



**H&R Real Estate Investment Trust and H&R Finance Trust
2014 Annual Report
Including Combined MD&A and Financial Statements**



The Bow, Calgary



Scotia Plaza, Toronto



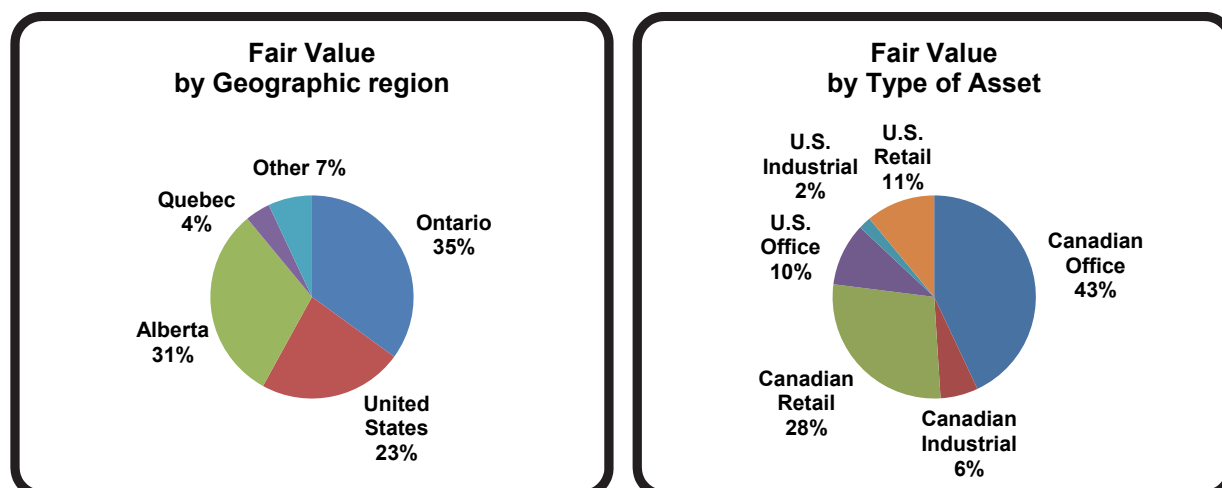
Corus Quay, Toronto

H&R Profile

H&R REIT is Canada's largest diversified real estate investment trust with a total assets of approximately \$13.4 billion as at December 31, 2014. H&R REIT is a fully internalized REIT and has ownership interests in a North American portfolio of high quality office, retail and industrial properties comprising over 49 million square feet.

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. The current note receivable balance is U.S. \$220.5 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 and on 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

2014 has proven to be another successful and transformational year for H&R REIT. Highlights include:

- **Launch of a New Industrial Platform**

Through the sale of an ownership interest in over \$1.4 Billion of our industrial properties we have created a strategic alliance with PSP and Crestpoint, forming a new platform to become a dominant force in the sector. In doing so, we have further leveraged our management and acquisition expertise to earn fees that will achieve enhanced returns to our unitholders.

- **Launch of a New Residential Platform**

Working creatively and opportunistically, we acquired land with our partner, Tishman Speyer, for the development of approximately 1,800 residential units in Long Island City, New York. The site sits adjacent to our, 670,000 square foot, state of the art office tower, Two Gotham Center, located minutes from midtown Manhattan. Construction has recently commenced with first occupancy scheduled for late 2017.

We have further entered the United States residential market with the acquisition of 696 rental apartment units with a focus on assets in the Sunbelt States.

- **Leveraging Primaris Platform to Earn Fees and Grow**

We have solidified and expanded our relationship with Montez Corporation through the sale of a 50% non-managing interest in four of our enclosed shopping centres and the joint acquisition of Kildonan Place, the third largest enclosed shopping centre in Winnipeg.

Enhancing the Value of our Existing Portfolio, in 2014, we:

1. Completed the 744,413 square foot state-of-the-art, built-to-suit distribution centre in Mississauga, ON, leased long term to Unilever Canada Inc.;
2. Sold a 50% non-managing interest in Telus Tower in Burnaby, BC for \$86.5 Million to a partnership comprised of Crestpoint and a major Canadian pension fund, further leveraging our expertise to earn fees;
3. Commenced a \$35 Million refurbishment of our iconic Place Bell office tower in downtown Ottawa;
4. Renovated and expanded Cataragui Centre in Kingston, ON through the investment of \$12.8 Million which included a new 10 year lease with Canadian Tire's Sport Chek division for 30,000 square feet and a 15,000 square foot new 20 year lease with Shoppers Drug Mart;
5. Welcomed a new 19,000 square foot H&M to Place D'Orleans in Orleans, ON, a 15,000 square foot Old Navy to Orchard Park in Kelowna, BC, a 20,000 square foot Forever 21 to Dufferin Mall in Toronto, ON, a 34,000 square foot Sport Chek to St. Albert Centre in St. Albert, AB, a 22,195 square foot H&M to Place Du Royaume in Chicoutimi, QC, and a 15,000 square foot Manitoba Liquor Commission to Grant Park in Winnipeg, MB;
6. Expanded our Florida Publix portfolio by the addition of Brooks Village, a 65,941 square foot Publix anchored shopping center in Naples, FL, and
7. The REIT also realised approximately \$144 Million from the sale of non-core assets in Canada and the United States.



In Q1 2015, we have also made some significant strides.

1. We have successfully completed the lease-up of 310 and 320 Front Street West in downtown Toronto with a lease to TD Bank for 231,170 square feet and 53,500 square feet to Penguin Random House Canada;
2. At 160 Elgin in downtown Ottawa, we have successfully renewed our lease with Gowlings for 130,274 square feet for a further 15 years;
3. We have entered into a direct lease with TransCanada Pipelines for over 153,000 square feet at Telus House, Calgary; and
4. We have entered into agreements for the purchase of an additional 1,484 residential rental units in the US bringing our total units under contract or ownership to 2,180 units.

- **Balance Sheet Strength**

We continue to deleverage our balance sheet with a lower debt ratio (46.3% versus 49.2% in 2013) while increasing our unencumbered pool of assets. Currently \$1.7 Billion of our properties are debt free with many more properties having a very low debt to value ratio.

Since inception we have delivered to our unitholders, a compound average annual return of 14% and for the 18th consecutive year, our portfolio occupancy rate remained above 97%, a testament to the high quality of our properties and management team.

Outlook

We are confident our strategy of safety and stability through size and diversity will shield and protect us against a challenging economic outlook for Canada. The United States, where H&R has a sizeable investment of approximately 23% of our assets, will show steady growth as the US economy continues its recovery.

Our low risk profile is highly predictable over the next five years with only 36.9% of our leases rolling and only 45.7% of our mortgages coming due. We have ample liquidity to retire high-cost debt as it matures and to fund further acquisition opportunities as they arise.

I would like to thank our investors for their trust, 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 in 2015.***

A handwritten signature in black ink, appearing to read 'Tom Hofstedter'. The signature is fluid and cursive, with a long horizontal stroke extending to the right.

Tom Hofstedter
President and Chief Executive Officer
April 1, 2015

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

For the Year ended December 31, 2014

Dated: February 17, 2015

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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, 2014 includes material information up to February 17, 2015. 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, 2014 and 2013 ("Trusts' 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 Trusts' 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, 2014.

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 "Results 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 17, 2015 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' 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 Trusts' Interests

Effective January 1, 2013, the Trusts adopted IFRS 11, *Joint Arrangements* which resulted in the Trusts no longer proportionately consolidating certain joint ventures and investments in associates. The Trusts now apply the equity method of accounting to joint ventures and investments in associates. Throughout this MD&A, any references to the "Trusts' Financial Statements" refer to amounts as reported under IFRS and any references to "The Trusts' interests" are non-GAAP measures which include amounts per the Trusts' Financial Statements plus the Trusts' proportionate share of equity accounted investments.

Property Operating Income, Same-Asset Property Operating Income and Adjusted 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. 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 which management believes is a measure useful for investors as it reports period-over-period performance for properties owned by the REIT throughout both years. This typically excludes acquisitions, business combinations, dispositions, equity accounted investments and transfers of properties under development to investment properties. Adjusted property operating income is a non-GAAP measure. Effective January 1, 2014, the REIT adopted IFRS Interpretations Committee 21, *Levies* ("IFRIC 21") which has been applied retrospectively. Adjusted property operating income excludes the impact of this change in accounting policy which relates to the timing of the liability recognition for U.S. realty taxes. Management believes that adjusted property operating income is an important non-GAAP measure as, by excluding the impact of IFRIC 21, it evenly matches U.S. realty taxes with realty tax recoveries throughout the year.

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 combined 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 property operating income to FFO and see Adjusted Funds from Operations for a reconciliation of FFO to AFFO and AFFO to Cash Provided by Operations.

Adjusted Funds from Operations ("AFFO")

AFFO is also a widely used measure in the real estate industry to assess the sustainability of cash distributions. 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 of combined AFFO may differ from other issuers' calculations. AFFO should not be construed as an alternative to net income or cash provided by operations calculated in accordance with IFRS. See "Adjusted Funds from Operations" for a reconciliation of AFFO to cash provided by operations.

Adjusted Cash provided by Operations

Under IFRS, the Trusts have elected to present interest paid with cash provided by financing activities. As a comparison to total distributions, the Trusts are of the view that cash provided by operating activities should be shown net of interest paid. Adjusted cash provided by operations is a non-GAAP measure which deducts interest paid from cash provided by operations. Management believes this to be a useful measure as it provides investors with an indication of how much cash is available for distributions.

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 may not be comparable.

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 a diversified portfolio of 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 on average 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, 2014, Finance Trust holds U.S. \$220.5 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 Trusts' Financial Statements, however the related foreign exchange difference is not eliminated upon combination as it flows through net income (loss) 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, Incentive Unit 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.

CHANGE IN ACCOUNTING POLICIES

Except as described below, the accounting policies applied by the Trusts as at and for the year ended December 31, 2014, are the same as those applied in the Trusts’ combined financial statements as at and for the year ended December 31, 2013. Effective

January 1, 2014, the REIT has adopted IFRIC 21 and this change in accounting policy has been applied retrospectively. In Q4 2014, the REIT made a voluntary change in accounting policy to no longer amortize leasing costs. Refer to notes 2 and 3 of the Trusts' Financial Statements for a detailed description and quantitative impact of these changes in accounting policies.

SECTION II

FINANCIAL HIGHLIGHTS

(in thousands except per unit amounts)	December 31, 2014	December 31, 2013
Total assets	\$13,368,380	\$13,583,027
Ratio of debt to total assets per the Trusts' Financial Statements ⁽¹⁾	46.3%	49.2%
Ratio of debt to total assets based on the Trusts' Interests ⁽¹⁾	48.1%	50.8%
Stapled Units outstanding	274,773	269,975
Exchangeable units outstanding	16,664	17,403
	Three months ended December 31, 2014	Three months ended December 31, 2013
Property rental revenue	\$308,597	\$314,574
Adjusted property operating income ⁽¹⁾⁽²⁾	201,313	204,600
Net income from equity accounted investments	12,222	19,163
FFO ⁽¹⁾	138,459	134,110
Weighted average number of basic Stapled Units for FFO	290,378	286,281
FFO per basic Stapled Unit ⁽¹⁾	0.48	0.47
Distributions paid per Stapled Unit	0.34	0.34
Payout ratio per Stapled Unit as a % of FFO ⁽¹⁾	70.8%	72.3%

Property operating 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 30-34.

(1) These are non-GAAP measures.

(2) Adjusted property operating income excludes the realty tax adjustment accounted for under IFRIC 21 from property operating income.

KEY PERFORMANCE DRIVERS

OPERATIONS		H&R Portfolio			Primaris Portfolio	Total*
		Office	Retail	Industrial		
<i>Occupancy as at December 31⁽¹⁾</i>	2014	96.5%	98.6%	98.5%	97.4%	97.8%
	2013	98.4%	98.9%	97.6%	97.6%	98.1%
<i>Occupancy – same asset as at December 31⁽¹⁾⁽²⁾</i>	2014	96.5%	99.0%	98.7%	N/A	98.0%
	2013	98.6%	99.1%	98.0%	N/A	98.5%
<i>Average contractual rent per square foot for the year ended December 31⁽¹⁾⁽³⁾</i>	2014	\$27.00	\$14.81	\$5.13	\$21.03	\$15.93
	2013	\$26.14	\$14.04	\$5.43	\$20.97	\$14.66

	December 31, 2014			December 31, 2013		
	H&R Portfolio	Primaris Portfolio	Total*	H&R Portfolio	Primaris Portfolio	Total*
Average remaining term to maturity of leases (in years) ⁽¹⁾	11.2	4.7	9.8	11.7	4.7	10.3
Average remaining term to maturity of mortgages payable (in years) ⁽¹⁾	6.7	4.9	6.4	7.2	6.0	7.0

* Weighted average total.

(1) Includes equity accounted investments and investment properties classified as assets held for sale.

(2) Same asset refers to those properties owned by the REIT for the two-year period ended December 31, 2014.

(3) All amounts are stated in Canadian dollars.

PORTFOLIO OVERVIEW

The geographic diversification of the Trusts' portfolio of properties and their related square footage, including those properties held in entities that the Trusts account for as equity accounted investments, as well as assets held for sale as at December 31, 2014, are outlined in the charts below:

NUMBER OF PROPERTIES	Canada				United States ⁽¹⁾⁽²⁾	Total
	Ontario	Alberta	Quebec	Other		
H&R Portfolio:						
Office	24	5	1	3	11	44
Retail	36	5	5	3	265	314
Industrial	43	17	12	19	23	114
Residential	-	-	-	-	2	2
	103	27	18	25	301	474
Primaris Portfolio:						
Office	-	1	-	-	-	1
Retail	5	14	1	6	-	26
	5	15	1	6	-	27
Total	108	42	19	31	301	501

Square Feet (in thousands) ⁽¹⁾	Canada				United States ⁽²⁾	Total
	Ontario	Alberta	Quebec	Other		
H&R Portfolio:						
Office	7,087	3,430	452	468	2,089	13,526
Retail	2,061	516	498	524	7,317	10,916
Industrial	5,945	1,762	1,489	634	6,841	16,671
Residential	-	-	-	-	543	543
	15,093	5,708	2,439	1,626	16,790	41,656
Primaris Portfolio:						
Office	-	52	-	-	-	52
Retail	2,215	3,613	604	1,809	-	8,241
	2,215	3,665	604	1,809	-	8,293
Total	17,308	9,373	3,043	3,435	16,790	49,949

(1) Square feet (in thousands) is based on the Trusts' interest in the net leasable area of properties.

(2) The REIT owns a 33.6% interest in Echo Realty LP ("ECHO"). The assets of ECHO include four office properties representing 65,601 square feet, 176 retail properties representing 2,130,803 square feet and six industrial properties representing 476,250 square feet for a total of 186 properties and 2,672,654 square feet, all of which are located in the United States and included in the table above. ECHO also has six development projects and six vacant land areas which are not included in the table above.

TOP TWENTY SOURCES OF REVENUE BY TENANT⁽¹⁾

Tenant	% of rentals from investment properties ⁽²⁾	Number of locations	REIT owned sq.ft. (in 000's)	Average lease term to maturity (in years) ⁽³⁾
1. Encana Corporation	11.4	2	2,086	23.0
2. Bell Canada	7.8	25	2,560	10.6
3. Hess Corporation	4.3	1	845	-(7)
4. TransCanada Pipelines Limited	3.7	1	936	6.3
5. New York City Department of Health	2.8	1	670	15.9
6. Giant Eagle, Inc.	2.7	176	1,993	14.1
7. Canadian Tire Corporation ⁽⁴⁾	2.4	20	2,587	10.2
8. Telus Communications	2.2	18	632	5.8
9. Bank of Nova Scotia	2.2	7	474	10.0
10. Rona Inc.	1.8	15	1,914	5.1
11. Nestle Canada and USA	1.8	4	2,338	3.7
12. Royal Bank of Canada	1.6	3	497	4.5
13. Corus Entertainment Inc.	1.6	1	472	18.2
14. Canadian Imperial Bank of Commerce	1.6	10	555	9.1
15. Loblaw Companies Limited ⁽⁵⁾	1.3	22	1,004	8.9
16. Ontario Realty Corporation and other Ontario Agencies ⁽⁶⁾	1.2	3	377	4.2
17. Shell Oil Products	1.0	19	253	7.5
18. Public Works and Government Services, Canada	0.9	4	313	2.5
19. Sobey's Inc.	0.8	15	545	5.8
20. Hudson's Bay/Home Outfitters	0.8	9	1,112	3.9
Total	53.9	356	22,163	

(1) Includes the Trusts' interests in equity accounted investments and investment properties classified as held for sale.

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

(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) Loblaw Companies Limited includes Loblaws, No Frills and Shoppers Drug Mart.

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

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

LEASE TO MATURITY PROFILE⁽¹⁾⁽²⁾

LEASE EXPIRIES	H&R Portfolio						Primaris Portfolio		Total	
	Office		Retail		Industrial		Sq.ft.	Rent per sq.ft. (\$) on expiry	Sq.ft.	Rent per sq.ft. (\$) on expiry
	Sq.ft.	Rent per sq.ft. (\$) on expiry	Sq.ft.	Rent per sq.ft. (\$) on expiry	Sq.ft.	Rent per sq.ft. (\$) on expiry				
2015	317,409	27.31	219,836	23.57	568,133	4.30	745,156	29.93	1,850,534	20.86
2016	800,345	21.40	253,925	18.30	1,555,348	4.00	986,375	24.93	3,595,993	14.62
2017	361,173	20.39	768,417	11.80	130,045	6.50	1,148,272	18.41	2,407,907	15.95
2018	460,549	21.41	694,290	14.22	3,071,697	4.31	998,771	22.22	5,225,307	10.56
2019	532,227	28.10	1,699,639	11.74	1,711,181	5.26	1,157,846	16.10	5,100,893	12.26
	2,471,703	23.46	3,636,107	13.40	7,036,404	4.51	5,036,420	21.62	18,180,634	13.60

(1) Includes the Trusts' interests in equity accounted investments and investment properties classified as held for sale.

(2) Rent per sq.ft. (\$) on expiry is stated in Canadian dollars.

SUMMARY OF SIGNIFICANT 2014 ACTIVITY

New Industrial Platform

In December 2014, the REIT entered into agreements to sell to an affiliate of the Public Sector Pension Investment Board ("PSP") and affiliates of Crestpoint Real Estate Investments Ltd. ("Crestpoint") (collectively, "CrestPSP") a 50% interest in a portfolio of Canadian industrial properties and a 49.5% interest in a portfolio of U.S. industrial properties (collectively the "Industrial Portfolio") for a total selling price of approximately \$559.8 million for the Canadian industrial properties and U.S. \$150.5 million for the U.S. industrial properties. H&R REIT Management Services LP will remain the property manager and collect industry standard fees. The Portfolio consists of a total of 101 properties comprising approximately 19.5 million square feet of industrial space located in Canada and in the United States. On December 22, 2014, the REIT sold interests in 84 of the 85 Canadian properties ("Tranche 1") to CrestPSP for a total selling price of approximately \$508.3 million. CrestPSP assumed mortgages of approximately \$161.7 million and received a mark-to-market adjustment on the assumed mortgages of approximately \$11.1 million. The REIT provided CrestPSP with a vendor take-back mortgage of approximately \$62.0 million. The net proceeds of \$273.5 million were used to repay bank indebtedness.

The remaining properties to be sold ("Tranche 2") will be comprised of interests in 16 U.S. properties and one Canadian property. The Tranche 2 sale is expected to close in Q1 2015 and CrestPSP is expected to assume mortgages of approximately U.S \$57.0 million. The expected net proceeds will be used to repay bank indebtedness. The REIT plans to build on this strategic alliance with PSP and Crestpoint by expanding on this new industrial platform.

