Consolidated Financial Statements
(In Canadian dollars)

NORTHWEST HEALTHCARE PROPERTIES REAL ESTATE INVESTMENT TRUST

Year ended December 31, 2011 and period from
March 25, 2010 to December 31, 2010

KPMG LLP
Chartered Accountants
Bay Adelaide Centre
333 Bay Street Suite 4600
Toronto ON M5H 2S5
Canada

Telephone (416) 777-8500
Fax (416) 777-8818
Internet www.kpmg.ca

INDEPENDENT AUDITORS' REPORT

To the Unitholders of NorthWest Healthcare
Properties Real Estate Investment Trust

We have audited the accompanying consolidated financial statements of NorthWest Healthcare Properties Real Estate Investment Trust, which comprise the consolidated balance sheets as at December 31, 2011, December 31, 2010 and March 25, 2010, the consolidated statements of income and comprehensive income, unitholders' equity and cash flows for the year ended December 31, 2011 and period from March 25, 2010 to December 31, 2010, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated 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 entity's 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 consolidated 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 consolidated financial statements present fairly, in all material respects, the consolidated financial position of NorthWest Healthcare Properties Real Estate Investment Trust as at December 31, 2011, December 31, 2010 and March 25, 2010, and its consolidated financial performance and its consolidated cash flows for the year ended December 31, 2011 and period from March 25, 2010 to December 31, 2010 in accordance with International Financial Reporting Standards.

KPMG LLP

Chartered Accountants, Licensed Public Accountants

February 29, 2012
Toronto, Canada

NORTHWEST HEALTHCARE PROPERTIES REAL ESTATE INVESTMENT TRUST

Consolidated Balance Sheets
(In Canadian dollars)

December 31, 2011, December 31, 2010 and March 25, 2010

	December 31, 2011	December 31, 2010	March 25, 2010
Assets			
Investment properties (note 4)	$ 985,384,439	$ 671,033,290	$ –
Goodwill (note 5)	4,457,894	4,457,894	–
Loan receivable (note 6)	8,000,000	–	–
Accounts receivable (note 7)	4,324,036	4,537,725	–
Other assets (note 8)	5,659,569	10,110,599	–
Restricted cash (note 9)	175,000	175,000	–
Cash and cash equivalents (note 10)	3,715,448	46,311,722	–
Total assets	$ 1,011,716,386	$ 736,626,230	$ –
Liabilities and Unitholders' Equity			
Liabilities:			
Mortgages payable (note 11)	$ 501,756,535	$ 372,051,861	$ –
Loans payable (note 12)	5,901,772	–	–
Class B exchangeable units (note 13)	87,502,624	89,787,921	–
Accounts payable and accrued liabilities	17,945,244	13,646,227	–
Distributions payable	2,348,919	1,839,145	–
Total liabilities	615,455,094	477,325,154	–
Unitholders' equity (note 14)	396,261,292	259,301,076	–
Commitments and contingencies (notes 18 and 21)			
Total liabilities and unitholders' equity	$ 1,011,716,386	$ 736,626,230	$ –

See accompanying notes to consolidated financial statements.

The consolidated financial statements were approved by the Board on February 29, 2012 and signed on its behalf by:

"Michael Knowlton" Trustee

"Peter Riggin" Trustee

NORTHWEST HEALTHCARE PROPERTIES REAL ESTATE INVESTMENT TRUST

Consolidated Statements of Income and Comprehensive Income
(In Canadian dollars)

Year ended December 31, 2011 and period from
March 25, 2010 to December 31, 2010

	2011	2010
Revenue from operations (note 18)	$ 118,152,010	$ 63,467,813
Property operating expenses (note 18)	53,675,024	28,816,529
Property operating income	64,476,986	34,651,284
Finance cost (note 20)	23,425,411	13,788,126
Interest income	(97,579)	(564,168)
Trust expenses	3,224,265	1,820,159
Income before finance cost (distributions on and fair value adjustment of Class B exchangeable units) and fair value adjustment of investment properties	37,924,889	19,607,167
Finance cost - Class B exchangeable unit distributions (note 20)	(6,118,823)	(4,762,167)
Finance cost - fair value adjustment of Class B exchangeable units (notes 13 and 20)	1,509,417	(13,083,309)
Fair value adjustment of investment properties (note 4)	45,025,562	833,242
Net income and comprehensive income	$ 78,341,045	$ 2,594,933

See accompanying notes to consolidated financial statements.

NORTHWEST HEALTHCARE PROPERTIES REAL ESTATE INVESTMENT TRUST

Consolidated Statements of Unitholders' Equity
(In Canadian dollars)

Year ended December 31, 2011	Unit capital	Retained earnings (deficit)	Total
Unitholders' equity, January 1, 2011	$ 269,759,615	$ (10,458,539)	$ 259,301,076
Public offering, net of costs (note 14(a))	82,439,772	–	82,439,772
Exchange of Class B exchangeable units (note 13)	775,880	–	775,880
Total net income and comprehensive income	–	78,341,045	78,341,045
Distributions	–	(27,087,978)	(27,087,978)
Distribution reinvestment plan (note 14(b))	2,491,497	–	2,491,497
Unitholders' equity, December 31, 2011	$ 355,466,764	$ 40,794,528	$ 396,261,292

Period from March 25, 2010 to December 31, 2010	Unit capital	Retained earnings (deficit)	Total
Unitholders' equity, March 25, 2010	$ –	$ –	$ –
Public offerings, net of costs (note 14(a))	253,988,472	–	253,988,472
Units issued on acquisition (note 3)	14,725,000	–	14,725,000
Exchange of Class B exchangeable units (note 13)	793,108	–	793,108
Total net income and comprehensive income	–	2,594,933	2,594,933
Distributions	–	(13,053,472)	(13,053,472)
Distribution reinvestment plan (note 14(b))	253,035	–	253,035
Unitholders' equity, December 31, 2010	$ 269,759,615	$ (10,458,539)	$ 259,301,076

Distributions per unit during the year ended December 31, 2011 - $0.80 (period from March 25, 2010 to December 31, 2010 - $0.615).

See accompanying notes to consolidated financial statements.

NORTHWEST HEALTHCARE PROPERTIES REAL ESTATE INVESTMENT TRUST

Consolidated Statements of Cash Flows
(In Canadian dollars)

Year ended December 31, 2011 and period from
March 25, 2010 to December 31, 2010

	2011	2010
Cash provided by (used in):		
Operating activities:		
Net income	$ 78,341,045	$ 2,594,933
Adjustments for:		
Finance cost (note 20)	28,034,817	31,633,602
Interest income	(97,579)	(564,168)
Fair value adjustment of investment properties	(45,025,562)	(833,242)
Change in non-cash operating items (note 22)	386,294	4,453,126
Cash generated from operating activities	61,639,015	37,284,251
Interest paid	(23,337,035)	(13,671,377)
Interest paid - Class B exchangeable units	(6,123,170)	(4,250,092)
Interest received	82,784	547,042
Net cash from operating activities	32,261,594	19,909,824
Investing activities:		
Acquisition of a business (note 3)	–	(105,624,502)
Acquisition of investment properties (note 3)	(217,682,498)	(52,706,731)
Additions to investment properties (note 4)	(13,069,452)	(9,644,047)
Loan receivable advance	(8,000,000)	–
Deposits on investment properties under contract	5,150,000	(6,800,000)
Net cash used in investing activities	(233,601,950)	(174,775,280)
Financing activities:		
Proceeds from issuance of units, net of issue costs	82,442,580	253,988,472
Distributions	(24,086,707)	(10,961,292)
Mortgage advances	155,275,000	14,000,000
Repayment of mortgages	(59,945,684)	(52,423,023)
Secured credit facility advance	66,500,000	16,500,000
Secured credit facility repayment	(60,500,000)	(16,500,000)
Secured interim bridge facility advances	95,000,000	–
Repayment of interim bridge facility	(95,000,000)	–
Repayment of acquired bank indebtedness	–	(2,790,787)
Transaction costs	(941,107)	(636,192)
Net cash from financing activities	158,744,082	201,177,178
Increase (decrease) in cash and cash equivalents	(42,596,274)	46,311,722
Cash and cash equivalents, beginning of period (note 10)	46,311,722	–
Cash and cash equivalents, end of period (note 10)	$ 3,715,448	$ 46,311,722

See accompanying notes to consolidated financial statements.

