



CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2010

TEMPLE REAL ESTATE INVESTMENT TRUST

CONSOLIDATED BALANCE SHEETS

	<u>June 30</u> <u>2010</u>	<u>December 31</u> <u>2009</u>
Assets		
Current assets		
Cash	\$ 8,659,217	\$ 7,401,442
Marketable securities (Note 3)	605,558	628,208
Accounts receivable (net of allowance for doubtful accounts of \$113,224, 2009 - \$102,057)	2,054,607	2,150,209
Inventories	828,844	716,220
Prepaid expenses	361,161	226,402
Current portion of net investment in lease (Note 4)	129,870	125,370
Defeasance assets (Note 5)	-	2,941,723
	<u>12,639,257</u>	<u>14,189,574</u>
Property and equipment (Note 6)	245,536,872	248,546,241
Net investment in lease (Note 4)	4,450,515	4,516,591
Other assets (Note 7)	1,901,266	952,794
Goodwill	<u>1,608,282</u>	<u>1,608,282</u>
	<u>\$266,136,192</u>	<u>\$269,813,482</u>
Liabilities and Equity		
Current liabilities		
Accounts payable and accrued liabilities	\$ 4,804,300	\$ 4,570,013
Gift certificate liability	1,879,615	2,132,718
Income taxes payable	-	135,042
Current portion of long-term debt (Note 8)	54,808,834	50,746,879
Defeased liability (Note 5)	-	2,834,896
Distribution payable	1,282,535	-
	<u>62,775,284</u>	<u>60,419,548</u>
Long-term debt (Note 8)	116,078,319	118,051,239
Convertible debentures (Note 9)	31,028,394	30,391,822
Future income taxes (Note 10)	<u>3,183,487</u>	<u>3,712,128</u>
	213,065,484	212,574,737
Equity	<u>53,070,708</u>	<u>57,238,745</u>
	<u>\$266,136,192</u>	<u>\$269,813,482</u>

Approved by the Trustees

"Arni Thorsteinson"

"David Drybrough"

TEMPLE REAL ESTATE INVESTMENT TRUST

CONSOLIDATED STATEMENTS OF INCOME (LOSS) AND COMPREHENSIVE INCOME (LOSS)

	Three Months Ended		Six Months Ended	
	June 30		June 30	
	2010	2009	2010	2009
Revenue				
Hotel revenue	\$ 15,229,834	\$ 16,001,921	\$ 29,720,164	\$ 32,554,016
Interest and other income	<u>524,287</u>	<u>778,448</u>	<u>1,014,974</u>	<u>1,494,775</u>
	15,754,121	16,780,369	30,735,138	34,048,791
Expenses				
Hotel operating costs	<u>10,595,054</u>	<u>10,279,359</u>	<u>20,703,723</u>	<u>20,769,353</u>
Operating income	<u>5,159,067</u>	<u>6,501,010</u>	<u>10,031,415</u>	<u>13,279,438</u>
Finance expense (Note 11)	4,001,516	3,541,697	8,074,809	7,221,897
Trust expense	219,383	225,491	583,390	424,300
Amortization	<u>1,745,028</u>	<u>1,595,755</u>	<u>3,489,626</u>	<u>3,190,293</u>
	<u>5,965,927</u>	<u>5,362,943</u>	<u>12,147,825</u>	<u>10,836,490</u>
Other				
Increase (decrease) in value of marketable securities	<u>(117,225)</u>	<u>26,175</u>	<u>(22,650)</u>	<u>(90,750)</u>
Income (loss) before income taxes	(924,085)	1,164,242	(2,139,060)	2,352,198
Income taxes recovery (expense):				
Current	(69,203)	(41,819)	(137,886)	(90,000)
Future	<u>231,234</u>	<u>(294,400)</u>	<u>528,641</u>	<u>(595,800)</u>
	<u>162,031</u>	<u>(336,219)</u>	<u>390,755</u>	<u>(685,800)</u>
Net income (loss) and comprehensive income (loss)	<u>\$ (762,054)</u>	<u>\$ 828,023</u>	<u>\$ (1,748,305)</u>	<u>\$ 1,666,398</u>
Net income (loss) per unit (Note 12)				
Basic and diluted	\$ (0.06)	\$ 0.06	\$ (0.14)	\$ 0.13

