

# Q3



2007 Third Quarter Report to Unitholders. For the three and nine months ended September 30, 2007.

## Letter to Unitholders

November 9, 2007

Strong room rate performance in Québec, and the Western and Atlantic regions, allowed InnVest to grow its RevPAR in the third quarter on a same hotel basis, while the contribution from the hotels acquired in 2006 after the end of the second quarter and the hotels acquired in 2007 allowed InnVest to grow its distributable income.

The 2007 hotel acquisitions will continue to increase InnVest's participation in the mid-scale with food and beverage and extended stay segments launched InnVest into the up-scale segment of the market with the Fairmont and Sheraton Suites brands and achieved InnVest's objective of greater presence in western Canada.

On July 12, 2007, InnVest, in partnership with Cadbridge Investors LP ("Cadbridge"), a joint venture entity between affiliates of Cadim, a division of the Caisse de Dépôt et Placement du Québec and Westmont Hospitality Group, announced a take-over bid for all of the outstanding units of Legacy Hotels Real Estate Investment Trust ("Legacy") at a price of \$12.60 per unit. The take-over bid was effected by LGY Acquisition LP, a newly-formed limited partnership, between InnVest and Cadbridge in which InnVest has an approximate 26% interest. LGY Acquisition completed the acquisition of Legacy's outstanding units on September 18, 2007. InnVest and Cadbridge subsequently reorganized Legacy's assets such that InnVest became the direct owner of ten of the following eleven up-scale hotels: The Fairmont Palliser, Sheraton Suites Calgary Eau Claire, Fairmont Hotel Macdonald, Delta Calgary Airport, Delta Winnipeg Hotel, Delta Ottawa Hotel and Suites, Delta Centre-Ville, Delta

Beauséjour, Delta Prince Edward, Delta Barrington and the Delta Halifax (collectively, the "Legacy Portfolio"), with the remaining hotel to be reorganized by the end of the year. The majority of this reorganization was completed on October 31, 2007 with the balance expected to be completed prior to the end of 2007.

The purchase price, including the assumption of existing debt, in respect of the eleven hotels was approximately \$652 million prior to closing and transaction costs.

The acquisition of the Legacy Portfolio enabled InnVest to significantly expand its presence in the up-scale hotel segment in Canada at a price below replacement cost. The Legacy Portfolio also expands InnVest's presence in western Canada, which is expected to continue to lead growth across the country, and further diversifies the REIT's brand association to include the internationally renowned Sheraton and Fairmont brands.

Upon the completion of the Legacy Portfolio acquisition, InnVest's total portfolio increased to 148 properties, totaling 19,381 rooms across Canada.

The acquired hotels are leading properties in their respective markets and include a number of historical landmarks. The majority of the acquired hotels have considerable meeting space, multiple food and beverage facilities and are located in downtown city centre locations within very close proximity to a number of demand drivers, including but not limited to shopping and recreation areas, businesses, restaurants, convention centres, historical sites and casinos.

## Letter to Unitholders

Details of the hotel properties being acquired by InnVest are as follows:

Hotel	Location	Rooms
The Fairmont Palliser	Calgary, Alberta	405
Sheraton Suites Calgary Eau Claire	Calgary, Alberta	323
The Fairmont Hotel Macdonald	Edmonton, Alberta	199
Delta Calgary Airport	Calgary, Alberta	296
Delta Winnipeg Hotel	Winnipeg, Manitoba	393
Delta Ottawa Hotel and Suites	Ottawa, Ontario	328
Delta Centre-Ville	Montréal, Québec	711
Delta Beauséjour	Moncton, New Brunswick	310
Delta Prince Edward	Charlottetown, Prince Edward Island	211
Delta Barrington	Halifax, Nova Scotia	200
Delta Halifax	Halifax, Nova Scotia	296
Total		3,672

Prior to the third quarter, InnVest entered into a contract to purchase three hotels and develop a fourth, with a total of 455 rooms, for a combined purchase price of \$48.3 million plus transaction costs and construction costs of \$14.0 million. The transactions to acquire these new build hotel properties have closed in stages as the construction of each hotel is completed, with two hotels closing in the third quarter and the third scheduled to close late in the fourth quarter or early in 2008. The hotels acquired include a 117 room Staybridge Suites located in London, Ontario and a 116 room Holiday Inn Express located in North Bay, Ontario, while the hotel to be acquired is a 116 room Staybridge Suites located in Guelph, Ontario and the hotel under development is a 106 room Staybridge Suites in Oakville, Ontario. On July 20, 2007 and September 13, 2007, the REIT closed the Staybridge Suites in London, Ontario at a cost of \$17.0 million plus transaction costs and the Holiday Inn Express in North Bay, Ontario at a cost of \$14.5 million plus transaction costs. The REIT assumed first mortgages of \$8.3 million and \$7.1 million, which bear interest at 6.4% and 6.0% respectively, each for a term of 10 years, with the balance being funded from cash on hand.

It is anticipated that the remaining acquisition and the hotel under development, will be funded through cash on hand, refinancing proceeds and new mortgage financing proceeds.

At the end of the third quarter, the REIT had unused operating loan availability of \$25 million and eight hotel properties which remained unencumbered. The REIT estimates that the unencumbered hotels could generate in excess of \$45 million in mortgage proceeds. The REIT also has an unused acquisition facility of \$40 million available

to acquire hotel properties and an unused loan facility of \$29.1 million available to fund capital expenditures.

Continuing with its strategy of investing in its hotels, InnVest deployed approximately \$6.8 million for capital asset improvements during the third quarter.

### Financial Review

For the quarter, InnVest's revenue per available room ("RevPAR") improved by 5.7% as RevPAR increased to \$80.18. Average daily rates increased by 6.4%, as occupancy declined slightly by 0.4% points. This is primarily due to the nature of the hotels InnVest acquired in 2006 after the end of the second quarter and in 2007, which typically yield higher rates than our base portfolio of hotels.

Room revenues for the three months ended September 30, 2007 were \$119.3 million, 15.4% higher than the \$103.3 million generated for the same period in 2006. The increase reflects \$7.4 million in revenues from the hotels acquired in 2006 after the end of the second quarter and \$7.6 million in revenues from the hotels acquired in 2007. The balance of the \$955 improvement reflects an overall increase in room revenue of 0.9% in the base portfolio. There were increases in Québec and the Western and Atlantic regions with the largest percentage and dollar increase experienced in the Western region.

Hotel expenses for the three months ended September 30, 2007 increased by \$16.4 million or 22.7% when compared to the same period in 2006. This increase reflects \$7.2 million in expenses incurred in the hotels acquired in 2006 after the end of the second quarter, which were not owned for the entire comparative period and \$8.0 million in

expenses in the hotels acquired in 2007. The remaining \$1.2 million related to the base portfolio represents a 1.6% increase over the same period in 2006.

Distributable income grew to \$34.6 million for the three months ended September, 2007, an improvement of \$3.1 million over the distributable income of \$31.5 million experienced in the same period in 2006. Distributable income per unit on a diluted basis decreased slightly to \$0.474 from \$0.519.

The REIT's cash position at September 30, 2007 was \$28.4 million, of which \$5.0 million is restricted under the REIT's trust indenture for the replacement of furniture, fixtures, and equipment and for capital improvements. Financial leverage is at 46.9% debt to gross asset value excluding convertible debentures and 56.3% including convertible debentures.

In 2006, 40.5% of the distributions made during that year were not taxable to unitholders. For calendar 2007, the REIT estimates that approximately 40% of unitholder distributions will not be taxable to unitholders.

#### Outlook

Supply and demand conditions in the hotel industry continue to be favourable. While varying by market, PKF Consulting Inc. ("PKF"), lodging industry experts, forecasts Canadian RevPAR continued growth in 2008 following anticipated growth of approximately 4% in 2007.

InnVest's geographic, customer, and brand diversity ideally positions it to continue to benefit from the anticipated growth in the Canadian hospitality industry. While InnVest is expecting RevPAR growth in its overall portfolio, there are certain markets, most notably Windsor, Oshawa and the GTA, that will continue to be more negatively impacted by the strength of the Canadian dollar. The decline in US visitation is expected to continue but is being offset by strengthening domestic and international corporate and group travel.

The acquisition of the Legacy Portfolio further expands the REIT's geographic diversity, notably within Western Canada which is experiencing the strongest growth in the country. The acquisition also enhances InnVest's presence in the upscale segment of the lodging industry which is forecast to lead RevPAR growth in 2008. Given that the Legacy acquisition closed late in the third quarter, the contribution on a per unit basis in 2007 is expected to be dilutive due to the seasonality inherent in the business. However, this acquisition is expected to be accretive in 2008.

Forecasted RevPAR growth, our ability to capitalize on our recent acquisitions and our ability to manage costs will drive InnVest's performance in 2008.



**Kenneth Gibson**  
*President and Chief Executive Officer*

November 9, 2007

## Management's discussion and analysis

### Third quarter 2007 financial and operating highlights

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- Eleven hotels with 3,672 rooms were acquired September 18, 2007 as part of the Legacy transaction;
- Revenue per available room ("RevPAR") growth was 0.9% during the third quarter of 2007 for InnVest's portfolio of hotels on a same hotel basis;
- Net income from continuing operations was \$30.2 million in the third quarter an increase of \$6.7 million over the comparable net income from continuing operations experienced for the same period in 2006;
- Distributable income grew 9.8% to \$34.6 million in the quarter, an increase of \$3.1 million over the same period in 2006. Distributable income per unit on a diluted basis decreased to \$0.474 from \$0.519;
- Payout ratio, distributions divided by distributable income on a trailing twelve-month basis, improved slightly by 0.9% points from 96.6% at June 30, 2007 to 95.7% as a result of the improvements in distributable income generated by the hotels acquired in 2006 after the end of the second quarter and the hotels acquired in 2007 resulting in distributable income increases outpacing increases in the distributions;
- The newly built 117 room London Staybridge Suites and 116 room North Bay Holiday Inn Express were acquired in the third quarter; and
- \$6.8 million was invested in our hotels.

### Overview of InnVest REIT

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The following is a discussion of the results of operations and financial condition of InnVest Real Estate Investment Trust ("InnVest" or the "REIT") for the three and nine months ended September 30, 2007, with a comparison to the results of operations of InnVest for the three and nine months ended September 30, 2006.

The following management's discussion and analysis ("MD&A") is dated November 7, 2007 and should be read in conjunction with the unaudited consolidated financial statements of the REIT and the notes thereto as at and for the three and nine months ended September 30, 2007, the audited consolidated financial statements of the REIT and the notes thereto as at and for the year ended December 31, 2006, and the MD&A for the year ended December 31, 2006 dated March 7, 2007.

The financial statements of InnVest are prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and are presented in Canadian dollars. Monetary data in tabular form and in the text, unless otherwise indicated, are in thousands of dollars, except for per unit, Average Daily Rate ("ADR") and Revenue per Available Room ("RevPAR") amounts.

InnVest is an unincorporated open-ended real estate investment trust governed by the laws of Ontario and a Declaration of Trust. It is publicly traded and listed on the Toronto Stock Exchange under the symbol INN.UN.

Additional information relating to InnVest, including InnVest's annual information form, can be found at [www.sedar.com](http://www.sedar.com).

#### InnVest's Portfolio of Hotels

At September 30, 2007, InnVest held Canada's largest hotel portfolio with 148 hotels and 19,381 rooms with locations in every province of Canada. InnVest also owns a 50% interest in Choice Hotels Canada Inc. ("Choice Canada"), the largest franchisor of hotels in Canada.

The portfolio consists of limited, mid-scale with food and beverage and full service hotel properties. Over 67% of InnVest's guest rooms are in Ontario and Québec.

InnVest operates these hotel properties under 15 internationally recognized franchise brands including Comfort Inn<sup>®</sup>, Quality Suites<sup>®</sup>, Quality Hotels<sup>®</sup>, Holiday Inn<sup>®</sup>, Radisson Hotels<sup>®</sup>, Radisson Suites<sup>®</sup>, Delta<sup>®</sup>, Hilton Hotels<sup>®</sup>, Fairmont Hotels<sup>®</sup>, Sheraton Suites<sup>®</sup>, Hilton Garden Inn<sup>®</sup>, Hilton Homewood Suites<sup>®</sup>, Travelodge<sup>®</sup>, Staybridge Suites<sup>®</sup> and Best Western<sup>®</sup>. Comfort Inn represents 35% of the portfolio based on number of guest rooms. InnVest's hotels are typically located near major thoroughfares in urban and suburban areas, business centres, government and manufacturing facilities, universities, airports and tourist attractions. The hotels have a diverse customer base, including business travelers, leisure travelers, groups, organizations and corporate clients.

Brands	No. of Hotels	No. of Guest Rooms	% of Guest Rooms
Comfort Inn	84	6,780	35.0%
Delta Hotel	11	3,327	17.2%
Holiday Inn	15	2,572	13.3%
Travelodge	10	1,723	8.9%
Quality Suites/Inn	8	1,096	5.7%
Quality Hotel	5	796	4.1%
Hilton Hotel	2	768	3.9%
Radisson Hotel/Suites	4	707	3.6%
Fairmont Hotel	2	604	3.1%
Sheraton Suites	1	323	1.7%
Best Western	1	130	0.7%
Hilton Garden Inn	1	120	0.6%
Staybridge Suites	1	117	0.6%
Hilton Homewood Suites	1	83	0.4%
Independent	2	235	1.2%
	148	19,381	100.0%

### The Geographic Distribution of InnVest's Hotels and Rooms by Brand

	Ontario			Québec			Atlantic			Western		
	No. of Hotels	No. of Guest Rooms	% of Guest Rooms	No. of Hotels	No. of Guest Rooms	% of Guest Rooms	No. of Hotels	No. of Guest Rooms	% of Guest Rooms	No. of Hotels	No. of Guest Rooms	% of Guest Rooms
Comfort Inn	38	3,155	16.3%	22	1,754	9.1%	15	1,126	5.8%	9	745	3.8%
Delta Hotel	2	573	3.0%	3	1,048	5.4%	4	1,017	5.2%	2	689	3.6%
Holiday Inn	14	2,376	12.3%	–	–	–	1	196	1.0%	–	–	–
Travelodge	6	827	4.3%	–	–	–	–	–	–	4	896	4.6%
Quality Suites/Inn	4	604	3.1%	4	492	2.6%	–	–	–	–	–	–
Quality Hotel	1	212	1.1%	2	298	1.5%	1	160	0.8%	1	126	0.7%
Hilton Hotel	–	–	–	1	571	2.9%	1	197	1.0%	–	–	–
Radisson Hotel/Suites	3	532	2.7%	1	175	0.9%	–	–	–	–	–	–
Fairmont Hotel	–	–	–	–	–	–	–	–	–	2	604	3.1%
Sheraton Suites	–	–	–	–	–	–	–	–	–	1	323	1.7%
Best Western	1	130	0.7%	–	–	–	–	–	–	–	–	–
Hilton Garden Inn	1	120	0.6%	–	–	–	–	–	–	–	–	–
Staybridge Suites	1	117	0.6%	–	–	–	–	–	–	–	–	–
Hilton Homewood Suites	1	83	0.4%	–	–	–	–	–	–	–	–	–
Independent	1	83	0.4%	–	–	–	–	–	–	1	152	0.8%
	73	8,812	45.5%	33	4,338	22.4%	22	2,696	13.8%	20	3,535	18.3%

## Management's discussion and analysis

### InnVest's Franchise, Office, Retail and Retirement Home Businesses

InnVest's franchise, office, retail and retirement home businesses remain substantially unchanged from the description provided in the MD&A for the year ended December 31, 2006.

### Hotel Key Performance Measures

There are several key metrics that are used to measure the performance of the hotel industry and the relative strength of participants in the industry. Those measures are occupancy, average daily rates ("ADR"), revenue per available room ("RevPAR"), gross operating profit ("GOP"), hotel operating income ("HOI"), funds from operations ("FFO") and distributable income ("DI").

### Regional performance

On a same hotel basis during the third quarter, InnVest experienced above average RevPAR growth in the Western region of 5.7%. The Atlantic region and Québec hotels posted RevPAR improvements of 4.5% and 3.4%, respectively. InnVest's Ontario hotels posted RevPAR declines of 1.6%.

### InnVest's Key Performance Measures

*Note: Measures related to room revenues are on a same hotel basis, excluding the hotels that have been classified as discontinued operations, and the hotels acquired after the end of the second quarter of 2006, the two new build hotels opened in the third quarter of 2007 and the 11 hotels acquired as part of the Legacy transaction, for which comparative data is not available.*

	Three months ended September 30			Nine months ended September 30		
	2007	2006	Var %	2007	2006	Var %
<b>Occupancy</b>						
Ontario	<b>69.2%</b>	71.5%	(3.2)%	<b>62.9%</b>	64.8%	(2.9)%
Québec	<b>74.1%</b>	74.8%	(0.9)%	<b>64.1%</b>	65.4%	(2.0)%
Atlantic	<b>84.1%</b>	84.9%	(0.9)%	<b>68.3%</b>	68.2%	0.1%
Western	<b>73.4%</b>	75.9%	(3.3)%	<b>66.9%</b>	65.2%	2.6%
Total	<b>72.3%</b>	74.2%	(2.6)%	<b>64.3%</b>	65.3%	(1.5)%
<b>ADR</b>						
Ontario	<b>\$ 108.53</b>	\$ 106.73	1.7%	<b>\$ 105.11</b>	\$ 103.22	1.8%
Québec	<b>\$ 101.00</b>	\$ 96.72	4.4%	<b>\$ 96.03</b>	\$ 93.11	3.1%
Atlantic	<b>\$ 109.45</b>	\$ 103.82	5.4%	<b>\$ 97.97</b>	\$ 93.62	4.6%
Western	<b>\$ 92.11</b>	\$ 84.30	9.3%	<b>\$ 86.60</b>	\$ 79.83	8.5%
Total	<b>\$ 104.90</b>	\$ 101.33	3.5%	<b>\$ 99.97</b>	\$ 97.07	3.0%
<b>RevPAR</b>						
Ontario	<b>\$ 75.12</b>	\$ 76.36	(1.6)%	<b>\$ 66.16</b>	\$ 66.90	(1.1)%
Québec	<b>\$ 74.85</b>	\$ 72.37	3.4%	<b>\$ 61.54</b>	\$ 60.85	1.1%
Atlantic	<b>\$ 92.08</b>	\$ 88.11	4.5%	<b>\$ 66.95</b>	\$ 63.89	4.8%
Western	<b>\$ 67.65</b>	\$ 64.01	5.7%	<b>\$ 57.95</b>	\$ 52.02	11.4%
Total	<b>\$ 75.83</b>	\$ 75.15	0.9%	<b>\$ 64.24</b>	\$ 63.41	1.3%

On a same hotel basis, the REIT's hotels posted a RevPAR improvement of 0.9% and 1.3% for the three and nine months ended September 30, 2007, respectively, over the same periods in the previous year. This quarter increase was achieved through a 3.5% or \$3.57 increase in ADR and a 2.6% decrease in occupancy, while the nine-month increase was achieved through a 3.0% or \$2.90 increase in ADR and a 1.5% decrease in occupancy.