NorthWest Healthcare Properties Real Estate Investment Trust (the "REIT") is a Canadian unincorporated open-ended real estate investment trust created pursuant to the Declaration of Trust dated January 1, 2010, as amended on March 25, 2010. The REIT commenced operations on March 25, 2010 when it issued units for cash pursuant to an initial public offering (the "IPO") and acquired a portfolio of 45 buildings or healthcare real estate commercial properties (note 3). The REIT invests primarily in real properties operated as medical offices in Canada. The registered office of the REIT is 284 King Street East, Suite 100, Toronto, Ontario, M5A 1K4.

1. Basis of preparation:

(a) Statement of compliance:

The consolidated financial statements of the REIT have been prepared by management in accordance with International Financial Reporting Standards ("IFRS"). These are the REIT's first consolidated financial statements prepared in accordance with IFRS and IFRS 1, First-time Adoption of International Financial Reporting Standards ("IFRS 1"), has been applied.

The disclosures required by IFRS 1 concerning the transition from Canadian generally accepted accounting principles ("Canadian GAAP") to IFRS are given in note 26. The REIT commenced operations on March 25, 2010 and the date of transition to IFRS is March 25, 2010 (the "Transition Date"). Note 26 includes reconciliations of equity and total comprehensive income for comparative periods reported under Canadian GAAP to amounts reported under IFRS.

(b) Basis of measurement:

The consolidated financial statements have been prepared on the historical cost basis, except for investment properties and the Class B exchangeable units which are stated at fair value.

The consolidated financial statements are presented in Canadian dollars, which is the REIT's functional currency.

1. Basis of preparation (continued):

(c) Significant judgements and key estimates:

The following are significant judgements and key estimates that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the period:

(i) Leases (the REIT as lessor):

The REIT uses judgement in assessing the classification of its leases with tenants as operating leases, in particular with long-term leases in single tenant properties. The REIT has determined that all its leases are operating leases.

(ii) Property valuations:

Investment properties, which are carried on the consolidated balance sheets at fair value, are valued by qualified external valuation professionals or management.

The valuations are based on a number of assumptions, such as appropriate discount rates and estimates of future rental income, operating expenses and capital expenditures. The valuation of investment properties is one of the principal estimates and uncertainties of the REIT. Refer to note 4 for further information on estimates and assumptions made in the determination of the fair value of investment properties.

(iii) Accounting for acquisitions:

Management must assess whether the acquisition of a property should be accounted for as an asset purchase or business combination. This assessment impacts the treatment of transaction costs, the acquisition accounting and whether or not goodwill is recognized. With the exception of the acquisition of the portfolio of 45 properties acquired at the time of the REIT's IPO, which was determined to be a business combination, the REIT's acquisitions are generally determined to be asset purchases as the REIT does not acquire an integrated set of processes as part of the transaction.

1. Basis of preparation (continued):

(iv) Goodwill:

Estimates are used when testing goodwill for impairment. Refer to note 5 for further information on estimates and assumptions made when testing goodwill for impairment.

(v) Income taxes:

The REIT is a mutual fund trust and a real estate investment trust pursuant to the Income Tax Act (Canada). Under current tax legislation, a real estate investment trust 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 Income Tax Act (Canada) relating to the nature of its assets and revenue (the "REIT Conditions"). The REIT has reviewed the REIT Conditions and has assessed their interpretation and application to the REIT's assets and revenue, and it has determined that it qualifies as a real estate investment trust for the period.

The REIT expects to continue to qualify as a real estate investment trust under the Income Tax Act (Canada), however, should it no longer qualify it would not be able to flow through its taxable income to unitholders and the REIT would therefore be subject to tax.

2. Significant accounting policies:

(a) Basis of consolidation:

The consolidated financial statements include the accounts of the REIT and its consolidated subsidiaries which are the entities over which the REIT has control. Control exists when the REIT has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

2. Significant accounting policies (continued):

Subsidiaries are fully consolidated from the date of acquisition, being the date on which the REIT obtains control, and continue to be consolidated until the date when such control ceases. The financial statements of the subsidiaries are prepared for the same reporting period as the REIT, using consistent accounting policies. All intra-group balances, transactions, unrealized gains and losses resulting from intra-group transactions and distributions are eliminated in full.

(b) Investment properties:

Investment properties include medical office properties that are held to earn rental income and properties that are being developed or constructed for use as investment properties. They are recognized initially at cost and subsequently at fair value, with changes in fair value recognized in the consolidated statements of comprehensive income in the period in which they arise.

Subsequent capital expenditures are added to the carrying value of investment property only when it is probable that future economic benefits of the expenditure will flow to the REIT and the cost can be measured reliably.

Leasing costs incurred by the REIT that are incremental and directly attributable to negotiating and arranging tenant leases are added to the carrying value of investment properties. Leasing costs that are not incremental are expensed in the period incurred.

(c) Goodwill:

The REIT measures goodwill arising in a business combination at the acquisition date as the fair value of the consideration transferred less the net recognized amount (generally fair value) of the identifiable assets acquired and liabilities assumed, all measured as of the acquisition date. Where the fair value of net assets acquired in a business combination exceeds the consideration transferred, the excess, known as bargain purchase gain, is recognized immediately in the consolidated statements of comprehensive income.

---

2. Significant accounting policies (continued):

For the purposes of goodwill impairment testing, goodwill acquired in a business combination is allocated to the group of assets or cash-generating units ("CGUs"), that are expected to benefit from the synergies of the combination. This allocation reflects the lowest level at which that goodwill is monitored for internal reporting purposes.

Goodwill is reviewed for impairment at least annually, and the recoverable amount of the CGU (or group of CGUs) containing goodwill is estimated each year at the same time. The recoverable amount of a CGU is the greater of its value in use and its fair value less costs to sell. An impairment loss is recognized if the carrying amount of the CGU exceeds its estimated recoverable amount. Any impairment loss is recognized immediately in the consolidated statements of comprehensive income. Impairment losses recognized in respect of CGUs are allocated first to reduce the carrying amount of any goodwill allocated to the CGU, and then to reduce the carrying amounts of the other assets in the CGU (group of CGUs) on a pro rata basis. An impairment loss is not subsequently reversed.

(d) Cash and cash equivalents:

Cash and cash equivalents include unrestricted cash and short-term investments. Short-term investments, comprising money market instruments, have a maturity of 90 days or less at their date of purchase and are stated at cost, which approximates fair value.

(e) Revenue recognition:

(i) Revenue from investment properties:

Revenue from investment properties includes base rent, realty tax and operating cost recoveries, parking and other incidental income. Base rent is recognized over the lease term. Realty tax and operating cost recoveries are recognized in the period in which the recoverable costs are charged to the tenant. Parking and other incidental income are recognized at the time the service is provided.

As a lessor, the REIT has retained the risks and benefits of its investment properties and assessed its leases with tenants as operating leases.

2. Significant accounting policies (continued):

Certain leases call for rental payments that vary significantly over their term due to changes in rates or rent inducements granted to tenants. The rental revenue from these leases is recognized on a straight-line basis, resulting in accruals for rent that are not billable or due until future years. These straight-line rent amounts are presented as accrued rent receivable and form a component of investment property.