TEMPLE REAL ESTATE INVESTMENT TRUST

CONSOLIDATED STATEMENTS OF EQUITY

	<u>Three Months Ended</u>		<u>Six Months Ended</u>	
	<u>June 30</u>		<u>June 30</u>	
	<u>2010</u>	<u>2009</u>	<u>2010</u>	<u>2009</u>
Trust units (Note 13)				
Balance, beginning of period	\$ 62,490,094	\$ 62,687,492	\$ 62,491,116	\$ 62,590,168
Units issued on conversion of debentures	-	-	-	85,597
Equity component of debentures converted	-	-	-	16,357
Unit issue costs	<u>787</u>	<u>-</u>	<u>(235)</u>	<u>(4,630)</u>
Balance, end of period	<u>62,490,881</u>	<u>62,687,492</u>	<u>62,490,881</u>	<u>62,687,492</u>
Unit based compensation (Notes 14 and 15)				
Balance, beginning of period	325,809	146,210	197,239	146,210
Value associated with unit options granted	-	-	116,370	-
Value of deferred units	<u>17,003</u>	<u>14,900</u>	<u>29,203</u>	<u>14,900</u>
Balance, end of period	<u>342,812</u>	<u>161,110</u>	<u>342,812</u>	<u>161,110</u>
Equity component of convertible mortgage (Note 8)				
Balance, beginning and end of period	<u>471,175</u>	<u>-</u>	<u>471,175</u>	<u>-</u>
Equity component of convertible debentures (Note 9)				
Balance, beginning of period	6,101,487	3,661,939	6,101,487	3,678,296
Equity component of debentures converted	<u>-</u>	<u>-</u>	<u>-</u>	<u>(16,357)</u>
Balance, end of period	<u>6,101,487</u>	<u>3,661,939</u>	<u>6,101,487</u>	<u>3,661,939</u>
Cumulative earnings and accumulated comprehensive earnings				
Balance, beginning of period	12,009,170	12,929,518	12,995,421	12,091,143
Net income (loss)	<u>(762,054)</u>	<u>828,023</u>	<u>(1,748,305)</u>	<u>1,666,398</u>
Balance, end of period	<u>11,247,116</u>	<u>13,757,541</u>	<u>11,247,116</u>	<u>13,757,541</u>
Cumulative distributions to unitholders				
Balance, beginning of period	(26,300,228)	(21,170,008)	(25,017,693)	(18,607,684)
Distribution to unitholders	<u>(1,282,535)</u>	<u>(1,282,535)</u>	<u>(2,565,070)</u>	<u>(3,844,939)</u>
Balance, end of period	<u>(27,582,763)</u>	<u>(22,452,543)</u>	<u>(27,582,763)</u>	<u>(22,452,623)</u>
Total unitholders' equity	<u>\$ 53,070,708</u>	<u>\$ 57,815,539</u>	<u>\$ 53,070,708</u>	<u>\$ 57,815,459</u>
Units issued and outstanding (Note 13)	<u>12,825,352</u>	<u>12,825,352</u>	<u>12,825,352</u>	<u>12,825,352</u>
Deferred units outstanding (Note 15)	<u>28,787</u>	<u>4,585</u>	<u>28,787</u>	<u>4,585</u>

(unaudited)

TEMPLE REAL ESTATE INVESTMENT TRUST

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Three Months Ended		Six Months Ended	
	June 30		June 30	
	2010	2009	2010	2009
Cash provided by (used in) operating activities				
Net income (loss) and comprehensive income (loss)	\$ (762,054)	\$ 828,023	\$ (1,748,305)	\$ 1,666,398
Items not affecting cash				
Accretion on debt component of convertible debentures	223,475	144,322	486,289	289,127
Accretion on debt component of convertible mortgage	20,911	-	41,306	-
Unit based compensation	17,003	14,900	145,573	14,900
Amortization	1,745,028	1,595,755	3,489,626	3,190,293
Amortization of transaction costs	236,509	206,121	532,832	420,052
Change in fair value of marketable equity securities	117,225	(26,175)	22,650	90,750
Future income taxes	(231,234)	294,400	(528,641)	595,800
	<u>1,366,863</u>	<u>3,057,346</u>	<u>2,441,330</u>	<u>6,267,320</u>
Changes in non-cash operating items	<u>(725,843)</u>	<u>(410,450)</u>	<u>(372,629)</u>	<u>811,270</u>
	<u>641,020</u>	<u>2,646,896</u>	<u>2,068,701</u>	<u>7,078,590</u>
Cash provided by (used in) financing activities				
Proceeds of long-term debt	5,000,000	-	5,000,000	-
Decrease in defeased liability	(2,744,883)	(97,699)	(2,849,560)	(193,177)
Repayment of long-term debt	(1,336,283)	(1,310,340)	(3,276,168)	(2,511,053)
Expenditures on transaction costs	(43,991)	-	(43,991)	(17,351)
Unit issue costs	787	-	(235)	-
Distributions paid on trust units	(1,282,535)	-	(1,282,535)	(2,562,404)
	<u>(406,905)</u>	<u>(1,408,039)</u>	<u>(2,452,489)</u>	<u>(5,283,985)</u>
Cash provided by (used in) investing activities				
Additions to property and equipment	(272,929)	(417,448)	(480,258)	(609,477)
Proceeds from expropriated land	-	811,615	-	811,615
Decrease in defeasance assets	2,773,850	138,393	2,941,723	275,874
Deposits on potential acquisitions	-	-	-	250,000
Return of capital from marketable equity securities	-	29,925	-	63,750
Purchase of marketable securities	-	-	-	(6,000)
Receipt of net investment in lease	31,060	28,943	61,576	57,379
Change in cash in escrow	(62,102)	(36,398)	(881,478)	141,313
	<u>2,469,879</u>	<u>555,030</u>	<u>1,641,563</u>	<u>984,454</u>
Change in cash	2,703,994	1,793,887	1,257,775	2,779,059
Cash, beginning of period	5,955,223	3,809,990	7,401,442	2,824,818
Cash, end of period	\$ 8,659,217	\$ 5,603,877	\$ 8,659,217	\$ 5,603,877
Supplementary cash flow information				
Interest paid	<u>\$ 4,005,149</u>	<u>\$ 3,595,688</u>	<u>\$ 7,081,550</u>	<u>\$ 6,286,553</u>
Income taxes paid	<u>\$ 263,394</u>	<u>\$ 196,750</u>	<u>\$ 263,394</u>	<u>\$ 196,750</u>

(unaudited)

TEMPLE REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2010

1 **Organization**

Temple Real Estate Investment Trust ("the Trust") is an open-end real estate investment trust established under the laws of the Province of Manitoba on July 12, 2006.

2 **Basis of presentation**

The consolidated interim financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles (GAAP). The consolidated interim financial statements of the Trust includes the accounts of the Trust's wholly-owned subsidiaries TR Trust, Temple Limited Partnership, Temple General Partner Inc. and Temple Gardens Mineral Spa Inc., with provision for its 50% proportionate share of assets, liabilities, revenues and expenses of the Moose Jaw Casino Co-ownership. Intercompany balances and transactions have been eliminated upon consolidation. The interim consolidated financial statements have been prepared on a consistent basis with the December 31, 2009 audited consolidated financial statements. These consolidated financial statements do not include all the information and disclosure required by Canadian generally accepted accounting principles for annual financial statements, and should be read in conjunction with the December 31, 2009 audited consolidated financial statements and notes thereto.