## InnVest's Geographical Performance Comparison

*Note: Measured on a same hotel basis for the nine months ended September 30, 2007.*

### RevPAR % Growth by Geographical Regions

	InnVest Portfolio	Canadian Market	Variance
Ontario	(1.1)%	0.9%	(2.0)%
Québec	1.1%	(1.5)%	2.6%
Atlantic	4.8%	6.2%	(1.4)%
Western	11.4%	9.0%	2.4%
Canada	1.3%	4.4%	(3.1)%

InnVest underperformed the market in Ontario and the Atlantic region and outperformed the market in Québec and the Western region in terms of increases in RevPAR. InnVest underperformed the market in Ontario because it owns a disproportionate number of the hotels in soft markets such as Windsor and Oshawa. In the Atlantic region strong growth was experienced in Newfoundland where the REIT only owns two hotels. InnVest underperformed the Canadian market by 3.1% in RevPAR growth partially because of its geographical distribution with relatively few hotels located in the Western region even though InnVest outperformed the market in the Western region.

### Recent Industry Performance

The Canadian hotel industry performed as expected in the first nine months of 2007. According to PKF Consulting, advisors to the Canadian hotel industry, occupancy and ADRs for the nine months ended September 30, 2007 experienced 0.6 points and 3.3% growth, respectively, resulting in RevPAR growth of 4.4% for the period.

## InnVest's strategy and objectives

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### InnVest's Operating Strategy and Objectives

InnVest's operating strategy and objectives remain substantially unchanged from the description provided in the MD&A for the year ended December 31, 2006.

### Acquisition Strategy and 2007 Activity

The 2007 hotel acquisitions continued to increase InnVest's participation in the mid-scale with food and beverage and extended stay segments launched InnVest into the up-scale segment of the market with the Fairmont and Sheraton Suites brands and achieved InnVest's objective of greater presence in western Canada.

On July 12, 2007, InnVest, in partnership with Cadbridge Investors LP ("Cadbridge"), a joint venture entity between affiliates of Cadim, a division of the Caisse de Dépôt et Placement du Québec and Westmont Hospitality Group, announced a take-over bid for all the outstanding units of Legacy Hotels Real Estate Investment Trust ("Legacy") at a price of \$12.60 per unit. The take-over bid was effected by LGY Acquisition LP, a newly-formed limited partnership, between InnVest and Cadbridge in which InnVest had an approximate 26% interest. LGY Acquisition completed the acquisition of 100% of Legacy's outstanding units on September 18, 2007 and InnVest and Cadbridge have reorganized Legacy's assets such that InnVest will become the owner of the following eleven up-scale hotels: The Fairmont Palliser, Sheraton Suites Calgary Eau Claire, Fairmont Hotel Macdonald, Delta Calgary Airport, Delta Winnipeg Hotel, Delta Ottawa Hotel and Suites, Delta Centre-Ville, Delta Beauséjour, Delta Prince Edward, Delta Barrington and the Delta Halifax (collectively the "Legacy Portfolio"). The majority of this reorganization was completed on October 31, 2007 with the balance expected to be completed prior to the end of 2007.

## Management's discussion and analysis

In order to partially fund the cost of the Legacy Portfolio acquisition, InnVest raised \$200 million of equity at a price of \$12.35 per subscription receipt representing the right to receive trust units of the REIT and \$70 million of extendible convertible unsecured subordinated debentures. The remainder of the purchase price was satisfied with the assumption of \$194 million in mortgage debt secured by the properties and \$215 million of bridge financing from a Canadian chartered bank. InnVest intends to refinance the existing mortgages and arrange new mortgage financing on certain of the acquired assets that are currently unencumbered. The bridge loan will be repaid from the proceeds of these financings.

The subscription receipts were exchanged on a one-for-one basis for units of InnVest upon completion of LGY Acquisition LP's take-over bid for Legacy. The convertible debentures have a maturity date of August 1, 2014, a coupon of 5.85% per annum and will pay interest semi-annually in arrears on August 1 and February 1 in each year commencing on February 1, 2008. The convertible debentures are convertible into 68.027 units of the REIT per \$1,000 principal amount, at any time, at the option of the holder, representing a conversion price of \$14.70 per unit.

Effective October 31, 2007, InnVest and Cadbridge reorganized LGY Acquisition LP's assets such that InnVest became the owner of ten of the eleven up-scale hotels listed below, with the remaining hotel to follow prior to the end of the year. The Legacy Portfolio's purchase price, including the assumption of existing debt, approximated \$652 million prior to closing and transaction costs. For accounting purposes, InnVest has included the results of operations of the Legacy Portfolio as though it was owned from September 18, 2007.

The acquired hotels are leading properties in their respective markets and include a number of historical landmarks. The majority of the acquired hotels have considerable meeting space, multiple food and beverage facilities and are ideally located in downtown city centre locations within very close proximity to a number of demand drivers, including but not limited to shopping and recreation areas, businesses, restaurants, convention centres, historical sites and casinos.

Details of the hotel properties acquired by InnVest are as follows:

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Total		3,672



The acquisition of the Legacy Portfolio enabled InnVest to significantly expand its foothold in the up-scale hotel segment in Canada at a price below replacement cost. The Legacy Portfolio also expands InnVest's presence in western Canada, which is expected to continue to lead growth across the country, and further diversifies the REIT's brand association to include the internationally renowned Sheraton and Fairmont brands.

The total acquisition purchase price of \$679 million, which includes all closing costs, was financed as outlined below. InnVest intends to refinance the existing mortgages and arrange new mortgage financing on certain of the acquired hotels that are currently unencumbered. The bridge loan will be repaid from the proceeds of these financings.

	Weighted Average Interest Rate	\$ millions
Assumed mortgages	7.1%	\$ 194
270-day bridge loan	7.6%	215
Convertible unsecured debentures <sup>(1)</sup>	5.85%	70
Equity <sup>(2)</sup>		200
		\$ 679

(1) The convertible debentures mature on August 1, 2014. The convertible debentures are convertible at any time, at the option of the holder, at a conversion price of \$14.70 per unit.

(2) InnVest initially issued subscription receipts representing the right to receive trust units of the REIT. These subscription receipts were exchanged on a one-for-one basis for units of InnVest on September 17, 2007.

Prior to the third quarter, InnVest entered into a contract to purchase three hotels and develop a fourth, with a total of 455 rooms, for a combined purchase price of \$48.3 million plus transaction costs and construction costs of \$14.0 million. The transaction to acquire these new build hotel properties will close in stages as the construction of each hotel is completed, with two hotels closing in the third quarter and the third scheduled to close late in the fourth quarter or early in 2008. The hotels acquired include a 117 room Staybridge Suites located in London, Ontario and a 116 room Holiday Inn Express located in North Bay, Ontario, while the hotel to be acquired is a 116 room Staybridge Suites located in Guelph, Ontario and the hotel under development is a 106 room Staybridge Suites in Oakville, Ontario. On July 20, 2007 and September 13, 2007, the REIT closed the Staybridge Suites in London, Ontario at a cost of \$17.0 million plus transaction costs and the Holiday Inn Express in North Bay, Ontario at a cost of \$14.5 million plus transaction costs, respectively. The REIT assumed first mortgages of \$8.3 million and \$7.1 million, which bear interest at 6.4% and 6.0% respectively, each for a term of 10 years, with the balance being funded from cash on hand.

It is anticipated that the remaining acquisition and the hotel under development, will be funded through cash on hand, refinancing proceeds and new mortgage financing proceeds.

The brand and geographic summary of the hotels to be acquired in the Legacy Portfolio, together with the Staybridge Suites London and Holiday Inn Express North Bay are as follows:

	Ontario		Québec		Atlantic		Western	
	No. of Hotels	No. of Guest Rooms	No. of Hotels	No. of Guest Rooms	No. of Hotels	No. of Guest Rooms	No. of Hotels	No. of Guest Rooms
Delta Hotel	1	328	1	711	4	1,017	2	689
Fairmont Hotel	—	—	—	—	—	—	2	604
Sheraton Suites	—	—	—	—	—	—	1	323
Staybridge Suites	1	117	—	—	—	—	—	—
Holiday Inn Express	1	116	—	—	—	—	—	—
	3	561	1	711	4	1,017	5	1,616

## Management's discussion and analysis

### Divestiture Strategy

InnVest monitors the operating performance of its individual assets on an ongoing basis. From time to time, certain assets are identified that may not support one or more of InnVest's objectives. Such assets may provide unstable or decreasing net operating income levels, which in turn affects InnVest's ability to maintain stable and growing cash distributions to its unitholders. Also, the retention of certain assets may be inconsistent with InnVest's objective of maximizing the long-term asset value of the portfolio.

Such a condition may exist where it is believed that further capital investment in an asset will not provide increases in net operating income sufficient to maintain or grow cash distributions. In addition, certain assets may not contribute to the proposition of long-term value appreciation given both the current and future market characteristics and the business environment. Overall, when assets are identified that do not support certain primary objectives of the REIT, an analysis is conducted to decide if the divestiture of such assets is in the best interest of unitholders. Such an analysis takes into consideration the implications for distributable income and overall diversification, market conditions and numerous other factors.

At the end of December 31, 2006, two hotels were classified as held for sale. One of these hotels was sold at the end of the first quarter of 2007, while the second hotel was sold early in the second quarter of 2007. An accounting gain of \$659 was recorded in the first quarter, and a further gain of \$174 was recorded in the second quarter.

### InnVest's Competitive Strengths

InnVest's competitive strengths remain substantially unchanged from the description provided in the MD&A for the year ended December 31, 2006.

## InnVest's operating results

Below is a comparison of the operating results for the three and nine months ended September 30, 2007 to the results of operations for the comparable periods in 2006.

	Three Months Ended Sept. 30, 2007	Three Months Ended Sept. 30, 2006	Nine Months Ended Sept. 30, 2007	Nine Months Ended Sept. 30, 2006
Hotel revenues	\$ 138,661	\$ 117,119	\$ 340,154	\$ 290,265
Hotel expenses	88,792	72,372	238,267	196,167
Hotel operating income	49,869	44,747	101,887	94,098
Net income from continuing operations	\$ 30,209	\$ 23,304	\$ 23,441	\$ 40,145
Net income from continuing operations				
per unit – basic	\$ 0.454	\$ 0.425	\$ 0.395	\$ 0.775
per unit – diluted	\$ 0.423	\$ 0.395	\$ 0.395	\$ 0.763
Net income (loss) from discontinued operations	\$ –	\$ 232	\$ 809	\$ (804)
Net income and comprehensive income	\$ 30,209	\$ 23,536	\$ 24,250	\$ 39,341
Add/ (deduct)				
Depreciation, amortization and accretion <sup>(1)</sup>	14,086	12,972	41,942	36,200
Future income tax (recovery) expense	(5,068)	(1,265)	2,022	(14,171)
Non-cash executive and trustee compensation	158	86	386	261
(Gain) on sale, write down of assets held for sale	–	–	(833)	1,000
Corporate reorganization expense	43	–	1,514	–
Funds from operations <sup>(2)</sup>	\$ 39,428	\$ 35,329	\$ 69,281	\$ 62,631
Funds from operations per unit <sup>(3)</sup>				
– basic	\$ 0.592	\$ 0.645	\$ 1.168	\$ 1.210
– diluted	\$ 0.535	\$ 0.578	\$ 1.089	\$ 1.118
Amortization of deferred financing costs	–	710	–	1,939
Non-cash portion of interest expense	540	–	2,017	–
Reserve for replacement of furniture, fixtures and equipment and capital improvements ("FF&E Reserve")	(5,551)	(4,746)	(13,630)	(11,688)
Convertible debentures accretion	214	211	616	595
Deferred land lease expense and retail lease income, net	8	34	25	84
Distributable income <sup>(2)</sup>	\$ 34,639	\$ 31,538	\$ 58,309	\$ 53,561
Distributable income per unit <sup>(3)</sup>				
– basic	\$ 0.520	\$ 0.575	\$ 0.983	\$ 1.034
– diluted	\$ 0.474	\$ 0.519	\$ 0.931	\$ 0.972
Distributions <sup>(4)</sup>	\$ 17,813	\$ 15,417	\$ 49,186	\$ 44,150
Distributions – per unit <sup>(4)</sup>	\$ 0.2813	\$ 0.2813	\$ 0.8438	\$ 0.8438

(1) For purposes of the calculation of funds from operations, amortization of deferred financing costs is excluded from depreciation, amortization and accretion.

(2) Funds from operations and distributable income are measures of earnings and cash flow commonly used by industry analysts that are not required under GAAP, and accordingly, may not be comparable to similar measures used by other organizations.

(3) Funds from operations and distributable income per unit amounts have been calculated on a basis consistent with that prescribed by GAAP for calculating earnings per unit.

(4) Distributions and distributions per unit include cash distributions and distributions arising from the Distribution Reinvestment Plan.

## Management's discussion and analysis

### Operating results review – three months ended September 30, 2007

InnVest's operations are seasonal and as such its results are not consistent throughout the year. Revenue earned from hotel operations fluctuate throughout the year, with the third quarter being the highest due to the increased level of leisure travel in the summer months and the first quarter being the lowest because leisure travel tends to be lower. The results from operations vary materially from quarter to quarter because of the seasonal nature of the revenue stream and the fact that certain costs such as property taxes, insurance, interest, depreciation and amortization, corporate and administrative are fixed or virtually fixed.

#### Hotel Operating Results Comparison

In summarizing the hotel operating results for the three months ended September 30, 2007 and comparing those results to the three months ended September 30, 2006, the REIT has categorized 133 of its hotels owned for the entire current and comparative period as its "Base Portfolio". The two Hilton hotels acquired after the end of the second quarter of 2006 are categorized as the "2006 Acquisitions", the two newly built London Staybridge Suites and the North Bay Holiday Inn Express and the eleven hotels acquired as part of the Legacy transaction are categorized as the "2007 Acquisitions".

#### Hotel Revenues

A summary of the hotel revenue categorized by room revenue and non-room revenue for the three months ended September 30, 2007 and 2006 are stated below:

	2007	2006	Variance
<b>Room Revenue</b>			
Base Portfolio	\$ 102,994	\$ 102,039	\$ 955
2006 Acquisitions	8,665	1,280	7,385
2007 Acquisitions	7,602	–	7,602
Sub-total	\$ 119,261	\$ 103,319	\$ 15,942
<b>Non-Room Revenue</b>			
Base Portfolio	\$ 12,934	\$ 13,196	\$ (262)
2006 Acquisitions	2,519	604	1,915
2007 Acquisitions	3,947	–	3,947
Sub-total	\$ 19,400	\$ 13,800	\$ 5,600
<b>Hotel Revenue</b>			
Base Portfolio	\$ 115,928	\$ 115,235	\$ 693
2006 Acquisitions	11,184	1,884	9,300
2007 Acquisitions	11,549	–	11,549
Total	\$ 138,661	\$ 117,119	\$ 21,542

#### Overall Hotel Portfolio

In the third quarter hotel revenue increased by \$21.5 million, with the majority of the increase due to the hotels acquired in 2006 and 2007. The Base Portfolio of 133 hotels contributed modestly with \$693 of the increase.

The increase of \$15.9 million in room revenues for the three months ended September 30, 2007 reflects \$7.4 million and \$7.6 million in revenues from the hotels acquired in 2006 and 2007, respectively. The balance of \$955 improvement reflects an overall increase in room revenue of 0.9% in the Base Portfolio. There were increases in the Québec, Atlantic and Western regions, with the largest dollar and percentage increase experienced in the Western region.

