



**H&R Real Estate Investment Trust and H&R Finance Trust  
2013 Annual Report  
Including Combined MD&A and Financial Statements**



**The Bow, Calgary**



**Scotia Plaza, Toronto**



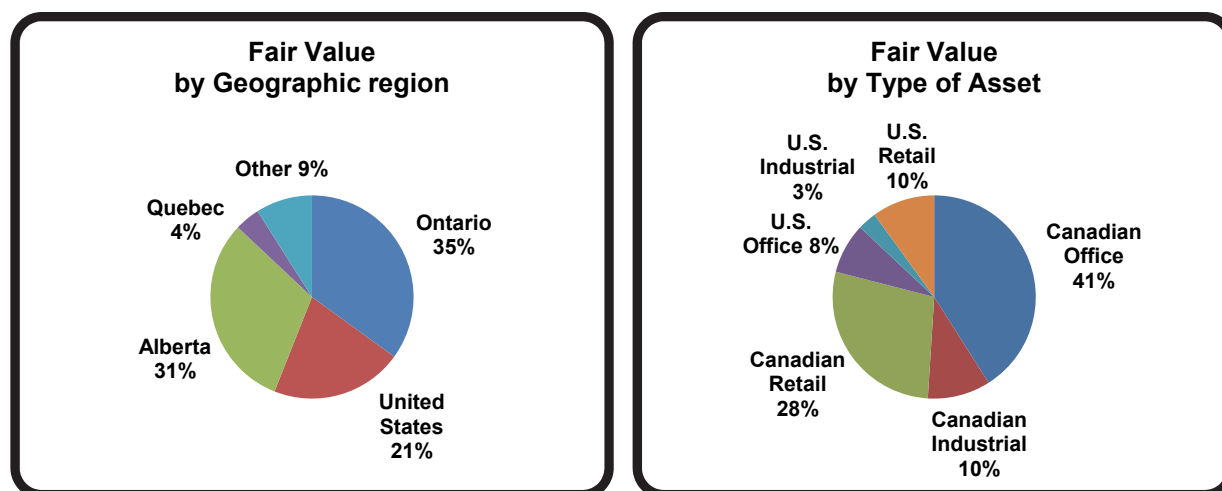
**Corus Quay, Toronto**

## H&R Profile

H&R REIT is an open-ended real estate investment trust, which owns a North American portfolio of 42 office, 112 industrial and 167 retail properties comprising over 53 million square feet and 2 development projects, with a fair value of approximately \$13 billion. In addition, H&R REIT owns a 33.7% interest in ECHO Realty LP (“ECHO”) which owns 173 properties, excluding properties under development and vacant land, totalling 7.3 million square feet. The foundation of H&R REIT's success since inception in 1996 has been a disciplined strategy that leads to consistent and profitable growth. H&R REIT leases its properties for long terms to creditworthy tenants and strives to match those leases with primarily long-term, fixed-rate financing.

H&R Finance Trust is an unincorporated investment trust, which primarily invests in notes issued by a U.S. corporation which is a subsidiary of H&R REIT. As at December 31, 2013, the note receivable balance is U.S. \$219.8 million. In 2008, H&R REIT completed an internal reorganization which resulted in each issued and outstanding H&R REIT unit trading together with a unit of H&R Finance Trust as a “Stapled Unit” on the Toronto Stock Exchange.

Additional information regarding H&R REIT and H&R Finance Trust is available at [www.hr-reit.com](http://www.hr-reit.com) and on [www.sedar.com](http://www.sedar.com).



## Primary Objectives

H&R strives to achieve two primary objectives: to provide unitholders with stable and growing cash distributions generated by revenues derived from a diversified portfolio of investment properties, and to maximize the value of units through active management of H&R's assets, acquisition of additional properties, and the development of new projects which are pre-leased to creditworthy tenants. We are committed to maximizing returns to unitholders while maintaining prudent risk management and conservative use of financial leverage.

## Stability and Growth through Discipline

Since inception in 1996, H&R has executed a disciplined and proven strategy that has provided stable cash flow and adjusted funds from operations. We achieve our primary objectives and mitigate risks through long-term property leasing and financing, combined with conservative management of assets and liabilities.

## President's Message to Unitholders

In H&R REIT's 17 year history as a public issuer, 2013 was truly the most transformational year. The 2013 financial results and highlights tell the story:

Acquisition of Primaris REIT - we have diversified our portfolio and strategically positioned ourselves to expand our retail holdings and enhance returns through the acquisition of a \$3.1 billion, high quality portfolio of enclosed shopping malls across Canada, together with an experienced team of specialized professionals.

Acquisition of 1/3<sup>rd</sup> Ownership Interest in Echo Realty - with the acquisition of an ownership Interest in Echo Realty, the active owner and developer of a portfolio of 173 primarily retail properties in the United States, with Giant Eagle Inc., the leading grocer in Pennsylvania and Ohio, anchoring the majority of these properties, we have succeeded in a strategic investment in not only bricks and mortar, but also in another retail management platform.

Completion of the BOW - our flagship development in downtown Calgary - 2013 marked the milestone completion of our flagship office building, the Bow, in downtown Calgary and commencement of the 25 year lease with EnCana Corporation. The final tranche of long-term bond financing secured by The Bow was also completed.

Construction launch of a 740,000 sq.ft. State-of-the-Art Distribution Centre - fully pre-leased long-term to Unilever Canada Inc., with completion scheduled for the end of 2014.

Internalization of Property Management - with the internalization of Property Management, we have successfully eliminated any perceived conflicts of interest and aligned the interests of unitholders and management.

Debt to total asset ratio, reduced to 49.2% - while reducing the debt to asset ratio, we have increased total assets to \$13.6 billion, our unencumbered pool of assets to \$1.3 billion and our market cap to \$5.8 billion at year end.

Since inception we have delivered to our unitholders, stability and growth through discipline, earning a compound average annual return of 14% and for the 17<sup>th</sup> consecutive year, our portfolio occupancy rate remained above 98%, a testament to the high quality of our properties, as well as our management team.

### Outlook

Economic forecasts for 2014 bode well for commercial real estate fundamentals in North America, particularly in the recovering US economy, where H&R REIT has a sizable investment.

With the REIT's units trading at relatively low price multiples, we believe the timing is right to initiate a repurchase/cancellation of H&R's Stapled Units. This move is a reflection of our confidence in our company and the commitment we have to using our balance sheet strength to sustain growth and generate economic value for our unitholders.

We are also actively exploring the sale and joint venture of certain assets, the proceeds of which may be used to repurchase units under the normal course issuer bid.

H&R's low risk profile is highly predictable over the next five years with only 30% of our leases rolling and only 42% of our mortgages coming due, at an overall loan to value ratio of 43%. With \$28 million of cash and \$300 million available from our credit and operating facilities at year end, H&R has ample liquidity to retire high-cost debt as it matures and to fund further acquisition opportunities.

I would also like to take this opportunity to formally welcome the Primaris team into the H&R family we have now worked with for over a year. We appreciate your skills, expertise and the ease with which you have so successfully integrated into our company.

On behalf of our management team, I would like to thank our investors for their confidence, our trustees for their advice and governance, and our employees for their hard work and commitment to the REIT's success over the past year.

With your continuing support, we look forward to further delivering ***stability and growth through discipline.***

A handwritten signature in black ink, consisting of a series of loops and a long horizontal stroke that tapers to the right.

President and Chief Executive Officer  
April 1, 2014

**COMBINED MANAGEMENT'S DISCUSSION  
AND ANALYSIS OF H&R REAL ESTATE  
INVESTMENT TRUST AND H&R FINANCE TRUST**

**For the Year ended December 31, 2013**

Dated: February 27, 2014

## TABLE OF CONTENTS

<b>SECTION I</b>			
<hr/>			
Basis of Presentation	1	Other Income and Expense Items	17
Forward-Looking Disclaimer	1	Assets	22
Non-GAAP Financial Measures	2	Liabilities	26
Overview	3	Equity	30
Changes in Accounting Policies	4	Funds from Operations	31
<hr/>		Adjusted Funds from Operations	33
<b>SECTION II</b>		Liquidity and Capital Resources	35
<hr/>		Off-Balance Sheet Items	37
Financial Highlights	5	Financial Instruments and Other Instruments	38
Key Performance Drivers	5	<hr/>	
Portfolio Overview	6	<b>SECTION IV</b>	
Summary of Significant 2013 Activity	8	Critical Accounting Estimates and Judgements	39
Selected Annual Information	9	Disclosure Controls & Procedures	40
Summary of Quarterly Results	9	<hr/>	
<hr/>		<b>SECTION V</b>	
<b>SECTION III</b>		Risks and Uncertainties	41
<hr/>		Outstanding Unit Data	46
Results of Operations	10	Additional Information	46
Property Operating Income	12	<hr/>	
Segmented Information	14		
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## **SECTION I**

### **BASIS OF PRESENTATION**

Financial data included in this combined Management's Discussion and Analysis ("MD&A") of combined results of operations and combined financial position of H&R Real Estate Investment Trust (the "REIT") and H&R Finance Trust ("Finance Trust" and together with the REIT, the "Trusts") for the year ended December 31, 2013 includes material information up to February 27, 2014. Financial data provided has been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). This MD&A should be read in conjunction with the combined financial statements of the Trusts and appended notes for the years ended December 31, 2013 and 2012 (the "Combined Financial Statements"). All amounts in this MD&A are in thousands of Canadian dollars, except where otherwise stated. Historical results, including trends which might appear, should not be taken as indicative of future operations or results. Certain prior period items have been reclassified to conform with the new accounting standards adopted in the current period.

On October 24, 2013, the Ontario Securities Commission (on its behalf and on behalf of the other provincial securities regulators) issued a decision which permits the REIT and Finance Trust to file one set of combined financial statements rather than separate financial statements. The Combined Financial Statements have been presented on a basis whereby the assets and liabilities of the REIT and Finance Trust have been combined in accordance with the accounting principles applicable to both the REIT and Finance Trust in accordance with IFRS to reflect the financial position and results of the REIT and Finance Trust on a combined basis. This same decision permits the REIT and Finance Trust to file one combined MD&A which has been done for the year ended December 31, 2013.

### **FORWARD-LOOKING DISCLAIMER**

Certain information in this MD&A contains forward-looking information within the meaning of applicable securities laws (also known as forward-looking statements) including, among others, statements made or implied under the headings "Discussion of Operations", "Liquidity and Capital Resources", "Outlook", "Risks and Uncertainties" and "Subsequent Events" relating to the Trusts' objectives, strategies to achieve those objectives, the Trusts' beliefs, plans, estimates, projections and intentions, and similar statements concerning anticipated future events, results, circumstances, performance or expectations that are not historical facts. Forward-looking statements generally can be identified by words such as "outlook", "objective", "may", "will", "expect", "intend", "estimate", "anticipate", "believe", "should", "plans", "project", "budget" or "continue" or similar expressions suggesting future outcomes or events. Such forward-looking statements reflect the Trusts' current beliefs and are based on information currently available to management.

Forward-looking statements are provided for the purpose of presenting information about management's current expectations and plans relating to the future and readers are cautioned that such statements may not be appropriate for other purposes. These statements are not guarantees of future performance and are based on the Trusts' estimates and assumptions that are subject to risks and uncertainties, including those described below under "Risks and Uncertainties" and those discussed in the Trusts' materials filed with the Canadian securities regulatory authorities from time to time, which could cause the actual results and performance of the Trusts to differ materially from the forward-looking statements contained in this MD&A. Those risks and uncertainties include, among other things, risks related to: unit price risk; real property ownership; credit risk and tenant concentration; interest and other debt-related risk; ability to access capital markets; lease rollover risk; joint arrangements risk; currency risk; construction risks; availability of cash for distributions; environmental risk; tax risk; tax consequences to U.S. holders; dilution; unitholder liability; redemption right risk and risks relating to debentures. Material factors or assumptions that were applied in drawing a conclusion or making an estimate set out in the forward-looking statements include that the general economy is stable; local real estate conditions are stable; interest rates are relatively stable; and equity and debt markets continue to provide access to capital. The Trusts caution that this list of factors is not exhaustive. Although the forward-looking statements contained in this MD&A are based upon what the Trusts believe are reasonable assumptions, there can be no assurance that actual results will be consistent with these forward-looking statements.

Readers are also urged to examine the REIT and Finance Trust's materials filed with the Canadian securities regulatory authorities from time to time as they may contain discussions on risks and uncertainties which could cause the actual results and performance of the REIT and Finance Trust to differ materially from the forward-looking statements contained in this MD&A. Neither Finance Trust nor any of its trustees or officers, assumes any responsibility for the completeness of the information contained in the REIT's materials filed with the Canadian securities regulatory authorities or for any failure of the REIT or its trustees or officers to disclose events or facts which may have occurred or which may affect the significance or accuracy of any such information. Neither the REIT nor any of its trustees or officers, assumes any responsibility for the completeness of the information contained in Finance Trust's materials filed with the Canadian securities regulatory authorities or for any failure of Finance Trust or its trustees or officers to disclose events or facts which may have occurred or which may affect the significance or accuracy of any such information.

All forward-looking statements in this MD&A are qualified by these cautionary statements. These forward-looking statements are made as of February 27, 2014 and the Trusts, except as required by applicable law, assume no obligation to update or revise them to reflect new information or the occurrence of future events or circumstances.

## **NON-GAAP FINANCIAL MEASURES**

The Trusts' Combined Financial Statements are prepared in accordance with IFRS. However, in this MD&A, a number of measures which do not have a meaning recognized under IFRS or Canadian Generally Accepted Accounting Principles ("GAAP") are presented. These measures, as well as the reasons why management believes these measures are useful to investors, are described below.

### **The REIT's Interests and The Trusts' Interests**

Effective January 1, 2013, the Trusts adopted IFRS 11, *Joint Arrangements* which resulted in the Trusts no longer proportionately consolidating certain joint arrangements. The Trusts now apply the equity method of accounting to joint arrangements, and this change in accounting policy has been applied retrospectively. Throughout this MD&A, any references to the "Combined Financial Statements" refer to amounts as reported under IFRS and any references to "The REIT's interests" or "The Trusts' interests" are non-GAAP measures which include amounts per the Combined Financial Statements plus equity accounted investments. These non-GAAP financial measures take into account the Trusts' proportionate share of the financial position and results of operations of the Trusts' entire portfolio, under the assumption that all investments have been proportionately consolidated.

### **Property Operating Income and Same-Asset Property Operating Income**

Property operating income is the rental revenue generated from the REIT's investment properties, net of the property operating expenses incurred. Management believes that this is a useful measure for investors as it provides a snapshot of how the REIT's properties are performing before financing costs and other sources of income and expenditures which are not directly related to the day-to-day operations of a property. Management also believes that same-asset property operating income is a useful measure as it shows the property operating income generated by investment properties owned by the REIT for a consistent period, which provides investors with a better understanding of the change in performance of properties period over period. Property operating income should not be construed as an alternative to net income calculated in accordance with IFRS. Same-asset property operating income is a non-GAAP financial measure used by the REIT to report period-over-period performance for properties owned by the REIT throughout both periods. This typically excludes acquisitions, dispositions, equity accounted investments and transfers of properties under development to investment properties.

### **Funds from Operations ("FFO")**

FFO is a non-GAAP financial measure widely used in the real estate industry as a measure of operating performance. The Trusts present their FFO calculations in accordance with the Real Property Association of Canada (REALPAC) guidelines however, this method of calculating FFO may differ when comparing to other issuers. Management believes this to be a useful measure for investors as it adjusts for items included in net income that are not recurring including gain (loss) on sale of real estate assets, as well as non-cash items such as the fair value adjustments on investment properties. FFO should not be construed as an alternative to net income or cash flows provided by operating activities calculated in accordance with IFRS. See "Funds from Operations" for a reconciliation of net income to FFO.

### **Adjusted Funds from Operations ("AFFO")**

AFFO is also a widely used measure in the real estate industry which management believes to be a useful alternative to cash provided from operations. AFFO is calculated by adjusting FFO for non-cash items such as: straight-lining of contractual rent, rent amortization of tenant inducements, effective interest rate accretion and unit-based compensation. Non-recurring costs that impact operating cash flow may be adjusted, and capital and tenant expenditures incurred and capitalized in the period by the Trusts are deducted. There is no standard industry definition of AFFO, and as a result, the Trusts' calculation may differ from other issuers' calculations. AFFO should not be construed as an alternative to net income or cash flows provided by operating activities calculated in accordance with IFRS. See "Adjusted Funds from Operations" for a reconciliation of FFO to AFFO to cash provided by operations.

None of these non-GAAP financial measures should be construed as an alternative to financial measures calculated in accordance with GAAP. Further, the Trusts' method of calculating these supplemental non-GAAP financial measures may differ from the methods of other real estate investment trusts or other issuers, and accordingly, these measures may not be comparable to those measures presented by other real estate investment trusts or issuers.



## OVERVIEW

The REIT is an unincorporated open-ended trust created by a declaration of trust (the "REIT Declaration of Trust") and governed by the laws of the Province of Ontario. Unitholders are entitled to have their REIT units comprising part of the Stapled Units (as defined below) redeemed at any time on demand payable in cash (subject to monthly limits) and/or *in specie*, provided that the corresponding Finance Trust units are being contemporaneously redeemed.

Finance Trust is an unincorporated investment trust. Finance Trust was established pursuant to a Plan of Arrangement (the "Plan of Arrangement") on October 1, 2008, as described in the REIT's information circular dated August 20, 2008, as an open-ended limited purpose unit trust pursuant to its declaration of Trust (the "Finance Trust Declaration of Trust"). Each issued and outstanding Finance Trust unit is "stapled" to a unit of the REIT on a one-for-one basis such that Finance Trust units and the REIT units trade together as stapled units ("Stapled Units"), and such Stapled Units are listed and posted for trading on the Toronto Stock Exchange ("TSX"). Apart from provisions necessary to achieve such stapling, each REIT unit and Finance Trust unit retains its own separate identity and is separately listed (but not posted for trading) on the TSX (unless there is an event of uncoupling, in which case Finance Trust units will cease to be listed on the TSX).

The REIT has two primary objectives:

- to provide unitholders with stable and growing cash distributions, generated by the revenue it derives from investments in income producing real estate assets; and
- to maximize unit value through ongoing active management of the REIT's assets, acquisition of additional properties and the development and construction of projects which are pre-leased to creditworthy tenants.

The REIT's strategy to accomplish these two objectives is to accumulate a diversified portfolio of high quality investment properties in Canada and the United States occupied by creditworthy tenants.

With the acquisition of Primaris Retail Real Estate Investment Trust ("Primaris") on April 4, 2013, the Trusts now have two operating segments. The properties owned and operated by the Trusts prior to the acquisition of Primaris are defined as one segment ("the H&R portfolio"), which consists of office, industrial and retail properties throughout Canada and the United States which focuses on creditworthy tenants with long-term leases as well as Finance Trust. Subsequent acquisitions of similar properties are included in this segment. Primaris is considered by the Trusts to be a second segment (the "Primaris portfolio") which operates enclosed shopping centres and multi-tenant retail plazas throughout Canada with shorter-term leases than the H&R portfolio. Subsequent acquisitions of enclosed shopping centres and multi-tenant plazas in Canada are included in this segment. The chief operating decision maker, determined to be the Chief Executive Officer ("CEO"), reviews the results of the H&R portfolio and the Primaris portfolio separately.

The primary purpose of Finance Trust is to be a flow-through vehicle to allow the REIT to indirectly access the capital markets in a tax-efficient manner by indirectly borrowing money from the REIT's unitholders. Finance Trust's primary activity is to hold debt issued by H&R REIT (U.S.) Holdings Inc. ("U.S. Holdco"), a wholly owned U.S. subsidiary of the REIT. As at December 31, 2013, Finance Trust holds U.S. \$219.8 million of aggregate principal amount of notes payable by U.S. Holdco ("U.S. Holdco Notes"). Subject to cash flow requirements, Finance Trust intends to distribute to its unitholders, who are also unitholders of the REIT, all of its cash flow, consisting primarily of interest paid by U.S. Holdco, less administrative and other expenses and amounts to satisfy liabilities. The U.S. Holdco Notes are eliminated in the Combined Financial Statements, however the related foreign exchange difference is not eliminated upon combination as it flows through net income on the Finance Trust financial statements and other comprehensive income (loss) on the REIT financial statements.

### Mechanics of "Stapling" the Units of Finance Trust and the REIT

Pursuant to the provisions of the Declarations of Trust for Finance Trust and the REIT at all times each REIT unit must be "stapled" to a Finance Trust unit (and each Finance Trust unit must be "stapled" to a REIT unit) unless there is an "event of uncoupling" (as described below). As part of the Plan of Arrangement, the REIT and Finance Trust entered into a support agreement (the "Support Agreement") which provided, among other things, for the co-ordination of the declaration and payment of all distributions so as to provide for simultaneous record dates and payment dates; for co-ordination so as to permit the REIT to perform its obligations pursuant to the REIT's Declaration of Trust, Unit Option Plan, Distribution Reinvestment Plan and Unit Purchase Plan ("DRIP") and Unitholder Rights Plan; for Finance Trust to take all such actions and do all such things as are necessary or desirable to enable and permit the REIT to perform its obligations arising under any security issued by the REIT (including securities convertible, exercisable or exchangeable into Stapled Units); for Finance Trust to take all such actions and do all such things as are necessary or desirable to enable the REIT to perform its obligations or exercise its rights under its convertible debentures; and for Finance Trust to take all such

actions and do all such things as are necessary or desirable to issue Finance Trust units simultaneously (or as close to simultaneously as possible) with the issue of REIT units and to otherwise ensure at all times that each holder of a particular number of REIT units holds an equal number of Finance Trust units, including participating in and cooperating with any public or private distribution of Stapled Units by, among other things, executing prospectuses or other offering documents.

In the event that the REIT issues additional REIT units, pursuant to the Support Agreement, the REIT and Finance Trust will coordinate so as to ensure that each subscriber receives both REIT units and Finance Trust units, which shall trade together as Stapled Units. Prior to such event, the REIT shall provide notice to Finance Trust to cause Finance Trust to issue and deliver the requisite number of Finance Trust units to be received by and issued to, or to the order of, each subscriber as the REIT directs. In consideration of the issuance and delivery of each such Finance Trust unit, the REIT (solely as agent for and on behalf of the purchaser) or the purchaser, as the case may be, shall pay (or arrange for the payment of) a purchase price equal to the fair market value (as determined by Finance Trust in consultation with the REIT) of each such Finance Trust unit at the time of such issuance. The remainder of the subscription price for Stapled Units shall be allocated to the issuance of REIT units by the REIT. The proceeds received by Finance Trust from any such issuance shall be invested in additional notes of the same series as the U.S. Holdco Notes or distributed to unitholders of Finance Trust.

An event of uncoupling ("Event of Uncoupling") shall occur only: (a) in the event that unitholders of the REIT vote in favour of the uncoupling of units of Finance Trust and units of the REIT such that the two securities will trade separately; or (b) at the sole discretion of the trustees, but only in the event of the bankruptcy, insolvency, winding-up or reorganization (under an applicable law relating to insolvency) of the REIT or U.S. Holdco or the taking of corporate action by the REIT or U.S. Holdco in furtherance of any such action or the admitting in writing by the REIT or U.S. Holdco of its inability to pay its debts generally as they become due.

#### **Investment Restrictions**

Under Finance Trust Declaration of Trust, the assets of Finance Trust may be invested only in:

- (a) U.S. Holdco Notes; and
- (b) temporary investments in cash, term deposits with a Canadian chartered bank or trust company registered under the laws of a province of Canada, short-term government debt securities, or money market instruments (including banker's acceptances) of, or guaranteed by, a Schedule 1 Canadian bank ("Cash Equivalents"), but only if each of the following conditions are satisfied: (a) if the Cash Equivalents have a maturity date, the trustees hold them until maturity; (b) the Cash Equivalents are required to fund expenses of Finance Trust, a redemption of units, or distributions to unitholders, in each case before the next distribution date; and (c) the purpose of holding the Cash Equivalents is to prevent funds from being non-productive, and not to take advantage of market fluctuations.

The Finance Trust Declaration of Trust provides that Finance Trust shall not make any investment, take any action or omit to take any action which would result in the units of Finance Trust not being considered units of a "mutual fund trust" for purposes of the Income Tax Act (Canada) (the "Tax Act") or that would disqualify Finance Trust as a "fixed investment trust" under the Internal Revenue Code of 1986 as amended (the "Code") and the applicable regulations. In order to qualify as a "fixed investment trust" under the Code, Finance Trust generally may not acquire assets other than the U.S. Holdco Notes or certain investments in cash or cash equivalents.

#### **CHANGES IN ACCOUNTING POLICIES**

Effective January 1, 2013, the Trusts adopted the new suite of standards, which are made up of IFRS 10, *Consolidated Financial Statements*, IFRS 11, *Joint Arrangements* and IFRS 12, *Disclosure of Interests in Other Entities*. Refer to note 3 of the December 31, 2013 Combined Financial Statements of the Trusts for a detailed description and quantitative restatement of all changes as a result of these changes in accounting policies.

**SECTION II**
**FINANCIAL HIGHLIGHTS**

(in thousands except per unit amounts)	December 31, 2013	December 31, 2012
Total assets	<b>\$13,583,027</b>	\$9,873,050
Ratio of debt to total assets per the Combined Financial Statements <sup>(1)</sup>	<b>49.2%</b>	50.3%
Ratio of debt to total assets per the Trusts' Interests	<b>50.8%</b>	51.6%
Stapled Units outstanding	<b>269,975</b>	194,677
Exchangeable units outstanding	<b>17,403</b>	5,438
	Three months ended December 31, 2013	Three months ended December 31, 2012
Property rental revenue	<b>\$314,574</b>	\$216,580
Property operating income <sup>(1)</sup>	<b>204,600</b>	145,014
Net income from equity accounted investments	<b>19,163</b>	5,408
FFO <sup>(1)</sup>	<b>134,250</b>	85,228
Weighted average number of basic Stapled Units for FFO	<b>286,281</b>	195,469
FFO per basic Stapled Unit <sup>(1)</sup>	<b>0.47</b>	0.44
Distributions paid per Stapled Unit	<b>0.34</b>	0.31
Payout ratio per Stapled Unit as a % of FFO <sup>(1)</sup>	<b>72.3%</b>	70.5%

Net income is reconciled to FFO which is reconciled to AFFO. AFFO is reconciled to cash provided by operations, being the most comparable GAAP financial measure to these non-GAAP financial measures. See pages 31-35.

<sup>(1)</sup> These are non-GAAP measures.

**KEY PERFORMANCE DRIVERS**

<b>OPERATIONS</b>		<u>H&amp;R Portfolio</u>			Primaris Portfolio	Total*
		Office	Retail	Industrial		
<i>Occupancy as at December 31<sup>(1)</sup></i>	<b>2013</b>	<b>98.4%</b>	<b>98.9%</b>	<b>97.6%</b>	<b>97.6%</b>	<b>98.1%</b>
	2012	98.6%	99.1%	98.6%	N/A	98.7%
<i>Occupancy – same asset as at December 31<sup>(1)(2)</sup></i>	<b>2013</b>	<b>98.0%</b>	<b>99.9%</b>	<b>98.0%</b>	<b>N/A</b>	<b>98.4%</b>
	2012	98.4%	99.9%	99.2%	N/A	99.1%
<i>Average contractual rent per square foot for the year ended December 31<sup>(1)(3)(4)</sup></i>	<b>2013</b>	<b>\$26.14</b>	<b>\$14.04</b>	<b>\$5.43</b>	<b>\$20.97</b>	<b>\$14.66</b>
	2012	\$25.73	\$13.49	\$5.72	N/A	\$13.44

	<u>December 31, 2013</u>			<u>December 31, 2012</u>
	H&R Portfolio	Primaris Portfolio	Total*	H&R Portfolio
Average remaining term to maturity of leases (in years) <sup>(1)</sup>	11.7	4.7	10.3	12.3
Average remaining term to maturity of mortgages payable (in years) <sup>(1)</sup>	7.2	6.0	7.0	7.7

\* Weighted average total.

<sup>(1)</sup> Includes equity accounted investments.

<sup>(2)</sup> Same asset refers to those properties owned by the REIT for the two-year period ended December 31, 2013.

<sup>(3)</sup> This does not include assets held for sale or properties sold during the two-year period ended December 31, 2013.

<sup>(4)</sup> For all acquisitions, including Primaris and ECHO, the average contractual rent for the period owned by the REIT has been extrapolated for the entire 12-month period.

**PORTFOLIO OVERVIEW**

The geographic diversification of the Trusts' portfolio of properties, including those properties held in entities that the Trusts account for as equity accounted investments as at December 31, 2013, are outlined in the charts below:

NUMBER OF PROPERTIES	<u>Canada</u>				United States <sup>(1)</sup>	Total
	Ontario	Alberta	Quebec	Other		
H&R Portfolio:						
Office	24	5	1	4	11	45
Retail	36	5	5	3	256	305
Industrial	45	19	12	19	23	118
	105	29	18	26	290	468
Primaris Portfolio:						
Office	-	1	-	-	-	1
Retail	5	14	1	5	-	25
	5	15	1	5	-	26
<b>Total</b>	<b>110</b>	<b>44</b>	<b>19</b>	<b>31</b>	<b>290</b>	<b>494</b>

Square Feet (in thousands) <sup>(1)</sup>	<u>Canada</u>				United States <sup>(2)</sup>	Total
	Ontario	Alberta	Quebec	Other		
H&R Portfolio:						
Office	7,120	3,430	452	884	2,090	13,976
Retail	2,058	515	498	524	7,257	10,852
Industrial	8,631	2,810	2,978	1,268	6,841	22,528
	17,809	6,755	3,928	2,676	16,188	47,356
Primaris Portfolio:						
Office	-	52	-	-	-	52
Retail	2,166	3,545	591	2,226	-	8,528
	2,166	3,597	591	2,226	-	8,580
<b>Total</b>	<b>19,975</b>	<b>10,352</b>	<b>4,519</b>	<b>4,902</b>	<b>16,188</b>	<b>55,936</b>

<sup>(1)</sup> Square feet (in thousands) is based on the REIT's interest in the net leasable area of properties including those held in entities that the Trusts account for as equity accounted investments.

<sup>(2)</sup> In August 2013, the REIT acquired a one-third interest in Echo Realty LP ("ECHO"). The assets of ECHO include four office properties representing 65,767 square feet, 163 retail properties representing 1,918,407 square feet and six industrial properties representing 477,451 square feet for a total of 173 properties and 2,461,625 square feet, all of which are located in the United States and included in the table above. ECHO also has seven development projects and four vacant land areas which are not included in the table above.

**TOP TWENTY SOURCES OF REVENUE BY TENANT<sup>(1)</sup>**

Tenant	% of rentals from investment properties <sup>(2)</sup>	Number of locations	REIT owned sq.ft. (in 000's)	Average lease term to maturity (in years) <sup>(3)</sup>
1. Encana Corporation	10.6	2	2,073	24.1
2. Bell Canada	7.5	24	2,568	11.5
3. Hess Corporation	3.7	1	845	( <sup>6</sup> )
4. TransCanada Pipelines Limited	3.5	2	950	7.3
5. Telus Communications	3.0	17	972	8.0
6. New York City Department of Health	2.4	1	670	16.9
7. Canadian Tire Corporation <sup>(4)</sup>	2.3	19	2,587	10.8
8. Giant Eagle, Inc.	2.2	165	1,918	14.7
9. Rona Inc.	1.9	15	2,406	6.0
10. Bank of Nova Scotia	1.9	6	461	11.0
11. Nestle Canada and USA	1.6	4	2,338	4.8
12. Royal Bank of Canada	1.6	4	500	5.5
13. Canadian Imperial Bank of Commerce	1.5	10	544	9.6
14. Corus Entertainment Inc.	1.4	1	472	19.2
15. Ontario Realty Corporation and other Ontario Agencies <sup>(5)</sup>	1.1	2	360	3.3
16. Versacold Logistics Canada Inc.	1.0	12	1,733	18.6
17. Hudson's Bay/Home Outfitters	1.0	9	1,481	5.0
18. Public Works and Government Services, Canada	0.9	4	327	3.1
19. Shell Oil Products	0.9	18	249	8.5
20. Purolator Courier	0.8	12	1,071	8.4
<b>Total</b>	<b>50.8</b>	<b>328</b>	<b>24,525</b>	

(1) Includes the REIT's interests in equity accounted investments.

(2) The percentage of rentals from investment properties is based on estimated annualized gross revenue excluding straight-lining of contractual rent, capital expenditure recoveries and investment properties held for sale.

(3) Average lease term to maturity is based on net rent.

(4) Canadian Tire Corporation includes Canadian Tire, Mark's Work Warehouse, Sport Chek, Atmosphere and Sports Experts.

(5) Other Ontario agencies include: Legal Aid Ontario, Ontario Lottery and Gaming Corporation, Liquor Control Board of Ontario, and Hydro One Networks.

(6) Due to the confidentiality under the tenant lease, the term is not disclosed.

**LEASE TO MATURITY PROFILE<sup>(1)</sup>**

LEASE EXPIRIES	H&R Portfolio						Total			
	Office		Industrial		Retail		Primaris Portfolio		Total	
	% of sq.ft.	Rent per sq.ft. (\$) on expiry	% of sq.ft.	Rent per sq.ft. (\$) on expiry	% of sq.ft.	Rent per sq.ft. (\$) on expiry	% of sq.ft.	Rent per sq.ft. (\$) on expiry	% of sq.ft.	Rent per sq.ft. (\$) on expiry
2014	1.2	19.85	0.7	5.82	0.4	22.49	1.2	26.21	3.5	19.53
2015	0.6	27.94	1.7	5.41	0.4	23.21	1.8	24.57	4.5	17.66
2016	1.4	20.83	3.4	4.00	0.5	16.67	1.9	24.24	7.2	13.49
2017	0.7	20.14	0.4	5.22	1.3	10.67	2.0	18.18	4.4	15.09
2018	0.7	20.20	6.9	4.47	1.2	13.41	1.9	22.17	10.7	9.64
	4.6	21.30	13.1	4.57	3.8	14.89	8.8	22.75	30.3	13.68

(1) Includes the REIT's interests in equity accounted investments.