Future changes to significant accounting policies

CICA Handbook Section 1582 - Business Combinations will apply prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2011. CICA Handbook Sections 1601 - Consolidations and 1602 - Non-Controlling Interests will be effective for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. Earlier adoption of these sections is permitted as of the beginning of a fiscal year. All three sections must be adopted concurrently. These sections replace the former CICA Handbook Sections 1581 - Business Combinations and 1600 - Consolidated Financial Statements. CICA Handbook Section 1582 establishes standards for the accounting for a business combination. CICA Handbook Section 1601 establishes standards for the preparation of consolidated financial statements. CICA Handbook section 1602 establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. The Trust is currently considering the effect on the financial statements of the new standards.

3 **Marketable securities**

	June 30 2010	December 31 2009
Marketable equity securities	\$ 280,800	\$ 303,450
Guaranteed investment certificates	<u>324,758</u>	<u>324,758</u>
	<u>\$ 605,558</u>	<u>\$ 628,208</u>

Marketable equity securities are recorded at fair value based on published market value and are classified as held-for-trading financial instruments. The investments were written down from their carrying value by \$117,225 for the three months ended June 30, 2010 (2009 - written up \$26,175) and by \$22,650 for the six months ended June 30, 2010 (2009 - \$90,750).

Guaranteed investment certificates bear interest at 0.001% - 2.15% (December 31, 2009 - 0.001% - 2.15%) with maturity dates in 2010 (December 31, 2009 - 2010).

TEMPLE REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2010

4 *Net investment in lease*

In 2002, Temple Gardens Mineral Spa Inc. entered into co-ownership of a Moose Jaw casino complex property. The co-ownership completed the development of a 23,400 square foot building and 140 parking stalls. The entire property is subject to a 25 year lease and the tenant must acquire ownership of the property at the end of the lease term for consideration of \$1. Under the terms of the lease, the tenant is responsible for all and every cost arising from or related to the leased premises, including the cost of replacement of the structure and foundation.

Pursuant to the terms of the co-ownership agreement, the co-owners each hold a 50% equity interest in the co-ownership, with all equity contributions, distributions, and net income allocations being made on this same 50% basis.

Future income related to the finance-type lease is recognized in a manner that produces a constant rate of return on the net investment in the lease. The investment in the lease for purposes of income recognition is comprised of net minimum lease payments and unearned finance income. The effective interest rate of the net investment in lease is 7.31%.

Interest income included in interest and other income for the three months ended June 30, 2010 was \$81,440 (2009 - \$83,557) relating to the net investment in lease and \$163,424 (2009 - \$167,620) for the six months ended June 30, 2010.

The net investment in lease includes the following:

	<u>June 30</u> <u>2010</u>	<u>December 31</u> <u>2009</u>
Total minimum lease payments receivable	\$ 7,762,500	\$ 7,987,500
Unearned income	<u>(3,182,115)</u>	<u>(3,345,539)</u>
Net investment in lease	4,580,385	4,641,961
Less current portion	<u>(129,870)</u>	<u>(125,370)</u>
	<u>\$ 4,450,515</u>	<u>\$ 4,516,591</u>

The Trust's proportionate share of future minimum lease payments is \$450,000 per annum through October 2011 escalating to \$477,500 until the end of the lease term, October 1, 2026.

TEMPLE REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2010

5 *Defeasance assets and defeased liability*

In conjunction with the refinancing of the Merit and Nomad hotels on September 24, 2007, an existing \$3,690,806 loan was defeased. The defeased loan was payable in monthly payments of \$56,551 including interest at 9.41% was originally amortized over 15 years and was due April 1, 2010. The Trust purchased Government of Canada bonds in the amount of \$4,151,677 and pledged them as security to the debtholder. The bonds matured between June 1, 2009 and December 1, 2009, had a weighted average interest rate of 4.14% and were placed in escrow. The defeasance assets and the defeased liability were measured at amortized cost using the effective interest rate method of amortization until April 1, 2010 at which time the assets were realized and the debt was extinguished.

The following table reflects the effect of the defeasance asset and the defeased liability.

	Recorded as	Six Months Ended June 30	
		2010	2009
Interest income on defeasance assets	Interest and other income	\$ 2,370	\$ 63,434
Interest expense on defeased liability	Finance expense	(64,172)	(144,645)
Amortization of transaction costs	Finance expense	(14,664)	(20,219)
		<u>\$ (76,466)</u>	<u>\$ (101,430)</u>

The unamortized balance of the defeasance transaction costs is nil (2009 - \$14,664).

6 *Property and equipment*

<u>June 30, 2010</u>	<u>Cost</u>	<u>Accumulated Amortization</u>	<u>Net Book Value</u>
Land	\$ 28,200,924	\$ -	\$ 28,200,924
Buildings	225,210,404	(15,644,584)	209,565,820
Furniture and equipment	<u>10,691,049</u>	<u>(2,920,921)</u>	<u>7,770,128</u>
	<u>\$264,102,377</u>	<u>\$ (18,565,505)</u>	<u>\$245,536,872</u>
 <u>December 31, 2009</u>			
	<u>Cost</u>	<u>Accumulated Amortization</u>	<u>Net Book Value</u>
Land	\$ 28,200,924	\$ -	\$ 28,200,924
Buildings	224,831,975	(12,696,248)	212,135,727
Furniture and equipment	<u>10,628,365</u>	<u>(2,418,775)</u>	<u>8,209,590</u>
	<u>\$263,661,264</u>	<u>\$ (15,115,023)</u>	<u>\$248,546,241</u>

TEMPLE REAL ESTATE INVESTMENT TRUST

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2010**

6 Property and equipment (continued)

Amortization of property and equipment consists of the following:

	Three Months Ended		Six Months Ended	
	June 30		June 30	
	<u>2010</u>	<u>2009</u>	<u>2010</u>	<u>2009</u>
Buildings	\$ 1,474,222	\$ 1,350,932	\$ 2,948,341	\$ 2,701,455
Furniture and equipment	<u>270,806</u>	<u>244,823</u>	<u>541,285</u>	<u>488,838</u>
	<u>\$ 1,745,028</u>	<u>\$ 1,595,755</u>	<u>\$ 3,489,626</u>	<u>\$ 3,190,293</u>

7 Other assets

	<u>June 30 2010</u>	<u>December 31 2009</u>
Cash in escrow	\$ 1,648,945	\$ 767,467
Deposits	158,096	91,102
Franchise application fee	<u>94,225</u>	<u>94,225</u>
	<u>\$ 1,901,266</u>	<u>\$ 952,794</u>

TEMPLE REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2010

8 Long-term debt

Long-term debt consists of the following:

	June 30 2010	December 31 2009
First mortgage loans secured by specific hotel properties bearing interest at fixed rates between 4.32% and 6.83% weighted average interest rate - 6.25% (2009 - rates between 5.06% and 6.83%, weighted average interest rate - 6.31%) and maturing between November 30, 2010 and August 1, 2014.	\$152,264,866	\$150,375,362
Moose Jaw Casino Co-ownership - 7.08% loan payable, maturing September 1, 2027 secured by a specific assignment of the Saskatchewan Gaming Corporation lease.	3,712,547	3,767,269
12% Second mortgage loan - secured by a specific hotel property with payments of interest only, maturing October 31, 2010.	7,040,000	7,040,000
6% Second mortgage loan - secured by a specific hotel property, maturing December 31, 2013.	4,693,971	4,804,919
4.5% Convertible mortgage loan - secured by a specific hotel property with payments of interest only, \$4,500,000 face value maturing July 31, 2014. The mortgage loan is convertible to trust units at any time during its term at a price of \$15.00 at the option of the lender. \$471,175 was allocated to equity on issuance of the debt for an estimated cost of borrowing of 7.0%.	<u>4,105,621</u>	<u>4,064,315</u>
	171,817,005	170,051,865
Transaction costs	(929,852)	(1,253,747)
Less current portion - net of transaction costs of \$446,915 (December 31, 2009 - \$522,700)	<u>(54,808,834)</u>	<u>(50,746,879)</u>
	<u>\$116,078,319</u>	<u>\$118,051,239</u>

Approximate principal repayments are as follows:

12 months ending June 30

2011	\$ 55,255,749
2012	10,588,444
2013	72,865,607
2014	23,235,965
2015	7,219,030
Thereafter	<u>3,046,589</u>
	<u>\$172,211,384</u>

TEMPLE REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2010

8 *Long term debt (continued)*

Mortgage loans are secured by mortgage charges registered against specific income properties and are also secured by assignments of book debts and inventories.

Certain of the mortgage loans payable are subject to covenants, include minimum debt service coverage requirements. In addition, capital expenditures must not exceed certain maximums. The Trust is not in compliance on one first mortgage loan in the amount of \$32,967,381, as a result of a breach of the debt service coverage requirement in respect of that mortgage loan. The loan balance of \$32,967,381 as at June 30, 2010 is included in principal repayments in the twelve months ended June 30, 2011.

The breach of the debt service covenant requirement is a result of the negative impact of the slow down of development activities in the oil sands industry and the associated decline in the market conditions in Fort McMurray. Given that the market conditions may not improve substantially in the near future, the breach in the debt service covenant requirement may continue. The Trust has notified the lender.

Transaction costs are incremental costs that are directly attributable to the acquisition of mortgage financing and include both fees and charges, brokerage fees and commissions, legal fees, advisor and similar costs. Transaction costs are amortized over the term of the respective mortgages using the effective interest method. The transaction cost amortization for the three months ended June 30, 2010 amounted to \$135,584 (2009 - \$145,273) and \$326,767 (2009 - \$300,720) for the six months ended June 30, 2010.

9 *Convertible debentures*

As of June 30, 2010, the Trust has three series of convertible debentures outstanding:

Series A

The Trust issued \$15,680,000 of Series A convertible redeemable debentures by way of private placement on February 15, 2007. The debentures are unsecured, bear interest at 7.5% payable semi-annually and mature on March 31, 2012. The debentures are convertible to trust units at any time during their term at a price of \$5.75 at the option of the debenture holder.

The debentures are redeemable at the option of the Trust at the principal amount, subject to certain terms and conditions, from March 31, 2010 and prior to March 31, 2011, providing that the 20-day weighted average trading price of the units is at least \$7.1875 and, on or after March 31, 2011, at their principal amount.

During the six months ended June 30, 2010 and year ended December 31, 2009 there were no conversions of Series A debentures.

TEMPLE REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2010

9 *Convertible debentures (continued)*

Series B

The Trust issued \$30,000,000 of Series B convertible redeemable debentures by way of private placement on April 8, 2008. The debentures are unsecured, bear interest at 8.5% semi-annually and mature on April 30, 2013. The debentures are convertible to trust units at any time during their term at a price of \$7.50 at the option of the debenture holder.

The debentures are redeemable at the option of the Trust at the principal amount, subject to certain terms and conditions, from April 30, 2011 and prior to April 30, 2012, providing that the 20-day weighted average trading price of the units is at least \$9.375 and, on or after April 30, 2012, at their principal amount.

During the six months ended June 30, 2010, there were no conversions of Series B debentures.

During the year ended December 31, 2009, \$100,000 of debentures were converted to 13,333 trust units.

Senior Secured Convertible Redeemable

The Trust issued \$15,000,000 of senior secured convertible redeemable debentures by way of public offering on November 27, 2009. The debentures are secured by a secondary charge on certain hotel properties, bear interest at 8.75% semi-annually and mature on November 30, 2014. The debentures are convertible to trust units at any time during their term at a price of \$3.65 at the option of the debenture holder.

