

Financial Statements  
(Expressed in U.S. dollars)

# **FIRST LEASIDE PROPERTIES FUND**

Year ended December 31, 2008 and period  
from July 3, 2007 to December 31, 2007



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## AUDITORS' REPORT

To the Unitholders of First Leaside Properties Fund

We have audited the balance sheets of First Leaside Properties Fund as at December 31, 2008 and 2007 and the statements of operations and comprehensive income, unitholders' equity and cash flows for the year ended December 31, 2008 and the period from July 3, 2007 to December 31, 2007. These financial statements are the responsibility of the Fund'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 financial statements present fairly, in all material respects, the financial position of the Fund as at December 31, 2008 and 2007 and the results of its operations and its cash flows for the year ended December 31, 2008 and the period from July 3, 2007 to December 31, 2007 in accordance with Canadian generally accepted accounting principles.

Chartered Accountants, Licensed Public Accountants

Toronto, Canada

April 29, 2009

# FIRST LEASIDE PROPERTIES FUND

Balance sheets  
(Expressed in U.S. dollars)

December 31, 2008 and 2007

	2008	2007
<b>Assets</b>		
Current assets:		
Cash	\$ 1,783	\$ 116,485
Due from entities within the First Leaside Group of Companies (note 7)	188,897	122,165
	<u>190,680</u>	<u>238,650</u>
Promissory notes receivable (note 2)	3,105,534	3,678,312
	<u>\$ 3,296,214</u>	<u>\$ 3,916,962</u>

## Liabilities and Unitholders' Equity

Current liabilities:		
Accounts payable and accrued liabilities	\$ 181,840	\$ 125,469
Due to entities within the First Leaside Group of Companies (note 7)	8,947	113,181
	<u>190,787</u>	<u>238,650</u>
Call premium derivative (note 2)	26,000	24,000
Redeemable units (note 3)	2,431,238	2,943,858
Unitholders' equity (note 5)	648,189	710,454
Subsequent events (note 11)		
	<u>\$ 3,296,214</u>	<u>\$ 3,916,962</u>

See accompanying notes to financial statements.

Approved on behalf of the Trustees:

"Robin Pullen" \_\_\_\_\_ Trustee

"Robert Gould" \_\_\_\_\_ Trustee

# FIRST LEASIDE PROPERTIES FUND

Statements of Operations and Comprehensive Income  
(Expressed in U.S. dollars)

Year ended December 31, 2008 and period from July 3, 2007 to December 31, 2007

	2008	2007
Revenue:		
Interest and other	\$ 316,904	\$ 67,157
Recovery of costs (note 4)	620,061	372,226
	<u>936,965</u>	<u>439,383</u>
Expenses:		
Interest	253,525	55,611
Administration	620,061	372,226
Change in fair value of call premium derivative	2,000	8,000
	<u>875,586</u>	<u>435,837</u>
Net income	61,379	3,546
Other comprehensive income (loss):		
Foreign currency translation	(145,605)	13,979
Comprehensive income (loss)	<u>\$ (84,226)</u>	<u>\$ 17,525</u>
Net income per unit	\$ 0.08	\$ 0.01
Weighted average number of units outstanding	758,260	277,500

See accompanying notes to financial statements.

# FIRST LEASIDE PROPERTIES FUND

Statements of Unitholders' Equity  
(Expressed in U.S. dollars)

Year ended December 31, 2008 and period from July 3, 2007 to December 31, 2007

	Class C units Number	Amount	Accumulated other comprehensive income (loss)	Total
Unitholders' equity, December 31, 2006	–	\$ –	\$ –	\$ –
Net income	–	3,546	–	3,546
Units issued	911,674	905,907	–	905,907
Distributions	–	(12,364)	–	(12,364)
Distributions reinvested	12,257	12,364	–	12,364
Unit redemptions	(211,039)	(212,978)	–	(212,978)
Foreign currency translation	–	–	13,979	13,979
Unitholders' equity, December 31, 2007	712,892	696,475	13,979	710,454
Net income	–	61,379	–	61,379
Units issued	22,405	21,961	–	21,961
Distributions	–	(64,111)	–	(64,111)
Distributions reinvested	68,331	64,111	–	64,111
Foreign currency translation	–	–	(145,605)	(145,605)
Unitholders' equity, December 31, 2008	803,628	\$ 779,815	\$ (131,626)	\$ 648,189

See accompanying notes to financial statements.