## **SUMMARY OF SIGNIFICANT 2013 ACTIVITY**

### The Bow

The REIT has now completed the construction of a two million square foot office building in Calgary, Alberta (the "Bow"), which is fully leased to Encana Corporation for a 25-year term. On March 15, 2013, the final floors were delivered to Encana Corporation and the 25-year lease term commenced, which will continue until May 14, 2038. Rent escalations will be at 0.75% per annum on the office space and 1.5% per annum on the parking income for the full 25-year term. Consistent with the REIT's strategy to secure long-term fixed rate financing, on June 20, 2013, the REIT issued \$300.0 million, Series C bonds at an annual rate of 3.797% due June 13, 2023. These bonds rank pari passu to the \$250.0 million, 3.690% Series A bonds due June 14, 2021 and the \$250.0 million, 3.693% Series B bonds due June 14, 2022, which were both issued on June 14, 2012.

### Primaris Acquisition

During the second quarter of 2013, the REIT acquired 100% of Primaris which consisted of 26 properties valued at \$3.2 billion. The acquisition was funded through the issuance of 62.5 million Stapled Units with a value of \$1.4 billion and the assumption of Primaris' outstanding mortgages, convertible debentures and bank indebtedness totalling \$1.6 billion. In addition, holders of 2.1 million exchangeable units of certain subsidiaries of Primaris received the same number of exchangeable units of subsidiaries of the REIT, each of which is exchangeable for 1.166 Stapled Units. The increased market capitalization relating to the acquisition of Primaris has enhanced liquidity for unitholders. Through this transaction, the REIT has achieved broader diversification by geographic region and tenant base into the enclosed shopping centre asset class at a time when U.S. and international retailers are expanding into Canada. In July 2013, the REIT, through Primaris, acquired Peter Pond Mall, a leading enclosed shopping centre in Fort McMurray, Alberta for \$168.5 million, at a capitalization rate of 6.3% (before property management fee income). The REIT also sold a 50% non-managing interest in Place d'Orleans, an enclosed shopping centre in the Ottawa region for \$110.6 million, at a capitalization rate of 5.5% before property management fee income. This transaction leverages the Primaris management platform to act as both owners and third party managers of regional shopping centres. The REIT has been pleased with its successful integration of the Primaris portfolio and platform.

### ECHO U.S. Retail Platform

In August 2013, the REIT acquired a one-third interest in ECHO, which focuses on developing and owning a core portfolio of grocery anchored shopping centres in the United States. ECHO's retail portfolio is primarily tenanted by Giant Eagle, Inc., the leading grocer in the western Pennsylvania and eastern Ohio regions. ECHO's portfolio consists of 173 investment properties, excluding properties under development and vacant land, totaling approximately 7.3 million square feet and is expected to generate, once its existing development projects are completed, in excess of U.S. \$84.0 million in net operating income annually, with an average remaining lease term of 12.9 years. The total ECHO portfolio was valued at approximately U.S. \$1.2 billion which equated to a weighted average capitalization rate of 7.3%. The REIT acquired ECHO limited partnership units issued from treasury for a total purchase price of approximately U.S. \$296.4 million before closing costs. One-third of this purchase price was paid in cash on closing, with a further one third expected to be paid 18 months from closing and the final one third expected to be paid 30 months from closing. However, should ECHO require funds for qualified asset acquisitions, a portion of the full outstanding deferred payment would be payable on accelerated demand at ECHO's option. The proceeds from the REIT will be used by ECHO to further expand its retail portfolio by acquiring additional retail properties in the eastern United States. As part of this acquisition, the REIT has appointed two directors to the ECHO board. ECHO is accounted for as an equity investment and will be reporting its financial information to the REIT one month in arrears. ECHO's results for August, September, October and November 2013 have been reported in the Trusts' year end Combined Financial Statements and this MD&A.

### Internalization of Property Management

In September 2013, the REIT completed its agreement with H&R Property Management Ltd. ("HRPM") to internalize the REIT's property management function effective July 1, 2013. On closing, a wholly owned subsidiary of the REIT, H&R REIT Management Services LP ("HRRMSLP"), acquired HRPM's REIT-related property management business in return for 9.5 million limited partnership units of HRRMSLP, which are exchangeable on a one-for-one basis for Stapled Units. The purchase price associated with the internalization did not utilize existing cash resources of the REIT, and HRPM has agreed to hold the exchangeable units (or Stapled Units upon exchange) for five years, subject to limited exceptions. As a result of the internalization, the REIT saved \$11.9 million in management and incentive fees which would otherwise have been payable to HRPM and incurred an additional \$2.2 million in property operating costs for the six months ended December 31, 2013.

Development of Airport Road Project

The REIT has entered into an agreement to build a 740,000 square foot state-of-the-art distribution centre on the Airport Road lands in Mississauga, Ontario. Unilever Canada Inc. has agreed to lease the property for 10 years providing the REIT with an anticipated 7% return on capital invested before financing. It is expected that the development will be completed by the end of 2014.

**SELECTED ANNUAL INFORMATION**

The following table summarizes certain financial information of the Trusts for the years indicated below:

<b>(in thousands of Canadian dollars except per unit amounts)</b>	Year Ended December 31, 2013	Year Ended December 31, 2012	Year Ended December 31, 2011
Rentals from investment properties	\$1,137,017	\$799,159	\$643,606
Finance income	2,108	1,854	1,036
Net income	323,635	508,860	338,043
Total comprehensive income	377,097	493,861	344,066
Total assets	13,583,027	9,873,050	8,929,340
Mortgages payable	4,897,726	3,813,613	3,092,618
Debentures payable	1,532,130	1,203,791	1,370,917
Cash distributions per unit	\$1.35	\$1.18	\$0.98

For a discussion of the changes between the 2013 and 2012 figures, please see Section III of this MD&A.

**SUMMARY OF QUARTERLY RESULTS**

<b>(in thousands of Canadian dollars)</b>	December 31, 2013	September 30, 2013 <sup>(1)</sup>	June 30 2013 <sup>(1)</sup>	March 31, 2013.
Rentals from investment properties	<b>\$314,574</b>	\$305,758	\$294,057	\$222,628
Net income from equity accounted investments	<b>19,163</b>	3,967	4,379	6,523
Finance income	<b>257</b>	346	760	745
Net income (loss)	<b>113,694</b>	(111,145)	188,977	132,109
Total comprehensive income (loss)	<b>136,788</b>	(125,629)	210,708	155,230

	December 31, 2012	September 30, 2012	June 30, 2012	March 31, 2012
Rentals from investment properties	\$216,580	\$200,015	\$199,593	\$182,971
Net income from equity accounted investments	5,408	10,866	1,676	8,223
Finance income	402	494	334	624
Net income	102,635	100,690	106,209	199,326
Total comprehensive income	109,488	72,060	116,219	196,094

<sup>(1)</sup> The above amounts have been adjusted to reflect the final purchase equation of Primaris.

Fluctuations between quarterly results for the H&R portfolio are not reflective of seasonality or cyclicity but generally from new property acquisitions, dispositions and changes in the fair value of real estate assets and liabilities. The Primaris portfolio is impacted by seasonality as revenues are typically higher in the fourth quarter due to higher percentage rent and specialty leasing. Revenues may also have significant fluctuations due to recoveries from tenants for changes to property operating costs depending on when major maintenance projects are incurred.

## SECTION III

## RESULTS OF OPERATIONS

Three months ended December 31

(in thousands of Canadian dollars)	2013			2012		
	Amounts per Combined Financial Statements	Equity accounted investments	The Trusts' interests	Amounts per Combined Financial Statements	Equity accounted investments	The Trusts' interests
Property operating income:						
Rentals from investment properties	\$314,574	\$24,011	\$338,585	\$216,580	\$13,916	\$230,496
Property operating costs	(109,974)	(8,177)	(118,151)	(71,566)	(6,105)	(77,671)
	204,600	15,834	220,434	145,014	7,811	152,825
Net income from equity accounted investments	19,163	(19,163)	-	5,408	(5,408)	-
Net loss from equity accounted investments	-	(191)	(191)	-	-	-
Finance costs:						
Finance income	257	36	293	402	7	409
Finance cost - operations	(83,807)	(4,796)	(88,603)	(64,030)	(2,563)	(66,593)
Loss on extinguishment of debt	-	-	-	(45)	-	(45)
Gain (loss) on change in fair value	(5,516)	-	(5,516)	17,730	-	17,730
	(89,066)	(4,760)	(93,826)	(45,943)	(2,556)	(48,499)
Trust expenses	(3,270)	220	(3,050)	(1,660)	-	(1,660)
Amortization	(2,089)	(257)	(2,346)	(1,437)	-	(1,437)
Fair value adjustment on real estate assets	(10,570)	8,336	(2,234)	30,499	153	30,652
Loss on sale of real estate assets	(204)	-	(204)	(1,080)	-	(1,080)
Gain on foreign exchange	6,772	-	6,772	1,535	-	1,535
Net income before income taxes	125,336	19	125,355	132,336	-	132,336
Income tax expense	(11,642)	(19)	(11,661)	(29,701)	-	(29,701)
Net income	113,694	-	113,694	102,635	-	102,635
Other comprehensive income:						
Unrealized gain on translation of U.S. denominated foreign operations	22,990	-	22,990	6,752	-	6,752
Transfer of realized loss on cash flow hedges to net income	104	-	104	101	-	101
	23,094	-	23,094	6,853	-	6,853
Total comprehensive income all attributable to unitholders	\$136,788	-	\$136,788	\$109,488	-	\$109,488

The increase in net income before income taxes for the three months ended December 31, 2013 as compared to the three months ended December 31, 2012 is primarily due to property operating income increasing due to acquisitions, including Primaris, and net income from equity accounted investments. This was offset by a lower fair value adjustment on real estate assets, higher finance costs - operations and a loss on change in fair value.



**RESULTS OF OPERATIONS**

Year ended December 31

(in thousands of Canadian dollars)	2013			2012		
	Amounts per Combined Financial Statements	Equity accounted investments	The Trusts' interests	Amounts per Combined Financial Statements	Equity accounted investments	The Trusts' interests
Property operating income:						
Rentals from investment properties	\$1,137,017	\$71,123	\$1,208,140	\$799,159	\$36,144	\$835,303
Property operating costs	(387,095)	(28,719)	(415,814)	(256,714)	(15,848)	(272,562)
	749,922	42,404	792,326	542,445	20,296	562,741
Net income from equity accounted investments	34,032	(34,032)	-	26,173	(26,173)	-
Net loss from equity accounted investments	-	(199)	(199)	-	-	-
Finance costs:						
Finance income	2,108	75	2,183	1,854	18	1,872
Finance cost - operations	(309,629)	(13,197)	(322,826)	(232,495)	(6,960)	(239,455)
Gain on extinguishment of debt	-	-	-	10,151	-	10,151
Gain (loss) on change in fair value	30,972	-	30,972	(5,143)	(2,593)	(7,736)
	(276,549)	(13,122)	(289,671)	(225,633)	(9,535)	(235,168)
Trust expenses	(5,564)	134	(5,430)	(15,220)	-	(15,220)
Amortization	(7,536)	(309)	(7,845)	(5,525)	-	(5,525)
Fair value adjustment on real estate assets	51,872	5,158	57,030	237,689	15,412	253,101
Loss on sale of real estate assets	(2,067)	-	(2,067)	(137)	-	(137)
Gain (loss) on foreign exchange	14,042	-	14,042	(7,007)	-	(7,007)
Transaction costs	(204,819)	-	(204,819)	-	-	-
Net income before income taxes	353,333	34	353,367	552,785	-	552,785
Income tax expense	(29,698)	(34)	(29,732)	(43,925)	-	(43,925)
Net income	323,635	-	323,635	508,860	-	508,860
Other comprehensive income (loss):						
Unrealized gain (loss) on translation of U.S. denominated foreign operations	53,048	-	53,048	(15,399)	-	(15,399)
Transfer of realized loss on cash flow hedges to net income	414	-	414	400	-	400
	53,462	-	53,462	(14,999)	-	(14,999)
Total comprehensive income all attributable to unitholders	\$377,097	-	\$377,097	\$493,861	-	\$493,861

The decrease in net income before income taxes for the year ended December 31, 2013 as compared to the year ended December 31, 2012 is primarily due to transaction costs, a lower fair value adjustment on real estate assets and higher finance costs - operations. This was partially offset by property operating income increasing due to acquisitions, including Primaris, and a gain on change in fair value.

**PROPERTY OPERATING INCOME**

Property operating income consists of rentals from investment properties ("rentals") less property operating costs. Rentals include all amounts earned from tenants related to lease agreements, including basic rent, parking income, operating costs and realty tax recoveries. Property operating costs primarily consist of realty taxes, maintenance, utilities and property management fees. Maintenance includes costs relating to items such as cleaning, interior and exterior building repairs and maintenance, elevator, HVAC, security and wages and benefits. "Same-asset" refers to those properties owned by the REIT for the 2-year period ended December 31, 2013. "Transactions" refers to property operating income earned from acquisitions, business combinations, dispositions and transfers of properties under development to investment properties.

(in thousands of Canadian dollars)	Three months ended December 31, 2013			Three months ended December 31, 2012		
	Same-Asset	Transactions	Total	Same-Asset	Transactions	Total
Rentals	\$187,818	\$121,120	\$308,938	\$183,302	\$16,668	\$199,970
Percentage rent	350	1,062	1,412	447	36	483
Straight-lining of contractual rent	893	3,331	4,224	264	15,863	16,127
Total rentals	189,061	125,513	314,574	184,013	32,567	216,580
Property operating costs	(63,175)	(46,799)	(109,974)	(60,746)	(10,820)	(71,566)
Property operating income	\$125,886	\$78,714	\$204,600	\$123,267	\$21,747	\$145,014

Same-asset property operating income increased by \$2.6 million in Q4 2013 compared to Q4 2012 in part due to the following:

- An increase of \$4.2 million due to the internalization of the property management.
- An increase of \$2.2 million due to the strengthening of the U.S. dollar compared to the Canadian dollar.
- An increase of \$1.3 million in rentals primarily due to a one-time lease termination payment of \$0.8 million received in Q4 2013.
- A decrease of \$4.0 million in additional rent recoverable from tenants in accordance with their leases for items which were capitalized to building improvements.
- A decrease of \$1.5 million due to management fees no longer being capitalized to leasing expenses.

Property operating income earned from Transactions increased by \$57.0 million in Q4 2013 compared to Q4 2012 primarily due to the REIT acquiring the Primaris portfolio on April 4, 2013 and the delivery of the Bow tranches to EnCana Corporation beginning in May 2012, with the final tranche delivered on March 15, 2013.

(in thousands of Canadian dollars)	Year ended December 31, 2013			Year ended December 31, 2012		
	Same-Asset	Transactions	Total	Same-Asset	Transactions	Total
Rentals	\$729,286	\$371,534	\$1,100,820	\$714,662	\$50,681	\$765,343
Percentage rent	1,280	2,087	3,367	1,154	54	1,208
Straight-lining of contractual rent	1,077	31,753	32,830	1,189	31,419	32,608
Total rentals	731,643	405,374	1,137,017	717,005	82,154	799,159
Property operating costs	(236,323)	(150,772)	(387,095)	(229,876)	(26,838)	(256,714)
Property operating income	\$495,320	\$254,602	\$749,922	\$487,129	\$55,316	\$542,445

Same-asset property operating income increased by \$8.2 million for the year ended December 31, 2013 as compared to the year ended December 31, 2012 in part due to the following:

- An increase of \$9.6 million due to the internalization of the property management.
- An increase of \$4.4 million due to the strengthening of the U.S. dollar compared to the Canadian dollar.
- An increase of \$4.2 million in rentals primarily due to higher sundry income of \$1.7 million.

- A decrease of \$5.7 million in additional rent recoverable from tenants in accordance with their leases for items which were capitalized to building improvements.
- A decrease of \$3.5 million due to management fees no longer being capitalized to leasing expenses in Q3 and Q4 2013.
- A decrease of \$1.6 million in straight-lining of contractual rent after adjusting for one-time smoothing adjustments to one property of \$2.4 million in 2013 and two properties of \$0.8 million in 2012.

Property operating income earned from Transactions increased by \$199.3 million for the year ended December 31, 2013 compared to the year ended December 31, 2012, primarily due to the REIT acquiring the Primaris portfolio on April 4, 2013 and the delivery of the Bow tranches to EnCana Corporation beginning in May 2012, with the final tranche delivered on March 15, 2013.

Refer to the “Segmented Information” section of this MD&A for further details on property operating income.

Included in same-asset property operating income are the following items which although they occur regularly, can be a source of significant variances between different periods:

(in thousands of Canadian dollars)	Three months ended December 31			Year ended December 31		
	2013	2012	Change	2013	2012	Change
Additional recoveries net of capital expenditures	\$1,007	\$5,034	(\$4,027)	\$7,453	\$13,136	(\$5,683)
Adjustment to straight-lining of contractual rent	-	-	-	(2,445)	(843)	(1,602)
Sundry income	846	205	641	2,526	870	1,656
Effect on same-asset - property operating income	\$1,853	\$5,239	(\$3,386)	\$7,534	\$13,163	(\$5,629)

Additional recoveries for capital expenditures vary from period to period as many of the REIT’s properties are single-tenant buildings with triple net leases, which allows for certain items to be recovered from tenants even if the cost of the work is capitalized to investment properties. Sundry income typically includes one-time, non-recurring items such as lease termination payments.

#### Significant Contractual Rental Step-Ups in 2014

The chart below lists the REIT’s contractual rental step-ups greater than \$0.1 million occurring over the next 12 months:

Property	Square Feet	Rent increase (\$ psf)	Effective date of increase	Annualized rental increases (in thousands of dollars)
9330 Amberton Pkwy., Dallas, TX	92,694	\$2.00 <sup>(1)</sup>	January 2014	\$185 <sup>(1)</sup>
1880 Matheson Blvd., E., Mississauga, ON	216,439	1.39	March 2014	301
5 <sup>th</sup> Ave., at Centre St., Calgary, AB	1,997,317	0.32	May 2014	639
100 Metropolitan Rd., Toronto, ON	738,102	0.55	May 2014	406
1501 McKinney, Houston, TX	844,763	1.37 <sup>(1)</sup>	July 2014	1,157 <sup>(1)</sup>
25 Sheppard Ave. W. Toronto, ON	160,437	5.50	July 2014	882
5115 Creekbank Rd., Mississauga, ON	249,118	2.53	July 2014	630
Rona Portfolio (9 properties)	973,484	0.95	November 2014	920

<sup>(1)</sup> Annualized rental increases for properties located in the United States have been disclosed in U.S. dollars.

**SEGMENTED INFORMATION****Operating Segments:**

The Trusts have two operating segments: the H&R portfolio and the Primaris portfolio. The investment policy of the H&R portfolio, which includes office, industrial and mostly single tenanted retail properties in Canadian and the United States, is to lease its properties on a long-term basis to creditworthy tenants. The Primaris portfolio consists of enclosed shopping centres and multi-tenant retail plazas in Canada. These Primaris assets are managed separately from those in the H&R portfolio, and the chief operating decision maker, the CEO, assesses the results of these operations separately. The CEO, primarily measures the performance of investment properties based on property operating income as this is a key indicator of the REIT's performance. Further disclosure of segmented information by operating segment can be found in the Combined Financial Statements of the Trusts.

<b>Property operating income for the three months ended December 31, 2013</b>	<b>H&amp;R Portfolio</b>	<b>Primaris Portfolio</b>	<b>Total per the Combined Financial Statements</b>	<b>Equity accounted investments</b>	<b>The REIT's interests</b>
<i>(in thousands of Canadian dollars)</i>					
Rentals from investment properties	\$233,988	\$80,586	\$314,574	\$24,011	\$338,585
Property operating costs	(77,169)	(32,805)	(109,974)	(8,177)	(118,151)
Property operating income	\$156,819	\$47,781	\$204,600	\$15,834	\$220,434

<b>Property operating income for the year ended December 31, 2013</b>	<b>H&amp;R Portfolio</b>	<b>Primaris Portfolio</b>	<b>Total per the Combined Financial Statements</b>	<b>Equity accounted investments</b>	<b>The REIT's interests</b>
<i>(in thousands of Canadian dollars)</i>					
Rentals from investment properties	\$910,119	\$226,898	\$1,137,017	\$71,123	\$1,208,140
Property operating costs	(293,469)	(93,626)	(387,095)	(28,719)	(415,814)
Property operating income	\$616,650	\$133,272	\$749,922	\$42,404	\$792,326

No comparative segmented disclosure has been provided for the three months or year ended December 31, 2012 as Primaris was acquired on April 4, 2013. Refer to the "Business Combination" section of this MD&A for further information on the Primaris acquisition. Refer to the "Property Operating Income" section of this MD&A for a discussion on the H&R portfolio operating segment.

*Property Operating Income – Primaris portfolio:*

For the three months ended December 31, 2013 and the period from April 4, 2013 to December 31, 2013, Primaris contributed property operating income of \$47.8 million and \$133.3 million, respectively. Included in property operating income for the three months ended December 31, 2013 is \$4.1 million in same-store property operating income which consists of seasonal revenues, including percent rent, common area rent, rental revenue from temporary tenants, and other sundry income items which are typically strongest in the fourth quarter of each year. For the 11 enclosed shopping centres within the Primaris portfolio, sales per square foot, on a same-tenant basis, for Commercial Retail Unit ("CRU"), sales have increased to \$496 per square foot for the twelve months ended December 31, 2013 from \$493 in the comparative period. For the same 11 properties within the Primaris portfolio, the all tenant total sales volume has increased 1.1% and same store sales per square foot increased by 0.6%. These figures below only include enclosed shopping centres owned by Primaris for the entire 24-month period ending December 31, 2013.

	All Store Sales (in thousands of Canadian dollars)			Same Store Sales (per square foot)		
	Rolling 12 month ended December 31			Rolling 12 month ended December 31		
	2013	2012	% Change	2013	2012	% Change
Cataraqui Town Centre	<b>\$88,478</b>	\$87,695	0.9%	<b>\$484</b>	\$492	(1.6%)
Dufferin Mall	<b>96,116</b>	95,594	0.5	<b>544</b>	543	0.2
Grant Park <sup>(1)</sup>	<b>17,870</b>	17,390	2.8	<b>469</b>	504	(6.9)
Northland Village	<b>40,999</b>	41,914	(2.2)	<b>509</b>	505	0.8
Orchard Park Shopping Centre	<b>144,969</b>	134,796	7.5	<b>522</b>	497	5.0
Park Place	<b>81,227</b>	78,621	3.3	<b>491</b>	490	0.2
Place d'Orleans <sup>(2)</sup>	<b>99,011</b>	97,752	1.3	<b>445</b>	432	3.0
Place du Royaume	<b>111,989</b>	113,675	(1.5)	<b>413</b>	421	(1.9)
St. Albert	<b>34,284</b>	34,334	(0.1)	<b>466</b>	457	2.0
Stone Road	<b>108,824</b>	114,918	(5.3)	<b>552</b>	566	(2.5)
Sunridge	<b>105,085</b>	102,192	2.8	<b>568</b>	550	3.3
<b>Total</b>	<b>\$928,852</b>	\$918,881	1.1%	<b>\$496</b>	\$493	0.6%

<sup>(1)</sup> The 2012 sales data includes a one-time corporate sale which is negatively impacting the year over year comparisons. Excluding this tenant's sales, the year over year change in the all store sales volume for this property would have been 10.5% and the same store sales per square foot would have been (1.8%).

<sup>(2)</sup> All store sales and same-store sales have been reported as if Primaris owned 100% of Place d'Orleans for the entire rolling 12 months ended December 31, 2013 and 2012.

<b>Segmented Statement of Financial Position</b> As at December 31, 2013 (in thousands of Canadian dollars)	H&R Portfolio	Primaris Portfolio	Elimination*	<b>Total per the Combined Financial Statements</b>
<b>Total assets</b>	<b>\$11,048,400</b>	<b>\$3,209,492</b>	<b>(\$674,865)</b>	<b>\$13,583,027</b>
<b>Total liabilities</b>	<b>\$6,253,602</b>	<b>\$1,730,489</b>	<b>(\$674,865)</b>	<b>\$7,309,226</b>

\* Elimination of intercompany loans between Primaris and the REIT.

No comparative segmented disclosure has been provided as at December 31, 2012 as Primaris was acquired on April 4, 2013.

**Geographic Segments:**

The Trusts have two geographic segments: Canada and the United States. Property operations for both Canada and the United States share the same investment and operating policies as described above in the "Operating Segments" section of the MD&A.

<b>Property operating income for the three months ended December 31, 2013</b> <b>(in thousands of Canadian dollars)</b>	<b>Canada</b>	<b>United States</b>	<b>Total per the Combined Financial Statements</b>	<b>Canadian equity accounted investments</b>	<b>U.S. equity accounted investments</b>	<b>The REIT's interests</b>
Rentals from investment properties	\$259,458	\$55,116	\$314,574	\$15,461	\$8,550	\$338,585
Property operating costs	(97,406)	(12,568)	(109,974)	(6,976)	(1,201)	(118,151)
<b>Property operating income</b>	<b>\$162,052</b>	<b>\$42,548</b>	<b>\$204,600</b>	<b>\$8,485</b>	<b>\$7,349</b>	<b>\$220,434</b>

<b>Property operating income for the three months ended December 31, 2012</b> <b>(in thousands of Canadian dollars)</b>	<b>Canada</b>	<b>United States</b>	<b>Total per the Combined Financial Statements</b>	<b>Canadian equity accounted investments</b>	<b>U.S. equity accounted investments</b>	<b>The REIT's interests</b>
Rentals from investment properties	\$166,815	\$49,765	\$216,580	\$13,916	\$ -	\$230,496
Property operating costs	(61,402)	(10,164)	(71,566)	(6,105)	-	(77,671)
<b>Property operating income</b>	<b>\$105,413</b>	<b>\$39,601</b>	<b>\$145,014</b>	<b>\$7,811</b>	<b>\$ -</b>	<b>\$152,825</b>

<b>Property operating income for the year ended December 31, 2013</b> <b>(in thousands of Canadian dollars)</b>	<b>Canada</b>	<b>United States</b>	<b>Total per the Combined Financial Statements</b>	<b>Canadian equity accounted investments</b>	<b>U.S. equity accounted investments</b>	<b>The REIT's interests</b>
Rentals from investment properties	\$925,236	\$211,781	\$1,137,017	\$58,624	\$12,499	\$1,208,140
Property operating costs	(341,412)	(45,683)	(387,095)	(26,035)	(2,684)	(415,814)
<b>Property operating income</b>	<b>\$583,824</b>	<b>\$166,098</b>	<b>\$749,922</b>	<b>\$32,589</b>	<b>\$9,815</b>	<b>\$792,326</b>

<b>Property operating income for the year ended December 31, 2012</b> <b>(in thousands of Canadian dollars)</b>	<b>Canada</b>	<b>United States</b>	<b>Total per the Combined Financial Statements</b>	<b>Canadian equity accounted investments</b>	<b>U.S. equity accounted investments</b>	<b>The REIT's interests</b>
Rentals from investment properties	\$595,680	\$203,479	\$799,159	\$36,144	\$ -	\$835,303
Property operating costs	(214,962)	(41,752)	(256,714)	(15,848)	-	(272,562)
<b>Property operating income</b>	<b>\$380,718</b>	<b>\$161,727</b>	<b>\$542,445</b>	<b>\$20,296</b>	<b>\$ -</b>	<b>\$562,741</b>

Had the property operating income for wholly owned properties located in the United States been shown in U.S. dollars and excluded: (i) the acquisitions during 2012 and 2013, (ii) the property operating income from those properties which have been sold or are held for sale, and (iii) the management fees saved as a result of the REIT internalizing its property management, the adjusted property operating income would have been \$37.6 million for the three months ended December 31, 2013 as compared to \$38.1 million for the three months ended December 31, 2012 and the adjusted property operating income would have been \$152.9 million for the year ended December 31, 2013 as compared to \$152.7 million for the year ended December 31, 2012.

**OTHER INCOME AND EXPENSE ITEMS**

The other income and expense items section of this MD&A provides management commentary on certain items of the Trusts' combined statements of comprehensive income, including net income from equity accounted investments, finance cost – operations, finance cost - gain (loss) on change in fair value, trust expenses, unit-based compensation, amortization, fair value adjustment on real estate assets, loss on sale of real estate assets, gain (loss) on foreign exchange, transaction costs and income taxes expense.

**Net Income, FFO and AFFO from Equity Accounted Investments\***

(in thousands of Canadian dollars)	Three months ended December 31			Year ended December 31		
	2013	2012	Change	2013	2012	Change
Rentals from investment properties	\$24,011	\$13,916	\$10,095	\$71,123	\$36,144	\$34,979
Property operating costs	(8,177)	(6,105)	(2,072)	(28,719)	(15,848)	(12,871)
Net loss from equity accounted investments	(191)	-	(191)	(199)	-	(199)
Finance income	36	7	29	75	18	57
Finance costs - operations	(4,796)	(2,563)	(2,233)	(13,197)	(6,960)	(6,237)
Loss on change in fair value	-	-	-	-	(2,593)	2,593
Trust expenses	220	-	220	134	-	134
Amortization	(257)	-	(257)	(309)	-	(309)
Fair value adjustment on real estate assets	8,336	153	8,183	5,158	15,412	(10,254)
Income tax expense	(19)	-	(19)	(34)	-	(34)
<b>Net income from equity accounted investments</b>	<b>19,163</b>	<b>5,408</b>	<b>13,755</b>	<b>34,032</b>	<b>26,173</b>	<b>7,859</b>
Loss on change in fair value	-	-	-	-	2,593	(2,593)
Amortization	257	-	257	309	-	309
Fair value adjustment on real estate assets	(8,336)	(153)	(8,183)	(5,158)	(15,412)	10,254
<b>FFO from equity accounted investments</b>	<b>11,084</b>	<b>5,255</b>	<b>5,829</b>	<b>29,183</b>	<b>13,354</b>	<b>15,829</b>
Straight-lining of contractual rent	16	(29)	45	(476)	144	(620)
Rent amortization of tenant inducements	236	2	234	321	2	319
Effective interest rate accretion	(355)	82	(437)	(238)	234	(472)
Capital expenditures	(2,100)	(113)	(1,987)	(4,449)	(113)	(4,336)
Tenant expenditures	(535)	(209)	(326)	(860)	(209)	(651)
<b>AFFO from equity accounted investments</b>	<b>\$8,346</b>	<b>\$4,988</b>	<b>\$3,358</b>	<b>\$23,481</b>	<b>\$13,412</b>	<b>\$10,069</b>

\* These amounts are at the REIT's proportionate ownership share held through their equity accounted investments.

Net income from equity accounted investments for the three months and year ended December 31, 2013 compared to the respective 2012 periods, increased by \$13.8 million and \$7.9 million, primarily due to an increase in property operating income as a result of the acquisition of a one-third interest in Scotia Plaza in June 2012, a one-third interest in 100 Yonge St. in June 2013 and a 33.7% interest in ECHO in August 2013. ECHO reports its financial results to the REIT one month in arrears due to time constraints on their reporting. Therefore, the above amounts include ECHO's financial information from acquisition to November 30, 2013. The loss on change in fair value for the year ended December 31, 2012 includes a loss of \$2.6 million upon termination of an interest rate swap in anticipation of issuing bonds relating to Scotia Plaza.

<b>Finance Cost - Operations</b> <b>(in thousands of Canadian dollars)</b>	Three months ended December 31			Year ended December 31		
	2013	2012	Change	2013	2012	Change
Contractual interest on mortgages payable	\$60,161	\$49,125	\$11,036	\$230,416	\$193,868	\$36,548
Contractual interest on debentures payable	16,793	14,993	1,800	61,701	62,815	(1,114)
Interest on construction loans	-	993	(993)	144	6,766	(6,622)
Effective interest rate accretion	(1,161)	544	(1,705)	(4,176)	1,323	(5,499)
Bank interest and charges	2,139	1,003	1,136	8,109	5,480	2,629
Exchangeable unit distributions	5,875	1,699	4,176	13,967	6,389	7,578
	83,807	68,357	15,450	310,161	276,641	33,520
Capitalized interest	-	(4,327)	4,327	(532)	(44,146)	43,614
Finance cost - operations	\$83,807	\$64,030	\$19,777	\$309,629	\$232,495	\$77,134

Included in contractual interest on mortgages payable for the three months and year ended December 31, 2013 is \$10.0 million and \$32.4 million, respectively, relating to mortgage interest on the Primaris properties acquired by the REIT in Q2 2013. The remaining increase for the year ended December 31, 2013 compared to the year ended December 31, 2012 is primarily due to mortgages and bonds issued during 2012 and 2013.

The increase in contractual interest on debentures payable of \$1.8 million for three months ended December 31, 2013 compared to the respective 2012 period is primarily due to the issuance of the Series G, Series H and Series I senior debentures, as well as the assumption of the 2018 convertible debentures from Primaris. This was offset by the redemption of the 2017 convertible debentures. The decrease in contractual interest on debentures payable of \$1.1 million for the year ended December 31, 2013 compared to the respective 2012 period is primarily due to the redemption of the 2013, 2014 and 2017 convertible debentures, offset by the issuance of the Series F, Series G, Series H and Series I senior debentures, as well as the assumption of the 2018 convertible debentures from Primaris.

Interest on construction loans and the amount of capitalized interest decreased for the three months and year ended December 31, 2013 as compared to the respective 2012 periods as the development of the Bow was substantially completed and delivered to Encana Corporation in tranches throughout 2012 and Q1 2013. As each tranche was completed, interest was no longer capitalized on that particular tranche. On March 15, 2013, the final floors were delivered to Encana Corporation and interest capitalization on the project ceased completely.

Exchangeable unit distributions increased by \$4.2 million and \$7.6 million for the three months and year ended December 31, 2013 compared to the respective 2012 periods primarily due to the exchangeable units assumed as part of the acquisition of Primaris in April 2013 and the issuance of exchangeable units as part of the property management internalization in July 2013. The exchangeable unit distributions relating to the property management internalization for July and August 2013 were included in transaction costs as these units were issued on September 3, 2013.