## Room Revenues

A geographical comparison of the room revenue variance between the three months ended September 30, 2007 and 2006, excluding the assets classified as discontinued operations, is as follows:

	Hotels	Rooms	As a % of total	Room Revenue variance	As a % of total	Var % over 2006
<b>Base Portfolio</b>						
Ontario	70	8,251	42.6%	\$ (834)	(5.2)%	(1.4)%
Québec	31	3,056	15.8%	604	3.8%	2.9%
Atlantic	17	1,482	7.6%	541	3.4%	4.5%
Western	15	1,919	9.9%	644	4.0%	5.7%
Sub-total	133	14,708	75.9%	955	6.0%	0.9%
<b>2006 Acquisitions</b>	2	768	4.0%	7,385	46.3%	577.0%
<b>2007 Acquisitions</b>	13	3,905	20.1%	7,602	47.7%	—
<b>Total</b>	<b>148</b>	<b>19,381</b>	<b>100.0%</b>	<b>\$ 15,942</b>	<b>100.0%</b>	<b>15.4%</b>

The Ontario hotels experienced a decline of \$834 or 1.4% in room revenues compared to the same period in 2006. The Ontario markets which contributed to the decline were Oshawa (\$686 or 16.5%), the Greater Toronto Area (“GTA”) (\$546 or 3.2%), Burlington-Oakville (\$355 or 7.7%), North Bay (\$125 or 6.5%) and London (\$94 or 2.5%), while InnVest’s hotels elsewhere in Ontario posted room revenue increases of \$972 or 3.7%. The GTA market was impacted by reduced convention activity and the strong Canadian dollar. The Oshawa market continues to be impacted by reduced activity in local automotive manufacturing and new competition, while the London and Burlington-Oakville market declines were the result of a decline in occupancy caused by new competition. The Ontario markets outside of the GTA with significant positive contribution to the results for the three-month period were Eastern Ontario (\$107 or 2.7%), Windsor (\$100 or 6.4%) and Ottawa (\$737 or 12.7%).

InnVest’s Base Portfolio of hotels in Québec experienced a room revenue increase of \$604 or 2.9%. The REIT’s rural Québec hotels contributed positively improving by \$290 or 3.5%, while the REIT’s Montreal hotels posted a modest improvement of \$105 or 1.1% and Québec City posted a gain of \$209 or 6.6%.

InnVest’s Base Portfolio of Atlantic region hotels experienced growth of \$541 or 4.5% from the same period in 2006, with consistent gains in all four provinces.

InnVest’s Base Portfolio of Western hotels continued to experience significant revenue growth posting an increase of \$644 or 5.7% over the same period in the prior year. The majority of the gains were posted by the hotels located in Alberta (\$280 or 3.9%) and Manitoba (\$153 or 11.2%). This increase was attributable to occupancy improvements and room rate increases related to economic activity generated by the oil and gas industry.

## Non-Room Revenues

Non-room revenues increased by \$5.6 million, reflecting the non-room revenues generated by the hotels the REIT acquired in 2006, which were not owned for the entire comparative period, and the 2007 Acquisitions. The majority of the hotels which were acquired in 2006 and 2007 generate a higher proportion of total revenues from non-room revenues such as food and beverage sales. Non-room revenues declined in the Base Portfolio by \$262, which included a decrease in food and beverage revenue of \$49, telephone revenue of \$111 and a reduction in gains on the conversion of American dollars to Canadian dollars.

## Management's discussion and analysis

### Hotel Operating Income Margin Analysis

The following chart illustrates the REIT's margins for the Base Portfolio, the 2006 Acquisitions and the 2007 Acquisitions for the three months ended September 30, 2007 and 2006:

2007	Base Portfolio	2006 Acquisitions <sup>(1)</sup>	2007 Acquisitions <sup>(2)</sup>	Total
Hotel revenues	\$ 115,928	\$ 11,184	\$ 11,549	\$ 138,661
Hotel expenses				
Operating expenses	59,694	7,528	6,549	73,771
Property taxes, rent and insurance	8,833	448	882	10,163
Management fees	3,909	332	617	4,858
	72,436	8,308	8,048	88,792
Hotel operating income	\$ 43,492	\$ 2,876	\$ 3,501	\$ 49,869
HOI margin	<b>37.5%</b>	<b>25.7%</b>	<b>30.3%</b>	<b>36.0%</b>

  

2006	Base Portfolio	2006 Acquisitions <sup>(1)</sup>	2007 Acquisitions <sup>(2)</sup>	Total
Hotel revenues	\$ 115,235	\$ 1,884	\$ —	\$ 117,119
Hotel expenses				
Operating expenses	58,705	999	—	59,704
Property taxes, rent and insurance	8,692	55	—	8,747
Management fees	3,883	38	—	3,921
	71,280	1,092	—	72,372
Hotel operating income	\$ 43,955	\$ 792	\$ —	\$ 44,747
HOI margin	<b>38.1%</b>	<b>42.0%</b>	<b>—</b>	<b>38.2%</b>

  

Variance	Base Portfolio	2006 Acquisitions <sup>(1)</sup>	2007 Acquisitions <sup>(2)</sup>	Total
Hotel revenues	\$ 693	\$ 9,300	\$ 11,549	\$ 21,542
Hotel expenses				
Operating expenses	989	6,529	6,549	14,067
Property taxes, rent and insurance	141	393	882	1,416
Management fees	26	294	617	937
	1,156	7,216	8,048	16,420
Hotel operating income	\$ (463)	\$ 2,084	\$ 3,501	\$ 5,122
HOI margin	<b>(0.6)%</b>	<b>(16.3)%</b>	<b>—</b>	<b>(2.2)%</b>

(1) The 2006 Acquisitions represent the two Hilton Hotels acquired in the third quarter of 2006 that were not owned for the entire comparative period.

(2) The 2007 Acquisitions represent the two new build hotels acquired in the third quarter of 2007 and the 11 hotels acquired in the Legacy transaction, that were not owned for any of the comparative period.

Total hotel operating income margin decreased by 2.2 points, which can be partially attributed to the impact of seasonality inherent in the 2006 Acquisitions, which were acquired in the second and third quarters of 2006, and the resulting lower margins experienced for the 2006 Acquisitions relative to the Base Portfolio. The 2007 Acquisitions generated a HOI margin of 30.3%, which is significantly below the Base Portfolio. The 2006 and 2007 Acquisitions generate a larger portion of their business in the non-room categories that typically yield lower margins and are subject to a higher level of fixed costs which increase the impact of seasonality on operating income. The Base Portfolio's operating margin decreased by 0.6 points as the result of less than inflation increases in room revenues and the decline in non-room revenue.

## Hotel Expenses

Hotel expenses for the three months ended September 30, 2007 increased by \$16.4 million or 22.7% when compared to the same period in 2006. This increase reflects \$7.2 million in expenses incurred in the hotels acquired in 2006 after the end of the first quarter that were not owned for the entire comparative period and \$8.0 million in expenses in the hotels acquired in 2007. The remaining \$1.2 million related to the Base Portfolio represents a 1.6% increase over the same period in 2006.

## Hotel Operating Income

Hotel operating income (“HOI”) for the three months ended September 30, 2007 improved by \$5.1 million to \$49.9 million. This was a result of an increase in hotel revenues of \$21.5 million less an overall increase in hotel expenses of \$16.4 million.

A geographical comparison of the HOI variance between the three months ended September 30, 2007 and 2006 is as follows:

	Hotels	Rooms	As a % of total	HOI variance	As a % of total	Var % over 2006
<b>Base Portfolio</b>						
Ontario	70	8,251	42.6%	\$ (1,349)	(26.3)%	(5.7)%
Québec	31	3,056	15.8%	235	4.6%	2.7%
Atlantic	17	1,482	7.6%	366	7.1%	5.8%
West	15	1,919	9.9%	285	5.6%	5.4%
Sub-total	133	14,708	75.9%	(463)	(9.0)%	(1.1)%
<b>2006 Acquisitions</b>	2	768	4.0%	2,084	40.7%	263.1%
<b>2007 Acquisitions</b>	13	3,905	20.1%	3,501	68.3%	—
<b>Total</b>	<b>148</b>	<b>19,381</b>	<b>100.0%</b>	<b>\$ 5,122</b>	<b>100.0%</b>	<b>11.4%</b>

Increases in the 2006 Acquisitions of \$2.1 million and the 2007 Acquisitions of \$3.5 million were partially offset by a decline in the Base Portfolio of \$463. In the Base Portfolio, increases in HOI were experienced in three of four regions with the largest dollar and percentage increase achieved in the Eastern region at \$366 and 5.8%. The reduction in Ontario was generated in the GTA (\$671 or 11.2%) and the Oshawa region (\$641 or 39.2%).

## Other Income and Expenses

The net amount of other income and expenses for the three months ended September 30, 2007 was \$24.7 million, \$2.0 million or 8.6% more than the same period in 2006. The main contributors to this increase were a \$1.8 million increase in interest on mortgages and other debt, a \$769 increase in convertible debentures interest and accretion, a \$427 increase in depreciation and amortization, a \$490 increase in corporate and administrative expenses, a \$1.3 million increase in other income and a \$337 reduction in capital tax. The increases were mainly related to the hotels acquired during 2006 and 2007. The increase in convertible debentures interest and accretion was the result of the issuance of the Series C – 5.85% Debentures on August 3, 2007. The reduction in capital tax was the result of the corporate reorganization completed on January 2, 2007.

## Income Taxes

Current income tax recovery for the three months ended September 30, 2007 was \$5 a decrease of \$54 from the recovery recorded as the result of losses carried back to prior periods in corporate subsidiaries of InnVest in the same period in 2006. Further, InnVest recorded a future income tax recovery of \$5.1 million to reflect the drawdown on the future income tax liability in the quarter.

## Management's discussion and analysis

### Net income from Continuing Operations

InnVest's net income from continuing operations was \$30.2 million or \$0.454 per unit basic (\$0.423 – diluted), compared with a net income in the prior year's period of \$23.3 million or \$0.425 per unit basic (\$0.395 – diluted). The increase of \$6.9 million is the combined result of income generated by the hotels acquired in 2006 after the end of the second quarter and the hotels acquired in 2007 and the increase in the future income tax recovery recorded of \$3.8 million.

### Non-GAAP financial measures

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InnVest uses non-GAAP financial measures to assess its operating performance. A discussion of non-GAAP financial measures used by the REIT, including reconciliations to GAAP financial measures, is included herein. Securities regulators require that companies caution readers that earnings and other measures adjusted to a basis other than GAAP do not have standardized meanings and are unlikely to be comparable to similar measures used by other companies.

### Funds from Operations

Funds from operations ("FFO") is widely used in the real estate industry. InnVest believes that FFO is a useful supplemental measure of the Trust's operating performance for investors. FFO assumes that the value of real estate investments does not necessarily decrease on a systematic basis over time, an assumption inherent in GAAP, and it adjusts for items included in GAAP net income that do not necessarily provide the best indicator of operating performance, such as gains or losses on the sale of, and provisions for impairment against hotel properties, along with depreciation and amortization relating to capital items. As an indicator of performance, FFO should not be considered a substitute for net income or funds from operating activities determined in accordance with GAAP.

The Real Property Association of Canada generally defines FFO as net income adjusted for extraordinary items, gains or losses on the sale of assets, provisions for impairment against property values, capital items and depreciation and amortization relating to capital items. The REIT's method of calculating FFO may be different from that of other organizations.

The REIT currently calculates FFO by using net income and adjusting for:

- i) Depreciation, amortization and accretion, excluding amortization of deferred financing costs,
- ii) Future income tax expense or recovery,
- iii) Non-cash executive and trustee compensation expense,
- iv) Gains or write down of assets held for sale, and
- v) Corporate restructuring expense.

FFO for the three months ended September 30, 2007 increased \$4.1 million to \$39.4 million or \$0.592 per unit basic (\$0.535 – diluted) from \$35.3 million or \$0.645 per unit basic (\$0.578 – diluted) in the same period of 2006.

### Distributable Income

Distributable income is commonly used in the real estate investment trust industry to measure performance. Distributable income is used by management to determine the level of distributions paid to unitholders. Distributable income is also used as a guideline by management in evaluating operating and financial decisions, including acquisitions and financings. Distributable income is one measure used by industry analysts and investors in the determination of the Trust's valuation, its ability to fund distributions and its investment return requirements. As a result, InnVest believes that distributable income is a useful supplemental measure of the Trust's operating performance for investors.



Distributable income is defined in the REIT's Declaration of Trust to mean net income of the REIT and its consolidated subsidiaries as reported in its consolidated financial statements adjusted for:

- i) Depreciation, amortization and accretion and future income tax expense,
- ii) Any gains or losses on the disposition of any real property and any future income tax benefits,
- iii) The reserve for replacement of furniture, fixtures and equipment and capital improvements ("FF&E reserve"), and
- iv) Any other adjustment determined by a majority of the Trustees of the REIT in their discretion.

The calculation of distributable income and the amounts of each adjustment from net income are disclosed in the notes to the financial statements. As outlined in the Declaration of Trust, the REIT is required to distribute not less than 80% of the estimated annualized distributable income of the REIT, payable in monthly installments.

The following table reconciles cash flows from operating activities to distributable income in accordance with Canadian Securities Administrators Staff Notice 41-201 Income Trusts and Other Indirect Offerings. Management considers distributable cash to be equivalent to distributable income. The reconciliation has been prepared using reasonable and supportable assumptions which reflect the REIT's planned courses of action given management's judgment about the most probable set of economic conditions.

	<b>Three Months Ended Sept. 30, 2007</b>	Three Months Ended Sept. 30, 2006	<b>Nine Months Ended Sept. 30, 2007</b>	Nine Months Ended Sept. 30, 2006
Reconciliation of Cash flow from operating activities to Distributable income				
Cash flow from operating activities	\$ 42,227	\$ 36,460	\$ 67,628	\$ 64,083
Changes in non-cash working capital	(2,067)	(156)	2,682	1,107
Miscellaneous, including changes in non-cash working capital – discontinued operations	(25)	(54)	90	(25)
Corporate reorganization expense	43	–	1,514	–
Reserve for replacement of furniture, fixtures and equipment and capital improvements ("FF&E Reserve")	(5,551)	(4,746)	(13,630)	(11,688)
Deferred land lease expense and retail lease income, net	8	34	25	84
<b>Distributable income</b>	<b>\$ 34,639</b>	<b>\$ 31,538</b>	<b>\$ 58,309</b>	<b>\$ 53,561</b>

A capital replacement reserve, as established by the REIT based on its knowledge of capital investment needs of the portfolio, is deducted in deriving distributable income. Historically, the capital replacement reserve has approximated 4% of the REIT's revenues. Capital investments above this amount will be considered to take advantage of market strengths and opportunities, as well as to better position hotels against new supply and renovated competitive products.

The non-recurring costs associated with InnVest's corporate reorganization in early 2007 have been added back to the calculation of distributable income since such a charge is not expected in future periods. Management also excludes the periodic movement in working capital in determining its distributable income. Due to the seasonal nature of operations, financial results and working capital movements are not evenly distributed throughout the year. Revenues are typically higher in the second and third quarters versus the first and fourth quarters in contrast to fixed costs such as amortization and interest, which are not significantly impacted by seasonal or short-term variations. Annual distributions are paid evenly through the year based on the annual outlook for the REIT, which does not consider seasonal variations in operations or working capital throughout the year.

For the three and nine months ended September 30, 2007, cash flows from operating activities exceeded distributable income by \$7.6 million and \$9.3 million, respectively.

## Management's discussion and analysis

For the three and nine months ended September 30, 2007, distributable income exceeded distributions declared by \$16.8 million and \$9.1 million, respectively. As previously noted, due to the seasonal nature of operations, financial results are not evenly distributed throughout the year. The first and the fourth quarters are typically weaker periods for InnVest's portfolio compared to distributions, which are paid evenly through the year.

Distributable income for the three months ended September 30, 2007 was \$34.6 million or \$0.520 per unit basic (\$0.474 – diluted). This reflects a \$3.1 million improvement over the distributable income experienced for the same period of the prior year of \$31.5 million or \$0.575 per unit basic (\$0.519 – diluted).

### Changes in Financial Position

The following discussion evaluates the cash flow results of InnVest from operating, financing and investing activities for the three months ended September 30, 2007.

#### **Operating Activities**

Funds generated from operating activities increased \$5.8 million to \$42.2 million for the three months ended September 30, 2007. The increase is mainly attributable to an increase in hotel operating income of \$5.1 million less an increase in the cash portion of interest expense on mortgages and other debt of \$1.5 million, an increase in the cash portion of convertible debentures interest of \$534, an increase in corporate and administrative expense of \$490, an increase in other income related to interest earned on the investment of the net proceeds from the August 3, 2007 equity and convertible debenture issues of \$1.3 million, plus a net decrease in capital taxes and current income taxes of \$283, plus a net increase of \$1.9 million in changes in non-cash working capital, including the amount from discontinued operations.

#### **Financing Activities**

Funds provided through financing activities were \$472.2 million for the three months ended September 30, 2007 compared to funds provided of \$32.6 million for the same period in 2006. The majority of the change relates to:

- Issuance of units of \$191.7 million, net of commissions and costs;
- Increase of proceeds from the issuance of convertible debentures of \$70 million;
- Increase of \$215 million in proceeds of bank indebtedness;
- Decrease in the net of proceeds and repayment of long-term debt of \$33.7 million;
- Increase in debt issuance costs incurred of \$2.7 million; and
- Increase in cash distributions of \$1.2 million.

#### **Investing Activities**

Funds used for investing activities were \$499.1 million during the three months ended September 30, 2007 compared to \$79.5 million in the same period in 2006. The majority of the change relates to:

- Increase in cash used for hotel acquisitions (net of changes in non-cash working capital and including hotel under development and other assets of \$422.1 million);
- Decrease in capital expenditures of \$1.3 million; and
- Use of \$4.4 million in cash restricted for future furniture, fixtures and equipment and capital expenditures versus \$5.7 million in the same period of the prior year.

In the three months ended September 30, 2007, InnVest spent \$6.8 million on capital items (2006 – \$8.0 million).

As part of the regular refurbishment program, InnVest sets aside 4% of revenue (5% for the two Fairmont Hotels acquired as part of the Legacy transaction) for the replacement of furniture, fixture and equipment and capital improvements ("FF&E reserve") shown as restricted cash in the financial statements. The FF&E reserve is managed over the longer term to maintain the hotel properties to ensure they remain competitive in their markets.

