding for the purposes of calculating net income per unit are as follows:

<b>For the Years Ended December 31</b>	<b>2008</b>	2007
<b>Basic</b>	<b>29,214,389</b>	23,348,712
<b>Unit option plan</b>	<b>849</b>	26,131
<b>Long-term incentive plan</b>	<b>387,293</b>	381,676
<hr/>		
<b>Fully diluted</b>	<b>29,602,531</b>	23,756,519

## 11. Unit Option Plan

The REIT adopted a Unit Option Plan providing for the issuance, from time to time, at the discretion of the trustees, of options to purchase Units for cash. Participation in the Unit Option Plan is restricted to the trustees and the officers of the REIT. The Unit Option Plan complies with the requirements of the Toronto Stock Exchange. The exercise price of any option granted will not be less than the closing market price of the units on the day preceding the date of grant. The options may have a maximum term of ten years from the date of grant.

On December 17, 2007, 710,000 options were granted to trustees and officers with an exercise price of \$21.13 and expiring on December 17, 2012. 128,331 options vested on December 17, 2008 and 128,338 options will vest on each of December 17, 2009 and December 17, 2010. 108,333 options will vest on each of December 17, 2009 and December 17, 2010, provided that certain performance achievements are met. 108,334 options expired in 2008 as certain performance achievements were not met.

On December 15, 2008, 3,750 options were granted to trustees and employees with an exercise price of \$10.87 and expiring on December 15, 2013. 1,250 options will vest on each of December 15, 2009, December 15, 2010 and December 15, 2011.

On January 15, 2009 130,000 options were granted to employees and officers with an exercise price of \$12.34 and expiring on January 15, 2014. 43,333, 43,333 and 43,334 options will vest on each of January

15, 2010, January 15, 2011 and January 15, 2012, provided that certain performance achievements are met.

The REIT accounts for its unit option plan using the fair value method, under which compensation expense is measured at the date options are granted and recognized over the vesting period.

Compensation expense under the Unit Option Plan and assumptions utilized in the calculation thereof using the Black-Scholes Model for option valuation are as follows:

For the Year Ended December 31	2008	2007
Compensation expense	\$489	\$36
Unit options granted	3,750	710,000
Unit option holding period (years)	5	5
Volatility rate	24.14%	19.8%
Distribution yield	11.05%	5.96%
Risk free interest rate	2.11%	3.94%
Value of options granted	\$3	\$1,504

A summary of the status of the Unit Option Plan is as follows:

	Units/ Options	Weighted Average Exercise Price
Options outstanding as at December 31, 2006	55,500	\$10.00
Options exercised in the year ended December 31, 2007	(13,000)	\$10.00
Options granted in the year ended December 31, 2007	710,000	\$21.13
Options outstanding as at December 31, 2007	752,500	\$20.50
Options exercised in the year ended December 31, 2008	(42,500)	\$10.00
Options granted in the year ended December 31, 2008	3,750	\$10.87
Options expired in the year ended December 31, 2008	(108,333)	\$21.13
Options outstanding as at December 31, 2008	605,417	\$21.06
Options exercisable as at December 31, 2008	128,331	\$21.13

## 12. Long-Term Incentive Plan

Officers and trustees of the REIT have been granted the right to participate in a LTIP, whereby the participants may subscribe for units for a purchase price equal to the weighted average trading price of the units for five trading days preceding the date of the grant. The purchase price is payable as to 5% upon issuance and as to the balance ("installment loan receivable") over a term not exceeding 10 years. The installment loan receivable bears interest at rates of 3% or 5% per annum on any outstanding balance and is a direct, personal obligation of the participant. The units issued under the LTIP are held by a custodian for the benefit of the participants until the installment loan receivable has been paid in full. The value of these units held by the Custodian as at December 31, 2008 and 2007 were \$4,822 and \$8,032, respectively. Cash distributions paid in respect of the units issued under the LTIP are applied first to the interest and then to reduce the balance of the installment loan receivable.

The fair value of the LTIP is the estimated present value of the imputed interest benefit over an estimated expected term of ten years, which is recorded as compensation cost. The LTIP installment loans receivable are recognized as deductions from units issued. Distributions received under the LTIP are charged to unitholders' equity while interest received under the LTIP is credited to distributions.