# FIRST LEASIDE PROPERTIES FUND

Statements of Cash Flows  
(Expressed in U.S. dollars)

Year ended December 31, 2008 and period from July 3, 2007 to December 31, 2007

	2008	2007
Cash provided by (used in):		
Operating activities:		
Net income	\$ 61,379	\$ 3,546
Items not involving cash:		
Change in fair value of call premium derivative	2,000	8,000
Non-cash interest income	(64,111)	-
Non-cash interest on promissory notes receivable	772	712
Transactions with entities within the		
First Leaside Group of Companies	(162,646)	108,966
Change in non-cash operating working capital	56,371	3,304
	(106,235)	124,528
Financing activities:		
Issuance of redeemable units	116,680	2,970,594
Redemption of Class C units	-	(212,978)
Redemption of redeemable units	(70,969)	(48,093)
Issuance of Class C units	21,961	905,907
	67,672	3,615,430
Investing activities:		
Investment in promissory notes receivable	(138,641)	(3,876,501)
Repayment of promissory notes receivable	70,969	261,071
	(67,672)	(3,615,430)
Effect of exchange rate changes on cash	(8,467)	(8,043)
Increase (decrease) in cash	(114,702)	116,485
Cash, beginning of period	116,485	-
Cash, end of period	\$ 1,783	\$ 116,485
Supplemental disclosure of non-cash financing and investing activities:		
Distributions reinvested	\$ 64,111	\$ 12,364
Fair value of call premium	-	16,000

See accompanying notes to financial statements.

# FIRST LEASIDE PROPERTIES FUND

Notes to Financial Statements  
(Expressed in U.S. dollars)

Year ended December 31, 2008 and period from July 3, 2007 to December 31, 2007

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First Leaside Properties Fund (the "Fund") is an open-ended mutual fund trust that has been established by way of a Declaration of Trust (the "Declaration of Trust") made as of July 3, 2007, amended and restated as of September 30, 2008, under the laws of the Province of Ontario, terminating on July 31, 2037 (note 11(b)). The Fund's investment objectives are to invest its funds in securities and investments of persons engaged in the ownership of primarily income-producing multiple-unit residential real property located in Canada and the United States.

## 1. Significant accounting policies:

### (a) Basis of presentation:

These financial statements are presented in U.S. dollars and are prepared in accordance with accounting principles generally accepted in Canada.

### (b) Investment income:

Investment income, which consists of interest income, is recorded on the accrual basis.

### (c) Foreign currency:

The Fund's functional currency is Canadian dollars but reporting currency is U.S. dollars. The translation of the items on the statement of operations and comprehensive income and cash flows into U.S. dollars is done using the exchange rates in effect at the date of the transaction and assets and liabilities are translated using the exchange rate at the end of the year. The exchange differences from the foregoing translation procedures are reported in a separate component of other comprehensive income.

### (d) Income taxes:

The Fund currently qualifies as a Mutual Fund Trust for Canadian income tax purposes (note 11(b)). Income earned by the Fund and distributed annually to unitholders is not subject to taxation in the Fund, but is taxed at the individual unitholder level. For financial statement reporting purposes, the tax deductibility of the Fund distributions is treated as an exemption from taxation as the Fund distributes and is committed to continue distributing all of its taxable income to its unitholders.

# FIRST LEASIDE PROPERTIES FUND

Notes to Financial Statements (continued)  
(Expressed in U.S. dollars)

Year ended December 31, 2008 and period from July 3, 2007 to December 31, 2007

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## 1. Significant accounting policies (continued):

On June 22, 2007, new legislation relating to the federal income taxation of a specified investment flow-through trust or partnership ("SIFT") received royal assent (the "SIFT Rules").

Under the SIFT Rules, 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. Distributions paid by a SIFT as returns of capital will not be subject to the tax.

The Fund is not subject to the SIFT tax regime as its units are not listed on a stock exchange or other public market.

Accordingly, the Fund does not record a provision for income taxes, or future income tax assets or liabilities, in respect of the Fund.

