

Consolidated Financial Statements of

**ARTIS REAL ESTATE  
INVESTMENT TRUST**

December 31, 2008 and 2007



### Management's Responsibility for Financial Statements

The management of Artis Real Estate Investment Trust is responsible for the preparation and integrity of the consolidated financial statements contained in the annual report. These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles and necessarily include some amounts that are based on management's best estimate and judgment. Management has determined such amounts on a reasonable basis and considers that the consolidated financial statements present fairly the financial position of the REIT, the results of its operations and its cash flows. Management has also prepared financial information presented elsewhere in this annual report and has ensured that it is consistent with that in the financial statements. To fulfill its responsibility, management maintains internal accounting controls and systems and establishes policies and procedures to ensure the reliability of financial information and to safeguard assets.

The Board of Trustees is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal control. The Board of Trustees carries out this responsibility principally through its Audit Committee, composed entirely of outside and unrelated trustees. The Audit Committee meets regularly with management of the REIT and with the independent auditors. The consolidated financial statements have been reviewed and approved by the Board of Trustees on the recommendation of its Audit Committee.

The REIT's independent auditors, KPMG LLP, have been appointed by the unitholders to audit the financial statements and express an opinion thereon.

\_\_\_\_\_  
"Armin Martens"

Armin Martens, P.Eng., MBA  
President and Chief Executive Officer  
March 17, 2009

\_\_\_\_\_  
"Jim Green"

Jim Green, CA  
Chief Financial Officer  
March 17, 2009



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## AUDITORS' REPORT

To the Unitholders of Artis Real Estate Investment Trust

We have audited the consolidated balance sheets of Artis Real Estate Investment Trust as at December 31, 2008 and 2007 and the consolidated statements of operations, unitholders' equity and cash flows for the years then ended. These financial statements are the responsibility of Artis Real Estate Investment Trust's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of Artis Real Estate Investment Trust as at December 31, 2008 and 2007 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Chartered Accountants

Winnipeg, Canada

March 17, 2009

# ARTIS REAL ESTATE INVESTMENT TRUST

Consolidated Balance Sheets  
As at December 31, 2008 and 2007

(In thousands of dollars)

	2008	2007
<b>ASSETS</b>		
Income-producing properties (note 4)	\$ 1,025,010	\$ 944,612
Other assets (note 5)	144,981	140,070
Future income taxes (note 18)	11,127	11,509
Deposits on income-producing properties (note 6)	6,712	11,826
Prepaid expenses	2,332	1,326
Notes receivable (note 7)	28,830	30,494
Rent and other receivables	10,859	6,543
Cash held in trust	588	682
Cash and cash equivalents	13,847	29,386
	<b>\$ 1,244,286</b>	<b>\$ 1,176,448</b>
<b>LIABILITIES AND UNITHOLDERS' EQUITY</b>		
Liabilities:		
Mortgages and loans payable (note 8)	\$ 676,369	\$ 612,996
Convertible debentures (note 9)	44,906	52,732
Intangible liabilities (note 10)	91,186	99,280
Security deposits and prepaid rent	4,822	4,033
Accounts payable and other liabilities (note 11)	25,109	11,725
Bank indebtedness (note 12)	32,500	-
	874,892	780,766
Non-controlling interest (note 13)	10,258	10,182
Unitholders' equity	359,136	385,500
Commitments and guarantees (note 22)		
Subsequent event (note 26)		
	<b>\$ 1,244,286</b>	<b>\$ 1,176,448</b>

See accompanying notes to consolidated financial statements.

# ARTIS REAL ESTATE INVESTMENT TRUST

Consolidated Statements of Operations  
Years ended December 31, 2008 and 2007

(In thousands of dollars, except per unit amounts)

	2008	2007
Revenue	\$ 142,976	\$ 97,708
Property operating expenses	45,245	31,051
Interest	97,731 41,047	66,657 27,922
	56,684	38,735
Expenses (Income):		
Corporate	4,969	4,798
Amortization	58,139	40,557
Unrealized gain on commodity derivatives	(223)	-
	62,885	45,355
Loss before income taxes	(6,201)	(6,620)
Future income tax (expense) recovery (note 18)	(457)	10,833
Income (loss) before non-controlling interest and discontinued operations	(6,658)	4,213
Non-controlling interest (note 13)	(247)	-
Income (loss) from continuing operations	(6,905)	4,213
Income from discontinued operations (note 21)	115	1,944
Income (loss) and comprehensive income (loss) for the year	\$ (6,790)	\$ 6,157
Basic income (loss) per unit (note 14 (e))		
Continuing operations	\$ (0.22)	\$ 0.17
Discontinued operations	\$ 0.01	\$ 0.08
Diluted income (loss) per unit (note 14 (e))		
Continuing operations	\$ (0.22)	\$ 0.16
Discontinued operations	\$ 0.01	\$ 0.08

See accompanying notes to consolidated financial statements.

# ARTIS REAL ESTATE INVESTMENT TRUST

Consolidated Statements of Unitholders' Equity  
Years ended December 31, 2008 and 2007

(In thousands of dollars, except unit amounts)

	Number of Units	Capital Contributions	Equity Component of Convertible Debentures	Deficit	Contributed Surplus	Total
Unitholders' equity, December 31, 2006	15,219,261	\$ 164,991	\$ 11,659	\$ (29,533)	\$ 649	\$ 147,766
Issuance of units	15,385,633	250,348	-	-	(170)	250,178
Unit-based compensation	-	-	-	-	1,039	1,039
Issuance of convertible debentures	-	-	1,125	-	-	1,125
Conversion of convertible debentures	566,174	7,123	(1,344)	-	-	5,779
Units acquired through normal course issuer bid, not cancelled at year end	(13,000)	(196)	-	-	-	(196)
Income for the year	-	-	-	6,157	-	6,157
Distributions for the year	-	-	-	(26,348)	-	(26,348)
Unitholders' equity, December 31, 2007	31,158,068	422,266	11,440	(49,724)	1,518	385,500
Issuance of units	552,357	7,238	-	-	(47)	7,191
Unit-based compensation	-	-	-	-	567	567
Conversion of convertible debentures	837,341	11,651	(2,172)	-	-	9,479
Units acquired and cancelled through normal course issuer bid	(197,400)	(2,673)	-	(112)	552	(2,233)
Units acquired through normal course issuer bid, not cancelled at year end	(43,600)	(226)	-	-	-	(226)
Loss for the year	-	-	-	(6,790)	-	(6,790)
Distributions for the year	-	-	-	(34,352)	-	(34,352)
Unitholders' equity, December 31, 2008	32,306,766	\$ 438,256	\$ 9,268	\$ (90,978)	\$ 2,590	\$ 359,136

See accompanying notes to consolidated financial statements.

# ARTIS REAL ESTATE INVESTMENT TRUST

Consolidated Statements of Cash Flows  
Years ended December 31, 2008 and 2007

(In thousands of dollars)

	2008	2007
Cash provided by (used for):		
Operating activities:		
Income (loss) for the year	\$ (6,790)	\$ 6,157
Adjustments for non-cash items:		
Amortization:		
Income-producing properties	26,842	18,898
Office equipment	8	7
Above-market rent	339	226
Acquired in-place leases	30,618	21,514
Customer relationships	18	22
Below-market rent	(14,224)	(9,780)
Tenant inducements and leasing costs	1,351	784
Tenant inducements amortized to revenue	110	-
Above- and below-market mortgages, net	(178)	(96)
Accretion on liability component of convertible debentures	1,464	1,713
Straight-line rent adjustment	(1,960)	(1,369)
(Gain) loss on disposal of income-producing property	197	(2,511)
Unrealized gain on commodity derivatives	(223)	-
Unit-based compensation expense	567	1,039
Amortization of financing costs included in interest	413	229
Future income tax expense (recovery)	548	(10,394)
Non-controlling interest (note 13)	265	-
	39,365	26,439
Changes in non-cash operating items (note 16)	(2,195)	2,147
	37,170	28,586
Investing activities:		
Acquisition of income-producing properties, net of related debt and issuance of units (note 3)	(46,411)	(197,680)
Disposition of income-producing properties, net of mortgage and costs	1,139	2,552
Additions to income-producing properties	(12,094)	(984)
Deposits on income-producing properties held for sale (notes 11 and 21)	10,000	-
Repayment of mortgage receivable	-	14,000
Advances of note and mortgage receivable	-	(45,000)
Notes receivable principal repayments	1,664	816
Additions to office equipment and software	(497)	(31)
Additions to tenant inducements and leasing costs	(7,255)	(3,469)
Change in deposits on income-producing properties	5,114	(1,374)
	(48,340)	(231,170)
Financing activities:		
Issuance of units, net of issue costs	5,115	248,893
Purchase of units under normal course issuer bid	(2,460)	-
Bank indebtedness	32,500	-
Distributions paid on REIT units	(34,352)	(26,348)
Distributions paid on Class B units, charged to non-controlling interest (note 13)	(189)	(186)
Mortgages and loans principal repayments	(12,773)	(6,665)
Advance of mortgage payable	7,790	1,024
	(4,369)	216,718
Increase (decrease) in cash and cash equivalents	(15,539)	14,134
Cash and cash equivalents at beginning of year	29,386	15,252
Cash and cash equivalents at end of year	\$ 13,847	\$ 29,386
Supplemental cash flow information:		
Interest paid, net of interest received	\$ 37,128	\$ 22,094

See accompanying notes to consolidated financial statements.