Development of Airport Road Project

The development of the 744,413 square foot state-of-the-art, built-to-suit distribution centre on the Airport Road lands in Mississauga, ON, was completed ahead of schedule, and as a result, the property is now classified in the Trusts' Financial Statements as an investment property. Unilever Canada Inc.'s lease for 10 years commenced October 1, 2014 and the REIT is expected to earn a 7% unlevered return on its cost. As it is part of the Industrial Portfolio sale to CrestPSP, a 50% interest in this property is classified as an asset held for sale as at December 31, 2014.

Primaris Portfolio Activity

In Q2 2014, the REIT sold a 50% non-managing interest in three enclosed shopping centres: Regent Mall in Fredericton, NB; McAllister Place in Saint John, NB; and Grant Park in Winnipeg, MB for a total price of \$219.0 million, at a capitalization rate of 5.6% before management fee income. The purchaser assumed 50% of the outstanding mortgages. Net proceeds were approximately \$111.6 million. In September 2014, the REIT acquired a 50% managing interest in Kildonan Place, an enclosed shopping centre in Winnipeg, MB for \$69.7 million, at an effective capitalization rate of 6.0% including property management fee income. Kildonan Place is the third largest enclosed shopping centre in Winnipeg, MB. The site has approximately 7.5 acres of excess lands which after rezoning would result in total excess density of approximately 100,000 square feet for potential future development. These transactions continue to leverage the Primaris management platform as an owner and third party manager of regional shopping centres.

Exposure to Target

Target Corporation has announced it is planning to discontinue operating stores in Canada through its subsidiary Target Canada Co. ("Target"). Primaris has an interest in nine malls where Target is a tenant: a 50% interest in four of these malls and a 100% interest in the other five malls. Three of the leases are guaranteed by Target Corporation, the U.S. parent of Target. The total 2014 annual gross rent from Target represents 0.6% of the Trusts' rentals from investment properties (including equity accounted investments) of \$1.3 billion. The Target stores are well positioned in these malls and leased at an average net rent of \$5.58 per square foot which provides the opportunity to subdivide and remerchandise for higher rents, should Target disclaim their leases.

Leasing Activity

Effective December 31, 2014, Royal Bank of Canada vacated 274,100 square feet at the REIT's Front Street office property in Toronto, ON. The REIT is pleased to announce it has leased 231,170 square feet to Toronto Dominion Bank for an average term of approximately 11 years, commencing in three phases: 96,090 square feet effective June 1, 2015; 99,312 square feet effective October 1, 2015; and, 35,768 square feet effective August 1, 2016. The REIT has also leased a further 53,500 square feet to Penguin Random House Canada effective November 2015 for 10.5 years.

In addition, Gowlings Canada Inc. has renewed, for a further 15 years, its 130,274 square foot lease at 160 Elgin St., Ottawa, ON, which was to expire in 2016.

Long Island City Project

In June 2014, the REIT purchased a 50% interest to develop a landmark luxury residential rental development (the "Long Island City Project") in Long Island City, NY. Tishman Speyer, a U.S. real estate company, will act as the developer and manager of the Long Island City Project. The parcel is zoned for 1.2 million square feet of mixed-used development, potentially accommodating up to approximately 1,600 residential rental units and approximately 30,000 square feet of retail space. The site is located adjacent to the REIT's 2 Gotham Center office property. Construction is scheduled to begin in 2015 with occupancy expected to commence in late 2017. The REIT's share of the total land cost is U.S. \$55.6 million. The total Long Island City Project cost of all phases at the 100% level is expected to be approximately U.S. \$875 million.

U.S. Residential Apartments

In November 2014, the REIT acquired two residential properties in Houston, TX for U.S. \$44.7 million (U.S. \$64,152 per unit) at an average expected capitalization rate of 6.5%. The two properties consist of 696 rental apartment units representing net rentable area of 543,516 square feet. As at December 31, 2014, average occupancy was 93.1% and average monthly rent was U.S. \$766 per unit. On February 10, 2015, the REIT acquired another residential property in Dallas, TX for U.S. \$52.3 million at an expected capitalization rate of 5.6%. The property consists of 398 rental apartment units representing net rentable area of 362,785 square feet. Average occupancy is 95.0% and average monthly rent is U.S. \$1,140 per unit.

H&R Portfolio Dispositions

Excluding the Industrial Portfolio and Primaris dispositions discussed above, the REIT also disposed of non-core assets both in Canada and the United States totaling approximately \$230.5 million, representing approximately 1.1 million square feet. Refer to the "2014 Dispositions" table in this MD&A for a full list of properties sold.

Mortgage Financing and Unencumbered Pool

In 2014, the REIT repaid 27 mortgages totalling \$245.5 million which were bearing interest at a weighted average interest rate of 6.0%. As at December 31, 2014, excluding the Trusts' interests in real estate assets included in equity accounted investments, the REIT had 78 unencumbered properties with a fair value of approximately \$1.7 billion. Also, due to the REIT's 18-year history and management's conservative strategy of securing long-term financing on individual properties, the REIT had numerous other properties with very low loan to value ratios. As at December 31, 2014, the REIT had 42 properties valued at approximately \$1.6 billion which are encumbered with mortgages totaling \$364.5 million. In this pool of assets, the average loan to value is 22.3%, the maximum loan to value is 29.9% and the minimum loan to value is 7.8%. In August 2014, DBRS Limited ("DBRS") upgraded the Trusts' credit rating from BBB with a Stable trend to BBB (high) with a Stable trend. The REIT believes the rating upgrade is primarily due to the stabilization of the Bow, the successful integration of Primaris and recent high-quality property investments, which have resulted in significant operating income and portfolio growth, lower debt levels, a growing unencumbered asset pool, and an increase in the Trusts' coverage ratios.

SELECTED ANNUAL INFORMATION

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

(in thousands of Canadian dollars except per unit amounts)	Year Ended December 31, 2014	Year Ended December 31, 2013	Year Ended December 31, 2012
Rentals from investment properties	\$1,227,803	\$1,137,017	\$799,159
Finance income	901	2,108	1,854
Net income	424,655	323,635	508,860
Total comprehensive income	515,190	377,097	493,861
Total assets	13,368,380	13,583,027	9,873,050
Mortgages payable	4,318,136	4,897,726	3,813,613
Debentures payable	1,535,838	1,532,130	1,203,791
Cash distributions per unit	\$1.35	\$1.35	\$1.18

For a discussion of the changes between the periods noted above, please see the December 31, 2013 and 2012 MD&As of the Trusts.

SUMMARY OF QUARTERLY RESULTS

(in thousands of Canadian dollars)	December 31, 2014	September 30, 2014	June 30, 2014	March 31, 2014
Rentals from investment properties	\$308,597	\$302,394	\$304,927	\$311,885
Net income from equity accounted investments	12,222	13,020	9,702	9,179
Finance income	223	250	204	224
Net income	137,708	136,452	37,348	113,147
Total comprehensive income	175,772	183,430	2,945	153,043

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

⁽¹⁾ 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 the fair value of 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)	2014			2013		
	Amounts per the Trusts' Financial Statements	Equity accounted investments	The Trusts' interests	Amounts per the Trusts' Financial Statements	Equity accounted investments	The Trusts' interests
Property operating income:						
Rentals from investment properties	\$308,597	\$26,704	\$335,301	\$314,574	\$24,231	\$338,805
Property operating costs	(100,336)	(9,386)	(109,722)	(102,266)	(8,473)	(110,739)
	208,261	17,318	225,579	212,308	15,758	228,066
Net income (loss) from equity accounted investments	12,222	(11,847)	375	19,163	(19,354)	(191)
Finance costs:						
Finance income	223	60	283	257	36	293
Finance cost - operations	(79,247)	(5,283)	(84,530)	(83,807)	(4,796)	(88,603)
Gain (loss) on change in fair value	5,178	-	5,178	(5,516)	-	(5,516)
	(73,846)	(5,223)	(79,069)	(89,066)	(4,760)	(93,826)
Trust expenses	(3,587)	219	(3,368)	(3,410)	220	(3,190)
Fair value adjustment on real estate assets	10,134	(473)	9,661	(20,227)	8,375	(11,852)
Gain (loss) on sale of real estate assets	(12,557)	5	(12,552)	(204)	-	(204)
Gain on foreign exchange	9,011	-	9,011	6,772	-	6,772
Net income (loss) before income taxes	149,638	(1)	149,637	125,336	239	125,575
Income tax expense	(11,930)	(14)	(11,944)	(11,642)	(19)	(11,661)
Net income (loss) attributable to the Trusts' unitholders	137,708	(15)	137,693	113,694	220	113,914
Non-controlling interest	-	15	15	-	(220)	(220)
Net income	137,708	-	137,708	113,694	-	113,694
Other comprehensive income:						
Unrealized gain on translation of U.S. denominated foreign operations	37,990	-	37,990	22,990	-	22,990
Transfer of realized loss on cash flow hedges to net income	74	-	74	104	-	104
	38,064	-	38,064	23,094	-	23,094
Total comprehensive income all attributable to unitholders	\$175,772	-	\$175,772	\$136,788	-	\$136,788

The increase in net income before income taxes for the three months ended December 31, 2014 as compared to the three months ended December 31, 2013 is primarily due to the fair value adjustment on real estate assets and the gain (loss) on change in fair value offset by the gain (loss) on sale of real estate assets.

RESULTS OF OPERATIONS

Year ended December 31

	2014			2013		
	Amounts per the Trusts' Financial Statements	Equity accounted investments	The Trusts' interests	Amounts per the Trusts' Financial Statements	Equity accounted investments	The Trusts' interests
(in thousands of Canadian dollars)						
Property operating income:						
Rentals from investment properties	\$1,227,803	\$104,550	\$1,332,353	\$1,137,017	\$71,312	\$1,208,329
Property operating costs	(424,527)	(38,104)	(462,631)	(387,095)	(28,719)	(415,814)
	803,276	66,446	869,722	749,922	42,593	792,515
Net income (loss) from equity accounted investments	44,123	(43,673)	450	34,032	(34,231)	(199)
Finance costs:						
Finance income	901	184	1,085	2,108	75	2,183
Finance cost - operations	(323,955)	(19,956)	(343,911)	(309,629)	(13,197)	(322,826)
Gain (loss) on change in fair value	(8,029)	-	(8,029)	30,972	-	30,972
	(331,083)	(19,772)	(350,855)	(276,549)	(13,122)	(289,671)
Trust expenses	(11,091)	(169)	(11,260)	(5,979)	134	(5,845)
Fair value adjustment on real estate assets	(42,523)	(2,424)	(44,947)	44,751	4,849	49,600
Gain (loss) on sale of real estate assets	(16,025)	583	(15,442)	(2,067)	-	(2,067)
Gain on foreign exchange	22,602	-	22,602	14,042	-	14,042
Transaction costs	-	-	-	(204,819)	-	(204,819)
Net income before income taxes	469,279	991	470,270	353,333	223	353,556
Income tax expense	(44,624)	(148)	(44,772)	(29,698)	(34)	(29,732)
Net income attributable to the Trusts' unitholders	424,655	843	425,498	323,635	189	323,824
Non-controlling interest	-	(843)	(843)	-	(189)	(189)
Net income	424,655	-	424,655	323,635	-	323,635
Other comprehensive income:						
Unrealized gain on translation of U.S. denominated foreign operations	90,140	-	90,140	53,048	-	53,048
Transfer of realized loss on cash flow hedges to net income	395	-	395	414	-	414
	90,535	-	90,535	53,462	-	53,462
Total comprehensive income all attributable to unitholders	\$515,190	-	\$515,190	\$377,097	-	\$377,097

The increase in net income before income taxes for the year ended December 31, 2014 as compared to the year ended December 31, 2013 is primarily due to a decrease in transaction costs and an increase in property operating income primarily due to the acquisition of Primaris, offset by the fair value adjustment on real estate assets, gain (loss) on change in fair value, higher finance costs - operations and the gain (loss) on sale of real estate assets.

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 and utilities. Maintenance includes costs relating to items such as cleaning, interior and exterior building repairs and maintenance, elevator, HVAC, security and wages and benefits. Adjusted property operating income adjusts property operating income to exclude the realty tax adjustment accounted for under IFRIC 21. “Same-asset” refers to those properties owned by the REIT for the 2-year period ended December 31, 2014. “Transactions” refers to property operating income earned related to properties acquired, disposed and transferred from properties under development to investment properties.

(in thousands of Canadian dollars)	Three months ended December 31, 2014			Three months ended December 31, 2013		
	Same-Asset	Transactions	Total	Same-Asset	Transactions	Total
Rentals	\$175,672	\$128,272	\$303,944	\$174,085	\$134,853	\$308,938
Percentage rent	141	1,080	1,221	383	1,029	1,412
Straight-lining of contractual rent	862	2,570	3,432	1,507	2,717	4,224
Total rentals	176,675	131,922	308,597	175,975	138,599	314,574
Property operating costs	(51,907)	(48,429)	(100,336)	(51,143)	(51,123)	(102,266)
Property operating income	124,768	83,493	208,261	124,832	87,476	212,308
Realty taxes accounted for under IFRIC 21	(6,885)	(63)	(6,948)	(7,590)	(118)	(7,708)
Adjusted property operating income	\$117,883	\$83,430	\$201,313	\$117,242	\$87,358	\$204,600

Adjusted property operating income earned from Transactions decreased by \$3.9 million for the year ended December 31, 2014 compared to the year ended December 31, 2013 primarily due to the disposition of an interest in numerous properties in 2014.

(in thousands of Canadian dollars)	Year ended December 31, 2014			Year ended December 31, 2013		
	Same-Asset	Transactions	Total	Same-Asset	Transactions	Total
Rentals	\$696,648	\$512,080	\$1,208,728	\$676,790	\$424,030	\$1,100,820
Percentage rent	552	2,346	2,898	1,347	2,020	3,367
Straight-lining of contractual rent	5,741	10,436	16,177	5,159	27,671	32,830
Total rentals	702,941	524,862	1,227,803	683,296	453,721	1,137,017
Property operating costs	(227,671)	(196,856)	(424,527)	(222,174)	(164,921)	(387,095)
Property operating income	475,270	328,006	803,276	461,122	288,800	749,922
Realty taxes accounted for under IFRIC 21	-	-	-	-	-	-
Adjusted property operating income	\$475,270	\$328,006	\$803,276	\$461,122	\$288,800	\$749,922

Same-asset adjusted property operating income increased by \$14.1 million or 3.1% for the year ended December 31, 2014 compared to the year ended December 31, 2013 primarily due to the strengthening of the U.S. dollar compared to the Canadian dollar and the termination of the REIT’s external property management contract as part of the property management internalization further described herein. Included in same-asset adjusted property operating income for the year ended December 31, 2013 is a one-time adjustment to straight-lining of contractual rent of \$2.4 million. Without this one-time adjustment, same-asset straight-lining of contractual rent would have been \$7.6 million and same-asset adjusted property operating income would have been \$463.5 million for the year ended December 31, 2013.

Adjusted property operating income earned from Transactions increased by \$39.2 million for the year ended December 31, 2014 compared to the year ended December 31, 2013 primarily due to the REIT acquiring the Primaris portfolio on April 4, 2013, offset by property dispositions throughout 2013 and 2014.

Included in same-asset adjusted 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		
	2014	2013	Change	2014	2013	Change
Additional capital expenditure recoveries net of capital expenditures	\$2,286	\$1,051	\$1,235	\$9,234	\$7,450	\$1,784
Sundry income	(1,084)	846	(1,930)	62	2,665	(2,603)
Effect on same-asset - property operating income	\$1,202	\$1,897	(\$695)	\$9,296	\$10,115	(\$819)

Additional recoveries net of 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.

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

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 CEO, who is the chief operating decision maker, 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 Trusts' Financial Statements.

Property operating income for the three months ended December 31, 2014			Total per the Trusts' Financial Statements	Equity accounted investments	The Trusts' interests
(in thousands of Canadian dollars)	H&R Portfolio	Primaris Portfolio			
Rentals from investment properties	\$231,591	\$77,006	\$308,597	\$26,704	\$335,301
Property operating costs	(68,946)	(31,390)	(100,336)	(9,386)	(109,722)
Property operating income	162,645	45,616	208,261	17,318	225,579
Realty taxes accounted for under IFRIC 21	(6,948)	-	(6,948)	(253)	(7,201)
Adjusted property operating income	\$155,697	\$45,616	\$201,313	\$17,065	\$218,378

Property operating income for the three months ended December 31, 2013			Total per the Trusts' Financial Statements	Equity accounted investments	The Trusts' interests
(in thousands of Canadian dollars)	H&R Portfolio	Primaris Portfolio			
Rentals from investment properties	\$233,988	\$80,586	\$314,574	\$24,231	\$338,805
Property operating costs	(69,461)	(32,805)	(102,266)	(8,473)	(110,739)
Property operating income	164,527	47,781	212,308	15,758	228,066
Realty taxes accounted for under IFRIC 21	(7,708)	-	(7,708)	296	(7,412)
Adjusted property operating income	\$156,819	\$47,781	\$204,600	\$16,054	\$220,654

Property operating income for the year ended December 31, 2014 (in thousands of Canadian dollars)	H&R Portfolio	Primaris Portfolio	Total per the Trusts' Financial Statements	Equity accounted investments	The Trusts' interests
Rentals from investment properties	\$930,432	\$297,371	\$1,227,803	\$104,550	\$1,332,353
Property operating costs	(299,773)	(124,754)	(424,527)	(38,104)	(462,631)
Property operating income	630,659	172,617	803,276	66,446	869,722
Realty taxes accounted for under IFRIC 21	-	-	-	-	-
Adjusted property operating income	\$630,659	\$172,617	\$803,276	\$66,446	\$869,722

Property operating income for the year ended December 31, 2013 (in thousands of Canadian dollars)	H&R Portfolio	Primaris Portfolio	Total per the Trusts' Financial Statements	Equity accounted investments	The Trusts' interests
Rentals from investment properties	\$910,119	\$226,898	\$1,137,017	\$71,312	\$1,208,329
Property operating costs	(293,469)	(93,626)	(387,095)	(28,719)	(415,814)
Property operating income	616,650	133,272	749,922	42,593	792,515
Realty taxes accounted for under IFRIC 21	-	-	-	-	-
Adjusted property operating income	\$616,650	\$133,272	\$749,922	\$42,593	\$792,515

Adjusted property operating income from the H&R portfolio decreased by \$1.1 million for the three months ended December 31, 2014 compared to the three months ended December 31, 2013 primarily due to the disposition of an interest in numerous properties in 2014, partially offset by an increase in adjusted property operating income due to the strengthening of the U.S. dollar compared to the Canadian dollar.

Property operating income from the Primaris portfolio decreased by \$2.2 million for the three months ended December 31, 2014 compared to the three months ended December 31, 2013 primarily due to a decrease of \$2.9 million as a result of the four partial dispositions that occurred in Q2 2014, partially offset by an increase in property operating income, as a result of the acquisition of Kildonan Place in September 2014, as well as increases in property operating income from the remainder of the properties .

Adjusted property operating income from the H&R portfolio increased by \$14.0 million for the year ended December 31, 2014 compared to the year ended December 31, 2013 primarily due to the strengthening of the U.S. dollar compared to the Canadian dollar and the termination of the REIT's external property management contract as part of the property management internalization transaction further described herein. These increases were partially offset by property dispositions throughout 2013 and 2014.

Property operating income from the Primaris portfolio increased by \$39.3 million for the year ended December 31, 2014 compared to the year ended December 31, 2013 primarily due to the fact that the Primaris portfolio was acquired on April 4, 2013 and therefore contributed slightly less than a full nine months of property operating income in 2013 compared to a full year of property operating income in 2014. For the 13 enclosed shopping centres within the Primaris portfolio, sales per square foot, on a same-tenant basis, for Commercial Retail Units ("CRU"), have increased to \$503 per square foot for the twelve months ended December 31, 2014 from \$502 in the comparative period. For the same 13 properties within the Primaris portfolio, all store sales decreased by 0.6%. These figures only include enclosed shopping centres owned by Primaris for the entire rolling 24-month period ending December 31, 2014.

