Introduction

InnVest Real Estate Investment Trust (the "REIT") is an unincorporated open-ended real estate investment trust which owns a portfolio of 144 hotels across Canada representing approximately 19,000 guest rooms operated under internationally recognized brands. The REIT leases its hotels to InnVest Operations Trust ("IOT"), an unincorporated open-ended taxable investment trust. IOT indirectly holds all of the hotel operating assets, earns revenues from hotel customers and pays rent to the REIT. IOT also indirectly holds a 50% interest in Choice Hotels Canada Inc., one of the largest franchisors of hotels in Canada, and earns revenues from franchising fees. The REIT and IOT are both governed by the laws of Ontario and a Declaration of Trust. The REIT and IOT are collectively referred to in this management's discussion and analysis ("MD&A") as "InnVest". This MD&A is dated November 9, 2011.

On December 31, 2010, InnVest completed an internal reorganization pursuant to a Plan of Arrangement as described in InnVest's information circular dated May 13, 2010. The reorganization resulted in each issued and outstanding unit of the REIT trading together with a non-voting unit of IOT as a "Stapled Unit" on the Toronto Stock Exchange under the symbol INN.UN. Refer to Corporate Developments for information on proposed changes to the tax treatment of REITs that have issued "stapled" securities.

The following MD&A is intended to assist readers in understanding InnVest, its history, business environment, strategies, performance and risk factors and includes a discussion of the results of operations and financial condition of InnVest for the three and nine months ended September 30, 2011, with a comparison to the results of operations of InnVest for the three and nine months ended September 30, 2010. The MD&A should be read in conjunction with the interim condensed consolidated financial statements of InnVest and the notes thereto as at, and for the three and nine months ended, September 30, 2011 and 2010. The condensed consolidated financial statements of InnVest include the financial statements of the REIT and IOT.

Effective January 1, 2011, International Financial Reporting Standards ("IFRS") replaced Canadian generally accepted accounting standards ("Canadian GAAP") and interpretations for publicly accountable enterprises. While the adoption of IFRS has not had an impact on InnVest's cash flows, there have been material impacts on its balance sheets and statements of net income (loss) and comprehensive income (loss). Refer to "Adoption of IFRS".

The accompanying interim financial statements of InnVest are prepared in accordance with International Accounting Standard ("IAS") 34 – *Interim Financial Reporting* and are presented in Canadian dollars. This MD&A should also be read in conjunction with InnVest's audited consolidated financial statements and accompanying notes for the year ended December 31, 2010 which were prepared in accordance with Canadian GAAP along with the related MD&A.

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.

Certain measures in this MD&A, such as hotel operating income ("HOI"), funds from operations ("FFO") and distributable income, do not have any standardized meaning as prescribed by IFRS, and therefore are considered non-IFRS measures. InnVest uses non-IFRS financial measures to assess its operating performance. Securities regulators require that entities caution readers that earnings and other measures adjusted to a basis other than IFRS do not have standardized meanings and are unlikely to be comparable to similar measures used by other companies. Please see "Non-IFRS Financial Measures" for a discussion of certain non-IFRS financial measures used by InnVest, including a reconciliation to IFRS financial measures.

Additional information relating to InnVest, including its Annual Information Form, can be accessed on the Canadian Securities Administrators' System for Electronic Document Analysis and Retrieval ("SEDAR") located at www.sedar.com and on its website at www.innvestreit.com.

Forward-looking statements

In the interest of providing InnVest unitholders and potential investors with information regarding InnVest, certain statements contained in this M&DA constitute forward-looking statements within the meaning of applicable securities laws. These statements include, but are not limited to, statements made concerning InnVest's objectives, its strategies to achieve those objectives, as well as other statements with respect to management's beliefs, plans, estimates and intentions, and similar statements concerning anticipated future events, results, circumstances and performance or expectations that are not historical facts. Forward-looking information typically contains statements with words such as "outlook", "objective", "may", "continue", "anticipate", "believe", "expect", "estimate", "plan", "intend", "forecast", "project" or similar expressions suggesting future outcomes or events. Such forward-looking statements reflect management's current beliefs and are based on information currently available to management.

These forward-looking statements are not guarantees of future events or performance and, by their nature, are based on InnVest's estimates and assumptions, which are subject to risks and uncertainties, including those described under "Risks and uncertainties" in this MD&A. Readers are cautioned not to place undue reliance on forward-looking statements, as there can be no assurance that the plans, intentions or expectations upon which they are based will occur. By its nature, InnVest's forward-looking information involves numerous assumptions, inherent risks and uncertainties, which may cause InnVest's actual performance and financial results in future periods to differ materially from any estimates or projections of future performance or results expressed or implied by such forward-looking statements. Factors that could cause actual results, performance, or achievements to differ materially from those expressed or implied by forward-looking statements include, but are not limited to, changes in business strategies; general global economic and business conditions; medical concerns relating to travel and/or specific destinations; general global credit market conditions; the effects of competition and pricing pressures; industry overcapacity; shifts in market demands; changes in laws and regulations, including environmental and regulatory laws; potential increases in maintenance and operating costs; uncertainties of litigation; labour disputes; timing of completion of capital or maintenance projects; currency and interest rate fluctuations; various events which could disrupt operations; and technological changes.

Although InnVest believes that the expectations represented by such forward-looking statements are reasonable, there can be no assurance that such expectations will be consistent with these forward-looking statements. The forward-looking statements contained in this MD&A are made as of the date of this MD&A. Except as required by law, InnVest does not undertake any obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. All forward-looking statements contained in this MD&A are expressly qualified by this cautionary statement.

Adoption of IFRS

InnVest has presented its financial results for the three and nine months ended September 30, 2011 and the comparative prior period information in accordance with IFRS. IFRS are premised on a conceptual framework similar to Canadian GAAP, although significant differences exist in certain matters of recognition, measurement and disclosure. While the adoption of IFRS did not have an impact on InnVest's cash flows, it did have a material impact on its consolidated balance sheets and statements of income.

In particular, the opening IFRS balance sheet reflects the revaluation of InnVest's hotel properties to fair value, the temporary classification of its trust units as liabilities and the classification of certain puttable equity instruments as liabilities which are remeasured at each reporting date. The impact of these differences on the January 1, 2010 opening balance sheet under IFRS compared to the December 31, 2009 balance sheet under Canadian GAAP resulted in a decrease in unitholders' equity of approximately $729.8 million, from $507.0 million to a deficit of $222.8 million. In addition, the impact of these differences on the December 31, 2010 balance sheet under IFRS compared to the December 31, 2010 balance sheet under Canadian GAAP resulted in a decrease in unitholders' equity of approximately $266.3 million, from $573.4 million to $307.1 million.

The financial statements have been prepared using the standards and interpretations currently issued and expected to be effective at the end of December 31, 2011, InnVest's first annual IFRS reporting period. The International Accounting Standards Board is currently in the process of amending several IFRS accounting standards that will be applicable to InnVest including, but not limited to, standards relating to leases. The evaluation of the potential impact of IFRS on InnVest's condensed consolidated financial statements will be an ongoing process as new standards and amendments to existing standards are issued. As a result, the impact of InnVest's conversion to IFRS may be different than its current expectation.

In addition to the disclosures in Note 3 in the accompanying unaudited condensed consolidated interim financial statements, the following discussion highlights key decisions and differences relating to the adoption of IFRS on InnVest's financial results. This section should also be read in conjunction with IFRS disclosures in InnVest's MD&A in the 2010 Annual Report.

IFRS 1: First-time adoption of IFRS ("IFRS 1")

The adoption of IFRS required the application of IFRS 1, which provides guidance for an entity's initial adoption of IFRS. IFRS generally requires an entity to apply all IFRS retrospectively, as though IFRS had been in place since inception. However, IFRS 1 provides certain mandatory exceptions and permits limited optional exemptions. The following are the optional exemptions applicable to InnVest under IFRS 1 which it applied in the preparation of its first financial statements under IFRS.

a) Fair value as deemed cost

IFRS 1 allows an entity to initially measure its property, plant and equipment ("PP&E") upon transition to IFRS at fair value as deemed cost. InnVest elected to apply the deemed cost election to its hotel properties and other real estate properties based on external and internal valuations.

b) Business combinations

Under IFRS 1, a first-time adopter may elect not to apply IFRS 3 – *Business Combinations* ("IFRS 3") retrospectively to business combinations that occurred before the date of transition to IFRS. InnVest made this election in order to only apply IFRS 3 to business combinations prospectively from the date of transition to IFRS.

c) Employee benefits

IFRS 1 allows entities to recognize all cumulative actuarial gains and losses immediately at transition. InnVest made this election for its existing defined benefit pension programs.

d) Other elections

InnVest also applied IFRS 1 elections relating to compound financial instruments, decommissioning liabilities and borrowing costs. These elections allow InnVest to apply IFRS prospectively and avoid the need to retrospectively adjust its financial statements. As such, no adjustments were required to opening retained earnings. Management did not believe the value of restating these assets and liabilities warranted the cost of retrospective application.

Impact of IFRS on statement of financial position

The following tables quantify the significant differences between Canadian GAAP and IFRS on InnVest's condensed consolidated balance sheets as at January 1, 2010 (transition date) and December 31, 2010.