# ARTIS REAL ESTATE INVESTMENT TRUST

Notes to Consolidated Financial Statements  
Years ended December 31, 2008 and 2007

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

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## 1. Organization:

Artis Real Estate Investment Trust (the "REIT") is an unincorporated open-end real estate investment trust (note 14) created under, and governed by, the laws of the province of Manitoba and was created pursuant to the Declaration of Trust dated November 8, 2004, subsequently amended and restated on October 31, 2006 (the "Declaration of Trust"). The purpose of the REIT is to directly, or indirectly, own, manage, lease and (where appropriate) develop retail, industrial and office properties in Canada.

The Declaration of Trust provides that the REIT makes monthly cash distributions to unitholders of the REIT's units. The amount distributed in each year (currently \$1.08 per unit), will be an amount not less than the amount of distributable income in the year set down in a policy by the Trustees.

## 2. Significant accounting policies:

### (a) Principles of consolidation:

The consolidated financial statements include the accounts of the REIT and its subsidiaries, together with its proportionate share of the assets, liabilities, revenue and expenses of the co-ownerships in which it participates.

### (b) Changes in accounting policies:

The CICA has issued three new accounting standards: Handbook Section 1535, Capital Disclosures, Handbook Section 3862, Financial Instruments - Disclosures, and Handbook Section 3863, Financial Instruments - Presentation, which were adopted by the REIT on January 1, 2008.

Section 1535 includes required disclosures of an entity's objectives, policies and processes for managing capital, and quantitative data about what the entity regards as capital (note 23).

Sections 3862 and 3863 replace the existing Section 3861, Financial Instruments - Disclosure and Presentation. These new sections revise and enhance disclosure requirements, and carryforward unchanged existing presentation requirements. These new sections require disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks (note 24).

The new standards have no impact on the classification and valuation of the REIT's financial instruments.

### (c) Financial Instruments - Recognition and Measurement:

Section 3855 provides guidance on recognizing financial instruments and non-financial derivatives on the consolidated balance sheet. The standard also specifies how financial instrument gains and losses are presented. Initially, all financial assets and liabilities must be recorded on the consolidated balance sheet at fair value. Subsequent measurement is determined by the classification of each financial asset and liability. Under this standard, all financial instruments are classified as one of: (a) held-to-maturity; (b) loans and receivables; (c) held-for-trading; (d) available-for-sale or (e) other liabilities. Financial assets and liabilities held for trading are measured at fair value with gains and losses recognized in net income. Financial instruments classified as held-to-maturity, loans and receivables, and other liabilities are measured at amortized cost. Available-for-sale financial instruments are measured at fair value, with unrealized gains and losses recognized in comprehensive income.

Upon adoption of this standard, the REIT designated its cash and cash equivalents and cash held in trust as held-for-trading; notes receivable and rent and other receivables as loans and receivables; mortgages and loans payable, convertible debentures, and accounts payable and other liabilities as other liabilities. 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 are accounted for as part of the respective asset or liability's carrying value at inception and amortized over the expected life of the financial instrument using the effective interest rate method.

All derivative instruments, including embedded derivatives, are recorded in the consolidated statement of operations at fair value unless the criteria for exemption from such treatment under Section 3855 is met.



# ARTIS REAL ESTATE INVESTMENT TRUST

Notes to Consolidated Financial Statements  
Years ended December 31, 2008 and 2007

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

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## 2. Significant accounting policies (continued):

### (d) Comprehensive Income:

Section 1530 requires a component of unitholders' equity, comprehensive income, to be included in the REIT's consolidated financial statements. In addition, the standard requires a statement of comprehensive income. The major components of the statement of comprehensive income may include items such as unrealized gains and losses on financial assets classified as available-for-sale, deferred gains and losses arising from the settlement of historic cash flow hedging transactions and changes in the fair value of the effective position of cash flow hedging instruments.

The REIT had no "other comprehensive income or loss" transactions during the years ended December 31, 2008 and 2007, and no opening or closing balances of accumulated other comprehensive income or loss.

### (e) Income-producing properties, other assets and intangible liabilities:

Income-producing properties include tangible and intangible assets.

Tangible assets include land, buildings, a leasehold interest, parking lots and improvements. Intangible assets include the value of in-place lease agreements, the value of the differential between original and market rents for in-place leases and the value of customer relationships.

Income-producing properties are carried at cost less accumulated amortization. If events or circumstances indicate that the carrying value of the income-producing property may be impaired, a recoverability analysis is performed based upon estimated undiscounted cash flows to be generated from the income-producing property. If the analysis indicates that the carrying value is not recoverable from future cash flows, the income-producing property is written-down to estimated fair value and an impairment loss is recognized.

Upon acquisition of income-producing properties, the purchase price is allocated based on estimated fair values to land, building, parking lots, tenant improvements and intangibles, including the value of above and below market leases, acquired in-place leases, and tenant relationships, if any.

Property under development includes initial acquisition costs, other direct costs and realty taxes, interest, and operating revenue and expenses during the period of development.

# ARTIS REAL ESTATE INVESTMENT TRUST

Notes to Consolidated Financial Statements  
Years ended December 31, 2008 and 2007

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

## 2. Significant accounting policies (continued):

- (e) Income-producing properties, other assets and intangible liabilities (continued):

Amortization on income-producing properties, other assets and intangible liabilities is provided on the following basis and rates:

<i><b>Asset</b></i>	<i><b>Basis</b></i>	<i><b>Rate/years</b></i>
Buildings	Straight-line	up to 40
Building improvements	Straight-line	up to 20
Tenant improvements	Straight-line	Remaining term of lease agreement and renewal years where applicable
Leasehold interest	Straight-line	40
Parking lots	Straight-line	20
Office equipment	Straight-line	5
Acquired in-place leases	Straight-line	Remaining term of lease agreement and renewal years where applicable
Above-market rent	Straight-line	Remaining term of lease agreement and fixed-rate non-cancelable renewal years
Below-market rent	Straight-line	Remaining term of lease agreement and fixed-rate non-cancelable renewal years
Tenant inducements and leasing costs	Straight-line	Term of lease agreement
Customer relationships	Straight-line	Remaining term of lease agreement and renewal years where applicable

- (f) Other assets:

Recoverable operating costs are recorded at cost and are deferred and amortized over the period which they are recoverable from tenants.

Leasing costs, such as commissions, are deferred and amortized on a straight-line basis over the term of the related lease

Payments to tenants under lease obligations are characterized either as tenant inducements owned by the landlord or as tenant inducements provided to the tenant. When the obligation is determined to be tenant inducements owned by the REIT, the REIT is considered to have acquired an asset. If the REIT determines that for accounting purposes it is not the owner of the tenant inducements, then the obligations under the lease are treated as incentives that reduce revenue. Tenant inducements are amortized on a straight-line basis over the term of the lease.

# ARTIS REAL ESTATE INVESTMENT TRUST

Notes to Consolidated Financial Statements  
Years ended December 31, 2008 and 2007

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

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## 2. Significant accounting policies (continued):

(g) Disposal of long-lived assets:

A long-lived asset, including income-producing properties and other related assets, is classified as held for sale at the point in time when it is available for immediate sale, management has committed to a plan to sell the asset and is actively locating a buyer for the asset at a sales price that is reasonable in relation to the current fair value of the asset, and the sale is probable and expected to be completed within a one-year period. Properties held for sale are stated at the lower of cost and fair value less selling costs. No further amortization is recorded on these properties once classified as held for sale. A property that is subsequently reclassified as held and in use is measured at the lower of: (i) its carrying amount before it was classified as held for sale, adjusted for any amortization expense that would have been recognized had it been continuously classified as held and in use; and (ii) its estimated fair value at the date of the subsequent decision not to sell.

The results of operations associated with properties disposed of, or classified as held for sale, are reported separately as income from discontinued operations when the REIT will have no continuing involvement with the ongoing cash flow of the assets.

(h) Cash and cash equivalents:

Cash and cash equivalents consist of cash with financial institutions and includes short-term investments with maturities of three months or less.

(i) Revenue recognition:

Revenue from income-producing properties includes rents earned from tenants under lease agreements, percentage rent, realty tax and operating costs recoveries and other incidental income and is recognized as revenue over the term of the underlying leases. All rent steps in lease agreements are accounted for on a straight-line basis over the term of the respective leases. Percentage rent is not recognized until a tenant is obligated to pay such rent.

(j) Co-ownerships:

The REIT carries out a portion of its activities through co-ownership agreements and records its proportionate share of assets, liabilities, revenues, expenses and cash flows of the co-ownerships in which it participates.

(k) Earnings per unit:

Basic earnings (loss) per REIT unit is computed by dividing net earnings (loss) by the weighted-average units outstanding during the reporting year. Diluted earnings (loss) per unit is calculated based on the weighted-average number of units outstanding during the year, plus the effect of dilutive unit equivalents such as options. The diluted per unit amounts are calculated using the treasury stock method, as if all the unit equivalents where average market price exceeds issue price had been exercised at the beginning of the reporting year, or the year of issue, as the case may be, and that the funds obtained thereby were used to purchase units of the REIT at the average trading price of the units during the year.