Units issued under the LTIP	Cumulative as at December 31, 2008	Year Ended December 31, 2008	Cumulative as at December 31, 2007
Number of units issued	412,293	-	412,293
Units issued	\$6,282	-	\$6,282
Compensation cost	474	-	474
	6,756	-	6,756

LTIP installment loans receivable	(5,852)	-	(5,852)
Interest on installment loans receivable	(552)	(166)	(386)
Distributions applied against installment loans receivable	1,637	505	1,132
Repayments of installment loans	145	-	145
	<b>(4,622)</b>	<b>339</b>	<b>(4,961)</b>
	<b>\$2,134</b>	<b>\$339</b>	<b>\$1,795</b>
Units issued under the LTIP	Cumulative as at December 31, 2007	Year Ended December 31, 2007	Cumulative as at December 31, 2006
Number of units issued	412,293	51,500	360,793
Units issued	\$6,282	\$1,160	\$5,122
Compensation cost	474	6	468
	6,756	1,166	5,590
LTIP installment loans receivable	(5,852)	(1,102)	(4,750)
Interest on installment loan receivable	(386)	(174)	(212)
Distributions applied against installment loan receivable	1,132	470	662
Repayments of installment loans	145	145	-
	<b>(4,961)</b>	<b>(661)</b>	<b>(4,300)</b>
	<b>\$1,795</b>	<b>\$505</b>	<b>\$1,290</b>

### 13. Income Taxes

The REIT is taxed as a "Mutual Fund Trust" for income tax purposes. The REIT is required by its Declaration of Trust to distribute or designate all of its taxable income to unitholders and to deduct such distributions or designation for income tax purposes. Accordingly, no provision for income taxes has been made. Income tax obligations relating to distributions of the REIT are the obligations of the unitholders.

### 14. Capital Management

The REIT defines capital as the aggregate of unitholder's equity, mortgages payable and bank indebtedness. The REIT manages its capital to comply with investment and debt restrictions pursuant to the Declaration; to comply with debt covenants; to ensure sufficient operating funds are available to fund business strategies; to fund leasing and capital expenditures; to fund acquisitions and development of properties; and to provide stable and growing cash distributions to unitholders.

Various debt, equity and earnings distributions ratios are used to monitor capital adequacy and requirements. For debt management, debt to gross book value, debt average term to maturity, variable debt as a percentage of total debt are the primary ratios used in capital management. The Declaration requires the REIT to maintain debt to gross book value, as defined by the Declaration, of less than 60% (65% of gross book value, including the principal amount of indebtedness outstanding pursuant to convertible debentures) and the variable rate debt and debt having maturities of less than one year to not exceed 15% of gross book value. As at December 31, 2008 and 2007, the REIT debt to gross book value is 49.4% and 55.2%, respectively, with the decrease primarily arising as a result of the issuance of 2,850,000 units by the REIT on July 2, 2008. As at December 31, 2008 and 2007, variable rate debt and debt having maturities of less than one year aggregated 2.9% of gross book value.

### 15. Financial Instrument Risk and Management

The fair value of the REIT's financial assets and liabilities with current maturities approximate their recorded values as at December 31, 2008 and December 31, 2007. The fair value of the mortgages payable is \$520,919 (December 31, 2007 - \$456,153).

The carrying value of the REIT's equity is impacted by earnings and distributions. The REIT is required to distribute at least 70% of its distributable income, as defined by the Declaration. For the years ended December 31, 2008 and 2007, the REIT distributed 79.1% and 75.8%, respectively of its distributable income.

Market risk is the risk that the fair value or future cash flow of a financial instrument will fluctuate because of changes in market prices. The REIT does not require, hold or issue derivative financial instruments for hedging or trading purposes.

**(a) Interest Rate Risk and Liquidity Risks**

The REIT is exposed to interest rate risk on its borrowings. All of the REIT's mortgages payable at December 31, 2008 are at fixed interest rates and are not exposed to changes in interest rates, during the term of the debt. However, there is interest rate risk associated with the REIT's fixed interest rate, term debt due to the expected requirement to refinance such debts upon maturity. Bank indebtedness is at floating rate interest rates and is exposed to changes in interest rates. As fixed rate debt matures and as the REIT utilizes additional floating rate debt under the revolving credit facilities, the REIT will be further exposed to changes in interest rates. There is a risk that interest rates will fluctuate from the date the REIT commits to a debt to the date the interest rate is set with the lender. Liquidity risk arises from the possibility of not having sufficient capital available to the REIT. Mitigation of liquidity risk is discussed in Note 14.

As part of its risk management program, the REIT endeavors to maintain an appropriate mix of fixed rate and floating rate debt, to stagger the maturities of its debt and to minimize the time between committing to a debt and the date the interest rate is set with the lender.

The following table outlines the impact of a 1% change in the interest rate on variable rate debt and mortgages payable maturing within one year.