January 1, 2010	Canadian GAAP	Other equity based instruments	Trust units	Convertible debentures conversion option	Hotel properties	Deferred income tax	Other	IFRS
ASSETS								
Current assets	131,640	–	–	–	–	–	3,557	135,197
Restricted cash	3,815	–	–	–	–	–	–	3,815
Hotel properties	1,740,642	–	–	–	(214,996)	–	39,918	1,565,564
Other real estate properties	15,770	–	–	–	–	–	(1,288)	14,482
Intangibles assets	52,657	–	–	–	–	–	(34,129)	18,528
Assets held for sale	5,685	–	–	–	–	–	(5,685)	–
	1,950,209	–	–	–	(214,996)	–	2,373	1,737,586
LIABILITIES								
Current liabilities	92,739	–	–	–	–	–	–	92,739
Long-term debt	931,685	–	–	–	–	–	–	931,685
Other long-term debt obligations	6,448	–	–	–	–	–	4,681	11,129
Convertible debentures	225,918	–	–	–	–	–	–	225,918
Deferred income tax liability	186,430	–	–	–	–	40,622	–	227,052
	1,443,220	–	–	–	–	40,622	4,681	1,488,523
Unitholders and other liabilities	–	–	–	3,990	–	–	–	3,990
Future distributions liability	–	2,423	465,489	–	–	–	–	467,912
UNITHOLDERS' EQUITY (DEFICIT)	506,989	(2,423)	(465,489)	(3,990)	(214,996)	(40,622)	(2,308)	(222,839)
	1,950,209	–	–	–	(214,996)	–	2,373	1,737,586

December 31, 2010	Canadian GAAP	Other equity based instruments	Trust units	Convertible debentures conversion option	Hotel properties	Deferred income taxes	Other	IFRS
ASSETS								
Current assets	46,097	–	–	–	–	–	241	46,338
Restricted cash	3,831	–	–	–	–	–	–	3,831
Hotel properties	1,694,210	–	–	–	(214,906)	–	19,181	1,498,485
Other real estate properties	16,955	–	–	–	473	–	(1,762)	15,666
Intangible assets	33,337	–	–	–	–	–	(15,808)	17,529
Deferred income tax asset	5,603	–	–	–	–	11,385	–	16,988
	1,800,033	–	–	–	(214,433)	11,385	1,852	1,598,837
LIABILITIES								
Current liabilities	164,775	–	–	–	–	–	–	164,775
Long-term debt	758,122	–	–	–	–	–	–	758,122
Other long term obligations	6,921	–	–	–	–	–	5,414	12,335
Convertible debentures	241,472	–	–	–	–	–	–	241,472
Deferred income tax liability	2,537	–	–	–	–	978	–	3,515
Liabilities related to assets held for sale	–	–	–	–	–	–	–	–
	1,173,827	–	–	–	–	978	5,414	1,180,219
Non-controlling interest	52,832	(52,832)	–	–	–	–	–	–
Unitholders' and other liabilities	–	91,683	–	19,097	–	–	721	111,501
Future distributions liability	–	–	–	–	–	–	–	–
UNITHOLDERS' EQUITY	573,374	(38,851)	–	(19,097)	(214,433)	10,407	(4,283)	307,117
	1,800,033	–	–	–	(214,433)	11,385	1,852	1,598,837

Hotel properties

In accordance with IFRS 1, InnVest elected to revalue its hotel properties as at January 1, 2010. A significant portion of the portfolio has been subject to external valuation with the remainder being valued by management and validated externally following the same methodology. The fair value of each hotel was determined based upon a direct capitalization method of valuation with consideration being given to minimum/maximum price per room values. Capitalization rates and price per room values were established based on individual markets, segments, and where available, recent comparable hotel sales activity. Based on this valuation work, the impact of the deemed cost election was a reduction in the carrying value of InnVest's opening balance sheet hotel properties as at January 1, 2010 of $215.0 million.

Hotel properties are accounted for as PP&E under IFRS. Similar to Canadian GAAP, PP&E is initially measured at cost. However, subsequent to initial recognition, IFRS requires that an entity choose either the cost model or the revaluation model to account for its PP&E. Following the initial revaluation to fair value at conversion to IFRS (refer to discussion under "IFRS 1 – First time adoption of IFRS" above), InnVest elected to use the cost model when preparing its financial statements under IFRS.

While the cost model is generally consistent with Canadian GAAP, IFRS's requirements to identify different components of PP&E are more explicit than those existing under Canadian GAAP. As a result, InnVest identified two additional components of its assets; finishes and electrical & mechanical. This change in components results in an increase in depreciation expense in future periods given the shorter useful life attributed to those individual components. Offsetting this increase is the lower deemed cost for hotel properties following the revaluation at IFRS conversion.

Trust units – liability vs equity

Under Canadian GAAP, trust units were presented as equity. Under IFRS, a trust unit may be considered a financial instrument where a liability arises when a financial instrument has a contractual obligation feature to deliver cash or another financial asset to another entity. Prior to June 16, 2010, the mandatory requirement to distribute taxable income under

InnVest's Declaration of Trust constituted such a contractual obligation and, accordingly, InnVest units are presented as a liability under IFRS. This liability is measured at fair value with any related gains and losses recognized on the income statement.

On June 16, 2010, InnVest modified its Declaration of Trust, with the consent of unitholders, to eliminate the mandatory distribution and leave distributions to the discretion of the Trustees. This change enables trust units to be presented as equity under IFRS from June 16, 2010 going forward.

Therefore at January 1, 2010 and at March 31, 2010, InnVest's units are presented as a liability on the IFRS balance sheet and are remeasured based on the fair value of InnVest units at each reporting date. The resulting non-cash charges are recorded as unrealized fair value gains (losses) on the income statement. Distributions paid on units prior to June 16, 2010 are reflected as finance charges on the income statement as compared to distributions on the statement of equity under Canadian GAAP.

Other equity based instruments – liability vs equity

Under Canadian GAAP, InnVest accounted for certain equity instruments as a component of unitholders' equity. Under IFRS, these instruments have been reclassified to liabilities because they are not the least subordinated instrument of units and because there is a redemption feature at the option of the holder. This treatment applies to InnVest's exchangeable shares and units granted to executives under a compensation program. In addition, IOT units reflected as non-controlling interest under Canadian GAAP are presented as a liability under IFRS.

Subsequent to initial measurement at cost, these financial liabilities are remeasured based on the fair value of InnVest units at each reporting date. As a result, net income during any given period may be greater or less than as determined under Canadian GAAP depending on whether an increase or decrease in fair value occurs during the period (based on InnVest's unit price).

Distributions made on equity based instruments classified as liabilities are recorded on the income statement as compared to distributions on the statement of equity under Canadian GAAP.

Conversion feature of convertible debentures

In accordance with IAS 32 – *Financial Instruments*, the conversion feature of convertible debentures is presented as a liability as compared to a component of equity under Canadian GAAP. The conversion feature is remeasured each reporting period with changes in the fair value being recorded as unrealized fair value gains (losses) on the income statement. Under IFRS, the conversion feature will be adjusted to unitholders' equity upon conversion of a debenture.

Deferred income taxes

On January 1, 2010, deferred income taxes were impacted by changes made to the carrying value of hotel properties and other real estate properties and components to the properties as well as changes to the rates applied using the undistributed tax rate.

As described above, prior to June 16, 2010, InnVest's units were classified as a future distribution liability and, accordingly, deferred taxes were reflected at the tax rate applicable for specified investment flow-through entities ("SIFT"), being approximately 31%. On June 16, 2010, the mandatory distribution feature was removed from InnVest's Declaration of Trust, with the impact that InnVest's units were reclassified to equity. Under IFRS, as the units no longer represent a future distribution liability, deferred taxes were then required to be recorded at the "undistributed" rate of approximately 45%.

On December 31, 2010, InnVest completed a corporate restructuring to become a Qualifying REIT. Prior to this transaction, IFRS required InnVest to recognize deferred income taxes and liabilities on temporary differences expected to reverse after January 1, 2011. As a result of the completion of its tax restructuring, the non-cash deferred tax liability that arose primarily as a result of the introduction of the SIFT legislation in 2007, reversed in the fourth quarter of 2010.

Other

The adoption of IFRS resulted in differences relating to accounting for employee benefits and asset retirement obligations. InnVest's deemed cost election for other real estate properties resulted in a reduction in the carrying value of InnVest's opening balance sheet other real estate properties as at January 1, 2010 of $2.0 million.

Additionally, the transition to IFRS resulted in historic intangible assets, which had been established under Canadian GAAP in respect of acquisitions and capitalized to hotel properties, to no longer be separately recognized under IFRS. As part of the deemed cost election, these were reclassified to hotel properties, license contracts and accounts receivable, as applicable.

Impact of IFRS on results of operations

The following tables quantify the significant differences between Canadian GAAP and IFRS on InnVest's condensed consolidated statements of net (loss) income for the nine months ended September 30, 2010 and the year ended December 31, 2010.

For the six months ended June 30, 2010	Canadian GAAP	Equity based instruments classified as liabilities	Convertible debenture conversion option	Depreciation and amortization	Deferred income taxes	Other	IFRS
Hotel Revenues	461,137	–	–	–	–	590	461,727
Hotel expenses	351,206	–	–	–	–	498	351,704
Hotel operating income	109,931	–	–	–	–	92	110,023
Other (income) and expenses							
Interest on mortgages and other debt	43,281	–	–	–	–	–	43,281
Convertible debentures interest and accretion	14,236	–	–	–	–	–	14,236
Corporate and administrative	4,436	390	–	–	–	–	4,826
Other business income, net	(3,739)	–	–	–	–	–	(3,739)
Other income	(321)	–	–	–	–	(327)	(648)
Depreciation and amortization	71,043	–	–	(324)	–	–	70,719
Loss before the undernoted	(19,005)	(390)	–	324	–	419	(18,652)
Finance costs – distributions	–	18,383	–	–	–	–	18,383
Unrealized loss on liabilities presented at fair value	–	95,147	20,751	–	–	–	115,898
Deferred income tax (recovery) expense	(1,917)	–	–	–	(6,558)	–	(8,475)
Loss from continuing operations	(17,088)	(113,920)	(20,751)	324	6,558	419	(144,458)
Net income from discontinued operations	461	–	–	–	–	(461)	–
Net loss and comprehensive loss	(16,627)	(113,920)	(20,751)	324	6,558	(42)	(144,458)

For the year ended December 31, 2010	Canadian GAAP	Equity based instruments classified as liabilities	Convertible debenture conversion option	Depreciation and amortization	Impairment	Deferred income taxes	Other	IFRS
Hotel Revenues	609,566		–	–	–	–	590	610,156
Hotel expenses	472,416		–	–	–	–	205	472,621
Hotel operating income	137,150	–	–	–	–	–	385	137,535
Other (income) and expenses								
Interest on mortgages and other debt	57,587		–	–	–	–	–	57,587
Convertible debentures interest and accretion	19,189		–	–	–	–	–	19,189
Corporate and administrative	8,079	368	–	–	–	–	–	8,447
Other business income, net	(5,231)		–	–	–	–	–	(5,231)
Other income	(558)		–	–	–	–	(327)	(885)
Depreciation and amortization	94,678		–	(563)	–	–	–	94,115
Writedown of hotel properties and intangible assets	5,907		–	–	1,505	–	(327)	7,085
Loss before the undernoted	(42,501)	(368)	–	563	(1,505)	–	1,039	(42,772)
Finance costs – distributions	–	18,403	–	–	–	–	–	18,403
Fair value loss	–	131,390	14,568	–	–	–	–	145,958
Future income tax recovery	(189,497)		–	–	–	(51,030)	–	(240,527)
Income from continuing operations	146,996	(150,161)	(14,568)	563	(1,505)	51,030	1,039	33,394
Income from discontinued operations	461		–	–	–	–	(461)	–
Net income and comprehensive income	147,457	(150,161)	(14,568)	563	(1,505)	51,030	578	33,394

Equity based instrument presented as financial liabilities

As described above, certain financial instruments are presented as liabilities under IFRS as opposed to equity under Canadian GAAP. These liabilities are remeasured at their fair value at each reporting date. As a result, net income during any given period may be greater or less than as determined under Canadian GAAP depending on whether an increase or decrease in fair value occurs during the period (based on InnVest's unit price). For InnVest's exchangeable shares and the IOT units, the resulting non-cash charges are recorded as unrealized fair value gains (losses). For the units granted to executives under a compensation program, the resulting non-cash charge at each reporting date is recorded as compensation expense.