(l) Income taxes:

Income taxes are accounted for using the asset and liability method. Under this method, future income taxes are recognized for the expected future tax consequences of temporary differences between the carrying amount of balance sheet items and their corresponding tax values.

Future income taxes are computed using enacted or substantively enacted income tax rates or laws for the years in which the temporary differences are expected to reverse or settle. When realization of future income tax assets does not meet the more likely than not criterion, a valuation allowance is provided for the difference.

# ARTIS REAL ESTATE INVESTMENT TRUST

Notes to Consolidated Financial Statements  
Years ended December 31, 2008 and 2007

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

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## 2. Significant accounting policies (continued):

(m) Unit-based compensation:

The REIT accounts for unit options issued under its unit option plan using the fair value method. Under this method, compensation expense is measured at fair value at the grant date using the Black-Scholes option pricing model and recognized over the vesting period.

(n) Use of estimates:

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the year. Actual results could differ from those estimates.

The significant areas of estimation include:

- Useful life of assets for the purpose of calculating amortization;
- Allocation of purchase price on the acquisition of income-producing properties;
- Valuation of future tax assets;
- Fair value of financial instruments;
- Impairment of assets; and
- Allowance for doubtful accounts.

# ARTIS REAL ESTATE INVESTMENT TRUST

Notes to Consolidated Financial Statements  
Years ended December 31, 2008 and 2007

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

### 3. Acquisitions of income-producing properties:

#### Acquisitions:

The REIT acquired the following properties during the year ended December 31, 2008:

<i>Property</i>	<i>Location</i>	<i>Acquisition Date</i>	<i>Type</i>
King Edward Centre	15 & 25 King Edward Centre, Coquitlam, BC	January 15, 2008	Retail
Leon's Building	6461 Metral Drive, Nanaimo, BC	February 1, 2008	Retail
Estevan Sobeys <sup>(1)</sup>	440 King Street, Estevan, SK	March 20, 2008	Retail
Moose Jaw Sobeys <sup>(1)</sup>	769 Thatcher Drive East, Moose Jaw, SK	March 20, 2008	Retail
Edson Shoppers	303 - 54th Street and 2nd Avenue, Edson, AB	April 15, 2008	Retail
Raleigh Shopping Centre	686 Springfield Road, Winnipeg, MB	April 15, 2008	Retail
Maynard Technology Centre	1930 Maynard Road, Calgary, AB	August 29, 2008	Industrial
Willingdon Green Building	3175/3185 Willingdon Green, Burnaby, BC	September 2, 2008	Office
Bridges Place	736 - 1st Avenue NE, Calgary, AB	December 17, 2008	Office

(1) Estevan Sobeys and Moose Jaw Sobeys were acquired as a portfolio.

The REIT acquired the following properties during the year ended December 31, 2007:

<i>Property</i>	<i>Location</i>	<i>Acquisition Date</i>	<i>Type</i>
CDI College Building	280 Main Street, Winnipeg, MB	January 13, 2007	Office
Keewatin Distribution Centre	959 & 989 Keewatin Street, Winnipeg, MB	January 31, 2007	Industrial
Clareview Town Centre	50th Street & 137th Avenue, Edmonton, AB	February 1, 2007	Retail
Centre 70 Building <sup>(1)</sup>	7015 Macleod Tr. SW & 555 - 69th St. SW, Calgary, AB	February 28, 2007	Office
Honeywell Building	2840 - 2nd Avenue SE, Calgary, AB	February 28, 2007	Industrial
Millennium Centre	4909 - 49th St. & 4902 - 48th St., Red Deer, AB	February 28, 2007	Office
Bower Centre	2319 Taylor Dr. & 2310 Gaetz Ave., Red Deer, AB	March 1, 2007	Industrial
Britannia Building <sup>(2)</sup>	703 - 6th Avenue SW, Calgary, AB	March 31, 2007	Office
Sierra Place <sup>(2)</sup>	706 - 7th Avenue SW, Calgary, AB	March 31, 2007	Office
MTS Call Centre	365 Osborne Street, Winnipeg, MB	April 1, 2007	Office
488 Albert St <sup>(3)</sup>	488 Albert Street, Nanaimo, BC	June 19, 2007	Office
6475 Metral Drive <sup>(3)</sup>	6475 Metral Drive, Nanaimo, BC	June 19, 2007	Office
Aulds Corner <sup>(3)</sup>	6551 Aulds Road, Nanaimo, BC	June 19, 2007	Retail
Can-K Building <sup>(4)</sup>	8220 Davies Road, Edmonton, AB	June 30, 2007	Industrial
Mayfield Industrial Plaza <sup>(4)</sup>	11304/24 - 163 Street, Edmonton, AB	June 30, 2007	Industrial
TransAlta Place <sup>(5)</sup>	110 - 12th Avenue SW, Calgary, AB	July 5, 2007	Office
Winnipeg Square <sup>(6)</sup>	360 Main Street, Winnipeg, MB	August 29, 2007	Office/Retail
Pepco Building	608 - 17th Avenue, Nisku, AB	September 15, 2007	Industrial
Delta Shoppers Mall	8037 - 120th Street, Delta, BC	September 24, 2007	Retail
Glenmore Commerce Court	2880 Glenmore Trail SE, Calgary, AB	November 9, 2007	Office
Winnipeg Industrial Portfolio <sup>(7)</sup>	Various locations in Winnipeg, MB	November 15, 2007	Industrial
Brick Centre	11226 - 100th Avenue, 11245 - 104th Avenue & 11345/53 - 104th Avenue, Grande Prairie, AB	November 30, 2007	Retail
Fort McMurray Portfolio <sup>(8)</sup>	Various locations in Edmonton and Fort McMurray, AB	November 30, 2007	Retail
Paramount Building	630 - 4th Avenue SW, Calgary, AB	December 1, 2007	Office

(1) The REIT acquired an undivided 85% interest in Centre 70, which is proportionately consolidated in the accounts of the REIT.

(2) The Britannia Building and Sierra Place were acquired together as the Dome Britannia Portfolio.

(3) 488 Albert Street, 6475 Metral Drive and Aulds Corner were acquired as a portfolio.

(4) Can-K Building and Mayfield Industrial Plaza were acquired as a portfolio.

(5) The acquisition of TransAlta Place also included the acquisition of a note receivable for \$31,000 (note 7).

(6) The REIT acquired an undivided 38% interest in the air rights leasehold with respect to Winnipeg Square, which is proportionately consolidated in the accounts of the REIT.

(7) The Winnipeg Industrial Portfolio is comprised of 8 single-tenant and 8 multi-tenant properties.

(8) The Fort McMurray Portfolio is comprised of one property in Edmonton and 6 properties in Fort McMurray.

# ARTIS REAL ESTATE INVESTMENT TRUST

Notes to Consolidated Financial Statements  
Years ended December 31, 2008 and 2007

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

### 3. Acquisitions of income-producing properties (continued):

#### Acquisitions (continued):

These acquisitions have been accounted for by the purchase method, with the results of operations included in the REIT's accounts from the date of acquisition.

The net assets acquired including acquisition costs were as follows:

	Year Ended December 31,	
	2008	2007
Land	\$ 24,010	\$ 126,881
Buildings	61,403	419,975
Parking lots	5,587	7,512
Improvements	5,482	20,972
Acquired in-place leases	26,042	86,925
Above-market rent	238	409
Below-market rent	(6,130)	(95,764)
Long-term debt including acquired above- and below-market mortgages	(68,121)	(349,230)
Series D convertible debenture	-	(20,000)
<b>Total consideration</b>	<b>48,511</b>	<b>197,680</b>
<b>Issuance of units (note 14)</b>	<b>(2,100)</b>	<b>-</b>
<b>Cash consideration</b>	<b>\$ 46,411</b>	<b>\$ 197,680</b>
<b>Acquisition costs included above</b>	<b>\$ 1,593</b>	<b>\$ 9,251</b>

#### Dispositions:

The REIT disposed of land and building, which comprised a portion of an income-producing property, during the year ended December 31, 2008. The proceeds from the sale, net of costs, were paid in cash in the amount of \$1,139, which were used to reduce the outstanding mortgage. The assets associated with the land and building were removed from the books and a loss on sale of property in the amount of \$197 was recorded.

The REIT disposed of the following property during the year ended December 31, 2007:

<i>Property</i>	<i>Location</i>	<i>Disposition Date</i>	<i>Type</i>
Royal Square	15 Worobetz Place, Saskatoon, SK	September 1, 2007	Retail

The proceeds from the sale of Royal Square, net of costs, were \$4,591. Consideration received was the assumption, by the purchaser, of the existing mortgage in the amount of \$1,729, a promissory note in the amount of \$310 (note 7), and cash in the amount of \$2,552. The assets, intangible assets and liabilities associated with the property were removed from the books and a gain on sale of property in the amount of \$2,511 was recorded.