(ii) Management fees:

Property management fees are recognized at the time the service is provided.

(f) Leasing costs:

Payments to tenants under lease contracts are characterized as either tenant improvements, which enhance the value of the property, or lease inducements. When the obligation is determined to be a tenant improvement, the REIT is considered to have acquired an asset. Accordingly, the tenant improvements are capitalized as part of investment property. When the obligation is determined to be a lease inducement, the amount is recognized as an asset which forms a component of investment property and is amortized over the term of the lease as a reduction of revenue.

(g) Compensation expense:

Compensation expense obligations are measured on an undiscounted basis and are expensed as the related service is provided. A liability is recognized for the amount expected to be paid under short-term cash bonus or deferred unit plan.

(h) Unit-based compensation:

The REIT has a deferred unit plan, which provides holders with the right to receive REIT units which are puttable. The REIT estimates the fair value of the deferred units at the service commencement date. The unit-based compensation expense is amortized over the vesting period commencing on the service commencement date. The awards are fair valued on the basis of the unit price at each reporting period and the change in fair value of the amortized unit-based compensation expense is recognized as unit-based compensation expense.

---

2. Significant accounting policies (continued):

(i) Income taxes:

The REIT is a mutual fund trust and a real estate investment trust pursuant to the Income Tax Act (Canada). Under current tax legislation, a real estate investment trust is not liable to pay Canadian income tax provided that its taxable income is fully distributed to unitholders each year. 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. Accordingly, no current or deferred income taxes have been recognized in the consolidated financial statements.

The REIT's corporate subsidiaries are subject to tax on their taxable income. Income taxes for corporate subsidiaries are accounted for using the asset and liability method, whereby deferred income tax assets and liabilities are determined based on the differences between the carrying amount of the balance sheet items and their corresponding tax values. Income taxes are computed using enacted and substantively enacted corporate income tax rates for the periods in which tax and accounting basis differences are expected to reverse. Adjustments to these balances are recognized in income as they occur.

(j) Class B exchangeable units:

The Class B exchangeable units of a subsidiary of the REIT are exchangeable into REIT units at the option of the holder. In accordance with International Accounting Standard ("IAS") 32, Financial Instruments: Presentation, the Class B exchangeable units are considered puttable instruments and are required to be classified as financial liabilities. Further, the Class B exchangeable units are classified as fair value through profit or loss financial liabilities and are measured at fair value each reporting period with any changes in fair value recognized in the consolidated statements of income and comprehensive income as finance cost. The distributions paid on the Class B exchangeable units are accounted for as a finance cost (note 20).

2. Significant accounting policies (continued):

(k) Financial instruments:

Financial instruments are classified as one of the following: (i) fair value through profit and loss, (ii) loans and receivables, (iii) held-to-maturity, (iv) available-for-sale, or (v) other liabilities. Financial instruments are recognized initially at fair value. Financial assets and liabilities classified at fair value through profit and loss are subsequently measured at fair value with gains and losses recognized in the consolidated statements of comprehensive income. Financial instruments classified as held-to-maturity, loans and receivables or other liabilities are subsequently measured at amortized cost. Available-for-sale financial instruments are subsequently measured at fair value and any unrealized gains and losses are recognized through other comprehensive income and presented in the fair value reserve in equity.

The REIT designated its restricted cash, and cash and cash equivalents, loan receivable, accounts receivable, mortgage escrow, deposits on investment properties under contract and other deposits as loans and receivables; and mortgages payable, loans payable, accounts payable and accrued liabilities as other liabilities. The Class B exchangeable units are classified as fair value through profit and loss. The REIT has neither available-for-sale nor held-to-maturity instruments.

Transaction costs that are directly attributable to the acquisition or issuance of financial assets or liabilities, other than financial assets and liabilities measured at fair value through profit and loss, are accounted for as part of the carrying amount of the respective asset or liability at inception.

Transaction costs on financial assets and liabilities measured at fair value through profit and loss are expensed in the period incurred.

Transaction costs related to financial instruments measured at amortized cost are amortized using the effective interest rate over the anticipated life of the related instrument.

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

(l) Unit capital:

The REIT's units are considered liability instruments under IFRS because of the features inherent in the open-ended trust structure. However, the units are the most subordinate class of units and, therefore, may be presented as equity under IFRS. External costs directly attributable to the issue of new units are shown in unitholders' equity as a deduction from the proceeds.

(m) Future accounting changes:

(i) IFRS 9, Financial Instruments (2010) ("IFRS 9 (2010)"), supersedes IFRS 9 (2009) and is effective for annual periods beginning on or after January 1, 2015, with early adoption permitted. For annual periods beginning before January 1, 2015, either IFRS 9 (2009) or IFRS 9 (2010) may be applied.

The REIT intends to adopt IFRS 9 (2010) in its financial statements for the annual period beginning on January 1, 2015. The extent of the impact of adoption of IFRS 9 (2010) has not yet been determined.

(ii) The REIT does not expect the amendments to IFRS 7, Disclosures - Transfers of Financial Assets ("IFRS 7"), to have a material impact on the financial statements because of the nature of the REIT's operations and the types of financial assets that it holds.

(iii) The REIT intends to adopt IFRS 10, Consolidated Financial Statements ("IFRS 10"), in its financial statements for the annual period beginning on January 1, 2013. The REIT does not expect IFRS 10 to have a material impact on the financial statements.

(iv) The REIT intends to adopt IFRS 12, Disclosure of Interest in Other Entities, in its financial statements for the annual period beginning on January 1, 2013. The REIT does not expect the amendments to have a material impact on the financial statements because of the nature of the REIT's interests in other entities.

2. Significant accounting policies (continued):

(v) The REIT intends to adopt IFRS 13, Fair Value Measurements ("IFRS 13"), prospectively in its financial statements for the annual period beginning on January 1, 2013. The extent of the impact of adoption of IFRS 13 has not yet been determined.

(vi) The REIT intends to adopt the amendments to IAS 1, Presentation of Financial Statements, in its financial statements for the annual period beginning on January 1, 2013. The extent of the impact of adoption of the amendments has not yet been determined.

(vii) The REIT intends to adopt the amendments to IAS 32, Financial Instruments - Presentation ("IAS 32"), and IFRS 7 in its financial statements for the annual period beginning on January 1, 2013, and the amendments to IAS 32 in its financial statements for the annual period beginning January 1, 2014. The extent of the impact of adoption of the amendments has not yet been determined.

(viii) The International Accounting Standards Board has published some limited scope amendments to IAS 12, Income Taxes ("IAS 12"), which are relevant only when an entity uses the fair value model for measurement in IAS 40, Investment Property. Under IAS 12, the measurement of deferred tax liabilities and deferred tax assets depends on whether an entity expects to recover an asset by using it or by selling it. To provide a practical approach in such cases, the amendment introduces a presumption that an investment property is recovered entirely through sale. This policy is effective for fiscal years after January 1, 2012; however, earlier adoption is permitted, including on transition to IFRS. The REIT has applied this policy effective March 25, 2010.