Distributions made on equity based instruments classified as liabilities are recorded on the income statement as compared to distributions on the statement of equity under Canadian GAAP. Distributions paid on exchangeable shares and the IOT units are recorded as finance costs. Distributions paid on units granted under a compensation program are recorded as compensation expense.

Conversion feature of convertible debentures

As described above, the conversion feature of convertible debentures is presented as a liability under IFRS. The conversion feature is remeasured at each reporting period with changes in the fair value being recorded as unrealized fair value gains (losses) in net income.

Depreciation and amortization expense

The transition to IFRS has resulted in a difference in depreciation expense resulting from changes to the opening cost base of hotel properties and other real estate properties (refer to deemed cost election above). In addition, changes were made to the asset componentization resulting in differences in useful lives and, in accordance, the depreciation charge.

Impairment

InnVest's impairment review under IFRS resulted in an incremental impairment based on changes to the opening deemed cost value and corresponding depreciation charge for one leasehold asset.

Deferred income taxes

Deferred income tax differences reflect the impact of InnVest's corporate restructuring to become a Qualifying REIT on December 31, 2010.

Other

The definition of discontinued operation under IFRS is more restrictive than under Canadian GAAP and as a result, InnVest reclassified operating results for hotels previously classified as discontinued. Other changes also reflect differences in the accounting for pension expenses.

Business overview

InnVest holds one of Canada's largest hotel portfolios together with a 50% interest in Choice Hotels Canada Inc., one of the largest franchisors of hotels in Canada. InnVest's portfolio is well diversified across hotel accommodation categories, brands, geography and customers.

Hotel real estate owner

As at September 30, 2011, InnVest's portfolio comprised 144 hotel properties operated under internationally recognized franchise brands. The portfolio is evenly divided between full-service and limited service hotels based on number of rooms. Full-service hotels however, generate higher revenues per room given higher ADRs charged and greater ancillary services sold. Year-to-date, approximately 80% of revenues are generated from room revenues and 20% from food and beverage services and other services including meeting space rental, parking, retail operations and telephone use.

InnVest's hotels are operated by four hotel management companies which earn base and incentive fees related to the revenues and profitability of each hotel. The hotels' primary operating costs include wages, food costs, utilities, management fees and sales and marketing expenses. Other property level expenses include property taxes, ground rent for leasehold interests and property insurance. Many of these property level expenses are relatively fixed and do not necessarily change in accordance with revenue levels.

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 travellers, leisure travellers, tours, associations and corporate groups.

	Ontario		Quebec		Atlantic		Western		Total		
	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	No. of hotels	No. of guest rooms	% of total guest rooms
Comfort Inn	36	2,934	22	1,754	15	1,126	9	745	82	6,559	34.7%
Delta Hotel	2	573	3	1,048	4	1,017	2	689	11	3,327	17.6%
Holiday Inn, Holiday Inn Express	11	1,752	1	175	1	196	1	152	14	2,275	12.0%
Quality Hotel, Quality Suites	5	881	5	694	1	160	1	126	12	1,861	9.9%
Travelodge	4	552	–	–	–	–	4	896	8	1,448	7.7%
Hilton Hotel	–	–	1	571	1	197	–	–	2	768	4.1%
Fairmont Hotels & Resorts	–	–	–	–	–	–	2	604	2	604	3.2%
Radisson Hotel/Suites	2	388	–	–	–	–	–	–	2	388	2.1%
Staybridge Suites	3	342	–	–	–	–	–	–	3	342	1.8%
Sheraton Suites	–	–	–	–	–	–	1	323	1	323	1.7%
Best Western	1	130	–	–	–	–	–	–	1	130	0.7%
Hilton Garden Inn	1	120	–	–	–	–	–	–	1	120	0.6%
Hilton Homewood Suites	1	83	–	–	–	–	–	–	1	83	0.4%
Independent	4	658	–	–	–	–	–	–	4	658	3.5%
	70	8,413	32	4,242	22	2,696	20	3,535	144	18,886	100.0%

Franchise business

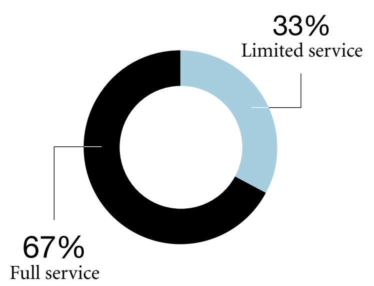
Generating $2.5 million during the nine months ended September 30, 2011 (2010 – $2.4 million), InnVest owns 50% of Choice Hotels Canada Inc. ("CHC"), which has franchise agreements with approximately 300 locations in Canada. The remaining 50% interest is owned by Choice Hotels International Inc. ("Choice International"), one of the largest hotel franchise companies in the world. In addition to strong international brand recognition, Choice International has a centralized reservation system, sales and marketing programs and proprietary property management systems.

In 1993, CHC was granted a 99-year licence to franchise all Choice hotel brands in Canada, including Comfort Inn, Quality Suites and Quality Hotels. CHC earns franchise revenue by charging hotel owners a monthly royalty fee based on a percentage of the revenue generated by the licenced properties and by selling franchises. InnVest's proportionate interest operating results are included in the condensed consolidated statements of income in other business income.

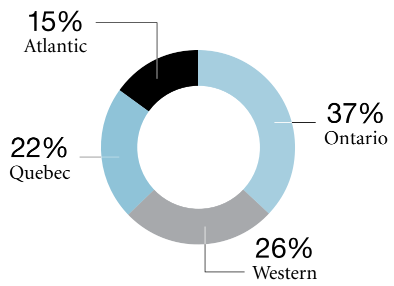
Office, retail and retirement home business

Generating $1.1 million during the nine months ended September 30, 2011 (2010 – $1.3 million), InnVest owns office and retail real estate as well as a retirement home. These real estate interests are adjacent to owned hotels and were acquired as part of certain hotel acquisitions. The operating results are included in the condensed consolidated statements of income in other business income.

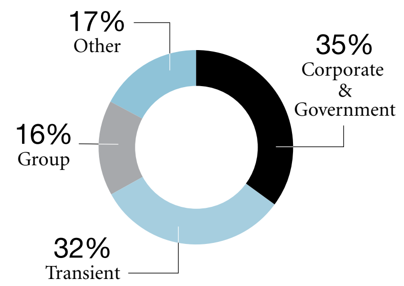
2010 Annual Hotel Revenues By Service Category



2010 Annual Hotel Revenues By Geography



2010 Annual Hotel Room Revenues By Customer



Business strategy

We are currently in a low point in the lodging cycle, however, our long-term view on the industry remains positive based on improving hotel demand and a low supply environment. InnVest is focused on internal growth in our existing portfolio through revenue enhancing and cost reduction initiatives and making prudent capital allocation decisions to increase long-term value and grow cash flows. Over the next two years, InnVest expects to undertake a significant capital investment program to help revitalize its portfolio of limited service hotels as well as invest in brand initiatives including Delta, Holiday Inn, Hilton and Radisson hotels.

Operating strategy

InnVest's operating focus aims to enhance the performance of each hotel and improve its RevPAR penetration versus its competitive set. Notable activities over the last year included an extensive sales training program implemented in late 2010 across the limited service portfolio aimed at engaging each hotel's executive staff in the sales and marketing of their property. Several profit-improving capital investment projects have also been initiated to help hotels capture greater market share from their competitors. InnVest continues to manage its portfolio aggressively with emphasis on cost efficiencies and maximizing the performance and cash flow of each of its hotels.

InnVest's diversification by location, brand, customer and market position is a core component of its operating strategy. Since individual markets can be affected by local events and economic conditions, geographic diversification helps limit the impact of such factors on the overall portfolio. Diversification across customers and brands allows InnVest to effectively manage its rooms based on changing demand drivers, thereby optimizing financial performance through improved occupancy and ADR.

InnVest's hotels are managed by four hotel management companies, each bringing unique expertise to the portfolio. Westmont Hospitality Canada Limited ("Westmont"), a division of one of the largest privately held managers of hotels in the world, manages the majority of InnVest's hotels (128 hotels). InnVest also partners with other third party managers including Delta Hotels (10 hotels), Fairmont Hotels (3 hotels) and Hilton Hotels (2 hotels), each an experienced hotel manager with recognized brands. One hotel in the portfolio is classified as an operating lease.

Capital allocation strategy

In order to drive the long-term profitability of the portfolio, InnVest continually evaluates its capital allocation opportunities. Following its inception, InnVest expanded its portfolio, broadening its market base and diversifying its risk profile. In recent years, InnVest's capital allocation efforts have been focused on maximizing the potential of its existing portfolio by investing capital into internal profit-improving opportunities. While acquisition opportunities have been limited over the past several years, availability is expected to increase as operating trends in the industry improve.

InnVest constantly evaluates its current real estate holdings to optimize diversification and capitalize on embedded value or higher return opportunities. From time to time, certain assets are identified that may not support its long term objectives given limited growth prospects in earnings and value.

InnVest's ability to recycle capital through hotel sales has been impacted by constrained financing availability which has limited the pool of buyers and proceeds offered. Financing conditions continue to improve, enabling buyer and seller expectations to converge. InnVest is exploring asset sale opportunities for a limited number of non-strategic hotels. During the third quarter of 2011, InnVest recognized a non-cash impairment charge of $7.7 million relating to four hotels triggered by InnVest's long-term holding expectation for these assets.