# ARTIS REAL ESTATE INVESTMENT TRUST

Notes to Consolidated Financial Statements  
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## 4. Income-producing properties:

	December 31, 2008		
	Cost	Accumulated amortization	Net book value
Land	\$ 254,501	\$ -	\$ 254,501
Buildings and building improvements	727,833	33,867	693,966
Leasehold interest	8,015	692	7,323
Tenant improvements	51,218	20,227	30,991
Parking lots	21,661	1,877	19,784
Property under development	2,725	-	2,725
	1,065,953	56,663	1,009,290
Income-producing properties held for sale (note 21)	16,425	705	15,720
	\$ 1,082,378	\$ 57,368	\$ 1,025,010

	December 31, 2007		
	Cost	Accumulated amortization	Net book value
Land	\$ 234,301	\$ -	\$ 234,301
Buildings and building improvements	667,846	16,944	650,902
Leasehold interest	8,015	489	7,526
Tenant improvements	46,807	12,199	34,608
Parking lots	15,513	963	14,550
Property under development	2,725	-	2,725
	\$ 975,207	\$ 30,595	\$ 944,612

## 5. Other assets:

	December 31, 2008		
	Cost	Accumulated amortization	Net book value
Acquired in-place leases	\$ 191,242	\$ 67,437	\$ 123,805
Above-market rent	1,795	821	974
Customer relationships	105	86	19
Tenant inducements and leasing costs	13,886	2,346	11,540
Recoverable operating costs	5,896	592	5,304
Office equipment and software	551	20	531
	213,475	71,302	142,173
Other assets held for sale (note 21)	4,229	1,421	2,808
	\$ 217,704	\$ 72,723	\$ 144,981

# ARTIS REAL ESTATE INVESTMENT TRUST

Notes to Consolidated Financial Statements  
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## 5. Other assets (continued):

	December 31, 2007		
	Cost	Accumulated amortization	Net book value
Acquired in-place leases	\$ 168,892	\$ 38,319	\$ 130,573
Above-market rent	1,573	498	1,075
Customer relationships	105	68	37
Tenant inducements and leasing costs	6,864	958	5,906
Recoverable operating costs	2,585	149	2,436
Office equipment and software	55	12	43
	<u>\$ 180,074</u>	<u>\$ 40,004</u>	<u>\$ 140,070</u>

## 6. Deposits on income-producing properties:

	Year Ended December 31, 2008	Year Ended December 31, 2007
Deposit on income-producing property (note 13):		
Balance, beginning of year	\$ 7,330	\$ 7,743
Property rent	(1,200)	(1,200)
Costs incurred	-	215
Distributions on 543,781 Class B units of AX L.P.	582	572
	<u>6,712</u>	<u>7,330</u>
Deposits on other income-producing properties	-	4,496
	<u>\$ 6,712</u>	<u>\$ 11,826</u>

## 7. Notes receivable:

	December 31, 2008	December 31, 2007
Note receivable from tenant maturing in May 2023, bearing interest at 5.894% per annum, repayable in varying blended monthly installments of principal and interest. The note is unsecured and is transferable at the option of the holder. A default under the terms of the note constitutes a default of the lease of the tenant.	\$ 28,536	\$ 30,187
Note receivable maturing in November 2010, bearing interest at 5.06% per annum, repayable in blended monthly instalments of principal and interest of \$2 and is unsecured. The note was received as partial consideration for the sale of Royal Square.	294	307
	<u>\$ 28,830</u>	<u>\$ 30,494</u>



# ARTIS REAL ESTATE INVESTMENT TRUST

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## 8. Mortgages and loans payable:

Substantially all of the REIT's assets have been pledged as security under mortgages and other security agreements. The mortgages and loans payable bear interest at fixed rates, with a weighted-average effective rate of 5.52% at December 31, 2008, a weighted-average nominal rate of 5.42% at December 31, 2008 (effective and nominal at December 31, 2007, 5.51% and 5.42%, respectively), and maturity dates ranging from July 1, 2009 to June 1, 2024.

Principal payment requirements on the mortgages and loans payable as at December 31, 2008 are as follows:

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2009	\$	48,762
2010		89,852
2011		50,351
2012		112,743
2013		115,611
2014 and thereafter		250,155
		<hr/>
		667,474
Net above- and below-market mortgage adjustments		781
Financing costs		(2,378)
Mortgages payable on assets held for sale (note 21)		10,492
		<hr/>
	\$	676,369

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## 9. Convertible debentures:

In conjunction with the private placement offering that closed August 4, 2005, the REIT issued Series A convertible redeemable 7.75% debentures totaling \$15,000. Interest is paid semi-annually on February 4 and August 4. The convertible debentures are convertible into units of the REIT by the holder at \$12.60 after August 4, 2006, and redeemable for cash at the option of the REIT at any time after August 4, 2007 provided that the market price of the units exceeds 150% of the conversion price, and will be redeemable at the option of the REIT at any time after August 4, 2009 provided that the market price of the units exceeds 125% of the conversion price. Debentures that are not converted into units of the REIT are to be repaid in cash on maturity, being August 4, 2010. The convertible debentures are compound financial instruments and the proceeds of the offering, at the time of issue, were allocated between a liability and equity component in the amount of \$12,169 and \$2,831, respectively. The equity component reflects the equity value of the conversion option embedded in the convertible debentures. During the year, Series A convertible debentures with a face value of \$2,550 (2007, \$7,015) were converted and the REIT issued 202,379 (2007, 561,538) units at the exercise price of \$12.60 per unit. The carrying value of the debt component was reduced by \$2,133 (2007, \$5,701), the equity component was reduced by \$482 (2007, \$1,323), future income taxes were increased by \$41 (2007, \$26), with an offsetting increase to capital contributions of \$2,656 (2007, \$7,050) (note 14(b)).

# ARTIS REAL ESTATE INVESTMENT TRUST

Notes to Consolidated Financial Statements  
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## 9. Convertible debentures (continued):

In conjunction with the private placement offering that closed November 9, 2005, the REIT issued Series B convertible redeemable 7.5% debentures totaling \$10,862. Interest is paid semi-annually on May 9 and November 9. The convertible debentures are convertible into units of the REIT by the holder after November 9, 2007 at a price of \$13.50 per unit. The debentures are redeemable for cash at the option of the REIT (i) at any time after November 9, 2007 provided that the market price of the units exceeds 150% of the conversion price; and (ii) at any time after November 9, 2009 provided that the market price of the units exceeds 125% of the conversion price. The debentures rank pari passu with the convertible debentures issued August 4, 2005. Debentures that are not converted into units of the REIT are to be repaid in cash on maturity, being November 9, 2010. The convertible debentures are compound financial instruments and the proceeds of the offering, at the time of issue, were allocated between a liability and equity component in the amount of \$8,715 and \$2,147, respectively. The equity component reflects the equity value of the conversion option embedded in the convertible debentures. During the year, Series B convertible debentures with a face value of \$8,549 were converted and the REIT issued 634,962 units at the exercise price of \$13.50 per unit. The carrying value of the debt component was reduced by \$7,157, the equity component was reduced by \$1,690, future income taxes were increased by \$125, accrued interest was reduced by \$23 for units issued in lieu of interest payable, with an offsetting increase to capital contributions of \$8,995 (note 14(b)). None of the Series B convertible debentures were converted into units of the REIT in fiscal 2007.

In conjunction with the prospectus that closed May 4, 2006, the REIT issued Series C convertible redeemable 6.25% debentures totaling \$30,000. Interest is paid semi-annually on May 31 and November 30. The convertible debentures are convertible into units of the REIT by the holder after May 31, 2009 at a price of \$17.25 per unit. The debentures are redeemable for cash at the option of the REIT (i) at any time after May 31, 2009 provided that the market price of the units exceeds 125% of the conversion price; and (ii) at any time after May 31, 2011. The debentures rank pari passu with the convertible debentures issued August 4, 2005 and November 9, 2005. Debentures that are not converted into units of the REIT are to be repaid in cash on maturity, being May 31, 2013. The convertible debentures are compound financial instruments and the proceeds of the offering, at the time of issue, were allocated between a liability and equity component in the amount of \$22,410 and \$7,590, respectively. The equity component reflects the equity value of the conversion option embedded in the convertible debentures. During the prior year, Series C convertible debentures with a face value of \$80 were converted and the REIT issued 4,636 units at the exercise price of \$17.25 per unit. The carrying value of the debt component was reduced by \$52 and the equity component was reduced by \$21, with an offsetting increase to capital contributions of \$73 (note 14(b)). None of the Series C convertible debentures were converted into units of the REIT in fiscal 2008.

In conjunction with the purchase of the Fort McMurray portfolio (note 3) effective November 30, 2007, the REIT issued a Series D convertible redeemable 5% debenture totaling \$20,000. Interest is paid semi-annually on May 31 and November 30. The convertible debenture is convertible into units of the REIT by the holder after November 30, 2009 at a price of \$17.75 per unit. The debenture is redeemable for cash at the option of the REIT at any time prior to maturity provided that the market price of the units exceeds 120% of the conversion price. The debenture ranks pari passu with the convertible debentures issued August 4, 2005, November 9, 2005 and May 4, 2006. If the debenture is not converted into units of the REIT it is to be repaid in cash on maturity, being November 30, 2014. The convertible debenture is a compound financial instrument and the proceeds of the offering, at the time of issue, were allocated between a liability and equity component in the amount of \$18,875 and \$1,125, respectively. The equity component reflects the equity value of the conversion option embedded in the convertible debenture. None of the Series D convertible debenture was converted into units of the REIT in fiscal 2008 or 2007.