For the Year Ended December 31, 2008		-1%	-1%	+1%	-1%
	Carrying Amount	Income	Equity	Income	Equity
<b>Bank indebtedness</b>	\$2,922	\$29	\$29	(\$29)	(\$29)
<b>Mortgages payable maturing within one year</b>	\$28,238	\$282	\$282	(\$282)	(\$282)

**(b) Credit Risk**

Credit risk arises from the possibility that tenants may experience financial difficulty and be unable to fulfill their lease commitments, resulting in the REIT incurring a financial loss. The REIT manages credit risk to mitigate exposure to financial loss by staggering lease maturities, diversifying revenue sources over a large tenant base, ensuring no individual tenant contributes a significant portion of the REIT's revenues and conducting credit review of new tenants. Management reviews tenant receivables on a regular basis and reduces carrying amounts through the use of allowance for doubtful accounts and the amount of any loss is recognized in the Consolidated Statement of Earnings within rental property operating cost. As at December 31, 2008 and December 31, 2007, allowance for doubtful accounts were \$650 and \$393, respectively. During the years ended December 31, 2008 and 2007, the loss recognized relating to the allowance for doubtful accounts were \$332 and \$291, respectively. As a result of a dispute regarding operating cost recoveries since 2006, a balance of \$2,341 is due from one tenant. Based on the advice of legal counsel and an independent firm of chartered accountants, Management is of the view that there is no merit to the tenant's position and is diligently pursuing the matter.

**16. Segmented Disclosure**

The REIT's assets are in, and its revenue is derived from, the downtown office markets in five major Canadian cities.

**17. Commitments and Contingencies**

The REIT has entered into commitments for acquisitions, building renovations, leasing commissions and tenant inducements with respect to leasing activities and for repairs and operating costs. The commitments as at December 31, 2008 and December 31, 2007 were \$2,500 and \$3,313, respectively.

The REIT is subject to legal and other claims in the normal course of business. Management and the REIT's legal counsel evaluate all claims. In the opinion of management any liability from such claims would not have a significant effect on the REIT's consolidated financial statements.

## 18. Related Party Transactions

### (a) Real Estate Services

The REIT engages in third-party property management business, including the provision of services for properties in which certain trustees of the REIT have an ownership interest. For the year ended December 31, 2008 real estate service revenue earned from these properties was \$224 (December 31, 2007 - \$323), which was fully paid in the year. These transactions are in the normal course of operations and were measured at the exchange amount set out in agreement between the respective property owners.

### (b) Rental Revenues

Rental revenues included amounts received from related parties as follows:

Related Party	Nature of Revenue	For the Years Ended December 31	2008	2007
Vendors of properties	Head Lease		\$3	\$23
TechSpaceCanada Inc.	Guarantee		80	63
Vendors of properties	Bridge Covenants		-	25
			<b>\$83</b>	<b>\$111</b>

#### Head Lease:

Certain vendors entered into a lease dated February 20, 2003 for 16,686 square feet of office space for a five year term, expiring on February 19, 2008 (the "Head Lease"). The vendors, which are under common control of certain trustees of the REIT, honoured all of their obligations under the Head Lease and were released from the balance of their obligations thereunder when the REIT entered into direct lease arrangements with acceptable replacement tenants on acceptable terms.

#### Guarantee:

TechSpace Canada Inc. ("TechSpace"), a subsidiary of Allied Canadian Development Corporation (the "Developer") leased 29,102 square feet of office space from the REIT on commercial terms. The lease was to expire on December 31, 2010. The Developer indemnified the REIT in respect of all of TechSpace's obligations under the lease. Effective July 1, 2005, the REIT entered into a direct lease of this space with Loblaws Properties Limited for a term ending October 31, 2010, on the condition that the original indemnity of the Developer remain in place to protect the REIT from any revenue shortfall (on a cash basis) from the original TechSpace lease.

#### Bridge Covenants:

Certain vendors of the rental properties provided bridge covenants (collectively the "Bridge Covenants") to the REIT in respect of certain office space leased to third party, non-related tenants. These Bridge Covenants provided the REIT with an income stream to coincide with rent-free periods that these vendors provided to the tenants prior to the REIT acquiring the rental properties. The vendors, which are under common control of certain trustees of the REIT, honoured all of their obligations under the Bridge Covenants.

### (c) Rental Property Acquisitions

Effective September 1, 2007, the REIT acquired from vendors that are under common control of certain Trustees of the REIT, 559 College Street for a purchase price of \$14,250. The purchase price net of standard adjustments were paid in cash and was determined by an independent appraisal.