H&R REIT AND H&R FINANCE TRUST - MD&A - DECEMBER 31, 2014

	All Store Sales (in thousands of Canadian dollars) Rolling 12 month ended December 31			Same Store Sales (per square foot) Rolling 12 month ended December 31		
	2014	2013	% Change	2014	2013	% Change
	Cataraqui Town Centre	\$85,661	\$88,403	(3.1%)	\$460	\$457
Dufferin Mall	98,167	100,151	(2.0)	579	587	(1.4)
Grant Park ⁽¹⁾	17,953	17,834	0.7	420	414	1.4
McAllister Place ⁽¹⁾	52,165	50,345	3.6	423	434	(2.5)
Northland Village ⁽²⁾	36,163	41,001	(11.8)	478	475	0.6
Orchard Park Shopping Centre	148,777	144,958	2.6	594	573	3.7
Park Place	84,968	81,586	4.1	517	506	2.2
Place d'Orleans ⁽¹⁾	97,686	101,229	(3.5)	431	438	(1.6)
Place du Royaume	106,915	112,080	(4.6)	421	434	(3.0)
Regent Mall ⁽¹⁾	73,608	73,189	0.6	518	514	0.8
St. Albert	36,112	34,311	5.2	485	469	3.4
Stone Road	108,949	108,564	0.4	545	548	(0.5)
Sunridge	105,306	105,063	0.2	555	552	0.5
Total⁽³⁾	\$1,052,430	\$1,058,714	(0.6%)	\$503	\$502	0.2%

(1) All store sales and same-store sales have been reported as if Primaris owned 100% of Place d'Orleans, McAllister Place, Grant Park and Regent Mall for the entire rolling 12 months ended December 31, 2014 and 2013.

(2) All store sales were negatively impacted by the departure of a single tenant, a travel agency, and excluding the impact of this one tenant, the decrease in all store sales would have been (3.0%).

(3) The total same-store sales figures have been presented on a weighted average basis.

Segmented Statement of Financial Position:

As at December 31, 2014

(in thousands of Canadian dollars)

	H&R Portfolio	Primaris Portfolio	Elimination*	Total per the Trusts' Financial Statements
Total assets	\$10,883,395	\$3,078,633	(\$593,648)	\$13,368,380
Total liabilities	\$6,010,777	\$1,423,583	(\$593,648)	\$6,840,712

As at December 31, 2013

(in thousands of Canadian dollars)

	H&R Portfolio	Primaris Portfolio	Elimination*	Total per the Trusts' Financial Statements
Total assets	\$11,048,400	\$3,209,492	(\$674,865)	\$13,583,027
Total liabilities	\$6,253,602	\$1,730,489	(\$674,865)	\$7,309,226

* Elimination of intercompany loans between Primaris and the REIT.

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.

Property operating income for the three months ended December 31, 2014			Total per the Trusts'	Canadian equity	U.S. equity	
(in thousands of Canadian dollars)	Canada	United States	Financial Statements	accounted investments	accounted investments	The Trusts' interests
Rentals from investment properties	\$249,782	\$58,815	\$308,597	\$16,154	\$10,550	\$335,301
Property operating costs	(94,402)	(5,934)	(100,336)	(7,629)	(1,757)	(109,722)
Property operating income	155,380	52,881	208,261	8,525	8,793	225,579
Realty taxes accounted for under IFRIC 21	-	(6,948)	(6,948)	-	(253)	(7,201)
Adjusted property operating income	\$155,380	\$45,933	\$201,313	\$8,525	\$8,540	\$218,378

Property operating income for the three months ended December 31, 2013			Total per the Trusts'	Canadian equity	U.S. equity	
(in thousands of Canadian dollars)	Canada	United States	Financial Statements	accounted investments	accounted investments	The Trusts' interests
Rentals from investment properties	\$259,458	\$55,116	\$314,574	\$15,461	\$8,770	\$338,805
Property operating costs	(97,406)	(4,860)	(102,266)	(6,976)	(1,497)	(110,739)
Property operating income	162,052	50,256	212,308	8,485	7,273	228,066
Realty taxes accounted for under IFRIC 21	-	(7,708)	(7,708)	-	296	(7,412)
Adjusted property operating income	\$162,052	\$42,548	\$204,600	\$8,485	\$7,569	\$220,654

Property operating income for the year months ended December 31, 2014			Total per the Trusts'	Canadian equity	U.S. equity	
(in thousands of Canadian dollars)	Canada	United States	Financial Statements	accounted investments	accounted investments	The Trusts' interests
Rentals from investment properties	\$998,836	\$228,967	\$1,227,803	\$63,550	\$41,000	\$1,332,353
Property operating costs	(376,018)	(48,509)	(424,527)	(29,729)	(8,375)	(462,631)
Property operating income	622,818	180,458	803,276	33,821	32,625	869,722
Realty taxes accounted for under IFRIC 21	-	-	-	-	-	-
Adjusted property operating income	\$622,818	\$180,458	\$803,276	\$33,821	\$32,625	\$869,722

Property operating income for the year ended December 31, 2013			Total per the Trusts'	Canadian equity	U.S. equity	
(in thousands of Canadian dollars)	Canada	United States	Financial Statements	accounted investments	accounted investments	The Trusts' interests
Rentals from investment properties	\$925,236	\$211,781	\$1,137,017	\$58,624	\$12,688	\$1,208,329
Property operating costs	(341,412)	(45,683)	(387,095)	(26,035)	(2,684)	(415,814)
Property operating income	583,824	166,098	749,922	32,589	10,004	792,515
Realty taxes accounted for under IFRIC 21	-	-	-	-	-	-
Adjusted property operating income	\$583,824	\$166,098	\$749,922	\$32,589	\$10,004	\$792,515

Adjusted property operating income from the Canadian geographic segment decreased by \$6.7 million for the three months ended December 31, 2014 compared to the three months ended December 31, 2013 primarily due to the disposition of an interest in numerous properties in 2014. Refer to the "2014 Dispositions" section of this MD&A for a list of properties sold during 2014. Adjusted property operating income from the Canadian geographic segment increased by \$39.0 million for the year ended December 31, 2014 compared to the year ended December 31, 2013 primarily due to the REIT acquiring the Primaris portfolio on April 4, 2013, offset by property dispositions throughout 2013 and 2014.

Adjusted property operating income from the U.S. geographic segment increased by \$3.4 million and \$14.4 million, respectively, for the three months and year ended December 31, 2014 compared to the respective 2013 periods primarily due to the strengthening of the U.S. dollar compared to the Canadian dollar. The average exchange rate for the three months ended December 31, 2014 was Canadian \$1.13 for each U.S. \$1.00 (Q4 2013 - \$1.06). The average exchange rate for the year ended December 31, 2014 was Canadian \$1.10 for each U.S. \$1.00 (December 31, 2013 - \$1.03).

Adjusted property operating income from U.S. equity accounted investments increased by \$22.6 million for the year ended December 31, 2014 compared to the year ended December 31, 2013 due to the REIT acquiring a 33.6% interest in ECHO in August 2013.

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, gain (loss) on change in fair value, trust expenses, unit-based compensation, fair value adjustment on real estate assets, gain (loss) on sale of real estate assets, gain 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		
	2014	2013	Change	2014	2013	Change
Rentals from investment properties	\$26,704	\$24,231	\$2,473	\$104,550	\$71,312	\$33,238
Property operating costs	(9,386)	(8,473)	(913)	(38,104)	(28,719)	(9,385)
Net income (loss) from equity accounted investments	375	(191)	566	450	(199)	649
Finance income	60	36	24	184	75	109
Finance costs - operations	(5,283)	(4,796)	(487)	(19,956)	(13,197)	(6,759)
Trust expenses	219	220	(1)	(169)	134	(303)
Fair value adjustment on real estate assets	(473)	8,375	(8,848)	(2,424)	4,849	(7,273)
Gain on sale of real estate assets	5	-	5	583	-	583
Income tax expense	(14)	(19)	5	(148)	(34)	(114)
Non-controlling interest	15	(220)	235	(843)	(189)	(654)
Net income from equity accounted investments	12,222	19,163	(6,941)	44,123	34,032	10,091
Realty taxes accounted for under IFRIC 21	(253)	296	(549)	-	-	-
Fair value adjustment on real estate assets	473	(8,375)	8,848	2,424	(4,849)	7,273
Gain on sale of real estate assets	(5)	-	(5)	(583)	-	(583)
FFO from equity accounted investments	12,437	11,084	1,353	45,964	29,183	16,781
Straight-lining of contractual rent	38	16	22	(730)	(476)	(254)
Rent amortization of tenant inducements	267	236	31	1,026	321	705
Effective interest rate accretion	(290)	(355)	65	(1,352)	(238)	(1,114)
Unit-based compensation	(301)	69	(370)	-	92	(92)
Capital expenditures	30	(2,100)	2,130	(3,461)	(4,449)	988
Tenant expenditures	(273)	(535)	262	(1,690)	(860)	(830)
AFFO from equity accounted investments	\$11,908	\$8,415	\$3,493	\$39,757	\$23,573	\$16,184

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

Net income from equity accounted investments for the three months ended December 31, 2014 compared to the three months ended December 31, 2013, decreased by \$6.9 million primarily due to the fair value adjustment on real estate assets offset by an increase in property operating income as a result of ECHO acquiring and completing the development of several properties in the last 12 months. Net income from equity accounted investments for the year ended December 31, 2014 compared to the year ended December 31, 2013, increased by \$10.1 million primarily due to an increase in property operating income as a result of the acquisition of a one-third interest in 100 Yonge St., in June 2013 and a 33.6% interest in ECHO in August 2013. ECHO reports its financial results to the REIT one month in arrears due to time constraints on its reporting. The above amounts for the three months ended December 31, 2014 and 2013 include ECHO's financial information from September 1 to November 30 of the respective years and the above amounts for the year ended December 31, 2014 include ECHO's financial information from December 1, 2013 to November 30, 2014. The above amounts for the year ended December 31, 2013 includes ECHO's financial information from August 1, 2013 to November 30, 2013. The Trusts are not aware of ECHO being a party to any significant transactions during December 2014.

Finance Cost - Operations (in thousands of Canadian dollars)	Three months ended December 31			Year ended December 31		
	2014	2013	Change	2014	2013	Change
Contractual interest on mortgages payable	\$54,312	\$60,161	(\$5,849)	\$228,807	\$230,416	(\$1,609)
Contractual interest on debentures payable	17,161	16,793	368	68,077	61,701	6,376
Interest on construction loans	-	-	-	-	144	(144)
Effective interest rate accretion	(918)	(1,161)	243	(4,304)	(4,176)	(128)
Bank interest and charges	3,067	2,139	928	9,545	8,109	1,436
Exchangeable unit distributions	5,625	5,875	(250)	23,162	13,967	9,195
	79,247	83,807	(4,560)	325,287	310,161	15,126
Capitalized interest	-	-	-	(1,332)	(532)	(800)
Finance cost - operations	\$79,247	\$83,807	(\$4,560)	\$323,955	\$309,629	\$14,326

The decrease in contractual interest on mortgages payable for the three months and year ended December 31, 2014 as compared to the respective 2013 periods is primarily due to mortgages being assumed or discharged upon the disposal of properties and the repayment of mortgages. For the year ended December 31, 2014 as compared to the year ended December 31, 2013, the decrease explained above was offset by an increase in contractual interest on mortgages payable resulting from the acquisition of the Primaris portfolio in April 2013 and the issuance of the Series C Bow Bonds in June 2013.

The increase in contractual interest on debentures payable of \$0.4 million and \$6.4 million for the three months and year ended December 31, 2014 compared to the respective 2013 periods is due to the issuance of the Series G, Series H and Series I senior debentures in 2013, as well as the assumption of the 2018 convertible debentures from Primaris in 2013. This was offset by the redemption of the 2017 convertible debentures in July 2013.

Exchangeable unit distributions increased by \$9.2 million for the year ended December 31, 2014 compared to the year ended December 31, 2013 due to the issuance of exchangeable units as part of the property management internalization transaction effective July 2013 and the exchangeable units assumed as part of the acquisition of Primaris in April 2013.

Finance Cost – Gain (Loss) on Change in Fair Value (in thousands of Canadian dollars)	Three months ended December 31			Year ended December 31		
	2014	2013	Change	2014	2013	Change
Gain (loss) on fair value of convertible debentures	\$2,940	(\$1,191)	\$4,131	(\$1,559)	\$22,378	(\$23,937)
Gain (loss) on fair value of exchangeable units	2,167	(3,657)	5,824	(6,859)	10,210	(17,069)
Net gain (loss) on derivative instruments	71	(668)	739	389	(1,616)	2,005
Finance cost - gain (loss) on change in fair value	\$5,178	(\$5,516)	\$10,694	(\$8,029)	\$30,972	(\$39,001)

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) on change in fair value.

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, 2014, the change in fair value is based on the quoted price of Stapled Units which was \$21.73 as at December 31, 2014 (September 30, 2014 - \$21.86, December 31, 2013 - \$21.40). 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).

Trust Expenses (in thousands of Canadian dollars)	Three months ended December 31			Year ended December 31		
	2014	2013	Change	2014	2013	Change
Other expenses	\$6,203	\$6,557	(\$354)	\$22,382	\$20,015	\$2,367
Unit-based compensation - as reported under IFRS	1,102	300	802	3,849	(4,136)	7,985
Management fees received from the Primaris portfolio	(3,718)	(3,447)	(271)	(15,140)	(9,900)	(5,240)
Trust expenses	\$3,587	\$3,410	\$177	\$11,091	\$5,979	\$5,112

Other expenses are primarily comprised of salaries, professional fees, trustee fees and corporate overhead expenses. Other expenses increased by \$2.4 million for the year ended December 31, 2014 compared to the year ended December 31, 2013 primarily due to the REIT acquiring the Primaris portfolio in April 2013. Management fees received from the Primaris portfolio increased by \$5.2 million for the year ended December 31, 2014 compared to the year ended December 31, 2013 due to the REIT acquiring the Primaris portfolio in April 2013.

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:

Unit-based Compensation (in thousands of Canadian dollars)	Three months ended December 31			Year ended December 31		
	2014	2013	Change	2014	2013	Change
Unit-based compensation	\$629	\$770	(\$141)	\$4,277	\$2,601	\$1,676
Fair value adjustment to unit-based compensation	473	(470)	943	(428)	(6,737)	6,309
Unit-based compensation - as reported under IFRS	\$1,102	\$300	\$802	\$3,849	(\$4,136)	\$7,985

Unit-based compensation increased by \$1.7 million for the year ended December 31, 2014 compared to the year ended December 31, 2013 primarily due to a one-time catch up adjustment of \$1.7 million in Q1 2014 relating to the calculation of how unit options vest over their three year period.

The fair value adjustment to unit-based compensation is comprised of the following two compensation plans: (i) the Unit Option Plan, which is measured based on the quoted price of the Stapled Units at the end of the period compared to the exercise price of each option on the date of grant and (ii) the Incentive Unit Plan, which is measured based on the quoted price of the Stapled Units at the end of the period compared to the market price of the Stapled Units on the date of grant. The quoted price of Stapled Units was \$21.73 as at December 31, 2014 (September 30, 2014 - \$21.86, December 31, 2013 - \$21.40). The quoted price of Stapled Units was \$21.40 as at December 31, 2013 (September 30, 2013 - \$21.19, December 31, 2012 - \$24.10).

Fair Value Adjustment on Real Estate Assets (in thousands of Canadian dollars)	Three months ended December 31			Year ended December 31		
	2014	2013	Change	2014	2013	Change
Fair value adjustment on real estate assets	\$10,134	(\$20,227)	\$30,361	(\$42,523)	\$44,751	(\$87,274)

The REIT records its real estate assets at fair value. The changes of \$30.4 million and (\$87.3 million) for the three months and year ended December 31, 2014 compared to the respective 2013 periods are due to changes in market assumptions used in the property valuations from quarter to quarter, IFRIC 21, capital and tenant expenditures and straight-lining of contractual rent. Refer to note 4 in the Trusts' Financial Statements for further details on the valuation of the portfolio.

Loss on Sale of Real Estate Assets (in thousands of Canadian dollars)	Three months ended December 31			Year ended December 31		
	2014	2013	Change	2014	2013	Change
Loss on sale of real estate assets	(\$12,557)	(\$204)	(\$12,353)	(\$16,025)	(\$2,067)	(\$13,958)

The loss on sale of real estate assets of \$12.6 million for the three months ended December 31, 2014 is primarily due to mark-to-market adjustments on the purchasers' assumption of mortgages on properties included in the sale of Tranche 1 of the Industrial Portfolio of \$11.1 million.

The loss on sale of real estate assets of \$16.0 million for the year ended December 31, 2014 is primarily due to the following: (i) mark-to-market adjustments on the purchasers' assumption of mortgages on 23 properties of \$16.6 million (of which 19 properties were included in the sale of Tranche 1 of the Industrial Portfolio); and (ii) one-time prepayment penalties of \$3.1 million to discharge the mortgages from the sale of 1618 Station St. and the four properties tenanted by U.S. grocer Bi-Lo. Excluding these mark-to-market adjustments and one-time prepayment penalties, the properties sold during the year ended December 31, 2014 generated a gain on sale of \$3.6 million.

Gain on Foreign Exchange (in thousands of Canadian dollars)	Three months ended December 31			Year ended December 31		
	2014	2013	Change	2014	2013	Change
Gain on foreign exchange	\$9,011	\$6,772	\$2,239	\$22,602	\$14,042	\$8,560

The amounts in the table above were 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 Trusts' 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 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.

Transaction Costs (in thousands of Canadian dollars)	Three months ended December 31			Year ended December 31		
	2014	2013	Change	2014	2013	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 which were expensed as incurred.

During the year ended December 31, 2013, H&R REIT Management Services LP ("HRRMSLP"), a subsidiary of the REIT, acquired H&R Property Management Ltd.'s ("HRPM") REIT-related property management business in return for 9.5 million partnership units of HRRMSLP, which are exchangeable on a one-for-one basis for Stapled Units. The 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 partnership units for the months of July and August totalling \$2.1 million were included in transaction costs. The remaining \$1.3 million of transaction costs in connection with the internalization transaction relate to professional fees.

Income Tax Expense (in thousands of Canadian dollars)	Three months ended December 31			Year ended December 31		
	2014	2013	Change	2014	2013	Change
Current income taxes	\$436	\$19	\$417	\$920	\$471	\$449
Deferred income taxes	11,494	11,623	(129)	43,704	29,227	14,477
Total income taxes	\$11,930	\$11,642	\$288	\$44,624	\$29,698	\$14,926

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, 2014, the REIT had net deferred tax liabilities of \$129.9 million (December 31, 2013 - \$76.6 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, 2014 and December 31, 2013 per the Trusts' Financial Statements:

	December 31, 2014		December 31, 2013	
	Investment Properties	Properties Under Development	Investment Properties	Properties Under Development
Opening balance, beginning of year	\$12,786,205	\$146,478	\$9,235,562	\$128,220
Acquisitions of investment properties, through business combination	-	-	3,179,418	-
Acquisition of investment properties including transaction costs	151,942	-	211,360	-
Additions to existing investment properties:				
Capital expenditures	38,206	-	33,704	-
Direct leasing costs	32,941	-	18,799	-
Redevelopment	52,684	-	52,196	-
Additions to properties under development (including capitalized interest)	-	50,880	-	22,631
Dispositions	(947,162)	-	(183,433)	(4,373)
Transfer of investment properties to assets classified as held for sale	(296,992)	-	-	-
Straight-line rents and blend and extend rents included in revenue	21,331	-	38,124	-
Transfer of property under development that has reached practical completion to investment properties	92,352	(92,352)	-	-
Change in foreign exchange	227,999	-	155,724	-
Fair value adjustment on real estate assets	(42,523)	-	44,751	-
Closing balance, end of year	\$12,116,983	\$105,006	\$12,786,205	\$146,478

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.