Using a term until maturity, the liability portion of the debentures at the date of issuance represents the present value of the mandatory cash payments of interest plus the present value of the principal amount due under the terms of the debentures discounted at 13%, or in the case of the Series C debentures, 11.75%, being the rate of interest that would be applicable to a debt-only instrument of comparable term and risk. The equity component, which represents the value ascribed to the conversion option issued, is calculated as the difference between the amount issued and the liability component. Interest expense is determined by applying the discount rate against the outstanding liability component of the debentures. The difference between actual interest payments and interest expense is treated as an addition to the liability component of the debentures.

# ARTIS REAL ESTATE INVESTMENT TRUST

Notes to Consolidated Financial Statements  
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## 9. Convertible debentures (continued):

Upon issuance, the Series D convertible debenture was separated into liability and equity components based on the respective estimated fair values at the date of issuance of the convertible debenture. The fair value of the liability component is estimated based on the present value of future interest and principal payments due under the terms of the convertible debenture using a discount rate for similar debt instruments without a conversion feature. The value assigned to the equity component is the estimated fair value ascribed to the holder's option to convert. Interest expense on the Series D convertible debenture is determined by applying an effective interest rate of 6% to the outstanding liability component. The difference between actual cash interest payments and interest expense is accreted to the liability component.

Particulars of the REIT's outstanding convertible debentures as at December 31, 2008 and December 31, 2007 are as follows:

Convertible debenture issue	Series A convertible redeemable	Series B convertible redeemable	Series C convertible redeemable	Series D convertible redeemable	2008	2007
Issue date	August 4, 2005	November 9, 2005	May 4, 2006	November 30, 2007		
Maturity date	August 4, 2010	November 9, 2010	May 31, 2013	November 30, 2014		
Interest rate	7.75%	7.50%	6.25%	5.00%		
Face value	\$ 620	\$ 2,313	\$ 29,920	\$ 20,000	\$ 52,853	\$ 63,952
Equity portion	116	457	7,570	1,125	9,268	11,440
Liability portion	504	1,856	22,350	18,875	43,585	52,512
Accretion to December 31, 2008 and December 31, 2007	78	286	2,080	146	2,590	2,166
Financing costs	(27)	(108)	(1,094)	(40)	(1,269)	(1,946)
Carrying value at December 31, 2008 and December 31, 2007	\$ 555	\$ 2,034	\$ 23,336	\$ 18,981	\$ 44,906	\$ 52,732

Accretion to the carrying value of the debt component was \$1,464 (2007, \$1,713) during the year ended December 31, 2008. The weighted-average effective rate of the debentures at December 31, 2008 is 10.33% (December 31, 2007, 11.06%).

# ARTIS REAL ESTATE INVESTMENT TRUST

Notes to Consolidated Financial Statements  
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## 10. Intangible liabilities:

	December 31, 2008		
	Cost	Accumulated amortization	Net book value
Below-market rent on income-producing properties	\$ 118,260	\$ 27,622	\$ 90,638
Below-market rent on assets held for sale (note 21)	821	273	548
<b>Below-market rent</b>	<b>\$ 119,081</b>	<b>\$ 27,895</b>	<b>\$ 91,186</b>

  

	December 31, 2007		
	Cost	Accumulated amortization	Net book value
Below-market rent	\$ 112,954	\$ 13,674	\$ 99,280

## 11. Accounts payable and other liabilities:

	December 31, 2008	December 31, 2007
Accounts payable and accrued liabilities	\$ 12,133	\$ 8,934
Deposits on income-producing properties held for sale (note 21)	10,000	-
Distributions payable (note 15)	2,976	2,791
	<b>\$ 25,109</b>	<b>\$ 11,725</b>

## 12. Bank indebtedness:

On September 28, 2008, the REIT entered into an amended and restated loan agreement for a revolving term credit facility in the amount of \$60,000, which may be utilized to fund acquisitions of office, retail and industrial properties. \$7,500 of the credit facility is available to purchase units under the normal course issuer bid, \$10,000 may be utilized to provide mezzanine financing, and an additional \$10,000 may be used for general corporate purposes. The credit facility may be extended for an additional year at the REIT's option; if the option is not exercised, the credit facility matures on September 28, 2009. Amounts drawn on the facility will bear interest at a floating rate equal to Canadian dollar bankers' acceptances with a term to maturity of 30 days, plus 3.40% per annum. The credit facility is secured by a first charge on Delta Centre, Grain Exchange Building, Johnston Terminal and Sears Centre. At December 31, 2008, the REIT had utilized \$32,500 (December 31, 2007, \$nil) of the facility.

# ARTIS REAL ESTATE INVESTMENT TRUST

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## 13. Non-controlling interest:

Non-controlling interest represents the amount of equity related to the Class B units of a subsidiary, AX L.P. ("AXLP."). This non-controlling interest has been accounted for in accordance with EIC-151, Exchangeable Securities Issued by Subsidiaries of Income Trusts. The accounts of AXLP are consolidated in these consolidated financial statements. Class B units of AXLP are only exchangeable on a one-for-one basis, at the option of the holder, into REIT units, and are transferable to third parties with the REIT's consent.

Holders of the Class B units of AXLP are entitled to receive distributions on a per unit amount equal to a per REIT unit amount provided to holders of REIT units.

Effective October 31, 2006, the REIT entered into a purchase and sale agreement with a third party whereby the vendor will develop a Class A office building in Calgary, Alberta. The purchase and sale agreement contains a scheduled closing date of November 1, 2008, with the vendor having the option to extend closing for up to an additional 12 months. The final purchase price of the income-producing property is to be calculated in accordance with a pre-determined formula, based on approved leases in place. Should the property be fully leased at the date of acquisition, the purchase price is estimated at \$89,900. In accordance with the agreement, the REIT paid \$7,800 as an interim payment towards the purchase price of the income-producing property, and recorded this amount as a deposit on income-producing properties. As consideration, the REIT issued 543,781 Class B units of AXLP at a price of \$14.34 per unit, and the REIT issued an equal number of special voting units as consideration. The Class B units have been released to the vendors, subject to trading restrictions as set out in the purchase and sale agreement. In accordance with the agreement, the REIT receives monthly property rent of \$100 from the vendor until the closing of the purchase transaction. Distributions paid to the vendor on the Class B units are netted against property rent and any remaining difference is recorded as a reduction to the deposit on the income-producing property. Once the purchase price is known, the remaining consideration will be required to be financed through a combination of mortgage financing and cash consideration.

Effective November 30, 2006, the REIT acquired, through AXLP, an undivided 50% interest in certain lands located in Calgary, Alberta. AXLP entered into a co-ownership agreement with the vendor with respect to a 50% interest in, and the development of, a Class A office building. Both the REIT and the vendor transferred their 50% interest in the lands into the co-ownership. Construction is anticipated to commence when a sufficient level of pre-leasing has been completed. To facilitate the development of the income-producing property, the REIT may be obligated to provide up to \$6,500 of mezzanine financing to the co-ownership, bearing interest at a rate of ten percent per annum. As payment for its interest in the lands, AXLP issued 177,566 Class B units at a price of \$14.71 per unit for aggregate consideration of \$2,612. The REIT also issued an equal number of special voting units.

The details of the non-controlling interest are as follows:

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Issuance of 543,781 Class B units of AXLP on October 31, 2006	\$	7,800
Issuance of 177,566 Class B units of AXLP on November 30, 2006		2,612
Costs relating to the issuance of Class B units of AXLP		(13)
Distributions on 177,566 Class B units of AXLP		(31)
<hr/>		
Balance at December 31, 2006		10,368
Distributions on 177,566 Class B units of AXLP		(186)
<hr/>		
Balance at December 31, 2007		10,182
Distributions on 177,566 Class B units of AXLP		(189)
Non-controlling interest from continuing operations		247
Non-controlling interest from discontinued operations (note 21)		18
<hr/>		
Balance at December 31, 2008	\$	10,258

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# ARTIS REAL ESTATE INVESTMENT TRUST

Notes to Consolidated Financial Statements  
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## 14. Capital contributions:

### (a) Authorized:

In accordance with the Declaration of Trust, the REIT may issue an unlimited number of units, with each unit representing an equal fractional undivided beneficial interest in any distributions from the REIT, and in the net assets in the event of termination or wind-up of the REIT. All units are of the same class with equal rights and privileges. The units are redeemable at any time at the option of the holder at a price defined in the Declaration of Trust, subject to a maximum of \$30 in cash redemptions by the REIT in any one month. Redemptions in excess of this amount will be paid by way of a distribution of notes of the REIT, or the notes of a wholly-owned subsidiary of the REIT.