<b>Finance Cost – Gain (Loss) on Change in Fair Value</b> <b>(in thousands of Canadian dollars)</b>	Three months ended December 31			Year ended December 31		
	2013	2012	Change	2013	2012	Change
Gain (loss) on fair value of convertible debentures	(\$1,191)	\$11,868	(\$13,059)	\$22,378	\$4,696	\$17,682
Gain (loss) on fair value of exchangeable units	(3,657)	5,927	(9,584)	10,210	(4,350)	14,560
Net loss on derivative instruments	(668)	(65)	(603)	(1,616)	(5,489)	3,873
Finance cost - gain (loss) on change in fair value	(\$5,516)	\$17,730	(\$23,246)	\$30,972	(\$5,143)	\$36,115

The REIT has elected to measure the outstanding convertible debentures at fair value. The REIT uses the quoted prices on the TSX to determine the fair value of each series of convertible debentures as permitted under IFRS 13, *Fair Value Measurement*. The fluctuation in fair value between each period is recorded as a gain (loss) in changes in fair values in comprehensive income.



Under IFRS, the exchangeable units are considered puttable instruments which are valued and classified as a financial liability. The gain (loss) on fair value of exchangeable units is due to the change in the exchangeable unit fair value during the respective quarter. At the end of each quarter, the fair value of each exchangeable unit is measured based on the quoted prices of the Stapled Units on the TSX. For the three months and year ended December 31, 2013, the change in fair value is based on the quoted price of Stapled Units which was \$21.40 as at December 31, 2013 (September 30, 2013 - \$21.19, December 31, 2012 - \$24.10). For the three months and year ended December 31, 2012, the change in fair value is based on the quoted price of Stapled Units which was \$24.10 as at December 31, 2012 (September 30, 2012 - \$25.19, December 31, 2011 - \$23.30).

The change in the fair value of the derivative instruments for the three months and year ended December 31, 2013 compared to the respective 2012 periods of (\$0.6 million) and \$3.9 million, is primarily due to the following: (i) a decrease of \$0.6 million and \$7.4 million for the three months and year ended December 31, 2013 compared to the respective 2012 periods due to the REIT entering into interest rate swaps and forward exchange forward contracts which are marked-to-market at the end of each quarter; (ii) a realized loss of \$6.9 million for the year ended December 31, 2012 upon termination of an interest rate swap in anticipation of refinancing a new mortgage for an office property and (iii) a realized loss of \$4.4 million for the year ended December 31, 2012 upon termination of an interest rate swap in anticipation of issuing the Series A and B Bow bonds. Refer to the "Derivative Instruments" table under "Liabilities" for a financial summary of all derivative instruments held by the REIT.

<b>Trust Expenses</b> <b>(in thousands of Canadian dollars)</b>	Three months ended December 31			Year ended December 31		
	2013	2012	Change	2013	2012	Change
Other expenses	\$2,970	\$2,169	\$801	\$9,700	\$9,098	\$602
Unit-based compensation - as reported under IFRS	300	(509)	809	(4,136)	6,122	(10,258)
Trust expenses	\$3,270	\$1,660	\$1,610	\$5,564	\$15,220	(\$9,656)

Other expenses are primarily comprised of salaries, professional fees, trustee fees and corporate overhead expenses. Included in trust expenses are amounts relating to: (i) the Primaris portfolio of \$0.7 million and \$1.4 million, respectively, for the three months and year ended December 31, 2013 (December 31, 2012 - nil), which consists of total costs of \$4.5 million and \$12.5 million, offset by property management fees and other charges to properties of \$3.8 million and \$11.1 million; and (ii) tax planning and reorganization costs of nil for the three months ended December 31, 2013 (December 31, 2012 - \$0.1 million) and \$0.1 million for the year ended December 31, 2013 (December 31, 2012 - \$1.1 million).

The REIT's Unit Option Plan is considered to be cash-settled under IFRS 2, *Share-based Payments* and as a result, is measured at each reporting period and settlement date at its fair value as defined by IFRS 2. The impact of the fair value adjustment to unit-based compensation is as follows:

<b>Unit-based Compensation</b> <b>(in thousands of Canadian dollars)</b>	Three months ended December 31			Year ended December 31		
	2013	2012	Change	2013	2012	Change
Unit-based compensation	\$770	\$804	(\$34)	\$2,601	\$3,128	(\$527)
Fair value adjustment to unit-based compensation	(470)	(1,313)	843	(6,737)	2,994	(9,731)
Unit-based compensation - as reported under IFRS	\$300	(\$509)	\$809	(\$4,136)	\$6,122	(\$10,258)

The fair value adjustment to unit-based compensation is measured based on the quoted price of the Stapled Units compared to the exercise price of each option on the date of grant. The quoted price of Stapled Units was \$21.40 as at December 31, 2013 (December 31, 2012 - \$24.10).

<b>Amortization</b> <b>(in thousands of Canadian dollars)</b>	Three months ended December 31			Year ended December 31		
	2013	2012	Change	2013	2012	Change
Amortization of leasing expenses	\$1,949	\$1,437	\$512	\$7,121	\$5,525	\$1,596
Amortization of leasehold improvements	140	-	140	415	-	415
Amortization	\$2,089	\$1,437	\$652	\$7,536	\$5,525	\$2,011

Leasing expenses are primarily comprised of commissions and other leasing costs which are deferred and amortized on a straight-line basis over the terms of the related leases.

<b>Fair Value Adjustment on Real Estate Assets</b> <b>(in thousands of Canadian dollars)</b>	Three months ended December 31			Year ended December 31		
	2013	2012	Change	2013	2012	Change
Fair value adjustment on real estate assets	(\$10,570)	\$30,499	(\$41,069)	\$51,872	\$237,689	(\$185,817)

The REIT records its real estate assets at fair value. The decrease of \$41.1 million and \$185.8 million for the three months and year ended December 31, 2013 compared to the respective 2012 periods is due to changes in market assumptions used in the property valuations from quarter to quarter. Refer to note 4 in the December 31, 2013 Combined Financial Statements for further details on the valuation of the portfolio.

<b>Loss on Sale of Real Estate Assets</b> <b>(in thousands of Canadian dollars)</b>	Three months ended December 31			Year ended December 31		
	2013	2012	Change	2013	2012	Change
Loss on sale of real estate assets	(\$204)	(\$1,080)	\$876	(\$2,067)	(\$137)	(\$1,930)

The loss on sale of real estate assets for the year ended December 31, 2013 is primarily due to commissions and other transaction costs incurred in selling several of the REIT's properties. Refer to the "2013 Dispositions" table in the "Assets" section of this MD&A for a list of properties sold by the REIT in 2013.

<b>Gain (Loss) on Foreign Exchange</b> <b>(in thousands of Canadian dollars)</b>	Three months ended December 31			Year ended December 31		
	2013	2012	Change	2013	2012	Change
Gain (loss) on foreign exchange	\$6,772	\$1,535	\$5,237	\$14,042	(\$7,007)	\$21,049

The gain (loss) on foreign exchange is made up of the following items:

- (i) A foreign exchange gain (loss) of \$6.8 million for the three months ended December 31, 2013 (Q4 2012 - \$1.5 million) and \$14.0 million for the year ended December 31, 2013 (December 31, 2012 - (\$4.5 million)) which was recorded by Finance Trust due to the translation of the U.S. Holdco Notes into Canadian dollars. The U.S. Holdco Notes are eliminated in the Combined Financial Statements however, the related foreign exchange difference is not eliminated on combination as it flows through net income of Finance Trust and other comprehensive income (loss) of the REIT. This is because U.S. Holdco is a subsidiary of the REIT and forms part of its net investment in the United States. U.S. Holdco is not a subsidiary of Finance Trust.
- (ii) The REIT loaned U.S. Holdco \$250.0 million on December 22, 2011 for the acquisition of Hess Tower in Houston, TX ,which was repaid on January 23, 2012. The loss represents a change in the foreign exchange rates between these dates. For accounting purposes this resulted in a foreign exchange loss of \$2.5 million for the year ended December 31, 2012. The REIT had entered into a foreign exchange forward contract which, on a cash basis, resulted in no gain or loss.

<b>Transaction Costs</b> <b>(in thousands of Canadian dollars)</b>	Three months ended December 31			Year ended December 31		
	2013	2012	Change	2013	2012	Change
Transaction costs on business combination	\$ -	\$ -	\$ -	\$6,605	\$ -	\$6,605
Transaction costs on property management internalization	-	-	-	198,214	-	198,214
Transaction costs	\$ -	\$ -	\$ -	\$204,819	\$ -	\$204,819

As a result of the acquisition of Primaris, which was accounted for as a business combination, for the year ended December 31, 2013, the REIT incurred \$6.6 million in transaction costs relating to this acquisition which were expensed as incurred.

During the year ended December 31, 2013, HRRMSLP acquired HRP's REIT-related property management business in return for 9.5 million limited partnership units of that subsidiary, which are exchangeable on a one-for-one basis for Stapled Units. The limited partnership units of the REIT's subsidiary were issued on September 3, 2013 at a quoted price of \$20.51 for a total value of \$194.8 million. Since the internalization transaction was effective July 1, 2013, exchangeable unit distributions on these limited partnership units for the months of July and August totalling \$2.1 million have been included in transaction costs. The remaining \$1.3 million of transaction costs in connection with the internalization transaction relate to professional fees.

<b>Income Tax Expense</b> <b>(in thousands of Canadian dollars)</b>	Three months ended December 31			Year ended December 31		
	2013	2012	Change	2013	2012	Change
Current income taxes	\$19	\$94	(\$75)	\$471	\$518	(\$47)
Deferred income taxes	11,623	29,607	(17,984)	29,227	43,407	(14,180)
Total income taxes	\$11,642	\$29,701	(\$18,059)	\$29,698	\$43,925	(\$14,227)

The REIT is generally subject to tax in Canada under the Tax Act with respect to its taxable income each year, except to the extent such taxable income is paid or made payable to unitholders and deducted by the REIT for tax purposes. The REIT's current income tax expense is primarily due to U.S. state taxes.

The REIT's deferred income tax expense is recorded in respect of U.S. Holdco and arose due to taxable temporary differences between the tax and accounting bases of assets and liabilities net of the benefit of unused tax credits, deferred interest deductions and losses that are available to be carried forward to future tax years to the extent that it is probable that the unused tax credits, deferred interest deductions and losses can be realized.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply when the assets are realized or the liabilities are settled, based on the tax laws that have been enacted or substantively enacted at the statement of financial position date. Deferred income tax relating to items recognized in equity will also be recognized in equity.

As at December 31, 2013, the REIT had net deferred tax liabilities of \$76.6 million (December 31, 2012 - \$43.4 million) primarily related to taxable temporary differences between the tax and accounting bases of U.S. investment properties.

**ASSETS****Real Estate Assets**

The following table below shows the change in real estate assets for the years ended December 31, 2013 and December 31, 2012 per the Combined Financial Statements:

	December 31, 2013		December 31, 2012	
	Investment Properties	Properties Under Development	Investment Properties*	Properties Under Development
Opening balance, beginning of year	\$9,235,562	\$128,220	\$7,094,147	\$1,721,743
Acquisitions of investment properties, including transaction costs	3,179,418	-	298,364	-
Acquisition of investment properties through business combination	211,360	-	-	-
Additions to existing investment properties:				
Capital expenditures	33,704	-	19,850	-
Direct leasing costs	18,799	-	14,022	-
Redevelopment	52,196	-	-	-
Additions to properties under development	-	22,631	-	196,288
Dispositions	(183,433)	(4,373)	(133,153)	(17,824)
Transfer of investment properties to assets classified as held for sale	-	-	(27,800)	-
Amortization of leasing costs, straight-line rents and blend and extend rents included in revenue	31,003	-	(4,573)	29,673
Transfer of property under development that has reached practical completion to investment properties	-	-	1,747,966	(1,747,966)
Change in foreign exchange	155,724	-	(64,644)	-
Fair value adjustment on real estate assets	51,872	-	291,383	(53,694)
Closing balance, end of year	\$12,786,205	\$146,478	\$9,235,562	\$128,220

\* These amounts have been restated for the effect of change in accounting policy for equity accounted investments.

Legal title to each of the properties in the United States is held by a separate legal entity which is 100% owned, directly or indirectly, by U.S. Holdco, a wholly owned subsidiary of the REIT. The assets of each such separate entity are not available to satisfy the debts or obligations of any other person or entity. Each such separate entity maintains separate books and records. The identity of the owner of a particular United States property is available from U.S. Holdco. This structure does not prevent distributions to U.S. entity owners provided there are no conditions of default.

**2013 Acquisitions**

In addition to Primaris, the REIT acquired five retail properties and two equity accounted investments shown in the table below. The REIT also acquired a parcel of land adjacent to an existing investment property for \$0.5 million during the year ended December 31, 2013. There were 11 properties and one equity accounted investment acquired during the year ended December 31, 2012.

Property/Acquisition	Year Built	Property Type	Date Acquired	Square Footage	Cash Purchase Price (\$ Millions)	Anchor/Major Tenants	Average Remaining Lease Term (years) <sup>(1)</sup>
100 Yonge St., Toronto, ON <sup>(2)</sup>	1989	H&R - Office	June 26, 2013	80,762	26.8	Bank of Nova Scotia	7.3
463855 State Rd., 200, Yulee, FL	2012	H&R - Retail	June 27, 2013	174,733	22.0	Publix, Kohl's T.J. Maxx, Ross Dress for Less	13.1
9713 Hardin St., Fort McMurray, AB (Peter Pond Mall)	1978/2013	Primaris - Retail	July 3, 2013	200,486	168.5	Sport Chek, Boomtown Casino, Atmosphere	7.3
Echo Portfolio <sup>(2)</sup>	-	H&R - Retail	Aug 1, 2013	2,436,452	305.3 <sup>(3)</sup>	Giant Eagle Inc.	12.9
500 Hwy. 118 W. & 100/150 Muskoka Rd. 118 W., Bracebridge, ON <sup>(2)</sup>	1989/1998	H&R - Retail	Dec 17, 2013	30,465	5.7	Bank of Montreal, Dollarama	4.6
505 Hwy. 118 W., Bracebridge, ON <sup>(2)</sup>	1988/2001	H&R - Retail	Dec 17, 2013	66,109	6.2	Metro, The Beer Store	2.6
555 Rossland Rd. E., Oshawa, ON <sup>(2)</sup>	1975	H&R - Retail	Dec 17, 2013	27,975	7.2	Metro, Shoppers Drug Mart, LCBO	3.7
<b>Total</b>				<b>3,016,982</b>	<b>541.7</b>		

<sup>(1)</sup> Average remaining lease term is based on net rent at the time of acquisition.

<sup>(2)</sup> Square feet and cash purchase price is based on the REIT's interests.

<sup>(3)</sup> One-third of this purchase price was paid on closing, with a further one-third payable 18 months from closing and the balance payable in 30 months from closing, except under certain circumstances when the loan would be payable on demand.

**2013 Dispositions:**

The REIT sold three industrial properties, two office properties, two retail properties (of which one sale was for the disposal of a 50% ownership interest in the property), a portion of an office property (sold as separate condominium units) and a parcel of land held for development during the year ended December 31, 2013. The REIT sold three industrial properties, four retail properties, a portion of an office property (sold as separate condominium units) and a parcel of land held for development during the year ended December 31, 2012.

Property	Property Type	Date Sold	Square Feet	Gross Proceeds (\$ Millions)	Ownership Interest Disposed
1330 Martin Grove Rd., Toronto, ON	H&R - Industrial	Jan 23, 2013	162,775	\$12.2	100%
351 Passmore Ave., Scarborough, ON	H&R - Industrial	Jan 31, 2013	161,137	8.3	100%
R.R. #1, Mile 295, Alaska Hwy., Fort Nelson, BC	H&R - Industrial	Mar 8, 2013	12,399	1.5	100%
295 The West Mall, Etobicoke, ON	H&R - Office	Mar 19, 2013	90,718	15.5	100%
200 Franklin Blvd., Cambridge, ON	Primaris Retail	April 5, 2013	190,061	35.0	100%
1235 Bay St., Toronto, ON	H&R - Office	Apr 11, 2013	97,020	25.0	100%
2800 Skymark Ave., Mississauga, ON	H&R - Office	May and Sep 2013	12,592	1.8	100%
110 Place d'Orleans Dr., Orleans, ON <sup>(1)</sup>	Primaris Retail	Aug 19, 2013	377,459	110.6	50%
Block 1, Plan 43M-1939 - 7900 Airport Rd., Brampton, ON <sup>(2)</sup>	Development	Dec 24, 2013	-	4.7	100%
<b>Total</b>			<b>1,104,161</b>	<b>\$214.6</b>	

<sup>(1)</sup> Square feet and cash sales price is based on the REIT's interest.

<sup>(2)</sup> Approximately 5.8 acres of land held for development was sold.

The following tables below disclose the fair values of the REIT's investment properties by asset and region, excluding assets held for sale:

<b>Type of Asset (millions)</b>	<b>Fair Value December 31, 2013<sup>(1)</sup></b>	<b>Fair Value December 31, 2012<sup>(1)</sup></b>
Office	\$6,881	\$6,576
Retail	5,200	1,501
Industrial	1,749	1,730
Total portfolio	13,830	9,807
Less: Trusts' interests of fair value of investment properties included in equity accounted investments	(1,044)	(571)
Fair value of investment properties per the Combined Financial Statements	<b>\$12,786</b>	<b>\$9,236</b>

<b>Region (millions)</b>	<b>Fair Value December 31, 2013<sup>(1)</sup></b>	<b>Fair Value December 31, 2012<sup>(1)</sup></b>
Ontario	\$4,879	\$3,867
Alberta	4,234	2,871
Quebec	594	366
Other	1,294	514
Canada	11,001	7,618
United States	2,829	2,189
Total portfolio	13,830	9,807
Less: Trusts' interests of fair value of investment properties included in equity accounted investments	(1,044)	(571)
Fair value of investment properties per the Combined Financial Statements	<b>\$12,786</b>	<b>\$9,236</b>

(1) Please refer to note 4 of the Combined Financial Statements for the assumptions and methods used in measuring the fair value of the portfolio.

Significant costs associated with investment properties, including those accounted for as equity accounted investments, are either capitalized or expensed in the year incurred. The REIT currently expects to incur the following costs over the next two years.

### **Business Combination**

On April 4, 2013, pursuant to a statutory plan of arrangement, the REIT acquired 100% of Primaris in exchange for the issuance of 62.5 million Stapled Units at a fair value of \$23.01 per Stapled Unit, which was the published closing share price on April 3, 2013, for an aggregate total of \$1.4 billion. The REIT acquired Primaris to further diversify its existing portfolio to include Canadian enclosed shopping centres. The Primaris portfolio consisted of 26 properties. The transaction costs relating to the acquisition of Primaris were \$6.6 million; these costs were expensed in the period incurred as transaction costs.

The following are the recognized amounts of identifiable assets acquired and liabilities assumed, measured at their respective fair values on the date of acquisition:

Investment properties	\$3,179,418
Cash and cash equivalents	45,108
Net working capital	(94,200)
Debentures payable <sup>(1)</sup>	(94,661)
Mortgages payable	(1,415,575)
Bank indebtedness	(125,000)
Exchangeable units <sup>(2)</sup>	(56,940)
Restricted cash	789
<b>Fair value of consideration</b>	<b>\$1,438,939</b>

	<u>Face Value</u>	<u>Fair Value</u>
(1) 2014 <sup>b</sup> Convertible Debentures (HR.DB.F)	\$1.2 million	\$2.7 million
2015 Convertible Debentures (HR.DB.G)	7.7 million	12.5 million
2018 Convertible Debentures (HR.DB.H)	<u>75.0 million</u>	<u>79.5 million</u>
	<u>\$83.9 million</u>	<u>\$94.7 million</u>

In May 2013, the REIT redeemed all of the remaining outstanding 2014<sup>b</sup> and 2015 Convertible Debentures.

(2) The REIT assumed 2.1 million exchangeable units of certain subsidiaries of Primaris for exchangeable units of the REIT, which became exchangeable into approximately 2.5 million Stapled Units.

During the three months ended December 31, 2013, the REIT recognized \$80.6 million of revenue and \$38.7 million of comprehensive income, before fair value adjustments, related to the acquisition of Primaris. During the year ended December 31, 2013, the REIT recognized \$226.9 million of revenue and \$94.1 million of comprehensive income, before fair value adjustments, related to the acquisition of Primaris.

**Equity Accounted Investments\***  
(in thousands of Canadian dollars)

	December 31, 2013	December 31, 2012
Investment properties	<b>\$1,043,306</b>	\$571,500
Properties under development	<b>15,079</b>	-
Other assets	<b>15,092</b>	604
Cash and cash equivalents	<b>8,649</b>	3,010
<b>Total assets</b>	<b>1,082,126</b>	575,114
Mortgages payable	<b>(456,401)</b>	(282,302)
Bank indebtedness	<b>(28,465)</b>	-
Accounts payable and accrued liabilities	<b>(30,842)</b>	(16,455)
Non-controlling interest	<b>(8,269)</b>	-
<b>Equity accounted investments</b>	<b>\$558,149</b>	\$276,357

\* These amounts are at the REIT's proportionate ownership share of their equity accounted investments.

**Mortgages and Amount Receivable**

The mortgage receivable of \$7.0 million outstanding at December 31, 2012 was repaid in 2013 and the REIT granted another mortgage receivable of \$9.7 million on the sale of 295 The West Mall which is due in April 2015.

**Assets Classified as Held For Sale**

As at December 31, 2013, there were no properties held for sale (December 31, 2012 - two properties: 1330 Martin Grove Ave., Toronto, ON and 295 The West Mall, Etobicoke, ON with a total fair value of \$27.8 million).

**Other Assets**

<b>(in thousands of Canadian dollars)</b>	<b>December 31, 2013</b>	December 31, 2012
Restricted cash	<b>\$10,623</b>	\$40,347
Accounts receivable	<b>15,719</b>	16,733
Prepaid expenses and sundry assets	<b>28,282</b>	7,759
Derivative instruments	<b>-</b>	1,679
Other assets	<b>\$54,624</b>	\$66,518

Restricted cash decreased from \$40.3 million as at December 31, 2012 to \$10.6 million as at December 31, 2013 primarily due to funds released from escrow for a new mortgage that closed on December 28, 2012 with funds received on January 2, 2013 and a full release of the remaining funds held in escrow relating to the Bow bonds during Q2 2013.

Prepaid expenses and sundry assets increased from \$7.8 million as at December 31, 2012 to \$28.3 million as at December 31, 2013. Included in prepaid expenses and sundry assets as at December 31, 2013 is \$10.3 million relating to the Primaris portfolio which mainly consists of prepaid realty taxes, leasehold improvements and other sundry assets. The remaining increase is primarily due to deposits and mortgage application fees on several properties and other sundry assets.

Derivative instruments in asset and liability positions are not presented on a net basis. Refer to the "Derivative Instruments" table under "Liabilities" for a summary of all derivative instruments held by the REIT.

**LIABILITIES**

The REIT's Declaration of Trust limits the indebtedness of the REIT (subject to certain exceptions) to a maximum of 65% of the total assets of the REIT. All ratios in the table below are non-GAAP measures.

	<b>December 31, 2013</b>	December 31, 2012
Debt to total assets per the Combined Financial Statements	<b>49.2%</b>	50.3%
Debt to total assets per the Trusts' Interests	<b>50.8%</b>	51.6%
Non-recourse mortgages as a percentage of total mortgages*	<b>62.9%</b>	70.9%
Floating rate debt as a percentage of total debt*	<b>6.1%</b>	0.1%
Canadian properties total debt to fair market value of total Canadian assets*	<b>49.5%</b>	50.2%
U.S. properties total debt to fair market value of total U.S. assets*	<b>55.7%</b>	56.8%

\* Presented per the Trusts' Interests



**Mortgages Payable**

The following table shows the change in mortgages payable from December 31, 2012 to December 31, 2013:

*(in thousands of Canadian dollars)*

Opening balance - December 31, 2012	\$3,813,613
Principal repayments	(145,515)
Mortgages repaid upon maturity	(490,599)
Assumed mortgages from business combination	1,415,575
New mortgages	301,877
Mortgages released on the sale of investment properties	(79,569)
Effective interest rate accretion on mortgages	(7,427)
Foreign exchange difference	89,771
<b>Closing balance – December 31, 2013</b>	<b>\$4,897,726</b>

The following table discloses the REIT's mortgage payable balance, adjusted to include debt related to equity accounted investments at the REIT's interests:

	December 31, 2013	December 31, 2012
Mortgages payable per the Combined Financial Statements	<b>\$4,897,726</b>	\$3,813,613
Add: REIT's interests of mortgages payable related to equity accounted investments	<b>456,401</b>	282,302
<b>Total mortgages payable</b>	<b>\$5,354,127</b>	\$4,095,915

The following table below shows the REIT's 5-year mortgage maturity profile as at December 31, 2013 and includes the REIT's interests of mortgages related to equity accounted investments:

<b>MORTGAGES PAYABLE</b>	Periodic Amortized Principal (\$000's)	Principal on Maturity (\$000's)	Total Principal <sup>(1)</sup> (\$000's)	% of Total Principal	Weighted Average Interest Rate on Maturity
2014	\$173,576	\$178,916	\$352,492	6.6%	6.1%
2015	177,052	310,672	487,724	9.2%	5.3%
2016	173,958	307,378	481,336	9.1%	5.4%
2017	168,718	466,605	635,323	11.9%	4.8%
2018	164,088	117,519	281,607	5.3%	5.4%
Thereafter			3,078,825	57.9%	
			5,317,307	100%	
Financing costs and mark-to-market adjustment arising on acquisitions <sup>(1)</sup>			36,820		
<b>Total</b>			<b>\$5,354,127</b>		

<sup>(1)</sup> Mark-to-market adjustment represents the difference between the actual mortgages assumed on property acquisitions and the fair value of the mortgages at the date of purchase and is recognized in finance cost over the life of the applicable mortgage using the effective interest rate method. Financing costs are deducted from the REIT's mortgages payable balances and are recognized in finance costs over the life of the applicable mortgage.

The mortgages outstanding as at December 31, 2013 bear interest at a weighted average rate of 4.9% (December 31, 2012 - 5.1%) and mature between 2014 and 2035. The weighted average term to maturity of the REIT's mortgages is 7.0 years (December 31, 2012 - 7.7 years). For a further discussion of liquidity please see "Funding of Future Commitments". For a further discussion of interest rate risk, please see "Risks and Uncertainties".

Debt related to certain Canadian properties is held by separate legal entities, where the rent received from each property is first used to satisfy the related debt obligations with any balance then available to satisfy the cash flow requirements of the REIT.

H&R REIT AND H&R FINANCE TRUST - MD&A - December 31, 2013

<b>Debentures Payable</b>						<b>December 31, 2013</b>	<b>December 31, 2012</b>
	<b>Maturity</b>	<b>Contractual Interest Rate</b>	<b>Effective Interest Rate</b>	<b>Conversion Price</b>	<b>Face Value (in \$ millions)</b>	<b>Carrying Value (in \$ millions)</b>	<b>Carrying Value (in \$ millions)</b>
<b>Convertible Debentures</b>							
2016 Convertible Debentures (HR.DB.E)	Dec 31, 2016	4.50%	4.50%	\$25.70	\$75.0	<b>\$77.3</b>	\$77.3
2018 Convertible Debentures (HR.DB.H)	Nov 30, 2018	5.40%	5.40%	\$24.73	74.4	<b>78.5</b>	-
2020 Convertible Debentures (HR.DB.D)	Jun 30, 2020	5.90%	5.90%	\$23.50	99.7	<b>104.1</b>	109.9
2017 Convertible Debentures (HR.DB.C)	(1)	6.00%	6.00%	\$19.00	-	<b>-</b>	213.3
					249.1	<b>259.9</b>	400.5
<b>Senior Debentures</b>							
Series A Senior Debentures	Feb 3, 2015	5.20%	5.40%	n/a	115.0	<b>114.8</b>	114.5
Series H Senior Debentures	Oct 9, 2015	(2)	(2)	n/a	235.0	<b>234.3</b>	-
Series D Senior Debentures	Jul 27, 2016	4.78%	4.96%	n/a	180.0	<b>179.3</b>	179.0
Series I Senior Debentures	Jan 23, 2017	(3)	(3)	n/a	60.0	<b>59.7</b>	-
Series B Senior Debentures	Feb 3, 2017	5.90%	6.06%	n/a	115.0	<b>114.5</b>	114.3
Series E Senior Debentures	Feb 2, 2018	4.90%	5.22%	n/a	100.0	<b>99.0</b>	98.8
Series G Senior Debentures	Jun 20, 2018	3.34%	3.54%	n/a	175.0	<b>173.5</b>	-
Series C Senior Debentures	Dec 1, 2018	5.00%	5.30%	n/a	125.0	<b>123.4</b>	123.1
Series F Senior Debentures	Mar 2, 2020	4.45%	4.63%	n/a	175.0	<b>173.7</b>	173.6
					1,280.0	<b>1,272.2</b>	803.3
<b>Total</b>					<b>\$1,529.1</b>	<b>\$1,532.1</b>	<b>\$1,203.8</b>

(1) In July 2013, the REIT redeemed all of the remaining outstanding 2017 Convertible Debentures.

(2) Bears interest at a rate equal to 3-month Canadian Dealer Offered Rate plus 150 basis points. The interest rate for the period from October 9, 2013 to January 8, 2014 was 2.775%.

(3) Bears interest at a rate equal to 3-month Canadian Dealer Offered Rate plus 165 basis points. The interest rate for the period from October 23, 2013 to January 22, 2014 was 2.925%.

Debentures payable increased by \$328.3 million from December 31, 2012 to December 31, 2013 mainly due to: (i) the issuance of the \$175.0 million Series G Senior Debentures in June 2013, (ii) the assumption of the 2018 Convertible Debentures formerly included in the Primaris portfolio and (iii) the issuance of the \$235.0 million and \$60.0 million Series H and I Senior Debentures, respectively, in October 2013. This was offset by the conversion of many of the 2017 Convertible Debentures into Stapled Units as this series of convertible debentures was redeemed by the REIT in July 2013.

**Exchangeable Units**

The REIT has issued exchangeable units which are puttable instruments where the REIT has a contractual obligation to issue Stapled Units to participating vendors upon redemption. These puttable instruments are classified as a liability under IFRS and are measured at fair value through net income. Holders of the exchangeable units are entitled to receive distributions on a per unit amount equal to a per Stapled Unit amount provided to holders of Stapled Units.

The following table shows the change in the number of exchangeable units outstanding from December 31, 2012 to December 31, 2013:

Opening balance - December 31, 2012	5,437,565
Exchangeable units assumed - Place du Royaume Limited Partnership, a subsidiary of Primaris	2,041,380
Exchangeable units assumed - Grant Park Limited Partnership, a subsidiary of Primaris	433,174 <sup>(1)</sup>
Exchangeable units issued – management internalization	9,500,000
Exchangeable units exchanged	(9,000)
<b>Closing balance – December 31, 2013</b>	<b>17,403,119</b>

<sup>(1)</sup> A subsidiary of the REIT holds Stapled Units to mirror these exchangeable units. Therefore, when these exchangeable units are exchanged for Stapled Units, the number of outstanding Stapled Units will not increase. These exchangeable units have been excluded from the weighting of exchangeable units used to calculate the FFO and AFFO per unit amounts.

Fair value is determined by using the quoted price of the Stapled Units on the TSX, as all of the 17.4 million (December 31, 2012 – 5.5 million) exchangeable units are exchangeable on a one-for-one basis, at the option of the holder, into Stapled Units. The quoted price of the Stapled Units as at December 31, 2013 was \$21.40 (December 31, 2012 - \$24.10).

**Deferred tax liability**

The REIT has certain subsidiaries in the United States that are subject to tax on their taxable income at a rate of approximately 38%. The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities are presented below:

	December 31, 2013	December 31, 2012
<b>Deferred tax assets:</b>		
Net operating losses and deferred interest deductions	<b>\$84.4</b>	\$72.1
Accounts payable and accrued liabilities	<b>1.9</b>	1.1
Other assets	<b>0.1</b>	0.2
	<b>86.4</b>	73.4
<b>Deferred liabilities:</b>		
Investment properties	<b>162.1</b>	116.4
Equity accounted investments	<b>1.1</b>	-
Derivative instruments	<b>(0.2)</b>	0.4
	<b>163.0</b>	116.8
Deferred tax asset (liability)	<b>(\$76.6)</b>	(\$43.4)

The deferred tax liability relating to the investment properties is derived on the basis that the US. Investment properties will be sold at their current fair value. The tax liability will only be realized upon an actual disposition.

<b>Derivative Instruments</b> <i>(in thousands of Canadian dollars)</i>	Fair value (liability) asset*	
	December 31, 2013	December 31, 2012
Foreign exchange forward contracts (a)	<b>(\$122)</b>	\$1,679
Mortgage interest rate swaps (b)	<b>(386)</b>	(601)
	<b>(\$508)</b>	\$1,078

(a) The REIT entered into foreign exchange forward contracts and swaps with Canadian chartered banks effectively locking the REIT's rate to exchange U.S. dollars into Canadian dollars.

(b) The REIT entered into an interest rate swap on one U.S. mortgage.

\* Derivative instruments in asset and liability positions are not presented on a net basis. When a derivative instrument is in an asset position, the amount is recorded in "Assets - Other Assets" section of this MD&A.

### **Accounts Payable and Accrued Liabilities**

Accounts payable and accrued liabilities increased by \$12.0 million between December 31, 2012 and December 31, 2013. The increase is primarily due to accounts payable and accrued liabilities relating to Primaris of \$39.3 million as at December 31, 2013, offset by a decrease of \$25.0 million due to lower costs to complete of the Bow.

## **EQUITY**

### **Unitholders' Equity**

Unitholders' equity increased by \$1.8 billion between December 31, 2012 and December 31, 2013. The increase is primarily due to the REIT and Finance Trust issuing 62.5 million Stapled Units in conjunction with the Primaris transaction which increased unitholders' equity by \$1.4 billion. The increase is also due to the REIT and Finance Trust issuing Stapled Units resulting from conversions of the 2014<sup>b</sup>, 2015 and 2017 convertible debentures, as well as comprehensive income for the period. This increase was partially offset by distributions paid to unitholders during the same period.

Other comprehensive income (loss) consists of the unrealized gain on translation of U.S. denominated foreign operations and the transfer of realized losses on cash flow hedges to net income.