2014 Acquisitions

During the year ended December 31, 2014, the REIT acquired one retail property, a 50% ownership interest in a retail property, one equity accounted investment, one parcel of land adjacent to an existing investment property and two residential properties. During the year ended December 31, 2013, in addition to Primaris, the REIT acquired five retail properties, two equity accounted investments and one parcel of land adjacent to an existing investment property.

Property/Acquisition	Year Built	Property Type	Date Acquired	Square Footage	Cash Purchase Price (\$ Millions)	Anchor/Major Tenants	Average Remaining Lease Term (years) ⁽¹⁾
3621 Dufferin St., Toronto, ON	-	H&R - Land	Feb 6, 2014	⁽²⁾	\$14.3	N/A	N/A
12975 Collier Blvd., Naples, FL	2009	H&R - Retail	Feb 19, 2014	65,941	15.3	Publix Supermarkets Inc.	11.6
Long Island City, NY Development	-	H&R - Residential Development	June 16, 2014	-	70.3 ⁽³⁾	N/A	N/A
Kildonan Place, Winnipeg, MB	1980/2013	Primaris - Retail	Sep 17, 2014	228,261 ⁽³⁾	69.7 ⁽³⁾	Target, Sears	4.7
12510 South Green Dr., Houston, TX	1984	H&R - Residential	Nov 25, 2014	323,568	31.5	N/A	N/A
12601 South Green Dr., Houston, TX	1984	H&R - Residential	Nov 25, 2014	219,948	18.7	N/A	N/A
Total				837,718	219.8		

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

⁽²⁾ Approximately 4.2 acres of land adjacent to an office property was purchased.

⁽³⁾ Square footage and cash purchase price are based on the REIT's interests.

2014 Dispositions:

During the year ended December 31, 2014, the REIT sold an office property including an adjacent parcel of land, a 50% ownership interest in an office property, a portion of an office property (sold as separate condominium units), five retail properties, a 50% ownership interest in three retail properties, five industrial properties and a 50% ownership interest in 84 industrial properties. During the year ended December 31, 2013, the REIT sold two office 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), three industrial properties and a parcel of land held for development.

Property	Property Type	Date Sold	Square Feet	Gross Proceeds (\$ Millions)	Ownership Interest Sold
1618 Station St., Vancouver, BC	H&R - Office	Mar 17, 2014	73,197	\$30.5	100%
2780-2800 Skymark Ave., Mississauga, ON	H&R - Office	Q2 and Q3 2014	27,280	4.1	100%
Regent Mall, Fredericton, NB ⁽¹⁾	Primaris - Retail	May 15, 2014	249,655	102.5	50%
McAllister Place, Saint John, NB ⁽¹⁾	Primaris - Retail	May 15, 2014	246,546	70.0	50%
115 Belfield Rd., Toronto, ON	H&R - Industrial	May 27, 2014	47,990	3.4	100%
Grant Park Shopping Centre, Winnipeg, MB ⁽¹⁾	Primaris - Retail	June 13, 2014	198,961	46.5	50%
2928-16 th St., N.E., Calgary, AB	H&R - Industrial	June 25, 2014	163,280	29.3	100%
3620-32 nd St., N.E., Calgary, AB	H&R - Industrial	June 25, 2014	65,120	10.1	100%
3777 Kingsway St., Burnaby, BC ⁽¹⁾	H&R - Office	June 30, 2014	343,085	86.5	50%
50 Cambridge St., Worcester, MA	H&R - Retail	July 18, 2014	69,020	17.1	100%
1628 Station St., Vancouver, BC	H&R - Land	July 28, 2014	- ⁽²⁾	4.5	100%
200 Chisholm Dr., Milton, ON	H&R - Industrial	Sept 24, 2014	91,828	7.3	100%
417 Blue Ridge St., Blairsville, GA	H&R - Retail	Sept 30, 2014	36,524	6.3	100%
420 Market St., Dayton, TN	H&R - Retail	Sept 30, 2014	45,983	6.0	100%
6951 Lee Hwy., Chattanooga, TN	H&R - Retail	Sept 30, 2014	48,261	10.1	100%
819 W. Carolina Ave., Hartsville, SC	H&R - Retail	Sept 30, 2014	32,998	10.6	100%
4248-14 th Ave., Markham, ON	H&R - Industrial	Dec 3, 2014	32,708	4.6	100%
Industrial Portfolio - Tranche 1 ⁽¹⁾	H&R - Industrial	Dec 22, 2014	6,171,907	508.3	50%
Total			7,944,343	\$957.7	

⁽¹⁾ Square feet and gross proceeds are based on the ownership interest disposed.

⁽²⁾ Approximately 1.25 acres of land adjacent to 1618 Station St. in Vancouver, BC was sold.

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

Type of Asset (millions)	Fair Value December 31, 2014⁽¹⁾	Fair Value December 31, 2013⁽¹⁾
Office	\$6,915	\$6,881
Retail	5,253	5,200
Industrial	1,038	1,749
Residential	52	-
Total portfolio	13,258	13,830
Less: Trusts' interests of fair value of investment properties included in equity accounted investments	(1,141)	(1,044)
Fair value of investment properties per the Trusts' Financial Statements	\$12,117	\$12,786

Region (millions)	Fair Value December 31, 2014⁽¹⁾	Fair Value December 31, 2013⁽¹⁾
Ontario	\$4,591	\$4,879
Alberta	4,120	4,234
Quebec	496	594
Other	1,003	1,294
Canada	10,210	11,001
United States	3,048	2,829
Total portfolio	13,258	13,830
Less: Trusts' interests of fair value of investment properties included in equity accounted investments	(1,141)	(1,044)
Fair value of investment properties per the Trusts' Financial Statements	\$12,117	\$12,786

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

Properties under Development

Development of Airport Road Project

The development of the 744,413 square foot state-of-the-art, built-to-suit distribution centre on the Airport Road lands in Mississauga, ON, was completed ahead of schedule, and as a result, the property is now classified in the Trusts' Financial Statements as an investment property. Unilever Canada Inc.'s lease for 10 years commenced October 1, 2014 and the REIT is expected to earn a 7% unlevered return on its cost. The cost transferred from properties under development to investment properties was \$92.4 million. As it is part of the Industrial Portfolio sale to CrestPSP, a 50% interest in this property is classified as an asset held for sale as at December 31, 2014.

Equity Accounted Investments*
(in thousands of Canadian dollars)

	December 31, 2014	December 31, 2013
Investment properties	\$1,140,757	\$1,043,306
Properties under development	106,347	15,079
Other assets	14,372	15,092
Cash and cash equivalents	15,143	8,649
Total assets	1,276,619	1,082,126
Mortgages payable	(472,535)	(456,401)
Bank indebtedness	(54,729)	(28,465)
Accounts payable and accrued liabilities	(37,246)	(30,842)
Non-controlling interest	(9,090)	(8,269)
Equity accounted investments	\$703,019	\$558,149

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

ECHO reports its financial position to the REIT one month in arrears due to time constraints on its reporting. Therefore, the above amounts include ECHO's financial reporting as at November 30, 2014. The Trusts are not aware of ECHO being a party to any significant transactions during December 2014.

Long Island City Project

In June 2014, the REIT purchased a 50% interest in the Long Island City Project. Tishman Speyer, a U.S. real estate company, will act as the developer and manager of the Project. The parcel is zoned for 1.2 million square feet of mixed-used development, potentially accommodating up to approximately 1,600 residential rental units and approximately 30,000 square feet of retail space developed in three phases. The site is located adjacent to the REIT's 2 Gotham Center office property. In the initial phase, the REIT and Tishman Speyer plan to construct a 42-storey tower, which will include 700 rental apartment units. Construction is expected to begin in 2015 with occupancy expected to commence in 2017. The REIT's share of the total land cost is U.S. \$55.6 million. The total Project cost of all phases at the 100% level is expected to be approximately U.S. \$875 million.

Assets and Liabilities Classified as Held for Sale

As at December 31, 2014, the REIT holds a 49.5% ownership interest in 16 industrial properties, a 50% ownership interest in one industrial property and a 100% ownership interest in one industrial property as held for sale (December 31, 2013 - nil). The total fair value of these properties was \$297.0 million with mortgages payable of \$66.0 million as at December 31, 2014.

Mortgages Receivable

Mortgages receivable increased from \$9.7 million as at December 31, 2013 to \$79.9 million as at December 31, 2014 due to the REIT granting a mortgage receivable of \$62.0 million as part of the sale of Tranche 1 of the Industrial Portfolio and a mortgage receivable of \$8.2 million as part of the sale of 3777 Kingsway St., in Burnaby, B.C.

Other Assets

Other assets decreased by \$11.9 million from \$54.6 million as at December 31, 2013 to \$42.7 million as at December 31, 2014. This is due to decreases in restricted cash of \$1.9 million, accounts receivable of \$3.5 million and prepaid expenses and sundry assets of \$6.5 million.

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 and amounts in the table below are non-GAAP measures.

	December 31, 2014	December 31, 2013
Debt to total assets per the Trusts' Financial Statements	46.3%	49.2%
Debt to total assets based on the Trusts' Interests	48.1%	50.8%
Non-recourse mortgages as a percentage of total mortgages ⁽¹⁾	53.8%	51.1%
Floating rate debt as a percentage of total debt ⁽¹⁾	4.1%	2.9%
Canadian properties total debt to fair market value of total Canadian assets ⁽¹⁾	46.8%	49.5%
U.S. properties total debt to fair market value of total U.S. assets ⁽¹⁾	52.3%	55.7%
Unencumbered assets (in thousands of Canadian dollars)	1,657,865	1,340,406
Interest coverage ratio ⁽¹⁾⁽²⁾	2.69:1	2.59:1
Weighted average interest rate of outstanding debt ⁽¹⁾⁽³⁾	4.7%	4.8%
Weighted average term to maturity of outstanding debt (in years) ⁽¹⁾⁽³⁾	5.7	6.1

⁽¹⁾ Presented based on the Trusts' Interests.

⁽²⁾ For the quarters ended December 31, 2014 and the year ended December 31, 2013, respectively.

⁽³⁾ Outstanding debt includes mortgages and debentures.

Mortgages Payable

The following table shows the change in mortgages payable from January 1, 2014 to December 31, 2014:

(in thousands of Canadian dollars)

Opening balance - January 1, 2014	\$4,897,726
Principal repayments	(153,035)
Mortgages repaid	(290,134)
New mortgages	141,580
Mortgages reclassified to liabilities held for sale	(65,958)
Mortgages released upon the sale of investment properties	(325,975)
Effective interest rate accretion on mortgages	(6,377)
Foreign exchange difference	120,309
Closing balance – December 31, 2014	\$4,318,136

The following table discloses the Trusts' mortgage payable balance, adjusted to include debt related to equity accounted investments at the Trusts' interests and mortgages classified as held for sale:

	December 31, 2014	December 31, 2013
Mortgages payable per the Trusts' Financial Statements	\$4,318,136	\$4,897,726
Trusts' interests of mortgages payable related to equity accounted investments	472,535	456,401
Mortgages payable classified as held for sale	65,958	-
Total mortgages payable	\$4,856,629	\$5,354,127

The following table below shows the Trusts' 5-year mortgage maturity profile as at December 31, 2014 and includes the Trusts' interests of mortgages related to equity accounted investments and mortgages classified as held for sale:

MORTGAGES PAYABLE	Periodic Amortized Principal (\$000's)	Principal on Maturity (\$000's)	Total Principal ⁽¹⁾ (\$000's)	% of Total Principal	Weighted Average Interest Rate on Maturity
2015	\$168,632	\$230,912	\$399,544	8.3%	5.3%
2016	175,394	312,401	487,795	10.1	5.4%
2017	164,987	402,586	567,573	11.8	4.7%
2018	162,285	120,259	282,544	5.8	5.4%
2019	153,934	314,510	468,444	9.7	3.5%
Thereafter			2,625,312	54.3	
			4,831,212	100%	
Financing costs and mark-to-market adjustment arising on acquisitions ⁽¹⁾			25,417		
Total			\$4,856,629		

⁽¹⁾ 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 Trusts' mortgages payable balances and are recognized in finance costs over the life of the applicable mortgage.

The mortgages outstanding as at December 31, 2014 bear interest at a weighted average rate of 4.7% (December 31, 2013 - 4.9%) and mature between 2015 and 2035. The weighted average term to maturity of the Trusts' mortgages is 6.4 years (December 31, 2013 - 7.0 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.

Debentures Payable

Debentures payable increased by \$3.7 million from \$1,532.1 million as at December 31, 2013 to \$1,535.8 million as at December 31, 2014 mainly due to a change in the quoted price of the Convertible Debentures as well as an increase in accumulated amortization of issue costs from the Senior Debentures. In February 2015, the REIT repaid all of the outstanding Series A Senior Debentures upon maturity for a total cash payment of \$115.0 million.

Exchangeable Units

Certain of the REIT's subsidiaries have 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 number of exchangeable units are issued and outstanding:

	Number of Exchangeable Units	Quoted Price of Stapled Units	Amounts per the Trusts' Financial Statements (\$000's)
As at December 31, 2013	17,403,119	\$21.40	\$372,427
Exchangeable units of H&R Portfolio Limited Partnership, a subsidiary partnership of the REIT, exchanged for Stapled Units	(739,303)	-	-
As at December 31, 2014	16,663,816	\$21.73	\$362,105

A subsidiary of the REIT holds 0.4 million Stapled Units to mirror these exchangeable units. Therefore, when these exchangeable units are exchanged for Stapled Units, the number of outstanding Stapled Units will only increase by 16.2 million. The 0.4 million exchangeable units have been excluded from the weighting of exchangeable units used to calculate FFO and AFFO per unit amounts.

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, 2014	December 31, 2013
Deferred tax assets:		
Net operating losses and deferred interest deductions	\$95.4	\$84.4
Accounts payable and accrued liabilities	2.1	1.9
Derivative instruments	0.1	0.2
Other assets	0.2	0.1
	97.8	86.6
Deferred liabilities:		
Investment properties	218.4	162.1
Equity accounted investments	9.3	1.1
	227.7	163.2
Deferred tax liability	(\$129.9)	(\$76.6)

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.

Accounts Payable and Accrued Liabilities

Accounts payable and accrued liabilities decreased by \$24.2 million from \$172.1 million as at December 31, 2013 to \$147.9 million as at December 31, 2014 primarily due to the following: (i) a decrease of \$9.9 million in accruals as part of the Trust's normal course of business operations; (ii) a decrease of \$7.8 million in prepaid rent; and (iii) a decrease of \$3.6 million in accounts payable relating to development projects.

EQUITY

Unitholders' Equity

Unitholders' equity increased by \$253.9 million from \$6,273.8 million as at December 31, 2013 to \$6,527.7 million as at December 31, 2014. The increase is primarily due to net income, other comprehensive income and proceeds from issuance of units under the DRIP, all of which was partially offset by distributions paid to unitholders during the same period.

Other comprehensive income 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.

NCIB

On April 11, 2014, the Trusts received approval from the TSX for a NCIB, allowing the Trusts to purchase for cancellation up to a maximum of 25 million Stapled Units on the open market until the earlier of April 14, 2015 or the date on which the Trusts have purchased the maximum number of Stapled Units permitted under the NCIB. During the year ended December 31, 2014, the Trusts purchased and cancelled 67,300 Stapled Units at a weighted average price of \$21.58 per unit, for a total cost of approximately \$1.5 million. Subsequent to December 31, 2014, the Trusts purchased and cancelled 179,400 Stapled Units at a weighted average price of \$21.94 per unit, for a total cost of approximately \$3.9 million.

FUNDS FROM OPERATIONS

FFO is a recognized measure that is widely used by the real estate industry, particularly by those publicly traded entities that own and operate investment properties. FFO is a financial measure which should not be considered as an alternative to net income, cash flow from operations, or any other operating or liquidity measure prescribed under IFRS. The Trusts present FFO in accordance with the REALpac White Paper on Funds From Operations. The use of FFO, combined with the required IFRS presentations, has been included for the purpose of improving the understanding of the operating results of the Trusts. FFO provides an operating performance measure that when compared period over period reflects the impact on operations of trends in occupancy levels, rental rates, property operating costs, acquisition activities and finance costs, that is not immediately apparent from net income determined in accordance with IFRS.

In April 2014, REALpac revised their definition of FFO to add an adjustment for property taxes accounted for under IFRIC 21 and an adjustment for incremental leasing costs of full-time or salaried staff.

Realty taxes accounted for under IFRIC 21:

As a result of the requirements of IFRIC 21 wherein the obligating event that gives rise to the property tax liability (where such property taxes meet the definition of a levy in IFRIC 21) does not occur over a period of time, an adjustment is made to FFO to reflect a pro-rata expense over the period of ownership.

Incremental leasing costs:

Leasing costs related to full-time or salaried staff, and related internal costs, that can be directly attributed to signed leases and that would otherwise be capitalized if incurred from external sources are added back to profit or loss in determining FFO. The purpose of this adjustment is to achieve consistency between entities that use internal leasing personnel and those that use external leasing personnel.

FUNDS FROM OPERATIONS

(in thousands of Canadian dollars except per unit amounts)	Three months ended December 31		Year ended December 31	
	2014	2013	2014	2013
Property operating income	\$208,261	\$212,308	\$803,276	\$749,922
Finance income	223	257	901	2,108
Finance cost - operations (excluding exchangeable unit distributions)	(73,622)	(77,932)	(300,793)	(295,662)
Trust expenses (excluding the fair value adjustment to unit-based compensation)	(3,114)	(3,880)	(11,519)	(12,716)
Current income taxes expense	(436)	(19)	(920)	(471)
FFO from equity accounted investments (page 19)	12,437	11,084	45,964	29,183
Realty taxes accounted for under IFRIC 21	(6,948)	(7,708)	-	-
Incremental leasing costs	1,658	-	6,042	-
FFO	\$138,459	\$134,110	\$542,951	\$472,364
Weighted average number of Stapled Units (in thousands of Stapled Units adjusted for conversion of exchangeable Stapled Units) ⁽¹⁾	290,378	286,281	288,871	259,458
Diluted weighted average number of Stapled Units (in thousands of Stapled Units) for the calculation of FFO ⁽¹⁾⁽²⁾⁽³⁾⁽⁴⁾⁽⁵⁾	300,865	296,734	299,464	274,231
FFO per Stapled Unit (basic – adjusted for conversion of exchangeable units)	\$0.48	\$0.47	\$1.88	\$1.82
FFO per Stapled Unit (diluted)	\$0.47	\$0.46	\$1.86	\$1.78
Distributions per Stapled Unit	\$0.34	\$0.34	\$1.35	\$1.35
Payout ratio per Stapled Unit as a % of FFO	70.8%	72.3%	71.8%	74.2%

(1) For the three months ended December 31, 2014 and 2013, included in the weighted average and diluted weighted average number of Stapled Units are exchangeable units of 16,230,642 and 16,972,391, respectively. For the year ended December 31, 2014 and 2013, included in the weighted average and diluted weighted average number of Stapled Units are exchangeable units of 16,698,530 and 11,740,609, respectively.

(2) For the three months ended December 31, 2014 and 2013, 319,596 Stapled Units and 285,166 Stapled Units, respectively, are included in the determination of diluted FFO with respect to the REIT's Unit Option Plan and Incentive Unit Plan. For the year ended December 31, 2014 and 2013, 425,505 Stapled Units and 358,536 Stapled Units, respectively, are included in the determination of diluted FFO with respect to the REIT's Unit Option Plan and Incentive Unit Plan.

(3) The 2016, 2018 and 2020 convertible debentures are dilutive for the three months and year ended December 31, 2014. Therefore, debenture interest of \$3.3 million and \$13.3 million, respectively, is added to FFO and 10,167,335 Stapled Units and 10,167,523 Stapled Units, respectively, are included in the diluted weighted average number of Stapled Units outstanding for these periods.

(4) 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 dilutive weighted average number of Stapled Units outstanding for this period.

