



**ALLIED PROPERTIES REAL ESTATE INVESTMENT TRUST**

**PROVIDING URBAN OFFICE ENVIRONMENTS  
THAT ENRICH EXPERIENCE AND ENHANCE PROFITABILITY**

**QUARTERLY REPORT, JUNE 30, 2010**

**AUGUST 4, 2010**

## TABLE OF CONTENTS

<b>LETTER TO UNITHOLDERS</b>	<b>3</b>
<b>MANAGEMENT’S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION AS AT JUNE 30, 2010</b>	<b>5</b>
<b>PART I</b>	
Forward-Looking Disclaimer	5
Business Overview and Strategy	5
Performance Measures	7
Business Environment and Outlook	9
<b>PART II</b>	
Summary Information and Performance for the Six-Month Period Ended June 30, 2010	10
Distributable Income	15
Funds From Operations	16
Adjusted Funds From Operations	16
Net Operating Income	17
<b>PART III</b>	
Financial Condition	17
Liquidity and Commitments	19
<b>PART IV</b>	
Summary Information and Performance for the Quarter Ended June 30, 2010	19
<b>PART V</b>	
Summary Quarterly Information and Performance	21
<b>Part VI</b>	
Critical Accounting Estimates	22
<b>Part VII</b>	
Future Changes in Accounting Policies--Adoption of International Financial Reporting Standards (“IFRS”)	23
<b>PART VIII</b>	
Related Party Transactions	25
<b>PART IX</b>	
Risk and Uncertainties	25
<b>PART X</b>	
Disclosure Controls and Internal Controls	27
<b>PART XI</b>	
Subsequent Events	27
<b>PART XII</b>	
Property Table	28
<b>CONSOLIDATED FINANCIAL STATEMENTS FOR THE PERIOD ENDED JUNE 30, 2010</b>	<b>30</b>
Consolidated Balance Sheets	31
Consolidated Statements of Unitholder’s Equity	32
Consolidated Statements of Earnings and Comprehensive Income	33
Consolidated Statements of Cash Flows	34
Notes to Consolidated Financial Statements	35

## LETTER TO UNITHOLDERS

### Fellow Unitholders of Allied Properties REIT

Canadian REITs held up well in the second quarter, taking advantage of generally stable operating environments and receptive equity and debt markets. Investment activity in Canada was up in the quarter and is expected to accelerate in the third and fourth quarters. This bodes well for Canadian REITs over the remainder of the year.

### Operations

Turning to our own operations, we had a solid second quarter. FFO per unit was 41 cents and AFFO per unit 30 cents, in-line with our expectations.

Leasing across our portfolio was strong. We finished the quarter with leased area of 95%, having renewed or replaced 51% of the leases that mature in 2010, in most cases at rental rates equal to or above in-place rents. This will result in an overall increase of 3% in net rental income per square foot from the affected space.

We finalized several more large-scale renewal negotiations at Cité Multimédia in Montréal. GFI agreed to a renewal and expansion for a total of 54,370 square feet, Fujitsu to a renewal for 15,594 square feet, Compuware to a partial renewal for 13,562 square feet (with GFI taking over most of the remaining space as part of its renewal and expansion) and Orthosoft to a renewal for 12,122 square feet.

We also made progress with CGI's space at Cité Multimédia, the lease for which expires at the end of this year. The space is comprised of six contiguous office floors between 30,000 and 38,000 square feet each and 19,020 square feet on the ground floor that is currently used as office space. We leased 10,867 square feet of the ground floor space to Kids & Co for a day-care facility, and we plan to lease the balance with a view to expanding the range of retail services available to tenants of the complex. (Two of our office tenants at the complex, Morgan Stanley and SAP Labs, have already made long-term commitments for a significant portion of the day-care capacity at the Kids & Co facility.) Of the six office floors, we've leased one floor to SAP Labs. This leaves us with five floors to lease, and we've made proposals to prospective new tenants for each of the five floors.

We've decided not to renew CGI's lease, as we believe we can achieve a superior outcome for the complex with replacement tenants. Even though we'll experience temporary turnover vacancy as a result, we believe the complex will be strengthened by reduced single-tenant exposure, an improved tenant-mix and a longer weighted average lease term.

Finally, we entered into three significant new leases, two for retail space and the other for office space. Patagonia has agreed to lease 6,195 square feet at 500 King Street West in Toronto for a term of 15 years at net rental rates above prior in-place rents. This is the first time in recent years that a clothing merchandiser has located in the King & Spadina area, an indication that the next wave of retail use in the area may be underway. A further indication of strength is the decision by Design Within Reach to expand its store at 425-439 King West by 3,397 square feet. At 645 Wellington Street in Montréal, which we acquired in May of this year, we leased the entire fourth floor (22,209 square feet) to a new tenant. The lease is expected to commence on March 1, 2011, furthering our plan to add value to the property in the next two years.

### Acquisitions

Our acquisition activity is accelerating. In the second quarter, we acquired 645 Wellington Street West, a brick-and-beam building near Cité Multimédia with value-add potential that we're beginning to realize. Earlier today, we announced \$50 million in Class I office acquisitions. The largest of the three acquisitions is the Loughheed Building in downtown Calgary. It will move our urban office platform ever closer to a national scale, something we believe will benefit both our tenants and unitholders going forward. The other two are 49 Front Street East and 252-264 Adelaide Street East in downtown Toronto. These acquisitions will boost our market share in the Downtown East sub-market to nearly 45%.

## Development

In the second quarter, we leased 544 King Street West in Toronto to The Hive for a term of five years commencing December 1, 2010. The Hive is a marketing firm that currently operates from 425-439 King Street West. It will move to make way for Loblaw Properties' expansion later this year, at which time 544 King will become a rental property for accounting purposes.

We also leased another 7,632 square feet at 47-47A Fraser Avenue in Toronto to Loblaw Properties for a term of three years commencing October 1, 2010, bringing the leased area to 100%. This property will also become a rental property for accounting purposes upon commencement of the lease.

We continued pre-leasing Phase I of QRC West in the second quarter. We expect that another 12 months will be required to secure an anchor office tenant of approximately 125,000 square feet in order to finance and initiate construction.

We completed the electrical upgrade at 905 King Street West in Toronto and expect to have the remaining infrastructure upgrade completed on schedule and well within budget. Our plan is to have 40,000 square feet upgraded and producing income early next year and to have the final 20,000 square feet upgraded and producing income early the following year. We expect to achieve a substantial increase in annual net rental revenue once this is done.

The cost of our Properties Under Development was 3.7% of Gross Book Value at the end of the second quarter. We expect this to decline further once 544 King and 47-47A Fraser become rental properties in the fourth quarter, leaving us with even greater capacity to pursue development opportunities.

## Liquidity

We finished the quarter in a strong liquidity position with a conservative Debt Ratio of 48%. Aside from nearly \$40 million drawn on our \$70 million line of credit, we had no variable rate debt at the end of the quarter. Going forward, we have a very moderate mortgage maturity schedule, with no remaining mortgages maturing this year, \$20 million next year and \$37 million in 2012.

Even with the acquisitions announced today, we expect our liquidity to strengthen over the remainder of the year as we take advantage of the favourable debt markets in Canada. We expect to complete a \$6.9 million first mortgage financing on 645 Wellington before the end of third quarter. We also expect to raise another \$20 million over the remainder of the year by placing first mortgages on unencumbered properties in our portfolio.

## Outlook

We anticipate a generally stable operating environment for the remainder of the year. We believe that our Class I portfolio will continue to perform well, just as it has in the past.

Our efforts to address the bulge in our lease-maturity schedule in 2010, 2011 and 2012 have met with success. By year-end, we expect to have completed this process, moderating our lease-maturity schedule considerably.

By year-end, we also expect to have completed between \$100 and \$150 million in acquisitions. We're more likely to complete smaller acquisitions in different target markets than a large-scale acquisition in any particular target market. We're also more likely to finance these acquisitions through debt financing than equity issuance. As always, we'll keep you apprised of our progress.

\* \* \*

If you have any questions or concerns, please don't hesitate to call me at (416) 977-0643 or e-mail me at [memory@alliedpropertiesreit.com](mailto:memory@alliedpropertiesreit.com).

Yours truly,

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

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION  
AS AT JUNE 30, 2010**

**PART I**

**Forward-Looking Disclaimer**

The terms "Allied Properties", "the REIT", "we", "us" and "our" in the following Management's Discussion and Analysis of Results of Operations and Financial Condition ("MD&A") refer to Allied Properties Real Estate Investment Trust and its consolidated financial position and results of operations for the six-month period and quarter ended June 30, 2010. This MD&A is based on financial statements prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). This MD&A should be read in conjunction with our consolidated financial statements and notes thereto for the six-month period and quarter ended June 30, 2010. Historical results and percentage relationships contained in our consolidated financial statements and MD&A, including trends that might appear, should not be taken as indicative of our future results, operations or performance. Unless otherwise indicated, all amounts in this MD&A are in thousands of Canadian dollars.

Certain information included in this Quarterly Report contains forward-looking statements within the meaning of applicable securities laws, including, among other things, statements concerning our objectives and our strategies to achieve those objectives, statements with respect to Management's beliefs, plans, estimates and intentions and statements concerning anticipated future events, circumstances, expectations, results, operations or performance that are not historical facts. Forward-looking statements can be identified generally by the use of forward-looking terminology, such as "indicators", "outlook", "objective", "may", "will", "expect", "intend", "estimate", "anticipate", "believe", "should", "plans", "continue" or similar expressions suggesting future outcomes or events. Such forward-looking statements reflect Management's current beliefs and are based on information currently available to Management.

The forward-looking statements in this Quarterly Report are not guarantees of future results, operations or performance and are based on estimates and assumptions that are subject to risks and uncertainties, including those described below in this MD&A under "Risks and Uncertainties", which could cause actual results, operations or performance to differ materially from the forward-looking statements in this Quarterly Report. Those risks and uncertainties include risks associated with property ownership, property development, geographic focus, asset-class focus, competition for real property investments, financing and interest rates, government regulations, environmental matters, construction liability, unitholder liability and taxation. Material assumptions that were made in formulating the forward-looking statements in this Quarterly Report include the following: that our current target markets remain stable, with moderating demand for office space and no material increase in supply of directly-competitive office space; that acquisition capitalization rates continue to stabilize; that the trend toward intensification within our target markets continues; and that the equity and debt markets continue to provide us with access to capital at a reasonable cost to fund our future growth, to refinance our mortgage debt as it matures; and that we have accurately evaluated the impact of the accounting principles to be adopted effective January 1, 2011, under International Financial Reporting Standards ("IFRS") which includes application to our 2010 comparative financial results. Although the forward-looking statements contained in this Quarterly Report are based on what Management believes are reasonable assumptions, there can be no assurance that actual results, operations or performance will be consistent with these statements.

All forward-looking statements in this Quarterly Report are qualified by this forward-looking disclaimer. These statements are made as of August 4, 2010, and, except as required by applicable law, we undertake no obligation to update publicly or revise any such statements to reflect new information or the occurrence of future events or circumstances.

**Business Overview and Strategy**

We are an unincorporated closed-end real estate investment trust created pursuant to the Declaration of Trust dated October 25, 2002, as amended and restated on February 6, 2003 and May 14, 2008 ("Declaration"). We are governed by the laws of Ontario. Our units are publicly traded on the Toronto Stock Exchange under the symbol AP.UN. Additional information on us, including our annual information form, is available on SEDAR at [www.sedar.com](http://www.sedar.com).

We are a leading owner, manager and developer of urban office environments that enrich experience and enhance profitability for business tenants operating from Toronto, Montréal, Winnipeg, Québec City and Kitchener-Waterloo. Our objectives are to provide stable and growing cash distributions to unitholders and to maximize unitholder value through effective management and accretive portfolio growth.

We specialize in an office format created through the adaptive re-use of light industrial structures in urban areas that has come to be known as Class I, the “I” stemming from the original industrial nature of the structures. This format typically features high ceilings, abundant natural light, exposed structural frames, interior brick and hardwood floors. When restored and retrofitted to the standards of our portfolio, Class I buildings can satisfy the needs of the most demanding office and retail tenants. When operated in the coordinated manner of our portfolio, these buildings become a vital part of the urban fabric and contribute meaningfully to a sense of community.

The Class I value proposition includes (i) proximity to central business districts in areas well served by public transportation, (ii) distinctive internal and external environments that assist tenants in attracting, retaining and motivating employees (iii) significantly lower overall occupancy costs than those that prevail in the central business districts. The value proposition has proven appeal to a diverse base of business tenants, including the full range of service and professional firms, telecommunications and information technology providers, media and film groups and storefront retailers.

### ***Property Portfolio***

We completed our Initial Public Offering (“IPO”) on February 20, 2003. We used the net proceeds of the IPO to acquire a portfolio of 14 predominantly Class I office properties in downtown Toronto with 820,000 square feet of gross leasable area (“GLA”). By the end of 2009, we had acquired another 43 office properties in downtown Toronto, 42 of them Class I office properties, bringing our total GLA in that market to 3.3 million square feet. We had also acquired 16 predominantly Class I office properties in downtown Montréal, seven in downtown Winnipeg, five in Québec City and one in Kitchener-Waterloo, bringing our total portfolio at the end of 2009 to 85 properties with almost six million square feet of GLA.

We also announced the following acquisitions in 2009, which are included in our calculation of future commitments, as set out in “Liquidity and Commitments” below:

- (i) an undivided 50% interest in 92 underground commercial parking spaces to be constructed as part of the condominium project at 478 King Street West in Toronto, which is adjacent to three of our properties, 468 King Street West, 500-522 King Street West and the King-Brant underground commercial parking structure;
- (ii) an undivided 50% interest in 140 underground commercial parking spaces and 18,360 square feet of retail space to be constructed as part of a condominium project at 560 King West in Toronto, which is adjacent to our 544 King West; and
- (iii) an undivided 75% interest in 71 underground commercial parking spaces to be constructed as part of the condominium project at 650 King Street West in Toronto, which is adjacent to our 662 King Street West and in close proximity to our 602-606 King Street West.

Each acquisition is conditional upon final condominium registration which is expected to close between 2011 and 2013, subject to normal conditions. We will manage all three underground commercial parking structures on behalf of the co-owners, giving us operating control over 303 parking spaces in addition to the 208 parking spaces at our King-Brant underground commercial parking structure and the large number of surface commercial parking spaces adjacent to our many properties in the King & Spadina area.

Thus far in 2010, we have made one acquisition for \$10.5 million, bringing our portfolio to 86 properties with over six million square feet of GLA. It was 645 Wellington Street in Montréal, a brick and beam building with 134,688 square feet of GLA and located in close proximity to Cité Multimédia.