### **USE OF PROCEEDS FROM FINANCING ISSUED DURING THE YEAR ENDED DECEMBER 31, 2013**

Financing	Disclosed Use of Proceeds	Actual Use of Proceeds
Private placement of \$300 million of first mortgage bonds secured by the Bow on June 13, 2013.	To repay outstanding indebtedness incurred under the REIT's credit facilities.	The net proceeds were used to repay bank indebtedness.
Public offering of \$175 million of unsecured debentures on June 20, 2013.	To repay outstanding indebtedness incurred under the REIT's credit facilities thereby enabling the REIT to have greater financial capacity to pursue future acquisitions and developments, and for general trust purposes.	The net proceeds were used to repay bank indebtedness and for general trust purposes.
Private Placement of \$235 million of floating rate unsecured debentures on October 9, 2013.	To repay existing indebtedness and for general trust purposes.	The net proceeds were used to repay bank indebtedness.
Private placement of \$60 million of floating rate unsecured debentures on October 23, 2013.	To repay existing indebtedness and for general trust purposes.	A portion of the proceeds were used to repay bank indebtedness and for general trust purposes.

**LIQUIDITY AND CAPITAL RESOURCES****FUNDS FROM OPERATIONS**

(in thousands of Canadian dollars except per unit amounts)	Three months ended December 31		Year ended December 31	
	2013	2012	2013	2012
<b>Net income</b>	<b>\$113,694</b>	\$102,635	<b>\$323,635</b>	\$508,860
Add (deduct):				
Exchangeable unit distributions	5,875	1,699	13,967	6,389
(Gain) loss on change in fair value	5,516	(17,730)	(30,972)	5,143
Amortization	2,089	1,437	7,536	5,525
Fair value adjustment to unit-based compensation	(470)	(1,313)	(6,737)	2,994
Fair value adjustment on real estate assets	10,570	(30,499)	(51,872)	(237,689)
Loss on sale of real estate assets	204	1,080	2,067	137
(Gain) loss on foreign exchange	(6,772)	(1,535)	(14,042)	7,007
Transaction costs	-	-	204,819	-
Deferred income taxes	11,623	29,607	29,227	43,407
REIT's interests of FFO adjustments from equity accounted investments	(8,079)	(153)	(4,849)	(12,819)
<b>FFO</b>	<b>\$134,250</b>	\$85,228	<b>\$472,779</b>	\$328,954
Weighted average number of Stapled Units (in thousands of Stapled Units adjusted for conversion of exchangeable Stapled Units) <sup>(1)</sup>	286,281	195,469	259,458	188,847
Diluted weighted average number of Stapled Units (in thousands of Stapled Units) for the calculation of FFO <sup>(1)(2)(3)(4)(5)(6)</sup>	296,734	212,041	273,450	211,048
FFO per Stapled Unit (basic – adjusted for conversion of exchangeable units)	\$0.47	\$0.44	\$1.82	\$1.74
FFO per Stapled Unit (diluted)	\$0.46	\$0.43	\$1.79	\$1.67
Distributions per Stapled Unit	\$0.34	\$0.31	\$1.35	\$1.18
Payout ratio	72.3%	70.5%	74.2%	67.8%

(1) For the three months and year ended December 31, 2013, included in the weighted average and diluted weighted average number of Stapled Units are exchangeable units of 16,972,391 and 11,740,609, respectively (three months and year ended December 31, 2012 - 5,437,565). Exchangeable units issued as consideration in connection with the property management internalization have been weighted as if they were issued on July 1, 2013 which is the effective date the transaction took place.

(2) For the three months ended December 31, 2013 and 2012, 285,166 Stapled Units and 552,392 Stapled Units, respectively, are included in the determination of diluted FFO with respect to the REIT's Unit Option Plan. For the year ended December 31, 2013 and 2012, 358,536 Stapled Units and 713,857 Stapled Units, respectively, are included in the determination of diluted FFO with respect to the REIT's Unit Option Plan.

(3) The 2016, 2018 and 2020 convertible debentures are dilutive for the three months ended December 31, 2013. Therefore, debenture interest of \$3.3 million is added to FFO and 10,167,942 Stapled Units are included in the diluted weighted average number of Stapled Units outstanding for this period.

(4) The 2016, 2017 and 2020 convertible debentures are dilutive for the three months ended December 31, 2012. Therefore, debenture interest of \$4.9 million is added to FFO and 16,019,549 Stapled Units are included in the dilutive weighted average number of Stapled Units outstanding for the period.

(5) The 2014<sup>a</sup>, 2015, 2016, 2017, 2018 and 2020 convertible debentures are dilutive for the year ended December 31, 2013. Therefore, debenture interest of \$16.4 million is added to FFO and 13,633,360 Stapled Units are included in the diluted weighted average number of Stapled Units outstanding for this period.

(6) The 2013, 2014, 2016, 2017 and 2020 convertible debentures are dilutive for the year ended December 31, 2012. Therefore, debenture interest of \$24.5 million is added to FFO and 21,486,952 Stapled Units are included in the diluted weighted average number of Stapled Units outstanding for this period.

Included in FFO are the following items which can be a source of significant variances between periods:

<b>(in thousands of Canadian dollars)</b>	<b>Three months ended December 31</b>			<b>Year ended December 31</b>		
	<b>2013</b>	<b>2012</b>	<b>Change</b>	<b>2013</b>	<b>2012</b>	<b>Change</b>
Additional recoveries for capital expenditures (including amounts relating to the REIT's interests of real estate assets included in equity accounted investments)	<b>\$1,418</b>	\$5,253	(\$3,835)	<b>\$8,647</b>	\$13,775	(\$5,128)
Gain (loss) on extinguishment of debt	-	(45)	45	-	10,151	(10,151)
Adjustment to straight-lining of contractual rent	-	-	-	<b>(3,356)</b>	(843)	(2,513)
Sundry income <sup>(1)</sup>	<b>1,079</b>	130	949	<b>3,944</b>	(1,517)	5,461
	<b>\$2,497</b>	\$5,338	(\$2,841)	<b>\$9,235</b>	\$21,566	(\$12,331)

(1) Sundry income includes lease termination payments, mortgage prepayment penalties and other one-time unusual items.

Excluding the above items, FFO would have been \$131.8 million for the three months ended December 31, 2013 (Q4 2012 - \$79.9 million) and \$0.46 per basic Stapled Unit (Q4 2012 - \$0.41 per basic Stapled Unit). For the year ended December 31, 2013, FFO would have been \$463.5 million (December 31, 2012 - \$307.4 million) and \$1.79 per basic Stapled Unit (December 31, 2012 - \$1.63 per basic Stapled Unit). Included in FFO for Q4 2013 is \$4.1 million of seasonal revenues from Primaris which includes percentage rent, common area rent, rental revenue from temporary tenants and other sundry income items which are typically strongest in the fourth quarter of each year.

**ADJUSTED FUNDS FROM OPERATIONS**

(in thousands of Canadian dollars except per unit amounts)	Three months ended December 31		Year ended December 31	
	2013	2012	2013	2012
<b>FFO</b>	<b>\$134,250</b>	\$85,228	<b>\$472,779</b>	\$328,954
Add (deduct):				
Straight-lining of contractual rent	(4,224)	(16,127)	(32,830)	(32,608)
Rent amortization of tenant inducements	440	369	1,795	1,465
Effective interest rate accretion	(1,161)	544	(4,176)	1,323
Mortgage interest accruals on non-recourse mortgage defaults	-	-	-	296
(Gain) loss on extinguishment of debt	-	45	-	(10,151)
Unit-based compensation	770	804	2,601	3,128
Capital expenditures	(11,367)	(8,026)	(33,704)	(19,850)
Tenant expenditures	(6,252)	(6,390)	(18,799)	(14,022)
REIT's interests of AFFO adjustments from equity accounted investments	(2,738)	(267)	(5,702)	58
<b>AFFO</b>	<b>\$109,718</b>	\$56,180	<b>\$381,964</b>	\$258,593
Weighted average number of Stapled Units (in thousands of Stapled Units adjusted for conversion of exchangeable Stapled Units) <sup>(1)</sup>	286,281	195,469	259,458	188,847
Diluted weighted average number of Stapled Units (in thousands of Stapled Units) for the calculation of AFFO <sup>(1)(2)(3)(4)(5)(6)</sup>	296,734	204,881	273,450	206,799
AFFO per Stapled Unit (basic - adjusted for conversion of exchangeable units)	\$0.38	\$0.29	\$1.47	\$1.37
AFFO per Stapled Unit (diluted)	\$0.38	\$0.29	\$1.46	\$1.34

(1) For the three months and year ended December 31, 2013, included in the weighted average and diluted weighted average number of Stapled Units are exchangeable units of 16,972,391 and 11,740,609 respectively (three months and year ended December 31, 2012 - 5,437,565). Exchangeable units issued as consideration in connection with the property management internalization have been weighted as if they were issued on July 1, 2013 which is the effective date the transaction took place.

(2) For the three months ended December 31, 2013 and 2012, 285,166 Stapled Units and 552,392 Stapled Units, respectively, are included in the determination of diluted AFFO with respect to the REIT's Unit Option Plan. For the year ended December 31, 2013 and 2012, 358,536 Stapled Units and 713,857 Stapled Units, respectively, are included in the determination of diluted AFFO with respect to the REIT's Unit Option Plan.

(3) The 2016, 2018 and 2020 convertible debentures are dilutive for the three months ended December 31, 2013. Therefore, debenture interest of \$3.3 million is added to AFFO and 10,167,942 Stapled Units are included in the diluted weighted average number of Stapled Units outstanding for this period.

(4) The 2017 convertible debentures are dilutive for the three months ended December 31, 2012. Therefore, debenture interest of \$2.5 million is added back to AFFO and 8,859,365 Stapled Units are included in the dilutive weighted average number of Stapled Units outstanding for this period.

(5) The 2014<sup>b</sup>, 2015, 2016, 2017, 2018 and 2020 convertible debentures are dilutive for the year ended December 31, 2013. Therefore, debenture interest of \$16.4 million is added to AFFO and 13,633,360 Stapled Units are included in the dilutive weighted average number of Stapled Units outstanding for this period.

(6) The 2013, 2014, 2016 and 2017 convertible debentures are dilutive for the year ended December 31, 2012. Therefore, debenture interest of \$18.6 million is added back to AFFO and 17,238,344 Stapled Units are included in the dilutive weighted average number of Stapled Units outstanding for this period.

Included in AFFO are the following items which can be a source of significant variances between periods:

(in thousands of Canadian dollars)	Three months ended December 31			Year ended December 31		
	2013	2012	Change	2013	2012	Change
Additional recoveries for capital expenditures <sup>(1)</sup>	\$1,418	\$5,253	(\$3,835)	\$8,647	\$13,775	(\$5,128)
Capital expenditures <sup>(1)</sup>	(13,467)	(8,139)	(5,328)	(38,153)	(19,963)	(18,190)
Tenant expenditures <sup>(1)</sup>	(6,787)	(6,599)	(188)	(19,659)	(14,231)	(5,428)
Sundry income <sup>(2)</sup>	1,079	130	949	3,944	(1,517)	(5,461)
	(\$17,757)	(\$9,355)	(\$8,402)	(\$45,221)	(\$21,936)	(\$23,285)

(1) Includes amounts relating to the REIT's interests of real estate assets included in equity accounted investments.

(2) Sundry income includes lease termination payments, mortgage prepayment penalties and other one-time unusual items.

Excluding the above items, AFFO would have been \$127.5 million for the three months ended December 31, 2013 (Q4 2012 - \$65.5 million) and \$0.45 per basic Stapled Unit (Q4 2012 - \$0.34 per basic Stapled Unit). For the year ended December 31, 2013, AFFO would have been \$427.2 million (December 31, 2012 - \$280.5 million) and \$1.65 per basic Stapled Unit (December 31, 2012 - \$1.49 per basic Stapled Unit). Included in AFFO for Q4 2013 is \$4.1 million of seasonal revenues from Primaris which includes percentage rent, common area rent, rental revenue from temporary tenants and other sundry income items which are typically strongest in the fourth quarter of each year.

Included in capital expenditures for the three months and year ended December 31, 2013 is \$4.4 million and \$12.9 million, respectively, relating to Primaris. The following table provides a summary of major capital expenditure projects incurred by the REIT in 2013:

Property	Type of Work	Three months ended December 31, 2013	Year ended December 31, 2013
<b>H&amp;R Portfolio:</b>			
Telus Tower	Lobby and related exterior work	\$1,896	\$3,944
Atrium on Bay	Garage repairs and washrooms	392	2,465
2300 Rue Senkus	Retrofit	854	2,169
3777 Kingsway St.	Window replacement, post tension work and oil circuit breakers	530	2,089
100 Wynford Dr.	Generator controls upgrade and new standby generator	-	1,291
5115 Creekbank Rd.	Roof replacement	1,000	1,000
200 Bouchard Boul.	Uninterruptible power supply distribution upgrade	152	963
310-320-330 Front St. W.	Elevator modification	-	889
26 Wellington St. E.	Replacement of exterior interlock	572	572
160 Elgin St.	Interior brackets	507	507
<b>Primaris Portfolio:</b>			
Dufferin Mall	Landlord work for Marshalls, parking lot lighting, freight elevator and electrical upgrade	765	4,180
Grant Park	Interior renovation	607	2,221
McAllister Place	Parking, energy and building improvements	60	967
Place d'Orleans	HVAC unit replacement and other improvements	234	806
Orchard Park	HVAC unit replacement	-	628
Park Place	Roof replacement	572	572
Cataraqui Town Centre	Redevelopment and expansion of tenant space	445	529
		\$8,586	\$25,792



The following is a reconciliation of the Trusts' AFFO to cash provided by operations.

(in thousands of Canadian dollars)	Three months ended December 31		Year ended December 31	
	2013	2012	2013	2012
<b>AFFO</b>	<b>\$109,718</b>	\$56,180	<b>\$381,964</b>	\$258,593
Straight-lining of contractual rent	<b>4,224</b>	16,127	<b>32,830</b>	32,608
Net income from equity accounted investments	<b>(19,163)</b>	(5,408)	<b>(34,032)</b>	(26,173)
Mortgage interest accruals on non-recourse mortgage defaults	-	-	-	(296)
Exchangeable unit distributions	<b>(5,875)</b>	(1,699)	<b>(13,967)</b>	(6,389)
Additions to capital expenditures and tenant expenditures	<b>17,619</b>	14,416	<b>52,503</b>	33,872
Finance cost - operations	<b>83,807</b>	64,030	<b>309,629</b>	232,495
Effective interest rate accretion	<b>1,161</b>	(544)	<b>4,176</b>	(1,323)
Adjustments for the REIT's interests in equity accounted investments (page 17)	<b>10,817</b>	420	<b>10,551</b>	12,761
Transaction costs - paid in cash	-	-	<b>(9,974)</b>	-
Realized loss on derivative instruments	-	-	-	(11,348)
Change in other non-cash operating items	<b>713</b>	1,014	<b>(116,289)</b>	(5,495)
<b>Cash provided by operations</b>	<b>\$203,021</b>	\$144,536	<b>\$617,391</b>	\$519,305

## LIQUIDITY AND CAPITAL RESOURCES

### Cash Distributions

In accordance with National Policy 41-201 - *Income Trusts and Other Indirect Offerings*, the Trusts are required to provide the following additional disclosure relating to cash distributions.

(in thousands of Canadian dollars)	Three months ended December 31, 2013	Year ended December 31, 2013	Year ended December 31, 2012	Year ended December 31, 2011
Cash provided by operating activities	<b>\$203,021</b>	<b>\$617,391</b>	\$519,305	\$404,568 <sup>(1)</sup>
Net income	<b>113,694</b>	<b>323,635</b>	508,860	338,043
Cash distributions relating to the period <sup>(2)</sup>	<b>70,257</b>	<b>256,780</b>	158,423	114,112
Excess of cash provided by operating activities over cash distributions paid	<b>132,764</b>	<b>360,611</b>	360,882	290,456
Excess of net income over cash distributions paid	<b>43,437</b>	<b>66,855</b>	350,437	223,931

(1) Cash provided by operating activities for the year ended December 31, 2011 has not been restated for the 2013 change in accounting policy (see note 3 in the Combined Financial Statements).

(2) Cash distributions exclude distributions reinvested in units pursuant to the Trusts' unitholder distribution reinvestment plan.

For all periods noted above, cash provided by operating activities exceeded cash distributions. Management expects this trend to continue. Net income exceeded cash distributions for all periods noted above. Non-cash items relating to the property management internalization, fair value of exchangeable units, fair value adjustments on real estate assets, gain (loss) on change in fair value, gain (loss) on extinguishment of debt, deferred income tax recoveries and amortization are deducted from or added to net income and have no impact on cash available to pay current distributions.

**Capital Resources**

Subject to market conditions, management expects to be able to meet all of the Trusts' ongoing obligations and to finance short-term development commitments through the general operating facilities discussed below and the Trusts' cash flow from operations. As at December 31, 2013, the Trusts are not in default or arrears on any of its obligations including interest or principal payments on debt and any debt covenant.

The REIT's general operating facility has been provided by the same chartered bank since the REIT's inception. This general operating facility of \$300.0 million expires on December 31, 2016 and is secured by certain investment properties. As at December 31, 2013, approximately \$151.5 million was available under this facility. The REIT, through Primaris, also has a second general operating facility of \$150.0 million with another Canadian chartered bank. This facility expires April 4, 2015 and is secured by certain investment properties. As at December 31, 2013, \$149.4 million was available under this facility. A third general operating facility of \$14.9 million, which is secured by certain investment properties, is due December 20, 2015. As at December 31, 2013, nil was available under this facility.

As at December 31, 2013, the REIT has 50 unencumbered properties, excluding the REIT's interests of real estate assets included in equity accounted investments, with a fair value of \$1.3 billion.

The following is a summary of material contractual obligations of the REIT including payments due as at December 31, 2013 for the next five years and thereafter:

<b>Contractual Obligations<sup>(1)</sup></b> <b>(in thousands of Canadian dollars)</b>	Payments Due by Period				Total
	2014	2015- 2016	2017- 2018	2019 and thereafter	
Mortgages payable <sup>(2)</sup>	\$352,492	\$969,060	\$916,930	\$3,078,825	\$5,317,307
2016 Convertible Debentures	-	75,000	-	-	75,000
2018 Convertible Debentures	-	-	74,414	-	74,414
2020 Convertible Debentures	-	-	-	99,654	99,654
Series A Senior Debentures	-	115,000	-	-	115,000
Series H Senior Debentures	-	235,000	-	-	235,000
Series D Senior Debentures	-	180,000	-	-	180,000
Series I Senior Debentures	-	-	60,000	-	60,000
Series B Senior Debentures	-	-	115,000	-	115,000
Series E Senior Debentures	-	-	100,000	-	100,000
Series G Senior Debentures	-	-	175,000	-	175,000
Series C Senior Debentures	-	-	125,000	-	125,000
Series F Senior Debentures	-	-	-	175,000	175,000
Bank indebtedness	-	116,762	-	-	116,762
Loan Payable <sup>(3)</sup>	203,054	-	-	-	203,054
Property acquisitions	28,883	-	-	-	28,883
<b>Total contractual obligations</b>	<b>\$584,429</b>	<b>\$1,690,822</b>	<b>\$1,566,344</b>	<b>\$3,353,479</b>	<b>\$7,195,074</b>

(1) The amounts in the above table are the principal amounts due under the contractual agreements.

(2) Includes the REIT's share of mortgages payable relating to equity accounted investments.

(3) 33.7% of this loan payable relating to ECHO has been eliminated upon consolidation of the Trust's Combined Financial Statements as the REIT has a 33.7% interest in ECHO, however there is a contractual obligation for the full amount.

DBRS Limited ("DBRS") provides credit ratings of debt securities for commercial entities. A credit rating generally provides an indication of the risk that the borrower will not fulfill its obligations in a timely manner with respect to both interest and principal commitments. Rating categories range from highest credit quality (generally AAA) to default payment (generally D). A credit rating is not a recommendation to buy, sell or hold securities.

DBRS has confirmed that the REIT has a credit rating of BBB with a Stable trend as at December 31, 2013. A credit rating of BBB by DBRS is generally an indication of adequate credit quality, where protection of interest and principal is considered acceptable. A credit rating of BBB or higher is an investment grade rating. There can be no assurance that any rating will remain in effect for any given period of time or that any rating will not be withdrawn or revised by DBRS at any time. The credit rating is reviewed periodically by DBRS.

The REIT has no material capital or operating lease obligations.

### **Funding of Future Commitments**

The REIT believes that as at December 31, 2013, through the combined amount available under its general operating facilities of \$301.0 million and its unencumbered property pool of \$1.3 billion, it has sufficient funds for future commitments.

The following summarizes the estimated loan to value ratios that will be outstanding on properties whose mortgages mature over the next five years, including investments in the REIT's share of mortgages relating to equity accounted investments:

Year	Number of Properties	Mortgage Debt due on Maturity (\$'000's) <sup>(1)</sup>	Weighted Average Interest Rate on Maturity	Fair Value of Investment Properties (\$'000's) <sup>(1)</sup>	Loan to Value
2014	23	\$178,916	6.1%	\$391,831	46%
2015	25	310,672	5.3%	766,502	41%
2016	44	307,378	5.4%	633,876	48%
2017	21	466,605	4.8%	962,375	48%
2018	36	117,519	5.4%	488,424	24%
	149	\$1,381,090		\$3,243,008	43%

<sup>(1)</sup> Converting U.S. dollars to Canadian dollars at an exchange rate of \$1.06 as at December 31, 2013.

Based on the low percentage of the projected loan to values of the maturing mortgages, the REIT is confident it will be able to refinance these mortgages upon maturity should it choose to do so.

### **OFF-BALANCE SHEET ITEMS**

The REIT has co-owners and partners in various projects. As a rule the REIT does not provide guarantees or indemnities for these co-owners pursuant to property acquisitions because should such guarantees be provided, recourse would be available against the REIT in the event of a default of the co-owners. In such case, the REIT would have a claim against the underlying real estate investment. However, in certain circumstances, subject to compliance with the REIT's Declaration of Trust and the determination by management that the fair value of the co-owners' investment is greater than the mortgages payable for which the REIT has provided guarantees, such guarantees will be provided.

At December 31, 2013, such guarantees amounted to \$69.8 million expiring in 2016 (December 31, 2012 - \$72.1 million, expiring in 2016), and no amount has been provided for in the Combined Financial Statements of the Trusts for these items. These amounts arise where the REIT has guaranteed a co-owner's share of the mortgage liability. The REIT, however, customarily guarantees or indemnifies the obligations of its nominee companies which hold separate title to each of its properties owned.

In addition, the REIT continued to guarantee certain debt assumed by purchasers in connection with past dispositions of properties, and will remain liable thereunder until such debts are extinguished or the lenders agree to release the REIT's guarantee. At December 31, 2013, the estimated amount of debt subject to such guarantees, and therefore the maximum exposure to credit risk is approximately \$224.4 million, expiring between 2014 and 2022 (December 31, 2012 - \$110.3 million, expiring between 2013 and 2018). There have been no defaults by the primary obligor for debts on which the REIT has provided its guarantees, and as a result, no contingent loss on these guarantees has been recognized in the Combined Financial Statements of the Trusts.

### **Related Party Transactions**

HRPM, a company partially owned by family members of the CEO, provided property management services for substantially all properties owned by the REIT, including leasing services, for a fee of 2% of gross revenue. HRPM also provided support services in connection with the acquisition, disposition and development activities of the REIT and was also entitled to an incentive fee. Acquisitions and development support services were provided for a fee of 2/3 of 1% of total acquisition and development costs. The support services relating to dispositions of investment properties were provided for a fee of 10% of the net gain on sale of investment

properties adjusted for the add back of accumulated depreciation and amortization. Services were provided by HRPMP pursuant to a property management agreement which was internalized effective June 30, 2013.

Effective July 1, 2013, the REIT executed an agreement with HRPMP to internalize the property management function in exchange for the issuance of 9.5 million exchangeable units. Upon closing of the transaction, HRRMSLP acquired HRPMP's REIT-related property management business in return for 9.5 million limited partnership units of HRRMSLP, such units to be exchangeable on a one-for-one basis for Stapled Units. The cost of internalizing the property management function, including the value of exchangeable units of \$194.8 million issued, was \$198.2 million. These costs were expensed as transaction costs in the period incurred.

Effective July 1, 2013, the REIT entered into an agreement with HRPMP for HRPMP to provide specified services including the cost sharing of premises, certain personnel and equipment and support systems, as well as additional services to be agreed upon from time to time. The agreement will continue until terminated by either party in accordance with the terms of the agreement. During the year ended December 31, 2013, the REIT incurred costs of \$0.8 million under this agreement.

During the three months ended December 31, 2013, the REIT recorded expenses pursuant to the property management agreement of nil (December 31, 2012 - \$3.8 million), of which nil (December 31, 2012 - \$0.1 million) was capitalized to the cost of investment properties acquired, nil (December 31, 2012 - \$0.1 million) was capitalized to properties under development and nil (December 31, 2012 - \$1.5 million) was capitalized to leasing expenses. These amounts include amounts relating to equity accounted investments. The REIT has also reimbursed HRPMP for certain direct property operating costs and tenant construction costs.

For the three months ended December 31, 2013, a further amount of nil (December 31, 2012 - \$1.1 million) was earned by the Property Manager pursuant to the property management agreement, in accordance with the annual incentive fee payable to HRPMP.

During the year ended December 31, 2013, the REIT recorded expenses pursuant to the property management agreement of \$8.2 million (December 31, 2012 - \$19.9 million), of which \$0.6 million (December 31, 2012 - \$4.8 million) was capitalized to the cost of investment properties acquired, nil (December 31, 2012 - \$1.1 million) was capitalized to properties under development and \$2.0 million (December 31, 2012 - \$5.5 million) was capitalized to leasing expenses. These amounts include amounts relating to equity accounted investments. The REIT has also reimbursed HRPMP for certain direct property operating costs and tenant construction costs.

For the year ended December 31, 2013, a further amount of \$2.2 million (December 31, 2012 - \$4.5 million) was earned by HRPMP pursuant to the property management agreement, in accordance with the annual incentive fee payable to HRPMP. Of this amount, \$1.1 million (December 31, 2012 - nil) has been waived by HRPMP and \$1.1 million (December 31, 2012 - \$4.5 million) has been expensed in the combined statements of comprehensive income.

As at December 31, 2013, nil (December 31, 2012 - \$1.8 million) was payable to HRPMP.

The REIT leases space to companies partially owned by family members of the CEO. The rental income earned for the three months ended December 31, 2013 is \$0.3 million (December 31, 2012 - \$0.4 million) and for the year ended December 31, 2013 is \$1.4 million (December 31, 2012 - \$1.4 million).

These transactions are measured at the amount of consideration established and agreed to by the related parties.

## **FINANCIAL INSTRUMENTS AND OTHER INSTRUMENTS**

Where appropriate, the REIT uses forward contracts to lock-in lending rates on certain anticipated mortgages. This strategy provides certainty to the rate of interest on borrowings when the REIT is involved in transactions that may close further into the future than usual for typical transactions. The REIT has entered into an interest rate swap on one U.S. mortgage which effectively locked the interest rate at 5.25%. At the end of each reporting period, this interest rate swap is marked-to-market, resulting in an unrealized gain or loss recorded in net income.

Where appropriate, the REIT uses forward exchange contracts to lock-in foreign exchange rates. This strategy provides certainty in the foreign exchange rates on transactions that will occur in the future. The REIT has entered into forward exchange contracts with a Canadian chartered bank, which effectively locks in the REIT's rate of exchange for U.S. dollars into Canadian dollars.

## SECTION IV

### CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

Preparation of the Combined Financial Statements of the Trusts requires management to make estimates and judgements that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenue and expenses during the reporting period.

Management believes the policies which are subject to greater estimation and judgement are outlined below. For a detailed description of these and other accounting policies refer to notes 1, 2 and 3 of the Combined Financial Statements of the Trusts.

#### Use of Estimates

Information about assumption and estimation uncertainties that have a significant risk of resulting in a material adjustment within the next financial year are:

- Fair value of real estate assets;
- Fair value of financial instruments;
- Fair value of cash-settled unit-based compensation;
- Fair value of convertible debentures; and
- Fair value of exchangeable units.

#### Use of Judgements

- Business combinations

Accounting for business combinations under IFRS 3, Business Combinations ("IFRS 3") is only applicable if it is determined that a business has been acquired. Under IFRS 3, a business is defined as an integrated set of activities and assets conducted and managed for the purpose of providing a return to investors or lower costs or other economic benefits directly and proportionately to the REIT. A business generally consists of inputs, processes applied to those inputs and resulting outputs that are, or will be, used to generate revenues. In the absence of meeting such criteria, a group of assets is deemed to have been acquired. If goodwill is present in a transferred set of activities and assets, the transferred set is presumed to be a business. Judgement is used by management in determining whether the acquisition of an individual property qualifies as a business combination in accordance with IFRS 3 or as an asset acquisition.

The acquisition of Primaris on April 4, 2013 has been recorded as a business combination. See note 6 of the Combined Financial Statements.

- Valuations of real estate assets

Real estate assets, which consist of investment properties and properties under development, are carried on the combined statements of financial position at fair value, as determined by either qualified external valuation professionals or by management. The valuations are based on a number of assumptions, such as appropriate discount rates and capitalization rates and estimates of future rental income, operating expenses and capital expenditures. Valuation of real estate assets is one of the principal estimates and uncertainties of the REIT. Refer to note 4 of the Combined Financial Statements of the Trusts for further information on estimates and assumptions made in the determination of the fair value of real estate assets.

- Leases

The REIT's policy for property rental revenue recognition is described in note 2(g) of the Combined Financial Statements of the Trusts. The REIT makes judgements in determining whether certain leases, in particular those tenant leases with long contractual terms and long-term ground leases where the REIT is the lessor, are operating or finance leases. The REIT has determined that all of its leases are operating leases.

- Income taxes

The REIT currently qualifies as a real estate investment trust and a mutual fund trust for Canadian income tax purposes. A real estate investment trust will not be subject to the tax levied on “specified investment flow-through” (“SIFT”) trusts provided it continues to meet prescribed conditions under the Tax Act, including with respect to the nature of its assets and revenue, (the “REIT Conditions”) at all times throughout a taxation year. Accordingly, no provision for current or deferred income taxes has been recorded by the REIT at December 31, 2013 in respect of its Canadian entities.

The REIT will not be subject to income tax in a year to the extent that it continues to qualify as a real estate investment trust and distributes all of its taxable income to its unitholders. Income allocated to unitholders will be taxed at the unitholder level. The REIT currently distributes, and is required to distribute, all of its income to its unitholders. Accordingly, for financial statement reporting purposes, the tax deductibility of the REIT’s distributions is treated as an exemption from taxation.

Deferred income taxes are recognized in respect of U.S. Holdco for the temporary differences between the financial statement carrying amounts of assets and liabilities and their respective tax bases. Deferred income tax assets and liabilities are measured using enacted or substantively enacted tax rates and laws that are expected to apply to taxable income in the years in which those temporary differences are expected to be reversed or settled. The effect on deferred income tax assets and liabilities of a change in tax rate is recognized in income or unitholders’ equity, as appropriate, in the period that includes the date of enactment or substantive enactment. Deferred tax assets are recognized for all deductible temporary differences, unused tax credits and unused tax losses to the extent that it is probable that taxable profit will be available against which these tax benefits can be utilized.

- Tenant improvements

The REIT makes judgements with respect to whether tenant improvements provided in connection with a lease enhance the value of the leased property, which determines whether such amounts are capitalized to investment properties.

- Impairment of equity accounted investments

The REIT determines at each reporting date whether there is any objective evidence that the equity accounted investments are impaired. If so, the REIT calculates the amount of impairment as the difference between the recoverable amount of the equity accounted investment and its carrying value and recognizes the amount in net income.

## **DISCLOSURE CONTROLS & PROCEDURES AND INTERNAL CONTROL OVER FINANCIAL REPORTING**

Each of the Trust’s CEO and CFO has designed, or caused to be designed under their direct supervision, the applicable Trusts’ disclosure controls and procedures (as defined in National Instrument 52-109 - *Certification of Disclosure in Issuers’ Annual and Interim Filings* (“NI 52-109”), adopted by the Canadian Securities Administrators to provide reasonable assurance that: (i) material information relating to the applicable Trust, including its consolidated subsidiaries, is made known to them by others within those entities, particularly during the period in which the annual filings are being prepared; and (ii) material information required to be disclosed in the annual filings is recorded, processed, summarized and reported on a timely basis. The Combined Financial Statements of the Trusts and this MD&A were reviewed and approved by the REIT’s Audit Committee and the Board of Trustees prior to this publication.

Effective April 4, 2013, the REIT completed the Primaris Acquisition. The results of Primaris’ operations have been included in the Combined Financial Statements of the Trusts since the date of the Primaris Acquisition. However, the REIT has not had sufficient time to appropriately assess the disclosure controls and procedures and internal control over financial reporting used by Primaris and integrate them with those of the Trusts. As a result, in accordance with the provisions of NI 52-109, the Primaris operations have been excluded in the Trusts’ annual assessment of disclosure controls and procedures and internal control over financial reporting. The Trusts are in the process of integrating the Primaris operations and will be expanding its disclosure controls and procedures and internal control over financial reporting to include Primaris during the next quarter.

Management of each Trust has reviewed its internal control over financial reporting on an annual basis. The Trusts have developed their internal control over financial reporting in accordance with the Integrated COSO Framework (1992). No changes were made to the design of either Trust’s internal control over financial reporting during the year ended December 31, 2013 that have materially affected, or are reasonably likely to materially affect, the Trusts’ internal control over financial reporting. Management has concluded that, except for the Primaris operations discussed above, its internal control over financial reporting is operating effectively, as of December 31, 2013.

Each Trust's management, including the CEO and CFO, does not expect that the applicable Trusts' controls and procedures will prevent or detect all misstatements due to error or fraud. Due to the inherent limitations in all control systems, an evaluation of controls can provide only reasonable, not absolute assurance, that all control issues and instances of fraud or error, if any, within the Trusts have been detected. The Trusts are continually evolving and enhancing its systems of controls and procedures.

## **SECTION V**

### **RISKS AND UNCERTAINTIES**

All real estate assets are subject to a degree of risk and uncertainty. They are affected by various factors including general market conditions and local market circumstances. An example of general market conditions would be the availability of long-term mortgage financing whereas local conditions would relate to factors affecting specific properties such as an oversupply of space or a reduction in demand for real estate in a particular area. Management attempts to manage these risks through geographic, type of asset and tenant diversification in the REIT's portfolio. The major risk factors are outlined below and in the REIT's Annual Information Form.