## Operating results review – nine months ended September 30, 2007

### Hotel Operating Results Comparison

In summarizing the hotel operating results for the nine months ended September 30, 2007 and comparing those results to the nine months ended September 30, 2006, the REIT has categorized 128 of its hotels owned for the entire current and comparative period as its “Base Portfolio”. The seven hotels acquired in 2006 are categorized as the “2006 Acquisitions”, the two new build hotels and the eleven hotels acquired as part of the Legacy transaction are categorized as the “2007 Acquisitions”.

### Hotel Revenues

A summary of the hotel revenue categorized by room revenue and non-room revenue for the nine months ended September 30, 2007 and 2006 are stated below:

	2007	2006	Variance
<b>Room Revenue</b>			
Base Portfolio	\$ 247,685	\$ 244,529	\$ 3,156
2006 Acquisitions	33,146	7,892	25,254
2007 Acquisitions	7,602	–	7,602
Sub-total	\$ 288,433	\$ 252,421	\$ 36,012
<b>Non-Room Revenue</b>			
Base Portfolio	\$ 34,246	\$ 35,062	\$ (816)
2006 Acquisitions	13,528	2,782	10,746
2007 Acquisitions	3,947	–	3,947
Sub-total	\$ 51,721	\$ 37,844	\$ 13,877
<b>Hotel Revenue</b>			
Base Portfolio	\$ 281,931	\$ 279,591	\$ 2,340
2006 Acquisitions	46,674	10,674	36,000
2007 Acquisitions	11,549	–	11,549
Total	\$ 340,154	\$ 290,265	\$ 49,889

### Overall Hotel Portfolio

Hotel revenue increased by \$49.9 million, with \$36.0 million and \$11.5 million of the increase due to the hotels acquired in 2006 and 2007 respectively. The Base Portfolio of 128 hotels contributed \$2.3 million of the increase, which represents a 0.8% improvement over the same period in the prior year. All of the 2006 Acquisitions were acquired prior to the end of the third quarter of 2006, with one hotel acquired on March 3, 2006, two Hiltons on April 28, 2006, two Deltas on May 25, 2006 and the two remaining Hiltons on September 19, 2006. The Staybridge Suites in London, Ontario and the Holiday Inn Express in North Bay, Ontario were acquired on July 20, 2007 and September 13, 2007 respectively, while the 11 hotels acquired as part of the Legacy transaction were acquired on September 18, 2007.

The increase of \$36.0 million in room revenues for the nine months ended September 30, 2007 reflects \$25.3 million in revenues from the hotels acquired in 2006 and \$7.6 million in revenues from the hotels acquired in 2007. The balance of \$3.2 million improvement reflects an overall increase in room revenue of 1.3% in the Base Portfolio. There were increases in the Québec, Atlantic and Western regions, with the largest dollar and percentage increase experienced in the Western region.

## Management's discussion and analysis

### Room Revenues

A geographical comparison of the room revenue variance between the nine months ended September 30, 2007 and 2006, excluding the assets classified as discontinued operations, is as follows:

	Hotels	Rooms	As a % of total	Room Revenue variance	As a % of total	Var % over 2006
<b>Base Portfolio</b>						
Ontario	67	7,986	41.2%	\$ (1,694)	(4.7)%	(1.2)%
Québec	29	2,719	14.0%	510	1.4%	1.1%
Atlantic	17	1,482	7.6%	1,236	3.4%	4.8%
Western	15	1,919	9.9%	3,104	8.6%	11.4%
Sub-total	128	14,106	72.7%	3,156	8.7%	1.3%
<b>2006 Acquisitions</b>	7	1,370	7.1%	25,254	70.2%	320.0%
<b>2007 Acquisitions</b>	13	3,905	20.2%	7,602	21.1%	—
<b>Total</b>	<b>148</b>	<b>19,381</b>	<b>100.0%</b>	<b>\$ 36,012</b>	<b>100.0%</b>	<b>14.3%</b>

The Ontario hotels experienced a decline of \$1.7 million or 1.1% in room revenues relative to the same period in 2006. The Ontario markets which contributed to the decline were Windsor (\$440 or 10.8%), Oshawa (\$1.6 million or 10.8%), London (\$544 or 4.9%), the GTA (\$654 or 1.6%) and Burlington-Oakville (\$648 or 5.5%), while InnVest's hotels elsewhere in Ontario posted room revenue increases of \$2.2 million or 3.2%. The Windsor market was impacted from Detroit hosting the Super Bowl in 2006. The Oshawa market continues to be impacted by reduced activity in local automotive manufacturing and new competition, while the London and Burlington-Oakville markets decline were the result of a decline in occupancy caused by new competition. The Ontario markets with significant positive contribution to the results for the nine-month period were Eastern Ontario (\$435 or 4.9%), Northern Ontario (\$233 or 3.5%) and Ottawa (\$1.6 million or 9.8%).

InnVest's Base Portfolio of hotels in Québec experienced room revenue increase of \$510 or 1.1%. The REIT's rural Québec hotels contributed positively improving by \$837 or 6.1%, while the REIT's Montreal hotels posted a decline of \$449 or 1.9% and Québec City posted a gain of \$122 or 1.7%.

InnVest's Base Portfolio of Atlantic region hotels experienced growth of \$1.2 million or 4.8% from the same period in 2006, with gains in all four provinces.

InnVest's Base Portfolio of Western hotels continued to experience significant revenue growth posting an increase of \$3.1 million or 11.4% over the same period in the prior year. The majority of the gains were posted by the hotels located in Alberta (\$1.9 million or 10.8%) and Saskatchewan (\$612 or 10.9%). This increase was attributable to occupancy improvements and room rate increases related to economic activity generated by the oil and gas industry.

### Non-Room Revenues

Non-room revenues increased by \$13.9 million, reflecting the non-room revenues generated by the hotels the REIT acquired in 2006, which were not owned for the entire comparative period and the 2007 Acquisitions. The majority of the hotels which were acquired in 2006 and 2007 generate a higher proportion of total revenues from non-room revenues such as food and beverage sales.

## Hotel Operating Income Margin Analysis

The following chart illustrates the REIT's margins for the Base Portfolio and the 2006 and 2007 Acquisitions, excluding the assets classified as discontinued operations, for the nine months ended September 30, 2007 and 2006:

2007	Base Portfolio	2006 Acquisitions <sup>(1)</sup>	2007 Acquisitions <sup>(2)</sup>	Total
Hotel revenues	\$ 281,931	\$ 46,674	\$ 11,549	\$ 340,154
Hotel expenses				
Operating expenses	157,367	33,493	6,549	197,409
Property taxes, rent and insurance	26,003	2,337	882	29,222
Management fees	9,529	1,490	617	11,636
	192,899	37,320	8,048	238,267
Hotel operating income	\$ 89,032	\$ 9,354	\$ 3,501	\$ 101,887
HOI margin	<b>31.6%</b>	<b>20.0%</b>	<b>30.3%</b>	<b>30.0%</b>

  

2006	Base Portfolio	2006 Acquisitions <sup>(1)</sup>	2007 Acquisitions <sup>(2)</sup>	Total
Hotel revenues	\$ 279,591	\$ 10,674	\$ —	\$ 290,265
Hotel expenses				
Operating expenses	153,966	6,312	0	160,278
Property taxes, rent and insurance	25,593	531	0	26,124
Management fees	9,441	324	0	9,765
	189,000	7,167	0	196,167
Hotel operating income	\$ 90,591	\$ 3,507	\$ —	\$ 94,098
HOI margin	<b>32.4%</b>	<b>32.9%</b>	<b>—</b>	<b>32.4%</b>

  

Variance	Base Portfolio	2006 Acquisitions <sup>(1)</sup>	2007 Acquisitions <sup>(2)</sup>	Total
Hotel revenues	\$ 2,340	\$ 36,000	\$ 11,549	\$ 49,889
Hotel expenses				
Operating expenses	3,401	27,181	6,549	37,131
Property taxes, rent and insurance	410	1,806	882	3,098
Management fees	88	1,166	617	1,871
	3,899	30,153	8,048	42,100
Hotel operating income	\$ (1,559)	\$ 5,847	\$ 3,501	\$ 7,789
HOI margin	<b>(0.8)%</b>	<b>(12.9)%</b>	<b>—</b>	<b>(2.4)%</b>

(1) The 2006 Acquisitions represent hotels acquired in 2006 that were not owned for the entire comparative period.

(2) The 2007 Acquisitions represent hotels acquired in 2007 that were not owned for the entire comparative period.

Total hotel operating income margin decreased by 2.4 points, which is primarily attributed to the impact of seasonality inherent in the 2006 Acquisitions, which were acquired in the second and third quarters of 2006 and the resulting lower margins experienced for the 2006 Acquisitions relative to the Base Portfolio. The 2007 Acquisitions generated a HOI margin of 30.3%, which is below the Base Portfolio. The 2006 and 2007 Acquisitions generate a larger portion of their business in the non-room categories that typically yield lower margins and are subject to a higher level of fixed costs which increase the impact of seasonality on operating income. The Base Portfolio's operating margin decreased by 0.8 points as the result of below than inflation increases in room revenues and the decline in non-room revenue.

## Management's discussion and analysis

### Hotel Expenses

Hotel expenses for the nine months ended September 30, 2007 increased by \$42.1 million or 21.5% when compared to the same period in 2006. This increase reflects \$30.2 million in expenses incurred in the hotels acquired in 2006, which were not owned for the entire comparative period, and \$8.0 million in expenses incurred in the 2007 Acquisitions. The remaining \$3.9 million relates to the Base Portfolio, and represents a 2.1% increase over the same period in 2006.

### Hotel Operating Income

Hotel operating income ("HOI") for the nine months ended September 30, 2007 improved by \$7.8 million to \$101.9 million. This was a result of an increase in hotel revenues of \$49.9 million less an overall increase in hotel expenses of \$42.1 million.

A geographical comparison of the HOI variance between the nine months ended September 30, 2007 and 2006 is as follows:

	Hotels	Rooms	As a % of total	HOI variance	As a % of total	Var % over 2006
<b>Base Portfolio</b>						
Ontario	67	7,986	41.2%	\$ (3,153)	(40.5)%	(6.1)%
Québec	29	2,719	14.0%	(543)	(7.0)%	(3.2)%
Atlantic	17	1,482	7.6%	825	10.6%	7.6%
West	15	1,919	9.9%	1,312	16.8%	11.9%
Sub-total	128	14,106	72.7%	(1,559)	(20.1)%	(1.7)%
<b>2006 Acquisitions</b>	7	1,370	7.1%	5,847	75.1%	166.7%
<b>2007 Acquisitions</b>	13	3,905	20.2%	3,501	45.0%	—
Total	148	19,381	100.0%	\$ 7,789	100.0%	8.3%

Increases in the 2006 Acquisitions of \$5.8 million and the 2007 Acquisitions of \$3.5 million were partially offset by a decline in the Base Portfolio of \$1.6 million. In the Base Portfolio, increases in HOI were experienced in two out of four regions with the largest dollar and percentage increase achieved in the Western region at \$1.3 million and 11.9%.

### Other Income and Expenses

The net amount of other income and expenses for the nine months ended September 30, 2007 was \$76.4 million, \$8.1 million or 11.9% more than the same period in 2006. The main contributors to this increase were a \$4.0 million increase in depreciation and amortization, a \$4.9 million increase in interest on mortgages and other debt, a \$2.2 million increase in corporate and administrative expenses, a \$1.0 million increase in other business income and a \$1.1 million reduction in capital tax and a \$348 increase in convertible debentures interest and accretion. The increases were mainly related to the hotels acquired during 2006 and 2007, while the corporate and administrative expense increase was the result of land transfer tax and legal costs associated with a reorganization of InnVest. The increase in convertible debentures interest and accretion was the net result of the issuance of the Series C – 5.85% Debentures on August 3, 2007, the conversion of debentures in the period and the amortization of costs associated with the issuing of the debentures because of the use of the effective interest method. The reduction in capital tax was the result of the corporate reorganization completed on January 2, 2007.

## Income Taxes

Current income tax recovery for the nine months ended September 30, 2007 was \$5, a decrease of \$181 from the recovery recorded as the result of losses carried back to prior periods in corporate subsidiaries of InnVest in the same period in 2006. Further, InnVest experienced a \$2.0 million future income tax expense during the nine-month period as compared to a recovery of \$14.2 million in the same period of the prior year which mainly resulted from reductions in the corporate income tax rates.

In 2006, 40.5% of the distributions made during that year were not taxable to unitholders. For calendar 2007, the REIT estimates that approximately 40% of unitholder distributions will not be taxable to unitholders.

## Net income from Continuing Operations

InnVest's net income from continuing operations was \$23.4 million or \$0.395 per unit basic and diluted, compared with a net income from continuing operations in the prior year's period of \$40.1 million or \$0.775 per unit basic (\$0.763 – diluted). The decrease of \$16.7 million is mainly the combined result of the recording of a future income tax expense of \$2.0 million compared to a recovery in the prior year's period of \$14.2 million.

## Funds from Operations

FFO for the nine months ended September 30, 2007 increased \$6.7 million to \$69.3 million or \$1.168 per unit basic (\$1.089 – diluted) from \$62.6 million or \$1.210 per unit basic (\$1.118 – diluted) in the same period of 2006.

## Distributable Income

Distributable income for the nine months ended September 30, 2007 was \$58.3 million or \$0.983 per unit basic (\$0.931 – diluted). This reflects a \$4.7 million improvement over the distributable income experienced for the same period of the prior year of \$53.6 million or \$1.034 per unit basic (\$0.972 – diluted).

## Changes in Financial Condition

The following discussion evaluates the cash flow results of InnVest from operating, financing and investing activities for the nine months ended September 30, 2007.

### **Operating Activities**

Funds generated from operating activities increased \$3.5 million to \$67.6 million for the nine months ended September 30, 2007. The increase is mainly attributable to an increase in hotel operating income of \$7.8 million less an increase in the cash portion of interest expense on mortgages and other debt of \$3.5 million, a decrease in the cash portion of convertible debentures interest of \$287, an increase in corporate and administrative expense of \$2.2 million, an increase in other income related to interest earned on the investment of the net proceeds from the August 3, 2007 equity and convertible debenture issues of \$1.3 million, an increase in other business income of \$1.0 million, plus a net decrease in capital taxes and current income taxes of \$930, minus a net decrease of \$1.6 million in changes in non-cash working capital, including the amount from discontinued operations.

## Management's discussion and analysis

### Financing Activities

Funds provided through financing activities were \$458.8 million for the nine months ended September 30, 2007 compared to funds provided of \$80.3 million for the same period in 2006. The majority of the change relates to:

- Issuance of units of \$191.7 million, net of commissions and costs;
- Decrease of proceeds from the issuance of convertible debentures of \$5 million;
- Increase of \$218.8 million in proceeds of bank indebtedness;
- Decrease in the net of proceeds and repayment of long-term debt of \$22.9 million;
- Increase in debt issuance costs incurred of \$643;
- Increase in cash distributions of \$1.2 million; and
- Increase in the repayment of debt from discontinued operations of \$2.2 million.

### Investing Activities

Funds used for investing activities were \$507.6 million during the nine months ended September 30, 2007 compared to \$147.7 million in the same period in 2006. The majority of the change relates to:

- Increase in cash used for hotel acquisitions (including changes in non-cash working capital), hotel under development and other assets of \$367.4 million;
- Sale of discontinued assets of \$6.4 million;
- Increase in capital expenditures of \$895; and
- Cash use of \$330 for cash restricted for future furniture, fixtures and equipment and capital expenditures versus the use of \$2.5 million in the prior period.

In the nine months ended September 30, 2007, InnVest spent \$20.3 million on capital items (2006 – \$19.4 million).

## Liquidity and capital resources

### Financial Commitments

The following chart summarizes InnVest's future contractual obligations as at September 30, 2007:

	Remainder of 2007	2008	2009	2010	2011	2012 and thereafter	Total
Bank indebtedness – principal	\$ –	\$ 215,000	\$ –	\$ –	\$ –	\$ –	\$ 215,000
Bank indebtedness – interest	4,091	7,338	–	–	–	–	11,429
Mortgages payable – principal	3,510	12,710	54,946	227,402	56,616	377,723	732,907
Mortgages payable – interest	11,297	46,676	43,286	33,190	25,373	57,700	217,522
Capital lease – principal	251	130	138	146	155	1,383	2,203
Capital lease – interest	35	234	235	239	239	537	1,519
Convertible debentures – principal	–	–	–	–	45,764	145,000	190,764
Convertible debentures – interest	3,623	11,455	11,455	11,455	10,025	19,035	67,048
Long-term land leases	1,196	4,787	4,790	4,862	4,409	96,738	116,782
Operating equipment and office leases	358	1,352	1,181	923	625	2,695	7,134
	\$ 24,361	\$ 299,682	\$ 116,031	\$ 278,217	\$ 143,206	\$ 700,811	\$1,562,308



The Legacy transaction bridge loan facility of \$215 million matures on June 13, 2008. It is expected that this facility will be repaid from mortgage financing to be secured against the majority of the 11 hotels acquired as part of the transaction prior to maturity.

The next material refinancing of long-term debt is scheduled to occur in 2010 when \$227.4 million of long-term debt with a weighted average interest rate of 6.7% matures. In the second quarter of 2007, the REIT completed an early extension of \$147.7 of mortgage debt with a weighted average interest rate of 7.4%, that was to have matured in July 2008, fixing the interest rate on \$130 million at 5.8% for a blended interest rate of 6.2% per annum for a period of seven years and maintained floating rate debt of \$17.7 million, which at current rates bears interest of approximately 6.3% per annum. As part of this early extension, InnVest increased its proceeds by \$25.9 million, which were used to repay the operating loan balance and to fund acquisitions.