Corporate developments

Proposed reorganization

On July 20, 2011, the Minister of Finance (the "Minister") announced changes in, among other things, the tax treatment of real estate investment trusts that have issued "stapled" securities. If the Minister's announcement is enacted as proposed and no changes are made to the existing structure of the REIT and IOT, then rents (and certain other amounts) paid by IOT to the REIT after the applicable transition date (expected to be July 20, 2012) (the "Transition Period") would cease to be deductible in computing the income of IOT for Canadian income tax purposes.

After careful consideration of options, the Board of Trustees of InnVest recommends a merger of IOT into the REIT effective on June 30, 2012. This reorganization would result in all the former stapled unitholders and stapled debenture holders of the REIT and IOT holding only units or convertible debentures, as the case may be, of the REIT. The merged entity would be governed as a trust. The proposed merger will be subject to unitholders' approval.

InnVest intends to schedule a special meeting of unitholders in the first quarter of 2012 to approve the merger (the "Special Meeting"). Unitholders will be provided with a notice of the Special Meeting and management information circular in respect of the Special Meeting and will be entitled to vote at the Special Meeting.

Pending completion of the proposed merger, InnVest is restricted from issuing stapled securities during the Transition Period, subject to certain exceptions. As a consequence, InnVest suspended its distribution reinvestment plan ("DRIP") beginning in August 2011 until further notice and will satisfy all Trustee compensation in cash as opposed to the usual partial satisfaction in the form of units.

Distribution reduction

In November 2011, InnVest announced a reduction in distributions paid to unitholders to $0.40 per unit annually, as compared to the prior distribution level of $0.50 per unit annually. This equates to a monthly distribution of $0.0333 per unit beginning in November 2011. The Board of Trustees unanimously approved the reduction of distributions after careful consideration of the environment faced by InnVest and its desire to conserve liquidity to fund profit-improving capital investments throughout the portfolio.

Normal course issuer bid

In November 2011, InnVest announced that the TSX has accepted notice of the intention of the REIT and IOT to jointly make normal course issuer bids for their stapled units and Series F 5.75% Stapled Convertible Debentures and the intention of the REIT to make normal course issuer bids for its Series B 6.00% Convertible Debentures, Series C 5.85% Convertible Debentures, Series D 6.75% Convertible Debentures, and Series E 6.00% Convertible Debentures.

Litigation settlement

Subsequent to the end of the quarter, InnVest settled an outstanding lawsuit in which it was the plaintiff. As a result, InnVest expects to record a gain of $2.9 million less legal and associated costs, in the fourth quarter of 2011.

Outlook

Current macro environment factors are impacting the global economy and reinforce the importance of strong operational expertise and regional focus for our business. InnVest's broad, diversified portfolio remains a key advantage in the current environment.

Looking ahead, we remain focused on driving internal growth within our existing portfolio. In 2011, we began an important multi-year capital program to enhance our product offering at a number of our full-service and limited-service hotels. These targeted investments are expected to improve our hotels' competitive positioning and operating performance through increased occupancies and rates. An enhanced product, coupled with improving demand and constrained new supply should enable InnVest to realize cash flow growth.

Third quarter highlights

- RevPAR on a same hotel basis increased 1.2% benefitting from a 0.9% improvement in ADR and a 0.2 point growth in occupancy;
- Hotel revenues improved 1.0% to $174.8 million;
- Hotel operating income ("HOI") was relatively unchanged at $50.8 million;
- InnVest realized net income of $66.9 million compared to a net loss of $4.4 million in 2010. Excluding non-cash charges relating to the IFRS implementation, deferred income taxes and a non-cash impairment charge during the quarter, InnVest's net income improved to $10.7 million compared to $7.7 million in the prior period; and
- Funds from operations and distributable income each improved reflecting the benefit of lower interest charges.

Operating summary

	Three months ended September 30, 2011	Three months ended September 30, 2010	**Nine months ended September 30, 2011**	Nine months ended September 30, 2010
Hotel revenues	**$ 174,832**	$ 173,022	**$ 465,703**	$ 461,727
Hotel operating income[1]	**50,774**	50,823	**109,470**	110,023
Net income (loss) and comprehensive income (loss)	**66,929**	(4,432)	**48,859**	(144,458)
Funds from operations[1]	**33,695**	31,964	**55,193**	52,250
Distributable income[1]	**28,128**	26,607	**40,892**	37,634
Distributions declared[2]	**11,701**	11,138	**34,766**	33,187
Per unit diluted:				
Net income (loss)	**0.581**	–	**0.508**	–
Funds from operations	**0.314**	0.324	**0.565**	0.572
Distributable income[3]	**0.262**	0.270	**0.425**	0.414
Distributions[2]	**$ 0.1251**	$ 0.1251	**$ 0.3753**	$ 0.3753

1. *See "Non-IFRS Financial Measures" on page 23.*
2. *Distributions and distributions per unit include cash distributions and distributions arising from the dividend reinvestment plan.*
3. *Distributable income per unit is calculated on a basis consistent with that prescribed by IFRS for calculating net income (loss) per unit.*

Hotel operating results comparison

For purposes of discussion of operating results within the MD&A, 143 of the 144 hotels have been classified as the "Base Portfolio". One hotel has been excluded from continuing operations for the comparative periods given that it is now classified as an operating lease.

Hotel revenues

Hotel revenues consist primarily of revenue generated from room occupancy and non-room revenue. Non-room revenue include food and beverage services and other miscellaneous revenue streams associated with hotel operations such as space leases, vending commissions, movie rentals, parking and telephone. Room revenues accounted for approximately 80% of total hotel revenues for the nine months ended September 30, 2011 (2010 – 79%).

Operating results – three months ended September 30, 2011

Overall hotel portfolio

The hospitality industry is highly correlated to the economy given its impact on discretionary travel demand, including demand from corporate and leisure customers. Despite relatively positive economic indicators in Canada, the debt crisis in Europe and a fragile U.S. recovery has increased market volatility and negatively affected consumer confidence, contributing to slowing economic growth. For the three months ended September 30, 2011, hotel revenues increased 1.0%, to $174.8 million.

RevPAR over this period increased 1.2%, benefitting from a 0.9% increase in ADR and a 0.2 point improvement in occupancy.

	Occupancy		ADR		RevPAR	
		Variance to 2010		Variance to 2010		Variance to 2010
Ontario	67.6%	(1.0 pts)	$ 106.58	(0.4%)	$ 72.10	(1.7%)
Quebec	73.6%	2.5 pts	$ 118.16	1.7%	$ 86.95	5.2%
Atlantic	79.4%	0.6 pts	$ 124.04	(0.8%)	$ 98.44	(0.1%)
Western	67.9%	0.1 pts	$ 142.17	3.3%	$ 96.57	3.5%
Total	70.7%	0.2 pts	$ 118.60	0.9 %	$ 83.89	1.2%

Note: On a same-hotel basis, excluding one hotel which is classified as an operating lease.

Room revenues

Room revenues for the three months ended September 30, 2011 increased 1.2%, or $1.7 million, to $144.3 million. Strength in the Quebec and Western regions offset a room revenue decline in Ontario.

Three months ended September 30, 2011

Room revenue variance	Number of hotel rooms	Variance to 2010	Variance to 2010
Base Portfolio			
Ontario	8,230	$ (966)	(1.7%)
Quebec	4,242	1,678	5.2%
Atlantic	2,696	(32)	(0.1%)
Western	3,535	1,049	3.5%
Sub-total	18,703	1,729	1.2%
Other	183	(36)	(100%)
Total	18,886	$ 1,693	1.2%

The Ontario region experienced a 1.7% decline in room revenue based on reduced ADR and occupancy. Third quarter results were impacted by the rebranding of one hotel in the region in 2011 as well as ongoing renovations at certain hotels in order to enter into new long-term franchise arrangements.

The Quebec region realized a 5.2% improvement in room revenue driven by gains in both occupancy and ADR. Quebec City led growth benefitting from the recent room renovations at the Hilton Quebec City, whose RevPAR grew almost 25% during the quarter.

Room revenue in the Atlantic region was relatively unchanged with strength in Newfoundland offsetting declines in New Brunswick.

InnVest's Base Portfolio of Western hotels realized room revenue growth of 3.5% driven by ADR improvement. Calgary led growth this quarter benefitting from the recent room renovations at the Fairmont Palliser, whose RevPAR grew over 10% during the quarter.

Non-room revenues

For the three months ended September 30, 2011, non-room revenues totalled $30.5 million, up 0.4%, compared to the prior year.

Hotel expenses

InnVest continually focuses on managing all costs to maximize overall profitability without impacting the service levels offered to guests. Further savings opportunities are limited given the extent of adjustments made throughout the portfolio. Management's focus is on limiting incremental costs associated with improved occupancy in the portfolio to enable margin expansion. Many property level expenses, including property taxes, leasehold payments and insurance, are relatively fixed and do not necessarily change in accordance with overall demand levels.

Hotel expenses for the three months ended September 30, 2011 increased $1.9 million or 1.5% to $124.1 million. Operating expenses increased 2.1% reflecting inflationary wage increases for hotel staff and higher energy costs during the quarter.

Hotel operating income

For the three months ended September 30, 2011, InnVest generated HOI of $50.8 million, unchanged from the prior year. The modest RevPAR gains achieved were not sufficient to offset inflationary cost increases, resulting in HOI margins declining 40 basis points to 29.0%.

Regional HOI results are reflective of the RevPAR achieved during the quarter.

Three months ended September 30, 2011

HOI variance	Number of hotel rooms		Variance to 2010	Variance to 2010
Base Portfolio				
Ontario	8,230	$	(980)	(5.5%)
Quebec	4,242		648	6.1%
Atlantic	2,696		(340)	(3.3%)
Western	3,535		519	4.2%
Sub-total	18,703		(153)	(0.3%)
Other	183		104	281.1%
Total	18,886	$	(49)	(0.1%)

Other income and expenses

Other income and expenses for the three months ended September 30, 2011 increased $4.7 million to $47.8 million. During the quarter, InnVest recognized a non-cash impairment charge of $7.7 million triggered by InnVest's long-term holding expectation for certain assets. The impairment provision, derived based on the estimated fair value less costs to sell, relates to four hotel properties representing 770 rooms.