In accordance with the Declaration of Trust, the REIT may also issue a class of special voting units, which are non-participating voting units of the REIT, to be issued to holders of securities which are exchangeable for units of the REIT (note 13). Special voting units are cancelled on the issuance of REIT units on exercise, conversion or cancellation of the corresponding exchangeable securities.

### (b) Issued and outstanding:

	Number of units	Amount
Balance at December 31, 2006	15,219,261	\$ 164,991
Public offerings, net of issue costs of \$10,709 (net of future income taxes of \$1,089)	15,270,000	248,572
Conversion of Series A convertible debentures	561,538	7,050
Conversion of Series C convertible debentures	4,636	73
Options exercised	81,355	1,223
Distribution Reinvestment Plan ("DRIP")	34,278	553
Units acquired through normal course issuer bid, not cancelled at year end	(13,000)	(196)
<b>Balance at December 31, 2007</b>	<b>31,158,068</b>	<b>422,266</b>
Conversion of Series A convertible debentures	202,379	2,656
Conversion of Series B convertible debentures	634,962	8,995
Options exercised	22,752	263
Distribution Reinvestment Plan ("DRIP")	411,297	4,875
Units issued on acquisition of income-producing property	118,308	2,100
Units acquired and cancelled through normal course issuer bid	(197,400)	(2,673)
Units acquired through normal course issuer bid, not cancelled at year end	(43,600)	(226)
<b>Balance at December 31, 2008</b>	<b>32,306,766</b>	<b>\$ 438,256</b>

At December 31, 2008, there were 721,347 special voting units issued and outstanding (note 13). There is no value assigned to the special voting units.

The REIT has a Distribution Reinvestment Plan ("DRIP") which allows Unitholders the option to elect to receive all or a portion of their regular monthly distributions in additional REIT units.

# ARTIS REAL ESTATE INVESTMENT TRUST

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## 14. Capital contributions (continued):

(c) Contributed surplus:

	Year Ended December 31, 2008	Year Ended December 31, 2007
Balance, beginning of year	\$ 1,518	\$ 649
Unit based compensation expense	567	1,039
Units purchased and cancelled under normal course issuer bid (note 14 (f))	552	-
Value of options exercised	(47)	(170)
<b>Balance, end of year</b>	<b>\$ 2,590</b>	<b>\$ 1,518</b>

Contributed surplus includes the recording of the fair value of options granted under the unit option plan (see note 14(d)). The fair value of the options is recorded to contributed surplus as the options vest. Upon exercise, the proceeds received, as well as any balance previously recorded to contributed surplus, are credited to capital contributions.

(d) Unit options:

The REIT has a unit option plan which is administered by the Board of Trustees of the REIT with unit options granted to trustees, management, management company employees and consultants as a form of compensation. The total number of units reserved under option for issuance may not exceed 5% of the units outstanding.

A summary of the REIT's unit options for the year ended ended December 31 are as follows:

	2008		2007	
	Units	Weighted average exercise price	Units	Weighted average exercise price
Balance, beginning of year	1,481,088	\$ 15.47	729,393	\$ 13.20
Granted	-	-	898,050	17.07
Exercised	(22,752)	11.25	(81,355)	12.94
Expired	-	-	(65,000)	15.25
<b>Balance, end of year</b>	<b>1,458,336</b>	<b>\$ 15.52</b>	<b>1,481,088</b>	<b>\$ 15.47</b>
Options exercisable at end of year	787,212		423,107	
Weighted-average fair value per unit of options granted during the year		\$ -		\$ 1.21

# ARTIS REAL ESTATE INVESTMENT TRUST

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## 14. Capital contributions (continued):

(d) Unit options (continued):

Options outstanding at December 31, 2008 consist of the following:

Range of exercise prices	Number outstanding	Weighted-average remaining contractual life	Options outstanding weighted-average exercise price	Number exercisable
\$11.25	217,036	2 years	\$11.25	145,938
\$14.40	380,500	2.75 years	\$14.40	281,000
\$15.85	269,750	3 years	\$15.85	132,750
\$17.60	319,050	3.5 years	\$17.60	159,524
\$17.75	272,000	3.75 years	\$17.75	68,000
	1,458,336		\$ 15.52	787,212

The compensation expense related to unit options granted under the unit option plan for the year ended December 31, 2008 amounted to \$567 (2007, \$1,039). The balance of contributed surplus at December 31, 2008 relates to unexercised options. The compensation expense was determined based on the fair value of the options at the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions:

	2008	2007
Expected option life	-	3.8 years
Risk-free interest rate	-	4.38%
Dividend yield	-	6.11%
Expected volatility	-	16.1%



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## 14. Capital contributions (continued):

(e) Weighted-average units:

	Year Ended December 31,	
	2008	2007
Income (loss)	\$ (6,790)	\$ 6,157
Diluted income (loss)	\$ (6,790)	\$ 6,157
The weighted-average number of units outstanding was as follows:		
Basic units	32,088,592	24,616,119
Effect of dilutive securities:		
Class B units of AXLP	-	721,347
Unit option plan	-	139,955
Diluted units	32,088,592	25,477,421
Income (loss) per unit:		
Basic	\$ (0.21)	\$ 0.25
Diluted	\$ (0.21)	\$ 0.24

The computation of diluted loss per unit for the year ended December 31, 2008 does not include Class B units, convertible debentures and unit options as these instruments are anti-dilutive. The computation of diluted income per unit for the year ended December 31, 2007 does not include convertible debentures as these instruments are anti-dilutive.

(f) Normal course issuer bid:

On December 11, 2008, the REIT announced that the Toronto Stock Exchange (the "Exchange") had approved the renewal of its normal course issuer bid. Under the renewed bid, the REIT will have the ability to purchase for cancellation up to a maximum of 3,122,697 units, representing 10% of the REIT's float of 31,226,967 on December 15, 2008. Purchases will be made at market prices through the facilities of the Exchange. The bid commenced on December 14, 2007, was extended for an additional one-year period on December 15, 2008, and will remain in effect until the earlier of December 14, 2009, or the date on which the REIT has purchased the maximum number of units permitted under the bid. During the year ended December 31, 2008, the REIT acquired 241,000 units and cancelled 197,400 units at market prices aggregating \$2,447, resulting in excess of redemption proceeds over stated capital of \$112, which was charged to the deficit. As a result of purchases that were for amounts less than stated capital, \$552 was recorded to contributed surplus. Since December 14, 2007, the REIT had acquired, to December 31, 2008, 254,000 units for cancellation.

# ARTIS REAL ESTATE INVESTMENT TRUST

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Years ended December 31, 2008 and 2007

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## 15. Distributions to unitholders:

Distributable Income, which is defined in the Declaration of Trust, means net income in accordance with generally accepted accounting principles, subject to certain adjustments as set out in the Declaration of Trust, including: (i) adding back amortization (excluding leasing costs) and accretion to the carrying value of debt and (ii) excluding gains or losses on the disposition of any asset, and (iii) adding or deducting other adjustments as determined by the Trustees at their discretion. Distributable Income is not a generally accepted accounting principles financial measure and should not be construed as an alternative to net income or cash flow from operating activities determined in accordance with generally accepted accounting principles as an indicator of the REIT's performance.

The REIT declared distributions to REIT unitholders of record in the amount of \$34,352 for the year ended December 31, 2008 (2007, \$26,348). The REIT declared distributions to the holders of Class B units of AXLP in the amount of \$771 for the year ended December 31, 2008 (2007, \$758). Total distributions payable at December 31, 2008 are \$2,976 (December 31, 2007, \$2,791).

## 16. Changes in non-cash operating items:

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	Year Ended December 31,	
	2008	2007
Recoverable operating costs	\$ (3,819)	\$ (2,029)
Amortization of recoverable operating costs	490	149
Prepaid expenses	(783)	(514)
Rent and other receivables	(2,350)	(2,235)
Cash held in trust	94	(355)
Security deposits and prepaid rent	789	2,639
Accounts payable and other liabilities	3,384	4,492
	<hr/>	<hr/>
	\$ (2,195)	\$ 2,147

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# ARTIS REAL ESTATE INVESTMENT TRUST

Notes to Consolidated Financial Statements  
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## 17. Related party transactions:

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	Year Ended December 31,	
	2008	2007
Legal fees expensed	\$ 151	\$ 101
Capitalized legal fees	480	1,775
Advisory fees	2,514	1,693
Capitalized acquisition fees	535	3,047
Property management fees	5,056	3,052
Capitalized leasing commissions	3,796	2,224
Capitalized building improvements	11,675	760
Tenant inducements	114	642
Recoverable operating costs	187	-

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The REIT incurred legal fees with a law firm associated with a trustee of the REIT in connection with the property acquisitions and general business matters. The amount payable at December 31, 2008 is \$nil (December 31, 2007, \$nil).

The REIT incurred advisory fees and acquisition fees under the asset management agreement with Marwest Management Canada Ltd. ("Marwest"), a company owned and controlled by certain trustees and officers of the REIT. The amount payable at December 31, 2008 is \$nil (December 31, 2007, \$nil). Under the asset management agreement, Marwest is entitled to an annual advisory fee equal to 0.25% of the adjusted cost base of the REIT's assets and an acquisition fee equal to 0.5% of the cost of each property acquired.