The long-term land leases require minimum annual average lease payments as outlined above and expire between 2023 and 2088. There are also future rental charges determined as a percentage of revenue that are not included in the amounts reflected above.

### Distributions to Unitholders

The following chart illustrates the distributable income that the REIT has generated relative to cash distributions paid to unitholders for the twelve months ended September 30, 2007 and for the years ended December 31, 2006, 2005, 2004 and 2003, the period ended December 31, 2002 and the cumulative period from the REIT's inception on July 26, 2002 to September 30, 2007:

	<b>12 months ended Sept. 30, 2007</b>	2006	Years ended December 31			Period ended Dec. 31, 2002 <sup>(1)</sup>	Cumulative since inception to Sept. 30, 2007
			2005	2004	2003		
Distributable income <sup>(2)</sup>	<b>\$ 67,519</b>	\$ 62,771	\$ 48,721	\$ 44,269	\$ 39,455	\$ 25,263	\$ 278,788
Distributions	<b>64,641</b>	59,605	52,884	50,164	46,280	20,000	278,119
Distributable income in excess of (less than) distributions	<b>2,878</b>	3,166	(4,163)	(5,895)	(6,825)	5,263	669
Non-cash distributions made through the distribution reinvestment plan ("DRIP")	<b>8,083</b>	4,166	3,303	3,168	1,367	-	18,663
Distributable income in excess of (less than) cash distributions	<b>\$ 10,961</b>	\$ 7,332	\$ (860)	\$ (2,727)	\$ (5,458)	\$ 5,263	\$ 19,332
Payout ratios:							
Total distributions	<b>95.7%</b>	95.0%	108.5%	113.3%	117.3%	79.2%	99.8%
Cash distributions (total distributions minus DRIP)	<b>83.8%</b>	88.3%	101.8%	106.2%	113.8%	79.2%	93.1%

(1) For the period from July 26, 2002 to December 31, 2002.

(2) Distributable income is calculated after deducting 4% of total hotel revenues as a reserve for future furniture, fixtures and equipment and capital expenditures.

## Management's discussion and analysis

The REIT's trailing twelve month payout ratio improved by 0.9% points from 96.6% at June 30, 2007 to 95.7% as a result of increases in distributable income from the hotels acquired after the end of the second quarter in 2006 and the hotels acquired in 2007. On a cash basis, the ratio improved by 1.5% points to 83.8% as the result of distributable income generated by the hotels acquired after the end of the second quarter in 2006 and the hotels acquired in 2007 and as the result of increased participation in the DRIP program. On a cumulative basis from the inception of the REIT on July 26, 2002, the payout ratio has been 99.8% or 93.1% on a cash basis. Liquidity to fund distributions is generated from cash flow from operations, cash on hand, bank operating lines available and by the ability to finance certain unencumbered or under-leveraged assets.

Distributions to unitholders are approved by the REIT's Board of Trustees. In exercising their discretion to approve the level of distributions, the Trustees use forecasts prepared by management and other financial information to determine if sufficient cash flow will be available to fund distributions. Such financial information is subject to change due to the nature of the Canadian hotel industry which can be difficult to predict even in the short-run. This includes the following factors:

1. Its exposure to the overall cyclical effects of the Canadian business environment,
2. The seasonal nature of the REIT's business,
3. The REIT's geographical diversity. InnVest's hotels are located in numerous regions throughout Canada each with its own unique characteristics,
4. Changing customer sentiment toward brands which the REIT's hotel properties use,
5. Changes in customer segmentation due to changing social, economic and political conditions, and
6. Numerous other macroeconomic, social and geopolitical factors which are beyond the control of the REIT.

All of these factors can have a material effect on the REIT's revenue and cost structure. An example is the significant impact of SARS on the Canadian hotel industry in 2003. As a result of the REIT's exposure to numerous factors which are beyond its control, it is difficult for management of the REIT to make predictions concerning distribution levels for future quarters. Therefore, management asserts that it would not be prudent to provide investors or potential investors with forward-looking information regarding distribution levels.

### Capital Resources

The REIT's cash position at September 30, 2007 was \$28.4 million, of which \$5.0 million is restricted under the REIT's trust indenture for the replacement of furniture, fixtures, and equipment and for capital improvements.

InnVest sets aside a reserve of 4% (5% for the two Fairmont Hotels) of total hotel revenue and certain amounts required for hotel acquisitions for replacing furniture, fixtures and equipment and capital improvements. Capital expenditures committed and yet to be incurred at September 30, 2007 were \$10 million. The current expectation is that capital spending on the hotel portfolio owned at September 30, 2007 will be approximately \$30 million for the year ending December 31, 2007.

The following chart shows the changes in the restricted cash balance for the three and nine months ended September 30, 2007 along with the comparable periods:

	<b>Three Months Ended Sept. 30, 2007</b>	Three Months Ended Sept. 30, 2006	<b>Nine Months Ended Sept. 30, 2007</b>	Nine Months Ended Sept. 30, 2006
Opening balance	\$ 567	\$ 2,870	\$ 4,693	\$ 6,079
FF&E Reserve	5,551	4,685	13,630	11,639
Adjustment – discontinued operations		61		49
Transferred to operating cash	(1,302)	–	–	–
Initial reserve – Hotels Acquired	6,967	9,000	6,967	10,200
Capital expenditures	(6,760)	(8,021)	(20,267)	(19,372)
Closing balance	\$ 5,023	\$ 8,595	\$ 5,023	\$ 8,595

InnVest is not permitted to exceed certain financial leverage amounts under the terms of the Declaration of Trust. The REIT is permitted to hold indebtedness excluding convertible debentures up to a level of 50% of gross book value. InnVest calculates indebtedness in accordance with GAAP excluding non-interest bearing indebtedness, trade accounts payable, and any future income tax liability. InnVest calculates gross book value as the total book value of assets on the REIT's balance sheet, plus the amount of accumulated depreciation and amortization, less any future income tax liabilities. Further, the REIT is permitted to have indebtedness and convertible debentures up to a level of 60% of gross asset value. At September 30, 2007, the REIT's leverage excluding and including convertible debentures was 46.9% and 56.3% respectively calculated as follows:

Total assets per Balance Sheet	\$ 2,094,303	
Accumulated depreciation and amortization	162,665	
Future income tax liability	(259,109)	
Future income tax liability not included in assets	23,909	
Gross Asset Value	\$ 2,021,768	
Book value of mortgage and other indebtedness <sup>(1)</sup>	\$ 947,907	46.9%
Convertible debentures <sup>(2)</sup>	190,764	9.4%
Total debt	\$ 1,138,671	56.3%

(1) Adjusted to eliminate financing issuance costs

(2) Adjusted to face value

The REIT also had unused operating loan availability of \$25 million at September 30, 2007 and eight hotel properties which remain unencumbered. The REIT estimates that the unencumbered hotels could generate approximately \$45 million in mortgage proceeds. The REIT also has an unused acquisition facility of \$40 million available to acquire hotel properties and an unused loan facility of \$29.1 million available to fund capital expenditures.

During the nine months ended September 30, 2007, the REIT distributed \$49.2 million or \$0.8438 per unit, of which \$6.7 million was distributed in units as part of the Distribution Reinvestment Plan ("DRIP"), at the rate of \$0.09375 per unit per month. A regular monthly distribution of \$0.09375 per unit for the month of September 2007 was paid in October 2007. A distribution at the same rate for October 2007 was declared and will be payable on November 15, 2007.

InnVest expects to make cash distributions based on cash flow to be generated from operations and its borrowing capacity. Future growth is expected to be funded from borrowing capacity and through the issuance of trust units.

## Management's discussion and analysis

### Equity

At September 30, 2007 a total of 72,610,235 units of the REIT were outstanding. There is only one class of trust units, with each unit eligible for one vote. For the nine months ended September 30, 2007 and subsequently to November 7, 2007, units of the REIT were issued as follows:

	Units	Amount
<b>Balance at December 31, 2006</b>	55,045,351	\$ 543,363
<i>First quarter activity of Units issued</i>		
DRIP	160,050	2,191
Executive compensation plan	20,139	275
Trustees compensation plan	1,650	23
Conversion of debentures	384,720	4,908
<b>Balance at March 31, 2007</b>	55,611,910	\$ 550,760
<i>Second quarter activity of Units issued</i>		
DRIP	207,068	2,743
Conversion of debentures	446,080	5,697
<b>Balance at June 30, 2007</b>	56,265,058	\$ 559,200
<i>Third quarter activity of Units issued</i>		
DRIP	145,308	1,725
Trustees compensation plan	4,869	64
Units issued	16,195,000	192,268
Conversion of debentures - adjustment	-	-
<b>Balance at September 30, 2007</b>	72,610,235	\$ 753,257
<i>Activity subsequent to September 30, 2007</i>		
Trustees compensation plan	15,140	181
DRIP	168,551	1018
<b>Balance at November 7, 2007</b>	72,793,926	\$ 754,456

A total of \$45.8 million of the Series A – 6.25% Debentures remained outstanding at September 30, 2007. These debentures are convertible into trust units at a strike price of \$12.50, bear interest at 6.25% per annum payable semi-annually on April 15 and October 15 of each year and are due April 15, 2011. No debentures were converted into units during the third quarter and no further debentures were converted into units of InnVest subsequent to September 30, 2007. The trust units to be issued upon conversion of the Series A – 6.25% Debentures outstanding at September 30, 2007 are 3,661,120.

A total of \$75 million of the Series B – 6.00% Debentures remained outstanding at September 30, 2007. The Series B – 6.00% Debentures are convertible into trust units at a strike price of \$14.90, bear interest at 6.00% per annum payable semi-annually on May 31 and November 30 of each year and are due May 31, 2013. The trust units to be issued upon conversion of the Series B – 6.00% Debentures total 5,033,557.

A total of \$70 million of Series C – 5.85% Debentures were issued during the third quarter. These debentures have a maturity date of August 1, 2014, have a coupon of 5.85% per annum and will pay interest semi-annually in arrears on August 1 and February 1 in each year commencing on February 1, 2008. The convertible debentures are convertible into approximately 68.027 units of the REIT per \$1,000 principal amount, at any time, at the option of the holder, representing a conversion price of \$14.70 per unit. The trust units to be issued upon conversion of the Series C – 5.85% Debentures total 4,761,904.

## Risks and uncertainties

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InnVest's risks and uncertainties remain substantially unchanged from the description provided in the MD&A for the year ended December 31, 2006, except as noted below.

In September 2007, InnVest, in partnership with Cadbridge acquired Legacy and in October 2007, ten of the hotels (and the operating assets relating thereto) previously held by Legacy were transferred to affiliates of the REIT as part of a reorganization of the affairs of Legacy (the "Reorganization"). An eleventh hotel is expected to be transferred to an affiliate of the REIT prior to the end of 2007.

Although the REIT conducted what it believes to be a prudent and thorough level of due diligence in connection with the acquisition of Legacy and the Reorganization, there can be no assurance that there are no undisclosed or unknown liabilities of, or issues concerning, Legacy or the Legacy Portfolio. Pursuant to an arrangement with Cadbridge, the REIT will be responsible for any residual liabilities of Legacy that are solely related to the Legacy Portfolio and 26% of residual liabilities of Legacy that are not solely related to a specific property. As a result, the REIT may discover undisclosed liabilities that could be material.

Each of the hotels in the Legacy Portfolio is managed by affiliates of Fairmont Hotels & Resorts Inc. ("Fairmont") pursuant to management agreements with such affiliates. These agreements expire at varying times, ranging from December 31, 2010 to December 31, 2047. The shorter term management agreements, which are in respect of certain Delta hotels, generally do not have any renewal options. In the event that the REIT is not able to negotiate a renewal of these agreements or a separate licence or franchise agreement to use the Delta name, the REIT may have to re-brand the hotels.

Although the Legacy Portfolio will continue to be managed by affiliates of Fairmont pursuant to existing management agreements, the REIT will be required to expend time and resources to effectively integrate these properties. This integration process could divert the attention of the REIT's management team and if such a diversion does occur, that this and any other difficulties the REIT may encounter in completing the transition could have a material adverse impact on the REIT.

### Proposed Tax Changes to Income Trusts

InnVest currently qualifies as a Mutual Fund Trust for income tax purposes. As required by its Declaration of Trust, InnVest intends to distribute all taxable income to its unitholders and to deduct these distributions for income tax purposes.

In June 2007, a Bill was enacted for the taxation of publicly traded trusts, including income trusts (the "Bill"). The Bill would apply to publicly traded trusts which existed prior to November 1, 2006 starting with taxation years ending in 2011, except for those existing trusts that qualify for the real estate investment trust ("Qualifying REIT") exception included in the legislation. There are certain circumstances where an existing trust may lose its relief from taxation in the interim periods to 2011 where it undergoes "undue expansion".

Pursuant to the legislation, a REIT which carries on Canadian hotel operations (including through subsidiaries) will not be a Qualifying REIT. As a result, InnVest will be subject to tax starting January 1, 2011 and has recognized a future income tax liability, in the second quarter, of \$122.6 million mainly resulting from temporary differences on hotel properties and licence contracts which are expected to reverse subsequent to January 1, 2011. For the nine months ended September 30, 2007, InnVest's future income tax liability has increased by \$132.2 million mainly due to the difference between income tax and book values of assets acquired as part of the Legacy transaction required under the enactment of the Bill. As well, the Bill may adversely affect the level of cash distribution to unitholders commencing in 2011 if InnVest does not become a Qualifying REIT by then.

## Management's discussion and analysis

Management is reviewing whether it is feasible to reorganize InnVest so that non-qualifying operations and assets are transferred under a plan of arrangement to a taxable entity that is held by InnVest unitholders, and the InnVest hotels, which continue to be owned by it, are leased by it to the taxable entity. It is not possible at this preliminary juncture to provide any assurances that any such reorganization or a similar reorganization can or will be implemented before 2011, or that any such reorganization, if implemented, would not result in material costs or other adverse consequences to InnVest and its unitholders.

## Outlook

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Supply and demand conditions in the hotel industry continue to be favourable. While varying by market, PKF Consulting Inc. ("PKF"), lodging industry experts, forecasts Canadian RevPAR continued growth in 2008 following anticipated growth of approximately 4% in 2007.

InnVest's geographic, customer, and brand diversity ideally positions it to continue to benefit from the anticipated growth in the Canadian hospitality industry. While InnVest is expecting RevPAR growth in its overall portfolio, there are certain markets, most notably Windsor, Oshawa and the GTA, that will continue to be more negatively impacted by the strength of the Canadian dollar. The decline in US visitation is expected to continue but is being offset by strengthening domestic and international corporate and group travel.

The acquisition of the Legacy Portfolio further expands the REIT's geographic diversity, notably within Western Canada which is experiencing the strongest growth in the country. The acquisition also enhances InnVest's presence in the upscale segment of the lodging industry which is forecast to lead RevPAR growth in 2008. Given that the Legacy acquisition closed late in the third quarter, the contribution on a per unit basis in 2007 is expected to be dilutive due to the seasonality inherent in the business. However, this acquisition is expected to be accretive in 2008.

Forecasted RevPAR growth, our ability to capitalize on our recent acquisitions and our ability to manage costs will drive InnVest's performance in 2008.

## Significant accounting policies

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### Related Party Transactions

#### **Franchise Business**

InnVest owns 50% of Choice Canada. The other 50% is owned by Choice Hotels International, which is one of the largest hotel franchise companies in the world. Choice Canada earns franchise revenue by charging monthly royalty fees to licenced hotel owners based on a percentage of the licenced hotels' revenue and by selling franchises. Under the terms of the joint venture agreement between Choice Hotels International and a subsidiary of the REIT, InnVest pays a below market royalty fee for its hotels that are franchised under the Choice hotel brands. This arrangement will remain in place for the duration of the joint venture until 2092. Royalty payments paid to Choice Canada by the REIT on a net basis for the three and nine months ended September 30, 2007 totaled \$136 and \$408, respectively.

#### **Hotel Management**

On July 26, 2002, the REIT entered into a management agreement for hotel management and accounting services and an administrative services agreement (the "Agreements") with Westmont. Westmont is controlled by a minority unitholder of the REIT. The Agreements have an initial term of 10 years with two successive five-year renewal terms, subject to the consent of Westmont and approval by the REIT. The Agreements will expire July 25, 2012. The Agreements are subject to non-competitive arrangements for limited service hotels in Canada. The Agreements provide for the payment of an annual management fee to Westmont equal to 3.375% of gross hotel revenue during the term of the Agreements, including renewal periods. In addition, Westmont may receive an annual incentive fee if the REIT achieves distributable income in excess of \$1.25 per unit. No management incentive fees were paid in the three or nine months ended September 30, 2007.

In addition to the base management fee and incentive fee, Westmont is entitled to reasonable fees based on a percentage of the cost of purchasing certain goods and supplies and certain construction costs and capital expenditures, fees for accounting services, reasonable out-of-pocket costs and expenses, other than general and administrative expenses or overhead costs except as otherwise provided in the Administrative Services Agreement, and project management and general contractor service fees related to hotel renovations managed by Westmont. Also, for certain hotels owned by InnVest and not managed by Westmont, Westmont is entitled to an asset management fee based on a fixed percentage of the purchase price of the hotel.

Total management fees paid to Westmont for the three and nine months ended September 30, 2007 were \$4.7 million and \$12.7 million respectively.

#### Hedging Transactions

InnVest's hedging transactions remain substantially unchanged from the description provided in the MD&A for the year ended December 31, 2006.

#### Critical Accounting Estimates

There have been no changes in InnVest's critical accounting estimates since December 31, 2006 and management is not anticipating any significant changes for the remainder of the year. A description of the REIT's significant accounting policies is summarized in Note 2 to the consolidated financial statements for the year ended December 31, 2006.