Four Toronto properties (47-47A Fraser Avenue, 134 Peter Street, 544 King Street West and 905 King Street West) and one Montréal property (4450 Saint-Laurent Boulevard) are currently properties under development (“Properties Under Development” or “PUDs”). They are undergoing redevelopment, development or intensification. Two Properties Under Development, 544 King Street West and 47-47A

Fraser Avenue, are scheduled for completion in the fourth quarter of 2010, at which time they will become rental properties for accounting purposes. See “Properties Under Development” below.

### **Property Management**

Our wholly owned subsidiary, Allied Properties Management Limited Partnership, provides property management and related services to us and to third-party property owners on a fee-for-service basis.

### **Sustainability**

We are committed to sustainability, both as it relates to our business and to the physical environment within which we operate. Most of our buildings were created through the adaptive re-use of structures built nearly a century ago. They are recycled buildings, and the recycling has had considerably less impact on the environment than new construction of equivalent GLA would have had. To the extent we undertake new construction through development or intensification, we are committed to obtaining LEED certification. See “Properties Under Development” and “Intensification” below. LEED certification is a program established by the U.S. Green Building Council for certifying the design, construction and operation of high-performance green buildings. The program has gained wide acceptance in North America and elsewhere.

### **Performance Measures**

We measure the success of our strategies through key financial and operating performance measures.

#### **Financial Measures**

##### **1. Distributions**

We are focused on increasing distributions to our unitholders on a regular and prudent basis. During our first 12 months of operations, we made regular monthly distributions of \$1.10 per unit on an annualized basis. Our distribution increases since then are set out in the table below:

	<b>March, 2004</b>	<b>March, 2005</b>	<b>March, 2006</b>	<b>March, 2007</b>	<b>March, 2008</b>
Annualized increase per unit	\$0.04	\$0.04	\$0.04	\$0.04	\$0.06
% increase	3.6%	3.5%	3.4%	3.3%	4.8%
Annualized distribution per unit	\$1.14	\$1.18	\$1.22	\$1.26	\$1.32

We did not increase distributions in 2009 and do not anticipate doing so in 2010.

##### **2. Distributable Income**

Increasing distributions can be achieved prudently by increasing Distributable Income (“DI”), as defined in the Declaration. See “Distributable Income” below. In the first half of 2010, DI per unit (diluted) was \$0.78, down 4.9% from the comparable period in 2009. The decline is largely attributable to lower occupancy and a lower Debt Ratio in the first half of 2010.

##### **3. DI Pay-Out Ratio**

To ensure we retain sufficient cash to meet our capital improvement and leasing objectives, we strive to maintain an appropriate DI pay-out ratio, the ratio of actual distributions to DI in a given period. In the first half of 2010, our DI pay-out ratio was 84.1%

##### **4. Funds From Operations**

Unlike DI, Funds From Operations (“FFO”) has a standardized definition. See “Funds From Operations” below. In the first half of 2010, FFO per unit (diluted) was \$0.84, down 5.6% from the comparable period in 2009. The decline is largely attributable to lower occupancy and a lower Debt Ratio in the first half of 2010.

##### **5. FFO Pay-Out Ratio**

To ensure we retain sufficient cash to meet our capital improvement and leasing objectives, we strive to maintain an appropriate FFO pay-out ratio, the ratio of actual distributions to FFO in a given period. In the first half of 2010, our FFO pay-out ratio was 78.6%.

##### **6. Adjusted Funds From Operations**

Increasing distributions cannot be achieved prudently without reference to adjusted funds from operations (“AFFO”), as this financial measure takes account of regular maintenance capital expenditures and

regular leasing expenditures while ignoring the impact of non-cash revenue. See “Adjusted Funds from Operations” below. In the first half of 2010, AFFO per unit (diluted) was \$0.67, down 15.2% from the comparable period in 2009. The decline is largely attributable to an abnormally high volume of leasing activity and corresponding leasing expenditure in the first half of 2010.

#### 7. AFFO Pay-Out Ratio

To ensure we retain sufficient cash to meet our capital improvement and leasing objectives, we strive to maintain an appropriate AFFO pay-out ratio, the ratio of actual distributions to AFFO in a given period. In the first half of 2010, our AFFO pay-out ratio was 97.8%.

#### 8. Debt Ratio

Gross Book Value (“GBV”) is defined as the book value of the assets shown on our most recent balance sheet plus accumulated depreciation and amortization and an amount equal to the property management internalization expense that we have recorded. A conservative ratio of debt to GBV (“Debt Ratio”) mitigates unitholder risk. On June 30, 2010, our Debt Ratio was 48.0%, down from 49.3% at the same time in 2009.

### **Operating Measures**

#### 1. Tenant Retention and Replacement

We place a high value on tenant retention, as the cost of retention is typically lower than the cost of securing new tenancies. If retention is neither possible nor desirable, we strive for high-quality replacement tenants. Leases representing 1,309,616 square feet of GLA mature in 2010. By June 30, 2010, we had renewed leases representing 437,528 square feet of this GLA and re-leased another 232,983 square feet of this GLA, representing 51.2% of the GLA covered by the maturing leases.

#### 2. Occupancy

We strive to maintain consistently high levels of occupancy. At June 30, 2010, our leased area was 95.0% (not including Properties Under Development). The chart below summarizes the year-end levels of GLA and leased area in our portfolio since the end of 2003:

	2003	2004	2005	2006	2007	2008	2009
GLA (square feet)	984,856	1,636,343	2,321,507	3,415,279	4,761,211	5,350,208	5,675,420
% leased	97.5	99.2	97.0*	96.3*	97.9*	97.3*	96.0*

\*not including Properties Under Development

#### 3. Same-Asset Net Operating Income

We strive to maintain or increase same-asset net operating income (“NOI”) over time. See “Net Operating Income” below. Same-asset refers to those properties that we owned and operated for the entire period in question and for the same period in the prior year. Ignoring the step-rent revenue and the amortization of the fair value assigned to above-market and below-market rents with respect to acquired properties (the mark-to-market rent adjustment), same-asset NOI was \$40,259 in the first half of 2010, down 4.8% from the comparable period in 2009. The decline is attributable to lower occupancy in the first half of 2010.

#### 4. Leasing Expenditures

We monitor leasing expenditures carefully. Leases for 541,846 square feet of GLA commenced in the first half of 2010. \$3,887 in leasing expenditures related to this space, representing \$7.16 per leased square foot, in line with our normal range of \$7 to \$10 per leased square foot.

#### 5. Capital Expenditures

We strive to maintain our properties in top physical condition. In the first half of 2010, we incurred \$1,411 in regular maintenance capital expenditures, representing 24 cents per square foot of our portfolio, in line with the amount per square foot in the first half of prior years.

### **Summary**

The following table summarizes the key financial and operating performance measures for the first half of 2010 and the comparable period in 2009, as well as the change between the two.

	H1 2010	H1 2009	Change	% Change
Period-end distribution level per unit annualized	\$1.32	\$1.32	\$0.00	0.0%
DI per unit (diluted)	\$0.78	\$0.82	(\$0.04)	(4.9%)
DI pay-out ratio	84.1%	80.4%	3.7%	
FFO per unit (diluted)	\$0.84	\$0.89	(\$0.05)	(5.6%)
FFO pay-out ratio	78.6%	74.0%	4.6%	
AFFO per unit (diluted)	\$0.67	\$0.79	(\$0.12)	(15.2%)
AFFO pay-out ratio	97.8%	82.7%	15.1%	
Debt Ratio	48.0%	49.3%	(1.3%)	
Renewal/replacement % of leases maturing in year	51.2%	51.2%	0.0%	
Period-end leased area (not including PUD)	95.0%	96.3%	(1.3%)	
Same-asset NOI	\$40,259	\$42,299	(\$2,040)	(4.8%)
Leasing expenditures	\$3,887	\$2,137	\$1,750	81.9%
Leasing expenditures per square foot	\$7.16	\$5.37	\$1.79	33.3%
Maintenance capital expenditures	\$1,411	\$278	\$1,133	407.6%
Maintenance capital expenditures per portfolio square foot	\$0.24	\$0.05	\$0.19	380.0%

## Business Environment and Outlook

We operate in five target markets—downtown Toronto, downtown and midtown Montréal, downtown Winnipeg, downtown Québec City and downtown Kitchener. The following is a brief description of our target markets and current outlook:

### ***Downtown Toronto***

This target market includes 13.3 million square feet of office inventory in three sub-markets, Downtown East (2.1 million square feet), Downtown West (9.2 million square feet) and King West (2.0 million square feet). Approximately half of the office inventory in this target market falls within the Class I category. At June 30, 2010, the overall vacancy rate for the downtown Toronto office market was 6.8%, with the Downtown East, Downtown West and King West sub-markets finishing the quarter at 10.6%, 7.0% and 16.9%, respectively.<sup>1</sup>

### ***Downtown and Midtown Montréal***

This target market includes 17.8 million square feet of office inventory in three sub-markets, Downtown East (7.5 million square feet), Old Montréal (7.8 million square feet) and Mile End (2.5 million square feet). Approximately half of the office inventory in this target market falls within the Class I category. At June 30, 2010, the overall vacancy rate for the downtown Montréal office market was 7.9%, with the Downtown East and Old Montréal sub-markets finishing the quarter at 2.8% and 7.7%, respectively.<sup>2</sup>

### ***Downtown Winnipeg***

This target market includes 1.8 million square feet of office inventory, principally in the Exchange District. Most of the office inventory in this target market falls within the Class I category. At June 30, 2010, the overall vacancy rate for downtown Winnipeg office market was 7.6%.<sup>3</sup>

<sup>1</sup> Cushman & Wakefield, *Second Quarter 2010 Statistical Summary, Toronto Office Market*.

<sup>2</sup> Cushman & Wakefield, *Second Quarter 2010 Statistical Summary, Montréal Office Market*.

<sup>3</sup> Cushman & Wakefield, *Second Quarter 2010 Statistical Summary, National Office Market*.

### **Downtown Québec City**

This target market includes 1.5 million square feet of office inventory in the Saint-Roch office node. Most of the office inventory in this target market falls within the Class I category. At June 30, 2010, the vacancy rate for the downtown Québec City office market was 5.9%.<sup>4</sup>

### **Downtown Kitchener**

This target market includes approximately 1 million square feet of existing and potential office inventory in the Warehouse District. Much of the office inventory in this target market falls within the Class I office category. At June 30, 2010, the overall vacancy rate in the downtown Kitchener office market was 16.3%.<sup>5</sup>

### **Outlook**

We anticipate a generally stable operating environment for the remainder of the year. We believe that our Class I portfolio will continue to perform well, just as it has in the past.

Our efforts to address the bulge in our lease-maturity schedule in 2010, 2011 and 2012 have met with success. By year-end, we expect to have completed this process, moderating our lease-maturity schedule considerably.

By year-end, we also expect to have completed between \$100 and \$150 million in acquisitions. We're more likely to complete smaller acquisitions in different target markets than a large-scale acquisition in any particular target market. We're also more likely to finance these acquisitions through debt financing than equity issuance. As always, we'll keep you apprised of our progress.

## **PART II**

### **Summary Information and Performance for the Six-Month Period Ended June 30, 2010**

The following sets out summary information and financial results for the six-month period ended June 30, 2010, and the comparable period, as well as the change between the two.

(In thousands except for per unit and % amounts)	H1 2010	H1 2009	Change	%Change
Revenue from rental properties	90,804	72,707	18,097	24.9%
Rental property operating cost	38,450	29,156	9,294	31.9%
Net rental income	52,354	43,551	8,803	20.2%
Real estate service income	116	135	(19)	(14.1%)
Financing expense				
Interest	16,425	13,583	2,842	20.9%
Amortization - Mortgage premium	(7)	(14)	7	(50.0%)
Amortization - Financing cost	415	321	94	29.3%
Amortization				
Rental properties	11,146	8,798	2,348	26.7%
Leasing cost and tenant improvements	1,613	1,823	(210)	(11.5%)
Origination cost and acquired tenant relationships	10,803	9,410	1,393	14.8%
Acquired contracts and customer relationships	48	48	-	0.0%
Computer and office equipment	158	138	20	14.5%
Income from operations	11,869	9,579	2,290	23.9%
Trust expense	2,680	1,753	927	52.9%
Net income	9,189	7,826	1,363	17.4%
Amortization				
Rental properties	11,146	8,798	2,348	26.7%
Mortgage premium	(7)	(14)	7	(50.0%)
Acquired leases	3,209	3,325	(116)	(3.5%)
M-T-M acquired leases	(952)	(134)	(818)	610.4%
Acquired tenant relationships	7,594	6,085	1,509	24.8%
Acquired contracts and customer relationships	48	48	-	0.0%
Step-rent adjustments	(180)	(406)	226	(55.7%)
Unit based compensation expense	555	111	444	400.0%
DI	30,602	25,639	4,963	19.4%

<sup>4</sup> Avison Young, *National Office Market Report, Second Quarter 2010*.

<sup>5</sup> Colliers International, *Second Quarter 2010*.

(In thousands except for per unit and % amounts)	H1 2010	H1 2009	Change	%Change
Weighted average units outstanding (basic)	38,709	30,940	7,769	25.1%
Weighted average units outstanding (diluted)	39,157	31,336	7,821	25.0%
Distributions	25,735	20,604	5,131	24.9%
DI per unit (basic)	\$0.79	\$0.83	(\$0.04)	(4.8%)
DI per unit (diluted)	\$0.78	\$0.82	(\$0.04)	(4.9%)
DI pay-out ratio	84.1%	80.4%	3.7%	
FFO	32,751	27,857	4,894	17.6%
FFO per unit (basic)	\$0.85	\$0.90	(\$0.05)	(5.6%)
FFO per unit (diluted)	\$0.84	\$0.89	(\$0.05)	(5.6%)
FFO pay-out ratio	78.6%	74.0%	4.6%	
AFFO	26,321	24,902	1,419	5.7%
AFFO per unit (basic)	\$0.68	\$0.80	(\$0.12)	(15.0%)
AFFO per unit (diluted)	\$0.67	\$0.79	(\$0.12)	(15.2%)
AFFO pay-out ratio	97.8%	82.7%	15.1%	
NOI	51,222	43,011	8,211	19.1%
Same-asset net operating income	40,259	42,299	(2,040)	(4.8%)
Total assets	1,158,995	942,806	216,189	22.9%
Total debt (excludes premium on assumed debt)	646,273	531,857	114,416	21.5%
Debt Ratio	48.0%	49.3%	(1.3%)	
Total GLA (s.f., excluding PUD)	5,816	5,451	365	6.7%
Leased GLA (s.f., excluding PUD)	5,524	5,246	278	5.3%
Leased GLA (% total GLA)	95.0%	96.3%	(1.3%)	

### **Net Income**

Net income for the six-month period ended June 30, 2010, was \$9,189, as compared to \$7,826 in the six-month period ended June 30, 2009. Net income per unit (diluted) for the period was \$0.23, as compared to \$0.25 in the comparable period. As part of an advantageous lease replacement at Cité Multimédia in Montréal, we received an early-termination payment in the first quarter. This non-recurring item added \$530 to our net income in the period.