(In Canadian dollars)

3. Acquisitions:

(a) Acquisitions during the year ended December 31, 2011:

During the year ended December 31, 2011, the REIT subsidiaries acquired nine investment properties for net cash consideration of $217,682,498. The acquisitions of the investment properties, and related assets and liabilities have been accounted for as asset purchases. The recognized amount of assets acquired and liabilities assumed were as follows:

Assets	
Investment properties	$ 255,058,177
Accounts receivable and other assets	314,042
	255,372,219
Liabilities	
Accounts payable and accrued liabilities	1,895,501
Assumed mortgages, including mark-to-market adjustment	35,794,220
	37,689,721
Net assets acquired for cash	$ 217,682,498

(In Canadian dollars)

3. Acquisitions (continued):

(b) Acquisitions during the period from March 25, 2010 to December 31, 2010:

(i) On March 25, 2010, subsidiaries of the REIT indirectly acquired from NorthWest Operating Trust ("NW Operating Trust") 45 commercial properties through its acquisition of Healthcare Properties LP ("HPLP") for a net purchase price of $171,899,206. The assets acquired and liabilities assumed have been accounted for as a business combination using the acquisition method of accounting. The REIT measures goodwill at the acquisition date as the fair value of the consideration transferred less the net recognized amount (generally fair value) of the identifiable assets acquired and liabilities assumed. The value of goodwill at the date of acquisition relates to the portfolio premium, attributed to acquiring an integrated portfolio in a single transaction, and the management platform that includes acquisitions, leasing, management, finance and accounting personnel systems. The recognized amounts of the assets acquired and liabilities assumed are as follows:

Assets	
Investment properties	$ 538,390,331
Goodwill	4,457,894
Other assets	5,127,932
	547,976,157
Liabilities	
Bank indebtedness	2,787,672
Assumed mortgages, including mark-to-market adjustments	358,487,430
Accounts payable and accrued liabilities	14,309,659
Unearned revenue	492,190
	376,076,951
Net assets acquired	$ 171,899,206
Consideration transferred indirectly by the REIT:	
Class B exchangeable units of NHP Holdings Limited Partnership ("NHP") (note 13)	$ 77,497,720
Cash	105,624,502
Due from NW Operating Trust	(11,223,016)
Total consideration transferred	$ 171,899,206

(In Canadian dollars)

3. Acquisitions (continued):

The amount due from NW Operating Trust in relation to this acquisition has been settled.

Immediately following the acquisition of HPLP, the REIT repaid $47,744,567 of the assumed mortgages.

(ii) During the period from March 25, 2010 to December 31, 2010, the REIT acquired five investment properties and two pieces of land adjacent to investment properties owned by the REIT for net consideration of $66,780,084. Included in this amount is net consideration of $28,831,278 related to the acquisition of one investment property and adjacent land from an affiliate of NW Operating Trust. The acquisition of investment properties and the related assets and liabilities have been recognized as asset purchases. The recognized amount of assets acquired and liabilities assumed were as follows:

Assets	
Investment properties	$ 121,652,060
Other assets	317,322
	121,969,382
Liabilities	
Bank indebtedness	3,115
Assumed mortgages, including mark-to-market adjustments	52,613,675
Account payable and accrued liabilities	2,572,508
	55,189,298
Net assets acquired	$ 66,780,084
Consideration given by the REIT:	
REIT units	$ 14,725,000
Cash	52,706,731
Due from NW Operating Trust (note 17)	(651,647)
Total consideration paid	$ 66,780,084

The amount due from NW Operating Trust in relation to these acquisitions have been settled.

(In Canadian dollars)

4. Investment properties:

Balance, January 1, 2011	$ 671,033,290
Acquisitions of investment properties	255,058,177
Additions	13,069,452
Increase in straight-line rents	1,197,958
Fair value adjustment	45,025,562
Balance, December 31, 2011	$ 985,384,439
Balance, March 25, 2010	$ –
Acquired in a business combination	538,390,331
Acquisitions of investment properties	121,652,060
Additions	9,589,107
Increase in straight-line rents	568,550
Fair value adjustment	833,242
Balance, December 31, 2010	$ 671,033,290

The REIT determined the fair value of each investment property using the discounted cash flow method. The discounted cash flow method discounts the expected future cash flows, generally over a term of 10 years, including a terminal value based on the application of a capitalization rate to estimated year 11 cash flows.

The key valuation assumptions as at December 31 for the REIT's commercial properties are set out in the following table:

	2011	2010
Discount rates - range	7.0% - 11.0%	7.8% - 11.0%
Discount rate - weighted average	8.0%	8.6%
Terminal capitalization rate - range	6.0% - 10.3%	7.0% - 10.3%
Terminal capitalization rate - weighted average	7.1%	7.8%

The fair values of investment properties are most sensitive to changes in discount rates and terminal capitalization rates. As at December 31, 2011, a 25-basis-point movement in the weighted average portfolio discount rate and terminal capitalization rate, would change the value of investment property by $36,000,000.

(In Canadian dollars)

4. Investment properties (continued):

The discounted cash flows reflect rental income from current leases and assumptions about rental income from future leases reflecting market conditions at the reporting date, less future cash outflows in respect of such leases.

Commercial properties with an aggregate fair value of $263,450,000 at December 31, 2011 (December 31, 2010 - nil; March 25, 2010 - nil) were valued by external valuation professionals with recognized and relevant professional qualification.

5. Goodwill:

Balance, December 31, 2011 and January 1, 2011	$ 4,457,894

Balance, March 25, 2010	$ –
Arising on business combination	4,457,894
Balance December 31, 2010	$ 4,457,894

HPLP is the lowest level within the entity where goodwill is monitored for internal management purposes; this is the level where all the properties and management company reside. Since goodwill cannot be allocated on a non-arbitrary basis, it has been allocated to a group of CGUs represented by the individual CGUs forming HPLP. The impairment test of goodwill at the HPLP level is based on fair value less cost-to-sell ("FVLCS").

FVLCS is based on management's determination of the business enterprise fair value of HPLP based on external sources of information that are used by the market to value the business in the real estate industry. Management has estimated its costs to sell based on market transaction for real estate transactions.

(In Canadian dollars)

6. Loan receivable:

	2011	2010
Loan receivable	$ 8,000,000	$ –

On December 23, 2011, the REIT funded a loan on a recently constructed property owned by a joint venture in which an affiliate of NW Operating Trust has a 50% interest.

The loan receivable has an interest rate of 7.5% and is repayable the earlier of:

(i) June 21, 2013;

(ii) the date of the sale of the property; or

(iii) as agreed with the borrower.

No principal amounts are due prior to maturity of the loan.

The loan is secured by a pledge of the partnership interest of the joint venture partners and guaranteed by the partners; each limited to 50% of the obligations under the loan.

Under the terms of the loan, the REIT has a right of first offer to acquire the property.

7. Accounts receivable:

	2011	2010
Tenant and other receivables	$ 3,359,987	$ 2,842,486
Due from NW Operating Trust (note 17)	964,049	1,695,239
	$ 4,324,036	$ 4,537,725

(In Canadian dollars)

8. Other assets:

	2011	2010
Prepaid expenses	$ 1,865,967	$ 1,394,981
Mortgage escrow	604,353	603,954
Deposits on investment properties under contract	1,850,000	7,000,000
Other deposits	839,782	815,116
Other	499,467	296,548
	$ 5,659,569	$ 10,110,599

9. Restricted cash:

Restricted cash represents an earn-out reserve, subject to meeting certain occupancy requirements, on a first mortgage on one of the REIT's properties.

10. Cash and cash equivalents:

	2011	2010
Cash at bank	$ 1,716,188	$ 2,740,352
Short-term deposits	1,999,260	43,571,370
	$ 3,715,448	$ 46,311,722

Short-term deposits consist of money market instruments and have a maturity of 90 days or less at their date of purchase.