(5) The 2014^o, 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 14,414,012 Stapled Units are included in the dilutive 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:

(in thousands of Canadian dollars)	Three months ended December 31			Year ended December 31		
	2014	2013	Change	2014	2013	Change
Additional capital expenditure recoveries net of capital expenditures (including amounts relating to the Trusts' interests of real estate assets included in equity accounted investments)	\$2,772	\$1,418	\$1,354	\$11,308	\$8,647	\$2,661
Adjustment to straight-lining of contractual rent	-	-	-	-	(3,356)	3,356
Sundry income ⁽¹⁾	(193)	1,079	(1,272)	2,096	3,944	(1,848)
	\$2,579	\$2,497	\$82	\$13,404	\$9,235	\$4,169

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

Excluding the above items, FFO would have been \$135.9 million for the three months ended December 31, 2014 (Q4 2013 - \$131.6 million) and \$0.47 per basic Stapled Unit (Q4 2013 - \$0.46 per basic Stapled Unit). For the year ended December 31, 2014, FFO would have been \$529.5 million (December 31, 2013 - \$463.1 million) and \$1.83 per basic Stapled Unit (December 31, 2013 - \$1.78 per basic Stapled Unit).

ADJUSTED FUNDS FROM OPERATIONS

In calculating AFFO, the Trusts adjust FFO for costs incurred relating to leasing and capital expenditures, straight-line rent in excess of contractual rent paid by tenants and non-cash expenses such as amortization. Capital expenditures excluded and not deducted in the calculation of AFFO relate to capital expenditures which generate a new investment stream, such as the construction of a new retail pad during property expansion or intensification, development activities or acquisition activities. AFFO is a supplemental measure that is used in the real estate industry to assess the sustainability of cash distributions.

AFFO is a financial measure not defined under IFRS. AFFO should not be considered as an alternative to net income, cash provided by operations or any other IFRS measure. There is no common industry definition or methodology for the calculation of AFFO. Furthermore, some entities present AFFO as a modified earnings measure and not as a cash measure as presented herein.

(in thousands of Canadian dollars except per unit amounts)	Three months ended December 31		Year ended December 31	
	2014	2013	2014	2013
FFO	\$138,459	\$134,110	\$542,951	\$472,364
Add (deduct):				
Straight-lining of contractual rent	(3,432)	(4,224)	(16,177)	(32,830)
Rent amortization of tenant inducements	434	440	1,725	1,795
Effective interest rate accretion	(918)	(1,161)	(4,304)	(4,176)
Unit-based compensation	629	770	4,277	2,601
Capital expenditures	(10,410)	(11,367)	(38,206)	(33,704)
Tenant expenditures	(9,064)	(6,252)	(32,941)	(18,799)
Incremental leasing costs	(1,658)	-	(6,042)	-
Trusts' interests of AFFO adjustments from equity accounted investments (page 19)	(529)	(2,669)	(6,207)	(5,610)
AFFO	\$113,511	\$109,647	\$445,076	\$381,641
Weighted average number of Stapled Units (in thousands of Stapled Units adjusted for conversion of exchangeable Stapled Units) ⁽¹⁾	290,378	286,281	288,871	259,458
Diluted weighted average number of Stapled Units (in thousands of Stapled Units) for the calculation of AFFO ⁽¹⁾⁽²⁾⁽³⁾⁽⁴⁾⁽⁵⁾	300,865	296,734	299,464	274,231
AFFO per Stapled Unit (basic - adjusted for conversion of exchangeable units)	\$0.39	\$0.38	\$1.54	\$1.47
AFFO per Stapled Unit (diluted)	\$0.39	\$0.38	\$1.53	\$1.45

⁽¹⁾ For the three months ended December 31, 2014 and 2013, included in the weighted average and diluted weighted average number of Stapled Units are exchangeable units of 16,230,642 and 16,972,391, respectively. For the year ended December 31, 2014 and 2013, included in the weighted average and diluted weighted average number of Stapled Units are exchangeable units of 16,698,530 and 11,740,609, respectively.

⁽²⁾ For the three months ended December 31, 2014 and 2013, 319,596 Stapled Units and 285,166 Stapled Units, respectively, are included in the determination of diluted AFFO with respect to the REIT's Unit Option Plan and Incentive Unit Plan. For the year ended December 31, 2014 and 2013, 425,505 Stapled Units and 358,536 Stapled Units, respectively, are included in the determination of diluted AFFO with respect to the REIT's Unit Option Plan and Incentive Unit Plan.

⁽³⁾ The 2016, 2018 and 2020 convertible debentures are dilutive for the three months and year ended December 31, 2014. Therefore, debenture interest of \$3.3 million and \$13.3 million, respectively, is added to AFFO and 10,167,335 Stapled Units and 10,167,523 Stapled Units, respectively, are included in the diluted weighted average number of Stapled Units outstanding for these periods.

⁽⁴⁾ 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 dilutive weighted average number of Stapled Units outstanding for this period.

⁽⁵⁾ The 2014^o, 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 14,414,012 Stapled Units are included in the dilutive weighted average number of Stapled Units outstanding for this period.

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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		
	2014	2013	Change	2014	2013	Change
Additional capital expenditure recoveries net of capital expenditures ⁽¹⁾	\$2,772	\$1,418	\$1,354	\$11,308	\$8,647	\$2,661
Sundry income ⁽²⁾	(193)	1,079	(1,272)	2,096	3,944	(1,848)
Capital expenditures ⁽¹⁾	(10,380)	(13,467)	3,087	(41,667)	(38,153)	(3,514)
Tenant expenditures ⁽¹⁾	(9,337)	(6,787)	(2,550)	(34,631)	(19,659)	(14,972)
	(\$17,138)	(\$17,757)	\$619	(\$62,894)	(\$45,221)	(\$17,673)

(1) Includes amounts relating to the Trusts' 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 \$130.6 million for the three months ended December 31, 2014 (Q4 2013 - \$127.4 million) and \$0.45 per basic Stapled Unit (Q4 2013 - \$0.45 per basic Stapled Unit). For the year ended December 31, 2014, AFFO would have been \$508.0 million (December 31, 2013 - \$426.9 million) and \$1.76 per basic Stapled Unit (December 31, 2013 - \$1.65 per basic Stapled Unit).

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	
	2014	2013	2014	2013
AFFO	\$113,511	\$109,647	\$445,076	\$381,641
Straight-lining of contractual rent	3,432	4,224	16,177	32,830
Net income from equity accounted investments	(12,222)	(19,163)	(44,123)	(34,032)
Finance cost - operations	79,247	83,807	323,955	309,629
Effective interest rate accretion	918	1,161	4,304	4,176
Exchangeable unit distributions	(5,625)	(5,875)	(23,162)	(13,967)
Transaction costs	-	-	-	(9,974)
Additions to capital expenditures and tenant expenditures	19,474	17,619	71,147	52,503
Adjustments for the Trusts' interests in equity accounted investments (page 19)	314	10,748	4,366	10,459
Change in other non-cash operating items	(716)	853	(31,822)	(115,874)
Cash provided by operations	\$198,333	\$203,021	\$765,918	\$617,391

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, 2014	Year ended December 31, 2014	Year ended December 31, 2013	Year ended December 31, 2012
Adjusted cash provided by operations ⁽¹⁾	\$115,902	\$461,509	\$322,503	\$241,254
Net income	137,708	424,655	323,635	508,860
Total distributions ⁽²⁾	92,379	366,802	331,040	215,479
Excess (shortfall) of adjusted cash provided by operations over total distributions	23,523	94,707	(8,537)	25,775
Excess (shortfall) of net income over total distributions	45,329	57,853	(7,405)	293,381

(1) Adjusted cash provided by operations is a non-GAAP measure which deducts interest paid from cash provided by operations.

(2) Total Distributions include cash distributions to unitholders and unit distributions issued under the DRIP.

Total distributions include unit distributions issued under the DRIP of \$22,483 and \$85,358 respectively, for the three months and year ended December 31, 2014. Total distributions include unit distributions issued under the DRIP of \$74,260 and \$57,056, respectively, for the years ended December 31, 2013 and 2012 which are non-cash distributions. Distributions exceeded adjusted cash provided by operations for the year ended December 31, 2013, which did not represent an economic return of capital but rather was primarily due to unit distributions issued under the DRIP. Unit distributions issued under the DRIP result in an increase in the number of Stapled Units outstanding which may result in increased cash distributions in the future assuming a stable cash component of distributions per unit. Distributions exceeded net income for the year ended December 31, 2013 which is primarily due to non-cash items. Non-cash items relating to the fair value of exchangeable units, fair value adjustments on real estate assets, gain (loss) on change in fair value, amortization, unrealized gain (loss) on foreign exchange and deferred income tax recoveries 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, 2014, 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. The maximum lending value as of December 31, 2014 is \$243.7 million. As at December 31, 2014, approximately \$173.3 million was available under this facility. The REIT, through Primaris, also has a second general operating facility of \$200.0 million with another Canadian chartered bank. This facility expires December 12, 2016 and is secured by certain investment properties. As at December 31, 2014, \$161.8 million was available under this facility. A third general operating facility of \$14.9 million, which is secured by certain investment properties, is due September 30, 2015. As at December 31, 2014, nil was available under this facility.

As at December 31, 2014, excluding the Trusts' interests of real estate assets included in equity accounted investments, the REIT had 78 unencumbered properties, with a fair value of approximately \$1.7 billion. Also, due to the REIT's 18-year history and management's conservative strategy of securing long-term financing on individual properties, the REIT had numerous other properties with very low loan to value ratios. As at December 31, 2014, the REIT had 42 properties valued at approximately \$1.6 billion which are encumbered with mortgages totaling \$364.5 million. In this pool of assets, the average loan to value is 22.3% the maximum loan to value is 29.9% and the minimum loan to value is 7.8%.

The following is a summary of material contractual obligations of the REIT including payments due as at December 31, 2014 for the next five years and thereafter:

Contractual Obligations ⁽¹⁾ (in thousands of Canadian dollars)	Payments Due by Period				Total
	2015	2016- 2017	2018- 2019	2020 and thereafter	
Mortgages payable ⁽²⁾	\$399,544	\$1,055,368	\$750,988	\$2,625,312	\$4,831,212
Convertible Debentures	-	75,000	74,399	99,654	249,053
Senior Debentures	350,000 ⁽⁴⁾	355,000	400,000	175,000	1,280,000
Bank indebtedness	14,850	109,013	-	-	123,863
Loan Payable ⁽³⁾⁽⁵⁾	222,210	-	-	-	222,210
Property acquisitions	60,668	-	-	-	60,668
Total contractual obligations	\$1,047,272	\$1,594,381	\$1,225,387	\$2,899,966	\$6,767,006

(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) The loan payable balance per the Trusts' Financial Statements as at December 31, 2014 was \$147.6 million which is payable to ECHO. 33.6% of the balance above has been eliminated upon consolidation of the Trusts' Financial Statements as the REIT has a 33.6% interest in ECHO, however there is a contractual obligation for the full amount.

(4) In February 2015, the REIT repaid all of the outstanding Series A Senior Debentures upon maturity for a total cash payment of \$115.0 million.

(5) In February 2015, the REIT repaid the first of two installments of the loan payable to ECHO for a total cash payment of approximately U.S. \$95.8 million.

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 (high) with a Stable trend as at December 31, 2014. A credit rating of BBB (high) by DBRS is generally an indication of adequate credit quality, where the capacity for payment of financial obligations is considered acceptable, however the entity may be vulnerable to future events. 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, 2014, through the combined amount available under its general operating facilities of \$335.1 million and its unencumbered property pool of approximately \$1.7 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 Trusts' Interests of mortgages relating to equity accounted investments and mortgages classified as held for sale:

Year	Number of Properties	Mortgage Debt due on Maturity (\$000's) ⁽¹⁾	Weighted Average Interest Rate on Maturity	Fair Value of Investment Properties (\$000's) ⁽¹⁾	Loan to Value
2015	17	\$230,912	5.3%	\$601,103	38%
2016	46	312,401	5.4%	650,300	48%
2017	21	402,586	4.7%	885,697	45%
2018	36	120,259	5.4%	517,300	23%
2019	22	314,510	3.5%	820,256	38%
	142	\$1,380,668	4.7%	\$3,474,656	40%

(1) Converting U.S. dollars to Canadian dollars at an exchange rate of \$1.16 as at December 31, 2014.

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, 2014, such guarantees amounted to \$229.0 million expiring in 2022 (December 31, 2013 - \$69.8 million, expiring in 2016), and no amount has been provided for in the Trusts' Financial Statements 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, 2014, the estimated amount of debt subject to such guarantees, and therefore the maximum exposure to credit risk is approximately \$152.2 million, expiring between 2016 and 2020 (December 31, 2013 - \$224.4 million, expiring between 2014 and 2020). 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 Trusts' Financial Statements.

Related Party Transactions

Prior to July 1, 2013, HRRPM, 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 pursuant to a property management agreement. HRRPM 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.

Effective July 1, 2013, the REIT executed an agreement with HRRPM to internalize the property management function. Upon closing of the transaction, HRRMSLP acquired HRRPM's REIT-related property management business in return for 9.5 million partnership units of HRRMSLP, such units to be exchangeable on a one-for-one basis for Stapled Units. In June 2014, the unitholders of the REIT approved the granting of voting rights to these 9.5 million partnership 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. No transaction costs were expensed during the three months and year ended December 31, 2014.

Effective July 1, 2013, the REIT entered into an agreement with HRRPM for HRRPM to provide specified services including the cost sharing of premises, certain personnel, 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 three months ended December 31, 2014, the REIT incurred costs of \$0.4 million (December 31, 2013 - \$0.6 million) under this agreement. During the year ended December 31, 2014, the REIT incurred costs of \$1.5 million (December 31, 2013 - \$0.8 million) under this agreement.

During the three months ended December 31, 2014 and December 31, 2013, the REIT recorded nil expenses pursuant to the property management agreement as this function has been internalized.

During the year ended December 31, 2013, the REIT recorded expenses pursuant to the property management agreement of \$8.2 million, of which \$0.6 million was capitalized to the cost of the investment properties acquired, nil was capitalized to properties under development and \$2.0 million was included in leasing expenses. These amounts include amounts relating to equity accounted investments. The REIT also reimbursed HRRPM for certain direct property operating costs and tenant construction costs. No amounts were incurred during the year ended December 31, 2014 as this function has been internalized.

During the year ended December 31, 2013, a further amount of \$2.3 million was earned by HRPM pursuant to the property management agreement, in accordance with the annual incentive fee payable to HRPM. Of this amount, \$1.1 million was waived by HRPM and \$1.1 million was expensed in the combined statement of comprehensive income. No amounts were incurred during the year ended December 31, 2014 as this function has been internalized.

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, 2014 is \$0.4 million (December 31, 2013 - \$0.3 million) and for the year ended December 31, 2014 is \$1.5 million (December 31, 2013 - \$1.4 million).

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

The REIT has interests in various investment properties through joint arrangements and investments in associates. Generally, the REIT provides asset and property management services to co-owners, partners, and third parties for which it earns market-based fees. Transactions subsequent to the formation of a co-ownership that are not contemplated by the co-ownership agreements are considered to be related party transactions for financial statement purposes.

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.

SECTION IV

CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

Preparation of the Trusts' Financial Statements 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 and 2 of the Trusts' Financial Statements.

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
- Deferred tax asset (liability).

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 or a group of properties, 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 Trusts' 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 Trusts' Financial Statements for further information on estimates and assumptions made in the determination of the fair value of real estate assets. Judgement is applied in determining whether certain costs are additions to the carrying value of the real estate assets, identifying the point at which practical completion of the property occurs and identifying the directly attributable borrowing costs to be included in the carrying value of the development properties.

- Leases

The REIT's policy for property rental revenue recognition is described in note 2(g) of the Trusts' Financial Statements. 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, 2014 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.

- 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.

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 Trusts' CEO and CFO have each concluded that such disclosure controls and procedures were appropriately designed and were operating effectively. The Trusts' Financial Statements and this MD&A were reviewed and approved by the REIT's Audit Committee and the Board of Trustees prior to this publication.

Management of each Trust has reviewed its internal control over financial reporting on an annual basis. The Trusts' management, under the supervision of the CFO, has evaluated the effectiveness of internal control over financial reporting using the framework and criteria established in Internal Control – Integrated Framework, issued by the Committee of Sponsoring Organizations of the Treadway Commission in May 2013 (2013 COSO Framework). Based on this evaluation, management has concluded that internal control over financial reporting was effective and in accordance with the criteria established in the 2013 COSO Framework as of December 31, 2014. No changes were made to the design of either Trust's internal control over financial reporting during the three month period ended December 31, 2014 that have materially affected, or are reasonably likely to materially affect, the Trusts' internal control over financial reporting.

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 their 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 including detailed descriptions 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, however, they remain liable to pay all remaining rent in accordance with their leases. 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 in the event that borrowers default on the repayment of the amounts owing to the REIT. Management mitigates this risk by ensuring adequate security has been provided in support of mortgages receivable.

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, may lead to the Trusts' debt being refinanced at higher rates, thereby reducing net income and cash flows which could ultimately affect the level of distributions. 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 36.9% 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 investments in associates. 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. 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 2014. 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.

The Tax Act includes rules affecting certain publicly traded stapled securities of SIFTs, REITs and corporations which can result in the denial of a deduction for certain payments made by another entity to a REIT, or to a subsidiary of a REIT (the "Stapled Security Rules"). 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.

Pursuant to rules in the Tax Act, if the REIT or Finance Trust experiences a "loss restriction event" (i) it will be deemed to have a year-end for tax purposes (which would result in an unscheduled distribution of undistributed net income and net realized capital gains, if any, at such time to Unitholders to the extent necessary so that such trust is not liable for income tax on such amounts under Part I of the Tax Act), and (ii) it will become subject to the loss restriction rules generally applicable to a corporation that experiences an acquisition of control, including a deemed realization of any unrealized capital losses and restrictions on its ability to carry forward losses. Generally, the REIT or Finance Trust will be subject to a loss restriction event if a person becomes a "majority-interest beneficiary", or a group of persons becomes a "majority-interest group of beneficiaries", of such trust, each as defined in the affiliated persons rules contained in the Tax Act, with certain modifications. Generally, a majority-interest beneficiary of a trust is a beneficiary of the trust whose beneficial interests in the income or capital of the trust, as the case may be, together with the beneficial interests in the income or capital of the trust, as the case may be, of persons and partnerships with whom such beneficiary is affiliated for the purposes of the Tax Act, represent greater than 50% of the fair market value of all the interests in the income or capital of the trust, as the case may be.

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, 2014, Finance Trust holds U.S. \$220.5 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

The REIT is classified as a foreign corporation for United States federal income tax purposes. 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. Unitholder with respect to such U.S. Unitholder's REIT Units, any distributions in respect of the REIT Units which are treated as "excess distribution" under the applicable rules 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 were 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.

The foregoing adverse consequences of PFIC characterization can be mitigated by making certain elections. U.S. Unitholders 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. If the REIT were a PFIC, U.S. Unitholders would be required to file an annual return on IRS Form 8621.

U.S. individuals are required to report an interest in any "specified foreign financial asset" if the aggregate value of such assets owned by the U.S. individual exceeds \$50,000 (or such higher threshold as may apply to a particular taxpayer pursuant to the instructions to IRS Form 8938). The REIT Units are treated as a specified foreign financial asset for this purpose.

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 39.6%. 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.

U.S. Unitholders are required to file an information return on IRS Form 3520 to report their interest in the Finance Trust and to include a copy of their Form 3520-A Foreign Grantor Trust Owner Statement, which is being provided by Finance Trust to its registered U.S. Unitholders. If you have not received a Foreign Grantor Trust Owner Statement, pro forma information to prepare a Form 3520-A Foreign Grantor Trust Owner Statement will be available on our website. You should consult with your own tax advisor regarding the requirements of filing information returns.