Interest on mortgages was lower by $2.3 million following the $95.0 million paydown of one mortgage in September 2010 and the benefit of a reduced interest rate on this remaining outstanding mortgage balance beginning in March 2011. Higher interest on convertible debentures reflects higher balances outstanding over the period following the issuances of $75.0 million in August 2010 and $50.0 million in March 2011 offset by the redemption of $45.7 million in September 2010.

Finance costs – distributions

For the three months ended September 30, 2011, $46 of distributions paid are categorized as finance costs as compared to $45 in the prior period. These relate to certain equity based instruments which are classified as liabilities under IFRS. (Refer to "Adoption of IFRS"). Given their presentation as liabilities, distributions paid on these financial instruments are treated as finance costs under IFRS as compared to distributions through the equity statement under Canadian GAAP. The change in presentation for distributions does not impact overall cash flow or total distributions paid.

Unrealized fair value gain (loss)

InnVest is required to account for various unit-based instruments as financial liabilities under IFRS. (Refer to "Adoption of IFRS"). These instruments are remeasured at their fair value at each reporting period resulting in non-cash items based upon the price of InnVest's units at each reporting date. The unrealized non-cash gains or losses are recognized in the condensed consolidated statement of net income (loss).

The decline in the market price of InnVest units at September 30, 2011 as compared to June 30, 2011 contributed to a reduced liability value as at the reporting date and a corresponding non-cash gain to earnings. The prior period adjustment reflected the higher market price of InnVest units over those periods.

Income taxes

For the three months ended September 30, 2011, InnVest generated a deferred income tax expense of $7.2 million as compared to a deferred income tax recovery of $5.4 million in 2010. The deferred tax expense in 2011 primarily reflects IOT's utilization of non-capital losses during the quarter. The current tax expense of $220 in 2011 reflects the tax provision based on IOT's taxable income during the quarter.

For 2011, InnVest estimates that the non-taxable portion of the distributions made to unitholders during the year will approximate 60% (2010 – 67%).

Net income (loss)

For the three months ended September 30, 2011, InnVest recorded net income of $66.9 million, or $0.581 per unit diluted compared to a net loss of $4.4 million for the same period in 2010. Excluding non-cash charges relating to the IFRS implementation, deferred income taxes and the non-cash impairment, InnVest's net income improved $3.0 million to $10.7 million compared to $7.7 million in the prior period.

As a result of the classification of units as financial liabilities for a significant portion of the 2010 comparative year, InnVest has not presented a per unit amount in the comparative period. Refer to "Adoption of IFRS".

Funds from operations

For the three months ended September 30, 2011, InnVest generated FFO of $33.7 million ($0.314 per unit diluted) compared to $32.0 million in the prior period ($0.324 per unit diluted) primarily reflecting reduced interest expenses. The reduction in per unit results reflects the higher number of units outstanding following an equity offering completed in March 2011. See "Non-IFRS Financial Measures" for a reconciliation of IFRS net income to FFO.

Distributable income

For the three months ended September 30, 2011, InnVest generated distributable income of $28.1 million ($0.262 per unit diluted) compared to $26.6 million in the prior year ($0.270 per unit diluted) primarily reflecting reduced interest expenses. The reduction in per unit results reflects the higher number of units outstanding following an equity offering completed in March 2011. See "Non-IFRS Financial Measures" for a reconciliation of IFRS net income to distributable income.

Distributions declared in the three months ended September 30, 2011 totalled $11.7 million, or $0.1251 per unit (2010 – $11.1 million or $0.1251 per unit). The increase in total distributions paid reflects the higher number of units outstanding following an equity offering completed in March 2011.

Operating results – nine months ended September 30, 2011

Overall hotel portfolio

For the nine months ended September 30, 2011, hotel revenues increased 0.9%, to $465.7 million reflecting growth in room revenues driven by improved demand.

Through the first nine months of the year, RevPAR increased 1.2% based on a 1.0 point improvement in occupancy which offset a 0.5% decline in ADR. Occupancy has improved consistently through the portfolio since early 2010 although pricing power has been limited in most markets driven by a competitive landscape.

	Occupancy		ADR		RevPAR	
		Variance to 2010		Variance to 2010		Variance to 2010
Ontario	61.5%	1.7 pts	$ 105.67	(2.1%)	$ 65.02	0.6%
Quebec	63.8%	1.2 pts	$ 114.85	0.6%	$ 73.31	2.6%
Atlantic	63.9%	0.2 pts	$ 117.63	0.3%	$ 75.16	0.7%
Western	62.3%	(0.2 pts)	$ 140.17	1.5%	$ 87.31	1.2%
Total	62.5%	1.0 pts	$ 116.05	(0.5%)	$ 72.57	1.2%

Note: On a same-hotel basis, excluding one hotel which is classified as an operating lease.

Room revenues

Room revenues for the nine months ended September 30, 2011 increased 0.9%, or $3.5 million, to $370.6 million. Growth was achieved across all regions led by markets which benefited from recent hotel renovations.

Nine months ended September 30, 2011

Room revenue variance	Number of hotel rooms		Variance to 2010	Variance to 2010
Base Portfolio				
Ontario	8,230	$	928	0.6%
Quebec	4,242		2,183	2.6%
Atlantic	2,696		358	0.7%
Western	3,535		968	1.2%
Sub-total	18,703		4,437	1.2%
Other	183		(950)	(100%)
Total	18,886	$	3,487	0.9%

Room revenue for the Ontario region grew 0.6% with occupancy growth offsetting ADR declines. Growth across the province through the first half of the year was somewhat offset by declines in the third quarter.

The Quebec region realized a 2.6% growth in room revenue driven by strength in the province's two key markets; Montreal and Quebec City. Quebec City saw particular growth following the completion of hotel renovations in the second quarter of 2011.

Room revenue in the Atlantic region increased 0.7% through a combination of occupancy and ADR growth.

InnVest's Base Portfolio of Western hotels realized room revenue increases of 1.2% led by growth in the third quarter. The region benefitted from hotel renovations completed at the Fairmont Palliser in Calgary in the second quarter of 2011.

Non-room revenues

For the nine months ended September 30, 2011, non-room revenues totalled $95.1 million, up $489, or 0.5%, compared to the prior year. Growth was driven by the second quarter inclusion of $2.1 million in interest earned related to prior periods' GST/HST input tax credits. Excluding this amount, non-room revenues declined approximately 1.7% primarily reflecting lower food and beverage revenues in the first quarter.

Hotel expenses

Hotel expenses for the nine months ended September 30, 2011 increased $4.5 million or 1.3% when compared to the same period in 2010 with a 2.0% increase in operating expenses (1.0 point improvement in occupancy or 1.6% increase in demand) which was somewhat offset by rent and property tax savings.

Hotel operating income

Growth in 2010 and year-to-date in 2011 has been driven by occupancy gains as opposed to ADR growth. While occupancy growth contributes to improved profitability, more profit is achieved through increases in ADR. The lack of consistent demand pressure throughout 2011 has limited the industry's ability to increase rates.

For the nine months ended September 30, 2011, hotel operating income margins declined 30 basis points to 23.5%. InnVest generated HOI of $109.5 million, down 0.5% or $553 as compared to the prior year. The growth in hotel revenues over this period was achieved through occupancy gains. The marginal contribution from this incremental demand was offset by higher operating costs. In addition, various rooms were taken out of the rental pool as a result of renovations which resulted in a reduction in hotel operating income of approximately $1.7 million during the first half of the year. Excluding the renovations displacement, HOI growth would have approximated 1.0%.

Nine months ended September 30, 2011

HOI variance	Number of hotel rooms		Variance to 2010	Variance to 2010
Base Portfolio				
Ontario	8,230	$	(86)	(0.2%)
Quebec	4,242		204	0.9%
Atlantic	2,696		(1,121)	(6.4%)
Western	3,535		129	0.4%
Sub-total	18,703		(874)	(0.8%)
Other	183		321	265.3%
Total	18,886	$	(553)	(0.5%)

Other income and expenses

Other income and expenses for the nine months ended September 30, 2011 increased 4.8 million to $133.5 million driven by the third quarter non-cash impairment charge of $7.7 million. This charge offset a net reduction in interest expense due to lower debt balances and weighted average interest rates as compared to the prior period. Reduced corporate and administrative expense also were realized given prior period expenses relating to the IFRS conversion as well as the decline in the market price of InnVest's units and its corresponding non-cash reduction in executive compensation over the period presented.

Finance costs – distributions

For the nine months ended September 30, 2011, $2.4 million of distributions paid are categorized as finance costs as compared to $18.4 million in the prior period. These relate to certain equity based instruments which are classified as liabilities under IFRS. (Refer to "Adoption of IFRS"). Given their presentation as liabilities, distributions paid on these financial instruments are treated as finance costs under IFRS as compared to distributions through the equity statement under Canadian GAAP. The change in presentation for distributions does not impact overall cash flow or total distributions paid.

The prior period included the presentation of all of InnVest's units as liabilities, the majority of which were reclassified to equity on June 16, 2010 following amendments to InnVest Declaration of Trust. (Refer to "Adoption of IFRS").

Unrealized fair value gain (loss)

InnVest is required to account for various unit-based instruments as financial liabilities under IFRS. (Refer to "Adoption of IFRS"). These instruments are remeasured at their fair value at each reporting period resulting in non-cash charges based upon the price of InnVest's units at each reporting date. The unrealized non-cash gains (losses) are recognized in the condensed consolidated statement of net income.

The decline in the market price of InnVest units at September 30, 2011 as compared to December 31, 2010 contributed to a reduced liability value as at the reporting date and a corresponding non-cash gain to earnings. The prior period adjustment reflected increasing market price of InnVest units over those periods.

Income taxes

For the nine months ended September 30, 2011, InnVest generated a deferred income tax recovery of $1.8 million as compared to a recovery of $8.5 million in 2010. The recovery in 2011 primarily reflects the estimated year-to-date losses in IOT which are recognized at the undistributed tax rate.

Net income

For the nine months ended September 30, 2011, InnVest recorded net income of $48.9 million, or $0.508 per unit diluted compared to a net loss of $144.5 million for the same period in 2010. Excluding non-cash charges relating to the IFRS implementation, deferred income taxes and the non-cash impairment charge, InnVest's net loss improved to $16.3 million compared to a loss of $18.7 million in the prior period.

As a result of the classification of units as financial liabilities for the majority of the comparative period, InnVest has not presented a per unit figure in the comparative period. Refer to "Adoption of IFRS".