(In Canadian dollars)

11. Mortgages payable:

All mortgages are secured by first or second charges on specific investment properties, with a carrying value of $863,770,097 at December 31, 2011, and are repayable as follows:

	Scheduled principal payments	Debt maturing during the year	Total mortgages payable
2012	$ 11,260,714	$ 10,028,231	$ 21,288,945
2013	10,931,936	60,166,146	71,098,082
2014	9,737,584	47,594,815	57,332,399
2015	8,340,914	56,117,405	64,458,319
2016	7,794,940	94,029,878	101,824,818
2017 and thereafter	16,359,808	166,796,788	183,156,596
Face value	$ 64,425,896	$ 434,733,263	499,159,159
Mark-to-market adjustment			3,066,964
Unamortized financing costs			(469,588)
Carrying amount			$ 501,756,535

	2011	2010
Mortgages at fixed rates - contractual amount	$ 499,159,159	$ 369,730,062
Mark-to-market adjustment	3,066,964	2,445,647
Unamortized financing costs	(469,588)	(123,848)
Carrying amount	$ 501,756,535	$ 372,051,861
Interest rates	3.40% - 6.53%	4.77% - 6.53%
Weighted average interest rate	5.22%	5.54%

12. Loans payable:

(a) Secured floating rate revolving credit facility:

The REIT has a floating rate revolving credit facility of $35,000,000 which expires on March 25, 2013. The facility bears interest at bankers' acceptance plus 2.75% or prime plus 1.75% and is secured by certain investment properties, with a carrying value of $73,844,000 at December 31, 2011, and the terms of a general security agreement. As at December 31, 2011, there was $5,901,772 outstanding on the credit facility net of unamortized financing costs of $98,228.

The credit facility was renegotiated and extended during the three months ended March 31, 2011. Prior to the extension, the credit facility of $35,000,000 bore interest at bankers' acceptance rate plus 3.5% or prime plus 2.5% and expired on March 25, 2011. As at December 31, 2010, there was nil outstanding balance on the credit facility. Unamortized financing costs of $125,113 related to the credit facility are included in prepaid expenses as at December 31, 2010.

(b) Senior secured interim bridge facility:

During the three months ended March 31, 2011, the REIT had obtained an $85,000,000 non-revolving senior secured interim bridge facility to fund the acquisition of certain investment properties. The interim bridge facility bore interest at the bankers' acceptance rate plus 3.5% or prime plus 2.5% and was secured by certain acquired properties. During the three months ended March 31, 2011, the REIT repaid $80,000,000 of the facility. The interim bridge facility was then amended such that the total commitment was reduced to $15,000,000 and the lender re-advanced $10,000,000. During the three months ended June 30, 2011, the REIT repaid $15,000,000 of the facility. As at December 31, 2011, the facility has expired and there is no outstanding balance.

(In Canadian dollars)

13. Class B exchangeable units:

Each Class B exchangeable unit of NHP, a subsidiary of the REIT, is exchangeable into one unit of the REIT. The Class B exchangeable units are economically equivalent to REIT units and are entitled only to receive distributions equal to those provided to holders of REIT units.

Class B exchangeable units outstanding:

	Units	Amount
Units issued, January 1, 2011	7,680,746	$ 89,787,921
Fair value adjustment of Class B exchangeable units (note 20)	–	(1,509,417)
Class B exchangeable units exchanged for REIT units	(65,200)	(775,880)
Units issued, December 31, 2011	7,615,546	$ 87,502,624
Class B exchangeable units issued, March 25, 2010	–	$ –
Class B exchangeable units of NHP issued	7,749,772	77,497,720
Fair value adjustment of Class B exchangeable units (note 20)	–	13,083,309
Class B exchangeable units exchanged for REIT units	(69,026)	(793,108)
Units issued, December 31, 2010	7,680,746	$ 89,787,921

During the year ended December 31, 2011, the REIT recognized $6,118,823 (period from March 25, 2010 to December 31, 2010 - $4,762,167) of distributions declared on Class B exchangeable units as finance cost.

14. Unitholders' equity:

The REIT is authorized to issue two categories of equity: (a) REIT units; and (b) special voting units attached to the Class B exchangeable units of NHP, a subsidiary of the REIT.

The REIT is authorized to issue an unlimited number of REIT units without par value. Each unit represents a single vote at any meeting of unitholders and entitles the unitholder to receive a pro rata share of all distributions. The unitholders have the right to require the REIT to redeem their units on demand. Upon receipt of the redemption notice by the REIT, all rights to and under the units tendered for redemption shall be surrendered and the holder thereof shall be entitled to receive a price per unit ("Redemption Price"), as determined by a market formula.

(In Canadian dollars)

14. Unitholders' equity (continued):

The Redemption Price will be paid in accordance with the conditions provided for in the Declaration of Trust.

The special voting units are only issued in tandem with Class B exchangeable units and are not transferable separately from the Class B exchangeable units to which they are attached. As Class B exchangeable units are exchanged or surrendered for REIT units, the corresponding special voting units will be cancelled for no consideration. Special voting units have no economic entitlement in the REIT, but entitle the holder to one vote per special voting unit at any meeting of the unitholders.

The REIT's Trustees have discretion in declaring distributions.

(a) Units outstanding:

	Units	Amount
Units issued, January 1, 2011	27,585,791	$ 269,759,615
Follow-on equity offering	6,400,000	75,200,000
Follow-on equity offering over-allotment option	960,000	11,280,000
Units issued on exchange of Class B exchangeable units	65,200	775,880
Distribution reinvestment plan	221,032	2,491,497
Units issued	35,232,023	359,506,992
Less issue costs	–	4,040,228
Units issued, December 31, 2011	35,232,023	$ 355,466,764

(In Canadian dollars)

14. Unitholders' equity (continued):

	Units	Amount
Units issued, March 25, 2010	–	$ –
Issuance of units through initial public offering	17,500,000	175,000,000
Issuance of units over-allotment option	1,250,000	12,500,000
Follow-on equity offering	6,495,000	75,017,250
Follow-on equity offering over-allotment option	974,250	11,252,588
Units issued on acquisition of investment property	1,274,891	14,725,000
Units issued on exchange of Class B exchangeable units	69,026	793,108
Distribution reinvestment plan	22,624	253,035
Units issued	27,585,791	289,540,981
Less issue costs	–	19,781,366
Units issued, December 31, 2010	27,585,791	$ 269,759,615

(b) Distribution reinvestment plan:

The REIT has established a distribution reinvestment plan for its unitholders, which allows participants to reinvest their monthly cash distributions in additional units at an effective discount of 3%.

15. Deferred unit plan:

In order to align the interest between the Trustees and certain officers of the REIT, there may be grants of deferred units under the deferred unit plan. Under the plan, the maximum number of units authorized for issuance shall not exceed 5% of the units issued and outstanding at any given time. The deferred units vest as follows:

- 50% of the deferred units on the third anniversary of the award date;
- 25% of the deferred units on the fourth anniversary of the award date; and
- 25% of the deferred units on the fifth anniversary of the award date.

(In Canadian dollars)

15. Deferred unit plan (continued):

(a) Liability:

January 1, 2011	$ 69,732
Unit-based compensation expense	672,883
December 31, 2011	$ 742,615
March 25, 2010	$ –
Unit-based compensation expense	69,732
December 31, 2010	$ 69,732

(b) Units outstanding:

January 1, 2011	10,806
Granted during the year	78,061
Distribution entitlement	3,852
December 31, 2011	92,719
Vested, but not issued, December 31, 2011	–

March 25, 2010	–
Granted during the period	10,806
December 31, 2010	10,806
Vested, but not issued, December 31, 2010	–

15. Deferred unit plan (continued):

For the year ended December 31, 2011, 78,061 units were granted under the deferred unit plan at an average unit price of $11.55. For the period from March 25, 2010 to December 31, 2010, there were 10,806 units granted under the deferred unit plan at an average unit price of $11.31.

Unit-based compensation expense is measured at the service commencement date, based on the fair market value of a REIT unit, and amortized over the vesting period. Unit-based compensation does not qualify as an equity award and is classified as a liability. The awards are fair valued every reporting period, based on the fair market value of a REIT unit, and the change in fair value recognized as compensation expense.

The deferred units can be settled at the holders' option in units or cash subject to the REIT's approval and are treated as a liability until redeemed.