The REIT incurred property management fees, leasing commission fees, and tenant improvement fees under the property management agreement with Marwest. The amount payable at December 31, 2008 is \$546 (December 31, 2007, \$nil). Marwest acts as the general property manager for the REIT's properties and is entitled to management fees, leasing renewal commissions and tenant improvement fees at commercially reasonable rates.

The REIT incurred costs for building improvements and tenant inducements paid to Marwest Construction Ltd., a company related to certain trustees and officers of the REIT. The amount payable at December 31, 2008 is \$292 (December 31, 2007, \$nil).

During 2008, the REIT acquired an income-producing property from entities under the control of certain Trustees of the REIT for an aggregate purchase price of \$1,500.

These transactions are in the normal course of operations and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

## 18. Future income taxes:

The REIT currently qualifies as a mutual fund trust for Canadian income tax purposes. Prior to new legislation relating to the federal income taxation of publicly listed or traded trusts, as discussed below, income earned by the REIT and distributed annually to unitholders was not, and would not be, subject to taxation in the REIT, but was taxed at the individual unitholder level. For financial statement reporting purposes, the tax deductibility of the REIT's distributions was treated as an exception from taxation as the REIT distributed, and was committed to continue distributing, all of its taxable income to its unitholders. Accordingly, the REIT did not previously record a provision for income taxes or future income tax assets or liabilities.

On June 22, 2007, new legislation relating to, among other things, the federal income taxation of a specified investment flow-through trust or partnership (a "SIFT") was enacted (the "New SIFT Rules"). A SIFT includes a publicly-listed or traded partnership or trust, such as an income trust.

# ARTIS REAL ESTATE INVESTMENT TRUST

Notes to Consolidated Financial Statements  
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## 18. Future income taxes (continued):

Under the New SIFT Rules, following a transition period for qualifying SIFTs, certain distributions from a SIFT will no longer be deductible in computing a SIFT's taxable income, and a SIFT will be subject to tax on such distributions at a rate that is substantially equivalent to the general tax rate applicable to a Canadian corporation. However, distributions paid by a SIFT as returns of capital should generally not be subject to the tax.

The New SIFT Rules do not apply to a "real estate investment trust" that meets prescribed conditions relating to the nature of its assets and revenue (the "REIT Conditions"). The REIT is currently reviewing the New SIFT Rules and is assessing their interpretation and application to the REIT's assets and revenues. There are uncertainties in the interpretation and application of the New SIFT Rules and it is not possible, at the current time, to determine with certainty whether the REIT will meet the REIT Conditions.

The New SIFT Rules provide that a SIFT which was publicly traded before November 1, 2006 will become subject to the tax on distributions commencing with the 2011 taxation year. However, a SIFT may become subject to this tax prior to 2011 if its equity capital increases beyond certain limits measured against the market capitalization of the SIFT at the close of trading on October 31, 2006 (the "Safe Harbour Limits"). In the case of the REIT, its subsequent offerings have exceeded the Safe Harbour Limits. Therefore, commencing on January 1, 2007, subject to the REIT's ability to meet the REIT Conditions, the REIT is subject to tax on certain income which may adversely impact the level of cash otherwise available for distribution.

If the REIT does not meet the REIT Conditions, the REIT may restructure its affairs in order to minimize, or if possible eliminate, the impact of the New SIFT Rules, if such restructuring is in the best interests of unitholders. There can be no assurances, however, that the REIT would be able to restructure such that the REIT would not be subject to the tax imposed by the New SIFT Rules, or that any such restructuring, if implemented, would not result in material costs or other adverse consequences to the REIT and its unitholders.

Under the New SIFT Rules, a flow-through subsidiary of the REIT may also be a SIFT. Certain technical amendments to the SIFT definition to exclude certain flow-through subsidiaries of a SIFT that are able to meet certain ownership conditions were passed into law on March 12, 2009.

# ARTIS REAL ESTATE INVESTMENT TRUST

Notes to Consolidated Financial Statements  
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## 18. Future income taxes (continued):

The tax effects of temporary differences that give rise to significant portions of the future tax asset are as follows:

	December 31, 2008	December 31, 2007
Future income tax assets (liabilities):		
Income-producing properties, other assets and intangible liabilities	\$ 10,654	\$ 8,395
Unit issue costs	2,679	4,282
Other	(2,206)	(1,168)
Future income tax assets	\$ 11,127	\$ 11,509

A reconciliation of expected income taxes based upon the statutory rates to the recorded income tax (recovery) expense after discontinued operations is as follows:

	December 31, 2008	December 31, 2007
Income tax expense (recovery) computed at the Canadian statutory rate of 30.45% (2007 - 35.12%) applicable to the REIT	\$ (1,820)	\$ (1,453)
Future income taxes arising from a change in tax status with the enactment of the SIFT rules	-	(11,080)
Non-deductible unit based compensation expense	173	365
Accretion in liability component of convertible debenture	378	497
Other permanent differences	5	(15)
Reduction of future income taxes arising from changes in tax rates	1,453	1,292
Other	359	-
Future income tax expense (recovery)	\$ 548	\$ (10,394)

# ARTIS REAL ESTATE INVESTMENT TRUST

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## 19. Co-ownership activities:

These consolidated financial statements include the REIT's proportionate share of assets, liabilities, revenue, expenses and cash flows of the co-ownerships in which it participates. The REIT is contingently liable for the obligations of its associates in certain co-ownerships. Management believes that the assets of the co-ownerships are available and are sufficient for the purpose of satisfying such obligations. The REIT's proportionate share of these co-ownerships range between 38% and 85%, summarized as follows:

	December 31, 2008	December 31, 2007
Assets	\$ 69,068	\$ 72,871
Liabilities	70,708	73,232

  

	December 31, 2008	December 31, 2007
Revenue	11,200	5,511
Expenses	10,039	5,872
Operating income (loss) from properties	1,161	(361)
Cash flows provided by operating activities	1,382	1,107
Cash flows used in investing activities	(378)	(22,247)
Cash flows provided by (used in) financing activities	(1,343)	21,897

## 20. Segmented information:

The REIT owns and operates various retail, office and industrial properties located in western Canada. Information related to these property types is presented below. REIT expenses as well as interest and amortization of financing costs relating to the convertible debentures have not been allocated to the segments.

	Year Ended December 31, 2008				
	Retail	Office	Industrial	REIT	Total
Revenue	\$ 49,678	\$ 77,627	\$ 15,090	\$ 581	\$ 142,976
Property operating expenses	14,289	26,418	4,538	-	45,245
	35,389	51,209	10,552	581	97,731
Interest	12,577	18,608	3,790	6,072	41,047
Corporate expenses	-	-	-	4,969	4,969
Amortization	19,677	30,581	7,834	47	58,139
Unrealized gain on commodity derivatives	-	-	-	(223)	(223)
	32,254	49,189	11,624	10,865	103,932
	3,135	2,020	(1,072)	(10,284)	(6,201)
Future income tax expense	-	-	-	(457)	(457)
Non-controlling interest	-	-	-	(247)	(247)
Income from discontinued operations	-	312	(197)	-	115
Income (loss) for the year	\$ 3,135	\$ 2,332	\$ (1,269)	\$ (10,988)	\$ (6,790)
Total assets	\$ 420,084	\$ 654,553	\$ 147,113	\$ 22,536	\$ 1,244,286

# ARTIS REAL ESTATE INVESTMENT TRUST

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## 20. Segmented information (continued):

	Year Ended December 31, 2007				
	Retail	Office	Industrial	REIT	Total
Revenue	\$ 33,067	\$ 55,449	\$ 7,118	\$ 2,074	\$ 97,708
Property operating expenses	9,669	19,644	1,738	-	31,051
	23,398	35,805	5,380	2,074	66,657
Interest	8,702	12,323	1,883	5,014	27,922
Corporate expenses	-	-	-	4,798	4,798
Amortization	13,759	22,810	3,943	45	40,557
	22,461	35,133	5,826	9,857	73,277
	937	672	(446)	(7,783)	(6,620)
Future income tax recovery	-	-	-	10,833	10,833
Loss from discontinued operations	2,511	(567)	-	-	1,944
Income (loss) for the year	\$ 3,448	\$ 105	\$ (446)	\$ 3,050	\$ 6,157
Total assets	\$ 381,908	\$ 637,582	\$ 114,923	\$ 42,035	\$ 1,176,448

## 21. Income from discontinued operations:

The REIT has entered into an unconditional agreement to sell two office properties in Calgary, Alberta; Airways Business Plaza and Glenmore Commerce Court. The properties will be sold for an aggregate of \$24,900, to be satisfied with the assumption of mortgages payable and cash consideration, of which \$10,000 has been received at December 31, 2008. The sale will result in an estimated gain of \$6,400. The disposition was originally expected to close in the third quarter of 2008, however the closing has been rescheduled to the first quarter of 2009. In 2008, the REIT disposed of a portion of an income-producing property for a loss of \$197. In 2007, the REIT disposed of an income-producing property for a gain of \$2,511. The results of operations from these properties have been separately disclosed below:

	Year Ended December 31,	
	2008	2007
Revenue	\$ 3,200	\$ 1,551
Property operating expenses	1,512	739
	1,688	812
Interest	563	272
Amortization	704	668
Net property operating income (loss)	421	(128)
Gain (loss) on disposal of income-producing properties	(197)	2,511
Future income tax (expense) recovery (note 18)	(91)	(439)
Non-controlling interest (note 13)	(18)	-
Income from discontinued operations	\$ 115	\$ 1,944

# ARTIS REAL ESTATE INVESTMENT TRUST

Notes to Consolidated Financial Statements  
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## 22. Commitments and guarantees:

(a) Letters of credit:

As of December 31, 2008, the REIT had issued letters of credit in the amount of \$2,215 (December 31, 2007, \$1,700).