### (e) Revenue recognition:

Interest income on promissory notes receivable and recovery of costs under the cost/payment reimbursement agreement with FL Master Sherman, Ltd. ("Master Sherman") (note 4) is recognized on an accrual basis in the period earned.

### (f) Use of estimates:

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

The most significant estimates that the Fund is required to make relate to the recoverability of its promissory notes receivable.

The estimates of fair value may depend upon, among other things, assumptions regarding local real estate market conditions, property and income taxes, interest rates and the availability, cost and terms of financing and other factors affecting the profitability of the borrower.

# FIRST LEASIDE PROPERTIES FUND

Notes to Financial Statements (continued)  
(Expressed in U.S. dollars)

Year ended December 31, 2008 and period from July 3, 2007 to December 31, 2007

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## 1. Significant accounting policies (continued):

These assumptions are limited by the availability of reliable comparable data, economic uncertainty and the uncertainty of predictions concerning future events. Illiquid credit markets and volatile equity, foreign currency and energy markets have combined to increase the uncertainty inherent in such estimates and assumptions. Accordingly, by their nature, estimates of fair value are subjective and do not necessarily result in precise determinations. Should the underlying assumptions change, the estimated fair value could change by a material amount.

### (g) Changes in accounting policies:

Effective January 1, 2008, the Fund adopted the new Handbook Sections issued by The Canadian Institute of Chartered Accountants ("CICA"): Section 1535, Capital Disclosures, Section 3862, Financial Instruments - Disclosures, and Section 3863, Financial Instruments - Presentation. In addition, the Fund implemented the revised Section 1400, General Standards of Financial Statement Presentation.

Section 1535 establishes standards for disclosure of an entity's objectives, policies and processes for managing capital, quantitative data about what is considered capital, whether an entity has complied with any capital requirements and consequences of any non-compliance. The adoption of this standard had no effect on the recognition or measurement of amounts recorded in the balance sheets and statements of operations and comprehensive income, unitholders' equity and cash flows. The effect of adopting this standard has been detailed in note 9.

Section 3862 and Section 3863, which replaced Section 3861, Financial Instruments - Disclosure and Presentation, revised and enhanced the disclosure requirements, and continued the existing presentation requirements for financial instruments. These standards require disclosures about the nature and extent of risks arising from financial instruments and the management of these risks. The adoption of this standard had no effect on the recognition or measurement of amounts recorded in the balance sheets and statements of operations and comprehensive income, unitholders' equity and cash flows. The effect of adopting this standard has been detailed in note 8.

Section 1400 was amended to include requirements to assess and disclose material uncertainties that may cast significant doubt upon an entity's ability to continue as a going concern. The application of this revised standard does not have a material impact on the financial position or results of operations.

# FIRST LEASIDE PROPERTIES FUND

Notes to Financial Statements (continued)  
(Expressed in U.S. dollars)

Year ended December 31, 2008 and period from July 3, 2007 to December 31, 2007

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## 1. Significant accounting policies (continued):

### (h) Future accounting changes:

#### (i) Goodwill and intangible assets:

In February 2008, the CICA issued the new Handbook Section 3064, Goodwill and Intangible Assets, to replace existing guidance on accounting for intangible assets. The revised standards reinforce the principle-based approach to the recognition of costs as an asset and clarify the application of the matching concept of revenue and expenses. The new standards clarify the distinction between assets and expenses and add guidance on the definition of an intangible asset and the recognition of internally generated intangible assets. These accounting standards are effective for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2009. The application of this standard is not anticipated to have a material impact on the financial position or results of operations of the Fund.

#### (ii) Credit risk and the fair value of financial assets and financial liabilities:

In January 2009, the Emerging Issues Committee ("EIC") of the CICA issued EIC Abstract 173, Credit Risk and the Fair Value of Financial Assets and Financial Liabilities. This abstract provides guidance on Handbook Section 3855, Financial Instruments - Recognition and Measurement, in particular, the determination of fair value of certain financial assets and financial liabilities. It establishes that an entity's own credit risk and the credit risk of the counterparty should be taken into account in determining the fair value of financial assets and financial liabilities, including derivative instruments. This guidance is effective for periods ending on or after January 2009, early adoption is encouraged. Application of this abstract is not anticipated to have a material impact on the financial position or results of the operations of the Fund.