#### **Unit Prices**

Publicly traded trust units will not necessarily trade at values determined solely by reference to the underlying value of trust assets. Accordingly, the Stapled Units may trade at a premium or a discount to the underlying value of the assets of the REIT and Finance Trust. Investors in Stapled Units will be subject to all of the risks of an investment in units of Finance Trust and of an investment in units of the REIT. See also "Forward-Looking Disclaimer".

One of the factors that may influence the quoted price of the Stapled Units is the annual yield on the Stapled Units. Accordingly, an increase in market interest rates may lead investors in Stapled Units to demand a higher annual yield, which could adversely affect the quoted price of Stapled Units. In addition, the quoted price for Stapled Units may be affected by changes in general market conditions, fluctuations in the markets for equity securities and numerous other factors beyond the control of the REIT and/or Finance Trust.

#### **Real Property Ownership**

All real property investments are subject to a degree of risk and uncertainty. Such investments are affected by various factors including general economic conditions, local real estate markets, demand for leased premises, competition from other available premises and various other factors.

The value of real property and any improvements thereto may also depend on the credit and financial stability of the tenants. Distributable cash and the REIT's income would be adversely affected if one or more major tenants or a significant number of tenants were to become unable to meet their obligations under their leases or if a significant amount of available space in the properties in which the REIT has an interest is not able to be leased on economically favourable lease terms. In the event of default by a tenant, delays or limitations in enforcing rights as lessor may be experienced and substantial costs in protecting the REIT's investment may be incurred. Furthermore, at any time, a tenant of any of the properties in which the REIT has an interest may seek the protection of bankruptcy, insolvency or similar laws that could result in the rejection and termination of such tenant's lease and thereby cause a reduction in the cash flow available to the REIT.

With respect to the Primaris portfolio, retail shopping centres have traditionally relied on there being a number of anchor tenants (department stores, discount department stores and grocery stores) in the centre, and therefore they are subject to the risk of such anchor tenants either moving out of the property or going out of business. Within the Primaris portfolio, certain of the major tenants are permitted to cease operating from their leased premises at any time at their option. Other major tenants are permitted to cease operating from their leased premises or to terminate their leases if certain events occur. Some commercial retail unit tenants have a right to cease operating from their premises if certain major tenants cease operating from their premises. The exercise of such rights by a tenant may have a negative effect on a property. There can be no assurance that such rights will not be exercised in the future.

The ability to rent unleased space in the properties in which the REIT has an interest will be affected by many factors and costs may be incurred in making improvements or repairs to property required by a new tenant. A prolonged deterioration in economic conditions could increase and exacerbate the foregoing risks. The failure to rent unleased space on a timely basis or at all would likely have an adverse effect on the REIT's financial condition.

Certain significant expenditures, including property taxes, maintenance costs, mortgage payments, insurance costs and related charges must be made throughout the period of ownership of real property regardless of whether the property is producing any

income. If the REIT is unable to meet mortgage payments on any property, losses could be sustained as a result of the mortgagee's exercise of its rights of foreclosure or sale.

The REIT may, in the future, be exposed to a general decline of demand by tenants for space in properties. As well, certain of the leases of the properties held by the REIT have early termination provisions which, if exercised, would reduce the average lease term. However, such termination rights are generally exercisable at a cost to the tenant only and the amount of space in the REIT portfolio which could be affected is not significant.

A mortgage on any one property may, from time to time, exceed the estimated current market value of the related property. The cash flow from such a property may not be sufficient to cover debt servicing for that property. The cash flow from the REIT portfolio is, however, expected by management to be sufficient to cover any cash flow shortfalls on such a property.

### **Credit Risk and Tenant Concentration**

The REIT is exposed to credit risk as an owner of real estate in that tenants may become unable to pay the contracted rents. Management mitigates this risk by carrying out appropriate credit checks and related due diligence on the significant tenants. Management has diversified the REIT's holdings so that it owns several categories of properties (office, industrial and retail) and acquires properties throughout Canada and the United States. In addition, management ensures that no tenant or related group of tenants, other than investment grade tenants, account for a significant portion of the cash flow. The only tenants which individually account for more than 5% of the rentals from investment properties of the REIT are Encana Corporation and Bell Canada. Both of these companies have a public debt rating that is rated with at least a BBB stable rating by a recognized rating agency.

### **Interest and Other Debt-Related Risk**

The REIT has been able to leverage off the low interest rate environment that the Canadian economy has experienced in recent years which has enhanced its return to unitholders. A reversal of this trend, however, can significantly affect the business's ability to meet its financial obligations. In order to minimize this risk, the REIT negotiates fixed rate term debt with staggered maturities on the portfolio and attempts to match average lease maturity to average debt maturity. Derivative financial instruments may be utilized by the REIT in the management of its interest rate exposure. In addition, the REIT Declaration of Trust restricts total indebtedness permitted on the portfolio.

### **Ability to Access Capital Markets**

As the REIT distributes a substantial portion of its income to unitholders, the REIT may need to obtain additional capital through capital markets and the REIT's ability to access the capital markets through equity issues and forms of secured or unsecured debt financing may affect the operations of the REIT as such financing may be available only on disadvantageous terms, if at all. If financing is not available on acceptable terms, further acquisitions or ongoing development projects may be curtailed and cash available for distributions or to fund future commitments may be adversely affected.

### **Lease Rollover Risk**

Lease rollover risk arises from the possibility that the REIT may experience difficulty renewing leases as they expire. Management attempts to enter into long-term leases to mitigate this risk. Management attempts to mitigate the risk by having staggered lease maturities and entering into longer term leases with built-in rental escalations. The leases for 30.3% of the REIT's total leasable area will expire in the next 5 years.

### **Joint Arrangement Risks**

The REIT has several investments in joint ventures and an investment in an associate. The REIT is subject to risks associated with the management and performance of these joint arrangements. Such risks include any disagreements with its partners relating to the development or operations of a property, as well as differences with respect to strategic decision making. Other risks include partners not meeting their financial or operational obligations. The REIT attempts to mitigate these risks by maintaining good working relationships with its partners, and conducting due diligence on their partners to ensure there is a similar alignment of strategy prior to creating a joint arrangement.



### **Currency Risk**

The Trusts are exposed to foreign exchange fluctuations as a result of ownership of assets in the United States and the rental income earned from these properties. In order to mitigate the risk, the REIT's debt on these properties is also held in U.S. dollars to act as a natural hedge.

The REIT is exposed to foreign exchange fluctuations as a result of the U.S. Holdco Notes being denominated in U.S. dollars.

### **Construction Risks**

It is likely that, subject to compliance with the REIT Declaration of Trust, the REIT will be involved in various development projects. The REIT's obligations in respect of properties under construction, or which are to be constructed, are subject to risks which include (i) the potential insolvency of a third party developer (where the REIT is not the developer); (ii) a third party developer's failure to use advanced funds in payment of construction costs; (iii) construction or other unforeseeable delays; (iv) cost overruns; (v) the failure of tenants to occupy and pay rent in accordance with existing lease agreements, some of which are conditional; (vi) the incurring of construction costs before ensuring rental revenues will be earned from the project; and (vii) increases in interest rates during the period of the development. Management strives to mitigate these risks where possible by entering into fixed price construction contracts with general contractors (and to the extent possible, on a bonded basis) and by attempting to obtain long-term financing as early as possible during construction.

### **Availability of Cash for Distributions**

As the monthly cash distribution paid by Finance Trust fluctuates, the monthly cash distribution paid by the REIT will also fluctuate in order to result in an aggregate monthly cash distribution as previously outlined. Although the REIT intends to make distributions of its available cash to unitholders in accordance with its distribution policy, these cash distributions may be reduced or suspended. The actual amount distributed by the REIT will depend on numerous factors including monthly cash distributions paid by Finance Trust, capital market conditions, the financial performance of the properties, the REIT's debt covenants and obligations, its working capital requirements, its future capital requirements, its development commitments and fluctuations in interest rates. Cash available to the REIT for distributions may be reduced from time to time because of items such as principal repayments on debt, tenant allowances, leasing commissions, capital expenditures or any other business needs that the trustees deem reasonable. The REIT may be required to use part of its debt capacity in order to accommodate any or all of the above items. The market value of Stapled Units may decline significantly if the REIT and/or Finance Trust suspends or reduces distributions. The REIT trustees retain the right to re-evaluate the distribution policy from time to time as they consider appropriate.

### **Environmental Risk**

As an owner and manager of real estate assets in Canada and the United States, the REIT is subject to various laws relating to environmental matters. These laws impose a liability for the cost of removal and remediation of certain hazardous materials released or deposited on properties owned by the REIT on or adjacent properties.

In accordance with best management practices, Phase 1 environmental audits are reviewed on all properties prior to acquisition. Further investigation is conducted if Phase 1 tests indicate a potential problem. The REIT has operating policies to monitor and manage risk. In addition, the standard lease utilized requires tenants to comply with environmental laws and regulations, and restricts tenants from carrying on environmentally hazardous activities or having environmentally hazardous substances on site.

### **Tax Risk**

The Tax Act includes rules (referred to herein as the "SIFT Rules") which effectively tax certain income of a publicly traded trust or partnership that is distributed to its investors on the same basis as would have applied had the income been earned through a taxable corporation and distributed by way of dividend to its shareholders. Significant relieving amendments to the SIFT Rules received royal assent on June 26, 2013. The SIFT Rules apply only to "SIFT trusts", "SIFT partnerships" (each as defined in the Tax Act, and collectively, "SIFTs") and their investors. A trust that qualifies as a "real estate investment trust" (as defined in the Tax Act) for a taxation year will not be considered to be a SIFT trust in that year (the "REIT Exemption").

Based on a review of the REIT's assets and revenues, management believes that the REIT satisfied the tests to qualify for the REIT Exemption for 2013. Management of the REIT intends to conduct the affairs of the REIT so that it qualifies for the REIT Exemption at all times. However, as the REIT Exemption includes complex revenue and asset tests, no assurances can be provided that the REIT will continue to qualify for any subsequent year.

On December 12, 2013, amendments to the Tax Act impacting certain publicly traded stapled securities of SIFTs, REITs and corporations, including amendments which will deny a deduction for certain payments made by another entity to a REIT, or to a subsidiary of a REIT (the "Stapled Security Rules") were enacted into law. Management of each of the REIT and Finance Trust has reviewed the Stapled Security Rules and has concluded that the Stapled Security Rules should not materially adversely affect the REIT, Finance Trust or holders of Stapled Units. However, no assurances can be given in this regard.

There can be no assurance that income tax laws and the treatment of mutual fund trusts will not be changed in a manner which adversely affects holders of Stapled Units. If the REIT or Finance Trust ceases to qualify as a "mutual fund trust" under the Tax Act and the units thereof cease to be listed on a designated stock exchange (which currently includes the TSX), the REIT Units or Finance Trust Units, as the case may be, will cease to be qualified investments for registered retirement savings plans, deferred profit sharing plans, registered retirement income funds, registered education savings plans, registered disability savings plans and tax-free savings accounts.

The REIT operates in the United States through U.S. Holdco which is capitalized with debt and equity provided by the REIT and debt in the form of U.S. Holdco Notes owed to Finance Trust. As at December 31, 2013, Finance Trust holds U.S. \$219.8 million of U.S. Holdco Notes.

U.S. Holdco treats the U.S. Holdco Notes as indebtedness for U.S. federal income tax purposes. If the IRS or a court were to determine that the U.S. Holdco Notes should be treated for U.S. federal income tax purposes as equity rather than debt, the interest on the U.S. Holdco Notes could be treated as a dividend, and interest on the U.S. Holdco Notes would not be deductible for U.S. federal income tax purposes. In addition, if the IRS were to determine that the interest rate on the U.S. Holdco Notes did not represent an arm's length rate, any excess amount over the arm's length rate would not be deductible and could be re-characterized as a dividend payment instead of an interest payment. This would significantly increase the U.S. federal income tax liability of U.S. Holdco, potentially including the tax liability for prior years in which U.S. Holdco has claimed a deduction for interest paid on the U.S. Holdco Notes. In addition, U.S. Holdco could be subject to penalties. Such an increase in tax liability could materially adversely affect U.S. Holdco's ability to make interest payments on the U.S. Holdco Notes or the REIT's ability to make distributions on its units. Additionally, payments of interest on the U.S. Holdco Notes considered to be paid to non-U.S. holders of Stapled Units as discussed below could be subject to withholding taxes.

To the extent that the REIT or a related party provided debt financing to U.S. Holdco (e.g., by acquiring U.S. Holdco Notes), in determining income for U.S. tax purposes, U.S. Holdco is subject to possible limitations on the deductibility of interest, if any, paid to the REIT or such related party. Section 163(j) of the Code applies to defer U.S. Holdco's deduction of interest paid on debt to the REIT or such related party in years that (i) the debt to equity ratio of U.S. Holdco exceeded 1.5:1, and (ii) the net interest expense exceeds an amount equal to 50% of its "adjusted taxable income" (generally, earnings before interest, taxes, depreciation, and amortization). The REIT's position is that, due to the treatment of Finance Trust as a grantor trust that is disregarded for U.S. federal tax purposes, the interest paid to Finance Trust is treated as having been paid to the holders of the Finance Trust Units and is therefore not subject to section 163(j). If section 163(j) applied to interest paid to Finance Trust, depending on the facts and circumstances and the availability of net operating losses to U.S. Holdco (which are subject to normal assessment by the IRS), the U.S. federal income tax liability of U.S. Holdco could increase. In such case, the amount of income available for distribution by the REIT to its Unitholders could be reduced.

#### **Additional Tax Risks Applicable to U.S. Holders**

A foreign corporation will be classified as a PFIC for United States federal income tax purposes if either (i) 75% or more of its gross income is passive income or (ii) on average for the taxable year, 50% or more of its assets (by value) produce or are held for the production of passive income. The properties of the REIT are managed by subsidiaries of the REIT rather than directly by its own employees. Although the REIT's officers and employees oversee the activities of the managers, it is unclear whether the REIT will be characterized as a PFIC for U.S. federal income tax purposes. If the REIT were treated as a PFIC, then in the absence of certain elections being made by a U.S. holder of REIT Units, any distributions in respect of the REIT Units which exceed 125% of the average amount of distributions in respect of such REIT Units during the preceding three years, or, if shorter, during the preceding years in the U.S. holder's holding period ("excess distributions") and any gain on a sale or other disposition of the REIT Units would be treated as ordinary income and would be subject to special tax rules, including an interest charge. In addition, if the REIT is treated as a PFIC, then dividends paid on the REIT Units will not qualify for the reduced 20% US federal income tax rate applicable to certain qualifying dividends received by noncorporate taxpayers. U.S. holders should consult with their own tax advisors regarding the implications of these rules and the advisability of making one of the applicable PFIC elections, taking into account their particular circumstances.

Finance Trust qualifies as an investment trust that is classified as a grantor trust for U.S. federal income tax purposes under Treasury Regulation section 301.7701-4(c) (a "Fixed Investment Trust") and section 671 of the Code. In general, an investment trust will qualify

as a Fixed Investment Trust if: (i) the trust has a single class of ownership interests, representing undivided beneficial interests in the assets of the trust; and (ii) there is no power under the trust agreement to vary the investment of the holders. If Finance Trust is a Fixed Investment Trust, then it will generally be disregarded for U.S. federal income tax purposes, with the result that the holders of Finance Trust Units will be treated as owning directly their pro rata shares of all of the Finance Trust assets (i.e. primarily the U.S. Holdco Notes). Moreover, all payments made on the U.S. Holdco Notes will be treated as payments made directly to the holders of the Finance Trust units in proportion to their interest in Finance Trust.

Provided that Finance Trust qualifies as a Fixed Investment Trust and the U.S. Holdco Notes are respected as debt for U.S. federal income tax purposes, payments of principal and interest on the U.S. Holdco Notes that are attributable to U.S. holders will be treated as payments directly to the U.S. holders. Interest on the U.S. Holdco Notes will generally be taxable to U.S. holders as ordinary income at the time it is paid or accrued and will be subject to U.S. federal taxation at a maximum marginal rate of 35%. If the U.S. Holdco Notes were treated as equity rather than debt for U.S. federal income tax purposes, then the stated interest on the U.S. Holdco Notes would be treated as a distribution with respect to units.

A holder of Stapled Units that is a resident of the U.S. for purposes of the Tax Act will generally be subject to Canadian withholding tax under Part XIII of the Tax Act at the rate of 25% on the portion of the income of the REIT and Finance Trust paid or credited (whether in cash or *in specie*) in respect of such Stapled Units, subject to reduction under the *Canada-U.S. Tax Convention* (the "**U.S. Treaty**") if applicable. In the case of income paid or credited on REIT Units, the withholding rate applicable to a U.S. resident holder entitled to the benefits of the U.S. Treaty in respect of such income would generally be reduced to 15%. In the case of income paid or credited to a U.S. resident holder on Finance Trust Units, there is uncertainty as to the appropriate rate of withholding under the U.S. Treaty. Management of Finance Trust is considering whether any changes to the withholding rate currently applied to distributions of income to U.S. holders is required in light of this uncertainty. Any such change could impact the after-tax return realized by U.S. holders on their Stapled Units.

In compliance with U.S. Treasury Department Circular 230, which provides rules governing certain conduct of U.S. tax advisors giving advice with respect to U.S. tax matters, please be aware that: (i) any U.S. federal tax advice contained herein is not intended to be used and cannot be used by the reader for the purpose of avoiding penalties that may be imposed under the Code; (ii) such advice was prepared in the expectation that it may be used in connection with the promotion or marketing (within the meaning of U.S. Treasury Department Circular 230) of Stapled Units; and (iii) prospective investors should seek advice based on their particular circumstances from an independent tax advisor.

### **Dilution**

The number of units each of the Trusts is authorized to issue is unlimited. The trustees have the discretion to issue additional Stapled Units in certain circumstances, including under the REIT's Unit Option Plan. Any issuance of Stapled Units may have a dilutive effect on the investors of Stapled Units.

### **Unitholder Liability**

The Declarations of Trust of each of the REIT and Finance Trust provides that unitholders will have no personal liability for actions of the Trusts and no recourse will be available to the private property of any unitholder for satisfaction of any obligation or claims arising out of a contract or obligation of a trust. Each Declaration of Trust of the REIT and Finance Trust further provides that this lack of unitholder liability, where possible, must be provided for in certain written instruments signed by the applicable Trust. In addition, legislation has been enacted in the Provinces of Ontario and certain other provinces that is intended to provide unitholders in those provinces with limited liability. However, there remains a risk, which the Trusts consider to be remote in the circumstances, that a unitholder could be held personally liable for a Trust's obligations to the extent that claims are not satisfied out of the Trusts' assets. It is intended that the Trusts' affairs will be conducted to seek to minimize such risk wherever possible.

### **Redemption Right**

Unitholders are entitled to have their units redeemed at any time on demand. It is anticipated that this redemption right will not be the primary mechanism for unitholders to liquidate their investments. The aggregate redemption price payable by the Trusts is subject to limitations. In certain circumstances, the REIT's Declaration of Trust provides for the *in specie* distributions of notes of H&R Portfolio LP Trust in the event of redemption of units of the REIT that are part of the Stapled Units. The notes which may be distributed *in specie* to unitholders in connection with a redemption will not be listed on any stock exchange, no established market is expected to develop for such notes and they may be subject to resale restrictions under applicable securities laws.

## Debentures

The likelihood that purchasers of the 2016, 2018 and 2020 convertible debentures and the Series A, B, C, D, E, F, G, H and I Senior Debentures will receive payments owing to them under the terms of such debentures will depend on the financial health of the REIT and its creditworthiness. In addition, such debentures are unsecured obligations of the REIT and are subordinate in right of payment to all the REIT's existing and future senior indebtedness as defined in each such respective trust indenture. Therefore, if the REIT becomes bankrupt, liquidates its assets, reorganizes or enters into certain other transactions, the REIT's assets will be available to pay its obligations with respect to such debentures only after it has paid all of its senior indebtedness in full. There may be insufficient assets remaining following such payments to pay amounts due on any or all of the debentures then outstanding.

The debentures are also effectively subordinate to claims of creditors (including trade creditors) of the REIT's subsidiaries except to the extent the REIT is a creditor of such subsidiaries ranking at least *pari passu* with such other creditors. Finance Trust is a creditor of U.S. Holdco, a subsidiary of the REIT. A parent entity is entitled only to the residual equity of its subsidiaries after all debt obligations of its subsidiaries are discharged. In the event of bankruptcy, liquidation or reorganization of the REIT, holders of indebtedness of the REIT (including holders of the convertible debentures), may become subordinate to lenders to the subsidiaries of the REIT. The indentures governing such debentures do not prohibit or limit the ability of the REIT or its subsidiaries to incur additional debt or liabilities (including senior indebtedness), to amend and modify the ranking of any indebtedness or to make distributions, except, in respect of distributions where an event of default has occurred and such default has not been cured or waived. The indentures do not contain any provision specifically intended to protect holders of debentures in the event of a future leveraged transaction involving the REIT.

## OUTSTANDING UNIT DATA

The beneficial interests in each of the Trusts are represented by a single class of units of each Trust respectively, which are unlimited in number. Each such unit carries a single vote at any meeting of unitholders of the respective Trust. As at February 24, 2014, there were 270,303,206 Stapled Units issued and outstanding (each comprised of a REIT unit and a Finance Trust unit).

As at December 31, 2013, the maximum number of units authorized to be granted under the REIT's Unit Option Plan was 28,000,000. Of this amount, 11,492,120 had been granted and 6,938,799 had been exercised and expired. As at February 24, 2014, there were 4,553,321 options to purchase Stapled Units outstanding of which 2,394,082 are fully vested.

As at December 31, 2013, the maximum number of units authorized to be granted under the REIT's restricted unit option plan was 5,000,000. Of this amount, no Stapled Units have been granted.

The following table lists the principal outstanding balance of the REIT's convertible debentures as at February 24, 2014 and the number of Stapled Units required to convert the convertible debentures to equity:

Convertible Debentures	Principal outstanding as at February 24, 2014	Maximum number of Stapled Units issuable
2016 Convertible Debentures (HR.DB.E)	\$75.0 million	2,918,287
2018 Convertible Debentures (HR.DB.H)	74.4 million	3,009,057
2020 Convertible Debentures (HR.DB.D)	99.7 million	4,240,595

## ADDITIONAL INFORMATION

Additional information relating to the REIT and Finance Trust, including the REIT's Annual Information Form, is available on SEDAR at [www.sedar.com](http://www.sedar.com).

Combined Financial Statements of

**H&R REAL ESTATE INVESTMENT TRUST**  
**and**  
**H&R FINANCE TRUST**

Years ended December 31, 2013 and 2012



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## INDEPENDENT AUDITORS' REPORT

To the Unitholders of H&R Real Estate Investment Trust

We have audited the accompanying combined financial statements of H&R Real Estate Investment Trust and H&R Finance Trust (collectively, the "Trusts"), which comprise the combined statements of financial position as at December 31, 2013 and 2012, the combined statements of comprehensive income, changes in unitholders' equity and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

### *Management's Responsibility for the Combined Financial Statements*

Management is responsible for the preparation and fair presentation of these combined financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of combined financial statements that are free from material misstatement, whether due to fraud or error.

### *Auditors' Responsibility*

Our responsibility is to express an opinion on these combined financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the combined financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the combined financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the combined financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Trusts' preparation and fair presentation of the combined financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trusts' internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the combined financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

### *Opinion*

In our opinion, the combined financial statements present fairly, in all material respects, the combined financial position of the Trusts' as at December 31, 2013 and 2012, and its combined financial performance and its combined cash flows for the years then ended in accordance with International Financial Reporting Standards.

Chartered Professional Accountants, Licensed Public Accountants

February 27, 2014  
Toronto, Canada

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Combined Statements of Financial Position  
(In thousands of Canadian dollars)

	December 31 2013	December 31 2012 (note 3)
<b>Assets</b>		
Real estate assets		
Investment properties (note 4)	\$ 12,786,205	\$ 9,235,562
Properties under development (notes 4 and 5)	146,478	128,220
	<b>12,932,683</b>	<b>9,363,782</b>
Equity accounted investments (note 7)	558,149	276,357
Mortgages and amount receivable	9,687	6,960
Assets classified as held for sale (note 8)	-	27,973
Other assets (note 9)	54,624	66,518
Cash and cash equivalents (note 10)	27,884	131,460
	<b>\$ 13,583,027</b>	<b>\$ 9,873,050</b>
<b>Liabilities and Unitholders' Equity</b>		
Liabilities		
Mortgages payable (note 11)	\$ 4,897,726	\$ 3,813,613
Debentures payable (note 12)	1,532,130	1,203,791
Exchangeable units (note 13)	372,427	131,045
Deferred tax liability (note 28)	76,554	43,407
Unit options payable (note 14(a))	6,313	10,585
Derivative instruments (note 15)	508	601
Loan payable (note 4)	134,713	-
Bank indebtedness (note 16)	116,762	2,905
Accounts payable and accrued liabilities (note 17)	172,093	160,091
	<b>7,309,226</b>	<b>5,366,038</b>
Unitholders' equity	<b>6,273,801</b>	<b>4,507,012</b>
Commitments and contingencies (note 29)		
	<b>\$ 13,583,027</b>	<b>\$ 9,873,050</b>

See accompanying notes to the combined financial statements.

Approved on behalf of the Board of Trustees:

“Robert Dickson” \_\_\_\_\_ Trustee

“Thomas J. Hofstedter” \_\_\_\_\_ Trustee

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Combined Statements of Comprehensive Income  
(In thousands of Canadian dollars)

Years ended December 31, 2013 and 2012

	2013	2012 (note 3)
Property operating income:		
Rentals from investment properties (note 19)	\$ 1,137,017	\$ 799,159
Property operating costs	(387,095)	(256,714)
	<b>749,922</b>	542,445
Net income from equity accounted investments (note 7)	<b>34,032</b>	26,173
Finance costs:		
Finance income	2,108	1,854
Finance cost - operations (note 20)	(309,629)	(232,495)
Gain on extinguishment of debt	-	10,151
Gain (loss) on change in fair value (note 21)	30,972	(5,143)
	<b>(276,549)</b>	(225,633)
Trust expenses	(5,564)	(15,220)
Amortization (note 22)	(7,536)	(5,525)
Fair value adjustment on real estate assets (note 4)	51,872	237,689
Loss on sale of real estate assets	(2,067)	(137)
Gain (loss) on foreign exchange	14,042	(7,007)
Transaction costs (notes 6 and 26)	(204,819)	-
Net income before income taxes	<b>353,333</b>	552,785
Income tax expense (note 28)	(29,698)	(43,925)
Net income	<b>323,635</b>	508,860
Other comprehensive income (loss) (note 18):		
Unrealized gain (loss) on translation of U.S. denominated foreign operations	53,048	(15,399)
Transfer of realized loss on cash flow hedges to net income	414	400
	<b>53,462</b>	(14,999)
Total comprehensive income all attributable to unitholders	<b>\$ 377,097</b>	\$ 493,861

See accompanying notes to the combined financial statements.



# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Combined Statements of Changes in Unitholders' Equity

(In thousands of Canadian dollars)

Years ended December 31, 2013 and 2012

UNITHOLDERS' EQUITY	Value of Units	Accumulated net income	Accumulated distributions	Accumulated other comprehensive income (loss) (note 18)	Total
Unitholders' equity, January 1, 2012	\$ 2,789,459	\$ 2,566,231	\$ (1,635,275)	\$ (9,872)	\$ 3,710,543
Proceeds from issuance of units	218,687	-	-	-	218,687
Issue costs	(6,606)	-	-	-	(6,606)
Net income	-	508,860	-	-	508,860
Distributions to unitholders (note 14(c))	-	-	(215,479)	-	(215,479)
Conversion of convertible debentures (note 12(c)), net	306,006	-	-	-	306,006
Other comprehensive income (loss) (note 18)	-	-	-	(14,999)	(14,999)
Unitholders' equity, December 31, 2012	3,307,546	3,075,091	(1,850,754)	(24,871)	4,507,012
<b>Proceeds from issuance of units</b>	<b>1,514,002</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>1,514,002</b>
<b>Issue costs</b>	<b>(507)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>(507)</b>
<b>Net income</b>	<b>-</b>	<b>323,635</b>	<b>-</b>	<b>-</b>	<b>323,635</b>
<b>Distributions to unitholders (note 14(c))</b>	<b>-</b>	<b>-</b>	<b>(331,040)</b>	<b>-</b>	<b>(331,040)</b>
<b>Conversion of convertible debentures (note 12(c)), net</b>	<b>207,237</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>207,237</b>
<b>Other comprehensive income (loss) (note 18)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>53,462</b>	<b>53,462</b>
<b>Unitholders' equity, December 31, 2013</b>	<b>\$ 5,028,278</b>	<b>\$ 3,398,726</b>	<b>\$ (2,181,794)</b>	<b>\$28,591</b>	<b>\$ 6,273,801</b>

See accompanying notes to the combined financial statements.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Combined Statements of Cash Flows  
(In thousands of Canadian dollars)

Years ended December 31, 2013 and 2012

	2013	2012
		(note 3)
Cash provided by (used in):		
Operations:		
Net income	\$ 323,635	\$ 508,860
Items not affecting cash:		
Net income from equity accounted investments (note 7)	(34,032)	(26,173)
Finance cost - operations (note 20)	309,629	232,495
Rent amortization of tenant inducements (note 19)	1,795	1,465
Amortization (note 22)	7,536	5,525
(Gain) loss on foreign exchange	(14,042)	7,007
Fair value adjustment on real estate assets (note 4)	(51,872)	(237,689)
Gain on extinguishment of debt	-	(10,151)
Loss on sale of real estate assets	2,067	137
Finance cost - gain on change in fair value (notes 15(c) and 21)	(30,972)	(6,205)
Transaction costs paid through issuance of exchangeable units (note 26)	194,845	-
Unit-based compensation (note 14(a))	(4,136)	6,122
Deferred tax liability (note 28)	29,227	43,407
Change in other non-cash operating items (note 23)	(116,289)	(5,495)
	<b>617,391</b>	<b>519,305</b>
Investing:		
Properties under development (notes 4 and 23)	(22,631)	(173,353)
Investment properties:		
Net proceeds on disposition of real estate assets	115,286	48,443
Acquisitions (notes 4 and 23)	(207,400)	(291,191)
Redevelopment (notes 4 and 23)	(76,617)	-
Capital expenditures (note 4)	(33,704)	(19,850)
Leasing expenses and tenant inducements (note 4)	(18,799)	(14,022)
Equity accounted investments, net	(112,875)	(202,010)
Mortgages receivable	9,500	-
Cash assumed on business combination (note 6)	45,108	-
Restricted cash (notes 6 and 9)	30,513	(18,237)
	<b>(271,619)</b>	<b>(670,220)</b>
Financing:		
Bank indebtedness	(11,143)	(437,268)
Interest paid	(294,888)	(278,051)
Mortgages payable:		
New mortgages payable	301,877	1,243,033
Principal repayments	(636,114)	(384,676)
Proceeds from issuance of debentures payable (note 12(c))	467,301	173,389
Redemption of debentures payable (note 12(c))	(5,601)	(31,088)
Proceeds from issuance of units, net of issue costs	(33)	150,848
Finance cost - exchangeable unit distributions (note 20)	(13,967)	(6,389)
Distributions to unitholders (note 14(c))	(256,780)	(158,423)
	<b>(449,348)</b>	<b>271,375</b>
Increase (decrease) in cash and cash equivalents	(103,576)	120,460
Cash and cash equivalents, beginning of year (note 10)	131,460	11,000
Cash and cash equivalents, end of year (note 10)	<b>\$ 27,884</b>	<b>\$ 131,460</b>

See notes on business combination (note 6) and supplemental cash flow information (note 23).

See accompanying notes to the combined financial statements.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

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These combined financial statements include the accounts of H&R Real Estate Investment Trust (the "REIT") and H&R Finance Trust ("Finance Trust", together with the REIT, the "Trusts"). The REIT is an unincorporated open-ended trust and Finance Trust is an unincorporated investment trust both domiciled in Canada. The REIT owns, operates and develops commercial properties across Canada and in the United States. The principal office and centre of administration of the Trusts is located at 3625 Dufferin Street, Suite 500, Toronto, Ontario M3K 1N4. Unitholders of each Trust participate pro rata in distributions of income and, in the event of termination of a Trust, participate pro rata in the net assets remaining after satisfaction of all liabilities of such Trust.

On October 1, 2008, the REIT completed an internal reorganization pursuant to a Plan of Arrangement (the "Plan of Arrangement") as described in the REIT's information circular dated August 20, 2008, resulting in the stapling of the Trusts' units. The Plan of Arrangement further resulted in, among other things, the creation on October 1, 2008 of Finance Trust. Each unitholder received, for each REIT unit held, a unit of Finance Trust. Each issued and outstanding Finance Trust unit is stapled to a unit of the REIT on a one-for-one basis so as to form stapled units ("Stapled Units"), and such Stapled Units are listed and posted for trading on the Toronto Stock Exchange ("TSX") under the symbol HR.UN. The units of each of the Trusts may only be transferred together as Stapled Units unless an event of "uncoupling" has occurred.

On October 24, 2013, the Ontario Securities Commission (on its behalf and on behalf of the other provincial securities regulators) issued a decision which permits the REIT and Finance Trust to file one set of combined financial statements rather than separate financial statements. These combined financial statements are being presented on a basis whereby the assets and liabilities of the REIT and Finance Trust have been combined in accordance with the accounting principles applicable to both the REIT and Finance Trust in accordance with International Financial Reporting Standards ("IFRS") to reflect the financial position and results of the REIT and Finance Trust on a combined basis. The combined presentation is useful to the unitholders of the Trusts, on the following basis:

- The units of the Trusts are stapled (as noted above), resulting in the Trusts being under common ownership;
- A support agreement between the Trusts ensures that until such time as an event of "uncoupling" occurs, when units are issued by the REIT, units must also be issued by Finance Trust simultaneously so as to maintain the stapled unit structure;
- The sole activity of Finance Trust is to provide capital funding to H&R REIT (U.S.) Holdings Inc. ("U.S. Holdco"), a wholly owned U.S. subsidiary of the REIT; and
- The investment activities of Finance Trust are restricted in its Declaration of Trust to providing such funding to U.S. Holdco and to make temporary investments of excess funds.