Funds from operations

For the nine months ended September 30, 2011, InnVest generated FFO of $55.2 million ($0.565 per unit diluted) compared to $52.3 million in the prior period ($0.572 per unit diluted) primarily reflecting reduced interest expenses. The reduction in per unit results reflects the higher number of units outstanding following an equity offering completed in March 2011. See "Non-IFRS Financial Measures" for a reconciliation of IFRS net income to FFO.

Distributable income

For the nine months ended September 30, 2011, InnVest generated distributable income of $40.9 million ($0.425 per unit diluted) compared to $37.6 million in the prior year ($0.414 per unit diluted) primarily reflecting reduced interest expenses. See "Non-IFRS Financial Measures" for a reconciliation of IFRS net income to distributable income.

Distributions declared in the nine months ended September 30, 2011 totalled $34.8 million, or $0.3753 per unit (2010 – $33.2 million or $0.3753 per unit). The increase in total distributions paid reflects the higher number of units outstanding following an equity offering completed in March 2011.

Changes in financial condition

Operating activities

For the nine months ended September 30, 2011, cash generated by operating activities declined $11.0 million to $39.8 million compared to $50.8 million in the comparative period. The decline reflects a $12.2 million reduction in working capital during the period owing to the prior period improvement in working capital usage relating to higher accounts payable balances.

Financing activities

Financing activities reflect the regular payment of principal amortization on mortgages during the periods presented. The prior period included the repayment of $95.0 million of mortgage principal and yield maintenance and other fees in late August 2010.

Year-to-date, financing activities reflect net proceeds of $71.7 million from the equity and convertible debentures issued in March 2011 (gross proceeds of $75.2 million). The prior period included net proceeds of $71.7 million from convertible debentures issued in August 2010 (gross proceeds of $75.0 million) and the subsequent redemption of the $45.7 million of outstanding debentures in September 2010.

In the first quarter of 2011, InnVest repaid the $7.2 million balance previously drawn from its line of credit. Year-to-date, InnVest has also repaid $1.5 million of a bridge loan following a one-year extension of the loan. InnVest had repaid $1.0 million on the bridge loan in the first quarter of 2010.

Cash distributions for the nine months ended September 30, 2011 totalled $32.0 million (2010 – $31.5 million) which excludes distributions which are included on the condensed consolidated statement of net income as finance charges and distributions which were satisfied through InnVest's dividend reinvestment program ("DRIP").

Investing activities

Each year, InnVest sets aside between 3% and 5% of total hotel revenues at each hotel to replace furniture, fixtures and equipment and to fund capital improvements (the "FF&E reserve"). Capital expenditures during the nine months ended September 30, 2011 totalled $35.6 million (2010 – $24.3 million) compared to the FF&E reserve of $19.1 million (2010 – $19.0 million).

The incremental $16.5 million invested above the reserve reflects a number of profit-improving projects designed to increase cash flow and improve profitability by capitalizing on changing market conditions and the favorable locations of InnVest's properties. Significant investments year-to-date include the completion of renovations to the executive gold floor and rooms at the Fairmont Palliser in Calgary and room renovations at the Hilton Quebec City. Other on-going projects include brand upgrades at a number of our Holiday Inn and Delta hotels. InnVest expects that its capital expenditures for 2011 will approximate $50.0 million.

Year-to-date investing activities also reflect proceeds from a vendor-take-back mortgage receivable of $2.7 million following the sale of a property in 2009.

Quarterly results

Seasonality

InnVest's operations are seasonal and as such its results are not consistent throughout the year. Revenue earned from hotel operations fluctuates 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, and corporate and administrative expenses are fixed or virtually fixed.

	As reported pursuant to IFRS							As reported pursuant to Canadian GAAP
Quarter ended (unaudited)	**September 30 2011**	**June 30 2011**	**March 31 2011**	December 31 2010	September 30 2010	June 30 2010	March 31 2010	December 31 2009
Hotel revenues	**$ 174,832**	**$ 162,552**	**$ 128,319**	$ 148,429	$ 173,022	$ 163,260	$ 125,445	$ 141,668
Hotel operating income	**$ 50,774**	**$ 42,948**	**$ 15,748**	$ 27,511	$ 50,825	$ 43,658	$ 15,542	$ 28,005
Hotel operating income margin	**29.0%**	**26.4%**	**12.3%**	18.5%	29.4%	26.7%	12.4%	19.8%
Net income (loss)	**$ 66,929**	**$ 1,965**	**$ (20,035)**	$ 181,612	$ (8,518)	$ (41,317)	$ (98,710)	$ (24,802)
FFO	**$ 33,695**	**$ 24,498**	**$ (3,000)**	$ 8,644	$ 31,964	$ 24,256	$ (3,970)	$ 11,528
Distributable income (loss)	**$ 28,128**	**$ 19,487**	**$ (6,722)**	$ 4,179	$ 26,607	$ 19,054	$ (8,027)	$ 5,909
Distributions declared	**$ 11,701**	**$ 11,694**	**$ 11,371**	$ 11,197	$ 11,138	$ 11,090	$ 10,959	$ 10,940
Per unit – diluted:								
Net income (loss)	**$ 0.581**	**$ 0.021**	**$ (0.222)**	$ –	$ –	$ –	$ –	$ (0.290)
FFO	**$ 0.314**	**$ 0.240**	**$ (0.033)**	$ 0.096	$ 0.326	$ 0.264	$ (0.042)	$ 0.131
Distributable income (loss)	**$ 0.262**	**$ 0.192**	**$ (0.074)**	$ 0.046	$ 0.271	$ 0.205	$ (0.088)	$ 0.069
Trust units outstanding	**93,538,022**	**93,518,392**	**93,336,231**	89,474,691	89,046,308	88,975,426	87,639,949	87,498,354
Weighted average trust units outstanding	**93,532,175**	**93,425,837**	**90,266,593**	89,556,904	89,017,278	88,430,620	87,577,502	85,500,095
Total assets	**$ 1,589,573**	**$ 1,613,106**	**$ 1,636,500**	$ 1,598,837	$ 1,614,517	$ 1,691,345	$ 1,701,942	$ 1,950,209
Total long-term debt	**$ 808,303**	**$ 815,330**	**$ 821,504**	$ 840,930	$ 832,818	$ 934,969	$ 929,170	$ 940,608

Liquidity and capital resources

InnVest has several sources of liquidity including the following:

Cash generated from hotel operations
InnVest's operations are seasonal with the third quarter typically being the strongest earnings period given the higher level of business and leisure travel during these months. Over the annual period, InnVest anticipates generating HOI sufficient to fund distributions to unitholders, capital expenditures and debt service requirements.

Line of credit
InnVest has a line of credit of up to $40.0 million with a major banking institution to finance temporary shortfalls in cash resulting from business seasonality and working capital fluctuations. The credit facility may also be used to provide short-term financing in the event of the acquisition of a new hotel. At September 30, 2011, InnVest's line of credit is undrawn.

Issuing additional debt
InnVest also has the ability to raise funds by mortgaging its properties or by issuing either debt or convertible debt securities. InnVest typically uses long-term debt financing to refinance existing debt or to finance an acquisition. The choice of debt instrument used is dependent on then-current market conditions. The ability to secure debt financing on reasonable terms is ultimately dependent on market conditions and the lender's determination of InnVest's creditworthiness. At September 30, 2011, substantially all of InnVest's assets have been pledged as security under debt agreements.

Issuing additional equity securities
InnVest's listing on The Toronto Stock Exchange gives it the ability to access, subject to market conditions, additional equity through the issuance of additional units or other equity instruments. When issued, additional equity is most often used to finance acquisitions or repay debt. InnVest issued $25.2 million of equity and $50.0 million of convertible debentures during the first quarter of 2011 which are expected to be used to fund capital projects and potential future acquisitions. Following tax changes announced in July 2011, InnVest is restricted from issuing stapled securities, subject to certain exceptions (Refer to Corporate Developments).

Management believes that InnVest's credit facilities, cash on hand and expected cash flow from operations, when combined with the potential to sell assets or access debt and equity markets, will allow InnVest to meet all its financial commitments. If necessary, near term disruptions to operating earnings and cash flow could be addressed through reductions in discretionary capital allocation decisions such as capital investments above the FF&E reserve and/or distributions.

Cash on hand

At September 30, 2011, InnVest has cash on hand totalling $29.0 million, of which $4.6 million is restricted for the replacement of furniture, fixtures, and equipment and for capital improvements.

Each year, InnVest sets aside an FF&E reserve totaling between 3% and 5% of total hotel revenue. Capital expenditures during the nine months ended September 30, 2011 totalled $35.6 million (2010 – $24.3 million) compared to the FF&E reserve of $19.1 million (2010 – $19.0 million). Incremental capital above the FF&E reserve in 2011 was funded with cash on hand or available credit facilities.

The following chart shows the changes in the restricted FF&E reserve cash balance for the three and nine months ended September 30, 2011, along with the comparable period.

	Three months ended September 30, 2011	Three months ended September 30, 2010	**Nine months ended September 30, 2011**	Nine months ended September 30, 2010
Opening balance	**$ 4,361**	$ 3,482	**$ 3,831**	$ 3,815
FF&E reserve	**7,186**	7,101	**19,138**	18,965
Transferred from operating cash	**7,022**	3,500	**17,254**	5,211
Capital expenditures	**(13,943)**	(10,405)	**(35,597)**	(24,313)
Closing balance	**$ 4,626**	$ 3,678	**$ 4,626**	$ 3,678

Debt strategy

InnVest's debt strategy involves the use of three forms of debt: conventional property-specific secured mortgages, unsecured convertible debentures and secured floating rate bank financing. Management's objectives are to access the lowest cost of debt with the most flexible terms and to have a staggered debt maturity schedule to manage interest rate and refinancing risk.

Credit facility/bridge loan

InnVest's operations are seasonal (see Quarterly Results). InnVest's credit facility ensures that the seasonal fluctuation in cash flows will not affect its ability to operate in the normal course of business.

InnVest has a $40.0 million line of credit secured by 13 unencumbered assets. The credit facility expires in August 2012. The amount of the operating line is subject to a mortgageability test which is based on the operating results of the secured properties. Interest rates are based on the lesser of (i) Canadian prime rate plus 2.5% and (ii) the Canadian Bankers' Acceptance rate plus 3.5%. Based on the operating results of the secured properties for the four quarters ended September 30, 2011, InnVest qualifies for $39.2 million of availability under the line of credit. At September 30, 2011, no amount was drawn on the credit facility (December 31, 2010 – $7.2 million). Letters of credit totalling $3.6 million were drawn against the facility.