#### (iii) Transition to international:

The Canadian Accounting Standards Board ("AcSB") has confirmed its plan to adopt all International Financial Reporting Standards ("IFRS"), as published by the International Accounting Standards Board, on or after January 1, 2011. The Fund will be required to prepare IFRS financial statements for interim and annual financial statements for fiscal years beginning on or after January 1, 2011. The transition date of January 1, 2011 will require restatement for comparative purposes of amounts reported by the Fund for the year ended December 31, 2010.

# FIRST LEASIDE PROPERTIES FUND

Notes to Financial Statements (continued)  
(Expressed in U.S. dollars)

Year ended December 31, 2008 and period from July 3, 2007 to December 31, 2007

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## 1. Significant accounting policies (continued):

The Fund is currently in the process of evaluating the potential impact of IFRS to its financial statements. This will be an on-going process as new standards and recommendations are issued by the International Accounting Standards Board and the AcSB.

### (i) Net income per unit:

Net income per unit is computed by dividing net income by the weighted average units outstanding during the year.

## 2. Promissory notes receivable:

Master Sherman borrowed funds from the Fund during 2007 and 2008. During 2007, the terms of the promissory notes receivable were not formally documented at the time, but the parties agreed that the loans would consist of three classes of notes, namely, Class A notes, Class B notes and Class C notes, each issuable in series. These notes are unsecured and non-recourse to the limited partners of Master Sherman. On September 30, 2008, the formalization of the promissory notes receivable resulted in a modification to the Class B notes, whereby the 9% interest is payable based on the original Canadian dollar equivalent and not the U.S. dollar equivalent. This modification does not significantly impact the cash flows of the promissory notes receivable.

The Class A notes are denominated in U.S. dollars and bear interest at 9% per annum. As at December 31, 2008, there were \$2,000 (2007 - \$2,000) of notes outstanding.

The Class B notes are denominated in Canadian dollars and bear interest at 9% per annum. As at December 31, 2008, there were \$2,429,238 (Cdn. \$2,958,877) (2007 - \$2,941,858; Cdn. \$2,916,195) of notes outstanding.

The Class C notes are denominated in Canadian dollars and bear interest at 9% per annum, and such interest is reinvested in Class C units on a monthly basis. As at December 31, 2008, there were \$659,779 (Cdn. \$803,629) (2007 - \$719,165; Cdn \$712,892) of notes outstanding.

# FIRST LEASIDE PROPERTIES FUND

Notes to Financial Statements (continued)  
(Expressed in U.S. dollars)

Year ended December 31, 2008 and period from July 3, 2007 to December 31, 2007

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## **2. Promissory notes receivable (continued):**

The promissory notes are due 10 years from issuance, which is on or before September 30, 2018. For all classes of notes, Master Sherman is able to redeem the notes subject to a call premium and to extend the term for a further 10 years. The promissory notes receivable are redeemable in whole or in part, at Master Sherman's option, and any time prior to the tenth anniversary of the original issuance of the promissory notes receivable, subject to a certain prepayment call premium. The prepayment option represents an embedded derivative that is to be accounted for separately at fair value. The fair value of the embedded derivative liability is \$26,000 (2007 - \$24,000). As a result of bifurcating the prepayment option from the promissory notes receivable on issuance of the notes, a basis adjustment of \$14,517 (2007 - \$15,289), net of accumulated amortization of \$1,483 (2007 - \$711), is included in the cost of the promissory notes receivable. This basis adjustment is amortized over the term of the receivable using the effective interest rate method and reported as a reduction to interest income.

## **3. Redeemable units:**

Class A units of the Fund are issuable in series and are denominated in U.S. dollars. Class A unitholders are entitled to one vote per Class A unit owned at all meetings of unitholders. All distributions made by the Fund to holders of Class A units shall be made in U.S. dollars including any payments relating to the participation rights (note 6). Each Class A unit will have a corresponding Series A promissory note denominated in U.S. dollars issued by Master Sherman to the Fund. The promissory note will be issued the same date the Class A units are issued.

Class B units of the Fund are issuable in series and are denominated in Canadian dollars. Class B unitholders are entitled to one vote per Class B unit owned at all meetings of unitholders. All distributions made by the Fund to holders of Class B units shall be made in Canadian dollars other than payments relating to the participation rights (which shall be made in U.S. dollars (note 6)). Each Class B unit will have a corresponding Series B promissory note denominated in Canadian dollars issued by Master Sherman to the Fund. The promissory note will be issued the same date the Class B units are issued.