### **1. Basis of preparation:**

#### **(a) Statement of compliance**

These combined financial statements have been prepared in accordance with IFRS as published by the International Accounting Standards Board ("IASB") and using accounting policies described herein.

The combined financial statements were approved by the Board of Trustees of the REIT on February 27, 2014.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

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### 1. Basis of preparation (continued):

#### (b) Basis of measurement

The combined financial statements have been prepared on the historical cost basis except for the following material items in the combined statements of financial position which have been measured at fair value:

- (i) Real estate assets;
- (ii) Derivative financial instruments;
- (iii) Liabilities for cash-settled unit-based compensation;
- (iv) Convertible debentures; and
- (v) Exchangeable units.

#### (c) Functional currency and presentation

These combined financial statements are presented in Canadian dollars, which is the Trusts' functional currency. All financial information presented in Canadian dollars has been rounded to the nearest thousand.

The Trusts present their combined statements of financial position based on the liquidity method, where all assets and liabilities are presented in ascending order of liquidity.

#### (d) Use of estimates and judgements

The preparation of these combined financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies, the reported amounts of assets, liabilities, income and expenses and disclosure of contingent assets and liabilities at the date of the combined financial statements. Actual results may differ from these estimates.

##### (i) Use of estimates

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected. Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment within the next financial year are included in the following notes:

- Fair value of real estate assets;
- Fair value of financial instruments;
- Fair value of cash-settled unit-based compensation;
- Fair value of convertible debentures; and
- Fair value of exchangeable units.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

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### 1. Basis of preparation (continued):

#### (ii) Use of judgements

The critical judgements made in applying accounting policies that have the most significant effect on the amounts recognized in these combined financial statements are as follows:

- Business combination

Accounting for business combinations under IFRS 3, *Business Combinations* ("IFRS 3") is only applicable if it is determined that a business has been acquired. Under IFRS 3, a business is defined as an integrated set of activities and assets conducted and managed for the purpose of providing a return to investors or lower costs or other economic benefits directly and proportionately to the REIT. A business generally consists of inputs, processes applied to those inputs, and resulting outputs that are, or will be, used to generate revenues. In the absence of such criteria, a group of assets is deemed to have been acquired. If goodwill is present in a transferred set of activities and assets, the transferred set is presumed to be a business. Judgement is used by management in determining whether the acquisition of an individual property qualifies as a business combination in accordance with IFRS 3 or as an asset acquisition.

- Valuations of real estate assets

Real estate assets, which consist of investment properties and properties under development, are carried on the combined statements of financial position at fair value, as determined by either qualified external valuation professionals or by management. The valuations are based on a number of assumptions, such as appropriate discount rates and capitalization rates and estimates of future rental income, operating expenses and capital expenditures. Valuation of real estate assets is one of the principal estimates and uncertainties of these combined financial statements. Refer to note 4 for further information on estimates and assumptions made in the determination of the fair value of real estate assets.

- Leases

The REIT makes judgements in determining whether certain leases, in particular those tenant leases with long contractual terms and long-term ground leases where the REIT is the lessor, are operating or finance leases. The REIT has determined that all of its leases are operating leases.

- Income taxes

The REIT is a mutual fund trust and a real estate investment trust pursuant to the *Income Tax Act* (Canada) ("Tax Act"). Under current tax legislation, the REIT is not liable to pay Canadian income tax provided that its taxable income is fully distributed to unitholders each year. The REIT is a real estate investment trust if it meets prescribed conditions under the Tax Act relating to the nature of its assets and revenue (the "REIT Conditions"). The REIT has reviewed the REIT Conditions and has assessed its interpretation and application to the REIT's assets and revenue, and it has determined that it qualifies as a real estate investment trust pursuant to the Tax Act. The REIT expects to continue to qualify as a real estate investment trust; however, should it no longer qualify it would not be able to flow through its taxable income to unitholders and the REIT would be subject to tax.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

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### 1. Basis of preparation (continued):

- Tenant improvements

The REIT makes judgements with respect to whether tenant improvements provided in connection with a lease enhance the value of the leased property, which determines whether such amounts are capitalized to investment properties.

- Impairment of equity accounted investments

The REIT determines at each reporting date whether there is any objective evidence that the equity accounted investments are impaired. If so, the REIT calculates the amount of impairment as the difference between the recoverable amount of the equity accounted investment and its carrying value and recognizes the amount in net income.

### 2. Significant accounting policies:

The accounting policies set out below have been applied consistently for all periods presented in these combined financial statements.

#### (a) *Basis of combination:*

The principles used to prepare these combined financial statements are similar to those used to prepare consolidated financial statements. The combined financial statements include the assets, liabilities, unitholders' equity, comprehensive income (loss) and operating results of the Trusts, after elimination of the following:

- (i) the REIT's notes payable to Finance Trust; and
- (ii) the REIT's interest expense and Finance Trust's interest income from the notes payable to Finance Trust.

The foreign exchange gain (loss) recorded in net income as a result of exchanging Finance Trust's U.S. dollar note receivable from U.S. Holdco is not eliminated on combination as it flows through net income on Finance Trust's books and other comprehensive income on the REIT's books. This is because U.S. Holdco is a subsidiary of the REIT and forms part of its net investment in the United States, but is not a subsidiary of Finance Trust.

The combination of the Trusts does not result in the elimination of the equity of Finance Trust as neither of the Trusts hold any interest in the other. The equity of the Trusts is presented by way of combining the two together.

#### (b) *Basis of consolidation:*

These combined financial statements include the accounts of all entities in which the REIT holds a controlling interest. The REIT carries out a portion of its activities through joint operations and records its proportionate share of assets, liabilities, revenues, expenses and cash flows of all joint operations in which it participates. All material intercompany transactions and balances have been eliminated upon consolidation.

#### (c) *Investment properties:*

Investment properties are held to earn rental income or for capital appreciation, or both, but not for sale in the ordinary course of business. All of the REIT's commercial properties are investment properties which are measured at fair value.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

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### 2. Significant accounting policies (continued):

The REIT performs an assessment of each investment property acquired to determine whether the acquisition is to be accounted for as an asset acquisition or a business combination. A transaction is considered to be a business combination if the acquired property meets the definition of a business: an integrated set of activities and assets that are capable of being managed for the purpose of providing a return to the unitholders. The REIT expenses transaction costs on business combinations and capitalizes transaction costs on asset acquisitions.

Upon acquisition, investment properties are initially recorded at cost. Subsequent to initial recognition, the REIT uses the fair value model to account for investment properties. Under the fair value model, investment properties are recorded at fair value, determined based on available market evidence at each reporting date. The related gain or loss in fair value is recognized in net income in the year in which it arises.

Subsequent capital expenditures are charged to investment properties only when it is probable that future economic benefits of the expenditure will flow to the REIT and the cost can be measured reliably. All other repairs and maintenance costs are expensed when incurred.

Gains or losses from the disposal of investment properties are determined as the difference between the net disposal proceeds and the carrying amount of the investment property and are recognized in net income in the year of disposal.

#### (d) *Properties under development:*

Properties under development for future use as investment property are accounted for as investment property under IAS 40, *Investment Property*. Costs eligible for capitalization to properties under development are initially recorded at cost, and subsequent to initial recognition are accounted for using the fair value method. At each reporting date, the properties under development are recorded at fair value based on available market evidence. The related gain or loss in fair value is recognized in net income in the year in which it arises.

The cost of properties under development includes direct development costs, realty taxes and borrowing costs that are directly attributable to the development. Borrowing costs associated with direct expenditures on properties under development are capitalized. Borrowing costs relating to the purchase of a site or property acquired for redevelopment are also capitalized. The amount of borrowing costs capitalized is determined first by reference to borrowing specific to the project, where relevant, and otherwise by applying a weighted average cost of borrowings to eligible expenditures after adjusting for borrowings associated with other specific developments. Borrowing costs are capitalized from the commencement of the development until the date of practical completion. The capitalization of borrowing costs is suspended if there are prolonged periods when development activity is interrupted.

Upon practical completion of a development, the development property is transferred to investment properties at the fair value on the date of practical completion. The REIT considers practical completion to have occurred when the property is capable of operating in the manner intended by management. Generally this occurs upon completion of construction and receipt of all necessary occupancy and other material permits. Where the REIT has pre-leased space as of or prior to the start of the development and the lease requires the REIT to construct tenant improvements which enhance the value of the property, practical completion is considered to occur on completion of such improvements.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

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### 2. Significant accounting policies (continued):

#### (e) *Assets held for sale and discontinued operations:*

Non-current assets comprising assets and liabilities, that are expected to be recovered primarily through sale rather than through continuing use, are classified as held for sale. For this purpose, a sale is highly probable if management is committed to a plan to achieve the sale; there is an active program to find a buyer; the non-current asset is being actively marketed at a reasonable price; the sale is anticipated to be completed within one year from the date of classification; and it is unlikely there will be changes to the plan.

In accordance with IFRS 5, *Non-Current Assets Held for Sale and Discontinued Operations*, investment properties that constitute a component of the REIT that has either been disposed of or are classified as held for sale are presented as discontinued operations in all periods presented if the property operations are expected to be eliminated and the REIT will not have significant continuing involvement following the disposition. A component of the REIT will generally represent a major line of business or geographical area of operation.

#### (f) *Amortization:*

Leasing costs, such as commissions and tenant inducements, are deferred and amortized on a straight-line basis over the terms of the related leases.

#### (g) *Revenue recognition:*

The REIT retains substantially all of the benefits and risks of ownership of its investment properties and therefore, accounts for its leases with tenants as operating leases. Rentals from investment properties include all amounts earned from tenants, including recovery of operating costs.

Rental revenue from investment property is recognized in net income on a straight-line basis over the term of the related lease. The difference between the rental revenue recognized and the amounts contractually due under the lease agreements is recorded in accrued rent receivable. Lease incentives granted are recognized as an integral part of total rental income over the term of the lease.

#### (h) *Income taxes:*

Income tax expense comprises current and deferred tax. Current tax and deferred tax are recognized in net income except to the extent that it relates to a business combination, or items recognized directly in equity or in other comprehensive income (loss).

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.



# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

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### 2. Significant accounting policies (continued):

The REIT is a mutual fund trust and a real estate investment trust pursuant to the Tax Act. Under current tax legislation, a real estate investment trust is entitled to deduct distributions of taxable income such that it is not liable to pay income tax provided that its taxable income is fully distributed to unitholders. The REIT intends to continue to qualify as a real estate investment trust and to make distributions not less than the amount necessary to ensure that the REIT will not be liable to pay income taxes.

The REIT qualified as a real estate investment trust throughout 2013 and the 2012 comparative year. Deferred tax is not recognized for the following temporary differences: the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable net income, and differences relating to investments in subsidiaries and jointly controlled entities to the extent that it is probable that they will not reverse in the foreseeable future. In addition, deferred tax is not recognized for taxable temporary differences arising on the initial recognition of goodwill. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, if such entities intend to settle current tax liabilities and assets on a net basis or the entities tax assets and liabilities will be realized simultaneously.

A deferred tax asset is recognized for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

Finance Trust qualifies as a mutual fund trust that is not a specified investment flow-through trust under the Tax Act. In accordance with the terms of Finance Trust's Declaration of Trust, all of the net income for tax purposes will be paid or be payable to unitholders in the taxation year so that no income tax is payable by Finance Trust. For financial statement reporting purposes, the tax deductibility of Finance Trust's distributions is treated as an exemption from taxation as Finance Trust has distributed and is committed to continue distributing all of its taxable income to its unitholders.

#### (i) *Unit option plan:*

The REIT has a unit option plan available for REIT trustees, officers, employees and consultants as disclosed in note 14(a). The unit option plan is considered to be a cash-settled liability under IFRS 2, *Share-based Payment* and as a result is measured at each reporting period and at settlement date at its fair value as defined by IFRS. The fair value of the amount payable to participants in respect of the unit option plan is recognized as an expense with a corresponding increase or decrease in liabilities, over the period that the employees unconditionally become entitled to payment. Any change in the fair value of the liability is recognized as a component of trust expenses.

#### (j) *Cash and cash equivalents:*

Cash and cash equivalents include deposits in banks, certificates of deposit and short-term investments with original maturities of less than 90 days.

#### (k) *Restricted cash:*

Restricted cash includes amounts held in reserve by lenders to fund mortgage payments, repairs and capital expenditures or property tax payments.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

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### 2. Significant accounting policies (continued):

(l) *Foreign currency translation:*

The REIT accounts for its investments in U.S. Holdco, a wholly owned subsidiary of the REIT, in the United States ("foreign operations") as a U.S. denominated foreign operation. Assets and liabilities of foreign operations are translated into Canadian dollars at the exchange rates in effect at the combined statement of financial position dates and revenue and expenses are translated at the average exchange rates for the reporting periods.

The foreign currency translation adjustment is recorded as a separate component of accumulated other comprehensive income (loss) until there is a reduction in the REIT's net investment in the foreign operations. The U.S. dollar denominated bank indebtedness is designated as a hedge of the REIT's investment in self-sustaining operations. Accordingly, the accumulated unrealized gains or losses arising from the translation of this obligation are recorded as a foreign currency translation adjustment in accumulated other comprehensive income (loss).

Finance Trust's U.S. dollar denominated assets and liabilities are translated into Canadian dollars at the exchange rates in effect at the combined statements of financial position dates and revenue and expenses are translated at the actual exchange rate on the date incurred, resulting in any gain (loss) recorded in comprehensive income.

(m) *Financial instruments:*

(i) Non-derivative financial assets

Cash and cash equivalents, restricted cash, accounts receivable and mortgages and amount receivable, with fixed or determinable payments that are not quoted in an active market, are non-derivative financial assets classified as loans and receivables. Such assets are recognized initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition, loans and receivables are measured at amortized cost using the effective interest method, less any impairment losses.

The Trusts derecognize a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Financial assets and liabilities are offset and the net amount presented in the combined statements of financial position when, and only when, the Trusts have a current legal right to offset the amounts and intends either to settle on a net basis or to realize the asset and settle the liability simultaneously.

(ii) Non-derivative financial liabilities

Non-derivative financial liabilities consist of mortgages payable, loan payable, senior debentures, bank indebtedness and accounts payable and accrued liabilities. Such financial liabilities are recognized initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition these financial liabilities are measured at amortized cost using the effective interest method.

The Trusts derecognize a financial liability when its contractual obligations are discharged or cancelled or expire.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

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### 2. Significant accounting policies (continued):

#### (iii) Derivative financial instruments

The REIT holds derivative financial instruments to hedge its foreign currency and interest rate risk exposures. Derivatives are recognized initially at fair value; attributable transaction costs are recognized in net income as incurred. Subsequent to initial recognition, derivatives are measured at fair value at the end of each reporting period. Any resulting gain or loss is recognized in net income immediately unless the derivative is designated and effective as a hedging instrument. None of the REIT's derivative instruments are accounted for as hedges.

#### (iv) Financial liabilities measured at fair value through net income

A financial liability is classified at fair value through net income if it is classified as held for trading or is designated as such upon initial recognition.

The convertible debentures, exchangeable units and unit options payable, were designated at fair value through net income upon initial recognition. Any gains or losses arising on remeasurement are recognized in net income.

#### (n) *Stapled Units:*

Under IAS 32, *Financial Instruments: Presentation* ("IAS 32"), puttable instruments, such as the Stapled Units are generally classified as financial liabilities unless the exemption criteria are met for equity classification. As a result of the REIT receiving consent of its unitholders to modify the REIT's Declaration of Trust to eliminate the mandatory distribution and leave distributions to the discretion of the trustees and the ability of the trustees to fund distributions by way of issuing additional units prior to the amendment, the REIT met the exemption criteria under IAS 32 for equity classification. Finance Trust also met the exemption criteria under IAS 32 for equity classification. Nevertheless, the Stapled Units are not considered ordinary units under IAS 33, *Earnings Per Share*, and therefore an income per unit calculation is not presented.

#### (o) *Finance costs:*

Finance costs are comprised of interest expense on borrowings, distributions on exchangeable units classified as liabilities, gain (loss) on change in fair value of convertible debentures, gain (loss) on change in fair value of exchangeable units, net gain (loss) on derivative instruments and gain on extinguishment of debt.

Finance costs associated with financial liabilities presented at amortized cost are recognized in net income using the effective interest method.

#### (p) *Investments in associates:*

An associate is an entity over which the Trust has significant influence. Significant influence is the power to participate in an entity's financial and operating policy decisions, which is presumed to exist when an investor holds 20 percent or more of the voting power of another entity. An investment is considered an associate when significant influence exists but there is no joint control over the investment. The Trusts account for investments in associates using the equity method.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

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### 2. Significant accounting policies (continued):

(q) *Joint Operations:*

The Trusts consider investments in joint arrangements to be a joint operation when they jointly make operating, financial and strategic decisions over one or more investment properties with another party and have direct rights to the assets, and obligations for the liabilities relating to the arrangement. When the arrangement is considered to be a joint operation, the Trusts will include their share of the underlying assets, liabilities, revenue and expenses in their financial results.

(r) *Joint Ventures:*

The Trusts consider investments in joint arrangements to be joint ventures when they jointly own one or more investment properties with another party and have rights to the net assets of the arrangements. This occurs when the joint arrangement is structured through a separate vehicle, such as a partnership, with separation maintained. When the arrangement is considered to be a joint venture, the Trusts will account for it using equity accounting.

Under equity accounting, the investment in a joint venture is carried on the combined statements of financial position at cost, adjusted for the Trusts' proportionate share of post-acquisition changes in the joint venture's net assets, less any identified impairment loss. The Trusts' share of profits and losses is recognized in the share of net income from joint venture investments in the combined statements of comprehensive income and the Trusts' other comprehensive income includes their share of the joint ventures' other comprehensive income.

A joint venture is considered to be impaired if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the joint venture and that event has a negative impact on the future cash flows of the joint venture that can be reliably estimated.

(s) *Business Combinations:*

The purchase method of accounting is used for acquisitions meeting the definition of a business. The consideration transferred in a business combination is measured at fair value, which is calculated as the sum of the acquisition date fair values of the assets transferred by the REIT, the liabilities incurred by the REIT to former owners of the acquiree, and the equity interests issued by the REIT.

Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their acquisition date fair values. The excess of the cost of acquisition over the fair value of the REIT's share of the identifiable net assets acquired, if any, is recorded as goodwill. If the cost of acquisition is less than the fair value of the REIT's share of the net assets acquired, the difference is recognized directly in the combined statements of comprehensive income for the year as an acquisition gain. Any transaction costs incurred with respect to the business combination are expensed in the period incurred.

(t) *Segmented Reporting:*

A reportable operating segment is a distinguishable component of the Trusts that is engaged either in providing related products or services (business segment) or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other reportable segments. The Trusts have both operating segments and geographic segments.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

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### 2. Significant accounting policies (continued):

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker, determined to be the Chief Executive Officer ("CEO"). The Trusts have two operating segments, the H&R portfolio ("H&R portfolio") and the Primaris Retail Real Estate Investment Trust ("Primaris") portfolio ("Primaris portfolio"). The H&R portfolio includes: (i) all the properties owned by the REIT prior to the acquisition of Primaris, (ii) acquisitions which the CEO deems to be part of the H&R portfolio and (iii) Finance Trust. The Primaris portfolio includes: (i) all the properties acquired from Primaris and (ii) acquisitions which the CEO deems to be part of the Primaris portfolio. The operating segments derive their revenue primarily from rental income from lessees. All of the Trusts' operating activities are reported within the H&R portfolio and the Primaris portfolio segments.

Geographic segments are separated into Canadian and U.S. properties. All of the Trusts' operating activities are reported within the Canadian and U.S. property geographic segments.

#### (u) *New standards and interpretations not yet adopted:*

Standards issued but not yet effective up to the date of issuance of these combined financial statements are described below. The Trusts intend to adopt these standards when they become effective.

##### (i) *Financial Instruments: Classification and Measurement ("IFRS 9")*

IFRS 9 as issued reflects the IASB's work to date on the replacement of IAS 39, *Financial Instruments - Recognition and Measurement* ("IAS 39"), and applies to classification and measurement of financial assets as defined in IAS 39. The approach to classifying an asset as either amortized cost or fair value in IFRS 9 is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of its financial assets. IFRS 9 also allows for separately identifiable and reliably measurable components of both financial and non-financial items to be hedged. The effective date for adoption for this standard has not yet been determined. In subsequent phases, the IASB will address impairment. The Trusts have not yet determined the impact of IFRS 9 on its combined financial statements.

##### (ii) *Levies ("IFRIC 21")*

In 2013, the IASB issued a new interpretation, IFRIC 21, *Levies*. IFRIC 21 addresses accounting for a liability to pay a levy if that liability is within the scope of IAS 37, *Provisions, Contingent Liabilities and Contingent Assets* and liabilities to pay a levy where the timing and amount is certain. This interpretation is effective for annual periods beginning on or after January 1, 2014, and is to be applied retrospectively. The Trusts have not yet determined the impact of IFRIC 21 on its combined financial statements.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

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### 3. Change in accounting policies:

- (a) Effective January 1, 2013, the Trusts have adopted IFRS 10, *Consolidated Financial Statements* ("IFRS 10"), which replaces IAS 27, *Consolidated and Separate Financial Statements*. Under IFRS 10, the Trusts will now assess whether it has control over an investee by determining when: (i) it has power over the investee; (ii) it is exposed or has rights to variable returns from its involvement with that investee; and (iii) it has the ability to affect those returns through its power over that investee. The Trusts have assessed the impact of adopting IFRS 10 and has determined that it has no significant impact on the combined financial statements.
- (b) Effective January 1, 2013, the Trusts have adopted IFRS 11, *Joint Arrangements* ("IFRS 11"), which replaces IAS 31, *Interests in Joint Ventures*. IFRS 11 separates investments in joint arrangements into two types: joint operations and joint ventures. The Trusts have assessed its investments in joint arrangements to determine which type of arrangement they are, and whether there is a change from its historical accounting for these joint arrangements. Based on the guidance in IFRS 11, the Trusts have reassessed their investments in joint arrangements to determine whether the historical accounting for these investments will change under the new standards. This change in accounting policy was applied on a retrospective basis.
- (c) Effective January 1, 2013, the Trusts adopted IFRS 12, *Disclosure of Interests in Other Entities* ("IFRS 12") which replaces the existing disclosure requirements for entities that have interests in subsidiaries, joint arrangements and associates. This standard also contains disclosure requirements for entities that have interests in unconsolidated structured entities. These disclosures aim to provide information in order to enable users to evaluate the nature of, and the risks associated with, an entity's interest in other entities, and the effects of those interests on the entity's financial position, financial performance and cash flows. The adoption of IFRS 12 has resulted in the Trusts expanding their disclosure relating to interests in other entities, as shown in note 7.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

### 3. Change in accounting policies (continued):

The impact of the adoption of IFRS 11 on the combined Statements of Financial Position as discussed in note 3(b) is as follows:

Combined Statements of Financial Position:	December 31, 2012		
	As originally reported	Impact of adoption	Restated
<b>Assets</b>			
<b>Real estate Assets</b>			
Investment properties	\$ 9,807,062	\$ (571,500)	\$ 9,235,562
Properties under development	128,220	-	128,220
	9,935,282	(571,500)	9,363,782
Equity accounted investments	-	276,357	276,357
Mortgages and amount receivable	6,960	-	6,960
Assets classified as held for sale	27,973	-	27,973
Other assets	67,122	(604)	66,518
Cash and cash equivalents	134,470	(3,010)	131,460
	\$ 10,171,807	\$ (298,757)	\$ 9,873,050
<b>Liabilities and Unitholders' Equity</b>			
<b>Liabilities</b>			
Mortgages payable	\$ 4,095,915	\$ (282,302)	\$ 3,813,613
Debentures payable	1,203,791	-	1,203,791
Exchangeable units	131,045	-	131,045
Deferred tax liability	43,407	-	43,407
Unit options payable	10,585	-	10,585
Derivative Instruments	601	-	601
Bank indebtedness	2,905	-	2,905
Accounts payable and accrued liabilities	176,546	(16,455)	160,091
	5,664,795	(298,757)	5,366,038
Unitholders' equity	4,507,012	-	4,507,012
	\$ 10,171,807	\$ (298,757)	\$ 9,873,050

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

### 3. Change in accounting policies (continued):

The impact of the change in accounting policy made by the Trusts, as discussed in note 3(b), on the year ended December 31, 2012 is as follows:

<b>Combined Statements of Comprehensive Income:</b>	<b>As originally reported</b>	<b>Impact of adoption</b>	<b>Restated</b>
Property operating income:			
Rentals from investment properties	\$ 835,303	\$ (36,144)	\$ 799,159
Property operating costs	(272,562)	15,848	(256,714)
	562,741	(20,296)	542,445
Net income from equity accounted investments	-	26,173	26,173
Finance costs:			
Finance income	1,872	(18)	1,854
Finance cost - operations	(239,455)	6,960	(232,495)
Gain on extinguishment of debt	10,151	-	10,151
Gain (loss) on change in fair value	(7,736)	2,593	(5,143)
	(235,168)	9,535	(225,633)
Trust expenses	(15,220)	-	(15,220)
Amortization of leasing expenses	(5,525)	-	(5,525)
Fair value adjustment of real estate assets	253,101	(15,412)	237,689
Loss on sale of real estate assets	(137)	-	(137)
Loss on foreign exchange	(7,007)	-	(7,007)
Net income before income taxes	552,785	-	552,785
Income tax expense	(43,925)	-	(43,925)
Net income	508,860	-	508,860
Other comprehensive income (loss):			
Unrealized loss on translation of U.S. denominated foreign operations	(15,399)	-	(15,399)
Transfer of realized loss on cash flow hedges to net income	400	-	400
	(14,999)	-	(14,999)
Total comprehensive income all attributable to unitholders	\$ 493,861	\$ -	\$ 493,861

### Combined Statements of Cash Flows:

The adjustments noted above have also been made to the combined statements of cash flows for the year ended December 31, 2012. This change in accounting policies did not result in other significant changes to the combined statements of cash flows.



# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

#### 4. Real estate assets:

	Investment Properties 2013	Properties Under Development 2013	Investment Properties 2012*	Properties Under Development 2012
Opening balance, beginning of year	\$ 9,235,562	\$ 128,220	\$ 7,094,147	\$ 1,721,743
Acquisition of investment properties through business combination (note 6)	3,179,418	-	-	-
Acquisitions of investment properties, including transaction costs	211,360	-	298,364	-
Additions to existing investment properties:				
Capital expenditures	33,704	-	19,850	-
Direct leasing costs	18,799	-	14,022	-
Redevelopment	52,196	-	-	-
Additions to properties under development	-	22,631	-	196,288
Dispositions	(183,433)	(4,373)	(133,153)	(17,824)
Transfer of investment properties to assets classified as held for sale	-	-	(27,800)	-
Amortization of leasing costs, straight-line rents and blend and extend rents included in revenue	31,003	-	(4,573)	29,673
Transfer of property under development that has reached practical completion to investment properties	-	-	1,747,966	(1,747,966)
Change in foreign exchange	155,724	-	(64,644)	-
Fair value adjustment on real estate assets	51,872	-	291,383	(53,694)
Closing balance, end of year	\$ 12,786,205	\$ 146,478	\$ 9,235,562	\$ 128,220

\* These amounts have been restated for the effect of the accounting policy change as described in note 3(b).

Legal title to each of the properties in the United States is held by a separate legal entity which is 100% owned, directly or indirectly, by U.S. Holdco, a wholly owned subsidiary of the REIT. The assets of each such separate legal entity are not available to satisfy the debts or obligations of any other person or entity. Each such separate legal entity maintains separate books and records. The identity of the owner of a particular United States property is available from U.S. Holdco. This structure does not prevent distributions to the entity owners provided there are no conditions of default.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

#### 4. Real estate assets (continued):

##### Asset Acquisitions:

During the year ended December 31, 2013, the REIT acquired five investment properties, two equity accounted investments and a parcel of land adjacent to an existing investment property (December 31, 2012 - 11 investment properties and one equity accounted investment). The results of operations for these acquisitions are included in these combined financial statements from the date of acquisition.

The following table summarizes the cost plus transaction costs incurred and expected to be incurred of the assets and liabilities as at the respective dates of acquisition:

	2013	2012
<b>Assets</b>		
Investment properties	\$ 210,355	\$ 296,683
Equity accounted investments:		
Investment in associate	306,177	-
Joint ventures	16,729	439,062
<b>Liabilities</b>		
Mortgages payable, net of mark to market adjustments	-	(7,173)
Loan payable*	(134,713)	-
<b>Total identifiable net assets settled by cash</b>	<b>\$ 398,548</b>	<b>\$ 728,572</b>

\* 50% of the loan payable balance is due February 2015 and the remaining balance is due February 2016. However, should ECHO require funds for qualified asset acquisitions, a portion of the full outstanding deferred payment would be payable on accelerated demand at ECHO's option.

During the year ended December 31, 2013, the REIT incurred additional costs of \$1,005 (December 31, 2012 - \$1,681) in respect to prior year acquisitions which are not included in the above table.

##### Fair value disclosure:

The estimated fair values of the REIT's real estate assets are based on the following methods and key assumptions:

- (i) Consideration of recent sales of similar properties within similar market areas;
- (ii) The discounted cash flow analysis which is based upon, among other things, rental income from current leases and assumptions about rental income from future leases reflecting market conditions at each reporting period, less future cash outflows in respect of such leases discounted generally over a term of ten years;
- (iii) The direct capitalization method which is based on the conversion of current earnings directly into an expression of fair value. The normalized net income for the year is divided by an overall capitalization rate; and
- (iv) The use of external independent appraisers. During the year ended December 31, 2013, certain properties were valued by professional external independent appraisers. These properties make up 27.7% of the investment properties as at December 31, 2013 (year ended December 31, 2012 - 38.7%). The remainder of the portfolio is valued by the REIT's internal valuation team. The properties that are externally appraised are judgmentally selected by management to form a representative cross section of the REIT's portfolio based on size, geography and the availability of market data. In addition, an external independent appraisal is often obtained for properties acquired or properties where the associated mortgage is being refinanced.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

#### 4. Real estate assets (continued):

The REIT utilizes external industry sources to determine a range of capitalization and discount rates. To the extent that the externally provided capitalization and discount rates ranges change from one reporting period to the next, the fair value of the investment properties would increase or decrease accordingly.

The REIT has utilized the following weighted average discount rates and terminal capitalization rates in estimating the fair value of the investment properties:

	Discount Rates			Terminal Capitalization Rates		
	Canada	United States		Canada	United States	
		Total	Total		Total	Total
December 31, 2013	6.56%	7.54%	6.74%	5.98%	7.18%	6.20%
December 31, 2012	6.67%	7.59%	6.89%	6.23%	7.22%	6.47%

Weighted Average Overall Capitalization Rates	2013			2012		
	REIT	Primaris	Total	REIT	Primaris	Total
Canada	6.22%	5.47%	5.99%	6.47%	-	6.47%
United States	6.69%	-	6.69%	6.90%	-	6.90%
Total	6.34%	5.47%	6.12%	6.60%	-	6.60%

The weighted average overall capitalization rate as at December 31, 2013 is determined using the property operating income for the three months ended December 31, 2013 (December 31, 2012 - based on the three months ended December 31, 2012). The calculation of the capitalization rate is adjusted for: straight-lining of contractual rent, rent amortization of tenant inducements, one-time non-recurring capital expenditure recoveries and other sundry income. The average capitalization rate at December 31, 2012 excludes the Bow as it was not generating full property operating income during the year ended December 31, 2012.

#### Fair value sensitivity:

The REIT's investment properties are classified as fair value level 3 assets under the fair value hierarchy, as the inputs in the valuations of these investment properties are not based on observable market data. The following table provides a sensitivity analysis for the weighted average capitalization rate applied as at December 31, 2013:

Capitalization Rate Sensitivity Increase (Decrease)	Weighted Average Overall Capitalization Rate	Fair Value of Investment Properties	Fair Value Variance	Ratio of Debt <sup>(1)</sup> to Total Assets
(0.75)%	5.37%	\$ 14,571,988	\$ 1,785,783	43.5%
(0.50)%	5.62%	\$ 13,923,768	\$ 1,137,563	45.4%
(0.25)%	5.87%	\$ 13,330,762	\$ 544,557	47.3%
<b>December 31, 2013</b>	<b>6.12%</b>	<b>\$ 12,786,205</b>	<b>\$</b>	<b>49.2%</b>
0.25%	6.37%	\$ 12,284,392	\$ (501,813)	51.1%
0.50%	6.62%	\$ 11,820,480	\$ (965,725)	52.9%
0.75%	6.87%	\$ 11,390,331	\$ (1,395,874)	54.8%

(1) For the above calculation, debt includes mortgages payable, the face value of debentures payable, loan payable and bank indebtedness.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

### 5. Properties under development:

Project	Address	December 31 2013	December 31 2012
Heart Lake	Mayfield West Business Park, Caledon, ON	\$ 79,176	\$ 76,650
Airport Road	7900 Airport Road, Brampton, ON	67,302	51,570
		\$ 146,478	\$ 128,220

### 6. Business combination:

On April 4, 2013, pursuant to a statutory plan of arrangement, the REIT acquired 100% of Primaris in exchange for the issuance of 62,535,370 Stapled Units at a fair value of \$23.01 per Stapled Unit, which was the published closing share price on April 3, 2013, for an aggregate total of \$1,438,939. The REIT acquired Primaris to further diversify its existing portfolio to include Canadian enclosed shopping centres. The Primaris portfolio consisted of 26 properties. The transaction costs relating to the acquisition of Primaris were \$6,605; these costs were expensed in the period incurred as transaction costs.

The following are the recognized amounts of identifiable assets acquired and liabilities assumed, measured at their respective fair values on the date of acquisition:

Investment properties	\$ 3,179,418
Cash and cash equivalents	45,108
Net working capital	(94,200)
Debentures payable <sup>(1)</sup>	(94,661)
Mortgages payable	(1,415,575)
Bank indebtedness	(125,000)
Exchangeable units <sup>(2)</sup>	(56,940)
Restricted cash	789
Fair value of consideration	\$ 1,438,939

	Face Value	Fair Value
(1) 2014 <sup>b</sup> Convertible Debentures (HR.DB.F)	\$1,220	\$2,684
2015 Convertible Debentures (HR.DB.G)	7,726	12,516
2018 Convertible Debentures (HR.DB.H)	74,963	79,461
	\$83,909	\$94,661

In May 2013, the REIT redeemed all of the remaining outstanding 2014<sup>b</sup> and 2015 Convertible Debentures.