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. Unitholder 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 of Finance Trust Units, there is uncertainty as to the appropriate rate of withholding under the U.S. Treaty and in light of this uncertainty, management of Finance Trust currently applies the 25% withholding rate under the Tax Act to income paid or credited to U.S. residents. U.S. Unitholders may be entitled to a refund of a portion of such withholding tax if the rate applied by Finance Trust were determined to be excessive. You should consult with your own tax advisor regarding the advisability of applying for such a refund.

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 provide 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 12, 2015, there were 274,949,324 Stapled Units issued and outstanding (each comprised of a REIT unit and a Finance Trust unit).

As at December 31, 2014, the maximum number of units authorized to be granted under the REIT's Unit Option Plan was 28,000,000. Of this amount, 12,428,066 had been granted, 7,132,499 had been exercised and expired and 5,295,567 options to purchase Stapled Units were outstanding. As at February 12, 2015, there were 6,923,930 options to purchase Stapled Units outstanding of which 3,314,415 are fully vested.

As at December 31, 2014, the maximum number of units authorized to be granted under the REIT's Incentive Unit Plan was 5,000,000. Of this amount, 162,332 Stapled Units have been granted. As at February 12, 2015, 297,686 Stapled Units have been granted.

The following table lists the principal outstanding balance of the REIT's convertible debentures as at February 12, 2015 and the number of Stapled Units required to convert the convertible debentures to equity:

Convertible Debentures	Principal outstanding as at February 12, 2015	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	3,008,451
2020 Convertible Debentures (HR.DB.D)	99.7 million	4,240,595

SUBSEQUENT EVENTS

- (a) In January 2015, the REIT sold an industrial property in Ontario, which was classified as held for sale as at December 31, 2014, for gross proceeds of approximately \$70.2 million and repaid the mortgage payable of approximately \$42.6 million bearing interest at 5.2% per annum.
- (b) In February 2015, the REIT issued, by way of private placement, U.S. \$125.0 million Series J senior floating rate unsecured debentures maturing on February 9, 2018.
- (c) In February 2015, the REIT acquired a residential property in Dallas, TX for a purchase price of approximately U.S. \$52.3 million.

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.

Combined Financial Statements of

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

Years ended December 31, 2014 and 2013



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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, 2014 and 2013, 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, 2014 and 2013, and their combined financial performance and their combined cash flows for the years then ended in accordance with International Financial Reporting Standards.

Chartered Professional Accountants, Licensed Public Accountants

February 17, 2015
Toronto, Canada

H&R REAL ESTATE INVESTMENT TRUST

H&R FINANCE TRUST

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

	December 31 2014	December 31 2013
Assets		
Real estate assets		
Investment properties (note 4)	\$ 12,116,983	\$ 12,786,205
Properties under development (notes 4 and 5)	105,006	146,478
	12,221,989	12,932,683
Equity accounted investments (note 7)	703,019	558,149
Mortgages receivable (note 8)	79,922	9,687
Assets classified as held for sale (note 9)	296,992	-
Other assets (note 10)	42,703	54,624
Cash and cash equivalents (note 11)	23,755	27,884
	\$ 13,368,380	\$ 13,583,027
Liabilities and Unitholders' Equity		
Liabilities		
Mortgages payable (note 12)	\$ 4,318,136	\$ 4,897,726
Debentures payable (note 13)	1,535,838	1,532,130
Exchangeable units (note 14)	362,105	372,427
Deferred tax liability (note 29)	129,864	76,554
Unit-based compensation payable (note 16(a)(ii))	9,035	6,313
Derivative instruments (note 17)	146	508
Liabilities classified as held for sale (note 9)	66,179	-
Loan payable (note 15)	147,608	134,713
Bank indebtedness (note 18)	123,863	116,762
Accounts payable and accrued liabilities (note 19)	147,938	172,093
	6,840,712	7,309,226
Unitholders' equity	6,527,668	6,273,801
Commitments and contingencies (note 30)		
Subsequent events (notes 13, 15, 16 and 31)		
	\$ 13,368,380	\$ 13,583,027

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, 2014 and 2013

	2014	2013 (note 3)
Property operating income:		
Rentals from investment properties (note 21)	\$ 1,227,803	\$ 1,137,017
Property operating costs	(424,527)	(387,095)
	803,276	749,922
Net income from equity accounted investments (note 7)	44,123	34,032
Finance costs:		
Finance income	901	2,108
Finance cost - operations (note 22)	(323,955)	(309,629)
Gain (loss) on change in fair value (note 23)	(8,029)	30,972
	(331,083)	(276,549)
Trust expenses	(11,091)	(5,979)
Fair value adjustment on real estate assets (note 4)	(42,523)	44,751
Loss on sale of real estate assets (note 4)	(16,025)	(2,067)
Gain on foreign exchange	22,602	14,042
Transaction costs (notes 6 and 27)	-	(204,819)
Net income before income taxes	469,279	353,333
Income tax expense (note 29)	(44,624)	(29,698)
Net income	424,655	323,635
Other comprehensive income (note 20):		
Unrealized gain on translation of U.S. denominated foreign operations	90,140	53,048
Transfer of realized loss on cash flow hedges to net income	395	414
	90,535	53,462
Total comprehensive income all attributable to unitholders	\$ 515,190	\$ 377,097

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, 2014 and 2013

UNITHOLDERS' EQUITY	Value of Units	Accumulated net income	Accumulated distributions	Accumulated other comprehensive income (loss) (note 20)	Total
Unitholders' equity, January 1, 2013	\$ 3,307,546	\$ 3,075,091	\$ (1,850,754)	\$ (24,871)	\$ 4,507,012
Proceeds from issuance of units	1,514,002	-	-	-	1,514,002
Issue costs	(507)	-	-	-	(507)
Net income	-	323,635	-	-	323,635
Distributions to unitholders (note 16(b))	-	-	(331,040)	-	(331,040)
Conversion of convertible debentures, net	207,237	-	-	-	207,237
Other comprehensive income	-	-	-	53,462	53,462
Unitholders' equity, December 31, 2013	5,028,278	3,398,726	(2,181,794)	28,591	6,273,801
Proceeds from issuance of units	106,943	-	-	-	106,943
Issue costs	(28)	-	-	-	(28)
Net income	-	424,655	-	-	424,655
Distributions to unitholders (note 16(b))	-	-	(366,802)	-	(366,802)
Conversion of convertible debentures, net	16	-	-	-	16
Units repurchased and cancelled (note 16(e))	(1,452)	-	-	-	(1,452)
Other comprehensive income	-	-	-	90,535	90,535
Unitholders' equity, December 31, 2014	\$ 5,133,757	\$ 3,823,381	\$ (2,548,596)	\$ 119,126	\$ 6,527,668

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, 2014 and 2013

	2014	2013 (note 3)
Cash provided by (used in):		
Operations:		
Net income	\$ 424,655	\$ 323,635
Items not affecting cash:		
Net income from equity accounted investments (note 7)	(44,123)	(34,032)
Finance cost - operations (note 22)	323,955	309,629
Rent amortization of tenant inducements (note 21)	1,725	1,795
Gain on foreign exchange	(22,602)	(14,042)
Fair value adjustment on real estate assets (note 4)	42,523	(44,751)
Loss on sale of real estate assets	16,025	2,067
Finance cost - (gain) loss on change in fair value (note 23)	8,029	(30,972)
Transaction costs (note 27)	-	194,845
Unit-based compensation (note 16(a)(ii))	3,849	(4,136)
Deferred tax liability (note 29)	43,704	29,227
Change in other non-cash operating items (note 24)	(31,822)	(115,874)
	765,918	617,391
Investing:		
Properties under development (notes 4 and 24)	(49,548)	(22,631)
Investment properties:		
Net proceeds on disposition of real estate assets	535,123	115,286
Acquisitions (notes 4 and 24)	(151,942)	(207,400)
Redevelopment (notes 4 and 24)	(56,606)	(76,617)
Capital expenditures (note 4)	(38,206)	(33,704)
Leasing expenses and tenant inducements (note 4)	(32,941)	(18,799)
Equity accounted investments, net	(75,906)	(112,875)
Mortgages receivable	(254)	9,500
Cash assumed on business combination (note 6)	-	45,108
Restricted cash (note 10)	1,939	30,513
	131,659	(271,619)
Financing:		
Bank indebtedness	7,101	(11,143)
Interest paid	(304,409)	(294,888)
Mortgages payable:		
New mortgages payable	141,580	301,877
Principal repayments	(443,169)	(636,114)
Proceeds from issuance of debentures payable (note 13(b))	-	467,301
Redemption of debentures payable (note 13(c))	-	(5,601)
Proceeds from issuance of units, net of issue costs	3,249	(33)
Units repurchased and cancelled (note 16(e))	(1,452)	-
Finance cost - exchangeable unit distributions (note 22)	(23,162)	(13,967)
Distributions to unitholders (note 16(b))	(281,444)	(256,780)
	(901,706)	(449,348)
Decrease in cash and cash equivalents	(4,129)	(103,576)
Cash and cash equivalents, beginning of year (note 11)	27,884	131,460
Cash and cash equivalents, end of year (note 11)	\$ 23,755	\$ 27,884

See notes on business combination (note 6) and supplemental cash flow information (note 24).

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, 2014 and 2013

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, for the following reasons:

- 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 17, 2015.

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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, except where otherwise stated, which is the Trusts' functional currency. All financial information 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 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 (note 4);
- Fair value of financial instruments;
- Fair value of cash-settled unit-based compensation (note 16(a));
- Fair value of convertible debentures; and
- Deferred tax asset (liability) (note 29).

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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 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 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, or group of properties, 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. Judgement is applied in determining whether certain costs are additions to the carrying value of the real estate assets, identifying the point at which practical completion of the property occurs and identifying the directly attributable borrowing costs to be included in the carrying value of the development properties.

- 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, the REIT would be subject to tax on its taxable income distributed to unitholders.

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1. Basis of preparation (continued):

- 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.

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 under IFRS 3, as set out in note 1(d)(ii). The REIT expenses transaction costs on business combinations and capitalizes transaction costs on asset acquisitions.

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2. Significant accounting policies (continued):

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 capitalized 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. Leasing costs, such as commissions incurred in negotiating tenant leases, are capitalized to investment properties.

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.

(e) *Assets and liabilities held for sale:*

Non-current assets 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.

Non-current liabilities that are to be assumed by the buyer on disposition of the non-current asset, are also classified as held for sale. Non-current assets and non-current liabilities held for sale must be classified separately from other assets and other liabilities in the statement of financial position. These amounts cannot be offset or presented as a single amount.

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2. Significant accounting policies (continued):

(f) *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.

(g) *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.

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.

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 2014 and the 2013 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.

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2. Significant accounting policies (continued):

(h) *Unit-based compensation:*

The REIT has a unit option plan and incentive unit plan available for REIT trustees, officers, employees and consultants as disclosed in note 16(a). These plans are 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 and incentive unit 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.

(i) *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.

(j) *Restricted cash:*

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

(k) *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.

(l) *Financial instruments:*

(i) Non-derivative financial assets

Cash and cash equivalents, restricted cash, accounts receivable and mortgages 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.

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2. Significant accounting policies (continued):

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.

(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 and exchangeable units were designated at fair value through net income upon initial recognition. Any gains or losses arising on remeasurement are recognized in net income.

(m) *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.

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2. Significant accounting policies (continued):

(n) *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 and net gain (loss) on derivative instruments.

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

(o) *Investment in associates and joint ventures:*

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.

The Trusts consider investments in joint arrangements to be joint ventures when they jointly control 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.

The Trusts' interest in its associates and joint ventures are accounted for using the equity method and are carried on the combined statements of financial position at cost, adjusted for the Trusts' proportionate share of post-acquisition changes in the net assets, less any identified impairment loss. The Trusts' share of profits and losses is recognized in the share of net income from the associate or joint venture investments in the combined statements of comprehensive income and the Trusts' other comprehensive income includes their share of the associate or joint ventures' other comprehensive income.

An associate or 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.

(p) *Joint Operations:*

The Trusts consider investments in joint arrangements to be joint operations when they make operating, financial and strategic decisions over one or more investment properties jointly 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.

(q) *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.

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2. Significant accounting policies (continued):

(r) *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.

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.

(s) *Levies:*

Effective January 1, 2014, the REIT has adopted IFRS Interpretations Committee, 21, *Levies* ("IFRIC 21"). IFRIC 21 provides guidance on accounting for levies in accordance with the requirements of IAS 37, *Provisions, Contingent Liabilities and Contingent Assets*. For the purposes of IFRIC 21, realty taxes payable by the REIT are considered levies. The adoption of IFRIC 21 requires the REIT to recognize the full amount of annual U.S. realty tax liabilities at the point in time when the realty tax obligation is imposed.

The REIT previously accrued for U.S. property taxes evenly over the year. In accordance with IFRIC 21, the REIT has determined that the liability to pay the U.S. realty taxes should be recognized in full at a single point in time, when the obligating event as stated in the legislation occurs. The impact was to recognize the annual U.S. realty tax accrual and corresponding U.S. expense in full in the three months ended March 31, 2014. The REIT has retrospectively applied the change in accounting policy.

There was no impact of the adoption of IFRIC 21 on the combined statements of financial position as at December 31, 2014, December 31, 2013 and January 1, 2013, combined statements of comprehensive income for the years ended December 31, 2014 and December 31, 2013 and combined statements of cash flow for the years ended December 31, 2014 and December 31, 2013.

(t) *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")*

In July 2014, the IASB issued IFRS 9 *Financial Instruments: Classification and Measurement* replacing IAS 39, *Financial Instruments: Recognition and Measurement*. The project had three main phases: classification and measurement, impairment, and general hedging. The standard becomes effective for annual periods beginning on or after January 1, 2018 and is to be applied retrospectively. Early adoption is permitted. The Trusts are currently assessing the impact of the new standard on the combined financial statements.

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2. Significant accounting policies (continued):

- (ii) On May 6, 2014, the IASB issued *Accounting for Acquisitions of Interests in Joint Operations (Amendments to IFRS 11)*. The amendments apply prospectively for annual periods beginning on or after January 1, 2016. The Trusts intend to adopt the amendments to IFRS 11 in the combined financial statements for the annual period beginning on January 1, 2016. The extent of the impact of adoption of the amendments has not yet been determined.
- (iii) On May 28, 2014, the IASB issued IFRS 15 *Revenue from Contracts with Customers*. The new standard is effective for annual periods beginning on or after January 1, 2017. IFRS 15 will replace IAS 11 *Construction Contracts*, IAS 18 *Revenue*, IFRIC 13 *Customer Loyalty Programmes*, IFRIC 15 *Agreements for the Construction of Real Estate*, IFRIC 18 *Transfer of Assets from Customers*, and SIC 31 *Revenue - Barter Transactions Involving Advertising Services*. The Trusts intend to adopt IFRS 15 in the combined financial statements for the annual period beginning on January 1, 2017. The extent of the impact of adoption of the standard has not yet been determined.
- (iv) On September 11, 2014, the IASB issued *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendments to IFRS 10 and IAS 28)*. The amendments apply prospectively for annual periods beginning on or after January 1, 2016. The Trusts intend to adopt these amendments in the combined financial statements for the annual period beginning on January 1, 2016. The extent of the impact of adoption of the amendment has not yet been determined.

3. Change in accounting policy:

In the fourth quarter of 2014, the REIT made a voluntary change in accounting policy related to leasing costs. Previously, such costs were deferred and amortized on a straight-line basis over the terms of the related leases. Following the change in accounting policy, they will no longer be amortized. There was no impact of the accounting policy change on the combined statements of financial position as of January 1, 2013 and December 31, 2013. The impact of the accounting policy change on the combined statements of comprehensive income for the year ended December 31, 2013 is to decrease amortization by \$7,536, decrease fair value adjustment on real estate assets by \$7,121 and increase trust expenses by \$415. Therefore, there has been no change to net income, other comprehensive income and cash provided by operations for the year ended December 31, 2013.

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4. Real estate assets:

	Investment Properties December 31 2014	Properties Under Development December 31 2014	Investment Properties December 31 2013	Properties Under Development December 31 2013
Opening balance, beginning of year	\$ 12,786,205	\$ 146,478	\$ 9,235,562	\$ 128,220
Acquisition of investment properties through business combination (note 6)	-	-	3,179,418	-
Acquisitions of investment properties, including transaction costs	151,942	-	211,360	-
Additions to existing investment properties:				
Capital expenditures	38,206	-	33,704	-
Direct leasing costs	32,941	-	18,799	-
Redevelopment	52,684	-	52,196	-
Additions to properties under development (including capitalized interest)	-	50,880	-	22,631
Dispositions	(947,162)	-	(183,433)	(4,373)
Transfer of investment properties to assets classified as held for sale (note 9)	(296,992)	-	-	-
Straight-line rents and blend and extend rents included in revenue	21,331	-	38,124	-
Transfer of property under development that has reached practical completion to investment properties	92,352	(92,352)	-	-
Change in foreign exchange	227,999	-	155,724	-
Fair value adjustment on real estate assets	(42,523)	-	44,751	-
Closing balance, end of year	\$ 12,116,983	\$ 105,006	\$ 12,786,205	\$ 146,478

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.

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4. Real estate assets (continued):

Asset acquisitions:

During the year ended December 31, 2014, the REIT acquired three investment properties, a 50% ownership interest in one investment property, one equity accounted investment and one parcel of land adjacent to an existing investment property (year ended December 31, 2013 - five investment properties, two equity accounted investments and a parcel of land adjacent to an existing investment property). 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 of the assets and liabilities as at the respective dates of acquisition:

	December 31 2014	December 31 2013
Assets		
Investment properties	\$ 151,890	\$ 210,355
Equity accounted investments:		
Investment in associate	71,065	306,177
Joint venture	-	16,729
Liabilities		
Loan payable (note 15)	-	(134,713)
Total identifiable net assets settled by cash	\$ 222,955	\$ 398,548

During the year ended December 31, 2014, the REIT incurred additional costs of \$52 (December 31, 2013 - \$1,005) in respect to prior year acquisitions which are not included in the above table.

Asset dispositions:

During the year ended December 31, 2014, the REIT sold a 50% ownership interest in 84 industrial properties, a 50% ownership interest in three retail properties and a 50% ownership interest in one office property. In addition, the REIT sold five industrial properties, five retail properties, one office property, a parcel of land and a portion of an office property (sold as separate condominium units) for proceeds of \$957,475, net of costs, related debt assumed by the purchaser and vendor take-back mortgages, the REIT received \$535,123 in cash and recognized a loss on sale of real estate assets of \$16,025. The loss on sale of real estate assets is primarily due to mark-to-market adjustments on the purchasers' assumption of mortgages on 23 properties of \$16,560 and one-time prepayment penalties of \$3,112 to discharge five mortgages. Excluding these costs, the properties sold during the year ended December 31, 2014 generated a gain of sale of \$3,647.

During the year ended December 31, 2013, the REIT sold a 50% ownership interest in one retail property. In addition, the REIT sold three industrial properties, one retail property, two office properties, a parcel of land and a portion of an office property (sold as separate condominium units) for proceeds of \$214,832, net of costs, related debt assumed by the purchaser and vendor take-back mortgages, the REIT received \$115,286 in cash and recognized a loss on sale of real estate assets of \$2,067 primarily due to selling costs.

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4. Real estate assets (continued):

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) On December 22, 2014, the REIT sold a 50% ownership interest in 85 properties that were not externally appraised. The 50% ownership interest retained by the REIT was valued at the selling price and make up 4.9% of the investment properties balance as at December 31, 2014;
- (iii) As at December 31, 2014, the REIT holds a 49.5% ownership interest in 16 industrial properties and a 50% ownership interest in one industrial property which has been classified as held for sale. The ownership interests that will be retained by the REIT was valued at the selling price, in accordance with the agreement of purchase and sale, and make up 1.9% of the investment properties balance as at December 31, 2014;
- (iv) 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;
- (v) The direct capitalization method which is based on the conversion of normalized earnings directly into an expression of fair value. The normalized net income for the year is divided by an overall capitalization rate; and
- (vi) The use of external independent appraisers. During the year ended December 31, 2014, certain properties were valued by professional external independent appraisers. These properties make up 24.8% of the investment properties balance as at December 31, 2014 (year ended December 31, 2013 - 27.7%). The remainder of the portfolio, after taking into account the 4.9% and 1.9% in (ii) and (iii) above, respectively, 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.