(b) Guarantee:

AXLP has guaranteed certain debt assumed by a purchaser in connection with the disposition of Royal Square. This guarantee will remain until the debt is modified, refinanced or extinguished. Credit risk arises in the event that the purchaser defaults on repayment of their debt since it is guaranteed by the REIT. This credit risk is mitigated as the REIT has recourse under this guarantee in the event of default by the purchaser, in which case the REIT would have a claim against the underlying property. The estimated amount of debt subject to the guarantee at December 31, 2008, is \$1,649 (December 31, 2007, \$1,709), with an estimated weighted-average remaining term of 1.8 years (December 31, 2007, 2.8 years). No liability in excess of the fair value of the guarantee has been recognized in these consolidated financial statements as the estimated fair value of the borrower's interest in the underlying property is greater than the mortgage payable for which the REIT provided the guarantee.

## 23. Capital management:

The REIT's objectives when managing capital are to safeguard the ability to continue as a going concern, and to generate sufficient returns to provide unitholders with stable cash distributions. The REIT defines capital as bank indebtedness, mortgages and loans payable, convertible debentures, non-controlling interest and unitholders' equity.

The REIT's Declaration of Trust permits the REIT to incur indebtedness, provided that after giving effect to incurring or assuming any indebtedness (as defined in the Declaration of Trust), the amount of such indebtedness of the REIT is not more than 70% of the gross book value of the REIT's total assets. Gross book value is defined in the Declaration of Trust as "the consolidated book value of the assets of the REIT, plus the amount of accumulated depreciation and amortization recorded in the books and records of the REIT, plus the amount of any future income tax liability arising out of any indirect acquisitions, calculated in accordance with generally accepted accounting principles". As at December 31, 2008, the ratio of such indebtedness to gross book value was 51.6% (December 31, 2007, 49.2%), which complies with the requirement in the Declaration of Trust and is consistent with the REIT's objectives.

In addition to the covenant outlined in the Declaration of Trust, the REIT must maintain a debt to gross book value ratio of 70%, a debt service coverage ratio of 1.4, and minimum unitholders' equity of \$275,000 for the purposes of the credit facility (note 12). As at December 31, 2008, the REIT was in compliance with these requirements.

The REIT's mortgage providers also have minimum limits on debt service coverage ratios. The REIT monitors these ratios and is in compliance with these requirements.

The total managed capital for the REIT is summarized below:

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	December 31, 2008	December 31, 2007
Mortgages and loans payable	\$ 676,369	\$ 612,996
Convertible debentures	44,906	52,732
Bank indebtedness	32,500	-
Total debt	753,775	665,728
Non-controlling interest	10,258	10,182
Unitholders' equity	359,136	385,500
	\$ 1,123,169	\$ 1,061,410

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# ARTIS REAL ESTATE INVESTMENT TRUST

Notes to Consolidated Financial Statements  
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## 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) Market risk:

##### (a) Interest rate risk:

The REIT is exposed to interest rate risk on its borrowings. It minimizes the risk by restricting debt to 70% of gross book value and by obtaining fixed rate debt to replace short-term floating rate borrowings. In addition, management considers the weighted-average term to maturity of long-term debt relative to the remaining average lease terms. At December 31, 2008, the REIT is a party to \$45,396 of variable rate debt, including the outstanding balance of bank indebtedness.

##### (b) Other price risk:

The REIT periodically enters into derivative transactions in regards to non-financial items, primarily natural gas and electrical contracts, to manage the price risk arising from fluctuations in these commodities.

#### (ii) Credit risk:

The REIT is exposed to credit risk as an owner of real estate in that tenants may become unable to pay the contracted rents. Management mitigates this risk by carrying out appropriate credit checks and related due diligence on the significant tenants. Management has diversified the REIT's holdings so that it owns several categories of properties (retail, office and industrial) and acquires properties throughout Western Canada. The allowance for doubtful accounts at December 31, 2008 was \$336, and \$154 at December 31, 2007. The credit quality of the rent and other receivables amount is considered adequate.

The REIT is also exposed to credit risk as a holder of notes receivable. Management mitigates this risk by carrying out appropriate credit checks and related due diligence of the borrowers.

#### (iii) Liquidity risk:

Liquidity risk is the risk that the REIT will not be able to meet its financial obligations as they come due. The REIT manages liquidity by maintaining adequate cash and by having appropriate lines of credit available. In addition, the REIT continuously monitors and reviews both actual and forecasted cash flows.

The following are the estimated maturities of the REIT's mortgages, loans, bank indebtedness and convertible debentures, with convertible debentures disclosed at their face value:

	Total	Less than 1 year	1 - 3 years	4 - 5 years	After 5 years
Mortgages, loans and bank indebtedness	\$ 710,466	\$ 91,754	\$ 140,203	\$ 228,354	\$ 250,155
Convertible debentures	52,853	-	2,933	29,920	20,000
	<u>\$ 763,319</u>	<u>\$ 91,754</u>	<u>\$ 143,136</u>	<u>\$ 258,274</u>	<u>\$ 270,155</u>

# ARTIS REAL ESTATE INVESTMENT TRUST

Notes to Consolidated Financial Statements  
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## 24. Risk management and fair values (continued):

### (b) Fair values:

The fair value of the REIT's rent and other receivables, accounts payable and other liabilities, and bank indebtedness approximate their carrying amounts due to the relatively short periods to maturity of these financial instruments.

The fair value of the notes receivable has been determined by discounting the cash flows of these financial assets using year end market rates for assets of similar terms and credit risks. Based on these assumptions, the fair value of notes receivable at December 31, 2008 has been estimated at \$29,203 (December 31, 2007, \$30,530), compared with the carrying value of \$28,830 (December 31, 2007, \$30,494).

The fair value of the mortgages and loans payable has been determined by discounting the cash flows of these financial obligations using year end market rates for debt of similar terms and credit risks. Based on these assumptions, the fair value of mortgages and loans payable at December 31, 2008 has been estimated at \$675,918 (December 31, 2007, \$607,981) compared with the carrying value of \$676,369 (December 31, 2007, \$612,996).

The fair value of the REIT's convertible debentures is \$39,867 (December 31, 2007, \$66,072) compared to its face value of \$52,853 (December 31, 2007, \$63,952) at December 31, 2008. Fair value is based on the market price of the debentures, or if no market price exists, fair value is determined by discounting the cash flows of these financial obligations using year end market rates for debt of similar terms and credit risks.

As at December 31, 2008, the REIT had entered into natural gas and electrical contracts with a fair value of \$223.

## 25. Future changes in accounting policies:

The CICA has issued a new accounting standard, Section 3064, Goodwill and Intangible Assets, which clarifies that costs can be capitalized only when they relate to an item that meets the definition of an asset. The REIT is in the process of evaluating the impact of this standard on its consolidated financial statements. Section 1000, Financial Statement Concepts, was also amended to provide consistency with this new standard. The new and amended standards will be effective for the REIT in the first quarter of 2009.

In February 2008, The Canadian Accounting Standards Board ("AcSB") confirmed that the adoption of International Financial Reporting Standards ("IFRS") would be effective for interim and annual periods beginning on or after January 1, 2011 for profit-oriented Canadian publicly accountable enterprises. IFRS will replace Canada's current GAAP for these enterprises. Comparative IFRS information for the previous fiscal year will also have to be reported. These new standards will be effective for the REIT in the first quarter of 2011.

The REIT's management is currently in the process of evaluating the potential impact of IFRS to the consolidated financial statements. This will be an ongoing process as new standards and recommendations are issued by the International Accounting Standards Board and the AcSB. The REIT's consolidated financial performance and financial position as disclosed in the current GAAP financial statements may be significantly different when presented in accordance with IFRS.

# ARTIS REAL ESTATE INVESTMENT TRUST

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## **26. Subsequent events:**

The REIT has entered into an unconditional agreement to dispose of the Plainsman Building for proceeds of \$8,050. The REIT anticipates that the disposition will close on March 31, 2009, and the sale price will be financed through a combination of the assumption of existing mortgage financing and cash consideration. The carrying value of the assets to be disposed of is \$7,465.

The REIT has completed the refinancing of the mortgage related to Sunridge Home Outfitters. The mortgage is for \$6,500, with an interest rate of 4.65% and a term of 3 years. The refinancing replaces the previous mortgage of \$5,134, which carried interest at 6.176%.

## **27. Comparative figures:**

Certain 2007 comparative figures have been reclassified to conform with the financial statement presentation adopted in 2008.