16. Segment disclosure:

All of the REIT's assets and liabilities are in, and its revenue derived from, the Canadian real estate industry segment. No single tenant accounts for 10% or more of the REIT's rental revenue.

17. Transactions with related parties:

The REIT is the ultimate Canadian parent entity.

The consolidated financial statements as at December 31, 2011 include the accounts of the REIT and all its subsidiaries. The significant subsidiaries of the REIT are wholly owned and include NHP Holdings Limited Partnership, Healthcare Properties LP and Northwest Healthcare Properties Corporation.

Except as disclosed elsewhere in the consolidated financial statements, the following are the related party transactions:

(a) The REIT has entered into head leases with NW Operating Trust on three properties. The annual minimum rent for the head leases, including parking, totals $2,504,042. The head leases commenced March 25, 2010 and have a term of five years subject to certain rights of termination upon third party leasing of such space. NW Operating Trust is responsible for any leasing costs incurred in leasing this space and reimburses the REIT for costs incurred.

(b) NW Operating Trust leased space in two properties owned by the REIT for the period from March 25, 2010 to September 30, 2010 and for the period from August 1, 2010 to April 30, 2011, respectively.

(c) The REIT earned revenue from a tenant which is owned by NW Operating Trust.

(d) The REIT has entered into Management and Cost Sharing Agreements with NW Operating Trust to provide property management services for two properties for a period of five years commencing March 25, 2010 for $418,630 per annum plus reimbursement of expenditures based on standard commercial terms provided by the REIT. One of the properties was acquired by the REIT on December 31, 2010 (note 3) and the fees were thereafter reduced to $215,565 plus reimbursement of expenditures.

17. Transactions with related parties (continued):

(e) The REIT has entered into a Leasing and Construction Supervision Services Agreement with NW Operating Trust to provide supervision and leasing services at the properties subject to the head leases for a period of five years commencing March 25, 2010.

(f) The REIT entered into a Sublease Agreement with an affiliate of NW Operating Trust to lease its head office premises. The sublease term is for the period from March 25, 2010 to December 31, 2010 and monthly thereafter. The REIT is to pay an annual minimum rent of $200,000 plus additional rents.

(g) The REIT has entered into a Support Services Agreement with NW Operating Trust to provide NW Operating Trust certain support services for a fee based on an allocation of the relevant costs of the support services incurred by the REIT.

(h) During the period from March 25, 2010 to December 31, 2010, the REIT earned interest on the balance representing the working capital deficiency of HPLP of $11,223,016 on the date of acquisition (note 3) and issue costs of $1,991,000 related to issuance of units (note 14), which were reimbursed by NW Operating Trust. NW Operating Trust agreed to pay interest at 4.5% per annum for the 30 days commencing July 5, 2010 and 8.0% per annum thereafter.

(i) On December 24, 2010, the REIT acquired an income-producing property from an affiliate of NW Operating Trust (note 3) for net consideration of $28,831,278. The REIT and an affiliate of NW Operating Trust have agreed to negotiate a development agreement respecting the prospective future development of the excess land associated with this property on mutually acceptable terms and conditions. The purchase agreement allows NW Operating Trust to repurchase the development land at $2,950,000 if agreement is not reached within a period of six months of the acquisition date or a period mutually agreed by the REIT and an affiliate of NW Operating Trust. This period has been mutually agreed to be extended to June 30, 2012. As at December 31, 2010, a working capital adjustment of $651,647, calculated according to the terms of the acquisition agreement, is included in accounts receivable.

(In Canadian dollars)

17. Transactions with related parties (continued):

(j) On December 23, 2011, the REIT funded a $8,000,000 loan on a property owned by a joint venture partnership in which an affiliate of NW Operating Trust has a 50% interest (note 6).

The following table summarizes the transactions with related parties noted in note 17(a) to (j) and discloses the amounts of outstanding balances, respectively:

	2011	2010
Minimum rent, operating cost recoveries, parking income (included in revenue)	$ 3,590,795	$ 3,376,340
Interest revenue (included in revenue)	7,397	460,138
Fee income and cost recovery (included in revenue)	488,340	593,145
Cost recovery	102,700	469,747
Head office rent expense (included in operating expenses and trust expenses)	408,908	157,188
Leasing costs	2,333,497	1,711,292
Accounts receivable at year end	964,049	1,695,239
Loan receivable at year end	4,000,000	–

The compensation of Trustees and key management personnel is set out in the following table:

	2011	2010
Compensation expense	$ 1,114,294	$ 821,826
Unit-based compensation expense (note 15)	538,263	69,732
	$ 1,652,557	$ 891,558

Compensation expense includes salary, bonus and other short-term benefits.

(In Canadian dollars)

18. Property operations:

The components of revenue are as follows:

	2011	2010
Revenue from investment properties	$ 117,663,670	$ 62,874,666
Management fee revenue	488,340	593,147
Revenue from operations	$ 118,152,010	$ 63,467,813

The REIT generally leases investment properties under operating leases with lease terms between 5 and 10 years, with options to extend up to a further 5 years.

Future minimum base rent lease payments on non-cancellable tenant operating leases are as follows:

2012	$ 53,578,742
2013 - 2016	143,208,687
2017 and thereafter	74,512,834
	$ 271,300,263

Property operating expenses include ground lease expense for the year ended December 31, 2011 of $225,000 and period from March 25, 2010 to December 31, 2010 of $173,125, representing rent expense associated with an operating lease for land on which one of the REIT's properties is situated. The ground lease expires on September 30, 2036, with monthly payments of $18,750.

Included in revenue from investment properties are realty tax and operating cost recoveries for the year ended December 31, 2011 of $46,890,627 and period from March 25, 2010 to December 31, 2010 of $24,603,826. There were no material contingent rents during the period.

(In Canadian dollars)

19. Employee costs:

	2011	2010
Compensation expense	$ 10,600,545	$ 6,515,959
Unit-based compensation expense (note 15)	672,883	69,732
	$ 11,273,428	$ 6,585,691

Compensation expense includes salary, bonus and other short-term benefits.

During the year ended December 31, 2011, the REIT capitalized $661,788 of compensation expense to investment properties (2010 - $629,580).

20. Finance cost:

	2011	2010
Interest on fixed rate debt	$ 22,671,190	$ 13,441,309
Interest on floating rate debt	1,205,093	461,957
Amortization of debt premiums	(1,100,031)	(535,871)
Amortization of transaction costs	649,159	420,731
	23,425,411	13,788,126
Distributions on Class B exchangeable units	6,118,823	4,762,167
Fair value adjustment of Class B exchangeable units	(1,509,417)	13,083,309
	$ 28,034,817	$ 31,633,602

(In Canadian dollars)

21. Commitments and contingencies:

Except as disclosed elsewhere in these consolidated financial statements, commitments and contingencies of the REIT include the following:

(a) The REIT has entered into fixed-price utility contracts with a third-party supplier in the amount of $2,119,546 to provide electricity and gas for its own use at its investment properties.

(b) 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 consolidated financial statements.

(c) As part of the purchase and sale agreement with an affiliate of NW Operating Trust related to the acquisition of an investment property, the REIT agreed that in the event a development agreement is not achieved with NW Operating Trust, the REIT would sever and sell the development land portion of the investment property to NW Operating Trust for $2,950,000.

22. Change in non-cash operating items:

	2011	2010
Decrease in accounts receivable	$ 322,002	$ 9,113,899
Increase in straight-line rents	(1,197,958)	(568,550)
Decrease (increase) in other assets, excluding deposits	(557,239)	379,873
Increase (decrease) in accounts payable and accrued liabilities	1,819,489	(4,472,096)
	$ 386,294	$ 4,453,126

23. Capital management:

The REIT's primary objective when managing capital is to maximize unit value through the ongoing active management of the REIT's investment properties, the acquisition of additional investment properties and the development and construction of projects which are leased to creditworthy tenants.