(2) The REIT assumed 2,122,261 exchangeable units of certain subsidiaries of Primaris for exchangeable units of the REIT, which became exchangeable into 2,474,554 Stapled Units (note 13).

During the year ended December 31, 2013, the REIT recognized \$226,898 of revenue and \$94,138 of comprehensive income, before fair value adjustments related to the acquisition of Primaris (note 27). Had the acquisition occurred on January 1, 2013, the REIT would have recognized an additional \$67,405 of revenue and \$21,239 of comprehensive income, before fair value adjustments for year ended December 31, 2013.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

### 7. Equity accounted investments:

The REIT has entered into a number of arrangements with other parties for the purpose of jointly owning and operating investment properties. In order to determine how these arrangements should be accounted for, the REIT has assessed the structure of the arrangement, and whether the REIT has control over the operations of such properties. The REIT has found that its arrangements fall into two categories: a) joint ventures, where the REIT has joint control over the operations, each investment is structured as a separate vehicle and the REIT has rights to the net assets of the entities; and b) investments in associates, where the REIT has significant influence over the investment but does not have joint control over the operations. Both of these types of arrangements are accounted for using the equity method. During the year ended December 31, 2013, the REIT acquired a net interest in one associate for \$306,177 and one joint venture for \$16,729 (note 4), inclusive of transaction costs. During the year ended December 31, 2012, the REIT acquired a net interest in one joint venture for \$439,062 inclusive of transaction costs. The REIT's interests in equity accounted investments are outlined as follows:

Name	Location	Principal activity	Ownership interest (%)	
			December 31 2013	December 31 2012
Investments in joint ventures:				
100 Yonge	Toronto, Ontario	Own and operate investment property	33.3	-
Scotia Plaza	Toronto, Ontario	Own and operate investment property	33.3	33.3
Telus Tower	Calgary, Alberta	Own and operate investment property	50.0	50.0
Investment in associate:				
ECHO Realty LP ("ECHO")	United States	Own and operate investment properties	33.7	-

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

### 7. Equity accounted investments (continued):

The following tables summarize the total amounts of the financial information of ECHO, 100 Yonge, Scotia Plaza and Telus Tower, and reconciles the summarized financial information to the amount of the REIT's interest in these arrangements:

	Investments in joint ventures	Investment in associate	*December 31 2013	**December 31 2012
<b>Equity accounted investments:</b>				
Investment properties	\$ 1,689,400	\$ 1,264,084	\$ 2,953,484	\$ 1,583,000
Properties under development	-	44,803	44,803	-
Loan receivable	64,300	203,054	267,354	64,300
Other assets	3,280	41,157	44,437	1,351
Cash and cash equivalents	4,147	19,538	23,685	6,746
Mortgages payable	(795,982)	(500,662)	(1,296,644)	(777,548)
Bank indebtedness	(1,158)	(83,428)	(84,586)	-
Accounts payable and accrued liabilities	(48,313)	(40,102)	(88,415)	(46,492)
Non-controlling interest	-	(24,568)	(24,568)	-
Net assets	915,674	923,876	1,839,550	831,357
REIT's share of net assets	341,520	317,121	658,641	308,507
Elimination of intercompany loan receivable	(32,150)	(68,342)	(100,492)	(32,150)
Amount in the combined statements of financial position	\$ 309,370	\$ 248,779	\$ 558,149	\$ 276,357

\* If new information relating to the investment in ECHO is obtained, within one year from the acquisition date, about facts and circumstances that existed at the acquisition date, it may result in adjustments to the above amounts. Therefore, the acquisition accounting may be revised.

\*\* 2012 comparatives only include amounts relating to investments in joint ventures as the investment in an associate was acquired in 2013.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

### 7. Equity accounted investments (continued):

	Investments in joint ventures	Investment in associate	2013	*2012
<b>Net income from equity accounted investments:</b>				
Rentals from investment properties	\$ 161,171	\$ 37,132	\$ 198,303	\$ 95,302
Property operating costs	(72,701)	(7,970)	(80,671)	(42,389)
Net loss from equity accounted investments	-	(593)	(593)	-
Finance income	2,812	2,558	5,370	2,758
Finance cost - operations	(27,874)	(8,652)	(36,526)	(17,825)
Loss on change in fair value	-	-	-	(7,779)
Trust expenses	-	398	398	-
Amortization	(21)	(893)	(914)	-
Fair value adjustment on real estate assets	10,338	(1,997)	8,341	31,427
Income taxes	(1)	(100)	(101)	-
Net income	73,724	19,883	93,607	61,494
REIT's share of net income	30,297	5,919	36,216	27,531
Elimination of intercompany loan interest	(1,354)	(830)	(2,184)	(1,358)
Amount in the combined statements of comprehensive income	\$ 28,943	\$ 5,089	\$ 34,032	\$ 26,173

\* 2012 comparatives only include amounts relating to investments in joint ventures as the investment in an associate was acquired in 2013.

ECHO reports its financial results to the REIT one month in arrears due to time constraints on their reporting. Therefore, the above amounts include ECHO's financial information from acquisition to November 30, 2013.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

### 8. Assets classified as held for sale:

As at December 31, 2013, there were no properties held for sale (December 31, 2012 - two properties; 1330 Martin Grove Ave., Toronto, ON and 295 The West Mall, Etobicoke, ON). The properties held for sale as at December 31, 2012 were sold during the year ended December 31, 2013.

The following table sets forth the combined statements of financial position items associated with investment properties classified as held for sale:

	December 31 2013	December 31 2012
<b>Assets</b>		
Investment properties	\$ -	\$ 27,800
Other assets:		
Accounts receivable	-	106
Prepaid expenses and sundry assets	-	67
	<b>\$ -</b>	<b>\$ 27,973</b>

### 9. Other assets:

	December 31 2013	December 31 2012
Restricted cash*	\$ 10,623	\$ 40,347
Accounts receivable	15,719	16,733
Prepaid expenses and sundry assets	28,282	7,759
Derivative instruments (note 15)	-	1,679
	<b>\$ 54,624</b>	<b>\$ 66,518</b>

\* Included in restricted cash are bank term deposits of \$4,076 (December 31, 2012 - \$4,000) at a rate of interest of 1.07% (December 31, 2012 - 1.00%).

### 10. Cash and cash equivalents:

Cash and cash equivalents as at December 31, 2013 includes cash on hand of \$27,628 (December 31, 2012 - \$81,142) and bank term deposits of \$256 (December 31, 2012 - \$50,318) at a rate of interest of 0.89% (December 31, 2012 - 0.91%).



# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

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### 11. Mortgages payable:

The mortgages payable are secured by real estate assets and letters of credit in certain cases, bearing fixed interest with a contractual weighted average rate of 4.91% (December 31, 2012 - 5.25%) per annum and maturing between 2014 and 2035. Included in mortgages payable at December 31, 2013 are U.S. dollar denominated mortgages of U.S. \$1,203,092 (December 31, 2012 - U.S. \$1,282,436). The Canadian equivalents of these amounts are \$1,275,278 (December 31, 2012 - \$1,269,612).

Debt related to certain Canadian properties is held by separate legal entities, where the rent received from each property is first used to satisfy the related debt obligations with any balance then available to satisfy the cash flow requirements of the REIT.

Future principal mortgage payments are as follows:

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Years ending December 31:	
2014	\$ 327,845
2015	470,126
2016	398,677
2017	614,417
2018	250,766
Thereafter	2,805,955
	<hr/>
	4,867,786
Financing costs and mark-to-market adjustment arising on acquisitions	29,940
	<hr/>
	\$ 4,897,726

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# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

### 12. Debentures payable:

The full terms of the debentures are contained in the public offering documents; the following table summarizes the key terms:

						December 31	December 31
						2013	2012
	Maturity	Contractual interest rate	Effective interest rate	Conversion price	Face value	Carrying value	Carrying value
Convertible Debentures (a)							
2016 Convertible Debentures (HR.DB.E)	December 31, 2016	4.50%	4.50%	\$ 25.70	\$ 75,000	\$ 77,250	\$ 77,250
2018 Convertible Debentures (HR.DB.H)	November 30, 2018	5.40%	5.40%	\$ 24.73	74,414	78,507	-
2020 Convertible Debentures (HR.DB.D)	June 30, 2020	5.90%	5.90%	\$ 23.50	99,654	104,138	109,896
2017 Convertible Debentures (HR.DB.C)	*	6.00%	6.00%	\$ 19.00	-	-	213,304
					249,068	259,895	400,450
Senior Debentures (b)							
Series A Senior Debentures	February 3, 2015	5.20%	5.40%	-	115,000	114,761	114,548
Series H Senior Debentures	October 9, 2015	**	**	-	235,000	234,306	-
Series D Senior Debentures	July 27, 2016	4.78%	4.96%	-	180,000	179,262	178,984
Series I Senior Debentures	January 23, 2017	***	***	-	60,000	59,697	-
Series B Senior Debentures	February 3, 2017	5.90%	6.06%	-	115,000	114,491	114,343
Series E Senior Debentures	February 2, 2018	4.90%	5.22%	-	100,000	98,976	98,757
Series G Senior Debentures	June 20, 2018	3.34%	3.54%	-	175,000	173,570	-
Series C Senior Debentures	December 1, 2018	5.00%	5.30%	-	125,000	123,413	123,138
Series F Senior Debentures	March 2, 2020	4.45%	4.63%	-	175,000	173,759	173,571
					1,280,000	1,272,235	803,341
					\$1,529,068	\$1,532,130	\$1,203,791

The carrying value of the Convertible Debentures (as defined below) is determined using the quoted price on the TSX on December 31, 2013 and December 31, 2012.

\* In July 2013, the REIT redeemed all of the remaining outstanding 2017 Convertible Debentures.

\*\* Bears interest at a rate equal to 3-month Canadian Dealer Offered Rate plus 150 basis points. The interest rate for the period from October 9, 2013 to January 8, 2014 was fixed at 2.775%.

\*\*\* Bears interest at a rate equal to 3-month Canadian Dealer Offered Rate plus 165 basis points. The interest rate for the period from October 23, 2013 to January 22, 2014 was fixed at 2.925%.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

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### 12. Debentures payable (continued):

- (a) *2016 Convertible Debentures, 2018 Convertible Debentures and 2020 Convertible Debentures (collectively, the "Convertible Debentures"):*

In July 2010, the REIT completed a public offering of \$100,000 Series D convertible unsecured subordinated debentures (the "2020 Convertible Debentures"). The 2020 Convertible Debentures may not be redeemed by the REIT on or before June 30, 2014. Thereafter, but prior to June 30, 2016, the 2020 Convertible Debentures may be redeemed, in whole or in part, only if the current market price of a Stapled Unit is at least 125% of the conversion price. On or after June 30, 2016 and prior to the maturity date, the 2020 Convertible Debentures may be redeemed by the REIT, in whole or in part, at a price equal to the principal amount plus accrued interest. Interest on the 2020 Convertible Debentures is payable semi-annually on June 30 and December 31.

In November 2011, the REIT completed a public offering of \$75,000 Series E convertible unsecured subordinated debentures (the "2016 Convertible Debentures"). The 2016 Convertible Debentures may not be redeemed by the REIT on or before November 30, 2014. Thereafter, but prior to November 30, 2015, the 2016 Convertible Debentures may be redeemed, in whole or in part, only if the current market price of a Stapled Unit is at least 125% of the conversion price. On or after November 30, 2015 and prior to the maturity date, the 2016 Convertible Debentures may be redeemed by the REIT, in whole or in part, at a price equal to the principal amount plus accrued interest. Interest on the 2016 Convertible Debentures is payable semi-annually on June 30 and December 31.

On April 4, 2013, the REIT assumed all of Primaris's outstanding convertible debentures (note 6). The 2014<sup>b</sup> and 2015 Convertible Debentures were fully redeemed in 2013. The remaining balance of the Series H convertible unsecured subordinated debentures (the "2018 Convertible Debentures") may not be redeemed by the REIT on or before November 30, 2014. Thereafter, but up to November 30, 2016, the 2018 Convertible Debentures may be redeemed, in whole or in part, only if the current market price of a Stapled Unit is at least 125% of the conversion price. On or after December 1, 2016 and prior to the maturity date, the 2018 Convertible Debentures may be redeemed by the REIT, in whole or in part, at a price equal to the principal amount plus accrued interest. Interest on the 2018 Convertible Debentures is payable semi-annually on May 31 and November 30.

Each Convertible Debenture is convertible into freely tradeable Stapled Units at the holder's option at (i) any time prior to the maturity date and (ii) the business day immediately preceding the date specified by the REIT for redemption of the Convertible Debentures, at a specified conversion price, subject to adjustment upon the occurrence of certain events in accordance with the indenture governing the Convertible Debentures.

On redemption or maturity of the Convertible Debentures, the REIT may, at its option and subject to certain conditions, elect to satisfy its obligation to repay all or any portion of the principal amount of the Convertible Debentures that are to be redeemed or that are to mature through the issuance of Stapled Units by way of issuing (or causing it to be issued) a variable number of Stapled Units equal to the principal amount of the Convertible Debentures that are to be redeemed or that are to mature divided by 95% of the then fair market value of the Stapled Units.

- (b) *Series A Senior Debentures, Series B Senior Debentures, Series C Senior Debentures, Series D Senior Debentures, Series E Senior Debentures, Series F Senior Debentures, Series G Senior Debentures, Series H Senior Debentures and Series I Senior Debentures (collectively, the "Senior Debentures"):*

In February 2010, the REIT issued \$115,000 Series A unsecured senior debentures (the "Series A Senior Debentures"). The interest on the Series A Senior Debentures is payable semi-annually on February 3 and August 3. On issuance, the REIT recorded a liability of \$113,981, net of issue costs of \$1,019.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

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### 12. Debentures payable (continued):

In February 2010, the REIT issued \$115,000 Series B unsecured senior debentures (the "Series B Senior Debentures"). The interest on the Series B Senior Debentures is payable semi-annually on February 3 and August 3. On issuance, the REIT recorded a liability of \$113,953, net of issue costs of \$1,047.

In September 2010, the REIT issued \$125,000 Series C unsecured senior debentures (the "Series C Senior Debentures"). The interest on the Series C Senior Debentures is payable semi-annually on June 1 and December 1. On issuance, the REIT recorded a liability of \$122,525, net of issue costs of \$2,475.

In January 2011, the REIT issued \$180,000 Series D unsecured senior debentures (the "Series D Senior Debentures"). The interest on the Series D Senior Debentures is payable semi-annually on January 27 and July 27. On issuance, the REIT recorded a liability of \$178,475, net of issue costs of \$1,525.

In October 2011, the REIT issued \$100,000 Series E unsecured senior debentures (the "Series E Senior Debentures"). The interest on the Series E Senior Debentures is payable semi-annually on February 2 and August 2. On issuance, the REIT recorded a liability of \$98,510, net of issue costs of \$1,490.

In April 2012, the REIT issued \$175,000 Series F unsecured senior debentures (the "Series F Senior Debentures"). The interest on the Series F Debentures is payable semi-annually on March 2 and September 2. On issuance, the REIT recorded a liability of \$173,389, net of issue costs of \$1,611.

In June 2013, the REIT issued \$175,000 Series G unsecured senior debentures (the "Series G Senior Debentures"). The interest on the Series G Debentures is payable semi-annually on June 20 and December 20. On issuance, the REIT recorded a liability of \$173,420, net of issue costs of \$1,580.

In October 2013, the REIT issued \$235,000 Series H floating rate unsecured senior debentures (the "Series H Senior Debentures"). The interest on the Series H Debentures is payable quarterly on January 9, April 9, July 9 and October 9. On issuance, the REIT recorded a liability of \$234,205, net of issue costs of \$795.

In October 2013, the REIT issued \$60,000 Series I floating rate unsecured senior debentures (the "Series I Senior Debentures"). The interest on the Series I Debentures is payable quarterly on January 23, April 23, July 23 and October 23. On issuance, the REIT recorded a liability of \$59,676, net of issue costs of \$324.

Interest expense is recorded as a charge to net income and is calculated at an effective interest rate with the difference between the coupon rate and the effective rate being credited to the carrying value such that, at maturity, the carrying value is equal to the face value of the then outstanding Senior Debentures.

At its option, the REIT may redeem any of the Senior Debentures, in whole at any time, or in part from time to time, prior to maturity on payment of a redemption price equal to the greater of (i) the Canada Yield Price as defined in the relevant supplemental trust indenture and (ii) par, together in each case with accrued and unpaid interest to the date fixed for redemption. The REIT will give notice of any redemption at least 30 days but not more than 60 days before the date fixed for redemption. Where less than all of any Senior Debentures are to be redeemed pursuant to their terms, the Senior Debentures to be so redeemed will be redeemed on a pro rata basis according to the principal amount of Senior Debentures registered in the respective name of each holder of Senior Debentures or in such other manner as the indenture trustee may consider equitable.

The Senior Debentures are rated BBB (with a Stable trend) by DBRS Limited.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

### 12. Debentures payable (continued):

(c) A summary of the carrying value of debentures payable is as follows:

	December 31 2013	December 31 2012
<b>Convertible Debentures (note 12(a))</b>		
Carrying value, beginning of year	\$ 400,450	\$ 742,240
Fair value of convertible debentures assumed on business combination (note 6)	94,661	-
Conversion - 2013 Convertible Debentures*	-	(87,274)
Conversion - 2014 Convertible Debentures*	-	(216,360)
Conversion - 2017 Convertible Debentures*	(192,066)	(2,020)
Conversion - 2020 Convertible Debentures*	(27)	(352)
Conversion - 2014 <sup>D</sup> Convertible Debentures*	(2,693)	-
Conversion - 2015 Convertible Debentures*	(12,451)	-
Redemption - 2013 Convertible Debentures	-	(29,791)
Redemption - 2014 Convertible Debentures	-	(1,297)
Redemption - 2014 <sup>D</sup> Convertible Debentures	(54)	-
Redemption - 2015 Convertible Debentures	(347)	-
Redemption - 2017 Convertible Debentures	(4,651)	-
Redemption - 2018 Convertible Debentures	(549)	-
Gain on change in fair value (note 21)	(22,378)	(4,696)
Carrying value, end of year	259,895	400,450
<b>Senior Debentures (note 12(b))</b>		
Carrying value, beginning of year	803,341	628,677
Issued - Series F Senior Debentures	-	173,389
Issued - Series G Senior Debentures	173,420	-
Issued - Series H Senior Debentures	234,205	-
Issued - Series I Senior Debentures	59,676	-
Accretion adjustment	1,593	1,275
Carrying value, end of year	1,272,235	803,341
	<b>\$ 1,532,130</b>	<b>\$ 1,203,791</b>

\* The conversion amounts above equal \$207,237 (December 31, 2012 - \$306,006).

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

### 13. Exchangeable units:

The REIT has issued exchangeable units which are puttable instruments where the REIT has a contractual obligation to issue Stapled Units to participating vendors upon redemption. These puttable instruments are classified as a liability under IFRS and are measured at fair value through net income (note 21). Fair value is determined by using the quoted prices for the listed Stapled Units as all of the 17,403,119 (December 31, 2012 - 5,437,565) exchangeable units are exchangeable on a one-for-one basis, at the option of the holder, into Stapled Units. The quoted price as at December 31, 2013 was \$21.40 (December 31, 2012 - \$24.10).

Holders of the exchangeable are entitled to receive distributions on a per unit amount equal to the per unit distribution provided to holders of Stapled Units.

As a result of a reorganization in 2009, H&R Portfolio Limited Partnership ("HRLP"), a subsidiary of the REIT, the REIT, Finance Trust and H&R Portfolio LP Trust (a subsidiary of the REIT) entered into an exchange and support agreement that provides, among other things, for (i) certain capital contributions to be made by the REIT in case HRLP has insufficient (a) funds to pay the required distributions on the Class B LP units of HRLP, or (b) U.S. Holdco Notes to pay the fair quoted value of the Finance Trust units required to be delivered upon exchange of any Class B LP unit; and (ii) the mechanics whereby Class B LP units may be exchanged for Stapled Units.

The following number of exchangeable units are issued and outstanding:

Balance as at January 1, 2012 and December 31, 2012: Class B LP units of HRLP, a subsidiary partnership of the REIT, issued to participating vendors in exchange for properties acquired by HRLP	5,437,565
Assumed on April 4, 2013: 1,750,756 Class B LP units of Place du Royaume Limited Partnership, a subsidiary of Primaris, each of which is exchangeable for 1.166 Stapled Units (note 6)	2,041,380
Assumed on April 4, 2013: 371,505 Class B LP units of Grant Park Limited Partnership, a subsidiary of Primaris, each of which is exchangeable for 1.166 Stapled Units (note 6)*	433,174
Issued on September 3, 2013, effective July 1, 2013: Class B LP units of H&R REIT Management Services Limited Partnership ("HRRMSLP"), a subsidiary of the REIT (note 26)	9,500,000
Class B LP units of Place Du Royaume Limited Partnership exchanged for Stapled Units	(9,000)
<b>As at December 31, 2013</b>	<b>17,403,119</b>

\* A subsidiary of the REIT holds Stapled Units to mirror these exchangeable units. Therefore, when these Class B LP units are exchanged for Stapled Units, the number of outstanding Stapled Units will not increase.

### 14. Unitholders' equity:

The REIT is an unincorporated open-ended trust. The beneficial interests in the REIT are represented by a single class of units which are unlimited in number. Each unit carries a single vote at any meeting of unitholders and carries the right to participate pro rata in any distributions.

Finance Trust is an unincorporated investment trust. The beneficial interests in Finance Trust are represented by a single class of units which are unlimited in number. Each unit carries a single vote at any meeting of unitholders and carries the right to participate pro rata in any distributions.

The units of the REIT are stapled with the units of Finance Trust effective October 1, 2008. These Stapled Units are listed and posted for trading on the TSX. The REIT has entered into a support agreement ("Support Agreement") with Finance Trust to coordinate the issuance of Stapled Units under various arrangements (note 14(d)).

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

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### 14. Unitholders' equity (continued):

The units of the Trusts are freely transferable and, other than as disclosed herein, the trustees shall not impose any restriction on the transfer of units. Provided that an event of uncoupling ("Event of Uncoupling") has not occurred: (a) each unit of the REIT may only be transferred together with a unit of Finance Trust; (b) no unit may be issued by the REIT to any person unless: (i) a unit of Finance Trust is simultaneously issued to such person, or (ii) the REIT has arranged that units will be consolidated (subject to any applicable regulatory approval) immediately after such issuance, such that each holder of a REIT unit will hold an equal number of Finance Trust units and units of the REIT immediately following such consolidation; and (c) a unitholder may require the REIT to redeem any particular number of units only if it also requires, at the same time, and in accordance with the provisions of the Finance Trust Declaration of Trust, Finance Trust to redeem that same number of units of Finance Trust.

An Event of Uncoupling shall occur only: (a) in the event that unitholders of the REIT vote in favour of the uncoupling of units of Finance Trust and units of the REIT such that the two securities will trade separately; or (b) at the sole discretion of the trustees of Finance Trust, but only in the event of the bankruptcy, insolvency, winding-up or reorganization (under an applicable law relating to insolvency) of the REIT or U.S. Holdco or the taking of corporate action by the REIT or U.S. Holdco in furtherance of any such action or the admitting in writing by the REIT or U.S. Holdco of its inability to pay its debts generally as they become due. The trustees of the Trusts shall use all reasonable efforts to obtain and maintain a listing for the units of the REIT and, unless an Event of Uncoupling has occurred, the Stapled Units, on one or more stock exchanges in Canada.

The unitholders have the right to require the Trusts to redeem their units on demand. Provided that no Event of Uncoupling has occurred, unitholders who tender their units of one of the Trusts for redemption will also be required to tender for redemption corresponding units of the other Trust in accordance with the provisions of the respective Declarations of Trust. Upon the tender of their units for redemption, all of the unitholder's rights to and under such units are surrendered and the unitholder is entitled to receive a price per unit as determined by the applicable Declaration of Trust.

Upon valid tender for redemption of each unit of the REIT, the unitholder is entitled to receive a price per unit of the REIT as determined by a formula based on the market price of Stapled Units less an amount based on the principal amount of U.S. Holdco Notes owing per outstanding unit of Finance Trust. The redemption price payable by the REIT will be satisfied by way of a cash payment to the unitholder or, in certain circumstances, including where such payment would cause the REIT's monthly cash redemption obligations to exceed \$50 (subject to adjustment in certain circumstances or waiver by the trustees) an *in specie* distribution of notes of H&R Portfolio LP Trust (a subsidiary of the REIT).

Upon valid tender for redemption of each unit of Finance Trust, the unitholder is entitled to receive, except as provided below, a price per unit payable in cash equal to the Canadian dollar equivalent of the outstanding principal amount of the U.S. Holdco Notes as of the redemption date, divided by the total number of Finance Trust units issued and outstanding immediately prior to the redemption date. In certain circumstances, including where such payment would cause Finance Trust's monthly cash redemption obligations to exceed \$50 (subject to adjustment in certain circumstances or waiver by the trustees) the redemption price per Finance Trust unit being redeemed, to which a redeeming unitholder is entitled shall be the fair market value of the Finance Trust units being redeemed, as determined by the trustees, which shall be payable by way of delivery of U.S. Holdco Notes.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

### 14. Unitholders' equity (continued):

The following number of Stapled Units are issued and outstanding:

As at January 1, 2012	172,553,996
Issued on November 29, 2012 (at a price of \$23.60 per Stapled Unit)	6,360,000
Issued under the Distribution Reinvestment Plan and Unit Purchase Plan (the "DRIP")	2,438,868
2013 Convertible Debentures converted into Stapled Units	3,682,768
2014 Convertible Debentures converted into Stapled Units	9,045,549
2017 Convertible Debentures converted into Stapled Units	83,350
2020 Convertible Debentures converted into Stapled Units	13,232
Options exercised	498,799
<b>As at December 31, 2012</b>	<b>194,676,562</b>
<b>Issued under the DRIP</b>	<b>3,491,649</b>
<b>Issued on April 4, 2013 (at a price of \$23.01 per unit) (note 6)</b>	<b>62,535,370</b>
<b>2017 Convertible Debentures converted into Stapled Units</b>	<b>8,612,404</b>
<b>2020 Convertible Debentures converted into Stapled Units</b>	<b>1,063</b>
<b>2014<sup>P</sup> Convertible Debentures converted into Stapled Units</b>	<b>110,939</b>
<b>2015 Convertible Debentures converted into Stapled Units</b>	<b>515,286</b>
<b>Options exercised</b>	<b>22,500</b>
<b>Exchangeable units exchanged into Stapled Units</b>	<b>9,000</b>
<b>As at December 31, 2013</b>	<b>269,974,773</b>

The weighted average number of basic Stapled Units for the year ended December 31, 2013 is 247,717,472 (December 31, 2012 - 183,409,596).

#### (a) *Unit option plan:*

As at December 31, 2013, a maximum of 28,000,000 (December 31, 2012 - 18,000,000) Stapled Units were authorized to be issued to the REIT's trustees, officers, employees and consultants, of which 11,492,120 options (December 31, 2012 - 9,924,320 options) have been granted. The exercise price of each option approximated the quoted price of the Stapled Units on the date of grant and shall be increased by the amount, if any, by which the fair quoted value of one Finance Trust unit at the time of exercise of such option exceeds the fair quoted value of one Finance Trust unit at the time of grant of such option. The options vest at 33.3% per year from the grant date, will be fully vested after three years, and expire ten years after the date of the grant.

During the year ended December 31, 2013, 1,567,800 options were granted (December 31, 2012 - 1,224,320).

As described in note 2(i), the unit option plan is considered a cash-settled plan with the fair value of the units recorded as a liability on the combined statements of financial position. The liability is released to equity when the unit options are converted to REIT units. The fair value of the unit options is remeasured at each reporting period using the Black-Scholes model. Measurement inputs include unit price on measurement date, exercise price of the instrument, expected volatility (based on weighted average historic volatility adjusted for changes expected due to publicly available information), weighted average expected life of the instruments (based on historical experience and general option holder behaviour), expected distributions, and the risk-free interest rate (based on government bonds). Service and non-market performance conditions attached to the transactions are not taken into account in measuring fair value. The fair value of the vested unit options as at December 31, 2013 is \$6,313 (December 31, 2012 - \$10,585).



# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

### 14. Unitholders' equity (continued):

Unit-based compensation expense of \$(4,136) for the year ended December 31, 2013 (December 31, 2012 - \$6,122) was included in trust expenses in the combined statements of comprehensive income.

A summary of the status of the unit option plan and the changes during the respective periods are as follows:

	2013		2012	
	Units	Weighted average exercise price	Units	Weighted average exercise price
Outstanding, beginning of year	3,008,021	\$ 20.01	2,282,500	\$ 17.12
Granted	1,567,800	22.92	1,224,320	23.18
Exercised	(22,500)	14.79	(498,799)	14.57
Outstanding, end of year	4,553,321	\$ 21.04	3,008,021	\$ 20.01
Options exercisable, end of year	1,802,642	\$ 18.60	875,367	\$ 16.33

The options outstanding at December 31, 2013 are exercisable at varying prices ranging from \$9.30 to \$23.18 (December 31, 2012 - \$9.30 to \$23.18) with a weighted average remaining life of 7.9 years (December 31, 2012 - 8.2 years). The vested options are exercisable at varying prices ranging from \$9.30 to \$23.18 (December 31, 2012 - \$9.30 to \$20.83) with a weighted average remaining life of 6.8 years (December 31, 2012 - 7.1 years).

#### (b) Incentive unit plan:

In order to provide long-term compensation to the REIT's trustees, officers, employees and consultants, there may be grants of incentive units, which are subject to certain restrictions. Under the REIT's incentive unit plan, the maximum number of total Stapled Units available for grant is limited to 5,000,000 Stapled Units. As at December 31, 2013, no Stapled Units have been granted under the incentive unit plan.

Incentive units granted to the REIT's trustees, officers, employees and consultants are recognized based on the grant date fair value. The awards will be satisfied either in Stapled Units issued from treasury or cash, as determined by the REIT Trustees, with the result that the awards are classified as cash-settled unit-based payments and presented as liabilities. The incentive units are subject to vesting conditions and are subject to forfeiture until the recipients of the awards have held office with or provided services to the REIT for a specified period of time. The incentive units may, if specified at the time of grant, accrue cash distributions during the vesting period and accrued distributions will be paid when the incentive units vest. These incentive units will be recognized as liabilities, which are indexed to changes in the fair value of the Stapled Units.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

### 14. Unitholders' equity (continued):

#### (c) Distributions:

Under the REIT's Declaration of Trust, the total amount of income of the REIT to be distributed to unitholders for each calendar month shall be subject to the discretion of the trustees, however, the total income distributed shall not be less than the amount necessary to ensure that the REIT will not be liable to pay income tax under Part I of the Tax Act for any year. The trustees have the discretion to pay the distributions in cash or Stapled Units. For the year ended December 31, 2013, the REIT declared per unit distributions of \$1.26 (December 31, 2012 - \$1.10).

Pursuant to Finance Trust's Declaration of Trust, unitholders of Finance Trust are entitled to receive all of the Distributable Cash of Finance Trust, as defined in the Declaration of Trust. Distributable Cash means, subject to certain exceptions, all amounts received by Finance Trust less certain costs, expenses or other amounts payable by Finance Trust, and less any amounts which, in the opinion of the trustees, may reasonably be considered to be necessary to provide for the payment of any costs or expenditures that have been or will be incurred in the activities and operations of Finance Trust and to provide for payment of any tax liability of Finance Trust. Finance Trust paid per unit distributions of \$0.09 for the year ended December 31, 2013 (December 31, 2012 - \$0.08).

The details of the distributions are as follows:

	2013	2012
Cash distributions to unitholders	\$ 256,780	\$ 158,423
Unit distributions (issued under the DRIP)	74,260	57,056
	<b>\$ 331,040</b>	<b>\$ 215,479</b>

#### (d) Support agreement:

Pursuant to provisions of the Declarations of Trust for Finance Trust and the REIT, at all times, each REIT unit must be stapled to a Finance Trust unit (and each Finance Trust unit must be stapled to a REIT unit) unless there is an Event of Uncoupling. As part of the Plan of Arrangement, the REIT and Finance Trust entered into the Support Agreement which provided, among other things, for the co-ordination of the declaration and payment of all distributions so as to provide for simultaneous record dates and payment dates; for co-ordination so as to permit the REIT to perform its obligations pursuant to the REIT's Declaration of Trust, Unit Option Plan, DRIP and Unitholder Rights Plan; for Finance Trust to take all such actions and do all such things as are necessary or desirable to enable and permit the REIT to perform its obligations arising under any security issued by the REIT (including securities convertible, exercisable or exchangeable into Stapled Units); for Finance Trust to take all such actions and do all such things as are necessary or desirable to enable the REIT to perform its obligations or exercise its rights under its convertible debentures; and for Finance Trust to take all such actions and do all such things as are necessary or desirable to issue Finance Trust units simultaneously (or as close to simultaneously as possible) with the issue of REIT units and to otherwise ensure at all times that each holder of a particular number of REIT units holds an equal number of Finance Trust units, including participating in and cooperating with any public or private distribution of Stapled Units by, among other things, signing prospectuses or other offering documents.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

### 14. Unitholders' equity (continued):

In the event that the REIT issues additional REIT units, pursuant to the Support Agreement, the REIT and Finance Trust will coordinate so as to ensure that each subscriber receives both REIT units and Finance Trust units, which shall trade together as Stapled Units. Prior to such event, the REIT shall provide notice to Finance Trust to cause Finance Trust to issue and deliver the requisite number of Finance Trust units to be received by and issued to, or to the order of, each subscriber as the REIT directs. In consideration of the issuance and delivery of each such Finance Trust unit, the REIT (on behalf of the purchaser) or the purchaser, as the case may be, shall pay (or arrange for the payment of) a purchase price equal to the fair market value (as determined by Finance Trust in consultation with the REIT) of each such Finance Trust unit at the time of such issuance. The remainder of the subscription price for Stapled Units shall be allocated to the issuance of REIT units by the REIT.