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.

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4. Real estate assets (continued):

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	Total	Canada	United States	Total
December 31, 2014	6.49%	7.42%	6.68%	5.91%	7.04%	6.14%
December 31, 2013	6.56%	7.54%	6.74%	5.98%	7.18%	6.20%

Weighted Average Overall Capitalization Rates	December 31, 2014			December 31, 2013		
	REIT	Primaris	Total	REIT	Primaris	Total
Canada	6.21%	5.53%	5.99%	6.33%	5.47%	6.06%
United States	6.69%	-	6.69%	6.69%	-	6.69%
Total	6.29%	5.53%	6.11%	6.42%	5.47%	6.18%

The weighted average capitalization rate as at December 31, 2014 is calculated based on property operating income for the three months ended December 31, 2014 (December 31, 2013 - based on the three months ended December 31, 2013). Property operating income is adjusted for: acquisitions, dispositions, straight-lining of contractual rent, rent amortization of tenant inducements, one-time non-recurring capital expenditure recoveries, Primaris seasonal revenues, other sundry income and IFRIC 21 - realty tax adjustment. There are no further adjustments to normalize property operating income to account for current vacancies.

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, 2014:

Capitalization Rate Sensitivity Increase (Decrease)	Weighted Average Overall Capitalization Rate	Fair Value of Investment Properties	Fair Value Variance	Ratio of Debt ⁽¹⁾ to Total Assets
(0.75)%	5.36%	\$ 13,812,456	\$ 1,695,473	41.1%
(0.50)%	5.61%	\$ 13,196,928	\$ 1,079,945	42.8%
(0.25)%	5.86%	\$ 12,633,919	\$ 516,936	44.5%
December 31, 2014	6.11%	\$ 12,116,983	\$ -	46.3%
0.25%	6.36%	\$ 11,640,686	\$ (476,297)	48.0%
0.50%	6.61%	\$ 11,200,418	\$ (916,565)	49.7%
0.75%	6.86%	\$ 10,792,240	\$ (1,324,743)	51.4%

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

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5. Properties under development:

Project	Address	December 31	December 31
		2014	2013
Heart Lake	Mayfield West Business Park, Caledon, ON	\$ 80,612	\$ 79,176
Airport Road	7900 Airport Road, Brampton, ON	24,394	67,302
		\$ 105,006	\$ 146,478

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 Primaris portfolio consisted of 26 properties. The total costs relating to the acquisition of Primaris were \$6,605. These costs were expensed as transaction costs in the period incurred. No transaction costs were expensed for the year ended December 31, 2014 (December 31, 2013 - \$6,605).

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 ⁽¹⁾	(94,661)
Mortgages payable	(1,415,575)
Bank indebtedness	(125,000)
Exchangeable units ⁽²⁾	(56,940)
Restricted cash	789
Fair value of consideration	\$ 1,438,939

	<u>Face Value</u>	<u>Fair Value</u>
(1) 2014 ^b 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)	<u>74,963</u>	<u>79,461</u>
	<u>\$83,909</u>	<u>\$94,661</u>

In May 2013, the REIT redeemed all of the remaining outstanding 2014^b 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 are exchangeable for 2,474,554 Stapled Units (note 14).

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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, 2014, the REIT acquired a net interest in one associate for \$71,065 (note 4). 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. The REIT's interests in equity accounted investments are outlined as follows:

Name	Location	Principal activity	Ownership interest (%)	
			December 31 2014	December 31 2013
Investments in joint ventures:				
100 Yonge	Toronto, Ontario	Own and operate investment property	33.3	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
Investments in associates:				
ECHO Realty LP ("ECHO")	United States	Own and operate investment properties	33.6	33.7
LIC Operator Co., L.P. ("LIC")	United States	Develop, own and operate investment property	50.0	-

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7. Equity accounted investments (continued):

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

December 31, 2014	Investments in joint ventures	Investments in associates	T total
Equity accounted investments:			
Investment properties	\$ 1,691,400	\$ 1,552,742	\$ 3,244,142
Properties under development	-	225,005	225,005
Loan receivable	64,300	222,210	286,510
Other assets	11,421	30,987	42,408
Cash and cash equivalents	16,450	23,013	39,463
Mortgages payable	(778,451)	(569,111)	(1,347,562)
Bank indebtedness	-	(163,017)	(163,017)
Accounts payable and accrued liabilities	(52,717)	(51,390)	(104,107)
Non-controlling interest	-	(27,075)	(27,075)
Net assets	952,403	1,243,364	2,195,767
REIT's share of net assets	355,216	454,554	809,770
Elimination of intercompany loan receivable	(32,150)	(74,601)	(106,751)
Amount in the combined statements of financial position	\$ 323,066	\$ 379,953	\$ 703,019

ECHO reports its financial position to the REIT one month in arrears due to time constraints on its reporting. Therefore, the above amounts include ECHO's financial information as at November 30, 2014. The REIT is not aware of ECHO being a party to any significant transactions that occurred during December 2014.

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

ECHO reports its financial position to the REIT one month in arrears due to time constraints on its reporting. Therefore, the above amounts include ECHO's financial information as at November 30, 2013. The REIT is not aware of ECHO being a party to any significant transactions that occurred during December 2013.

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7. Equity accounted investments (continued):

	Year ended December 31, 2014			Year ended December 31, 2013		
	Investments in joint ventures	Investments in associates	Total	Investments in joint ventures	Investment in associate	Total
Net income from equity accounted investments:						
Rentals from investment properties	\$ 174,335	\$ 122,064	\$ 296,399	\$ 161,171	\$ 37,695	\$ 198,866
Property operating costs	(82,688)	(24,929)	(107,617)	(72,701)	(7,970)	(80,671)
Net income (loss) from equity accounted investments	-	1,339	1,339	-	(593)	(593)
Finance income	2,798	6,767	9,565	2,812	2,558	5,370
Finance cost - operations	(27,890)	(28,835)	(56,725)	(27,874)	(8,652)	(36,526)
Trust expenses	-	(502)	(502)	-	398	398
Fair value adjustment on real estate assets	(7,732)	2,632	(5,100)	10,317	(2,890)	7,427
Gain on sale of real estate assets	-	1,736	1,736	-	-	-
Income taxes	-	(440)	(440)	(1)	(100)	(101)
Net income	58,823	79,832	138,655	73,724	20,446	94,170
Net (income) loss attributable to non-controlling interest	-	(2,510)	(2,510)	-	(563)	(563)
Net income attributable to shareholders	58,823	77,322	136,145	73,724	19,883	93,607
REIT's share of net income attributable to shareholders	21,586	26,015	47,601	30,297	5,919	36,216
Elimination of intercompany loan interest	(1,354)	(2,124)	(3,478)	(1,354)	(830)	(2,184)
Amount in the combined statements of comprehensive income	\$ 20,232	\$ 23,891	\$ 44,123	\$ 28,943	\$ 5,089	\$ 34,032

ECHO reports its financial results to the REIT one month in arrears due to time constraints on its reporting. Therefore, the above amounts include ECHO's financial information for December 1, 2013 to November 30, 2014 and August 1, 2013 (date of acquisition) to November 30, 2013. The REIT is not aware of ECHO being a party to any significant transactions that occurred during December 2014 and 2013.

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8. Mortgages receivable:

Mortgages receivable represent vendor take-back financing and other arrangements. As at December 31, 2014, mortgages receivable bear interest at effective rates between 3.13% and 4.40% per annum with a weighted average effective rate of 3.36% per annum, and mature between 2015 and 2026.

Future repayments are as follows:

	December 31 2014
Years ending December 31:	
2015	\$ 9,688
2016	61,981
2017	-
2018	-
2019	-
Thereafter	8,253
	\$ 79,922

9. Assets and liabilities classified as held for sale:

As at December 31, 2014, the REIT holds a 49.5% ownership interest in 16 industrial properties, a 50% ownership interest in one industrial property and a 100% ownership interest in one industrial property as held for sale (December 31, 2013 - nil).

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

	December 31 2014	December 31 2013
Assets		
Investment properties	\$ 296,992	\$ -
Liabilities		
Mortgages payable	\$ 65,958	\$ -
Accounts payable and accrued liabilities	221	-
	\$ 66,179	\$ -

10. Other assets:

	December 31 2014	December 31 2013
Restricted cash*	\$ 8,684	\$ 10,623
Accounts receivable	12,263	15,719
Prepaid expenses and sundry assets	21,756	28,282
	\$ 42,703	\$ 54,624

* Included in restricted cash are bank term deposits of nil (December 31, 2013 - \$4,076) at a rate of interest of nil (December 31, 2013 - 1.07%).

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11. Cash and cash equivalents:

Cash and cash equivalents at December 31, 2014 includes cash on hand of \$23,496 (December 31, 2013 - \$27,628) and bank term deposits of \$259 (December 31, 2013 - \$256) at a rate of interest of 0.88% (December 31, 2013 - 0.89%).

12. Mortgages payable:

The mortgages payable are secured by the REIT's real estate assets and letters of credit in certain cases, bearing fixed interest with a contractual weighted average rate of 4.85% (December 31, 2013 - 4.91%) per annum and maturing between 2015 and 2035 (December 31, 2013 - maturing between 2014 and 2035). Included in mortgages payable at December 31, 2014 are U.S. dollar denominated mortgages of U.S. \$1,122,169 (December 31, 2013 - U.S. \$1,203,092). The Canadian equivalents of these amounts are \$1,301,716 (December 31, 2013 - \$1,275,278).

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:

	December 31
	2014
Years ending December 31:	
2015	\$ 369,853
2016	376,693
2017	539,599
2018	237,419
2019	260,832
Thereafter	2,513,258
	4,297,654
Financing costs and mark-to-market adjustment arising on acquisitions	20,482
	\$ 4,318,136

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13. 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	
					2014	2013	
		Contractual	Effective	Conversion	Face	Carrying	Carrying
	Maturity	interest	interest	price	value	value	value
		rate	rate				
Convertible Debentures (a)							
2016 Convertible Debentures (HR.DB.E)	December 31, 2016	4.50%	4.50%	\$ 25.70	\$ 75,000	\$ 76,208	\$ 77,250
2018 Convertible Debentures (HR.DB.H)	November 30, 2018	5.40%	5.40%	\$ 24.73	74,399	79,607	78,507
2020 Convertible Debentures (HR.DB.D)	June 30, 2020	5.90%	5.90%	\$ 23.50	99,654	105,623	104,138
					249,053	261,438	259,895
Senior Debentures (b)							
Series A Senior Debentures	February 3, 2015	5.20%	5.40%	-	115,000	114,986	114,761
Series H Senior Debentures	October 9, 2015	*	*	-	235,000	234,700	234,306
Series D Senior Debentures	July 27, 2016	4.78%	4.96%	-	180,000	179,555	179,262
Series I Senior Debentures	January 23, 2017	**	**	-	60,000	59,792	59,697
Series B Senior Debentures	February 3, 2017	5.90%	6.06%	-	115,000	114,648	114,491
Series E Senior Debentures	February 2, 2018	4.90%	5.22%	-	100,000	99,207	98,976
Series G Senior Debentures	June 20, 2018	3.34%	3.54%	-	175,000	173,873	173,570
Series C Senior Debentures	December 1, 2018	5.00%	5.30%	-	125,000	123,703	123,413
Series F Senior Debentures	March 2, 2020	4.45%	4.63%	-	175,000	173,936	173,759
					1,280,000	1,274,400	1,272,235
					\$1,529,053	\$1,535,838	\$1,532,130

The carrying value of the Convertible Debentures (as defined below) is determined using the quoted price on the TSX on December 31, 2014 and December 31, 2013.

* Bears interest at a rate equal to 3-month Canadian Dealer Offered Rate plus 150 basis points. The REIT entered into an interest rate swap on the Series H Senior Debentures to fix the interest rate at 2.94%.

** 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, 2014 to January 22, 2015 was 2.92%.

In February 2015, the REIT repaid all of its outstanding Series A Senior Debentures upon maturity for a total cash payment of \$115,000.

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13. 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^b 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.

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13. 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 (high) with a Stable trend by DBRS Limited.

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13. Debentures payable (continued):

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

	December 31 2014	December 31 2013
Convertible Debentures (note 13(a))		
Carrying value, beginning of year	\$ 259,895	\$ 400,450
Fair value of convertible debentures assumed on business combination (note 6)	-	94,661
Conversion - 2017 Convertible Debentures*	-	(192,066)
Conversion - 2018 Convertible Debentures*	(16)	-
Conversion - 2020 Convertible Debentures*	-	(27)
Conversion - 2014 ^D Convertible Debentures*	-	(2,693)
Conversion - 2015 Convertible Debentures*	-	(12,451)
Redemption - 2014 ^D Convertible Debentures	-	(54)
Redemption - 2015 Convertible Debentures	-	(347)
Redemption - 2017 Convertible Debentures	-	(4,651)
Redemption - 2018 Convertible Debentures	-	(549)
(Gain) loss on change in fair value (note 23)	1,559	(22,378)
Carrying value, end of year	261,438	259,895
Senior Debentures (note 13(b))		
Carrying value, beginning of year	1,272,235	803,341
Issued - Series G Senior Debentures	-	173,420
Issued - Series H Senior Debentures	-	234,205
Issued - Series I Senior Debentures	-	59,676
Accretion adjustment	2,165	1,593
Carrying value, end of year	1,274,400	1,272,235
	\$ 1,535,838	\$ 1,532,130

* The conversion amounts above total to \$16 as at December 31, 2014 (December 31, 2013 - \$207,237).

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14. Exchangeable units:

Certain of the REIT's subsidiaries have issued exchangeable Class B limited partnership 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 23). Fair value is determined by using the quoted prices for the Stapled Units as the exchangeable units are exchangeable into 16,663,816 (December 31, 2013 - 17,403,119) Stapled Units at the option of the holder. The quoted price as at December 31, 2014 was \$21.73 (December 31, 2013 - \$21.40).

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 REIT and Finance Trust have entered into various exchange and support agreements that provide, among other things, the mechanics whereby Class B LP units may be exchanged for Stapled Units.

The following number of exchangeable units are issued and outstanding:

As at January 1, 2013: Class B LP units of H&R Portfolio Limited Partnership ("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 27)	9,500,000
Class B LP units of Place Du Royaume Limited Partnership exchanged for Stapled Units	(9,000)
As at December 31, 2013	17,403,119
Class B LP units of HRLP exchanged for Stapled Units	(739,303)
As at December 31, 2014	16,663,816

* 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.

15. Loan payable:

The loan payable to ECHO is due in two installments; 50% of the 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 on ECHO's option.

In February 2015, the REIT repaid the first installment of the loan payable to ECHO for a total cash payment of U.S. \$95,780.

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16. 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 16(c)).

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.

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16. Unitholders' equity (continued):

The following number of Stapled Units are issued and outstanding:

As at January 1, 2013	194,676,562
Issued under the Distribution Reinvestment Plan and Unit Purchase Plan (the "DRIP")	3,491,649
Issued on April 4, 2013 (at a price of \$23.01 per unit) (note 6)	62,535,370
2017 Convertible Debentures converted into Stapled Units	8,612,404
2020 Convertible Debentures converted into Stapled Units	1,063
2014 ^D Convertible Debentures converted into Stapled Units	110,939
2015 Convertible Debentures converted into Stapled Units	515,286
Options exercised	22,500
Exchangeable units exchanged into Stapled Units	9,000
As at December 31, 2013	269,974,773
Issued under the DRIP	3,932,252
Options exercised	193,700
2018 Convertible Debentures converted into Stapled Units	606
Exchangeable units exchanged into Stapled Units	739,303
Repurchased through normal course issuer bid	(67,300)
As at December 31, 2014	274,773,334

The weighted average number of basic Stapled Units for the year ended December 31, 2014 is 272,172,222 (December 31, 2013 - 247,717,472).

(a) Unit-based compensation:

In order to provide long-term compensation to the REIT's trustees, officers, employees and consultants, there may be grants of options and incentive units, which are each subject to certain restrictions.

(i) Unit option plan:

As at December 31, 2014, a maximum of 28,000,000 (December 31, 2013 - 28,000,000) Stapled Units were authorized to be issued, of which 12,428,066 options (December 31, 2013 - 11,492,120 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, 2014, 935,946 options were granted (year ended December 31, 2013 - 1,567,800 options).

As described in note 2(h), the REIT's unit option plan is considered a cash-settled plan with the fair value of the Stapled Units underlying option grants recorded as a liability on the combined statements of financial position. The liability is released to equity when the options are converted to Stapled Units. The fair value of the options is remeasured at each reporting period using the Black-Scholes model. Measurement inputs include Stapled 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.

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16. Unitholders' equity (continued):

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

	2014		2013	
	Units	Weighted average exercise price	Units	Weighted average exercise price
Outstanding, beginning of year	4,553,321	\$ 21.04	3,008,021	\$ 20.01
Granted	935,946	22.17	1,567,800	22.92
Exercised	(193,700)	16.42	(22,500)	14.79
Outstanding, end of year	5,295,567	\$ 21.41	4,553,321	\$ 21.04
Options exercisable, end of year	2,906,308	\$ 20.37	1,802,642	\$ 18.60

The options outstanding at December 31, 2014 are exercisable at varying prices ranging from \$9.30 to \$23.18 (December 31, 2013 - \$9.30 to \$23.18) with a weighted average remaining life of 7.4 years (December 31, 2013 - 7.9 years). The vested options are exercisable at varying prices ranging from \$9.30 to \$23.18 (December 31, 2013 - \$9.30 to \$23.18) with a weighted average remaining life of 6.5 years (December 31, 2013 - 6.8 years).

(ii) Incentive unit plan:

As at December 31, 2014, a maximum of 5,000,000 (December 31, 2013 - 5,000,000) Stapled Units were authorized to be issued under the incentive unit plan, of which 162,332 incentive units (December 31, 2013 - nil incentive units) have been granted.

Incentive units 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's trustees, with the result that the awards are classified as cash-settled unit-based payments and presented as liabilities. 100% of the incentive units vest on the third anniversary of the grant date 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 are recognized as liabilities, which are indexed to changes in fair value of the Stapled Units. During the year ended December 31, 2014, 162,332 incentive units were granted (year ended December 31, 2013 - nil incentive units).

The fair value of the vested unit options and incentive units payable are as follows:

	2014	2013
Options	\$ 7,746	\$ 6,313
Incentive units	1,289	-
	\$ 9,035	\$ 6,313

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16. Unitholders' equity (continued):

Unit-based compensation expense (benefit) included in trust expenses is as follows:

	2014	2013
Options	\$ 2,560	\$ (4,136)
Incentive units	1,289	-
	\$ 3,849	\$ (4,136)

(b) 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, 2014, the REIT declared per unit distributions of \$1.24 (December 31, 2013 - \$1.26).

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 \$0.11 for the year ended December 31, 2014 (December 31, 2013 - \$0.09).

The details of the distributions are as follows:

	2014	2013
Cash distributions to unitholders	\$ 281,444	\$ 256,780
Unit distributions (issued under the DRIP)	85,358	74,260
	\$ 366,802	\$ 331,040

(c) 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.

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16. 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.

(d) 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, 2014, \$175,000 of Senior Debentures have been issued under the short form base shelf prospectus.

(e) Normal course issuer bid:

On April 11, 2014, the Trusts received approval from the TSX for a normal course issuer bid ("NCIB"), allowing the Trusts to purchase for cancellation up to a maximum of 25,000,000 Stapled Units on the open market until the earlier of April 14, 2015 or the date on which the Trusts have purchased the maximum number of Stapled Units permitted under the NCIB. During the year ended December 31, 2014, the Trusts purchased and cancelled 67,300 Stapled Units at a weighted average price of \$21.58 per unit, for a total cost of \$1,452. Subsequent to December 31, 2014, the Trusts purchased and cancelled 179,400 Stapled Units at a weighted average price of \$21.94 per unit, for a total cost of \$3,937.