DI for the six-month period ended June 30, 2010, increased by 18.8% to \$30,602 from \$25,639 for the six-month period ended June 30, 2009. DI per unit (diluted) for the period was \$0.78, as compared to \$0.82 in the comparable period.

### **Net Rental Income**

Net rental income for the six-month period ended June 30, 2010, increased by 20.2% to \$52,354 from \$43,551 in the six-month period ended June 30, 2009, as follows: (i) \$3,056 decrease in same-asset net rental income from properties owned for year and the entire comparable year (which includes the period-over-period change in step-rent adjustments and mark-to-market rent adjustments); and (ii) \$11,859 due to net rental income from properties not owned for the entire quarter and the entire comparable quarter. The non-recurring item referred to under "Net Income" above added \$1,122 to our net rental income in the period.

Net rental income per occupied square foot for the sixth-month period ended June 30, 2010, was \$18.95 annualized, as compared to \$16.60 annualized in the comparable period.

### **Real Estate Service Income**

The Property Manager provides real estate services to third-party property owners. Real estate service income for the six-month period ended June 30, 2010, was \$116, as compared to \$135 in the six-month period ended June 30, 2009.

### **Financing Expense**

Financing expense includes interest cost on mortgage debt and other credit facilities and the amortization of the premiums and discounts on assumed mortgages. For the six-month period ended June 30, 2010, interest increased by 20.9% to \$16,425 from \$13,583 in the six-month period ended June 30, 2009, due to the increase in financing expense associated with additional properties acquired in 2009 and 2010.

### **Amortization**

We record amortization on our buildings on a straight-line basis over their expected life. Amortization recorded on buildings for the six-month period ended June 30, 2010, increased by 26.7% to \$11,146 from \$8,798 in the six-month period ended June 30, 2009.

We record amortization of leasing cost, tenant improvements and the assigned fair value of the origination cost and tenant relationships for in-place leases acquired on acquisition of a rental property on a straight-line basis over the term of the corresponding lease.

### **Trust Expense**

Trust expense includes cost not directly attributable to rental property, such as officers' compensation, trustees' fees, professional fees for legal and audit services, trustees' and officers' insurance premiums and general administrative expenses. Trust expense for the six-month period ended June 30, 2010, increased by 52.9% to \$2,680 from \$1,753 in the six-month period ended June 30, 2009, due to costs associated with the implementation of IFRS and executive compensation.

### **Leasing Activity**

Leasing activity as at June 30, 2010, is summarized in the following table:

	GLA	SF Leased by June 30	% Leased by June 30	SF Vacant on June 30*
Vacancy on January 1, 2010*	250,446	112,938	45.1	137,508
Arranged vacancies for H1 2010	20,517	-	-	20,517
Acquired vacancies for H1 2010	17,632	8,226	46.7	9,406
Maturities in H1 2010	493,063	368,859	74.8	124,204
Maturities in remainder of 2010	816,553	301,652	36.9	-
<b>Total</b>	<b>1,598,211</b>	<b>791,675</b>	<b>49.5</b>	<b>291,635</b>

\*not including Properties Under Development

250,446 square feet of GLA was vacant at the beginning of 2010. By June 30, 2010, we leased 112,938 square feet of this GLA, leaving 137,508 square feet vacant at the end of the quarter.

Leases for 493,063 square feet of GLA matured in the six-month period ended June 30, 2010. By the end of the period, we renewed or replaced leases for 368,859 square feet of this GLA, leaving 124,204 square feet vacant at the end of the period. Of the 816,553 square feet of GLA maturing in the third and fourth quarter of 2010, we renewed or replaced 301,652 square feet by the end of the period.

With respect to the maturing leases renewed or replaced in the six-month period ended June 30, 2010 (670,511 square feet of GLA), we achieved rental rates (i) above in-place rental rates with respect to 59.6% of this GLA, (ii) equal to in-place rental rates with respect to 14.0% of this GLA and below in-place rates with respect to 26.4% of this GLA. This will result in an overall increase of approximately 3% in net rental income per square foot from the GLA covered by the maturing leases.

We monitor the level of sub-lease space in our portfolio. We are unaware of any space being offered for sub-lease in our Québec and Winnipeg portfolios. We are aware of 33,887 square feet of space being offered for sub-lease in our Toronto portfolio, 31,280 square feet being offered for sub-lease in our Montréal portfolio and 27,099 square feet in our Kitchener-Waterloo portfolio. This level of sub-lease space is consistent with past experience and does not represent an operating or leasing challenge to us, especially in light of the fact that almost all of the sub-lease space in question has limited remaining term. In our experience, prospective sub-tenants of such space will strive to enter into a direct leasing relationship with us and thereby obtain extended term. This tends to put us in a very good bargaining position opposite both the head-tenant and the sub-tenant.

In the first quarter, we finalized four large-scale lease negotiations, three at Cité Multimédia in Montréal and one at 425-439 King Street West in Toronto.

- Motorola leased 73,532 square feet at Cité Multimédia pursuant to a lease expiring on May 31, 2011. Morgan Stanley has agreed to lease a portion of this space for a term of 10 years from September 1, 2010, and the balance of the space for a term of nine years and eight months from May 1, 2011, in both cases at net rental rates above in-place rents and with a net rent escalation for the second five years of the term.

- SAP Labs currently leases 75,882 square feet at Cité Multimédia pursuant to a lease that expires on August 31, 2011. SAP Labs has agreed to renew its lease with respect to 53,029 square feet and take up another 30,236 square feet for a term of 10 years from September 1, 2011, at net rental rates above in-place rents and with a net rent escalation for the second five years of the term.
- Loblaw Properties currently leases 45,561 square feet at 425-439 King Street West in Toronto pursuant to a lease that expires on October 31, 2010. Loblaw has agreed to renew its lease and take up another 15,187 square feet for a term of two and one-half years from November 1, 2010, at net rental rates above in-place rents.

We also filled two important vacancies in the first quarter, one in Toronto and one in Winnipeg. 96 Spadina Avenue in Toronto became a rental property in May of 2009 with 22,446 square feet unleased (24.5% of the total), including in 9,361 square feet of storefront space that had been reconfigured for retail use. Dollarama has agreed to lease this space for a term of 10 years from September 1, 2010, with a net rental escalation for the second five years of the term. CanTalk has agreed to lease 9,500 square feet at 70 Arthur Street in Winnipeg for a term of 10 years commencing October 1, 2010.

In the second quarter, we finalized several more large-scale renewal negotiations at Cité Multimédia in Montréal.

- GFI currently leases 42,175 square feet pursuant to several leases that expire between 2010 and 2013. GFI has agreed to renew its leases and take up another 12,195 square feet for a term of 10 years from January 1, 2011, at net rental rates above in-place rents and with a net rental escalation for the second five years of the term.
- Fujitsu currently leases 15,594 square feet pursuant to a lease that expires on October 31, 2010. Fujitsu has agreed to renew its lease for a term of two years at net rental rates above in-place rents.
- Compuware currently leases 54,166 square feet pursuant to a lease that expires on September 30, 2010. Compuware has agreed to renew its lease with respect to 13,562 square feet (with GFI taking over the most of its remaining space as part of its renewal and expansion) for a term of five years at net rental rates below in-place rents.
- Orthosoft currently leases 12,122 square feet pursuant to a lease that expires on December 31, 2010. Orthosoft has agreed to renew its lease for a term of five years at net rental rates equal to in-place rents.

We also made progress with CGI's space at Cité Multimédia, the lease for which expires at the end of this year. The space is comprised of six contiguous office floors between 30,000 and 38,000 square feet each and 19,020 square feet on the ground floor that is currently used as office space. We leased 10,867 square feet of the ground floor space to Kids & Co for a day-care facility, and we plan to lease the balance with a view to expanding the range of retail services available to tenants of the complex. (Two of our office tenants at the complex, Morgan Stanley and SAP Labs, have already made long-term commitments for a significant portion of the day-care capacity at the Kids & Co facility.) Of the six office floors, we've leased one floor to SAP Labs. This leaves us with five floors to lease, and we've made proposals to prospective new tenants for each of those floors.

We've decided not to renew CGI's lease, as we believe we can achieve a superior outcome for the complex with replacement tenants. Even though we'll experience temporary turnover vacancy as a result, we believe the complex will be strengthened by reduced single-tenant exposure, an improved tenant-mix and a longer weighted average lease term.

Finally, we entered into three significant new leases, two for retail space and the other for office space. Patagonia has agreed to lease 6,195 square feet at 500 King Street West in Toronto for a term of 15 years at net rental rates above prior in-place rents. This is the first time in recent years that a clothing merchandiser has located in the King & Spadina area, an indication that the next wave of retail use in the area may be underway. A further indication of strength is the decision by Design Within Reach to expand its store at 425-439 King West by 3,397 square feet. At 645 Wellington Street in Montréal, which we acquired in May of this year, we leased the entire fourth floor (22,209 square feet) to a new tenant. The

lease is expected to commence on March 1, 2011, furthering our plan to add value to the property in the next two years.

### **Capital Expenditures**

Our portfolio requires ongoing maintenance capital expenditures and leasing expenditures. Leasing expenditures include the cost of in-suite or base-building improvements made in connection with the leasing of vacant space or the renewal or replacement of tenants occupying space covered by maturing leases, as well as improvement allowances and commissions paid in connection with the leasing of vacant space and the renewal or replacement of tenants occupying space covered by maturing leases.

In the six-month period ended June 30, 2010, we incurred (i) \$1,411 in regular maintenance capital expenditures (\$0.24 per portfolio square foot) and (ii) \$3,887 in leasing expenditures (\$7.16 per leased square foot) in connection with new leases or lease-renewals that commenced in the period. In addition, we incurred \$1,913 in revenue-enhancing capital and leasing expenditures in connection with space that was significantly reconfigured and retrofitted to accommodate high-value new tenancies and in connection with the completion of redevelopment projects.

\$455 of the salary expense incurred in the period was capitalized in connection with capital improvements to our rental properties and Properties Under Development. This amount was equivalent to approximately 8.58% of the associated development costs.

### **Properties Under Development**

Our Properties Under Development are identified in the following table and described briefly below:

<b>PUDs in Progress</b>	<b>Estimated GLA</b>
47-47A Fraser, Toronto	31,772
4450 Saint-Laurent, Montréal*	22,000
544 King West, Toronto*	20,000
134 Peter, Toronto*	300,000
905 King West, Toronto	112,096
<b>Total</b>	<b>485,868</b>

\*Conditional on satisfactory pre-leasing

47-47A Fraser Avenue, Toronto, is a satellite building at The Castle in Liberty Village with 31,772 square feet of GLA. We leased another 7,632 square feet at the property to Loblaw Properties for a term of three years commencing October 1, 2010, bringing the leased area to 100%. 47-47A Fraser will become a rental property for accounting purposes upon commencement of the lease.

4450 Saint-Laurent Boulevard, Montréal, includes 5,500 square feet of land adjacent to our Class I office building at 4446 Saint-Laurent Boulevard. Our plan is to construct on the land an office building with Class I attributes and approximately 22,000 square feet of GLA. The execution of this project, as currently conceived, is contingent upon achieving a level of pre-leasing satisfactory to Management and the Trustees.

544 King Street West, Toronto, includes a renovated brick-and-beam building with 20,000 square feet of GLA and 28 surface parking spaces. We have now leased the entire building to The Hive for a term of five years commencing December 1, 2010. A long-standing tenant, The Hive is a marketing firm that currently operates from 425-439 King Street West. It will move to make way for Loblaw Properties' expansion later this year, at which time 544 King will become a rental property for accounting purposes.

134 Peter Street, Toronto, includes approximately 14,500 square feet of surplus land with frontage on Peter and Richmond Streets. Our plan is to restore the existing historic building and to construct a new, LEED-certified, office building with Class I attributes and approximately 250,000 square feet of GLA. The execution of this project is contingent upon achieving a level of pre-leasing satisfactory to Management and the Trustees.

On December 17 2009, we acquired of 375-381 Queen Street West. Located on the southwest corner of the intersection of Queen and Peter Streets, just north of 134 Peter Street, this Class I property is comprised of 34,979 square feet of gross leasable area and 4,381 square feet of surplus land. We plan to incorporate the surplus land into the project by creating dedicated parking spaces for 134 Peter Street using parking-stacker technology. We also plan to incorporate the building into the project and to create

additional office space by building onto and out from the building. Although it will be incorporated into the intensification project, 375-381 Queen Street West provides a going-in yield of 7.4% and will be a rental property for accounting purposes for the time being.

By incorporating 375-381 Queen Street West, the intensification of 134 Peter Street will now extend along Peter Street from Queen to Richmond Streets. For this reason, we've decided to refer to the expanded project as Queen Richmond Centre West or QRC West. Not only is this name descriptive, it builds on the fact that we own QRC, one of the very best Class I office complexes in Downtown East, as well as the neighbouring QRC South.

QRC West will be completed in two phases. Phase I is the 134 Peter component, for which municipal approval has been received. Site-plan approval is underway and expected to be complete by the fourth quarter of this year. The pre-leasing of Phase I has commenced and further details are available at [www.qrcwest.com](http://www.qrcwest.com). Phase II is the 375-381 Queen component. We are currently seeking municipal approval for this component of the project.

In November of 2009, we put 905 King Street West into development after identifying it as an optimal building for expanding the capacity of 151 Front Street West. The building already has four diverse fibre-entry points, internal point-of-presence with Allstream, Bell, Cogeco and Rogers, significant electrical power with two feeder lines, a 600 kilowatt diesel generator on the roof, diesel fuel storage in the lower parking levels and room for expansion of both electrical power and cooling. We have now completed the electrical upgrade and expect to have the rest of the infrastructure upgrade completed on schedule and well within budget. Our plan is to have 40,000 square feet upgraded and producing income early next year and to have the final 20,000 square feet upgraded and producing income in the early part of the following year. We expect to achieve a substantial increase in annual net rental revenue once this is done.

Properties Under Development are stated at the lower of cost and net recoverable value. Cost includes the cost of acquisition, 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 development-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 development-period ends if warranted by circumstances relating to the relevant Property Under Development.