The debentures are redeemable at the option of the Trust at the principal amount, subject to certain terms and conditions, from November 30, 2012 and prior to November 30, 2014, providing that the current trading price of the units is at least \$4.5625 and, on or after November 30, 2013, at their principal amount.

During the six months ended June 30, 2010 and the year ended December 31, 2009 there were no conversions of senior secured convertible debentures.

The following schedule allocates the convertible debentures between the debt and equity components on the basis of the net present value of future interest and principal payments at an estimated cost of borrowing without conversion option as reflected in the schedules:

<u>June 30, 2010</u>	Estimated Cost of <u>Borrowing</u>	<u>Debt</u>	<u>Equity</u>	<u>Total</u>	<u>Face Value</u>
Series A	12.00 %	\$ 2,314,786	\$ 412,489	\$ 2,727,275	\$ 2,464,500
Series B	13.00 %	17,660,668	3,249,450	20,910,118	19,866,100
Senior Secured	13.25 %	12,773,934	2,439,548	15,213,482	15,000,000
Transaction costs		<u>(1,720,994)</u>	<u>-</u>	<u>(1,720,994)</u>	<u>-</u>
		<u>\$31,028,394</u>	<u>\$ 6,101,487</u>	<u>\$37,129,881</u>	<u>\$ 37,330,600</u>

TEMPLE REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2010

9 *Convertible debentures (continued)*

<u>December 31, 2009</u>	Estimated Cost of <u>Borrowing</u>	<u>Debt</u>	<u>Equity</u>	<u>Total</u>	<u>Face Value</u>
Series A	12.00 %	\$ 2,259,094	\$ 412,489	\$ 2,671,583	\$ 2,464,500
Series B	13.00 %	17,410,097	3,249,450	20,659,547	19,866,100
Senior Secured	13.25 %	12,593,908	2,439,548	15,033,456	15,000,000
Transaction costs		<u>(1,871,277)</u>	<u>-</u>	<u>(1,871,277)</u>	<u>-</u>
		<u>\$30,391,822</u>	<u>\$ 6,101,487</u>	<u>\$36,493,309</u>	<u>\$ 37,330,600</u>

Transaction costs are incremental costs that are directly attributable to issuance of convertible debentures and include both fees and charges, brokerage fees and commissions, legal fees, advisor fees and similar costs. Transaction costs are amortized over the term of the debenture using the effective interest method. The transaction cost amortization for the three months ended June 30, 2010 amounted to \$97,217 (2009 - \$50,622) and the six months ended June 30, 2010 amounted to \$191,401 (2009 - \$99,113).

The accretion of the debt component for the three months ended June 30, 2010 was \$223,475 (2009 - \$144,322) and \$486,289 (2009 - \$289,127) for the six months ended June 30, 2010, which increases the debt component from the initial carrying amount, is included in financing expense on convertible debentures.

10 *Income taxes*

The expected tax rates applicable to SIFT's of 29.5% for 2011 and 28.0% for 2012 and later have been applied in the periods that temporary tax differences of the Trust are expected to reverse.

The future tax liability of the Trust and its wholly owned subsidiary corporations consists of the following:

	<u>June 30 2010</u>	<u>December 31 2009</u>
Tax liability related to difference in tax and book values	\$ 5,161,275	\$ 5,092,306
Tax asset related to deductible issue costs	(374,527)	(520,393)
Tax asset related to income tax loss carryforward	<u>(1,603,261)</u>	<u>(859,785)</u>
	<u>\$ 3,183,487</u>	<u>\$ 3,712,128</u>

TEMPLE REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2010

11 *Finance expense*

Financing costs are comprised of the following:

	Three Months Ended June 30		Six Months Ended June 30	
	2010	2009	2010	2009
Mortgage loan interest	\$ 2,724,132	\$ 2,651,687	\$ 5,357,232	\$ 5,317,533
Accretion of the debt component of convertible mortgage loan	20,911	-	41,306	-
Defeasance mortgage interest	-	71,203	64,172	144,645
Accretion of the debt component of convertible debentures	223,475	144,322	486,289	289,127
Interest on debentures	796,489	468,364	1,592,978	1,050,540
Amortization of transaction costs	232,801	195,895	518,168	399,833
Amortization of defeasance transaction costs	<u>3,708</u>	<u>10,226</u>	<u>14,664</u>	<u>20,219</u>
	<u>\$ 4,001,516</u>	<u>\$ 3,541,697</u>	<u>\$ 8,074,809</u>	<u>\$ 7,221,897</u>

12 *Per unit calculations*

Basic per unit information is calculated based on the weighted average number of units and deferred units (Note 15) outstanding for the period. Diluted per unit information is calculated based on the weighted average diluted number of units for the period, considering the potential exercise of outstanding unit options to the extent that the unit options are dilutive and the potential conversion of outstanding convertible debentures to the extent that the debentures are dilutive.

Income (loss) per unit calculations are based on the following:

	Three Months Ended June 30		Six Months Ended June 30	
	2010	2009	2010	2009
Income (loss) and diluted income (loss)	<u>\$ (762,054)</u>	<u>\$ 828,023</u>	<u>\$ (1,748,305)</u>	<u>\$ 1,666,398</u>
Weighted average number of units				
- basic and diluted	<u>12,849,395</u>	<u>12,828,589</u>	<u>12,846,903</u>	<u>12,822,131</u>

TEMPLE REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2010

12 *Per unit calculations (continued)*

The following securities were not included in the diluted net income per unit calculation as the effect would have been anti-dilutive.