#### Changes in Significant Accounting Policies

##### **Comprehensive Income**

Effective January 1, 2007, the REIT adopted the new Canadian Institute of Chartered Accountants ("CICA") recommendations under Section 1530 that comprehensive income includes net earnings and other comprehensive income ("OCI"), which represents changes in the unitholders' equity during a period arising from transactions and other events with non-owners sources. The standard requires prospective application and accordingly, comparative amounts for prior periods, have not been restated. For the three and nine months ended September 30, 2007, there is no difference between the REIT's Consolidated Statement of Net Income and Statement of Comprehensive Income.

##### **Financial Instruments**

Effective January 1, 2007, the REIT adopted several new CICA recommendations related to accounting for Financial Instruments, including Section 3855 – Financial Instruments and Measurement. All financial instruments are required to be measured at fair value on initial recognition, except for certain related party transactions. Measurement in subsequent periods depends on whether the financial instrument has been classified as held-for-trading, available-for-sale, held-to-maturity, loans and receivables, or other liabilities. This standard requires a prospective application and accordingly, comparative amounts for prior periods, have not been restated.

As a result of implementing this Section, the REIT has recorded the interest expense for both the mortgage debt and convertible debentures using the effective interest method ("EIM"). Transaction costs that are directly attributable to the issue of financial instruments classified as other than "held-for-trading" are included in the initial carrying value of such instruments and amortized using the EIM, therefore the deferred financing costs which were related to these instruments were re-classified to the appropriate debt on the balance sheet. The amortization of these costs is included in interest expense in the financial statements, in a manner that yields a constant rate of interest over the life of the respective financial instrument, for the three and nine months ended September 30, 2007. An adjustment has been made to the opening cumulative net income in the amount of \$654 to reflect the application of the EIM.

In accordance with Section 3855, the REIT conducted a search for embedded derivatives in all contractual arrangements dated subsequent to October 31, 2002 and identified embedded features that required separate presentation, but all embedded features were determined to have negligible fair value.

## Management's discussion and analysis

With the introduction of the new standards relating to financial instruments – Section 3251, that establishes standards for the presentation of equity and changes in equity during the reporting period, the equity is presented as accumulated net income and other comprehensive income, distributions and total deficit.

### **Controls and Procedures**

#### *Internal Controls over Financial Reporting*

The REIT did not make any changes to its internal controls over financial reporting during the three and nine months ended September 30, 2007, that have materially affected, or are reasonably likely to affect, those controls. However, a control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. The inherent limitations in all controls systems ensure that no evaluation of controls can provide absolute assurance that all control issues, including instances of fraud, if any, have been detected. These inherent limitations include, amongst other items: (i) that management's assumptions and judgment could ultimately prove to be incorrect under varying conditions and circumstances; and (ii) the impact of material errors.

Additionally controls may be circumvented by the unauthorized acts of individuals, by collusion of two or more people, or by management override. The design of any system of controls is also based, in part, upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential (future) conditions.

#### Forward-looking information

The preceding management's discussion and analysis contains forward looking or outlook information with respect to InnVest. Because forward-looking information addresses future events and conditions, it involves risk and uncertainties that could cause actual results to differ materially from those contemplated by the forward-looking information. These risks and uncertainties are discussed earlier in management's discussion and analysis, as well as the REIT's annual information form.

InnVest disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, unless required to do so by applicable securities laws.



## Consolidated balance sheets

(in thousands of dollars)

	<b>September 30, 2007</b>	December 31, 2006
	(Unaudited)	(Restated, Note 2)
<b>Assets</b>		
<b>Current Assets</b>		
Cash	\$ 23,423	\$ 4,531
Accounts receivable	35,079	13,661
Prepaid expenses and other assets	16,005	5,627
Assets held for sale (Note 19)	–	42
	<b>74,507</b>	23,861
Restricted cash	5,023	4,693
Hotel properties (Note 3 and Note 4)	1,936,945	1,136,830
Other real estate properties (Note 5)	16,651	16,933
Licence contracts (accumulated amortization \$6,822; December 31, 2006 – \$5,835)	19,498	20,485
Other assets (Note 6)	41,210	19,721
Assets held for sale (Note 19)	–	5,566
	<b>\$ 2,093,834</b>	\$ 1,228,089
<b>Liabilities</b>		
<b>Current Liabilities</b>		
Bank indebtedness (Note 7)	\$ 215,000	\$ 3,300
Accounts payable and accrued liabilities	75,427	40,977
Acquisition related liabilities	21,172	957
Distributions payable	5,726	5,161
Current portion of long-term debt (Note 8)	12,796	11,434
Liabilities related to assets held for sale (Note 19)	–	139
	<b>330,121</b>	61,968
Long-term debt (Note 8)	716,021	490,998
Other long-term obligations (Note 9)	6,672	4,480
Convertible debentures (Note 10)	176,830	126,339
Future income tax liability (Note 11)	259,425	124,759
Long-term debt related to assets held for sale (Note 19)	–	2,191
	<b>1,489,069</b>	810,735
Unitholders' equity	604,765	417,354
	<b>\$ 2,093,834</b>	\$ 1,228,089

The accompanying notes are an integral part of these consolidated financial statements.

## Consolidated statements of net income and comprehensive income

(in thousands of dollars, except per unit amounts) (Unaudited)	Three Months Ended Sept. 30, 2007	Three Months Ended Sept. 30, 2006  (Restated) (Note 19)	Nine Months Ended Sept. 30, 2007	Nine Months Ended Sept. 30, 2006  (Restated) (Note 19)
Total revenues (reference only) (Note 17)	\$ 141,426	\$ 119,963	\$ 347,378	\$ 295,559
Hotel revenues	\$ 138,661	\$ 117,119	\$ 340,154	\$ 290,265
Hotel expenses				
Operating expenses (Note 15)	73,771	59,704	197,409	160,278
Property taxes, rent and insurance	10,163	8,747	29,222	26,124
Management fees (Note 15)	4,858	3,921	11,636	9,765
	88,792	72,372	238,267	196,167
Hotel operating income	49,869	44,747	101,887	94,098
Other (income) and expenses				
Interest on mortgages and other debt	9,467	7,619	27,021	22,116
Convertible debentures interest and accretion	2,916	2,147	7,529	7,181
Corporate and administrative (Note 15)	1,561	1,071	5,676	3,444
Capital tax	(10)	327	38	1,149
Other business income, net (Note 18)	(1,861)	(1,904)	(4,230)	(3,255)
Other income	(1,426)	(152)	(1,547)	(275)
Depreciation and amortization	14,086	13,659	41,942	37,950
	24,733	22,767	76,429	68,310
Income before income tax expense (recovery)	25,136	21,980	25,458	25,788
Income tax expense (recovery) (Note 11)				
Current	(5)	(59)	(5)	(186)
Future	(5,068)	(1,265)	2,022	(14,171)
	(5,073)	(1,324)	2,017	(14,357)
Net income from continuing operations	30,209	23,304	23,441	40,145
Income (loss) from discontinued operations (Note 19)	-	232	(24)	196
Gain on sale (writedown) of assets held for sale (Note 19)	-	-	833	(1,000)
	-	232	809	(804)
Net income and comprehensive income	\$ 30,209	\$ 23,536	\$ 24,250	\$ 39,341
Net income from continuing operations, per unit (Note 13)				
Basic	\$ 0.454	\$ 0.425	\$ 0.395	\$ 0.775
Diluted	\$ 0.423	\$ 0.395	\$ 0.395	\$ 0.763
Net income and comprehensive income, per unit (Note 13)				
Basic	\$ 0.454	\$ 0.429	\$ 0.409	\$ 0.760
Diluted	\$ 0.423	\$ 0.398	\$ 0.408	\$ 0.750
Net income (loss) from discontinued operations, per unit				
Basic	\$ -	\$ 0.004	\$ 0.014	\$ (0.015)
Diluted	\$ -	\$ 0.003	\$ 0.013	\$ (0.013)

The accompanying notes are an integral part of these consolidated financial statements.

## Consolidated statements of unitholders' equity

(in thousands of dollars) (Unaudited)	Accumulated Net Income (Loss) and Comprehensive Income (Loss)	Distributions	Deficit	Units in \$	Executive and Trustee Compensation	Holders' Conversion Option	Total
Balance December 31, 2005	\$ 57,033	\$(169,328)	\$(112,295)	\$ 464,164	\$ 186	\$ 5,588	\$ 357,643
Changes during the period							
Net income and							
comprehensive income	39,341	-	39,341	-	-	-	39,341
Unit distributions (Note 14)	-	(44,150)	(44,150)	-	-	-	(44,150)
Distribution reinvestment							
plan units issued	-	-	-	2,742	-	-	2,742
Conversion of							
debentures (Note 10)	-	-	-	68,988	-	(2,556)	66,432
Redemption of							
debentures (Note 10)	-	-	-	4,719	-	(172)	4,547
Issue of new debentures (Note 10)	-	-	-	-	-	3,400	3,400
Vested executive compensation	-	-	-	152	(152)	-	-
Executive and trustee compensation	-	-	-	81	183	-	264
Balance September 30, 2006	\$ 96,374	\$(213,478)	\$(117,104)	\$ 540,846	\$ 217	\$ 6,260	\$ 430,219
<b>Balance December 31, 2006</b>	<b>\$ 95,629</b>	<b>\$(228,778)</b>	<b>\$(133,149)</b>	<b>\$ 543,363</b>	<b>\$ 278</b>	<b>\$ 6,208</b>	<b>\$ 416,700</b>
<b>Change in accounting policy for</b>							
<b>financial instruments (Note 2)</b>	<b>654</b>	<b>-</b>	<b>654</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>654</b>
<b>Restated balance</b>							
<b>December 31, 2006</b>	<b>\$ 96,283</b>	<b>\$(228,778)</b>	<b>\$(132,495)</b>	<b>\$ 543,363</b>	<b>\$ 278</b>	<b>\$ 6,208</b>	<b>\$ 417,354</b>
Changes during the period							
<b>Net income and</b>							
<b>comprehensive income</b>	<b>24,250</b>	<b>-</b>	<b>24,250</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>24,250</b>
<b>Unit distributions (Note 14)</b>	<b>-</b>	<b>(49,186)</b>	<b>(49,186)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>(49,186)</b>
<b>Distribution reinvestment</b>							
<b>plan units issued</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>6,659</b>	<b>-</b>	<b>-</b>	<b>6,659</b>
<b>Conversion of</b>							
<b>debentures (Note 10)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>10,605</b>	<b>-</b>	<b>(519)</b>	<b>10,086</b>
<b>Issue of new</b>							
<b>debentures (Note 10)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>2,953</b>	<b>2,953</b>
<b>Issue of new units</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>192,268</b>	<b>-</b>	<b>-</b>	<b>192,268</b>
<b>Vested executive compensation</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>275</b>	<b>(275)</b>	<b>-</b>	<b>-</b>
<b>Executive and</b>							
<b>trustee compensation</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>87</b>	<b>294</b>	<b>-</b>	<b>381</b>
<b>Balance September 30, 2007</b>	<b>\$ 120,533</b>	<b>\$(277,964)</b>	<b>\$(157,431)</b>	<b>\$ 753,257</b>	<b>\$ 297</b>	<b>\$ 8,642</b>	<b>\$ 604,765</b>

The accompanying notes are an integral part of these consolidated financial statements.

## Consolidated statements of cash flows

(in thousands of dollars, except per unit amounts) (Unaudited)	Three Months Ended Sept. 30, 2007	Three Months Ended Sept. 30, 2006	Nine Months Ended Sept. 30, 2007	Nine Months Ended Sept. 30, 2006
<b>Operating activities</b>				
Net income from continuing operations	\$ 30,209	\$ 23,304	\$ 23,441	\$ 40,145
Add (deduct) items not affecting operations				
Depreciation, amortization and accretion	14,086	13,659	41,942	37,950
Non-cash portion of interest expense	540	–	2,017	–
Future income tax expense (recovery)	(5,068)	(1,265)	2,022	(14,171)
Non-cash executive and trustee compensation	181	89	381	264
Convertible debentures accretion	214	211	616	594
Discontinued operations	(2)	306	(109)	408
Changes in non-cash working capital	2,067	156	2,682	(1,107)
	<b>42,227</b>	<b>36,460</b>	<b>67,628</b>	<b>64,083</b>
<b>Financing activities</b>				
Repayment of long-term debt	(1,502)	(2,184)	(7,498)	(6,476)
Proceeds from long-term debt	15,400	49,800	41,324	63,300
Issue of convertible debentures	70,000	–	70,000	75,000
Issue of new units (net)	191,748	–	191,748	–
Unit distributions	(15,636)	(14,459)	(41,962)	(40,765)
Increase (decrease) in bank indebtedness	215,000	–	211,700	(7,100)
Discontinued operations repayment of debt	–	(11)	(2,191)	(32)
Debt issue costs	(3,315)	(568)	(4,626)	(3,983)
Changes in non-cash working capital related to financing activities	500	16	335	381
	<b>472,195</b>	<b>32,594</b>	<b>458,830</b>	<b>80,325</b>
<b>Investing activities</b>				
Capital expenditures on hotel properties	(6,760)	(8,021)	(20,267)	(19,346)
Discontinued operations capital expenditures	–	–	–	(26)
Hotel under development expenditures	(4,073)	–	(6,945)	–
Sale of discontinued assets, net of costs (Note 19)	–	–	6,400	–
Other assets	1,361	(84)	(634)	(260)
Acquisition of hotel properties and other real estate properties	(505,673)	(65,035)	(505,673)	(127,845)
Changes in restricted cash	(4,456)	(5,725)	(330)	(2,516)
Collection of vendor-take-back mortgage	–	–	–	200
Changes in non-cash working capital related to investing activities	20,474	(660)	19,883	2,126
	<b>(499,127)</b>	<b>(79,525)</b>	<b>(507,566)</b>	<b>(147,667)</b>
Increase (decrease) in cash during the period	15,295	(10,471)	18,892	(3,259)
Cash, beginning of period	8,128	13,105	4,531	5,893
Cash, end of period	\$ 23,423	\$ 2,634	\$ 23,423	\$ 2,634
<b>Supplemental disclosure of cash flow information:</b>				
Cash paid for interest	\$ 9,430	\$ 7,655	\$ 30,717	\$ 26,410
Cash paid for income taxes (including capital tax)	\$ 41	\$ 318	\$ 180	\$ 828

The accompanying notes are an integral part of these consolidated financial statements.

## Notes to consolidated financial statements

September 30, 2007 (all dollar amounts are in thousands, except unit and per unit amounts) (Unaudited)

### Note 1. Basis of Presentation

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InnVest Real Estate Investment Trust (“InnVest” or the “REIT”) is an unincorporated open-ended real estate investment trust governed by the laws of Ontario. The REIT began operations on July 26, 2002. The units of the REIT are traded on the Toronto Stock Exchange (“TSX”) under the symbol of “INN.UN”. As at September 30, 2007, the REIT owned 148 Canadian hotels with 19,381 guest rooms operated under international brands and has a 50% interest in Choice Hotels Canada Inc. (“CHC”).

The accompanying unaudited interim consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles (“GAAP”). The accounting principles used in these financial statements are consistent with those used in the annual consolidated financial statements for the year ended December 31, 2006, except as disclosed in Note 2. These financial statements do not include all the information and disclosure required by GAAP for annual financial statements, and should be read in conjunction with the annual consolidated financial statements.

Revenues earned from hotel operations fluctuate throughout the year, with the third quarter being the highest due to the increased level of leisure travel in the summer months, and the first quarter being the lowest as leisure travel tends to be lower at that time of the year.

### Note 2. Changes in Accounting Policies

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The accounting policies followed in preparation of these financial statements are consistent with those as set out in the audited financial statements for the year ended December 31, 2006, except as follows:

#### Principles of consolidation

The consolidated financial statements include the accounts of the REIT and its subsidiaries and the proportionate share of the assets, liabilities, revenues and expenses of joint ventures, including the REIT’s 50% interest in CHC and the REIT’s 26% interest in Legacy Hotels Real Estate Investment Trust, described in note 3.

#### Comprehensive Income

Effective January 1, 2007, the REIT adopted the new Canadian Institute of Chartered Accountants (“CICA”) recommendations under Section 1530 – Comprehensive Income, wherein comprehensive income includes net earnings and other comprehensive income (“OCI”), which represents changes in the unitholders’ equity during a period arising from transactions and other events with non-owner sources. The standard requires prospective application and; accordingly, comparative amounts for prior periods have not been restated. For the period ended September 30, 2007, there is no difference between the REIT’s Consolidated Statement of Net Income and its Statement of Comprehensive Income.

#### Inventory

Inventory, comprised of operating supplies including food and beverage, is valued at the lower of cost, determined on a first-in, first-out basis, and replacement cost. Inventory is included in the ‘Prepaid expenses and other assets’ in the current asset section of the balance sheet.

#### Financial Instruments – Recognition and Measurement

Effective January 1, 2007, the REIT adopted several new CICA recommendations related to accounting for Financial Instruments, including Section 3855 – Financial Instruments, Recognition and Measurement. All financial instruments are required to be measured at fair value on initial recognition, except for certain related party transactions. Measurement in subsequent periods depends on whether the financial instrument has been classified as held-for-trading, available-for-sale, held-to-maturity, loans and receivables, or other liabilities. This standard requires a prospective application and, accordingly, comparative amounts for prior periods have not been restated.