The REIT considers its capital to be its unitholders' equity, Class B exchangeable units, mortgages payable and loans payable. The REIT 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 to economic conditions.

The REIT's strategy is also driven by policies as set out in the Amended and Restated Declaration of Trust, as well as requirements from certain lenders.

The requirements of the REIT's operating policies as outlined in the Amended and Restated Declaration of Trust include requirements that the REIT will not:

(a) incur or assume indebtedness on properties in excess of 75% of the property's market value; and

(b) incur or assume indebtedness which would cause the total indebtedness of the REIT to exceed 65% of Gross Book Value as defined.

23. Capital management (continued):

The REIT is required under the terms of its credit facility to meet certain financial covenants, including:

(a) a Debt to Gross Book Value ratio of not more than 65%;

(b) an Interest Coverage Ratio of not less than 1.75%;

(c) a Debt Service Coverage Ratio of not less than 1.50; and

(d) a minimum Adjusted Unitholders' Equity of not less than the aggregate of: (i) $200,000,000; and (ii) 75% of net proceeds in connection with equity offerings after March 31, 2010.

In addition, the REIT is required under certain property mortgage terms to meet financial covenant ratios.

The REIT complied with all financial covenants during the year ended December 31, 2011.

24. Risk management and fair values:

(a) Risk management:

In the normal course of business, the REIT is exposed to a number of risks that can affect its operating performance. These risks and the actions taken to manage them are as follows:

(i) Interest rate risk:

Floating rate debt puts the REIT at risk that interest rates may rise before long-term fixed rate debt is arranged. At December 31, 2011, none of the REIT's mortgages bear interest at floating rates. The REIT staggers the maturities of its fixed rate mortgages payable in order to minimize the exposure to future interest rate fluctuations. The REIT has $6,000,000 of floating rate debt at December 31, 2011 pursuant to its secured floating rate revolving credit facility. A 1% change in the interest rate will change the annual finance cost related to the outstanding balance by $60,000.

(ii) Credit risk:

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the REIT by failing to discharge its obligations. The REIT is exposed to credit risk on all financial assets and its exposure is generally limited to the carrying amount on the consolidated balance sheets. The REIT actively manages to minimize its credit risk through careful selection and assessment of its credit parties based on knowledge obtained through means such as due diligence carried out in respect of leasing transactions to new tenants.

24. Risk management and fair values (continued):

(iii) Liquidity risk:

Liquidity risk is the risk that the REIT will encounter difficulty in meeting its financial obligations when they come due. The REIT's exposure to refinancing risk arises from maturing mortgages payable and loans payable. Management's strategy to managing liquidity risk is to ensure, to the extent possible, that it always has sufficient financial assets to meet its financial liabilities when they come due, by forecasting cash flows from operations and anticipated investing and financing activities. The REIT, whenever possible, enters into long-term leases with creditworthy tenants which assist in maintaining a predictable cash flow. The REIT's policy is to ensure adequate funding is available from operations, established lending facilities and other sources as required. The ability to obtain funding from external sources depends on several factors, including current economic climate and the underlying assets being financed.

The contractual principal and interest payments on the REIT's mortgages payable for the years ended December 31 are as follows:

2012	$ 46,415,125
2013	94,204,314
2014	77,046,986
2015	80,186,529
2016	115,280,298
2017 and thereafter	205,364,923
	$ 618,498,175

(iv) Market risk:

Market risk is the risk that changes in market prices, such as interest rates and equity prices, will affect the REIT's financial instruments. All of the REIT's investment properties are focused on the Canadian medical office sector. All of the REIT's operations are denominated in Canadian dollars, resulting in no direct foreign exchange risk.

24. Risk management and fair values (continued):

(b) Fair values:

The REIT uses various methods in estimating the fair values recognized in the consolidated financial statements. The fair value hierarchy reflects the significance of inputs used in determining the fair values

- Level 1 - quoted prices in active markets;
- Level 2 - inputs other than quoted prices in the active markets or valuation techniques where significant inputs are based on observable market data; and
- Level 3 - valuation technique for which significant inputs are not based on observable market data.

The fair value of the REIT's mortgages payable at December 31, 2011 is $531,397,262 (December 31, 2010 - $375,872,767). The fair values have been estimated based on the current market rates for mortgages with similar terms and conditions (Level 2).

The REIT's Class B exchangeable units are carried at fair value and the fair value of the Class B exchangeable units has been determined with reference to the trading price of the REIT's units on the consolidated balance sheet date (Level 1).

The fair value of the deferred units is determined with reference to the trading price of the REIT's units on the consolidated balance sheet dates (Level 1).

The carrying values of the REIT's financial assets, which include accounts receivable, loan receivable, mortgage escrow, deposits, restricted cash and cash and cash equivalents, as well as financial liabilities, which include accounts payable and accrued liabilities, approximate their recorded fair values due to their short-term nature.

25. Subsequent events:

On February 1, 2012, the secured floating rate revolving credit facility was expanded to $50,000,000 and now bears interest at a rate equal to the bank's prime rate plus 1.25% or bankers' acceptances plus 2.25%. The term was also extended to March 25, 2014. As part of the expansion, two investment properties with a carrying value at December 31, 2011 of $26,541,440 were added to the security.

The REIT has acquired two additional income-producing properties for aggregate consideration of $15,000,000.

During the period from January 1, 2012 to February 29, 2012, the REIT declared distributions of $0.13334 per unit or $4.7 million.

The REIT has entered into a commitment to refinance one of its properties for $10,500,000.

26. Explanation of transition to IFRS:

As stated in note 1, these are the first IFRS annual consolidated financial statements and are prepared in accordance with IFRS. The accounting policies adopted under IFRS have been applied in preparing the consolidated financial statements for the year ended December 31, 2011, the comparative information for the period from March 25, 2010 to December 31, 2010, and the preparation of an opening IFRS balance sheet at March 25, 2010. The REIT commenced operations on March 25, 2010 and the Transition Date to IFRS is March 25, 2010. However, since the REIT had no assets or liabilities on March 25, 2010, a reconciliation between IFRS and Canadian GAAP has not been presented as at that date.

The REIT's IFRS adoption date is January 1, 2011. The REIT has adjusted amounts previously reported in financial statements and interim reports prepared in accordance with its previous basis of accounting, Canadian GAAP.

(In Canadian dollars)

26. Explanation of transition to IFRS (continued):

An explanation of how the transition from Canadian GAAP to IFRS has affected the REIT's financial position and performance is set out in the tables below and the notes accompanying them.

Reconciliation of equity as at December 31, 2010:

Canadian GAAP presentation	Note	Canadian GAAP	IFRS adjustments	IFRS	IFRS presentation
Assets					**Assets**
Income-producing properties	(a)	$ 584,479,525	$ 86,553,765	$ 671,033,290	Investment properties
Goodwill and intangible assets	(a)	72,343,718	(67,885,824)	4,457,894	Goodwill
Accounts receivable	(a)	5,106,275	(568,550)	4,537,725	Accounts receivable
Leasing costs	(c)	6,501,046	(6,501,046)	–	
Other assets	(a)	9,814,051	296,548	10,110,599	Other assets
Restricted cash		175,000	–	175,000	Restricted cash
Cash and cash equivalents		46,311,722	–	46,311,722	Cash and cash equivalents
		$ 724,731,337	$ 11,894,893	$ 736,626,230	
Liabilities and Unitholders' Equity					**Liabilities and Unitholders' Equity**
Mortgages payable		$ 372,051,861	$ –	$ 372,051,861	Mortgages payable
	(b)	–	89,787,921	89,787,921	Class B exchangeable units
Accounts payable and accrued liabilities	(b) (d)	13,134,151	512,076	13,646,227	Accounts payable and accrued liabilities
Below-market leases	(a)	7,494,276	(7,494,276)	–	
Distributions payable	(b)	2,351,220	(512,075)	1,839,145	Distributions payable
		395,031,508	82,293,646	477,325,154	
Unitholders' equity	(a) (b) (c)	329,699,829	(70,398,753)	259,301,076	Unitholders' equity
		$ 724,731,337	$ 11,894,893	$ 736,626,230	