As at June 30, 2010, the cost of our Properties Under Development was \$48,812, which was equivalent to 3.7% of our GBV.

### ***Intensification***

The buildings on most of our 57 Toronto properties have considerably less GLA than is permissible under the current zoning. This affords us the opportunity to create additional GLA without land cost and with correspondingly higher returns on equity. The combined land area of our Toronto properties is approximately 1,050,000 square feet or 24 acres. We have evaluated the Toronto portfolio on a property-by-property basis and have estimated that it is practically possible to create between 1.25 million and 1.75 square feet of additional GLA in the near term, market conditions permitting. QRC West is a very good example of the intensification that is possible within our existing portfolio.

### **Distributable Income**

We define DI as the net income determined in accordance with GAAP adjusted by adding back or deducting as required:

- (i) amortization on rental properties;
- (ii) amortization of the premiums or discounts on assumed mortgages;
- (iii) non-cash rental revenue recorded to recognize rental income rateably over the life of each lease;
- (iv) non-cash compensation expense with respect to the LTIP and Unit Option Plan;

- (v) amortization of values ascribed in a building acquisition to in-place leases and tenant relationships;
- (vi) amortization of values ascribed in a building acquisition to above-market and below-market leases;
- (vii) amortization of values ascribed in the property management internalization to acquired contracts and customer relationships; and
- (viii) property management internalization expense.

DI is a non-GAAP financial measure used by some Canadian real estate investment trusts and should not be considered as an alternative to net income, cash flow from operations or any other measure prescribed under GAAP. DI does not have any standardized meaning prescribed by GAAP. As computed by us, DI may differ from similar computations reported by other Canadian real estate investment trusts and, accordingly, may not be comparable to similar computations reported by such organizations. Management considers DI to be a useful measure of cash available for distributions. The following reconciles cash flow from operations, as presented in the consolidated financial statements, to DI.

(In thousands)	Six Months ended June 30, 2010	Six Months ended June 30, 2009
Cash flow from operations	19,963	26,308
Amortization of leasing cost, tenant improvements	(1,613)	(1,823)
Amortization of financing cost	(415)	(321)
Amortization of computer and office equipment	(158)	(138)
Change in non-cash operating items	12,825	1,613
DI	30,602	25,639

Distributions for the six-month period ended June 30, 2010, were \$25,735, representing a DI pay-out ratio of 84.1%, as compared to distributions for the six-month period ended June 30, 2009, of \$20,604 representing a DI pay-out ratio of 80.4%.

### Funds From Operations

FFO is a non-GAAP financial measure used by most Canadian real estate investment trusts and should not be considered as an alternative to net income, cash flow from operations or any other measure prescribed under GAAP. While FFO does not have any standardized meaning prescribed by GAAP, the Real Property Association of Canada ("REALpac") established a standardized definition of FFO in its White Paper on Funds From Operations dated November 30, 2004. Essentially, the REALpac definition is net income with most non-cash expenses added back. Management believes that this definition is followed by most Canadian real estate investment trusts and that it is a useful measure of cash available for distributions. The following reconciles net income, as presented in the consolidated financial statements, with FFO, as calculated in accordance with recommendations of the REALpac definition.

(In thousands)	Six Months ended June 30, 2010	Six Months ended June 30, 2009
Net income	9,189	7,826
Amortization on rental properties	11,146	8,798
Amortization of leasing cost and tenant improvements	1,613	1,823
Amortization of origination cost and acquired tenant relationships	10,803	9,410
FFO	32,751	27,857

Distributions for the six-month period ended June 30, 2010, represented an FFO pay-out ratio of 78.6%, as compared to distributions for the six-month period ended June 30, 2009, which represented an FFO pay-out ratio of 74.0%.

### Adjusted Funds From Operations

AFFO is a non-GAAP financial measure used by most Canadian real estate investment trusts and should not be considered as an alternative to net income, cash flow from operations or any other measure prescribed under GAAP. AFFO does not have any standardized meaning prescribed by GAAP. As computed by us, AFFO may differ from similar computations reported by other Canadian real estate investment trusts and, accordingly, may not be comparable to similar computations reported by such organizations. Management considers AFFO to be a useful measure of cash available for distributions.

The principal advantage of AFFO is that it starts from the standardized definition of FFO and takes account of maintenance capital expenditures and regular leasing expenditures while ignoring the impact of non-cash revenue. Because maintenance capital expenditures and regular leasing expenditures are not incurred evenly throughout a fiscal year, there can be volatility in AFFO on a quarterly basis. The following reconciles net income, as presented in the consolidated financial statements, with AFFO, calculated in accordance with what Management believes to be industry practice.

(In thousands)	Six Months ended June 30, 2010	Six Months ended June 30, 2009
FFO	32,751	27,857
Step-rent adjustments	(180)	(406)
M-T-M acquired leases	(952)	(134)
Leasing expenditures	(3,887)	(2,137)
Maintenance capital expenditures	(1,411)	(278)
<b>AFFO</b>	<b>26,321</b>	<b>24,902</b>

Distributions for the six-month period ended June 30, 2010, represented an AFFO pay-out ratio of 97.8%, as compared to distributions for the six-month period ended June 30, 2009, which represented an AFFO pay-out ratio of 82.7%.

### Net Operating Income

NOI is a non-GAAP financial measure and should not be considered as an alternative to net income, cash flow from operations or any other measure prescribed under GAAP. NOI does not have any standardized meaning prescribed by GAAP. As computed by us, NOI may differ from similar computations reported by other Canadian real estate investment trusts and, accordingly, may not be comparable to similar computations reported by such organizations. Management considers NOI to be a useful measure of performance for rental properties. The following reconciles net rental income, as presented in the consolidated financial statements, to NOI.

(In thousands)	Six Months ended June 30, 2010	Six Months ended June 30, 2009
Revenue from rental properties	90,804	72,707
Rental property operating cost	38,480	29,156
Net rental income	52,354	43,551
M-T-M acquired leases	(952)	(134)
Step-rent adjustments	(180)	(406)
<b>NOI</b>	<b>51,222</b>	<b>43,011</b>

## PART III

### Financial Condition

We finance our operations through three sources of capital: (i) mortgage debt secured by our rental properties, (ii) secured short-term debt financing with a Canadian chartered bank and (iii) equity. As at June 30, 2010, we had mortgage debt of \$605,933, bank indebtedness of \$40,340 and unitholders' equity of \$466,664.

#### **Unitholders' Equity**

As at June 30, 2010, we had a market capitalization of approximately \$767,857 based on a closing unit price of \$19.61 on the Toronto Stock Exchange. As at June 30, 2009, we had a market capitalization of approximately \$462,664 based on a closing unit price of \$14.75 on the Toronto Stock Exchange.

In the six-month period ended June 30, 2010, we issued a total of 115,028 units under our distribution re-investment plan at an average price of \$18.75 per unit for equity contributions of \$2,157. Costs incurred to issue the units were nil. As at August 4, 2010, we had 39,189,656 units issued and outstanding.

We adopted a Unit Option Plan at the time of our IPO. In May of 2004, we adopted a long-term incentive plan ("LTIP") whereby our trustees and officers ("Participants") may from time to time, at the discretion of the trustees and subject to regulatory approval, subscribe for units at a market price established in accordance with the provisions of the LTIP. The price for the units is payable as to 5% upon issuance and as to the balance ("LTIP Loan") over 10 years with interest on the LTIP Loan at an annual rate

established in accordance with the provisions of the LTIP. The units issued pursuant to the LTIP are registered in the name of a Custodian on behalf of the Participants who are the beneficial owners. The units are pledged to us as security for payment of the LTIP Loan, and all distributions paid on the units are forwarded by the Custodian to us and applied first on account of interest on the LTIP Loan and then to reduce the outstanding balance of the LTIP Loan. In May of 2010, we amended the Unit Option Plan and the LTIP to limit the number of units authorized for issuance under the Unit Option Plan, the LTIP or any other equity compensation plan to 8.1% of the issued and outstanding units from time to time. As of August 4, 2010, we had options to purchase 1,620,177 units outstanding, of which 402,495 had vested, and 378,043 units issued under the LTIP.

In March of 2010, we adopted a restricted unit plan (the Restricted Unit Plan”), whereby restricted units (“Restricted Units”) are granted to certain key employees of the Trust, at the discretion of the trustees. The Restricted Units are purchased in the open market. Employees who are granted Restricted Units have the right to vote and to receive distributions from the date of the grant. The Restricted Units vest (in the sense that such Units are not subject to forfeiture) as to one-third on each of the three anniversaries following the date of the grant. Whether vested or not, without the specific authority of the Governance and Compensation Committee, the Restricted Units may not be sold, mortgaged or otherwise disposed of for a period of six years following the date of the grant. The Restricted Unit Plan contains provisions providing for the forfeiture within specified time periods of unvested Restricted Units in the event the employee’s employment is terminated. As of June 30, 2010, we had 55,659 Restricted Units granted under the Restricted Unit Plan.

### **Mortgages Payable**

Mortgages payable as at June 30, 2010, consisted of mortgage debt of \$605,933. The following sets out the maturity schedule of our mortgage debt and the weighted average interest rate on the maturing mortgages.

(In thousands)	Periodic Principal Payments	Balance Due at Maturity	Total Principal	% of Total Principal	WA Interest Rate
2010	8,237	-	8,237	1.4%	0.0%
2011	16,743	19,660	36,403	6.0%	5.9%
2012	16,707	36,805	53,512	8.8%	5.9%
2013	17,390	21,997	39,387	6.5%	6.0%
2014	13,457	161,663	175,120	28.9%	5.5%
Thereafter	29,692	263,582	293,274	48.4%	6.0%
Total	102,226	503,707	605,933	100.0%	

The principal balances due at maturity by type of lender are as follows:

(In thousands)	Direct Mortgage Lender	Conduit Mortgage Lender
2010	-	-
2011	14,505	5,155
2012	24,488	12,317
2013	21,997	-
2014	142,780	18,883
Thereafter	197,368	66,214
Total	401,138	102,569

Interest rates on the mortgage debt are between 2.39% and 8.10% with a weighted average interest rate of 5.9%. The weighted average term of the mortgage debt is 5.3 years. Each individual mortgage loan is secured by a mortgage registered on title of a rental property and by security agreements covering assignment of rents and personal property with respect to such property. The mortgage debt provides the holder with recourse to our assets. We attempt to stagger the maturity of our mortgages and to have mortgages maturing each year to be in a position to upward finance the principal amount of maturing mortgages as needed. Additionally, we attempt to maintain 15 to 20% of our rental properties free from traditional long-term mortgage financing with a view to providing these assets as security for bank credit facilities.

### **Bank Credit Facility**

As at June 30, 2010, we had a \$70,000 revolving credit facility (“Facility”) with a Canadian chartered bank bearing interest at bank prime and maturing on August 31, 2010. The credit facility is secured by a combination of mortgage charges and security agreements on certain of our rental properties. In the six-

month period ended June 30, 2010, the average borrowings under the Facility were \$16,048. As at June 30, 2010, the borrowings under the Facility were \$40,340. In the period, we renewed the Facility for a term of one year with the following modification: from September 1, 2010, the Facility will bear interest at bank prime plus 175 basis points or bankers' acceptance plus 275 basis points.

## Liquidity and Commitments

Net operating income generated from our rental properties is the primary source of liquidity to fund our financing expense, trust expense and distributions to unitholders.

We expect that increased financing on maturing mortgages will provide sufficient cash flow to fund mortgage repayments. We plan to fund anticipated ongoing commitments, obligations, capital expenditures and leasing expenditures by using retained cash flow from operations and availing ourselves of borrowing capacity under the Facility.

The Facility, new mortgage financing and the access to the public equity markets will provide the necessary capital we require for acquisitions. Our acquisition capacity, meaning our ability to use unutilized borrowing capacity while not exceeding the 60% Debt Ratio, is \$383,000.

As at June 30, 2010, we had future commitments as set out below.

(In thousands)	June 30, 2010
Leasing commissions	1,642
Tenant improvements	5,821
Building renovations and maintenance capital expenditures	1,629
Revenue-enhancing capital and leasing expenditure	491
Expenses	224
Conditional acquisitions	14,500
<b>Total</b>	<b>24,307</b>

## PART IV

### Summary Information and Performance for the Quarter Ended June 30, 2010

The following sets out summary information and financial results for the quarter ended June 30, 2010, and the comparable quarter and the change between the two.

(In thousands except for per unit and % amounts)	Q2 2010	Q2 2009	Change	%Change
Revenue from rental properties	43,780	35,732	8,048	22.5%
Rental property operating cost	18,150	13,912	4,238	30.5%
Net rental income	25,630	21,820	3,810	17.5%
Real estate service income	59	70	(11)	(15.7%)
Financing expense				
Interest	8,248	6,884	1,364	19.8%
Amortization - Mortgage premium	(4)	(6)	2	(33.3%)
Amortization - Deferred financing cost	219	157	62	39.5%
Amortization				
Rental properties	5,600	4,417	1,183	26.8%
Deferred leasing cost and tenant improvements	792	755	37	4.9%
Origination cost and acquired tenant relationships	4,882	4,806	76	1.6%
Acquired contracts and customer relationships	24	24	-	0.0%
Computer and office equipment	79	71	8	11.3%
Income from operations	5,849	4,782	1,067	22.3%
Trust expense	1,241	832	409	49.2%
Net income	4,608	3,950	658	16.7%
Amortization				
Rental properties	5,600	4,417	1,183	26.8%
Mortgage premium	(4)	(6)	2	(33.3%)
Acquired leases	1,412	1,739	(327)	(18.8%)
M-T-M acquired leases	(663)	(252)	(411)	163.1%
Acquired tenant relationships	3,470	3,067	403	13.1%
Acquired contracts and customer relationships	24	24	-	0.0%
Step-rent adjustments	(142)	(191)	49	(25.7%)
Compensation expenses, LTIP and stock options	436	55	381	692.7%
<b>DI</b>	<b>14,741</b>	<b>12,803</b>	<b>1,938</b>	<b>15.1%</b>

(In thousands except for per unit and % amounts)	Q2 2010	Q2 2009	Change	%Change
Weighted average units outstanding (basic)	38,738	30,966	7,772	25.1%
Weighted average units outstanding (diluted)	39,204	31,370	7,834	25.0%
Distributions	12,877	10,308	2,569	24.9%
DI per unit (basic)	\$0.38	\$0.41	(\$0.03)	(7.3%)
DI per unit (diluted)	\$0.38	\$0.41	(\$0.03)	(7.3%)
DI pay-out ratio	87.4%	80.5%	6.9%	
FFO	15,882	13,928	1,954	14.0%
FFO per unit (basic)	\$0.41	\$0.45	(\$0.04)	(8.9%)
FFO per unit (diluted)	\$0.41	\$0.44	(\$0.03)	(6.8%)
FFO pay-out ratio	81.1%	74.0%	7.1%	
AFFO	11,641	12,632	(991)	(7.8%)
AFFO per unit (basic)	\$0.30	\$0.41	(\$0.11)	(26.8%)
AFFO per unit (diluted)	\$0.30	\$0.40	(\$0.10)	(25.0%)
AFFO pay-out ratio	110.6%	81.6%	29.0%	
NOI	24,825	21,377	3,448	16.1%
Same-asset net operating income	19,044	20,972	(1,928)	(9.2%)
Total assets	1,158,995	942,806	216,189	22.9%
Total debt (excludes premium on assumed debt)	646,273	531,857	114,416	21.5%
Debt Ratio	48.0%	49.3%	(1.3%)	
Total GLA (s.f., excluding PUD)	5,816	5,451	365	6.7%
Leased GLA (s.f., excluding PUD)	5,524	5,246	278	5.3%
Leased GLA (% total GLA)	95.0%	96.3%	(1.3%)	

### **Net Income**

Net income for the quarter ended June 30, 2010 was \$4,608, as compared to \$3,950 in the quarter ended June 30, 2009. Net income per unit (diluted) for the quarter was \$0.12, as compared to \$0.13 in the comparable quarter.