17. Derivative instruments:

	Net gain (loss) on derivative contracts**			
	Fair value (liability) asset *		December 31	
	December 31 2014	December 31 2013	December 31 2014	December 31 2013
Foreign exchange forward contracts (a)	\$ -	\$ (122)	\$ 126	\$ (1,865)
Mortgage interest rate swap (b)	(146)	(386)	263	249
	\$ (146)	\$ (508)	\$ 389	\$ (1,616)

(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 other assets.

** Excludes amounts relating to foreign exchange which have been recorded in accumulated other comprehensive income (loss) (note 20).

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18. 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, 2014 is \$300,000 (December 31, 2013 - \$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 maximum lending value as of December 31, 2014 is \$243,682. The amount available at December 31, 2014, after taking into account the bank indebtedness drawn of \$71,360 (December 31, 2013 - \$101,912) and the REIT providing additional security, outstanding letters of credit and other items, is \$173,313 (December 31, 2013 - \$151,547). The Canadian dollar bank indebtedness bears interest at rates approximating the prime rate of a Canadian chartered bank. At December 31, 2014, the Canadian prime interest rate was 3.00% (December 31, 2013 - 3.00%) per annum.

Included in bank indebtedness at December 31, 2014 are U.S. dollar denominated amounts of \$51,269 (December 31, 2013 - U.S. \$78,253). The Canadian equivalents of these amounts are \$59,472 (December 31, 2013 - \$82,948).

- (b) A general operating facility which is secured by fixed charges over certain investment properties due on December 12, 2016. The total facility as at December 31, 2014 is \$200,000 (December 31, 2013 - \$150,000). The amount available at December 31, 2014, after taking into account the bank indebtedness drawn of \$37,653 (December 31, 2013 - nil) and the outstanding letters of credit is \$161,792 (December 31, 2013 - \$149,446). The Canadian dollar bank indebtedness bears interest at rates approximating the prime rate of a Canadian chartered bank.
- (c) A general operating facility which is secured by fixed charges over certain investment properties due on September 30, 2015. The total facility as at December 31, 2014 is \$14,850 (December 31, 2013 - \$14,850). The amount available at December 31, 2014, after taking into account the bank indebtedness drawn of \$14,850 (December 31, 2013 - \$14,850), is nil (December 31, 2013 - nil). The Canadian dollar bank indebtedness bears interest at rates approximating the prime rate of a Canadian chartered bank.

19. Accounts payable and accrued liabilities:

	2014	2013
Current:		
Other accounts payable and accrued liabilities	\$ 95,135	\$ 105,007
Accounts payable relating to the Bow	3,536	7,140
Debenture interest payable	16,563	16,382
Prepaid rent	17,667	25,465
Mortgage interest payable	11,298	14,012
Non-current:		
Security deposits	3,739	4,087
	\$ 147,938	\$ 172,093

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20. Accumulated other comprehensive income (loss):

	Cash flow hedges	Foreign operations	Total
Balance as at January 1, 2013	\$ (1,182)	\$ (23,689)	\$ (24,871)
Transfer of realized loss on cash flow hedges to net income	414	-	414
Unrealized gain on translation of U.S. denominated foreign operation	-	53,048	53,048
Balance as at December 31, 2013	(768)	29,359	28,591
Transfer of realized loss on cash flow hedges to net income	395	-	395
Unrealized gain on translation of U.S. denominated foreign operation	-	90,140	90,140
Balance as at December 31, 2014	\$ (373)	\$ 119,499	\$ 119,126

21. Rentals from investment properties:

	2014	2013
Rental income	\$ 1,213,351	\$ 1,105,982
Straight-lining of contractual rent	16,177	32,830
Rent amortization of tenant inducements	(1,725)	(1,795)
	\$ 1,227,803	\$ 1,137,017

Operating Leases:

The REIT leases its investment properties under operating leases (note 2(f)). The future minimum lease payments under non-cancellable leases are as follows:

	December 31 2014	December 31 2013
Less than 1 year	\$ 677,137	\$ 733,743
Between 1 and 5 years	2,389,763	2,605,811
More than 5 years	4,294,296	4,839,679
	\$ 7,361,196	\$ 8,179,233

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22. Finance cost - operations:

	2014	2013
Contractual interest on mortgages payable	\$228,807	\$ 230,416
Contractual interest on debentures payable	68,077	61,701
Interest on construction loans	-	144
Effective interest rate accretion	(4,304)	(4,176)
Bank interest and charges	9,545	8,109
Exchangeable unit distributions	23,162	13,967
	325,287	310,161
Capitalized interest*	(1,332)	(532)
	\$323,955	\$ 309,629

* Capitalized interest is determined using the REIT's weighted average rate of borrowings, excluding any borrowings specifically for properties under development, of 4.79% (December 31, 2013 - 5.17%).

23. Gain (loss) on change in fair value:

	2014	2013
Gain (loss) on fair value of convertible debentures (note 13(c))	\$ (1,559)	\$ 22,378
Gain (loss) on fair value of exchangeable units	(6,859)	10,210
Net gain (loss) on derivative instruments (note 17)	389	(1,616)
	\$ (8,029)	\$ 30,972

24. Supplemental cash flow information:

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

	2014	2013
Straight-lining of contractual rent	\$ (24,304)	\$ (41,294)
Prepaid expenses and sundry assets	6,526	(9,205)
Accounts receivable	3,134	8,389
Accounts payable and accrued liabilities	(17,178)	(73,764)
	\$ (31,822)	\$ (115,874)

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24. Supplemental cash flow information (continued):

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

	2014	2013
Non-cash distributions to unitholders in the form of DRIP units (note 16(b))	\$ 85,358	\$ 74,260
Non-cash conversion of convertible debentures (note 13(c))	16	207,237
Non-cash issuance of exchangeable units (note 27)	-	(194,845)
Increase in equity-accounted investments through issuance of loan payable	-	(134,713)
Decrease in accounts payable on redevelopment	(3,922)	(24,953)
Capitalized interest on redevelopment (note 22)	1,332	-
Capitalized interest on properties under development (note 22)	-	532
Non-cash adjustment to proceeds on options exercised	1,127	136
Non-cash release of mortgage payable on disposition of investment properties	(325,975)	(79,569)
Increase in accounts payable included in finance cost - operations	(2,020)	(5,482)
Mortgages receivable from the sale of investment properties	69,981	16,187
Mortgage receivable discharged on acquisition of investment property	-	(3,960)
Exchangeable units exchanged for Stapled Units	17,181	193

25. 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.

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, 2014, this ratio was 44.4% (December 31, 2013 - 47.3%). 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 18(a) and 18(b)) have the following covenants which are required to be calculated based on the REIT's and Finance Trust's combined financial statements:

	Covenant	2014	2013
(a) Maximum indebtedness to gross book value	65%	44.4%	47.3%
(b) Minimum interest coverage ratio	1.65 : 1	2.65 : 1	2.51 : 1
(c) Minimum unitholders' equity	\$3,000,000	\$6,527,668	\$6,273,801

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25. Capital risk management (continued):

The REIT has various other covenants with respect to its debt. The REIT is in compliance with the covenants as at December 31, 2014 and December 31, 2013.

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, 2014 and December 31, 2013. The REIT monitors these ratios and is in compliance with such external requirements.

26. Risk management:

(a) Credit risk:

The REIT is exposed to credit risk in the event that borrowers default on the repayment of the amounts owing to the REIT. Management mitigates this risk by ensuring adequate security has been provided in support of mortgages receivable.

The REIT is exposed to credit risk as an owner of investment properties in that tenants may become unable to pay the contracted rent. 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. 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.

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

	December 31 2014	December 31 2013
Mortgages receivable (note 8)	\$ 79,922	\$ 9,687
Accounts receivable (note 10)	12,263	15,719
	\$ 92,185	\$ 25,406

(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:

	2015	Thereafter	Total
Mortgages payable (note 12)*	\$ 369,853	\$ 3,927,801	\$ 4,297,654
Debentures payable (note 13)*	349,686	1,186,152	1,535,838
Loan payable (note 15)*	147,608	-	147,608
Derivative instruments (note 17)*	146	-	146
Bank indebtedness (note 18)*	14,850	109,013	123,863
Accounts payable and accrued liabilities (note 19)	144,199	3,739	147,938
	\$ 1,026,342	\$ 5,226,705	\$ 6,253,047

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

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26. Risk management (continued):

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 18(a) and 18(b), available to draw on to fund its obligations.

(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 \$1.10 for the year ended December 31, 2014 (December 31, 2013 - \$1.03) would have decreased other comprehensive income (loss) by approximately \$86,600 (December 31, 2013 - \$78,100) and decreased net income by approximately \$9,300 (December 31, 2013 - \$6,600). 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, 2014 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, 2014, the percentage of fixed rate debt to total debt was 96.4% (December 31, 2013 - 93.8%). 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, 2014 would have decreased net income by approximately \$1,300 (December 31, 2013 - \$1,400). 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, 2014 would have decreased net income by approximately \$600 (December 31, 2013 - \$300). This analysis assumes that all other variables, in particular foreign exchange rates, remain constant.

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26. Risk management (continued):

(d) *Fair values:*

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

The fair values of the Trusts' mortgages 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.

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, 2014 has been estimated at \$4,723,891 (December 31, 2013 - \$4,956,307) compared with the carrying value of \$4,318,136 (December 31, 2013 - \$4,723,891).

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, 2014 has been estimated at \$1,349,227 (December 31, 2013 - \$1,321,378) compared with the carrying value of \$1,274,400 (December 31, 2013 - \$1,272,235).

The fair value of the loan payable to ECHO approximates the carrying value as ECHO has the option to demand accelerated repayment (note 15).

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

Assets and liabilities 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, 2014	Level 1	Level 2	Level 3	Total
Assets measured at fair value				
Investment properties	\$ -	\$ -	\$ 12,116,983	\$ 12,116,983
Properties under development	-	-	105,006	105,006
	-	-	12,221,989	12,221,989
Liabilities measured at fair value				
Convertible debentures (note 13)	(261,438)	-	-	(261,438)
Exchangeable units	(362,105)	-	-	(362,105)
Derivative instruments liabilities	-	(146)	-	(146)
Liabilities for which fair values are disclosed				
Mortgages payable	-	-	(4,723,891)	(4,723,891)
Senior debentures	-	-	(1,349,227)	(1,349,227)
	(623,543)	(146)	(6,073,118)	(6,696,807)
	\$ (623,543)	\$ (146)	\$ 6,148,871	\$ 5,525,182

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26. Risk management (continued):

December 31, 2013	Level 1	Level 2	Level 3	Total
Assets				
Investment properties	\$ -	\$ -	\$ 12,786,205	\$ 12,786,205
Properties under development	-	-	146,478	146,478
	-	-	12,932,683	12,932,683
Liabilities				
Convertible debentures (note 13)	(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

27. Related party transactions:

Prior to July 1, 2013, 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, pursuant to a property management agreement. 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.

Effective July 1, 2013, the REIT executed an agreement with HRPM to internalize the property management function. Upon closing of the transaction, HRRMSLP acquired HRPM's REIT-related property management business in return for 9,500,000 partnership units of HRRMSLP, such units to be exchangeable on a one-for-one basis for Stapled Units. In June 2014, the unitholders of the REIT approved the granting of voting rights to these 9,500,000 partnership units. The total 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. No transaction costs were expensed during the year ended December 31, 2014.

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, 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, 2014, the REIT incurred costs of \$1,497 (December 31, 2013 - \$811) under this agreement.

During the year ended December 31, 2013, the REIT recorded expenses pursuant to the property management agreement of \$8,211, of which \$550 was capitalized to the cost of the investment properties acquired, nil was capitalized to properties under development and \$2,030 was included in leasing expenses. These amounts include amounts relating to equity accounted investments. The REIT also reimbursed HRPM for certain direct property operating costs and tenant construction costs. No amounts were incurred during the year ended December 31, 2014 as this function has been internalized.

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27. Related party transactions (continued):

During the year ended December 31, 2013, a further amount of \$2,250 was earned by HRPM pursuant to the property management agreement, in accordance with the annual incentive fee payable to HRPM. Of this amount, \$1,125 was waived by HRPM and \$1,125 was expensed in the combined statement of comprehensive income. No amounts were incurred during the year ended December 31, 2014 as this function has been internalized.

The REIT leases space to companies partially owned by family members of the CEO. The rental income earned for the year ended December 31, 2014 is \$1,488 (December 31, 2013 - \$1,358).

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

The REIT has interests in various investment properties through joint arrangements and investments in associates. Generally, the REIT provides asset and property management services to co-owners, partners and third parties for which it earns market-based fees. Transactions subsequent to the formation of a co-ownership that are not contemplated by the co-ownership agreements are considered to be related party transactions for financial statement purposes.

Key management personnel compensation:

	2014	2013
Short-term employee salaries and benefits	\$ 5,024	\$ 4,334
Employee unit-based compensation	2,695	(3,725)
	\$ 7,719	\$ 609

28. Segmented disclosures:

(i) Operating segments:

The Trusts have two operating segments: the H&R portfolio, which includes Finance Trust, comprised of 474 properties, including assets held for sale and equity accounted investments (December 31, 2013 - 468) and the Primaris portfolio, comprised of 27 properties, including assets held for sale (December 31, 2013 - 26).

December 31, 2014	H&R	Primaris	Elimination*	Total
Real estate assets:				
Investment properties	\$ 10,193,390	\$ 3,064,350	\$ -	\$ 13,257,740
Properties under development	211,353	-	-	211,353
	10,404,743	3,064,350	-	13,469,093
Less: Trusts' proportionate share of investment properties and properties under development relating to equity accounted investments	(1,247,104)	-	-	(1,247,104)
	\$ 9,157,639	\$ 3,064,350	\$ -	\$ 12,221,989
Total assets	\$ 10,883,395	\$ 3,078,633	\$ (593,648)	\$ 13,368,380
Total liabilities	\$ 6,010,777	\$ 1,423,583	\$ (593,648)	\$ 6,840,712

* Elimination of intercompany loans between Primaris and the REIT.

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28. Segmented disclosures (continued):

December 31, 2013	H&R	Primaris	Elimination*	Total
Real estate assets:				
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
Less: Trusts' proportionate share of investment properties and properties under development relating to equity accounted investments	(1,058,385)	-	-	(1,058,385)
	\$ 9,742,783	\$ 3,189,900	\$ -	\$ 12,932,683
Total assets	\$ 11,048,400	\$ 3,209,492	\$ (674,865)	\$ 13,583,027
Total liabilities	\$ 6,253,602	\$ 1,730,489	\$ (674,865)	\$ 7,309,226

* Elimination of intercompany loans between Primaris and the REIT.

Property operating income by reportable segment for the year ended December 31, 2014 and December 31, 2013 is as follows:

	H&R	Primaris	2014	H&R	Primaris	2013
Property operating income:						
Rentals from investment properties	\$ 930,432	\$ 297,371	\$ 1,227,803	\$ 910,119	\$ 226,898	\$ 1,137,017
Property operating costs	(299,773)	(124,754)	(424,527)	(293,469)	(93,626)	(387,095)
	\$ 630,659	\$ 172,617	\$ 803,276	\$ 616,650	\$ 133,272	\$ 749,922

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28. Segmented disclosures (continued):

(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.

	December 31 2014	December 31 2013
Canada	\$ 10,314,535	\$ 11,147,166
United States	3,154,558	2,843,902
	13,469,093	13,991,068
Less: Trusts' proportionate share of investment properties and properties under development relating to equity accounted investments	(1,247,104)	(1,058,385)
	\$ 12,221,989	\$ 12,932,683

	2014	2013
Rentals from investment properties:		
Canada	\$ 1,062,386	\$ 983,860
United States	269,967	224,469
	1,332,353	1,208,329
Less: Trusts' proportionate share of rentals relating to equity accounted investments	(104,550)	(71,312)
	\$ 1,227,803	\$ 1,137,017

29. Income tax expense:

	2014	2013
Income tax computed at the Canadian statutory rate of nil applicable to the REIT for 2014 and 2013	\$ -	\$ -
Current U.S. income taxes	920	471
Deferred income taxes applicable to U.S. Holdco	43,704	29,227
Income tax expense in the determination of net income	\$ 44,624	\$ 29,698

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29. Income tax expense (continued):

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:

	December 31 2014	December 31 2013
Deferred tax assets:		
Net operating losses and deferred interest deductions	\$ 95,483	\$ 84,434
Accounts payable and accrued liabilities	2,101	1,865
Derivative instruments	56	195
Other assets	218	158
	97,858	86,652
Deferred tax liabilities:		
Investment properties	218,397	162,055
Equity accounted investments	9,325	1,151
	227,722	163,206
Deferred tax liability	\$ (129,864)	\$ (76,554)

As at December 31, 2014, U.S. Holdco had accumulated net operating losses and deferred interest deductions available for carryforward for U.S. income tax purposes of \$248,979 (December 31, 2013 - \$219,708). The net operating losses will expire between 2018 and 2034. The deferred interest deductions and the deductible temporary differences do not generally expire under current tax legislation.

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30. 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, 2014, the REIT has outstanding letters of credit totalling \$55,857 (December 31, 2013 - \$47,070), including \$17,781 (December 31, 2013 - \$17,438) which has been pledged as security for certain mortgages payable. Of these letters of credit, \$55,857 (December 31, 2013 - \$41,419) are secured in the same manner as the bank indebtedness (notes 18(a) and 18(b)) and nil (December 31, 2013 - \$5,651) by a specific investment property.
- (b) The REIT provides guarantees on behalf of third parties, including co-owners. As at December 31, 2014, the REIT issued guarantees amounting to \$229,048 (December 31, 2013 - \$69,766), which expire in 2022 (December 31, 2013 - 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, 2014, the estimated amount of debt subject to such guarantees, and therefore the maximum exposure to credit risk, is \$152,185 (December 31, 2013 - \$224,377) which expires between 2016 and 2020 (December 31, 2013 - expires between 2014 and 2020). 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.

31. Subsequent events:

- (a) In January 2015, the REIT sold an industrial property in Ontario, which was classified as held for sale as at December 31, 2014, for gross proceeds of approximately \$70,200 and repaid the mortgage payable of approximately \$42,600 bearing interest at 5.22% per annum.
- (b) In February 2015, the REIT issued by way of private placement, U.S. \$125,000 Series J senior floating rate unsecured debentures maturing on February 9, 2018.
- (c) In February 2015, the REIT acquired a residential property in Dallas, TX for a purchase price of approximately U.S. \$52,300.

Corporate Information

H&R REIT Board of Trustees

Thomas J. Hofstedter ⁽¹⁾, President and Chief Executive Officer, H&R Real Estate Investment Trust
Robert Dickson ^(1,2,3,4), Strategic financial consultant, marketing communications industry
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H&R Finance Trust Board of Trustees

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Shimshon (Stephen) Gross ⁽²⁾, President, LRG Holdings Inc.
Marvin Rubner ⁽²⁾, Manager and Founder, YAD Investments Limited.
Neil Sigler ⁽²⁾, 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: The 2014 distributions by H&R REIT were comprised of capital gains (50.6%), other taxable income (33.6%), foreign non-business income (6.1%) and tax deferred return of capital (9.7%). The 2014 distributions by H&R Finance Trust were comprised of foreign non-business income (86.5%) and tax deferred return of capital (13.5%). For a Canadian resident unitholder, only 66.7% of the 2014 distributions on a Stapled Unit are subject to tax when considering these allocations and the non-taxable portion of the capital gains.

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, Website: www.canstockta.com.

Contact Information: Investors, investment analysts and others seeking financial information should go to our website at www.hr-reit.com, or e-mail 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



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