(In Canadian dollars)

26. Explanation of transition to IFRS (continued):

Reconciliation of comprehensive income for the period from March 25, 2010 to December 31, 2010:

Canadian GAAP presentation	Note	Canadian GAAP	IFRS adjustments	IFRS	IFRS presentation
Revenue	(a) (d)	$ 64,973,645	$ (1,505,832)	$ 63,467,813	Revenue from operations
Expenses:					
Property operating	(a) (c) (d)	18,772,521	10,044,008	28,816,529	Property operating expenses
Property taxes	(d)	8,752,797	(8,752,797)	–	
				34,651,284	Operating income
Mortgage and facility interest		13,788,126	–	13,788,126	Finance cost
	(d)	–	(564,168)	(564,168)	Interest income
Trust expenses		1,820,159	–	1,820,159	Trust expenses
Depreciation of income-producing properties	(a)	8,110,978	(8,110,978)	–	
Amortization of leasing costs	(a)	333,558	(333,558)	–	
Amortization of in-place leases and tenant relationship	(a)	12,344,265	(12,344,265)	–	
		63,922,404			
				19,607,167	Income before undernoted items
	(b)	–	(4,762,167)	(4,762,167)	Finance cost - Class B exchangeable unit distributions
	(b)	–	(13,083,309)	(13,083,309)	Finance cost - fair value adjustment of Class B exchangeable units
	(a)	–	833,242	833,242	Fair value adjustment of investment properties
Net income and comprehensive income		$ 1,051,241	$ 1,543,692	$ 2,594,933	Net income and comprehensive income

26. Explanation of transition to IFRS (continued):

Reconciliation of statement of cash flows from Canadian GAAP to IFRS:

Consistent with the REIT's accounting policy choice under IAS 7, Statement of Cash Flows, interest paid and interest received have moved into the body of the statement of cash flows, whereas they were previously disclosed as supplementary information. There are no other material differences between the statement of cash flows presented under IFRS and the statement of cash flows presented under previous Canadian GAAP.

Notes to reconciliation:

IFRS 1 sets forth guidance for the initial adoption of IFRS. Under IFRS 1, the standards are applied retrospectively with all adjustments to assets and liabilities taken to retained earnings unless certain optional exemptions are elected and mandatory exceptions are applied.

In preparing its first IFRS financial statements, the REIT has applied the mandatory exception from full retrospective application of IFRS for estimates. This mandatory exception requires that estimates made at the Transition Date, and in the comparative reporting periods, be consistent with estimates made under Canadian GAAP, unless either the estimates are adjusted to reflect a revised accounting policy or there is objective evidence that the estimates made under Canadian GAAP were in error. The REIT has, however, not elected any optional exemptions from the general requirement for retrospective application of IFRS.

(a) Investment properties:

Under IAS 40, Investment Properties, the REIT may elect subsequent to initial recognition to account for investment property using either the fair value model or the cost model. The REIT has elected the fair value model to account for its investment properties subsequent to initial recognition. Under the fair value model, investment properties are carried on the consolidated balance sheets at fair value. The properties are not depreciated and changes in the fair value of the properties are recognized in the consolidated statements of income and comprehensive income in the period in which they occur. Under Canadian GAAP, the REIT's income-producing properties and certain intangibles were carried on the consolidated balance sheets at cost less accumulated depreciation and amortization.

26. Explanation of transition to IFRS (continued):

The REIT commenced operations on March 25, 2010, and pursuant to the commencement of its operations, the REIT's investment properties were assessed to be at fair value by management. At the commencement of operations, the values assigned to investment properties under IFRS are the same as the total of the values assigned to income-producing properties and certain intangibles under Canadian GAAP.

As at December 31, 2010, the REIT has reclassified intangibles related to in-place leases ($38,042,869), tenant relationships ($24,706,517), above-market leases ($5,136,438) and below-market leases ($7,494,276) to investment properties.

As at December 31, 2010, the REIT reclassified straight-line rents receivable from accounts receivable to investment properties to conform with the REIT's presentation under IFRS.

As at December 31, 2010, the REIT reclassified $296,548 of furniture and equipment from income-producing properties to other assets to conform with the REIT's presentation under IFRS. During the period from March 25, 2010 to December 31, 2010, the REIT eliminated depreciation and amortization of $20,725,386 recognized under Canadian GAAP, to conform to the fair value method under IFRS. In addition, $63,415 of depreciation on furniture and equipment was reclassified to property operating expenses for the period from March 25, 2010 to December 31, 2010.

During the period from March 25, 2010 to December 31, 2010, the REIT eliminated the net amortization of $941,664 of above-market and below-market leases to reflect the elimination of the related intangibles under IFRS.

During the period from March 25, 2010 to December 31, 2010, the REIT recognized a fair value increase on investment properties of $833,242.

The changes to unitholders' equity in the reconciliation of Canadian GAAP to IFRS reflect the elimination of accumulated depreciation on income-producing properties, recognized under Canadian GAAP, and the changes in the fair values of investment properties subsequent to initial recognition under IFRS. In addition, certain intangible assets disclosed separately under Canadian GAAP have been reclassified to investment properties under IFRS and are no longer amortized.

26. Explanation of transition to IFRS (continued):

(b) Classification of Class B exchangeable units:

Under Canadian GAAP, the REIT's Class B exchangeable units are presented as equity on the consolidated balance sheets. However, under IFRS, the Class B exchangeable units are classified as a liability and measured at fair value. Changes in value are recognized in the consolidated statements of income and comprehensive income in the period in which they arise and distributions on the Class B exchangeable units are recorded as finance cost rather than distributions.

Under IFRS, for the period from March 25, 2010 to December 31, 2010, the REIT recognized: (i) a charge to the consolidated statements of income and comprehensive income of $13,083,309 representing the increase in the fair value of the Class B exchangeable units; and (ii) $ $4,762,167 representing distributions to the Class B exchangeable units that is recorded as a finance cost.

As at December 31, 2010, the carrying value of the Class B exchangeable units under Canadian GAAP of $76,807,460 was reclassified from unitholders' equity to a liability for Class B exchangeable units. Under IFRS, the carrying value of the Class B exchangeable units was adjusted to $89,787,921 as at December 31, 2010 to reflect the fair value of the Class B exchangeable units.

Distributions payable of $512,075 were reclassified from distributions payable to accounts payable and accrued liabilities as at December 31, 2010 to reflect the treatment of distributions on the Class B exchangeable units as a finance cost under IFRS.

(c) Internal leasing costs:

IAS 17, Leases, requires certain internal initial direct costs incurred by lessors in negotiating and arranging an operating lease previously capitalized and amortized on a straight-line basis over the term of the lease under Canadian GAAP to be expensed. As a result, the REIT has charged $1,227,796 of leasing costs to property operating expenses for the period from March 25, 2010 to December 31, 2010.

26. Explanation of transition to IFRS (continued):

As at December 31, 2010, the REIT reclassified $6,501,046 of leasing costs, net of amounts charged to property operations expenses, to investment properties.

(d) Other reclassifications:

During the period from March 25, 2010 to December 31, 2010, the REIT reclassified $564,168 of interest income from revenue to interest income to conform with the REIT's presentation under IFRS.

During the period from March 25, 2010 to December 31, 2010, the REIT reclassified $8,752,797 of property taxes from property taxes to property operating expenses to conform with the REIT's presentation under IFRS.