The Class A and Class B units of the Fund have identical rights relating to redemption, distributions and upon termination of the Fund as Class C units described in note 5.

# FIRST LEASIDE PROPERTIES FUND

Notes to Financial Statements (continued)  
(Expressed in U.S. dollars)

Year ended December 31, 2008 and period from July 3, 2007 to December 31, 2007

### 3. Redeemable units (continued):

During the year ended December 31, 2008, the Fund issued 117,682 Class B units for total consideration of \$116,680 (Cdn. \$117,682). During the year ended December 31, 2008, the Fund redeemed 75,000 Class B units for total consideration of \$70,969 (Cdn. \$75,000).

	Class A		Class B		Total	
	Units	Amount	Units	Amount	Units	Amount
As at July 3, 2007	-	\$ -	-	\$ -	-	\$ -
Units issued	2,000	2,000	2,967,246	2,908,384	2,969,246	2,910,384
Unit redemptions	-	-	(51,051)	(48,093)	(51,051)	(48,093)
Foreign exchange	-	-	-	81,567	-	81,567
As at December 31, 2007	2,000	2,000	2,916,195	2,941,858	2,918,195	2,943,858
Units issued	-	-	117,682	116,680	117,682	116,680
Unit redemptions	-	-	(75,000)	(70,969)	(75,000)	(70,969)
Foreign exchange	-	-	-	(558,331)	-	(558,331)
As at December 31, 2008	2,000	\$ 2,000	2,958,877	\$ 2,429,238	2,960,877	\$ 2,431,238

### 4. Management agreement and cost/payment reimbursement agreement:

The Fund entered into a management agreement with F.L. Securities Inc. on July 3, 2007 whereby F.L. Securities Inc. will manage the operations of the Fund. The agreement was for 10 years with an automatic renewal for successive 10-year periods until cancelled in writing. The fee for performing such services was up to \$100,000 per annum, and reimbursement of reasonable out-of-pocket expenses. F.L. Securities Inc. waived the management fee for the period ended September 30, 2008, and the management agreement was mutually terminated on September 30, 2008 and a new agreement was entered into with First Leaside Management Inc. with effect from July 3, 2007, whereby First Leaside Management Inc. will provide certain management, administrative and support services on behalf of the Fund. In accordance with the new agreement, there will be no fee charged for performing the management services. The term of the agreement, which can be terminated by either party at any time, is 10 years with an automatic renewal of an additional 10 years.

# FIRST LEASIDE PROPERTIES FUND

Notes to Financial Statements (continued)  
(Expressed in U.S. dollars)

Year ended December 31, 2008 and period from July 3, 2007 to December 31, 2007

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## **4. Management agreement and cost/payment reimbursement agreement (continued):**

The Fund also entered into a Fee Payment Agreement with First Leaside Properties Limited Partnership ("FLP") on July 3, 2007 whereby FLP has agreed to pay all of the fees and expenses of the Fund. On September 30, 2008, this agreement was terminated and a new agreement was entered into with Master Sherman, whereby Master Sherman has agreed to pay all of the fees and expenses of the Fund, including prospectus costs incurred. Commencing January 1, 2009, the fees and expenses cannot exceed \$250,000 on an annual basis without the prior written consent of the Fund. This new agreement terminates on July 3, 2037.

The Fund has recorded a recovery charge in the statements of operations of \$620,061 during the year ended December 30, 2008 (2007 - \$372,226).

## **5. Unitholders' equity:**

Pursuant to the Declaration of Trust dated July 3, 2007, the number of Class C units that are authorized and may be issued is unlimited.

Class C units of the Fund are issuable in series and are denominated in Canadian dollars. Class C unitholders are entitled to one vote per Class C unit owned at all meetings of unitholders. All distributions made by the Fund to holders of Class C units shall be made in Canadian dollars other than payments relating to the participation rights (which shall be made in U.S. dollars (note 6)). The cash distributions shall not be paid to the holders of Class C units; any amounts payable to holders of Class C units shall be paid by issuing additional Class C units.