DI for the quarter ended June 30, 2010 increased by 15.1% to \$14,741 from \$12,803 for the quarter ended June 30, 2009. DI per unit (diluted) for the quarter was \$0.38, as compared to \$0.41 in the comparable quarter.

### **Net Rental Income**

Net rental income for the quarter ended June 30, 2010 increased by 17.5% to \$25,630 from \$21,820 in the quarter ended June 30, 2009 as follows: (i) \$2,584 decrease in same-asset net rental income from properties owned for the entire quarter and the entire comparable quarter (which includes the quarter-over-quarter change in step-rent adjustments and mark-to-market rent adjustments); and (ii) \$6,394 due to net rental income from properties not owned for the entire quarter and the entire comparable quarter.

Net rental income per occupied square foot for the quarter ended June 30, 2010 was \$18.56 annualized, as compared to \$16.64 annualized in the comparable quarter.

### **Real Estate Service Income**

The Property Manager provides real estate services to third-party property owners. Real estate service income for the quarter ended June 30, 2010 was \$59, as compared to \$70 in the quarter ended June 30, 2009.

### **Financing Expense**

Financing expense includes interest cost on mortgage debt and other credit facilities and the amortization of the premiums and discounts on assumed mortgages. For the quarter ended June 30, 2010, interest increased by 19.8% to \$8,248 from \$6,884 in the quarter ended June 30, 2009, due to the increase in financing expense associated with additional properties acquired in 2009 and 2010.

### **Amortization**

We record amortization on our buildings on a straight-line basis over their expected life. Amortization recorded on buildings for the quarter ended June 30, 2010 increased by 26.8% to \$5,600 from \$4,417 in the quarter ended June 30, 2009.

We record amortization of deferred leasing cost, tenant improvements and the assigned fair value of the origination cost and tenant relationships for in-place leases acquired on acquisition of a rental property on a straight-line basis over the term of the corresponding lease.

### **Trust Expense**

Trust expense includes cost not directly attributable to rental property, such as officers' compensation, trustees' fees, professional fees for legal and audit services, trustees' and officers' insurance premiums and general administrative expenses. Trust expense for the quarter ended June 30, 2010, increased by a 49.2% to \$1,241 from \$832 in the quarter ended June 30, 2009, due to costs associated with the implementation of IFRS and executive compensation.

## **PART V**

### **Summary Quarterly Information and Performance**

The following sets out summary information and financial results for the eight most recently completed fiscal quarters.

(In thousands except for per unit and % amounts)	<b>Q2 2010</b>	<b>Q1 2010</b>	<b>Q4 2009</b>	<b>Q3 2009</b>	<b>Q2 2009</b>	<b>Q1 2009</b>	<b>Q4 2008</b>	<b>Q3 2008</b>
Revenue from rental properties	43,780	47,024	43,667	35,851	35,732	36,975	35,202	33,795
Rental property operating cost	18,150	20,300	18,461	14,517	13,912	15,244	14,332	12,776
Net rental income	25,630	26,724	25,206	21,334	21,820	21,731	20,870	21,019
Real estate service income	59	57	58	70	70	65	73	95
Financing expense	8,463	8,370	7,838	7,046	6,884	6,855	7,018	6,745
Amortization	11,377	12,391	11,513	9,795	10,073	10,144	9,723	9,831
Income from operations	5,849	6,020	5,913	4,563	4,782	4,797	4,202	4,538
Trust expense	1,241	1,439	1,229	774	832	921	906	828
Net income (loss)	4,608	4,581	4,684	3,789	3,950	3,876	3,296	3,710
Amortization								
Rental properties	5,600	5,546	5,187	4,462	4,417	4,381	4,284	4,221
Mortgage premium	(4)	(3)	(4)	(4)	(6)	(8)	(5)	(76)
Acquired leases	1,412	1,797	1,674	1,539	1,739	1,586	1,644	1,647
M-T-M acquired leases	(663)	(289)	(220)	263	(252)	118	195	265
Acquired tenant relationships	3,470	4,124	3,904	2,846	3,067	3,018	3,110	3,282
Acquired contracts and customer relationships	24	24	24	24	24	24	24	24
Step-rent adjustments	(142)	(38)	(312)	123	(191)	(215)	(341)	(244)
Unit based compensation expense	436	119	261	56	55	56	123	122
DI	14,741	15,861	15,198	13,098	12,803	12,836	12,330	12,951
Weighted average units (basic)	38,738	38,681	38,547	30,993	30,966	30,914	30,796	30,654
Weighted average units (diluted)	39,204	39,119	38,975	31,411	31,370	31,302	31,184	31,042
Distributions	12,877	12,858	12,839	10,320	10,308	10,296	10,255	10,218
DI per unit (basic)	\$0.38	\$0.41	\$0.39	\$0.42	\$0.41	\$0.42	\$0.40	\$0.42
DI per unit (diluted)	\$0.38	\$0.41	\$0.39	\$0.42	\$0.41	\$0.41	\$0.40	\$0.42
DI pay-out ratio	87.4%	81.1%	84.5%	78.8%	80.5%	80.2%	83.2%	78.9%
FFO	15,822	16,869	16,092	13,480	13,928	13,929	13,023	13,449
FFO per unit (basic)	\$0.41	\$0.44	\$0.42	\$0.43	\$0.45	\$0.45	\$0.42	\$0.44
FFO per unit (diluted)	\$0.41	\$0.43	\$0.41	\$0.43	\$0.44	\$0.44	\$0.42	\$0.43
FFO pay-out ratio	81.1%	76.2%	79.8%	76.6%	74.0%	73.9%	78.7%	76.0%
AFFO	11,641	14,680	13,261	12,401	12,632	12,270	10,603	11,600
AFFO per unit (basic)	\$0.30	\$0.38	\$0.34	\$0.40	\$0.41	\$0.40	\$0.34	\$0.38

(In thousands except for per unit and % amounts)	Q2 2010	Q1 2010	Q4 2009	Q3 2009	Q2 2009	Q1 2009	Q4 2008	Q3 2008
AFFO per unit (diluted)	\$0.30	\$0.38	\$0.34	\$0.40	\$0.40	\$0.39	\$0.34	\$0.37
AFFO pay-out ratio	110.6%	87.6%	96.8%	83.2%	81.6%	83.9%	96.7%	88.1%
NOI	24,825	26,397	24,674	21,720	21,377	21,634	20,724	21,040
Net income per unit (basic)	\$0.12	\$0.12	\$0.12	\$0.12	\$0.13	\$0.13	\$0.11	\$0.12
Net income per unit (diluted)	\$0.12	\$0.12	\$0.12	\$0.12	\$0.13	\$0.12	\$0.11	\$0.12
Total assets	1,158,995	1,152,390	1,155,158	937,342	942,806	945,985	949,385	956,344
Total debt	646,273	620,013	614,298	533,348	531,857	527,174	526,478	527,879
Debt Ratio	48.0%	47.0%	47.0%	49.4%	49.3%	49.3%	49.4%	49.7%
Total GLA (excluding PUD)	5,816	5,665	5,675	5,452	5,451	5,335	5,350	5,236
Leased GLA (excluding PUD)	5,524	5,379	5,448	5,247	5,246	5,183	5,204	5,095
Leased Area (%GLA)	95.0%	95.0%	96.0%	96.2%	96.3%	97.2%	97.3%	97.3%

Factors that cause variation from quarter to quarter include but are not limited to our Debt Ratio, the extent to which we have cash that has not been deployed, the extent to which we have invested capital in PUDs, our same-asset NOI, our rate of property acquisition, our regular leasing expenditures and our regular maintenance capital expenditures.

## PART VI

### Critical Accounting Estimates

The significant accounting policies used in preparing our consolidated financial statements are described in Note 3 to our consolidated financial statements for the six-month period and quarter ended June 30, 2010, and for the year ended March 31, 2009. The following is a discussion of Management's estimates that are most important to the presentation of our results of operations and financial condition and are most subjective as a result of matters that are inherently uncertain.

#### ***Fair Value of Assumed Mortgages Payable and Fair Value of Mortgages Payable***

GAAP requires that the mortgages payable assumed on acquisition of properties be recorded at fair value. The fair value of the mortgages payable has been determined by discounting the cash flows of these financial obligations using market rates for debt of similar terms and credit risks. Market rates for debt are based on the yield of Canadian government bonds with similar maturity dates plus a credit spread based on Management's experience in obtaining financing and the current market conditions.

#### ***Impairment of Assets***

We are required to write down to fair value any long-lived assets that are determined to have been permanently impaired. Our long-lived assets consist of rental properties. Our policy is to assess any potential impairment by making a comparison of the current and projected operating cash flow of a rental property over its remaining useful life, on an un-discounted basis, to the carrying amount of the rental property. If such carrying amount was in excess of the projected operating cash flow of the rental property, impairment in value would be recognized to adjust the carrying amount to its estimated fair market value. Current operating cash flows are based on leases in place and projected operating cash flows are based on Management's estimates of future rental rates. Prior to acquiring a rental property, we commission an appraisal and conduct due-diligence to satisfy ourselves that the acquisition price is representative of fair market value.

#### ***Amortization***

A significant portion of the purchase price of rental properties is allocated to buildings. The amortization recorded on buildings is based on the straight-line basis over their expected useful life. The allocation of purchase price to buildings and the estimated useful life are based on Management's estimates and, if these estimates prove incorrect, the amortization will not be appropriately recorded.

#### ***Mark-to-Market Rent Adjustment, Cité Multimédia***

We completed the acquisition of Cité Multimédia on April 18, 2007, with an effective date of April 1, 2007. At the time of acquisition, based on data compiled by an independent real estate appraiser, Management estimated that the average in-place rental rates for the tenants at Cité Multimédia exceeded current

market rental rates by approximately 9%. Accordingly, our financial statements for the six-month period and quarter ended June 30, 2010, recognize a \$1,655 net mark-to-market rent adjustment in respect of Cité Multimédia. Our net income was affected by this mark-to-market rent adjustment. Our DI and AFFO were not affected, as we add non-cash items back in calculating DI and AFFO. Our FFO was affected, as we do not add mark-to-market rent adjustments back in calculating FFO.

## **PART VII**

### **Future Changes in Accounting Policies--Adoption of International Financial Reporting Standards ("IFRS")**

The Canadian Accounting Standards Board has confirmed that the transition date to IFRS from current GAAP will be January 1, 2011. We will issue consolidated financial statements in accordance with IFRS commencing in the first quarter ended March 31, 2011, with comparative information. We commenced a conversion project in 2008, which consists of the following: (i) training and education; (ii) an assessment of the impact of IFRS on our financial statements, information-technology data systems, disclosure and control procedures and internal control processes; (iii) design and implementation of systems and process changes; and (iv) post-implementation review.

#### ***Training and Education***

Several of our key employees involved in the IFRS conversion have completed training in 2009 and specific training for all affected staff continues and will be completed in the third quarter of 2010. Internal accounting policy and procedures manuals will be updated in the fourth quarter of 2010.

#### ***Assessment of Impact***

We have completed an assessment and have identified differences between current GAAP and IFRS that will impact on our financial statements. We continue to assess the implications of these differences and evaluate the accounting policy alternatives and the impact on our financial statements. The development of a real estate valuations strategy and process is almost complete. We have engaged a third-party appraiser to assist in determining the fair value of investment properties as at January 1, 2010, the results of which have not been finalized. The appraiser is retained to assist with determining fair value for subsequent reporting periods. Required changes to information technology data systems are being identified as the conversion plan progresses, and we expect changes will be impacted by accounting policies related to investment properties and the need for capturing information under a dual reporting requirements. We continue to assess exiting disclosure and control procedures and internal control processes and will design and implement any necessary changes throughout 2010 to address the changes to existing accounting policies and the implementation of our real estate valuations process.

#### ***Design and Implementation***

The conclusions and recommendations derived from the assessment of the impact of IFRS will be integrated into the design and implementation of systems and process changes throughout 2010 in order for us to compile IFRS compliant financial statements. The necessary changes to our business processes and training programs will be developed concurrently, with post-implementation review to assess and test systems, processes, financial statements, notes, policies, and internal controls throughout 2010 for IFRS conversion.

#### ***Summary of Key Difference***

We have progressed through the conversion project as planned and implementation continues to adapt due to changes in IFRS and from the completion of more detailed analysis. The comparison of current GAAP and IFRS and any conclusions discussed below are preliminary and are subject to changes based on further analysis and interpretations by Management. IFRS is based on a conceptual framework similar to current GAAP, however significant differences exist with respect to recognition, measurement and disclosure. The significant differences that are expected to have an impact on our consolidated financial statements include the following:

##### **1. Investment Property**

IFRS defines investment property as a property (land or a building) held to earn rental income, capital appreciation, or both. A key characteristic of an investment property is that it generates cash flows largely independent of the other assets held by an entity. All of our income properties and Properties Under Development will qualify as investment property under IFRS. Under IFRS we need to choose either the

cost model or the fair value model to account for our investment properties. Under the fair value model, investment properties will be carried on the consolidated balance sheet at their fair values and changes in fair value during each period will be recorded in the consolidated statement of income. Amortization related to investment properties is not recognized under the fair value model. The cost model is generally consistent with current GAAP, whereby investment properties are carried on the consolidated balance sheet at its cost less any accumulated amortization and any accumulated impairment losses. Under the fair value model, investment properties will be carried on the consolidated balance sheet at their fair values and changes in fair value during each period will be recorded in the consolidated statement of income. Amortization related to investment properties is not recognized under the fair value model.