At September 30, 2011, InnVest has a $4.5 million (December 31, 2010 – $6.0 million) bridge loan secured by one hotel. In 2011, the bridge loan was extended to March 1, 2012. The bridge loan bears interest at the Canadian Bankers' Acceptance rate plus 3.5%.

Mortgages payable and convertible debentures

InnVest attempts to stagger the maturity of fixed term debt to minimize interest and financing risks.

At September 30, 2011, InnVest has mortgages payable of $812.6 million with a weighted average term of 2.1 years (December 2010 – 2.8 years) and a weighted average interest rate of 5.6% (December 2010 – 6.0%). Approximately 10.1% of InnVest's mortgage debt is at floating rate.

During the third quarter of 2011, InnVest extended the maturity of a mortgage previously scheduled to mature on September 20, 2011 until November 20, 2011. Management is finalizing the renewal of this $50.7 million mortgage at comparable terms and conditions. The mortgage is secured by two full service hotels.

Mortgage maturities in 2012 total $176.5 million at an average interest rate of 7.5%. This includes three separate maturities including one of approximately $164.1 million with a large Canadian institutional lender. Forty limited service hotels serve as collateral on this mortgage which matures in November 2012. InnVest also has one $146.0 million maturity in February 2012, which includes a one-year extension (to February 28, 2013), at InnVest's option, subject to certain minimum thresholds at the time of maturity. This mortgage, secured by seven full service hotels, has been reflected as a 2013 maturity. The interest rate for the renewal term would be based on the one-year Composite Swap Rate plus 1.85%, calculated as at February 28, 2012. Management has begun discussions for early extensions of both maturities.

At September 30, 2011, InnVest has approximately $131.5 million of mortgages secured by conduit financing maturing in 2014 and 2015.

InnVest has five series of fixed-rate convertible debentures which mature between 2013 and 2018. InnVest issued $50.0 million of Series F convertible debentures in March 2011. At September 30, 2011, convertible debentures outstanding totaled $306.3 million in (December 31, 2010 – $258.5 million).

InnVest expects to address all its maturities in the normal course of business. The global financial credit markets have experienced significant volatility since August 2008, which has impacted hotel lending. Prior to August 2011, credit spreads were showing signs of contraction. Following concerns raised by the European debt crisis in August 2011, credit spreads have begun to increase. Notwithstanding, the underlying bond yields have decreased significantly over the past three years such that the overall cost of debt remains attractive.

Leverage

InnVest is not permitted to exceed certain financial leverage amounts under the terms of the REIT and IOT Declarations of Trust. In order to address InnVest's transition to IFRS which came into effect January 1, 2011, InnVest amended the REIT Declaration of Trust and the IOT Declaration of Trust to adjust the maximum financial leverage ratio to 60% of gross asset value (75% including convertible debentures). This compares to the prior maximum ratio level of 50% of gross asset value (60% including convertible debentures). The financial ratio will be computed as of the last day of each financial year excluding any indebtedness under any operating line, non-interest bearing indebtedness, trade accounts payable and for greater certainty, deferred income tax liability. The amendments were made in light of the impact of the conversion to IFRS which resulted in the reduction of the book value of assets as well as the elimination of accumulated depreciation and amortization. Refer to "Adoption of IFRS" for a complete discussion.

At September 30, 2011, InnVest's leverage excluding and including convertible debentures was 45.8% (December 31, 2010 – 48.8%) and 63.0% (December 31, 2010 – 63.7%), respectively.

	September 30, 2011	
Total assets per consolidated balance sheet	$ 1,589,573	
Accumulated depreciation and amortization	214,410	
Future income tax asset and liability	(21,766)	
Gross asset value	$ 1,782,217	
Book value of mortgages and other indebtedness[1]	$ 817,145	45.8%
Convertible debentures[2]	306,338	17.2%
Total debt	$ 1,123,483	63.0%

1. *Adjusted to eliminate financing issuance costs.*
2. *Adjusted to face value.*

Contractual obligations repayment summary

Given available liquidity, access to capital and expectations of improving economic and operating trends, management expects to be able to fund all commitments in the normal course of business.

The following table summarizes InnVest's contractual obligations as at September 30, 2011.

	Remainder of 2011	2012	2013	2014	2015	2016 and thereafter	Total
Accounts payable and other liabilities	$ 77,327	$ –	$ –	$ –	$ –	$ –	$ 77,327
Mortgages payable – principal	58,491	200,881	161,985	301,165	72,900	17,223	812,645
Mortgages payable – interest	10,713	42,437	22,617	10,900	3,335	1,779	91,781
Bank indebtedness – principal	250	4,250	–	–	–	–	4,500
Bank indebtedness – interest	49	33	–	–	–	–	82
Convertible debentures – principal	–	–	74,980	70,000	–	161,358	306,338
Convertible debentures – interest	2,250	18,424	15,799	13,924	9,829	17,415	77,641
Long-term land leases	1,200	4,826	4,826	4,826	4,826	83,225	103,729
	$ 150,280	$ 270,851	$ 280,207	$ 400,815	$ 90,890	$ 281,000	$ 1,474,043

Distributions to unitholders

For the nine months ended September 30, 2011, distributions totalling $34.8 million were declared, of which $309, was distributed in units as part of the DRIP. In August 2011, InnVest suspended its DRIP until further notice. This represents year-to-date distributions declared of $0.3753 per unit, unchanged from the prior year. Subsequent to the end of the quarter, InnVest announced a reduction in distributions paid to unitholders to $0.40 per unit annually, as compared to the prior distribution level of $0.50 per unit annually. This equates to a monthly distribution of $0.0333 per unit beginning in November 2011. The Board of Trustees unanimously approved the reduction of distributions after careful consideration of the environment faced by InnVest and its desire to conserve liquidity to fund profit-improving capital investments throughout the portfolio.

For the twelve months ended September 30, 2011, InnVest's payout ratio was 102.0% or 101.1% on a cash basis (excluding the non-cash distributions made through the DRIP). The payout ratio reflects modest growth in distributable income achieved and the impact of a higher number of units outstanding.

Liquidity to fund distributions is generated from cash flow from operations, cash on hand, available bank operating lines and by the ability to finance certain unencumbered or under-leveraged assets. First and fourth quarter distributions are typically partially funded through cash on hand or InnVest's credit facility given the seasonality of revenues in contrast to costs which are fixed through the year.

	Twelve months ended September 30, 2011	Years ended December 31, 2010	2009	2008	2007	2006
Distributable income	**$ 45,072**	$ 41,813	$ 51,524	$ 85,540	$ 71,995	$ 62,771
Distributions	**45,963**	44,384	51,297	78,473	70,758	59,605
Distributable income (less than) in excess of distributions	**(891)**	(2,571)	227	7,067	1,237	3,166
Non-cash distributions made through the DRIP	**411**	1,688	2,756	13,234	10,606	4,166
Distributable income (less than) in excess of cash distributions	**$ (480)**	$ (883)	$ 2,983	$ 20,301	$ 11,843	$ 7,332
Payout ratios:						
Total distributions	**102.0%**	106.1%	99.6%	91.7%	98.3%	95.0%
Cash distributions (total distributions minus DRIP)	**101.1%**	102.1%	94.2%	76.3%	83.6%	88.3%

Distributions to unitholders are approved by InnVest's Board of Trustees. Each month, InnVest may distribute such percentage of its estimated distributable income as the Trustees determine in their discretion. 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 (see "Risks and Uncertainties").

Unit information

As part of the internal reorganization completed on December 31, 2010, the REIT distributed one IOT non-voting unit to unitholders for each one REIT unit held on December 31, 2010. Effective January 1, 2011 each issued and outstanding REIT unit trades together with an IOT non-voting unit on a "stapled" basis on the TSX. The REIT, through a subsidiary, holds all of the voting units of IOT. Refer to Corporate Developments for a description of the planned reorganization of InnVest in 2012.

At November 9, 2011, a total of 93,538,022 units of each of the REIT and IOT were outstanding. During the nine months ended September 30, 2011 and 2010, InnVest issued units as follows:

	2011	2010
Units outstanding, January 1	**89,474,691**	87,498,354
Units issued	**3,600,000**	–
Conversion of debentures	**371,221**	1,257,754
Dividend reinvestment plan	**47,609**	261,626
Executive compensation plan	**27,740**	22,215
Trustee compensation plan	**16,761**	6,359
Units outstanding, September 30	**93,538,022**	89,046,308

Units issuable on conversion of convertible debentures

The following table summarizes the number of units issuable based on the convertible debentures outstanding as at September 30, 2011.

Convrtible Debentures	Maturity date	Conversion strike price	Balance outstanding	Units to be issued upon conversion
Series B – 6.00%	May 31, 2013	$ 14.90	$ 74,980	5,032,214
Series C – 5.85%	August 1, 2014	$ 14.70	$ 70,000	4,761,904
Series D – 6.75%	March 31, 2016	$ 5.70	$ 36,358	6,378,596
Series E – 6.00%	September 30, 2017	$ 8.00	$ 75,000	9,375,000
Series F – 5.75%	March 30, 2018	$ 9.45	$ 50,000	5,291,005

On September 15, 2010, InnVest redeemed the remaining $45.7 million of its Series A – 6.25% Debentures which were scheduled to mature on April 15, 2011. On March 15, 2011, InnVest closed a bought deal of $50.0 million, 5.75% convertible unsecured subordinated debentures ("Series F – 5.75% Debentures") due March 30, 2018.

During the nine months ended September 30, 2011, $2.1 million Series D – 6.75% Debentures were converted to 371,221 units (2010 – $7.2 million converted to 1,257,754 units).

For each series of debentures, InnVest may elect, from time to time, to satisfy its obligation to pay interest by delivering units. Also, for each of its debentures, InnVest may, at its option, on not more than 60 days' and not less than 30 days' prior notice and subject to applicable regulatory approval, elect to satisfy its obligation to repay all or any portion of the principal amount of the debentures that are to be redeemed or that are to mature by issuing units. The number of units to be issued in respect of each debenture will be determined by dividing the principal amount by 95% of the volume-weighted average trading price of the units on the Toronto Stock Exchange for the 20 consecutive trading days ending on the fifth trading day preceding the date fixed for redemption or maturity, as the case may be.