	Exercise/Conversion Price	Number of units if converted or exercised at June 30, 2010
Unit options		
	\$ 3.00	7,666
	\$ 3.01	80,000
	\$ 5.00	109,000
	\$ 6.19	351,000
Convertible debentures		
Series A	\$ 5.75	428,609
Series B	\$ 7.50	2,648,813
Senior Secured	\$ 3.65	4,109,589
Convertible mortgage loan	\$ 15.00	300,000

13 *Trust units*

	Three Months Ended June 30, 2010		Six Months Ended June 30, 2010	
	Units	Amount	Units	Amount
Outstanding, beginning of period	12,825,352	\$ 62,490,094	12,825,352	\$ 62,491,116
Units issue costs	-	787	-	(235)
Outstanding, end of period	<u>12,825,352</u>	<u>\$ 62,490,881</u>	<u>12,825,352</u>	<u>\$ 62,490,881</u>
	Three Months Ended June 30, 2009		Six Months Ended June 30, 2009	
	Units	Amount	Units	Amount
Outstanding, beginning of period	12,825,352	\$ 62,687,492	12,812,019	\$ 62,590,168
Units issued on exercise of convertible debentures	-	-	13,333	85,597
Equity component of debentures converted	-	-	-	16,357
Unit issue costs	-	-	-	(4,630)
Outstanding, end of period	<u>12,825,352</u>	<u>\$ 62,687,492</u>	<u>12,825,352</u>	<u>\$ 62,687,492</u>

14 *Unit options*

Option plan

The Trust may grant options to trustees, senior officers, employees of the Trust or of a subsidiary of the Trust, management company employees of the Trust or any subsidiary of the Trust investor relations' consultants and technical consultants to the Trust.

The maximum number of units reserved for issuance under all securities compensation arrangements is limited to 10% of the total number of issued and outstanding units. The maximum number of units that may be issued to a participant shall not exceed 5% of the total number of issued and outstanding units provided that person is other than a consultant or person employed in investor relations activities and 2% of the total number of issued and outstanding units for all consultants and persons employed in investor relations activities.

TEMPLE REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2010

14 Unit options (continued)

The Trustees set the exercise price at the time that an option is granted under the plan, which exercise price shall not be less than the discounted market price of the shares. The discounted market price is the market price of the shares, less a discount, which shall not exceed 25% if the market price is \$0.50 or less, 20% if the market price is from \$0.51 to \$2.00, and 15% if the market price is above \$2.00 as determined under the policies of the Exchange.

The options have a maximum term of five years from the date of grant unless otherwise specifically provided by the Board of Trustees and authorized by the Exchange. For a participant employed in investor relations activities, no option shall be exercisable for a period exceeding 12 months from the date of grant, with no more than 1/4 of the options vesting in any three-month period.

Unit options

	Three Months Ended June 30, 2010		Six Months Ended June 30, 2010	
	Unit options	Weighted Average Exercise Price	Unit options	Weighted Average Exercise Price
Outstanding, beginning of period	547,666	\$ 5.44	467,666	\$ 5.86
Unit options granted during period	-	-	80,000	3.01
Unit options outstanding and vested, beginning and end of period	<u>547,666</u>	<u>\$ 5.44</u>	<u>547,666</u>	<u>\$ 5.44</u>
Weighted average remaining life (years)	<u>2.68</u>		<u>2.68</u>	
	Three Months Ended June 30, 2009		Six Months Ended June 30, 2009	
	Unit options	Weighted Average Exercise Price	Units	Weighted Average Exercise Price
Unit options outstanding and vested, beginning and end of period	<u>467,666</u>	<u>\$ 5.86</u>	<u>467,666</u>	<u>\$ 5.86</u>
Weighted average remaining life (years)	<u>3.35</u>		<u>3.35</u>	

On January 12, 2010, the Trust granted options to purchase 80,000 units at \$3.01 per unit. The options vest immediately and will expire five years from the date they were granted. The fair value of \$116,370 associated with the options issued, included in trust expense, was calculated using the Black-Scholes model for option valuation and charged to unit-based compensation, assuming a weighted average volatility of 200% on the underlying units, a dividend yield rate of 13.25% and the weighted average risk free interest rate (typically the Canada bond rate at the date of grant).

TEMPLE REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2010

15 *Deferred unit plan*

The Trust has a deferred unit plan available for trustees, officers, employees, or consultants of the Trust under which, any trustee, officer, employee, or consultants of the Trust have their annual bonus, annual board retainer or board meeting fees payable to that person by the Trust paid in the form of deferred units. The fair value based method of accounting is applied to all unit-based compensation. The fair value of deferred units granted is estimated on the date of grant using the market value of units of the Trust. Compensation expense is recognized when deferred units are granted. On the redemption of deferred units, the accumulated deferred unit value is credited to the units of the Trust.

The number of deferred units received by a participant is determined by dividing the amount of the annual bonus, annual board retainer or board meeting fees as applicable to be paid in the form of deferred units on that date by the fair market value of the Trust's units.

Deferred units granted to Trustees shall vest immediately. Deferred units granted to participants other than Trustees shall vest 33% on the first anniversary of grant, 33% on the second anniversary of grant, and 34% on the third anniversary of grant. In the event of any change of control, any unvested deferred units shall vest upon the earlier of the next applicable vesting date and the date that is immediately prior to the date upon which the change of control is completed. The board shall have the discretion to vary the manner in which deferred units vest for any participant.

The deferred units credited to a participant (including deferred units that have not yet vested) shall vest immediately and be redeemable by the participant following the termination other than for cause, retirement, or death, of the participant. In the event that a participant is terminated for cause, only the deferred units that have vested shall be redeemable and any unvested deferred units shall be cancelled.

Whenever cash distributions are paid on the units of the Trust, additional deferred units will be credited to the participant based on the number of deferred units held, the amount of the distribution and the market value of a unit of the Trust on the date of the distribution. Additional deferred units shall vest at the same time and on the same basis as the deferred units in respect of which they are credited.