## 2. Properties Under Development

Properties Under Development are considered investment properties. Under IFRS, operating revenues and expenses cannot be capitalized and subject to meeting certain tests, capitalization of interest costs directly attributable to a property under development is required.

## 3. Impairment

Under current GAAP, impairment is recognized if the future cash flows of the investment property are lower than its carrying value. Under the cost model for IFRS, an entity is required to recognize an impairment charge if the recoverable amount, determined as the higher of the estimated fair value less cost to sell or value-in-use, is less than its carrying value. Under IFRS, recognition of impairments would likely be more frequent. IFRS allows impairment losses to be reversed if there is an increase in value. The reversal of impairment is not permitted under Canadian GAAP. Impairment is not applicable to the fair value model.

## 4. Leases

Current GAAP and IFRS both require that tenant allowances be capitalized and amortize as a reduction to rental revenue over the term of the leases. Currently, we capitalized and amortize tenant improvements and certain other leasing costs through amortization expense. Under IFRS, portions of such costs are likely to be considered leasing incentives and will be amortized as a reduction of the rental revenue over the term of the lease.

## 5. Business Combinations

Both IFRS and current GAAP require the acquisition method of accounting for all business combinations, however significant differences exist between the two standards. Current GAAP allows the capitalization of transaction costs, whereas IFRS does for an asset purchase but not for a business combination, in which case the transaction costs are expensed as incurred. Transaction cost typically includes land transfer taxes, appraisal fees and due-diligence expenditures.

## 6. Equity – Trust Units

Under current GAAP trust units are presented as equity on our Consolidated Balance Sheet. Based on our understanding of IFRS, our trust units met the definition of a liability as under our Declaration of Trust we had a mandatory requirement to distribute taxable income. Many Canadian REITs have modified their Declaration of Trust to eliminate the mandatory distribution and leave distributions to the discretion of the Trustees so that trust units can be presented as equity. At our Annual and Special Meeting on May 11, 2010, Unitholders approved the elimination of mandatory distributions.

## 7. Income Taxes

Under the current IFRS income tax standard we may be required to recognize deferred income taxes, notwithstanding we meet the REIT Exception under the SIFT rules.

## **PART VIII**

### **Related Party Transactions**

Allied Canadian Development Corporation (“ACDC”) is a company controlled by the President and Chief Executive Officer of the REIT and in which the Executive Vice President of the REIT has an interest. At the time of our IPO, a subsidiary of ACDC leased 29,102 square feet of office space from us pursuant to a lease expiring on September 30, 2010. Effective July 1, 2005, we entered into a direct lease of this space with Loblaws Properties for a term ending October 31, 2010, on the condition that the original

indemnity of ACDC protecting us from any revenue shortfall (on a cash basis) from the original lease remain in full force and effect.

We have an option agreement (“Option Agreement”) with ACDC, pursuant to which it must offer to sell to us at fair market value all developed or redeveloped office properties upon substantial completion. Seven of the properties in our portfolio were acquired pursuant to the Option Agreement. ACDC has no properties under development or redevelopment at this time. While the Option Agreement permits it to engage in development and redevelopment activity on an ongoing basis, ACDC is not currently pursuing office development or redevelopment opportunities and does not expect to do so in the foreseeable future.

## PART IX

### Risk and Uncertainties

There are certain risk factors inherent in the investment and ownership of real estate. Real estate investments are capital intensive, and success from real estate investments depends upon maintaining occupancy levels and rental income flows to generate acceptable returns. These success factors are dependent on general economic conditions and local real estate markets, demand for leased premises and competition from other available properties. The general economic conditions continue to be unstable in the past year. While this instability has not yet had a commensurate impact on the demand for leased premises in our target markets, it is reasonable to expect that it will going forward and that it will heighten the financing and interest rate risk, credit risk, lease roll-over risk and development risk outlined below.

Our portfolio is focused on a particular asset class in five metropolitan real estate markets in Canada. This focus enables Management to capitalize on certain economies of scale and competitive advantages that would not otherwise be available.

#### **Financing and Interest Rate Risk**

We are subject to risk associated with debt financing. The availability of debt to re-finance existing and maturing loans and the cost of servicing such debt will influence our success. In order to minimize risk associated with debt financing, we strive to re-finance maturing loans with long-term fixed-rate debt and to stagger the maturities over time.

Interest rates on our mortgage debt are between 2.39% and 8.10% with a weighted average interest rate of 5.9%. The weighted average term of our mortgage debt is 5.3 years.

#### **Credit Risk**

We are subject to credit risk. Credit risk arises from the possibility that tenants may not be able to fulfill their lease obligations. We strive to mitigate this risk by maintaining a diversified tenant-mix and limiting exposure to any single tenant.

The following sets out our tenant-mix on the basis of percentage of rental revenue for the period ended June 30, 2010:

Category	% of Rental Revenue Six-Month Period Ended June 30, 2010
Business service and professional	22.4%
Telecommunications and information technology	37.7%
Retail (head office and storefront)	12.2%
Media and entertainment	13.9%
Financial services	4.7%
Government	1.2%
Other	7.9%

The following sets out the percentage of rental revenue from our top-10 tenants by rental revenue for the period ended June 30, 2010.

Tenant	% of Rental Revenue Six-Month Period Ended June 30, 2010
Switch and Data Toronto	5.1%
C.G.I.	4.1%
Ubisoft Divertissement	3.3%
MTS Allstream	2.9%

Visa Desjardins	2.8%
Peer 1 Network Enterprises	1.9%
Cossette	1.9%
Telehouse Centre Canada	1.9%
Autodesk Canada	1.8%
SAP Labs Inc.	1.7%

### Lease Roll-Over Risk

We are subject to lease roll-over risk. Lease roll-over risk arises from the possibility that we may experience difficulty renewing or replacing tenants occupying space covered by leases that mature. We strive to stagger our lease maturity schedule so that we are not faced with a disproportionately large level of lease maturity in a given year.

95.0% of the GLA in our portfolio was leased as at June 30, 2010 (not including Properties Under Development). The weighted average term to maturity of our leases at that time was 3.8 years. The following sets out, as of today's date, the total GLA of the leases that mature to the end of 2014, assuming tenants do not exercise renewal options, the percentage of total GLA represented by the maturing leases, the weighted average in-place net rental rate on the maturing leases and the weighted average market net rental rate on the space covered by the maturing leases. The weighted average market net rental rate is based on Management's current estimates and is supported in part by independent appraisals of certain of the relevant properties. There can be no assurance that Management's current estimates are accurate or that they will not change with the passage of time.

Year Ended	Square Feet	% of Total GLA	WA Rental Rate	WA Market Rate
December 31, 2010	720,607	12.4%	\$18.36	\$17.76
December 31, 2011	883,233	15.2%	\$19.33	\$19.98
December 31, 2012	870,239	15.0%	\$18.69	\$17.50
December 31, 2013	942,374	16.2%	\$18.58	\$17.50
December 31, 2014	270,254	4.6%	\$21.62	\$19.07

The following sets out lease maturity information for each of our five target markets, with our Toronto and Kitchener target markets being combined.

#### 1. Toronto and Kitchener

Year Ended	Square Feet	% of Total GLA	WA Rental Rate	WA Market Rate
December 31, 2010	213,077	3.7%	\$20.89	\$23.91
December 31, 2011	452,534	7.8%	\$23.55	\$26.56
December 31, 2012	460,259	7.9%	\$20.58	\$20.21
December 31, 2013	472,027	8.1%	\$23.98	\$24.67
December 31, 2014	185,126	3.2%	\$26.33	\$24.37

#### 2. Montréal

Year Ended	Square Feet	% of Total GLA	WA Rental Rate	WA Market Rate
December 31, 2010	450,663	7.7%	\$18.50	\$16.11
December 31, 2011	358,302	6.2%	\$16.11	\$14.05
December 31, 2012	357,413	6.1%	\$17.46	\$15.33
December 31, 2013	398,579	6.9%	\$13.76	\$15.06
December 31, 2014	48,715	0.8%	\$9.35	\$7.23

#### 3. Winnipeg

Year Ended	Square Feet	% of Total GLA	WA Rental Rate	WA Market Rate
December 31, 2010	47,213	0.8%	\$7.56	\$7.61
December 31, 2011	61,226	1.1%	\$7.79	\$7.82
December 31, 2012	26,126	0.4%	\$7.51	\$7.33
December 31, 2013	53,328	0.9%	\$8.23	\$7.63
December 31, 2014	20,395	0.4%	\$7.24	\$5.73

#### 4. Québec City

Year Ended	Square Feet	% of Total GLA	WA Rental Rate	WA Market Rate
December 31, 2010	9,654	0.2%	\$8.52	\$9.00
December 31, 2011	11,171	0.2%	\$15.17	\$9.87
December 31, 2012	26,441	0.5%	\$13.33	\$9.57
December 31, 2013	18,440	0.3%	\$14.44	\$8.74
December 31, 2014	16,018	0.3%	\$22.79	\$10.80

In evaluating our lease roll-over risk, it is informative to determine our sensitivity to a decline in occupancy. For every full-year decline of 100 basis points in occupancy at our average rental rate per

square foot, our annual AFFO would decline by approximately \$1,900 (approximately five cents per unit). The decline in AFFO per unit would be more pronounced if the decline in occupancy involved space leased above our average rental rate per square foot and less pronounced if the decline in occupancy involved space leased below our average rental rate per square foot.

### ***Environmental Risk***

As an owner of real property, we are subject to various federal, provincial and municipal laws relating to environmental matters. Such laws provide that we could be liable for the costs of removal of certain hazardous substances and remediation of certain hazardous locations. The failure to remove or remediate such substances or locations, if any, could adversely affect our ability to sell such real estate or to borrow using such real estate as collateral and could potentially also result in claims against us. We are not aware of any material non-compliance with environmental laws at any of the properties in our portfolio. We are also not aware of any pending or threatened investigations or actions by environmental regulatory authorities in connection with any of the properties in our portfolio or any pending or threatened claims relating to environmental conditions at the properties in our portfolio.

### ***Development Risk***

As an owner of Properties Under Development, we are subject to development risks, such as construction delays, cost over-runs and the failure of tenants to take occupancy and pay rent in accordance with lease arrangements. In connection with all Properties Under Development, we incur development costs prior to (and in anticipation of) achieving a stabilized level of rental revenue. In the case of the development of ancillary or surplus land, these risks are managed by not commencing construction until a satisfactory level of pre-leasing is achieved. Overall, these risks are managed by ensuring that Properties Under Development do not represent a large component of our GBV. As at June 30, 2010, the cost of Properties Under Development was equivalent to 3.7% of our GBV.

### ***Taxation Risk***

On June 22, 2007, rules changing the manner in which trusts are taxed were proclaimed into force. Trusts that meet the REIT exemption are not subject to these rules. The determination as to whether we qualify for the REIT exemption in a particular taxation year can only be made with certainty at the end of that taxation year. While there can be no assurance in this regard, due to uncertainty surrounding the interpretation of the relevant provisions of the REIT exemption, we expect that we will qualify for the REIT exemption in 2010 and beyond.

## **PART X**

### **Disclosure Controls and Internal Controls**

Management maintains information systems, procedures and controls designed reasonably to ensure that publicly discussed information is complete, reliable and timely. The Chief Executive Officer and Chief Financial Officer have designed disclosure controls and procedures to provide reasonable assurance that material information about our business is made known to them in a timely way. They have also designed 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.

There was no change in the design of internal controls over financial reporting in the second quarter of 2010 that has materially affected, or is reasonably likely to materially affect, our internal controls over financial reporting.

It should be noted that a control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance of control issues, including instances of fraud, if any, have been detected. These inherent limitations include, among other items: (i) that management's assumptions and judgments could ultimately prove to be incorrect under varying conditions and circumstances; (ii) the impact of any undetected errors; and (iii) that controls may be circumvented by the unauthorized acts of individuals, by collusion of two or more people, or by management override.

## PART XI

### Subsequent Events

On July 29, 2010, we received a commitment from a Canadian chartered bank for a first mortgage on 645 Wellington Avenue in Montréal in the principal amount of \$6,900, having a term of three years, bearing interest at approximately 3.8% and payable in blended instalments of principal and interest based on a 25-year amortization.

On August 4, 2010, we announced the acquisition of the Lougheed Building in Calgary for \$31,000. Located at 604, 1<sup>st</sup> Street SW, the property is comprised of 86,478 square feet of GLA and is fully leased with a weighted average lease term of over eight years.

On August 4, 2010, we announced the acquisition of 49 Front Street East and 252-264 Front Street East in Toronto for \$19,000. Located on the south side of Front Street and one building east of our Beardmore and Perkins/Dixon buildings, 49 Front is comprised of 19,936 square feet of GLA and is fully leased. Located on the north side of Adelaide, just east of Jarvis Street, 252-264 Adelaide is comprised of 50,217 square feet of GLA and is fully leased.