Each Class C unit will have a corresponding series C promissory note denominated in Canadian dollars attached to it issued by Master Sherman to the Fund. The promissory note will be issued the same date the Class C units are issued. If the initial term of the Master Sherman promissory note is extended beyond 10 years, the distributions payable during the extension period to the Class C unitholders will not be reinvested, but will be paid in Canadian dollars.

# FIRST LEASIDE PROPERTIES FUND

Notes to Financial Statements (continued)  
(Expressed in U.S. dollars)

Year ended December 31, 2008 and period from July 3, 2007 to December 31, 2007

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## 5. Unitholders' equity (continued):

Redemption rights by Fund unitholders:

Each Fund unitholder shall be entitled to require the Fund to redeem on a monthly basis at the demand of the Fund unitholder all or any part of the Fund units registered in the name of the Fund unitholder at the fair market value of the unit as determined by the Trustees. The Trustees shall be entitled in their discretion to determine and designate whether any payments made in respect of any redemption are on account of income or capital, and whether any such redemption shall be effected by an in-specie redemption or by a cash redemption. A cash redemption shall not be applicable to Fund units tendered for redemption by a Fund unitholder, if the total amount payable by the Fund in the same calendar month exceeds \$50,000 unless waived by the Trustees of the Fund.

Distributions:

The computation of distributable cash flow is defined in the Declaration of Trust. Distributions for a class of unit will include such things as all cash amounts received from Master Sherman promissory notes that correspond to the series of a Class of units and all other income, distributions, interest, dividends, proceeds from the disposition of securities, returns of capital and repayments of indebtedness. The distributions will be reduced for all costs and expenses attributable to the series of a class of units and any series of a class of units' proportionate share of the common expenses of the Fund.

In the event that the Trustees determine that the Fund does not have available cash in an amount sufficient to make payment of the full amount of any distribution that has been declared to be payable to Fund unitholders, the Fund may issue, on a pro rata basis, additional units, or fractions of units, if necessary, having a value equal to the difference between the amount of such distribution and the amount of cash that has been determined by the Trustees to be available for the payment of such distribution, subject to all necessary regulatory approvals.

Termination of Fund:

Upon the termination of the Fund, the proceeds of the net assets of the Fund after paying for all known liabilities and obligations will be distributed to the unitholders in accordance with their pro rata interests.

# FIRST LEASIDE PROPERTIES FUND

Notes to Financial Statements (continued)  
(Expressed in U.S. dollars)

Year ended December 31, 2008 and period from July 3, 2007 to December 31, 2007

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## 6. Participation rights:

Effective September 30, 2008, the Fund has received participation rights from FLP, the limited partner of Master Sherman, concurrent with the promissory notes issued by Master Sherman to the Fund. The cost of the participation rights is 1/10 of U.S. \$0.01 for each U.S. \$1.00 principal amount of promissory note issued by Master Sherman. As at December 31, 2008, the fair value of these participation rights is nil.

Each participation right entitles the Fund, upon exercise, to a cash payment equal to the fair market value of one FLP unit as determined by FLP or the closing price of the FLP unit if FLP is a reporting issuer and the FLP units are traded on an exchange, as at the time that the participation right in question is exercised less the base FLP unit cost equal to 120% of the fair market value of one FLP unit at the time that the participation right in question is granted. Each series of participation rights shall vest on the tenth anniversary of the date of the grant of such participation rights, being September 30, 2008, and shall expire 30 days after the vesting date. If the term of the promissory notes that corresponds to a series of participation rights is extended for a further 10 years, then the vesting date of the corresponding participation rights is extended for a further 10 years. The participation rights are retractable, subject to a call premium, by FLP at any prior to the vesting date.

If the Fund's unitholders redeem some or all of the Fund's units, the participation rights that correspond to the promissory notes attached to the Fund units will expire and terminate.