Deferred units granted to Trustees totaled 6,259 (2009 - 4,585) units for the three months ended June 30, 2010 and 10,499 (2009 - 4,585) for the six months ended June 30, 2010. The Trust expensed \$17,003 for the three months ended June 30, 2010 (2009 - \$14,900) and \$29,203 (2009 - \$14,900) for the six months ended June 30, 2010 of unit based compensation related to the deferred unit plan which was included in Trust expenses in the consolidated statements of income and comprehensive income.

TEMPLE REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2010

16 *Related party transactions*

Asset management agreement

The Trust entered into an asset management agreement, for an initial term expiring October 1, 2011, with Shelter Canadian Properties Limited, a unitholder. The agreement provides for Shelter to receive an asset management fee of 1.5% of the gross revenues of the Trust and its subsidiaries on a consolidated basis. The asset management agreement requires Shelter to act as administrator of the Trust by providing accounting, human resource services, office space and equipment and the necessary clerical and secretarial personnel for the administration of the day-to-day activities of the Trust.

The Trust incurred service fees to Shelter Canadian Properties Limited of \$234,277 (2009 - \$253,967) for the three months ended June 30, 2010 and \$463,035 (2009 - \$515,635) for the six months ended June 30, 2009. Included in accounts payable and accrued liabilities is \$234,415 (2009 - \$245,750) due to Shelter Canadian Properties Limited.

17 *Investment in co-ownership*

During the 2002 fiscal year, Temple Gardens Mineral Spa Inc. entered into co-ownership of a Moose Jaw casino complex property. The co-ownership completed the development of a 23,400 square foot building and 140 parking stalls. The entire property is subject to a 25 year lease and the tenant must acquire ownership of the property at the end of the lease term for consideration of \$1. Under the terms of the lease, the tenant is responsible for all and every cost arising from or related to the leased premises, including the cost of replacement of the structure and foundation.

Pursuant to the terms of the co-ownership agreement, the co-owners each hold a 50% equity interest in the co-ownership, with all equity contributions, distributions, and net income allocations being made on this same 50% basis.

18 *Risk management and fair values*

Risk management

In the normal course of business, the Trust is exposed to financial risk that arises from its indebtedness, including fluctuations in interest rates and in the credit quality of its customers. Management's involvement in operations helps identify risks and variations from expectations. The Trust does not manage risk through the use of hedging transactions. As a part of the overall operation of the Trust, management takes steps to avoid undue concentrations of risk. The Trust manages the risks, as follows:

Liquidity risk

The Trust's principal liquidity needs arise from working capital requirements, debt servicing and repayment obligations, planned funding of maintenance, leasing costs and distributions to Unitholders, and possible property acquisition funding requirements. Revenues from hotel operations tend to fluctuate throughout the year, with greater demand in the last three quarters of the calendar year.

The above liquidity needs are funded from cash flows from operations, with the exception of debt repayment obligations and property acquisition funding requirements. These are funded from refinancing the Trust's maturing debt or financing unencumbered properties. The particular features and quality of the underlying assets being financed and the debt market parameters existing at the time will affect the success of this strategy. If this strategy is unsuccessful, other sources of funding include raising new equity by issuing Units. The risk with issuing new capital is that the capital markets may not be receptive to an equity issue with financial terms favourable to the Trust.

TEMPLE REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2010

18 Risk management and fair values (continued)

There is a risk that lenders will not refinance maturing debt on terms and conditions acceptable to the Trust or on any terms at all. The risk associated with the refinancing of maturing debt is mitigated as the maturity dates of the mortgage portfolio are staggered over a number of years. The following are the estimated maturities of the Trust's financial liabilities from continuing operations with convertible debentures disclosed at their face value as at June 30, 2010:

	<u>Total</u>	<u>1 year</u>	<u>2 years</u>	<u>3 years</u>	<u>4 years</u>	<u>5 years</u>	<u>Thereafter</u>
Accounts payable and accrued liabilities	\$ 4,812,859	\$ 4,812,859	\$ -	\$ -	\$ -	\$ -	\$ -
Long-term debt	172,211,384	55,255,749	10,588,444	72,865,607	23,235,965	7,219,030	3,046,589
Convertible debentures	<u>37,330,600</u>	<u>-</u>	<u>2,464,500</u>	<u>19,866,100</u>	<u>15,000,000</u>	<u>-</u>	<u>-</u>
Total	<u>\$214,354,843</u>	<u>\$60,068,608</u>	<u>\$13,052,944</u>	<u>\$92,731,707</u>	<u>\$38,235,965</u>	<u>\$ 7,219,030</u>	<u>\$ 3,046,589</u>

Interest rate risk

Interest rate risk is the risk that changes in market interest rates may have an effect on the cash flows associated with some financial instruments, known as interest rate cash flow risk, or on the fair value of other financial instruments, known as interest rate price risk.

Obtaining long-term mortgages with fixed interest rates minimizes interest rate cash flow risk.

Market risk

Market risk is the risk that changes in market prices will have an effect on future cash flows associated with financial instruments. Market risk comprises three types of risk: credit risk, currency risk, and other price risk.

Credit risk

Credit risk arises from the possibility that debtors may be unable to fulfill their commitments. For a financial asset, this is typically the gross carrying amount, net of any amounts offset and any impairment losses.

The Trust has credit policies to address credit risk, which are applied when granting credit and does include the analysis of the financial position of the debtor and review of credit limits. The Trust also does review credit history and credit performance as part of the credit accreditation process. An allowance for doubtful accounts or other impairment provisions are established based upon factors surrounding credit risk, historical trends and other information.