PART XII

Property Table

June 30, 2010 Properties	OFFICE GLA	Retail GLA	Total GLA	% Total GLA	Office Vacant	Retail Vacant	Total Leased	Leased %
555 College	40,913	19,145	60,058		-	-	60,058	100.0%
860 Richmond W	24,199	-	24,199		-	-	24,199	100.0%
The Castle	106,393	34,323	140,716		-	-	140,716	100.0%
<b>King West</b>	<b>171,505</b>	<b>53,468</b>	<b>224,973</b>	<b>3.9%</b>	-	-	<b>224,973</b>	<b>100.0%</b>
141 Bathurst (+ land)	10,558	-	10,558		5,105	-	5,453	51.6%
183 Bathurst	24,879	-	24,879		-	-	24,879	100.0%
420 Wellington W	33,813	3,137	36,950		-	-	36,950	100.0%
425 Adelaide W	74,434	4,104	78,538		1,669	-	76,869	97.9%
425-439 King W	75,333	17,297	92,630		-	-	92,630	100.0%
441-443 King W	6,820	3,065	9,885		-	-	9,885	100.0%
445-455 King W	27,640	23,048	50,688		5,250	-	45,438	89.6%
468 King W	65,027	-	65,027		-	-	65,027	100.0%
469 King W	64,334	11,250	75,584		-	-	75,584	100.0%
489 King W	15,621	10,650	26,271		-	-	26,271	100.0%
495 King W	10,698	-	10,698		-	-	10,698	100.0%
499 King W	-	8,400	8,400		-	-	8,400	100.0%
500-522 King W	94,892	34,238	129,130		-	-	129,130	100.0%
579 Richmond W	29,043	-	29,043		-	-	29,043	100.0%
602-606 King W	39,727	24,320	64,047		-	-	64,047	100.0%
662 King W	30,774	2,126	32,900		-	-	32,900	100.0%
96 Spadina	80,679	9,361	90,040		18,047	-	71,993	91.7%
King-Brant Parking	-	-	0		-	-	-	0.0%
<b>King West Central</b>	<b>684,272</b>	<b>150,996</b>	<b>835,268</b>	<b>14.4%</b>	<b>30,071</b>	-	<b>805,197</b>	<b>96.4%</b>
116 Simcoe	15,389	-	15,389		-	-	15,389	100.0%
151-20 York	305,676	22,658	328,334		-	-	328,334	100.0%
179 John St	67,331	-	67,331		3,609	-	63,722	94.6%
185 Spadina	55,814	-	55,814		-	-	55,814	100.0%
200 Adelaide W	28,024	-	28,024		-	-	28,024	100.0%
208-210 Adelaide W	12,422	-	12,422		2,313	-	10,109	81.4%
217-225 Richmond W	35,393	21,200	56,593		-	-	56,593	100.0%
257 Adelaide W	46,914	-	46,914		13,760	-	33,154	70.7%
312 Adelaide W	66,043	5,665	71,708		-	-	71,708	100.0%
331-333 Adelaide W	20,503	3,210	23,713		-	-	23,713	100.0%
358-360 Adelaide W	54,250	-	54,250		-	-	54,250	100.0%
364 Richmond W	22,956	17,300	40,256		-	-	40,256	100.0%
388 King W	32,603	11,765	44,368		12,668	-	31,700	71.4%
375-381 Queen W	23,641	11,088	34,729		-	-	34,729	100.0%
82 Peter	38,811	8,287	47,098		7,885	-	39,213	83.3%
99 Spadina	39,327	11,392	50,719		3,637	-	47,082	92.8%
<b>Entertainment District</b>	<b>865,097</b>	<b>112,565</b>	<b>977,662</b>	<b>16.8%</b>	<b>43,872</b>	-	<b>933,790</b>	<b>95.5%</b>
67 Richmond W	44,702	5,804	50,506		-	-	50,506	100.0%
193 Yonge	34,836	16,318	51,154		-	-	51,154	100.0%
<b>Downtown</b>	<b>79,538</b>	<b>22,122</b>	<b>101,660</b>	<b>1.7%</b>	-	-	<b>101,660</b>	<b>100.0%</b>
106 Front E	24,386	10,109	34,495		-	-	34,495	100.0%
35-39 Front E	30,812	17,850	48,662		-	-	48,662	100.0%
36-40 Wellington E	12,630	11,550	24,180		-	-	24,180	100.0%
41-45 Front E	20,024	19,811	39,835		-	-	39,835	100.0%
45-55 Colborne	27,815	12,526	40,341		-	-	40,341	100.0%
50 Wellington E	21,937	11,049	32,986		-	-	32,986	100.0%
<b>St. Lawrence Market</b>	<b>137,604</b>	<b>82,895</b>	<b>220,499</b>	<b>3.8%</b>	-	-	<b>220,499</b>	<b>100.0%</b>
145 Berkeley	8,124	2,687	10,811		2,058	-	8,753	81.0%
204-214 King St E	128,970	5,460	134,430		-	-	134,430	100.0%
230 Richmond E	73,667	-	73,667		-	-	73,667	100.0%
489 Queen E	25,242	-	25,242		-	-	25,242	100.0%
70 Richmond St E	34,414	-	34,414		-	-	34,414	100.0%
Dominion Square	65,339	45,622	110,961		15,621	2,204	93,136	83.9%
Queen Richmond Centre	155,968	64,593	220,561		11,555	5,255	203,751	91.0%
QRC South	36,783	-	36,783		10,059	-	26,724	72.7%
<b>Queen Richmond</b>	<b>528,507</b>	<b>118,362</b>	<b>646,869</b>	<b>11.1%</b>	<b>39,293</b>	<b>7,459</b>	<b>600,117</b>	<b>92.8%</b>
<b>Total Toronto</b>	<b>2,466,523</b>	<b>540,408</b>	<b>3,006,931</b>	<b>51.7%</b>	<b>113,236</b>	<b>7,459</b>	<b>2,886,236</b>	<b>96.0%</b>

Properties	Office GLA	Retail GLA	Total GLA	% Total GLA	Office Vacant	Retail Vacant	Total Leased	Leased %
3575 Saint-Laurent	168,793	17,464	186,257		8,901	-	177,356	94.4%
400 Atlantic	86,284	-	86,284		8,727	-	77,557	88.0%
425 Viger W (+ land)	205,193	820	206,013		-	-	206,013	100.0%
4446 Saint-Laurent	74,961	7,667	82,628		18,057	-	64,571	78.1%
5505 Saint-Laurent	252,452	2,524	254,976		-	-	254,976	100.0%
451-481 Saint Catherine	22,222	8,434	30,656		-	-	30,656	100.0%
6300 Avenue du Parc	215,703	950	216,653		50,202	-	166,451	75.0%
645 Wellington St	123,894	-	123,894		8,226	-	115,668	93.4%
111 Duke St: Phase IV	374,817	-	374,817		-	-	374,817	100.0%
50 Queen St: Phase I	28,799	-	28,799		2,805	-	25,994	90.3%
700 Wellington St: Phased V	128,229	1,925	130,154		-	-	130,154	100.0%
75 Queen St: Phase VI & VII	249,450	2,128	251,578		11,123	-	240,455	95.6%
80 Queen St: Phase II	70,256	-	70,256		15,205	-	55,051	78.4%
87 Prince St: Phase III	106,617	1,065	107,682		-	-	107,682	100.0%
<b>Total Montréal</b>	<b>2,107,670</b>	<b>42,977</b>	<b>2,150,647</b>	<b>37.0%</b>	<b>123,246</b>	<b>-</b>	<b>2,027,401</b>	<b>94.3%</b>
115 Bannatyne	34,587	4,029	38,616		-	-	38,616	100.0%
138 Portage East	39,465	-	39,465		9,511	-	29,954	75.9%
165 Garry	9,000	5,800	14,800		1,800	-	13,000	87.8%
250 McDermot	34,946	10,040	44,986		2,661	-	42,325	94.1%
309 Hargrave	19,070	1,400	20,470		5,573	-	14,897	72.8%
50-70 Arthur	105,857	15,380	121,237		10,265	-	110,972	91.2%
1500 Notre Dame	109,518	-	109,518		-	-	109,518	100.0%
<b>Total Winnipeg</b>	<b>352,443</b>	<b>36,649</b>	<b>389,092</b>	<b>6.7%</b>	<b>29,810</b>	<b>-</b>	<b>359,282</b>	<b>92.3%</b>
390 Charest	68,413	4,686	73,099		9,536	-	63,563	87.0%
410 Charest	23,637	1,300	24,937		-	-	24,937	100.0%
420 Charest	43,551	13,285	56,836		1,245	-	55,591	97.8%
622 Saint Joseph	3,620	3,300	6,920		645	-	6,275	90.7%
633 Saint Joseph	15,655	6,000	21,655		5,852	-	15,803	73.0%
<b>Total Québec City</b>	<b>154,876</b>	<b>28,571</b>	<b>183,447</b>	<b>3.2%</b>	<b>17,278</b>	<b>-</b>	<b>166,169</b>	<b>90.6%</b>
72 Victoria	87,709	-	87,709		606	-	87,103	99.3%
<b>Total Kitchener-Waterloo</b>	<b>87,709</b>	<b>-</b>	<b>87,709</b>	<b>1.5%</b>	<b>606</b>	<b>-</b>	<b>87,103</b>	<b>99.3%</b>
<b>Total Rental Portfolio</b>	<b>5,169,221</b>	<b>648,605</b>	<b>5,817,826</b>	<b>100.0%</b>	<b>284,176</b>	<b>7,459</b>	<b>5,526,191</b>	<b>95.0%</b>

47 & 47-A Fraser, Toronto	31,772	-	31,772
134 Peter, Toronto	30,151	19,518	49,669
544 King, Toronto	20,000	-	20,000
905 King W-removed	103,105	8,991	112,096
4450 Saint-Laurent, Montréal	-	-	-
<b>Total PUD</b>	<b>185,028</b>	<b>28,509</b>	<b>213,537</b>

**ALLIED PROPERTIES REAL ESTATE INVESTMENT TRUST**  
**CONSOLIDATED FINANCIAL STATEMENTS FOR THE QUARTER ENDED JUNE 30, 2010**

**Consolidated Balance Sheets**  
**(Unaudited)**

(in thousands)	Note	June 30, 2010	December 31, 2009
<b>Assets</b>			
Rental properties	4	\$1,021,786	\$1,017,883
Properties under development		48,812	41,928
Intangibles	5	34,400	43,751
Other assets	6	53,286	50,326
Cash		711	1,270
		<b>\$1,158,995</b>	<b>\$1,155,158</b>
<b>Liabilities</b>			
Mortgages payable	7	\$602,147	\$593,619
Bank indebtedness	7	40,340	16,923
Accounts payable and other liabilities	8	45,387	58,795
Distributions payable		4,307	4,295
		<b>692,181</b>	<b>673,632</b>
<b>Unitholders' Equity</b>	<b>9</b>	<b>466,814</b>	<b>481,526</b>
		<b>\$1,158,995</b>	<b>\$1,155,158</b>

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

"Gordon Cunningham"

Gordon Cunningham  
Trustee

"Michael R. Emory"

Michael R. Emory  
Trustee

**Consolidated Statements of Unitholders' Equity  
(Unaudited)**

(in thousands)

	Notes	Cumulative Capital	Cumulative Issue Costs	Cumulative Net Income	Cumulative Distributions	Contributed Surplus	Total
Unitholders' equity, December 31, 2008		\$489,538	(\$24,122)	\$41,732	(\$122,022)	\$525	\$385,651
Year ended December 31, 2009							
Net income		-	-	16,299	-	-	\$16,299
Distributions		-	-	-	(43,763)	-	(43,763)
Public offering		125,400	(5,643)	-	-	-	119,757
Distribution reinvestment plan		2,793	-	-	-	-	2,793
Unit option plan – options exercised	11	5	-	-	-	-	5
Contributed surplus unit option plan	11	-	-	-	-	428	428
Long-Term incentive plan	12	356	-	-	-	-	356
Unitholders' equity, December 31, 2009		\$618,092	(\$29,765)	\$58,031	(\$165,785)	\$953	\$481,526
<b>Six Months Ended June 30, 2010</b>							
<b>Net income</b>		-	-	<b>\$9,189</b>	-	-	<b>\$9,189</b>
<b>Distributions</b>		-	-	-	<b>(25,735)</b>	-	<b>(25,735)</b>
<b>Distribution reinvestment plan</b>		<b>2,157</b>	-	-	-	-	<b>2,157</b>
<b>Restricted unit plan</b>		<b>(1,142)</b>	-	-	-	<b>163</b>	<b>(979)</b>
<b>Contributed surplus, unit option plan</b>		-	-	-	-	<b>392</b>	<b>392</b>
<b>Long-Term Incentive plan</b>	<b>12</b>	<b>264</b>	-	-	-	-	<b>264</b>
<b>Unitholders' equity, June 30, 2010</b>		<b>\$619,371</b>	<b>(\$29,765)</b>	<b>\$67,220</b>	<b>(\$191,520)</b>	<b>\$1,508</b>	<b>\$466,814</b>

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

## Consolidated Statements of Earnings and Comprehensive Income (Unaudited)

(in thousands, except unit and per unit amounts)

	Three Months Ended June 30, 2010	Three Months Ended June 30, 2009	Six Months Ended June 30, 2010	Six Months Ended June 30, 2009
<b>Revenues</b>				
Rental properties	\$43,780	\$35,732	\$90,804	\$72,707
Real estate services	155	131	296	285
	<b>43,935</b>	35,863	<b>91,100</b>	72,992
<b>Expenses</b>				
Rental property operating	18,150	13,912	38,450	29,156
Real estate services	96	61	180	150
Financing	8,463	7,035	16,833	13,890
Trust	1,241	832	2,680	1,753
Amortization of rental properties	5,600	4,417	11,146	8,798
Amortization of intangibles	4,906	4,830	10,851	9,458
Amortization of leasing cost	443	352	876	833
Amortization of other assets	428	474	895	1,128
	<b>39,327</b>	31,913	<b>81,911</b>	65,166
<b>Net income and comprehensive income for the period</b>	<b>\$4,608</b>	\$3,950	<b>\$9,189</b>	\$7,826
<b>Net income per unit</b>				
Basic	\$0.12	\$0.13	\$0.24	\$0.25
Fully diluted	\$0.12	\$0.13	\$0.23	\$0.25
Weighted average number of units (Note 10)				
Basic	38,737,721	30,966,186	38,709,292	30,940,192
Fully diluted	39,203,751	31,369,657	39,156,758	31,335,800

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

## Consolidated Statements of Cash Flows (Unaudited)

(in thousands)