## 7. Transactions with First Leaside Group of Companies:

The First Leaside Group of Companies are multi-disciplinary investment management and advisory firms, which include entities such as First Leaside Management Inc., which is the manager of the Fund. Except as disclosed elsewhere, amounts due from/to entities within the First Leaside Group of Companies are due on demand, are unsecured and non-interest bearing as follows:

	2008	2007
Due from:		
Master Sherman	\$ 48,110	\$ —
FLP	140,787	122,165
	<hr/>	<hr/>
	\$ 188,897	\$ 122,165

# FIRST LEASIDE PROPERTIES FUND

Notes to Financial Statements (continued)  
(Expressed in U.S. dollars)

Year ended December 31, 2008 and period from July 3, 2007 to December 31, 2007

## 7. Transactions with First Leaside Group of Companies (continued):

	2008	2007
Due to:		
Master Sherman	\$ –	\$ 113,181
FLP	8,947	–
	<u>\$ 8,947</u>	<u>\$ 113,181</u>

## 8. Risk management and financial instruments:

### (a) Interest rate risk:

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

The risk of future cash flows fluctuating is managed by having fixed rates on the promissory notes receivable.

### (b) Credit and collection risk:

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the Fund by failing to discharge its obligation. The nature and maximum exposure to credit risk as at December 31, 2008 is:

	Carrying amount
Cash	\$ 1,783
Promissory notes receivable	3,091,017
Due from entities within the First Leaside Group of Companies	188,897
	<u>\$ 3,281,697</u>

The majority of cash is held with highly rated financial institutions in Canada.

The Fund is also exposed to credit risk on its promissory notes receivable in the event the borrower is unable to make the contracted payments. Such risk is mitigated through careful evaluation of the value of the underlying assets held by the borrower.

# FIRST LEASIDE PROPERTIES FUND

Notes to Financial Statements (continued)  
(Expressed in U.S. dollars)

Year ended December 31, 2008 and period from July 3, 2007 to December 31, 2007

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## 8. Risk management and financial instruments (continued):

### (c) Liquidity risk:

Liquidity risk is the risk that the Fund will encounter difficulty in meeting its contractual obligations associated with financial liabilities.

The Fund manages its liquidity risk through the use of budgets and forecasts. Cash requirements are monitored regularly based on actual financial results and actual cash flows to ensure that there are sufficient resources to meet operational requirements.

### (d) Fair values of financial instruments:

The fair market values of cash, due from related parties, accounts payable and accrued liabilities and due to related party approximate their fair values due to the immediate or short-term maturities of these financial instruments.

The fair values of promissory notes receivable and redeemable units could not be reasonably calculated as no comparable commercial terms are obtainable.

## 9. Capital management:

The Fund's capital management objective is to maximize unitholder returns while ensuring that the Fund is capitalized in a manner which appropriately supports working capital needs and business expansion. The Fund's capital management practices are focused on preserving the quality of its financial position by maintaining a strong capital base. Capital of the Fund consists of long-term debt and unitholders' equity.

The Fund's capital is primarily utilized in its ongoing business operations to support working capital requirements, long-term investments made by the Fund, business expansion and other strategic objectives.

# FIRST LEASIDE PROPERTIES FUND

Notes to Financial Statements (continued)  
(Expressed in U.S. dollars)

Year ended December 31, 2008 and period from July 3, 2007 to December 31, 2007

## 9. Capital management (continued):

Capital structure:

The Fund defines its capital structure to include unitholders' equity and redeemable units, net of cash.

	2008	2007
Cash	\$ (1,783)	\$ (116,485)
Redeemable units	2,431,238	2,943,858
Unitholders' equity	648,189	710,454
	<u>\$ 3,077,644</u>	<u>\$ 3,537,827</u>

There are no external or internal restrictions on the Fund's capital.

## 10. Economic dependence:

The promissory notes receivable and virtually all of the interest income are from Master Sherman. The loss of interest income or the inability of Master Sherman to repay the promissory notes receivable could have a material adverse effect on the Fund's results of operations and financial position.

## 11. Subsequent events:

- (a) Subsequent to year end, the Fund issued approximately 2,200,000 Class C units for total gross proceeds of approximately \$2,200,000 pursuant to its initial public offering. In addition, the Fund received total gross proceeds of approximately \$3,550,000 through the issuance of approximately 3,550,000 redeemable units.
- (b) As a consequence of the amended Declaration of Trust as of September 30, 2008, resulting in a unit reclassification, the Fund no longer met the legislated requirements of a Mutual Fund Trust under the Income Tax Act (Canada) as of January 1, 2009. Management has implemented a plan to ensure the Fund meets the requirements of a Mutual Fund Trust upon completion of the Initial Closing.