A financial asset is past due when a debtor has failed to make a payment when contractually due. The following is an aging of rents receivable past due but not impaired:

	<u>June 30 2010</u>	<u>December 31 2009</u>
Accounts receivable:		
0 to 30 days overdue	\$ 83,015	\$ 125,163
More than 30 days overdue	<u>150,154</u>	<u>112,897</u>
	<u>\$ 233,169</u>	<u>\$ 238,060</u>

TEMPLE REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2010

18 Risk management and fair values (continued)

The following is an analysis of bad debt charges to income included in hotel operating costs:

	Three Months Ended June 30		Six Months Ended June 30	
	2010	2009	2010	2009
Amounts charged to income	\$ 8,335	\$ (16,100)	\$ 17,535	\$ (12,400)
Percent of hotel revenue	0.05%	(0.10%)	0.06%	(0.04%)

Currency risk

Currency risk is the risk that changes in foreign exchange rates may have an effect on future cash flows associated with financial instruments. The Trust has no transactions denominated in foreign currency and is not exposed to foreign currency risk.

Other price risk

Other price risk is the risk that changes in market prices, including commodity or equity prices, will have an effect on future cash flows associated with financial instruments. The cash flows associated with financial instruments of the Trust are not exposed to other price risk.

Fair values

Financial instruments include cash, accounts receivable, investment in marketable securities, cash in escrow, defeasance assets, accounts payable, long-term debt, defeased liability, and the debt component of convertible debentures payable.

Fair value is an estimate of the amount at which items might be exchanged in an arm's length transaction between knowledgeable willing parties who are under no compulsion to act. Fair value should not be interpreted as an amount that could be realized in immediate settlement of the instruments. The estimate of fair value at the financial statement date may not represent fair values at any other date. The determination of fair value is affected by the use of judgment and by uncertainty.

Financial instruments carried at fair value include cash, marketable securities and cash in escrow. The methods used to establish fair value are summarized as follows:

- Quoted prices in active markets for identical assets or liabilities
- Use of a model with inputs other than quoted prices that are directly or indirectly observable market data

The following schedule summarizes the method used to determine the fair value of financial instruments.

	June 30, 2010		December 31, 2009	
	Quoted Prices	Observed Inputs	Quoted Prices	Observed Inputs
Cash	\$ 8,659,217	\$ -	\$ 7,439,955	\$ -
Marketable securities	280,800	324,758	303,450	324,758
Cash in escrow	1,648,945	-	767,467	-

The carrying values of accounts receivable, accounts payable, defeasance assets and defeased liability approximate fair value due to the short term nature of such financial instruments.

TEMPLE REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2010

18 *Risk management and fair values (continued)*

The carrying value of the long-term debt are impacted by changes in market yields which can result in differences between the carrying value and fair value of instruments. The fair value of long-term debt has been estimated based on the current market rates for debt with similar terms and conditions. The estimated fair value of long-term debt as at June 30, 2010 is \$177,319,466 (December 31, 2009 - \$175,832,017).

The carrying value of the debt components of convertible debentures payable are impacted by changes in market yields which can result in differences between the carrying value and fair value of instruments. The fair value of the debt component of convertible debentures payable has been estimated based on the current market rates for debentures with similar terms and conditions. The estimated fair value of the debt component of convertible debentures payable as at June 30, 2010 is \$35,296,201 (December 31, 2009 - \$34,066,577).

19 *Management of capital*

The capital structure of the Trust is comprised of the following:

	June 30 2010	December 31 2009
Mortgage debt	\$ 170,887,153	\$ 168,798,118
Convertible debentures	31,028,394	30,391,822
Unitholders' equity	<u>53,070,708</u>	<u>57,238,745</u>
Total	<u>\$ 254,986,255</u>	<u>\$ 256,428,685</u>

The Trust manages capital in order to safeguard its ability to continue as a going concern; to help ensure that returns are provided to Unitholders, and to help ensure an appropriate balance of risk and return.

The overall capital management strategy addresses the following considerations:

- The equity component of acquired properties is primarily funded from the proceeds of trust units or convertible debentures.
- Mortgage debt financing is arranged to optimize the leveraged returns from the hotel portfolio.
- Total mortgage debt financing is maintained within the overall debt limits as established by the Declaration of Trust. The Declaration of Trust allows total mortgage indebtedness of the Trust up to 75% of the appraised value of all properties.
- The Trust will endeavour to obtain a fixed rate of interest.
- Mortgage due dates are structured to reflect the nature of the properties being financed and debt maturity dates will be staggered, to the extent possible, in order to manage refinancing risk.

As of June 30, 2010 and December 31, 2009, total mortgage indebtedness was 54% of the appraised value of properties as at both dates. The individual property appraisals were prepared between 2007 and 2009.

TEMPLE REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2010

19 *Management of capital (continued)*

The Trust monitors capital from time-to-time using a variety of measures which are applicable to the hotel industry. Monitoring procedures are typically performed as a part of the overall management of operations and are performed with the goal of enhancing the ability of the Trust to access capital and/or reduce the cost of capital.

In order to maintain or adjust the capital structure the Trust may issue units, debentures or mortgage debt; adjust the amount of distributions paid to shareholders; return capital to shareholders; or reduce debt.

Market requirements for attracting capital may vary and may not be accurately predicted by the Trust.

20 *Commitments*

Operating lease agreements

The Trust is committed under the terms of operating lease agreements for occupancy and equipment with the following annual lease payments over the next four years.

2010	244,765
2011	489,530
2012	430,942
2013	138,000

Operating cost agreement

The Trust has entered into commitments to fix natural gas rates at \$8.85 per gigajoule at Temple Gardens Mineral Spa until October 2012. The commitments are in accordance with the Trust's expected usage requirements at this location.

Hotel management

Temple REIT has retained Atlific Hotels and Resorts to manage all of the hotels for its existing property portfolio. For the three and six months ended June 30, 2010, the Trust paid management fees of \$357,019 (2009 - \$370,071) and \$714,277 (2009 - \$736,785).