## Notes to consolidated financial statements

As a result of implementing Section 3855, the REIT has recorded the interest expense for both the mortgage debt and convertible debentures using the effective interest method (“EIM”). Transaction costs that are directly attributable to the issue of financial instruments classified as other than “held-for-trading” are included in the initial carrying value of such instruments and amortized using the EIM; therefore, the deferred financing costs which were related to these instruments were reclassified to the appropriate debt on the balance sheet. The amortization of these costs is included in interest expense in the financial statements in a manner that yields a constant rate of interest over the life of the respective financial instrument, for the three and nine months ended September 30, 2007. An adjustment has been made to the opening cumulative net income in the amount of \$654 to reflect the application of the EIM.

In accordance with Section 3855, the REIT conducted a search for embedded derivatives in all contractual arrangements dated subsequent to October 31, 2002 and identified certain embedded features that required separate presentation; however, all embedded features were determined to have a negligible fair value.

With the introduction of the new standards relating to financial instruments, Section 3251 – Equity was applied effective January 1, 2007. Section 3251 establishes standards for the presentation of equity and changes in equity during the reporting period. Equity is presented as accumulated net income and other comprehensive income, distributions and total deficit.

### Note 3. Asset Acquisitions

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During the first quarter of 2007, the REIT entered into a contract to purchase three hotels with a total of 349 rooms for a combined purchase price of \$48,300 plus transaction costs. The transaction to acquire these new build hotel properties will close in stages as the construction of each hotel is completed. The hotels include a 117 room Staybridge Suites located in London, Ontario, a 116 room Holiday Inn Express located in North Bay, Ontario and a 116 room Staybridge Suites located in Guelph, Ontario. On July 20 and September 13, 2007, the REIT completed the purchases of the Staybridge Suites London and the Holiday Inn Express North Bay (“New-build Acquisitions”) respectively. These transactions were funded through cash on hand. The Staybridge Suites Guelph is scheduled to open in the first quarter of 2008.

On July 12, 2007, InnVest, in partnership with Cadbridge Investors LP (“Cadbridge”), a joint venture entity between affiliates of Cadim, a division of the Caisse de Dépôt et Placement du Québec and an affiliate of InnVest’s hotel manager, announced a take-over bid for all of the outstanding units of Legacy Hotels Real Estate Investment Trust (“Legacy”) at a price of \$12.60 per unit. The take-over bid was effected by LGY Acquisition LP (“LGY”), a newly-formed limited partnership, owned by InnVest (through a wholly-owned limited partnership) and Cadbridge in which InnVest has an approximate 26% interest with joint control over LGY. On September 18, 2007, the take-over of the acquisition of 100% of Legacy’s outstanding units was successfully completed. InnVest and Cadbridge will reorganize Legacy’s assets such that InnVest will become the owner of the following eleven first class hotels: The Fairmont Palliser, Sheraton Suites Calgary Eau Claire, Delta Calgary Airport, Fairmont Hotel Macdonald, Delta Winnipeg Hotel, Delta Ottawa Hotel and Suites, Delta Centre-Ville, Delta Beauséjour, Delta Prince Edward, Delta Barrington and the Delta Halifax (collectively, the “Legacy Portfolio”). This reorganization was completed on October 31, 2007, except for the Delta Calgary Airport which is expected to be completed by December 31, 2007. With the completion of the reorganization, InnVest will no longer have an interest in, or exercise joint control over, LGY.

	New-build Acquisitions	Legacy Portfolio	Total
Cash	\$ –	\$ 8,146	\$ 8,146
Current assets	–	21,147	21,147
Hotel properties	32,180	779,115	811,295
Other assets	357	31,330	31,687
	32,537	839,738	872,275
Assumption of existing long-term debt	–	(196,674)	(196,674)
Future income tax liability	–	(133,164)	(133,164)
Current liabilities	–	(26,125)	(26,125)
Long-term liabilities	–	(2,493)	(2,493)
	\$ 32,537	\$ 481,282	\$ 513,819
The consideration paid consists of the following:			
Cash	\$ 32,537	\$ –	\$ 32,537
Bank indebtedness	–	215,000	215,000
Units issued	–	191,748	191,748
Debentures issued	–	66,685	66,685
Acquisition payables	–	7,849	7,849
	\$ 32,537	\$ 481,282	\$ 513,819

As at September 30, 2007, the REIT is continuing to evaluate the fair value of the net assets acquired, and based on this ongoing evaluation, the purchase price allocation may be adjusted in future periods.

#### Note 4. Hotel Properties

	Cost	Accumulated Depreciation	Sept. 30, 2007 Net Book Value	December 31, 2006 Net Book Value
Land	\$ 176,031	\$ –	\$ 176,031	\$ 94,623
Buildings	1,794,904	123,852	1,671,052	987,515
Furniture, fixtures and equipment	109,639	27,063	82,576	54,350
	2,080,574	150,915	1,929,659	1,136,488
Hotel under development	7,286	–	7,286	342
	\$ 2,087,860	\$ 150,915	\$ 1,936,945	\$ 1,136,830

#### Note 5. Other Real Estate Properties

	Cost	Accumulated Depreciation	Sept. 30, 2007 Net Book Value	December 31, 2006 Net Book Value
Land	\$ 1,675	\$ –	\$ 1,675	\$ 1,675
Buildings	15,455	522	14,933	15,220
Furniture, fixtures and equipment	59	16	43	38
	\$ 17,189	\$ 538	\$ 16,651	\$ 16,933

Other real estate includes office and retail properties and a retirement residence which were acquired during the year ended December 31, 2006.

## Notes to consolidated financial statements

### Note 6. Other Assets

	Cost	Accumulated Amortization	Sept. 30, 2007 Net Book Value	December 31, 2006 Net Book Value
Deferred financing (Note 2)	\$ –	\$ –	\$ –	\$ 8,592
Other assets	45,722	4,512	41,210	11,129
	<b>\$ 45,722</b>	<b>\$ 4,512</b>	<b>\$ 41,210</b>	<b>\$ 19,721</b>

In accordance with the new CICA recommendations related to accounting for Financial Instruments, including Section 3855 – Financial Instruments and Measurement, the unamortized balance of deferred financing costs was reallocated as a reduction to long-term debt effective January 1, 2007.

Other assets include franchise fee costs, customer and tenant relationships, lease origination costs, above and below market leases and franchise rights recognized upon acquisition of new hotel properties and other real estate properties.

### Note 7. Bank Indebtedness

The REIT has a \$25,000 operating loan facility that bears interest at Canadian bank prime plus 0.5% or Canadian Bankers' Acceptance rate plus 1.5%. It is secured by nine properties and is payable on demand. At September 30, 2007, the REIT had drawn \$ nil on this facility (December 31, 2006 – \$3,300).

The REIT entered into a \$215,000 bridge loan facility as part of the financing for the acquisition of the Legacy Portfolio. It is secured by five properties, is due June 13, 2008 and bears interest at Canadian Bankers' Acceptance rate plus 2.75%.

InnVest intends to refinance the existing mortgages on the Legacy Portfolio and arrange new mortgage financing on five of the acquired assets that are currently unencumbered. The bridge loan will be repaid from the proceeds of these financings.

### Note 8. Long-term Debt

	September 30, 2007	December 31, 2006
Mortgages payable	\$ 732,907	\$ 502,432
Less debt issuance costs, net	(4,090)	–
Total long-term debt	728,817	502,432
Less current portion	(12,796)	(11,434)
Net long-term debt	<b>\$ 716,021</b>	<b>\$ 490,998</b>

Substantially all of the REIT's assets have been pledged as security under various debt agreements. At September 30, 2007, long-term debt had a weighted average interest rate of 6.4% (December 31, 2006 – 6.5%) and a weighted average effective interest rate of 6.6%. The long-term debt is repayable in average monthly payments of principal and interest totalling \$4,902 (December 31, 2006 – \$3,495) per month, and matures at various dates from June 1, 2009 to September 11, 2017.

Scheduled repayment of long-term debt is as follows:

2007 (remainder of the year)	\$ 3,510
2008	12,710
2009	54,946
2010	227,402
2011	56,616
2012 and thereafter	377,723
	<b>\$ 732,907</b>



The current portion of long-term debt on the balance sheet is based on the year ending September 30, 2008, whereas the repayment schedule above reflects the fiscal year.

The estimated fair value of the REIT's long-term debt at September 30, 2007 was approximately \$729,294 (December 31, 2006 – \$507,243). This estimate was determined by discounting expected cash flows at the interest rates currently being offered to the REIT for debt of the same remaining maturities.

Long-term debt includes \$94,074 (December 31, 2006 – \$68,305) of mortgages payable which are subject to floating interest rates. Interest expense will increase by \$941 for every 1% increase in the base Bankers' Acceptance rate.

In the second quarter, the REIT completed an early extension of \$147,665 of mortgage debt that was to have matured on July 26, 2008, fixing the interest rate on \$130,000 at 5.8% for a blended interest rate of 6.1% per annum for a period of seven years, and maintained floating rate debt of \$17,665 which, at current rates, bears interest at approximately 6.7% per annum. As part of this early extension, the REIT increased its fixed-rate proceeds by \$25,924 which was used to repay the operating loan balance and to fund potential acquisitions.

During the quarter, the REIT raised new debt on the Staybridge Suites London of \$8,300 at an interest rate of 6.4% for a ten year term and \$7,100 of new debt on the Holiday Inn Express North Bay at an interest rate of 6.0% for a ten year term.

## Note 9. Other Long-term Obligations

	September 30, 2007	December 31, 2006
Capital lease	\$ 1,861	\$ 1,861
Other lease obligations	342	299
	<b>2,203</b>	2,160
Less current portion (included in accounts payable and accrued liabilities)	<b>(230)</b>	(207)
Total long-term obligations	<b>1,973</b>	1,953
Pension liability	<b>2,935</b>	1,212
Asset retirement obligation	<b>1,764</b>	1,315
Total other long-term obligations	<b>\$ 6,672</b>	\$ 4,480

### Defined Benefit Pension Plan

Defined benefit pension plans were assumed pursuant to the acquisition of certain hotels in 2006 and the Legacy Portfolio in the third quarter 2007. The most recent actuarial valuation with respect to the funding of the REIT's pension plans was prepared on September 30, 2007. The pension plan assets and liabilities as at September 30, 2007 consist of the following:

	Management Pension Benefit Plans	Non-Union Non-Management Pension Benefit Plans	Sept. 30, 2007 Total Benefit Plans	December 31, 2006 Total Benefit Plans
Accrued benefit obligation	\$ 5,631	\$ 1,681	\$ 7,312	\$ 3,873
Fair value of plan assets	3,001	1,376	4,377	2,661
Funded status – plan deficit	2,630	305	2,935	1,212
Unamortized net actuarial gain	163	172	335	167
Accrued employee future benefit liability	\$ 2,793	\$ 477	\$ 3,270	\$ 1,379

## Note 10. Convertible Debentures

The details of the two series of convertible debentures are outlined in the tables below:

Debenture	Maturity Date	Interest Rate	Effective Interest Rate	Original Face Amount	Converted to Trust Units	Face Amount Outstanding	Holders' Conversion Option	Accretion	Deferred Financing	Sept. 30, 2007
Series A	April 15, 2011	6.25%	7.73%	\$ 57,500	\$ (11,736)	\$ 45,764	\$ (2,289)	\$ 1,074	\$ (1,483)	\$ 43,066
Series B	May 31, 2013	6.00%	7.53%	75,000	–	75,000	(3,400)	651	(2,549)	69,702
Series C	August 1, 2014	5.85%	7.42%	70,000	–	70,000	(2,953)	68	(3,053)	64,062
				\$ 202,500	\$ (11,736)	\$ 190,764	\$ (8,642)	\$ 1,793	\$ (7,085)	\$ 176,830

Debenture	Maturity Date	Interest Rate	Original Face Amount	Converted to Trust Units	Face Amount Outstanding	Holders' Conversion Option	Accretion	December 31, 2006
Series A	April 15, 2011	6.25%	\$ 57,500	\$ (1,351)	\$ 56,149	\$ (2,808)	\$ 1,096	\$ 54,437
Series B	May 31, 2013	6.00%	75,000	–	75,000	(3,400)	302	71,902
			\$ 132,500	\$ (1,351)	\$ 131,149	\$ (6,208)	\$ 1,398	\$ 126,339

### Series C Debentures

On August 3, 2007, the REIT announced the closing on a bought deal basis of \$70,000, 5.85% convertible unsecured subordinated debentures ("Series C – 5.85% Debentures"). These debentures are convertible into trust units at a strike price of \$14.70, bear interest at 5.85% per annum payable semi-annually on February 1 and August 1 of each year and will mature August 1, 2014. The trust units to be issued upon conversion of the Series C – 5.85% Debentures are 4,761,905. Each \$1 principal amount is convertible at the option of the holder into 68 units. The Series C – 5.85% Debentures are not redeemable prior to August 1, 2010. On or after August 1, 2010 and prior to August 1, 2012, the Series C – 5.85% Debentures may be redeemed by the REIT, in whole or in part, on not more than 60 days and on not less than 30 days prior notice, at a redemption price equal to the principal amount thereof plus accrued and unpaid interest, provided that the volume-weighted average trading price of the units on the TSX for the 20 consecutive trading days ending on the fifth trading day preceding the date on which the notice of the redemption exceeds 125% of the conversion price. On or after August 1, 2012 and prior to August 1, 2014, the Series C – 5.85% Debentures may be redeemed by the REIT at any time at a redemption price equal to the principal amount thereof plus accrued and unpaid interest.

The holder conversion option was valued separately from the convertible debentures at \$2,953. The holder conversion option is being accreted over the term of the Series C – 5.85% Debentures. There were no conversions of Series C debentures during the year.

## Note 11. Income Taxes and Future Income Tax Liability

Future income taxes are the result of temporary differences between tax bases of assets and liabilities and their carrying amounts for accounting purposes. Such temporary differences are then measured using substantively enacted tax rates that will be in effect when these differences are expected to reverse.

InnVest currently qualifies as a Mutual Fund Trust for income tax purposes. As required by its Declaration of Trust, InnVest intends to distribute all taxable income to its unitholders and to deduct these distributions for income tax purposes.

In June 2007, a Bill was enacted for the taxation of publicly traded trusts, including income trusts (the “Bill”). The Bill applies to publicly traded trusts which existed prior to November 1, 2006 starting with taxation years ending in 2011, except for those trusts that qualify for the real estate investment trust (“Qualifying REIT”) exception included in the legislation. An existing trust may lose its relief from taxation in the interim periods to 2011 where it undergoes “undue expansion”. Pursuant to the legislation, a REIT which carries on Canadian hotel operations (including through subsidiaries) will not be a Qualifying REIT. As a result, InnVest will be subject to tax starting January 1, 2011.

For the nine months ended September 30, 2007, InnVest’s future income tax liability has increased by \$134,666 which is explained as follows:

Effects of the reorganization in the first quarter	\$ (115,431)
Effects of the enactment of the Bill in the second quarter	122,626
Effects of on-going operations and capital expenditures	(5,173)
Future income tax expense for the nine months ended September 30, 2007	2,022
Tax benefit of unit issuance costs recorded in unitholders’ equity	(520)
Effects of the Legacy transaction	133,164
	\$ 134,666

The Bill may adversely affect the level of cash distribution to unitholders commencing in 2011 if InnVest does not become a Qualifying REIT by then. Management is reviewing whether it is feasible to reorganize InnVest so that non-qualifying operations and assets are transferred under a plan of arrangement to a taxable entity that is held by InnVest unitholders, and that the InnVest hotels, which continue to be owned by the REIT, are leased by it to the taxable entity. It is not possible at this preliminary juncture to provide any assurances that any such reorganization or a similar reorganization can or will be implemented before 2011, or that any such reorganization, if implemented, would not result in material costs or other adverse consequences to InnVest and its unitholders.

## Note 12. Unitholders’ Equity

The REIT is authorized to issue an unlimited number of units, each of which represents an equal undivided beneficial interest in any distributions from the REIT. All units are of the same class with equal rights and privileges.

	Units	Amount
Balance as at December 31, 2005	47,961,163	\$ 464,164
Units issued under distribution reinvestment plan	227,295	2,742
Units issued on conversion of debentures	6,250,412	68,988
Units issued on redemption of debentures	392,307	4,719
Units issued for vested executive compensation	12,218	152
Units issued under trustee compensation plan	6,107	81
Balance at September 30, 2006	54,849,502	\$ 540,846
<b>Balance at December 31, 2006</b>	<b>55,045,351</b>	<b>543,363</b>
<b>Units issued for acquisition of Legacy Portfolio</b>	<b>16,195,000</b>	<b>192,268</b>
<b>Units issued on conversion of debentures</b>	<b>830,800</b>	<b>10,605</b>
<b>Units issued under distribution reinvestment plan</b>	<b>512,426</b>	<b>6,659</b>
<b>Units issued for vested executive compensation</b>	<b>20,139</b>	<b>275</b>
<b>Units issued under trustee compensation plan</b>	<b>6,519</b>	<b>87</b>
<b>Balance at September 30, 2007</b>	<b>72,610,235</b>	<b>\$ 753,257</b>

## Notes to consolidated financial statements

### Trustee Compensation Plan

The members of the Board of Trustees receive 50% of their annual retainer in units (based on the then current market price of the units). The REIT has set aside 100,000 units in reserve for this purpose. The balance in this reserve account at September 30, 2007 is 54,559 units. Under the Trustee Compensation Plan, 6,519 units were issued during the nine months ended September 30, 2007 (September 30, 2006 – 6,107 units).

### Executive Compensation Plan

The senior executives participate in the executive compensation plan under which units are granted by the Board of Trustees from time to time. The REIT has reserved a maximum of 1,000,000 units for issuance under the plan. The balance in this reserve account at September 30, 2007 is 850,785 units. A unit granted through the plan entitles the holder to receive, on the vesting date, the then current fair market value of the unit plus the value of the cash distributions that would have been paid on the unit if it had been issued on the date of grant assuming the reinvestment of the distribution into REIT units. The payment will be satisfied through the issuance of units.