#### (e) Short form base shelf prospectus:

On April 3, 2013, the Trusts filed a short form base shelf prospectus, qualifying the Trusts to offer and issue Stapled Units and the REIT to offer and issue the following securities: (i) preferred units; (ii) unsecured debt securities; (iii) subscription receipts exchangeable for Stapled Units and/or other securities of the REIT; (iv) warrants exercisable to acquire Stapled Units and/or other securities of the REIT; and (v) securities comprised of more than one of Stapled Units, preferred units, debt securities, subscription receipts and/or warrants offered together as a unit, or any combination thereof having an offer price of up to \$2,000,000 in aggregate (or the equivalent thereof, at the date of issue, in any other currency or currencies, as the case may be) at any time during the 25-month period that the short form base shelf prospectus (including any amendments) remains valid. As at December 31, 2013, \$175,000 of Senior Debentures have been issued under the short form base shelf prospectus.

### 15. Derivative instruments:

		Fair value (liability) asset *		Net gain (loss) on derivative contracts**	
		December 31	December 31	December 31	December 31
		2013	2012	2013	2012
Foreign exchange forward contracts	(a)	\$ (122)	\$ 1,679	\$ (1,865)	\$ 2,244
Interest rate swap - the Bow Facility	(b)	-	-	-	3,520
Mortgage interest rate swaps	(c)	(386)	(601)	249	(11,253)
		\$ (508)	\$ 1,078	\$ (1,616)	\$ (5,489)

(a) The REIT entered into foreign exchange forward contracts and swaps with Canadian chartered banks effectively locking the REIT's rate to exchange U.S. dollars into Canadian dollars.

(b) The REIT entered into an interest rate swap that was intended to limit its interest rate exposure during the term of the Bow Facility (note 16(d)). The swap was settled in June 2012.

(c) The REIT entered into interest rate swaps on two Canadian mortgages and one U.S. mortgage. The two interest rate swaps on the Canadian mortgages were settled during 2012 in the amount of \$11,348.

\* Derivative instruments in asset and liability positions are not presented on a net basis. When a derivative instrument is in an asset position, the amount is recorded in other assets (note 9).

\*\* Excludes amounts relating to foreign exchange which have been recorded in accumulated other comprehensive income (loss) (note 18).

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

### 16. Bank indebtedness:

The REIT has the following facilities:

- (a) A general operating facility which is secured by fixed charges over certain investment properties due on December 31, 2016. The total facility as at December 31, 2013 is \$300,000 (December 31, 2012 - \$300,000) and can be drawn in either Canadian or U.S. dollars (to a maximum of \$150,000 U.S. dollars for U.S. borrowings). The amount available at December 31, 2013, after taking into account the bank indebtedness drawn of \$101,912 (December 31, 2012 - \$2,905) and the outstanding letters of credit and other items, is \$151,547 (December 31, 2012 - \$252,523). The Canadian dollar bank indebtedness bears interest at rates approximating the prime rate of a Canadian chartered bank. At December 31, 2013, the Canadian prime interest rate was 3.00% (December 31, 2012 - 3.00%) per annum.

Included in bank indebtedness at December 31, 2013 are U.S. dollar denominated amounts of \$78,253 (December 31, 2012 - U.S. \$298). The Canadian equivalents of these amounts are \$82,948 (December 31, 2012 - \$295).

- (b) A general operating facility which is secured by fixed charges over certain investment properties due on April 4, 2015. The total facility as at December 31, 2013 is \$150,000 (December 31, 2012 - not applicable). The amount available at December 31, 2013, after taking into account the bank indebtedness drawn of nil (December 31, 2012 - not applicable) and the outstanding letters of credit is \$149,446 (December 31, 2012 - not applicable).
- (c) A general operating facility which is secured by fixed charges over certain investment properties due on December 20, 2015. The total facility as at December 31, 2013 is \$14,850 (December 31, 2012 - not applicable). The amount available at December 31, 2013, after taking into account the bank indebtedness drawn of \$14,850 (December 31, 2012 - not applicable), is nil (December 31, 2012 - not applicable).
- (d) A \$300,000 general operating facility which was secured by The Bow (the "Bow Facility") due on November 21, 2013 was cancelled in June 2013. As at December 31, 2012, the REIT had drawn nil under the Bow facility.

### 17. Accounts payable and accrued liabilities:

	2013	2012
Current		
Other accounts payable and accrued liabilities	\$ 105,007	\$ 71,697
Accounts payable relating to the Bow	7,140	30,974
Debenture interest payable	16,382	14,139
Prepaid rent	25,465	27,220
Mortgage interest payable	14,012	12,302
Non-current		
Security deposits	4,087	3,759
	<b>\$ 172,093</b>	<b>\$ 160,091</b>

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

### 18. Accumulated other comprehensive income (loss):

	Cash flow hedges	Foreign operations	Total
Balance as at January 1, 2012	\$ (1,582)	\$ (8,290)	\$ (9,872)
Transfer of realized loss on cash flow hedges to net income	400	-	400
Unrealized loss on translation of U.S. denominated foreign operation	-	(15,399)	(15,399)
Balance as at December 31, 2012	(1,182)	(23,689)	(24,871)
<b>Transfer of realized loss on cash flow hedges to net income</b>	<b>414</b>	<b>-</b>	<b>414</b>
<b>Unrealized gain on translation of U.S. denominated foreign operation</b>	<b>-</b>	<b>53,048</b>	<b>53,048</b>
<b>Balance as at December 31, 2013</b>	<b>\$ (768)</b>	<b>\$ 29,359</b>	<b>\$ 28,591</b>

### 19. Rentals from investment properties:

	2013	2012
Rental income	\$ 1,105,982	\$ 768,016
Straight-lining of contractual rent	32,830	32,608
Rent amortization of tenant inducements	(1,795)	(1,465)
	<b>\$ 1,137,017</b>	<b>\$ 799,159</b>

#### *Operating Leases:*

The REIT leases its investment properties under operating leases (note 4). The future minimum lease payments under non-cancellable leases are as follows:

	December 31 2013	December 31 2012
Less than 1 year	\$ 733,743	\$ 559,938
Between 1 and 5 years	2,605,811	2,177,639
More than 5 years	4,839,679	5,111,904
	<b>\$ 8,179,233</b>	<b>\$ 7,849,481</b>

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

### 20. Finance cost - operations:

	2013	2012
Contractual interest on mortgages payable	\$ 230,416	\$ 193,868
Contractual interest on debentures payable	61,701	62,815
Interest on construction loans	144	6,766
Effective interest rate accretion	(4,176)	1,323
Bank interest and charges	8,109	5,480
Exchangeable unit distributions	13,967	6,389
	310,161	276,641
Capitalized interest*	(532)	(44,146)
	<b>\$ 309,629</b>	<b>\$ 232,495</b>

\* Capitalized interest is determined using the weighted average rate of the REIT's borrowings, excluding any borrowings specifically for properties under development, of 5.17% (December 31, 2012 - 5.34%).

### 21. Gain (loss) on change in fair value:

	2013	2012
Gain (loss) on fair value of convertible debentures	\$ 22,378	\$ 4,696
Gain (loss) on fair value of exchangeable units	10,210	(4,350)
Net gain (loss) on derivative instruments (note 15)	(1,616)	(5,489)
	<b>\$ 30,972</b>	<b>\$ (5,143)</b>

### 22. Amortization:

	2013	2012
Amortization of leasing expenses	\$ 7,121	\$ 5,525
Amortization of leasehold improvements	415	-
	<b>\$ 7,536</b>	<b>\$ 5,525</b>

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

### 23. Supplemental cash flow information:

The change in other non-cash operating items are as follows:

	2013	2012
Straight-lining of contractual rent	\$ (41,294)	\$ (31,522)
Prepaid expenses and sundry assets	(9,620)	4,714
Accounts receivable	8,389	(3,718)
Accounts payable and accrued liabilities	(73,764)	25,031
	<b>\$ (116,289)</b>	<b>\$ (5,495)</b>

The following non-cash amounts have been excluded from operating, investing and financing activities in the combined statements of cash flows:

	2013	2012
Non-cash distributions to unitholders (note 14(c))	\$ 74,260	\$ 57,056
Non-cash conversion of convertible debentures (note 12(c))	207,237	306,006
Non-cash issuance of exchangeable units (note 26)	(194,845)	-
Increase in equity accounted investments through issuance of loan payable	(134,713)	-
Decrease in accounts payable on redevelopment	(24,953)	(21,211)
Capitalized interest (note 20)	532	44,146
Non-cash proceeds on options exercised	136	4,177
Mortgages receivable from the sale of investment properties	16,187	-
Non-cash release of mortgage payable on disposition of investment property	(79,569)	(91,167)
Mortgage receivable discharged on acquisition of investment property	(3,960)	-
Release of mortgage obligation upon lenders' consent	-	(20,675)
Release of mortgage interest obligation included in accounts payable and accrued liabilities	-	(679)
Non-cash transfer of investment properties to lenders	-	10,812
Acquisition of investment property through assumption of mortgage payable, net of mark-to-market adjustment	-	7,173
Exchangeable units exchanged for Stapled Units	193	-

### 24. Capital risk management:

The REIT's primary objectives when managing capital are:

- (a) to provide unitholders with stable and growing distributions generated by revenue it derives from investments in real estate assets; and
- (b) to maximize unit value through the ongoing active management of the REIT's assets, the acquisition of additional properties and the development and construction of projects which are pre-leased to creditworthy tenants.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

### 24. Capital risk management (continued):

The REIT considers its capital to be its unitholders' equity, exchangeable units, mortgages payable, debentures payable, loan payable and bank indebtedness. As long as the REIT complies with its investment and debt restrictions set out in its Declaration of Trust, it is free to determine the appropriate level of capital in context with its cash flow requirements, overall business risks and potential business opportunities. As a result of this, the REIT will make adjustments to its capital based on its investment strategies and changes in economic conditions.

The REIT's level of indebtedness is subject to the limitations set out in its Declaration of Trust. The REIT is limited to a total indebtedness to total assets ratio of 65% (for this purpose "indebtedness" excludes, among other things, Convertible Debentures, and U.S. Holdco notes payable to Finance Trust). As at December 31, 2013, this ratio was 47.3% (December 31, 2012 - 46.9%). Management uses this ratio as a key indicator in managing the REIT's capital.

In addition to the above key ratio, the REIT's general operating facilities (note 16(a) and 16(b)) have the following covenants which are required to be calculated based on the REIT's and Finance Trust's combined financial statements:

	<b>Covenant</b>	<b>2013</b>	2012
(a) Maximum indebtedness to gross book value	65%	<b>47.3%</b>	46.9%
(b) Minimum interest coverage ratio	1.65 : 1	<b>2.51 : 1</b>	2.40 : 1
(c) Minimum unitholders' equity	\$2,000,000	<b>\$6,285,509</b>	\$4,507,012

The REIT has various other covenants with respect to its debt. The REIT is in compliance with the covenants as at December 31, 2013 and December 31, 2012.

The REIT's mortgage providers also have minimum limits on debt-to-service coverage ratios ranging from 1.10 to 1.50 as at December 31, 2013 and December 31, 2012. The REIT monitors these ratios and is in compliance with such external requirements.

### 25. Risk management:

#### (a) *Credit risk:*

The REIT is exposed to credit risk as an owner of investment properties in that tenants may experience financial difficulty and be unable to fulfill their lease commitment or the failure of tenants to occupy and pay rent in accordance with existing lease agreements. Management mitigates this risk by carrying out appropriate credit checks and related due diligence on significant tenants. Management has diversified the REIT's holdings so that it owns several categories of properties and acquires investment properties throughout Canada and the United States.

In addition, management ensures that no tenant or related group of tenants, other than investment grade tenants, account for a significant portion of the REIT's cash flow. Bell Canada and Encana Corporation, rated A (low) and BBB (stable), respectively, by a recognized rating agency, are the only tenants which account for more than 5% of the rental from income properties.



# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

### 25. Risk management (continued):

The REIT's exposure to credit risk is as follows:

	December 31 2013	December 31 2012
Mortgages and amount receivable	\$ 9,687	\$ 6,960
Accounts receivable (note 9)	15,719	16,733
Derivative instruments (note 9)	-	1,679
	<b>\$ 25,406</b>	<b>\$ 25,372</b>

#### (b) Liquidity risk:

The Trusts are subject to liquidity risk whereby it may not be able to refinance or pay its debt obligations when they become due.

The Trusts' liquidity risk is as follows:

	2014	Thereafter	Total
Mortgages payable (note 11)*	\$ 327,845	\$ 4,539,941	\$ 4,867,786
Debentures payable (note 12)*	-	1,532,130	1,532,130
Loan payable*	134,713	-	134,713
Derivative instruments (note 15)*	508	-	508
Bank indebtedness (note 16)*	-	116,762	116,762
Accounts payable and accrued liabilities (note 17)	168,006	4,087	172,093
	<b>\$ 631,072</b>	<b>\$ 6,192,920</b>	<b>\$ 6,823,992</b>

\* Amounts in the above table only include the principal amount for each debt obligation.

Management's strategy for managing liquidity risk is to ensure, to the extent possible, that it will always have sufficient liquidity to meet its liabilities when they come due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Trusts' reputation. In order to meet this strategy, the REIT strives to enter into long-term leases with creditworthy tenants which assists in the REIT's primary strategy of maintaining predictable cash flows. The REIT attempts to appropriately structure the term of mortgages to closely match the term of leases for each property. This strategy enables the REIT to meet its contractual monthly mortgage obligations. Due to the long-term length of most of the REIT's mortgages, a significant amount of principal is usually paid by the time the mortgages mature.

The agreements and indentures governing indebtedness of the REIT contain covenants that, among other things, require the REIT to maintain financial ratios and thresholds and impose on the REIT restrictions (subject in each case to exceptions) regarding the creation of liens or granting of negative pledges and the purchase or redemption of securities. As a result, the REIT is limited by such covenants and restrictions.

Management monitors its liquidity risk through review of financial covenants contained in debt agreements and in accordance with the REIT's Declaration of Trust. In order to maintain liquidity, the REIT has two general operating facilities, as described in note 16(a) and 16(b), available to draw on to fund its obligations.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

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### 25. Risk management (continued):

(c) *Market risk:*

The Trusts are subject to currency risk and interest rate risk. The Trusts' objective is to manage and control market risk exposure within acceptable parameters, while optimizing the return on risk.

(i) *Currency risk:*

A portion of the REIT's properties are located in the United States, resulting in the REIT being subject to foreign currency fluctuations which may impact its financial position and results. In order to mitigate the risk, the REIT's debt on these properties is also held in U.S. dollars to act as a natural hedge.

A \$0.10 weakening of the U.S. dollar against the average Canadian dollar exchange rate of \$1.03 for the year ended December 31, 2013 (December 31, 2012 - \$1.00) would have decreased other comprehensive income (loss) by approximately \$80,600 (December 31, 2012 - \$53,100) and decreased net income by approximately \$3,000 (December 31, 2012 - \$6,400). This analysis assumes that all other variables, in particular interest rates, remain constant (a \$0.10 weakening of the Canadian dollar against the U.S. dollar at December 31, 2013 would have had the equal but opposite effect).

(ii) *Interest rate risk:*

The Trusts are exposed to interest rate risk on its borrowings. It minimizes this risk by obtaining long-term fixed interest rate debt. At December 31, 2013, the percentage of fixed rate debt to total debt was 93.8% (December 31, 2012 - 99.9%). Therefore, a change in interest rates at the reporting date would not affect net income with respect to these fixed rate instruments.

The bank indebtedness is subject to variable interest rates. An increase in interest rates of 100 basis points for the year ended December 31, 2013 would have decreased net income by approximately \$1,400 (December 31, 2012 - \$1,800). This analysis assumes that all other variables, in particular foreign exchange rates, remain constant.

The floating rate senior debentures are subject to variable interest rates. An increase in interest rates of 100 basis points for the year ended December 31, 2013 would have decreased net income by approximately \$300 (December 31, 2012 - not applicable). This analysis assumes that all other variables, in particular foreign exchange rates, remain constant.

(d) *Fair values:*

(i) *Financial assets and liabilities carried at amortized cost:*

The fair values of the Trusts' mortgages and amount receivable, accounts receivable, cash and cash equivalents, bank indebtedness and accounts payable and accrued liabilities approximate their carrying amounts due to the relatively short periods to maturity of these financial instruments.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

### 25. Risk management (continued):

The fair value of the mortgages payable has been determined by discounting the cash flows of these financial obligations using year-end market rates for debt of similar terms and credit risks. Based on these assumptions, the fair value of mortgages payable at December 31, 2013 has been estimated at \$4,956,307 (December 31, 2012 - \$3,938,704) compared with the carrying value of \$4,897,726 (December 31, 2012 - \$3,813,613).

The fair value of the Senior Debentures payable has been measured based on the ask price of each series of Senior Debenture similar terms and credit risks. Based on these assumptions, the fair value of the Senior Debentures payable at December 31, 2013 has been estimated at \$1,321,378 (December 31, 2012 - \$860,810) compared with the carrying value of \$1,272,235 (December 31, 2012 - \$803,341).

The fair value of the loan payable to ECHO approximates the carrying value.

(ii) *Assets and Liabilities carried at fair value:*

Financial instruments measured at fair value in the combined statements of financial position are categorized using a fair value hierarchy that reflects the significance of the inputs used in determining the fair values:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

December 31, 2013	Level 1	Level 2	Level 3	Total
<b>Assets</b>				
Investment properties	\$ -	\$ -	\$ 12,786,205	\$ 12,786,205
Properties under development	-	-	146,478	146,478
	-	-	12,932,683	12,932,683
<b>Liabilities</b>				
Convertible debentures (note 12)	(259,895)	-	-	(259,895)
Exchangeable units	(372,427)	-	-	(372,427)
Derivative instruments liabilities	-	(508)	-	(508)
Mortgages payable	-	-	(4,956,307)	(4,956,307)
Senior debentures	-	-	(1,321,378)	(1,321,378)
	(632,322)	(508)	(6,277,685)	(6,910,515)
	\$ (632,322)	\$ (508)	\$ 6,654,998	\$ 6,022,168

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

### 25. Risk management (continued):

December 31, 2012	Level 1	Level 2	Level 3	Total
<b>Assets</b>				
Investment properties	\$ -	\$ -	\$ 9,235,562	\$ 9,235,562
Properties under development	-	-	128,220	128,220
Investment properties held for sale (note 8)	-	-	27,800	27,800
Derivative instrument asset (note 9)	-	1,679	-	1,679
	-	1,679	9,391,582	9,393,261
<b>Liabilities</b>				
Convertible debentures (note 12)	(400,450)	-	-	(400,450)
Exchangeable units	(131,045)	-	-	(131,045)
Derivative instruments liabilities (note 15)	-	(601)	-	(601)
Mortgages payable	-	-	(3,938,704)	(3,938,704)
Senior debentures	-	-	(860,810)	(860,810)
	(531,495)	(601)	(4,799,514)	(5,331,610)
	\$ (531,495)	\$ 1,078	\$ 4,592,068	\$ 4,061,651

### 26. Related party transactions:

H&R Property Management Ltd. ("HRPM"), a company partially owned by family members of the CEO, provided property management services for substantially all properties owned by the REIT, including leasing services, for a fee of 2% of gross revenue. HRPM also provided support services in connection with the acquisition, disposition and development activities of the REIT and was also entitled to an incentive fee. Acquisitions and development support services were provided for a fee of 2/3 of 1% of total acquisition and development costs. The support services relating to dispositions of investment properties were provided for a fee of 10% of the net gain on sale of investment properties adjusted for the add back of accumulated depreciation and amortization. Services were provided by HRPM pursuant to a property management agreement which was internalized effective June 30, 2013.

Effective July 1, 2013, the REIT executed an agreement with HRPM to internalize the property management function in exchange for the issuance of 9,500,000 exchangeable units. Upon closing of the transaction, HRRMSLP acquired HRPM's REIT-related property management business in return for 9,500,000 limited partnership units of HRRMSLP, such units to be exchangeable on a one-for-one basis for Stapled Units. The cost of internalizing the property management function, including the value of the exchangeable units issued of \$194,845, was \$198,214. These costs were expensed as transaction costs in the period incurred.

Effective July 1, 2013, the REIT entered into an agreement with HRPM for HRPM to provide specified services including the cost sharing of premises, certain personnel and equipment and support systems, as well as additional services to be agreed upon from time to time. The agreement will continue until terminated by either party in accordance with the terms of the agreement. During the year ended December 31, 2013, the REIT incurred costs of \$811 under this agreement.

During the year ended December 31, 2013, the REIT recorded expenses pursuant to the property management agreement of \$8,211 (December 31, 2012 - \$19,912), of which \$550 (December 31, 2012 - \$4,777) was capitalized to the cost of the investment properties acquired, nil (December 31, 2012 - \$1,128) was capitalized to properties under development and \$2,030 (December 31, 2012 - \$5,478) was capitalized to leasing expenses. These amounts include amounts relating to equity accounted investments. The REIT has also reimbursed HRPM for certain direct property operating costs and tenant construction costs.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

### 26. Related party transactions (continued):

For the year ended December 31, 2013, a further amount of \$2,250 (December 31, 2012 - \$4,500) has been earned by HRPM pursuant to the property management agreement, in accordance with the annual incentive fee payable to HRPM. Of this amount, \$1,125 (December 31, 2012 - nil) has been waived by HRPM and \$1,125 (December 31, 2012 - \$4,500) has been expensed in the combined statements of comprehensive income.

As at December 31, 2013, nil (December 31, 2012 - \$1,837) was payable to HRPM.

The REIT leases space to companies partially owned by family members of the CEO. The rental income earned for the year ended December 31, 2013 is \$1,358 (December 31, 2012 - \$1,432).

These transactions are measured at the amount of consideration established and agreed to by the related parties.

Key management personnel compensation:

	2013	2012
Short-term employee salaries and benefits	\$ 4,334	\$ 3,224
Employee unit-based compensation	(3,725)	5,522
	<b>\$ 609</b>	<b>\$ 8,746</b>

### 27. Segmented disclosures:

#### (i) Operating segments:

The Trusts have two operating segments: the H&R portfolio, comprised of 468 properties including equity accounted investments (December 31, 2012 - 295) and the Primaris portfolio, comprised of 26 properties (December 31, 2012 - not applicable).

December 31, 2013	H&R	Primaris	Elimination*	Total
<b>Real estate assets:</b>				
Investment properties	\$ 10,639,611	\$ 3,189,900	\$ -	\$ 13,829,511
Properties under development	161,557	-	-	161,557
	10,801,168	3,189,900	-	13,991,068
<b>Less: Trusts' proportionate share of investment properties and properties under development relating to equity accounted investments</b>	<b>(1,058,385)</b>	<b>-</b>	<b>-</b>	<b>(1,058,385)</b>
	<b>\$ 9,742,783</b>	<b>\$ 3,189,900</b>	<b>\$ -</b>	<b>\$ 12,932,683</b>
<b>Total assets</b>	<b>\$ 11,048,400</b>	<b>\$ 3,209,492</b>	<b>\$ (674,865)</b>	<b>\$ 13,583,027</b>
<b>Total liabilities</b>	<b>\$ 6,253,602</b>	<b>\$ 1,730,489</b>	<b>\$ (674,865)</b>	<b>\$ 7,309,226</b>

\* Elimination of intercompany loans between Primaris and the REIT.

No comparative segmented disclosure has been provided as at December 31, 2012 as Primaris was acquired on April 4, 2013 (note 6).

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

### 27. Segmented disclosures (continued):

Property operating income by reportable segment for the year ended December 31, 2013 is as follows:

	H&R	Primaris	2013
<b>Property operating income:</b>			
Rentals from investment properties	\$ 910,119	\$ 226,898	\$ 1,137,017
Property operating costs	(293,469)	(93,626)	(387,095)
	<b>\$ 616,650</b>	<b>\$ 133,272</b>	<b>\$ 749,922</b>

No comparative segmented disclosure has been provided for the year ended December 31, 2012 as Primaris was acquired on April 4, 2013 (note 6).

### (ii) Geographic segments:

The Trusts operate in Canada and the United States.

Investment properties and properties under development are attributed to countries based on the location of the properties.

	2013	2012
Canada	\$ 11,147,166	\$ 7,774,143
United States	2,843,902	2,188,939
	<b>13,991,068</b>	<b>9,963,082</b>
Less: Trusts' proportionate share of investment properties and properties under development relating to equity accounted investments	(1,058,385)	(571,500)
Less: investment properties relating to assets held for sale	-	(27,800)
	<b>\$ 12,932,683</b>	<b>\$ 9,363,782</b>

	2013	2012
<b>Rentals from investment properties:</b>		
Canada	\$ 983,860	\$ 631,824
United States	224,280	203,479
	<b>1,208,140</b>	<b>835,303</b>
Less: Trusts' proportionate share of rentals relating to equity accounted investments	(71,123)	(36,144)
	<b>\$ 1,137,017</b>	<b>\$ 799,159</b>

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

Years ended December 31, 2013 and 2012

### 28. Income tax expense:

	2013	2012
Income tax computed at the Canadian statutory rate of nil applicable to the REIT for 2013 and 2012	\$ -	\$ -
Current U.S. income taxes	471	518
Deferred income taxes applicable to U.S. Holdco	29,227	43,407
	<b>\$ 29,698</b>	<b>\$ 43,925</b>

The Tax Act contains legislation (the "SIFT Rules") affecting the tax treatment of "specified investment flow-through" ("SIFT") trusts. A SIFT includes a publicly traded trust. Under the SIFT Rules, distributions of certain income by a SIFT are not deductible in computing the SIFT's taxable income, and a SIFT is subject to tax on such income at a rate that is substantially equivalent to the general tax rate applicable to a Canadian corporation. The SIFT Rules do not apply to a publicly traded trust that qualifies as a real estate investment trust under the Tax Act. The REIT completed the necessary tax restructuring to qualify as a real estate investment trust effective June 30, 2010.

The REIT has certain subsidiaries in the United States that are subject to tax on their taxable income at a rate of approximately 38%. The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities are presented below:

	2013	2012
<b>Deferred tax assets:</b>		
Net operating losses and deferred interest deductions	\$ 84,434	\$ 72,090
Accounts payable and accrued liabilities	1,865	1,129
Other assets	158	148
	<b>86,457</b>	<b>73,367</b>
<b>Deferred tax liabilities:</b>		
Investment properties	162,055	116,360
Equity accounted investments	1,151	-
Derivative instruments	(195)	414
	<b>163,011</b>	<b>116,774</b>
Deferred tax liability	<b>\$ (76,554)</b>	<b>\$ (43,407)</b>

As at December 31, 2013, U.S. Holdco had accumulated net operating losses and deferred interest deductions available for carryforward for U.S. income tax purposes of \$219,708 (December 31, 2012 - \$187,733). The net operating losses will expire between 2018 and 2033. The deferred interest deductions and the deductible temporary differences do not generally expire under current tax legislation.

# H&R REAL ESTATE INVESTMENT TRUST

## H&R FINANCE TRUST

Notes to Combined Financial Statements

(In thousands of Canadian dollars, except unit and per unit amounts)

**Years ended December 31, 2013 and 2012**

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### **29. Commitments and contingencies:**

- (a) In the normal course of operations, the REIT has issued letters of credit in connection with developments, financings, operations and acquisitions. As at December 31, 2013, the REIT has outstanding letters of credit totalling \$47,070 (December 31, 2012 - \$50,198), including \$17,438 (December 31, 2012 - \$17,343) which has been pledged as security for certain mortgages payable. Of these letters of credit, \$41,419 (December 31, 2012 - \$44,547) are secured in the same manner as the bank indebtedness (notes 16(a) and 16(b)), and \$5,651 (December 31, 2012 - \$5,651) by a specific investment property.
- (b) The REIT provides guarantees on behalf of third parties, including co-owners. As at December 31, 2013, the REIT issued guarantees amounting to \$69,766 (December 31, 2012 - \$72,091), which expire in 2016 (December 31, 2012 - expire in 2016), relating to the co-owner's share of mortgage liability. In addition, the REIT continues to guarantee certain debt assumed by purchasers in connection with past dispositions of properties, and will remain liable until such debts are extinguished or the lenders agree to release the REIT's covenants. At December 31, 2013, the estimated amount of debt subject to such guarantees, and therefore the maximum exposure to credit risk, is \$224,377 (December 31, 2012 - \$110,292) which expires between 2014 and 2022 (December 31, 2012 - expires between 2013 and 2018). There have been no defaults by the primary obligor for debts on which the REIT has provided its guarantees, and as a result, no contingent loss on these guarantees has been recognized in these combined financial statements.

Credit risks arise in the event that these parties default on repayment of their debt since they are guaranteed by the REIT. These credit risks are mitigated as the REIT has recourse under these guarantees in the event of a default by the borrowers, in which case the REIT's claim would be against the underlying real estate investments.

- (c) The REIT is involved in litigation and claims in relation to the investment properties that arise from time to time in the normal course of business. In the opinion of management, any liability that may arise from such contingencies would not have a significant adverse effect on the combined financial statements.

### **30. Comparative figures:**

Certain comparative figures have been reclassified to conform with the combined financial statement presentation adopted in the current year.



## **Unitholder Distribution Reinvestment Plan and Unit Purchase Plan**

Since January 1, 2000, H&R has offered registered holders of stapled units resident in Canada the opportunity to participate in its Unitholder Distribution Reinvestment Plan (the "DRIP") and Unit Purchase Plan.

The DRIP allows participants to have their monthly cash distributions reinvested in additional stapled units at the weighted average price of the stapled units on the TSX for the five trading days (the "Average Market Price") immediately preceding the cash distribution date. In addition, participants will be entitled to receive an additional distribution equal to 3% of each cash distribution reinvested pursuant to the DRIP which will be reinvested in additional stapled units.

The Unit Purchase Plan allows participants to purchase additional stapled units on a monthly basis at the Average Market Price subject to a minimum purchase of \$250 per month (up to a maximum of \$13,500 per year) for each participant.

For more information on the DRIP and/or the Unit Purchase Plan, please contact us by email through the "Contact Us" webpage of our website or contact the plan agent: CST Trust Company, P.O. Box 7010, Adelaide Street Postal Station, Toronto, Ontario M5C 2W9, Tel: 416-643-5500 (or for callers outside of the 416 area code: 1-800-387-0825), Fax: 416-643-5501, Email: [inquiries@cibcmellon.com](mailto:inquiries@cibcmellon.com).

## Corporate Information

### H&R REIT Board of Trustees

Thomas J. Hofstedter <sup>(1)</sup>, President and Chief Executive Officer, H&R Real Estate Investment Trust  
Robert Dickson <sup>(1,2,3,4)</sup>, Strategic financial consultant, marketing communications industry  
Edward Gilbert <sup>(1,2,3,4)</sup>, Chief Operating Officer, Firm Capital Mortgage Investment Trust  
Laurence A. Lebovic <sup>(1,2,3,4)</sup>, Chief Executive Officer, Runnymede Development Corporation Ltd.  
Ronald C. Rutman <sup>(1,2,3,4)</sup>, Partner, Zeifman & Company, Chartered Accountants

### H&R Finance Trust Board of Trustees

Thomas J. Hofstedter, President and Chief Executive Officer, H&R Real Estate Investment Trust  
Shimshon (Stephen) Gross <sup>(2)</sup>, President, LRG Holdings Inc.  
Marvin Rubner <sup>(2)</sup>, Manager and Founder, YAD Investments Limited.  
Neil Sigler <sup>(2)</sup>, Vice President, Gold Seal Management Inc.

- (1) Investment Committee
- (2) Audit Committee
- (3) Compensation and Governance Committee
- (4) Nominating Committee

### Officers

Thomas J. Hofstedter, President and Chief Executive Officer  
Larry Froom, Chief Financial Officer  
Nathan Uhr, Chief Operating Officer (H&R REIT)  
Pat Sullivan, Chief Operating Officer (Primaris)  
Cheryl Fried, Executive Vice-President, Finance (H&R REIT)  
Lesley Gibson, Executive Vice-President, Finance (Primaris)  
Blair Kundell, Vice-President, Operations (H&R REIT)  
Jason Birken, Vice-President, Finance (H&R REIT)

**Auditors:** KPMG LLP

**Legal Counsel:** Blake, Cassels & Graydon LLP

**Taxability of Distributions:** 53% of the distributions made by H&R REIT and 5% of the distributions made by H&R Finance Trust to unitholders during 2013 were tax deferred.

**Plan Eligibility:** RRSP, RRIF, DPSP, RESP, RDSP, TFSA

**Stock Exchange Listing:** Stapled Units and debentures of H&R are listed on the Toronto Stock Exchange under the trading symbols HR.UN; HR.DB.D, HR.DB.E and HR.DB.H.

**Unitholder Distribution Reinvestment Plan and Direct Unit Purchase Plan:** Since January 2000, H&R REIT has offered registered holders of its units resident in Canada the opportunity to participate in its Unitholder Distribution Reinvestment Plan (the "DRIP") and Direct Unit Purchase Plan. The DRIP allows participants to have their monthly cash distributions of H&R REIT reinvested in additional Stapled Units of H&R at a 3% discount to the weighted average price of the Stapled Units on the TSX for the five trading days (the "Average Market Price") immediately preceding the cash distribution date. The Direct Unit Purchase Plan allows participants to purchase additional Stapled Units on a monthly basis at the Average Market Price subject to a minimum purchase of \$250 per month (up to a maximum of \$13,500 per year) for each participant. For more information on the DRIP and/or the Direct Unit Purchase Plan, please contact us by email through the "Contact Us" webpage of our website, or contact our Registrar and Transfer Agent.

**Registrar and Transfer Agent:** CST Trust Company, P.O. Box 7010, Adelaide Street Postal Station, Toronto, Ontario, Canada M5C 2W9 Telephone: 416-643-5500 within the Toronto area or 1-800-387-0825, Fax: 416-643-5501, E-mail: [inquiries@canstockta.com](mailto:inquiries@canstockta.com), Website: [www.canstockta.com](http://www.canstockta.com).

**Contact Information:** Investors, investment analysts and others seeking financial information should go to our website at [www.hr-reit.com](http://www.hr-reit.com), or e-mail [info@hr-reit.com](mailto:info@hr-reit.com), or call 416-635-7520 and ask for Larry Froom, Chief Financial Officer, or fax 416-398-0040, or write to H&R Real Estate Investment Trust, 3625 Dufferin Street, Suite 500, Toronto, Ontario, Canada, M3K 1N4



**H&R Real Estate Investment Trust and H&R Finance Trust**



**The Bow, Calgary**



**Scotia Plaza, Toronto**



**Corus Quay, Toronto**