	Notes	Three Months Ended June 30, 2010	Three Months Ended June 30, 2009	Six Months Ended June 30, 2010	Six Months Ended June 30, 2009
<b>CASH PROVIDED BY (USED IN):</b>					
<b>Operating activities</b>					
Net income		\$4,608	\$3,950	\$9,189	\$7,826
Items not affecting cash					
Amortization of rental properties		5,600	4,417	11,146	8,798
Amortization of office equipment		79	71	158	138
Amortization of intangibles		4,906	4,830	10,851	9,458
Amortization of leasing cost		443	352	876	833
Amortization of tenant improvements		349	403	737	990
Step rent adjustments (revenue)		(178)	(255)	(390)	(556)
Step rent adjustments (expenses)		36	64	210	150
Mark to market rent adjustments		(663)	(252)	(952)	(134)
Amortization, premium on assumed mortgages		(4)	(6)	(7)	(14)
Changes in other non-cash financing expenses		219	157	415	321
Compensation expense		436	55	555	111
		15,831	13,786	32,788	27,921
Change in other non-cash operating items		(9,483)	(1,072)	(12,825)	(1,613)
<b>Cash from operating activities</b>		<b>6,348</b>	<b>12,714</b>	<b>19,963</b>	<b>26,308</b>
<b>Investing activities</b>					
Rental properties acquired, net of non-cash consideration	2	(11,853)	(4,365)	(11,853)	(4,365)
Capital expenditures, rental properties and other assets		(2,808)	(916)	(4,340)	(1,515)
Capital expenditures, properties under development		(3,527)	(1,513)	(6,884)	(3,528)
Tenant improvements and leasing cost		(3,527)	(1,858)	(4,329)	(3,133)
Tenant inducements		(172)	(37)	(209)	(215)
<b>Cash used in investing activities</b>		<b>(21,887)</b>	<b>(8,689)</b>	<b>(27,615)</b>	<b>(12,756)</b>
<b>Financing Activities</b>					
Repayment of mortgages payable		(4,011)	(8,545)	(9,942)	(21,449)
Proceeds from new mortgages payable		(180)	-	18,062	911
Distributions		(11,656)	(9,947)	(23,566)	(18,987)
Restricted unit plan	13	-	-	(1,142)	-
Proceeds from units issued under the LTIP (net of issue costs)	12	173	87	264	167
Net increase (decrease) in bank indebtedness		30,272	13,226	23,417	25,913
<b>Cash provided by (used in) financing activities</b>		<b>14,598</b>	<b>(5,179)</b>	<b>7,093</b>	<b>(13,445)</b>
<b>Increase (decrease) in cash and cash equivalents</b>		<b>(941)</b>	<b>(1,154)</b>	<b>(559)</b>	<b>107</b>
<b>Cash and cash equivalents, beginning of period</b>		<b>1,652</b>	<b>2,045</b>	<b>1,270</b>	<b>784</b>
<b>Cash and cash equivalents, end of period</b>		<b>\$711</b>	<b>\$891</b>	<b>\$711</b>	<b>\$891</b>
<b>Other cash flow information</b>					
Interest paid		\$8,981	\$7,180	\$17,825	\$14,370
<b>Supplemental cash flow information</b>					
Units issued		\$1,214	\$358	\$2,157	\$1,603

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

**Notes To Consolidated Financial Statements**  
**(In thousands of dollars except per unit and unit amounts)**  
**(Unaudited)**  
**June 30, 2010 and June 30, 2009**

**1. The REIT**

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**

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

	For the Six Months Ended June 30, 2010	For the Three Months Ended June 30, 2010	For the Year Ended December 31, 2009
Rental properties	\$10,709	\$10,709	\$214,718
Other assets	328	328	83
Fair value of in-place leases and tenant relationships	1,501	1,501	14,000
Fair value of above-market leases	6	6	3,301
Fair value of below-market leases	(665)	(665)	(9,125)
Accounts payable and accrued liabilities	(26)	(26)	(13,930)
Cash consideration paid for the net assets acquired	\$11,853	\$11,853	\$209,047

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 unaudited interim consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and are consistent with the accounting policies used in the REIT's audited consolidated financial statements for the year ended December 31, 2009, except as described in Note 3(b) below. The interim consolidated financial statements do not include all the information and disclosures required for annual financial statements and therefore consolidated financial statements should be read in conjunction with the annual audited consolidated financial statements.

(b) Unit-Based Compensation Plan

The REIT uses the fair value based method of accounting for its Restricted Unit Plan whereby compensation expense is recognized over the vesting period.

(c) Comparative Amounts

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

(d) Future Changes to Accounting Policies

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 June 30, 2010	Cost	Accumulated Amortization	Net Carrying Amount
Buildings, improvements and other costs	\$900,532	\$77,452	\$823,080
Land	198,706	-	198,706
	<b>\$1,099,238</b>	<b>77,452</b>	<b>\$1,021,786</b>
As at December 31, 2009	Cost	Accumulated Amortization	Net Carrying Amount
Buildings, improvements and other costs	\$891,059	\$66,306	\$824,753
Land	193,130	-	193,130
	<b>\$1,084,189</b>	<b>\$66,306</b>	<b>\$1,017,883</b>

Included in Properties Under Development is interest capitalized during the six months ended June 30, 2010 of \$1,296 and during the year ended December 31, 2009 of \$1,235.

#### 5. Intangibles

Intangibles consist of costs incurred by the REIT, net of accumulated amortization of \$55,023 (December 31, 2009 - \$51,565)

As at June 30, 2010	Cost	Accumulated Amortization	Net Carrying Amount
Leasing costs and tenant relationships on rental properties acquired	\$88,464	\$54,543	\$33,921
Amounts recorded on the acquisition of the property manager – contracts and customer relationships	959	480	479
	<b>\$89,423</b>	<b>\$55,023</b>	<b>\$34,400</b>
As at December 31, 2009	Cost	Accumulated Amortization	Net Carrying Amount
Leasing costs and tenant relationships on rental properties acquired	\$94,357	\$51,134	\$43,223
Amounts recorded on the acquisition of the property manager – contracts and customer relationships	959	431	528
	<b>\$95,316</b>	<b>\$51,565</b>	<b>\$43,751</b>

#### 6. Other Assets

Other assets consist of:

	June 30, 2010	December 31, 2009
Leasing costs, net of accumulated amortization of \$3,300 (December 31, 2009 - \$2,763)	\$10,307	\$7,814
Above-market rents of leases acquired through rental property acquisitions net of accumulated amortization of \$12,918 (December 31, 2009 - \$13,786)	8,388	10,901
Accounts receivable	15,545	15,835
Tenant inducements, net of accumulated amortization of \$373 (December 31, 2009 - \$317)	1,137	1,001
Tenant improvements, net of accumulated amortization of \$3,531 (December 31, 2009 - \$3,280)	6,707	6,484
Prepaid expenses	7,548	1,585
Escrow accounts held by mortgagees	3,130	6,072
Computer and office equipment, net of accumulated amortization of \$707 (December 31, 2009 - \$548)	524	634
	<b>\$53,286</b>	<b>\$50,326</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 2.39% and 8.1% (contractual 2.39% and 8.10%).

Mortgages payable at June 30, 2010 are due as follows:

	Principal Repayments	Balance due at Maturity	Total
Year ended December 31, 2010	\$8,237	\$-	\$8,237
Year ended December 31, 2011	16,743	19,660	36,403
Year ended December 31, 2012	16,707	36,805	53,512
Year ended December 31, 2013	17,390	21,997	39,387
Year ended December 31, 2014	13,457	161,663	175,120
Thereafter	29,692	263,582	293,274
	<b>\$102,226</b>	<b>\$503,707</b>	<b>\$605,933</b>
Net discount on assumed mortgages (net of accumulated amortization of \$1,333)			(223)
Deferred financing costs (net of accumulated amortization of \$2,207)			(3,563)
			<b>\$602,147</b>

Mortgages payable at December 31, 2009 are due as follows:

	Principal Repayments	Balance due at Maturity	Total
Year ended December 31, 2010	15,904	7,039	22,943
Year ended December 31, 2011	16,588	14,868	31,456
Year ended December 31, 2012	16,595	36,805	53,400
Year ended December 31, 2013	17,019	21,997	39,016
Year ended December 31, 2014	13,042	161,663	174,705
Thereafter	29,635	246,220	275,855
	<b>\$108,783</b>	<b>\$488,592</b>	<b>\$597,375</b>
Net premium on assumed mortgages (net of accumulated amortization of \$1,327)			(216)
Deferred financing costs (net of accumulated amortization of \$1,805)			(3,540)
			<b>\$593,619</b>

The REIT has a \$70,000 revolving credit facility with a Canadian chartered bank, which matures August 31, 2011 and bears interest at bank prime rate to August 31, 2010. Effective September, 2010 the facility will bear interest at bank prime plus 175 basis points or bankers' acceptance plus 275 basis points. 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 June 30, 2010.

At June 30, 2010 the amount outstanding under the credit facility was \$40,340 (December 31, 2009 \$16,923).

#### **8. Accounts Payable and Other Liabilities**

Accounts payable and other liabilities consist of:

	June 30, 2010	December 31, 2009
General operating payables and tenant deposits	<b>\$28,035</b>	\$38,578
Below market rents of leases acquired through rental property acquisition – net of accumulated amortization of \$9,399 (December 31, 2009 - \$7,295)	<b>14,627</b>	17,433
Accrued interest	<b>2,725</b>	2,784
	<b>\$45,387</b>	<b>\$58,795</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, 2008	31,235,670
Units issued pursuant to offering on October 2, 2009	7,600,000
Units issued under the Distribution Reinvestment Plan	205,273
Units issued under the Unit Option Plan (Note 11)	416
<hr/>	
Units outstanding, December 31, 2009	<b>39,041,359</b>
<hr/>	
<b>Units issued under the Distribution Reinvestment Plan</b>	<b>115,028</b>
<hr/>	
<b>Units outstanding, June 30, 2010</b>	<b>39,156,387</b>

### **10. Weighted Average Units**

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

	<b>Three Months Period Ended June 30, 2010</b>	Three Months Period Ended June 30, 2009	<b>Six Months Period Ended June 30, 2010</b>	Six Months Period Ended June 30, 2009
<b>Basic</b>	<b>38,737,721</b>	30,966,186	<b>38,709,292</b>	30,940,192
<b>Unit option plan</b>	<b>84,531</b>	16,178	<b>63,087</b>	8,315
<b>Long-term incentive plan</b>	<b>381,499</b>	387,293	<b>384,380</b>	387,293
<hr/>				
<b>Fully diluted</b>	<b>39,203,751</b>	31,369,657	<b>39,156,758</b>	31,335,800

### **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 236,664 options vested on December 17, 2009. 125,003 options will vest on December 17, 2010 and an additional 108,333 options will vest on December 17, 2010, provided that certain performance achievements are met. 118,333 options have expired.

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. 1,249 options vested on December 15, 2009, and 1,250 and 1,251 options will vest on December 15, 2010 and December 15, 2011, respectively, provided that certain performance achievements are met. 416 options were exercised.

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 options vested on January 15, 2010 and 43,333 and 43,334 options will vest on January 15, 2011 and January 15, 2012, respectively, provided that certain performance achievements are met.

On March 9, 2010, 895,176 options were granted to trustees, officers and employees with an exercise price of \$19.39 and expiring on March 9, 2015. 298,391, 298,392, and 298,393 options will vest on March 9, 2011, March 9, 2012 and March 9, 2013, respectively.

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 for the quarters ended June 30, 2010 and 2009 were \$305 and \$55, respectively. The Unit Option Plan and assumptions utilized in the calculation thereof using the Black-Scholes Model for option valuation are as follows:

	March 2010	January 2009	December 2008	December 2007
Unit options granted	895,176	130,000	3,750	710,000
Unit option holding period (years)	5	5	5	5
Volatility rate	24.1%	24.0%	24.1%	19.8%
Distribution yield	6.8%	10.6%	11.1%	6.0%
Risk free interest rate	2.8%	1.6%	2.1%	3.9%
Value of options granted	\$1,726	\$70	\$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, 2008	605,417	\$21.06
Options granted in the year ended December 31, 2009	130,000	\$12.34
Options exercised in the year ended December 31, 2009	(416)	\$10.87
Options outstanding as at December 31, 2009	735,001	\$19.52
Options granted in the period ended June 30, 2010	895,176	\$19.39
Options expired	(10,000)	\$21.13
Options outstanding as at June 30, 2010	1,620,177	\$19.44
Options exercisable as at June 30, 2010	402,495	\$20.16

## 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 June 30, 2010 and December 31, 2009 were \$7,413 and \$7,490, 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 June 30, 2010	Six Months Ended June 30, 2010	Cumulative as at December 31, 2009
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	(779)	(72)	(707)
Distributions applied against installment loans receivable	2,403	255	2,148
Repayments of installment loans	226	81	145
	(4,002)	264	(4,266)
	\$2,754	\$264	\$2,490

Units issued under the LTIP	Cumulative as at December 31, 2009	Year Ended December 31, 2009	Cumulative as at December 31, 2008
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 loan receivable	(707)	(155)	(552)
Distributions applied against installment loan receivable	2,148	511	1,637
Repayments of installment loans	145	-	145
	(4,266)	356	(4,622)
	\$2,490	\$356	\$2,134

### **13. Restricted Unit Plan**

Certain officers and employees of the REIT may be granted Restricted Units pursuant to the terms of the 2010 Restricted Unit Plan, which are subject to vesting conditions and disposition restrictions, in order to provide a long-term compensation incentive. The Restricted Units remain subject to forfeiture until the participant has held his or her position with the REIT for specific period of time. Full vesting of Restricted Units will not occur until the participant has remained employed by the REIT for three years from the date of grant. Units required under the Restricted Unit Plan are acquired in the secondary market through a custodian and then distributed to the individual participant accounts. During the first quarter of 2010, 55,659 Units of the REIT were acquired in the secondary market for the 2010 Restricted Unit Plan and are included in the units outstanding. Compensation expense for the quarter ended June 30, 2010 were \$131.

### **14. Segmented Disclosure**

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

### **15. 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 June 30, 2010 and December 31, 2009 were \$9,807 and \$4,604, 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.

The REIT has entered into conditional purchase and sale agreement for the acquisition for approximately \$14.5 million of managing co-ownership interests in 303 underground commercial parking spaces and 18,360 square feet of retail space to be constructed as part of three separate condominium projects. Each condominium project is adjacent to one or more of our Class I office properties in the King & Spadina area of Toronto. Each acquisition is conditional upon condominium registration being obtained and is scheduled to close between 2011 and 2013.

### **16. 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 three months ended June 30, 2010 and 2009 real estate service revenue earned from these properties was \$58 and \$55, respectively. For the six months ended June 30, 2010 and 2009 real estate service revenue earned from these properties was \$111 and \$108, respectively. These revenues were fully paid in the respective period. 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 include amounts received from related parties for the guarantee of income. 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 September 30, 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 Loblaw's 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. The related party revenue for the quarter ended June 30, 2010 and June 30, 2009 were \$24 and \$23, respectively. For the six months ended June 30, 2010 and 2009, related party revenue was \$47 for both periods.

#### **17. Subsequent Events**

On July 29, 2010, we received a commitment from a Canadian chartered bank for a first mortgage on 645 Wellington Avenue in Montréal in the principal amount of \$6,900, having a term of three years, bearing interest at approximately 3.8% and payable in blended instalments of principal and interest based on a 25-year amortization.

On August 4, 2010, we announced the acquisition of the Lougheed Building in Calgary for \$31,000. Located at 604, 1<sup>st</sup> Street SW, the property is comprised of 86,478 square feet of GLA and is fully leased with a weighted average lease term of over eight years.

On August 4, 2010, we announced the acquisition of 49 Front Street East and 252-264 Front Street East in Toronto for \$19,000. Located on the south side of Front Street and one building east of our Beardmore and Perkins/Dixon buildings, 49 Front is comprised of 19,936 square feet of GLA and is fully leased. Located on the north side of Adelaide, just east of Jarvis Street, 252-264 Adelaide is comprised of 50,217 square feet of GLA and is fully leased.