The following table summarizes the status of the executive compensation plan at September 30, 2007, excluding granted units which have fully vested:

	Unvested Executive units	Units Accumulated from Distributions	Total Units
January 1, 2004 – granted	10,218	3,800	14,018
January 1, 2005 – granted	13,118	3,658	16,776
January 1, 2006 – granted	12,968	2,149	15,117
January 1, 2007 – granted	15,000	996	15,996
January 1, 2007 – units vested	(5,109)	(1,675)	(6,784)
	46,195	8,928	55,123

On March 30, 2007, the Board of Trustees approved the granting of 15,000 units effective as of January 1, 2007. These units vest equally on the third and fourth anniversaries of the effective date of grant.

### Distribution Reinvestment Plan (“DRIP”)

The REIT has a DRIP whereby eligible Canadian unitholders may elect to have their distributions of income from the REIT automatically reinvested in additional units. Unitholders who so elect will receive a further bonus distribution of units equal in value to 3% of each distribution that was reinvested.

## Note 13. Per Unit Information

	Three Months Ended September 30, 2007			Three Months Ended September 30, 2006	
		Weighted Average Units		Weighted Average Units	
Net income from continuing operations – basic	\$ 30,209	66,566,306	\$ 23,304	54,811,022	
Convertible debentures interest and accretion	2,917	11,696,747	2,148	9,608,757	
Dilutive effect of executive compensation plan	–	54,489	–	55,033	
Net income from continuing operations – diluted	\$ 33,126	78,317,542	\$ 25,452	64,474,812	

	Nine Months Ended September 30, 2007			Nine Months Ended September 30, 2006	
		Weighted Average Units		Weighted Average Units	
Net income from continuing operations – basic	\$ 23,441	59,316,788	\$ 40,145	51,777,943	
Convertible debentures interest and accretion	–	–	4,848	7,105,464	
Dilutive effect of executive compensation plan	–	53,349	–	53,824	
Net income from continuing operations – diluted	\$ 23,441	59,370,137	\$ 44,993	58,937,231	

	Three Months Ended September 30, 2007			Three Months Ended September 30, 2006	
		Weighted Average Units		Weighted Average Units	
Net income and comprehensive income – basic	\$ 30,209	66,566,306	\$ 23,536	54,811,022	
Convertible debentures interest and accretion	2,917	11,696,747	2,148	9,608,757	
Dilutive effect of executive compensation plan	–	54,489	–	55,033	
Net income and comprehensive income – diluted	\$ 33,126	78,317,542	\$ 25,684	64,474,812	

	Nine Months Ended September 30, 2007			Nine Months Ended September 30, 2006	
		Weighted Average Units		Weighted Average Units	
Net income and comprehensive income – basic	\$ 24,250	59,316,788	\$ 39,341	51,777,943	
Convertible debentures interest and accretion	–	–	4,848	7,105,464	
Dilutive effect of executive compensation plan	–	53,349	–	53,824	
Net income and comprehensive income – diluted	\$ 24,250	59,370,137	\$ 44,189	58,937,231	

All of the convertible debentures have been included in the three months ended September 30, 2007 and the three and nine months ended September 30, 2006 per unit calculations above, but have been excluded in the nine month ended September 30, 2007 calculation because the impact of the conversions would not be dilutive. The dilutive effect of the executive compensation plan has been included in all of the calculations.

**Note 14. Distributions to Unitholders**

Distributions to unitholders are computed based on distributable income as defined by the Declaration of Trust.

Distributable income is a measure of cash flow that is not defined under Canadian GAAP and, accordingly, may not be comparable to similar measures used by other issuers. Distributable income per unit has been calculated on a basis consistent with that prescribed by Canadian GAAP for calculating earnings per unit.

Distributable income is defined as net income in accordance with Canadian GAAP, subject to certain adjustments as set out in the Declaration of Trust, including adding back depreciation and amortization, amortization of fair value debt adjustment and future income tax (recovery) expense, excluding any gains or losses on the disposition of real property and future income taxes, deducting the amount calculated, at 4% of hotel revenues, for the reserve for the replacement of furniture, fixtures and equipment and capital improvements, the accretion on convertible debentures that is included in the computation of net income, and making any other adjustments determined by the trustees of the REIT in their discretion. As outlined in the Declaration of Trust, the REIT is required to distribute monthly to unitholders not less than one-twelfth of eighty percent (80%) of distributable income of the REIT for the calendar year.

	<b>Three Months Ended Sept. 30, 2007</b>	Three Months Ended Sept. 30, 2006
Net income and comprehensive income	<b>\$ 30,209</b>	\$ 23,536
Add (deduct)		
Depreciation, amortization and accretion	<b>14,086</b>	13,682
Non-cash portion of interest expense	<b>540</b>	–
Future income tax recovery	<b>(5,068)</b>	(1,265)
Reserve for replacement of furniture, fixtures and equipment and capital improvements	<b>(5,551)</b>	(4,746)
Corporate reorganization costs	<b>43</b>	–
Convertible debentures accretion	<b>214</b>	211
Non-cash executive and trustee compensation	<b>158</b>	86
Deferred land lease expense and retail lease income, net	<b>8</b>	34
	<b>4,430</b>	8,002
Distributable income	<b>34,639</b>	31,538
Distributions		
Required under the Declaration of Trust	<b>27,711</b>	25,230
Timing adjustment	<b>(9,898)</b>	(9,813)
Distributions paid	<b>17,813</b>	15,417
Distributions less than distributable income	<b>\$ (16,826)</b>	\$ (16,121)

	Nine Months Ended Sept. 30, 2007	Nine Months Ended Sept. 30, 2006
Net income and comprehensive income	\$ 24,250	\$ 39,341
Add (deduct)		
Depreciation, amortization and accretion	41,942	38,139
Non-cash portion of interest expense	2,017	–
Future income tax expense (recovery)	2,022	(14,171)
Reserve for replacement of furniture, fixtures and equipment and capital improvements	(13,630)	(11,688)
Convertible debentures accretion	616	595
Corporate reorganization costs	1,514	–
Non-cash executive and trustee compensation	386	261
Deferred land lease expense and retail lease income, net	25	84
(Gain on sale) writedown of assets held for sale	(833)	1,000
	<b>34,059</b>	14,220
Distributable income	<b>58,309</b>	53,561
Distributions		
Required under the Declaration of Trust	46,647	42,849
Discretionary	2,539	1,301
Distributions paid	<b>49,186</b>	44,150
Distributions less than distributable income	<b>\$ (9,123)</b>	\$ (9,411)

## Note 15. Management Agreements

### Westmont Hospitality Canada Limited

On July 26, 2002, the REIT entered into a Management Agreement for hotel management and accounting services and an Administrative Services Agreement (the “Agreements”) with Westmont Hospitality Canada Limited (“Westmont”). Westmont manages all but four of the REIT’s hotels.

The Agreements have an initial term of 10 years with two successive five-year renewal terms, subject to the consent of Westmont and approval of the REIT. The Agreements will expire July 25, 2012. The Agreements provide for the payment of an annual management fee to Westmont in an amount equal to 3.375% of gross revenues during the term of the Agreements, including renewal periods. In addition, Westmont may receive an annual incentive fee if the REIT achieves distributable income (Note 14) in excess of \$1.25 per unit. No management incentive fees were paid during the periods presented. Accounting fees are calculated based on a fixed charge per room which increases by the Consumer Price Index change annually.

In addition to the base management fee and incentive fee, Westmont is entitled to reasonable fees based on a percentage of the cost of purchasing certain goods and supplies and certain construction costs and capital expenditures, fees for accounting services, reasonable out-of-pocket costs and expenses (other than general and administrative expenses or overhead costs except as otherwise provided in the Administrative Services Agreement) and project management and general contractor service fees related to hotel renovations managed by Westmont.

## Notes to consolidated financial statements

During the three and nine months ended September 30, 2007 and 2006, the fees charged to the REIT pursuant to the Agreements were as follows:

	<b>Three Months Ended Sept. 30, 2007</b>	Three Months Ended Sept. 30, 2006
Fees from continuing operations:		
Management fees	\$ 3,795	\$ 3,754
Asset management fees (included in hotel operating expenses)	78	–
Accounting services (included in hotel operating expenses)	579	575
Administrative services (included in corporate and administrative expenses)	113	144
Project management and general contractor services (capitalized to hotel properties)	143	125
Fees from discontinued operations	–	35
	<b>\$ 4,708</b>	<b>\$ 4,633</b>

	<b>Nine Months Ended Sept. 30, 2007</b>	Nine Months Ended Sept. 30, 2006
Fees from continuing operations:		
Management fees	\$ 9,733	\$ 9,570
Asset management fees (included in hotel operating expenses)	235	–
Accounting services (included in hotel operating expenses)	1,724	1,708
Administrative services (included in corporate and administrative expenses)	325	419
Project management and general contractor services (capitalized to hotel properties)	539	419
Fees from discontinued operations	107	87
	<b>\$ 12,663</b>	<b>\$ 12,203</b>

In addition, salaries of REIT employees paid by Westmont and reimbursed by the REIT were \$159 (September 30, 2006 – \$157). Included in accounts payable and accrued liabilities are amounts outstanding at September 30, 2007 totalling \$1,510 (December 31, 2006 – \$1,479).

The REIT paid Westmont an Acquisition Fee of \$6,518 as part of the acquisition of the Legacy Portfolio.

### Other Management Agreements

The REIT entered into management agreements with Hilton Canada Co. (“Hilton”) to manage the two Hilton hotels acquired in 2006. The agreements provide for the payment of an annual management fee to Hilton in an amount equal to 2% of gross revenues during the term of the agreements. The agreements mature on December 31, 2026. For the nine-month period ended September 30, 2007, total management fees paid to Hilton were \$595 (September 30, 2006 - \$38).

The REIT assumed the hotel management agreements with Delta Hotels Limited (“Delta”), dated January 1, 2003 when two Delta hotels were purchased in 2006. The agreements provide for the payment of an annual management fee to Delta in an amount equal to 3% of total revenues from the hotel, plus 0.5% of total revenues from the hotel if the hotel’s annual gross operating profit is greater than the budgeted gross operating profit. The agreements mature on December 31, 2015, with two ten-year extension options. For the nine-month period ended September 30, 2007, total management fees paid to Delta were \$475 (September 30, 2006 - \$157).

With the acquisition of the Legacy Portfolio, InnVest assumed the existing hotel management agreements with Fairmont Hotel and Resorts (“Fairmont”) or Delta for each of the Legacy Portfolio hotels. The agreements provide for the payment of an annual management fee to Fairmont or Delta in an amount equal to 3% of total revenues from the hotel for nine of the hotels and 2% of total revenues for the remaining two hotels. The agreements mature from December 31, 2010 to December 31, 2047. For the 13 day period from September 18, 2007 to September 30, 2007, total management fees paid for the Legacy Portfolio were \$598.



## Note 16. Segmented Financial Information

The REIT operates hotel properties throughout Canada. Information related to these properties by geographic segment is presented below. The REIT primarily evaluates operating performance based on hotel operating income. All key financing, investing and capital allocation decisions are centrally managed.

	Western	Ontario	Québec	Atlantic	Total
<b>Three months ended</b>					
<b>September 30, 2007</b>					
<b>Hotel revenues</b>	\$ 18,086	\$ 67,638	\$ 34,358	\$ 18,579	\$ 138,661
<b>Hotel expenses</b>	10,703	45,465	22,124	10,500	88,792
<b>Hotel operating income</b>	\$ 7,383	\$ 22,173	\$ 12,234	\$ 8,079	\$ 49,869
Three months ended					
September 30, 2006					
Hotel revenues	\$ 12,140	\$ 67,539	\$ 24,247	\$ 13,193	\$ 117,119
Hotel expenses	6,852	44,037	14,769	6,714	72,372
Hotel operating income	\$ 5,288	\$ 23,502	\$ 9,478	\$ 6,479	\$ 44,747
<b>Nine months ended</b>					
<b>September 30, 2007</b>					
<b>Hotel revenues</b>	\$ 37,945	\$ 178,697	\$ 84,672	\$ 38,840	\$ 340,154
<b>Hotel expenses</b>	23,814	128,276	61,044	25,133	238,267
<b>Hotel operating income</b>	\$ 14,131	\$ 50,421	\$ 23,628	\$ 13,707	\$ 101,887
Nine months ended					
September 30, 2006					
Hotel revenues	\$ 29,612	\$ 177,489	\$ 54,629	\$ 28,535	\$ 290,265
Hotel expenses	18,603	124,195	35,886	17,483	196,167
Hotel operating income	\$ 11,009	\$ 53,294	\$ 18,743	\$ 11,052	\$ 94,098
<b>Capital expenditures</b>					
<b>Three months ended</b>					
<b>September 30, 2007</b>					
	\$ 636	\$ 4,573	\$ 1,020	\$ 531	\$ 6,760
Three months ended					
September 30, 2006					
	\$ 373	\$ 6,400	\$ 688	\$ 560	\$ 8,021
<b>Capital expenditures</b>					
<b>Nine months ended</b>					
<b>September 30, 2007</b>					
	\$ 2,383	\$ 12,375	\$ 3,989	\$ 1,520	\$ 20,267
Nine months ended					
September 30, 2006					
	\$ 926	\$ 14,791	\$ 2,129	\$ 1,500	\$ 19,346
<b>Hotel properties</b>					
<b>September 30, 2007</b>	\$ 514,051	\$ 711,468	\$ 446,978	\$ 264,448	\$ 1,936,945
December 31, 2006	\$ 73,270	\$ 681,326	\$ 266,167	\$ 116,067	\$ 1,136,830

## Notes to consolidated financial statements

### Note 17. Total Revenues

	<b>Three Months Ended Sept. 30, 2007</b>	Three Months Ended Sept. 30, 2006	<b>Nine Months Ended Sept. 30, 2007</b>	Nine Months Ended Sept. 30, 2006
Hotel revenues	\$ 138,661	\$ 117,119	\$ 340,154	\$ 290,265
Other business revenues (Note 18)	2,765	2,844	7,224	5,294
	<b>\$ 141,426</b>	<b>\$ 119,963</b>	<b>\$ 347,378</b>	<b>\$ 295,559</b>

### Note 18. Other Business Income

	<b>Franchise Business</b>	<b>Retail/ Office</b>	<b>Retirement Residence</b>	<b>Three Months Ended Sept. 30, 2007</b>	Three Months Ended Sept. 30, 2006
Revenues	\$ 1,925	\$ 565	\$ 275	\$ 2,765	\$ 2,844
Expenses	602	138	164	904	940
Other business income, net	\$ 1,323	\$ 427	\$ 111	\$ 1,861	\$ 1,904

	<b>Franchise Business</b>	<b>Retail/ Office</b>	<b>Retirement Residence</b>	<b>Nine Months Ended Sept. 30, 2007</b>	Nine Months Ended Sept. 30, 2006
Revenues	\$ 4,363	\$ 2,049	\$ 812	\$ 7,224	\$ 5,294
Expenses	1,649	843	502	2,994	2,039
Other business income, net	\$ 2,714	\$ 1,206	\$ 310	\$ 4,230	\$ 3,255

Other business income includes Franchise Business Income, which is InnVest's 50% share of Choice Canada's operations and the income from the other real estate properties acquired with the Québec Deltas during the year ended December 31, 2006.

## Note 19. Assets Held for Sale and Discontinued Operations

On April 18, 2006, the REIT reclassified one Ontario hotel property to assets held for sale. At September 30, 2006, the REIT reclassified a second hotel property, in Atlantic Canada, to assets held for sale.

On March 30, 2007, the REIT sold the hotel held for sale in Atlantic Canada for \$2,350 less closing costs of \$250, and recorded a gain of \$659. On April 10, 2007, the Ontario hotel property held for sale was sold for \$4,650 less closing costs of \$350, and the REIT recorded a gain of \$174. The debt owing of \$1,010 and \$1,181, respectively, was paid out of the proceeds. The operations for these two hotels are included as discontinued operations as summarized below.

Discontinued operations for the three and six months ended September 30, 2007 and 2006 are as follows:

	<b>Three Months Ended Sept. 30, 2007</b>	Three Months Ended Sept. 30, 2006
Hotel revenues	\$ —	\$ 815
Hotel expenses		
Operating expenses	—	445
Property taxes, rent and insurance	—	47
Management fees	—	28
	—	520
Hotel operating income	—	295
Interest on mortgages	—	40
Depreciation and amortization	—	23
	—	63
(Loss) income from discontinued operations	—	232
Writedown of assets held for sale	—	—
Net income (loss) from discontinued operations	\$ —	\$ 232

  

	<b>Three Months Ended Sept. 30, 2007</b>	Three Months Ended Sept. 30, 2006
Hotel revenues	\$ 462	\$ 1,916
Hotel expenses		
Operating expenses	383	1,207
Property taxes, rent and insurance	49	146
Management fees	16	65
	448	1,418
Hotel operating income	14	498
Interest on mortgages	38	113
Depreciation and amortization	—	189
	38	302
Loss from discontinued operations	(24)	196
Gain on sale (writedown) of assets held for sale	833	(1,000)
Net income (loss) from discontinued operations	\$ 809	\$ (804)

## Note 20. Comparative Information

Certain prior period amounts have been reclassified to conform to the current period presentation.



## Corporate Office

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## Registrar and Transfer Agent

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Inquiries regarding change of address, registered holdings, transfers and duplicate mailings should be directed to the following:

Computershare Trust Company of Canada

100 University Avenue  
11<sup>th</sup> Floor  
Toronto, Ontario  
Phone: 1-800-564-6253  
Fax: 1-866-249-7775

## Stock Exchange Listing

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The Toronto Stock Exchange  
Trading Symbol: INN.UN