Unvested units granted

During the nine months ended September 30, 2011, 27,740 units granted under the executive compensation program vested and were issued to plan participations (2010 – 22,215 units). Units granted vest equally on the third and fourth anniversary of the effective date of grant. At September 30, 2011, there were 113,566 (December 31, 2010 – 106,869) unvested executive units granted under the plan. Given current restrictions on the issuance of stapled securities during the Transition Period (see Corporate Developments), executive compensation units which vest during the Transition Period will be satisfied in cash as opposed to the issuance of units.

Non-IFRS financial measures

Included in this MD&A are certain non-IFRS financial measures, which are measures of InnVest's historical or future financial performance that are not calculated and presented in accordance with IFRS. These non-IFRS financial measures are unlikely to be comparable to similar measures presented by other entities. The following discussion defines non-IFRS measures used by InnVest and presents why management believes they are useful supplemental measures of InnVest's performance.

Hotel operating income ("HOI")

HOI is defined as hotel revenues less hotel expenses. HOI is a commonly used measure by lodging real estate owners which, when considered with IFRS measures, gives management a more complete understanding of property level results before debt service. It also facilitates comparisons between InnVest and its competitors. Management believes that HOI is one of InnVest's key performance indicators since it helps management, lenders and investors evaluate the ongoing hotel profitability. Management believes hotel operating income to be a meaningful indicator of hotel performance.

HOI has been calculated as follows:

	Three months ended September 30, 2011	Three months ended September 30, 2010	**Nine months ended September 30, 2011**	Nine months ended September 30, 2010
Hotel revenues	**$ 174,832**	$ 173,022	**$ 465,703**	$ 461,727
Hotel expenses	**124,058**	122,199	**356,233**	351,704
Hotel operating income	**$ 50,774**	$ 50,823	**$ 109,470**	$ 110,023

Funds from operations ("FFO")

FFO is a common measure of performance in the real estate investment trust industry. FFO is one measure used by industry analysts and investors in the determination of InnVest's valuation, its ability to fund distributions and investors' investment return requirements. As a result, InnVest believes that FFO is a useful supplemental measure of its 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 IFRS, and it adjusts for items included in IFRS 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.

FFO should not be considered a substitute for net income or cash flow from operating activities determined in accordance with IFRS.

InnVest presents FFO in accordance with Real Property Association of Canada's ("REALpac") White Paper on Funds From Operations issued in June 2010 except that InnVest excludes unusual items which are not in the normal course of business and are not expected to reoccur. InnVest's method of calculating FFO may be different from that of other organizations.

InnVest 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 writedown of assets held for sale as well as the impairment provision on hotel properties;

iv) Non-cash effect of units classified as financial liabilities under IFRS (includes distributions treated as interest expense and changes to fair value each reporting period); and

v) Non-recurring costs that may impact cash flow.

A reconciliation of IFRS net income (loss) to FFO is as follows:

	Three months ended September 30, 2011	Three months ended September 30, 2010	**Nine months ended September 30, 2011**	Nine months ended September 30, 2010
Net income (loss)	**$ 66,929**	$ (4,432)	**$ 48,859**	$ (144,458)
Add/(deduct):				
Depreciation and amortization	**22,668**	24,125	**71,134**	70,719
Deferred income tax expense (recovery)	**7,186**	(5,443)	**(1,815)**	(8,475)
Unrealized (gain) loss on liabilities presented at fair value	**(71,434)**	17,486	**(73,677)**	115,898
Finance costs – distributions	**46**	45	**2,392**	18,383
Gain on sale of asset held for sale	**–**	(327)	**–**	(327)
SIFT transition expenses	**589**	510	**589**	510
Writedown of hotel properties	**7,711**	–	**7,711**	–
FFO	**$ 33,695**	$ 31,964	**$ 55,193**	$ 52,250
FFO per unit:				
Basic	**$ 0.360**	$ 0.359	**$ 0.597**	$ 0.591
Diluted	**$ 0.314**	$ 0.324	**$ 0.565**	$ 0.572
Weighted average units outstanding:				
Basic	**93,532,175**	89,017,278	**92,420,163**	88,347,074
Diluted	**124,841,890**	111,335,287	**112,142,501**	98,099,766

Distributable income

Distributable income is commonly used in the real estate investment trust industry to measure performance. Distributable income is intended to approximate cash earnings. It is defined in InnVest's Declaration of Trust to mean net income of InnVest and its consolidated subsidiaries as reported in its condensed consolidated financial statements adjusted for:

i) Depreciation, amortization and accretion and future income tax (recovery) expense;

ii) Any gains or losses on the disposition of any real property;

iii) The reserve for replacement of furniture, fixtures and equipment and capital improvements; and

iv) Any other adjustment determined by the Trustees in their discretion.

A reconciliation of IFRS net income (loss) to distributable income is as follows:

	Three months ended September 30, 2011	Three months ended September 30, 2010	Nine months ended September 30, 2011	Nine months ended September 30, 2010
Net income (loss)	**$ 66,929**	$ (4,432)	**$ 48,859**	$ (144,458)
Add/(deduct):				
Depreciation and amortization	**22,668**	24,125	**71,134**	70,719
Deferred income tax expense (recovery)	**7,186**	(5,443)	**(1,815)**	(8,475)
Non-cash portion of convertible debenture interest and accretion	**952**	1,104	**2,828**	2,815
Non-cash portion of mortgage interest expense	**667**	640	**2,009**	1,534
Unrealized (gain) loss on liabilities presented at fair value	**(71,434)**	17,486	**(73,677)**	115,898
Finance costs – distributions	**46**	45	**2,392**	18,383
Gain on sale of asset held for sale	**–**	(327)	**–**	(327)
SIFT transition expenses	**589**	510	**589**	510
Writedown of hotel properties	**7,711**	–	**7,711**	–
FF&E Reserve	**(7,186)**	(7,101)	**(19,138)**	(18,965)
Distributable income	**$ 28,128**	$ 26,607	**$ 40,892**	$ 37,634
Distributable income per unit:				
Basic	**$ 0.301**	$ 0.299	**$ 0.442**	$ 0.426
Diluted	**$ 0.262**	$ 0.270	**$ 0.425**	$ 0.414
Weighted average units outstanding:				
Basic	**93,532,175**	89,017,278	**94,420,163**	88,347,074
Diluted	**124,841,890**	111,335,287	**112,142,501**	98,099,766

Distributable income is one measure used by industry analysts in the determination of InnVest's per unit value, its ability to fund distributions and investment returns for current or potential investors. Distributable income is also used by management and the Board of Trustees to determine the level of distributions to unitholders and also serves as an important measure for investors in their evaluation of the performance of management.

In addition, when evaluating acquisition opportunities, the distributable income to be generated by the asset is reviewed by management to determine whether a proposed acquisition will generate an increase in distributable income per unit. Therefore, distributable income is an important measure for management as a guideline through which operating and financial decisions are made and is an integral part of the investment decision for investors and potential investors.

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 InnVest's planned courses of action given management's judgment about the most probable set of economic conditions.

The reconciliation of cash flow from operating activities to distributable income is as follows:

	Three months ended September 30, 2011	Three months ended September 30, 2010	Nine months ended September 30, 2011	Nine months ended September 30, 2010
Cash flow from operating activities	**$ 31,859**	$ 31,416	**$ 39,831**	$ 50,758
Changes in non-cash working capital	**148**	2,202	**17,620**	5,426
Other	**3,307**	90	**2,579**	415
FF&E reserve	**(7,186)**	(7,101)	**(19,138)**	(18,965)
Distributable income	**$ 28,128**	$ 26,607	**$ 40,892**	$ 37,634

Related party transactions

Hotel management

On July 26, 2002, InnVest 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 InnVest. The current term of the Agreements expires June 25, 2017 and includes an additional renewal term for a five year extension, subject to the consent of Westmont and approval by InnVest. The Agreements are subject to non-compete 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 InnVest achieves distributable income in excess of $1.25 per unit. To date, no management incentive fees have been paid under the Agreements.

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 Agreements, 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 or a fixed percentage of HOI, subject to an annual minimum fee.

Total management and other fees paid to Westmont for the nine months ended September 30, 2011 were $13.2 million (2010 – $13.3 million). These fees represent approximately 66% (2010 – 66%) of total hotel management and other fees paid by InnVest to the four hotel management companies with which it partners over the period presented.

Risks and uncertainties

The achievement of InnVest's objectives is, in part, dependent on the successful mitigation of business risks identified. All real estate investments are subject to a degree of risk including changes in general economic and local market conditions, competition from other hotels, new supply, equity and credit markets conditions, fluctuations in interest costs, compliance with legislative requirements and various other factors.

There have been no changes to InnVest's assessment of its risk factors since December 31, 2010. For a discussion of risk factors that have been identified, readers should refer to InnVest's 2010 Annual Report and InnVest's latest Annual Information Form, both of which are available on SEDAR.

Critical accounting estimates

The significant accounting policies used in the preparation of these interim condensed consolidated financial statement are consistent with those reported in the unaudited interim condensed consolidated financial statements for the three months ended March 31, 2011. IFRS requires management to make estimates and assumptions concerning the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the balance sheet date and the reported amounts of revenue and expenses during the reporting period. Management uses its judgment and knowledge from past experience as a basis for estimates and other assumptions required in the preparation of the financial statements. Management's estimates and assumptions are evaluated and updated on a regular basis taking into account current market conditions. The actual results may materially differ, if management were to use different estimates and assumptions.

InnVest's MD&A for the three months ended March 31, 2011 contains a discussion of InnVest's significant accounting policies most affected by estimates and judgments used in the preparation of its financial statements, being its valuation of hotel properties, the allocation of fair value to hotel properties, the accounting policies relating to the expected useful life of hotel properties, the valuation of financial instruments and defined benefit pension plans. Management has determined that as at September 30, 2011, there is no change to its assessment of its significant accounting policies most affected by estimates and judgments as detailed in the MD&A for the three months ended March 31, 2011.

Future accounting changes

InnVest has reviewed new and revised accounting pronouncements that have been issued but are not yet effective and determined that the following may have an impact on its condensed consolidated financial statements and note disclosures:

IFRS 9 – Financial instruments – classification and measurement

In November 2009, IFRS 9 was issued which contained requirements for financial assets. In October 2010, requirements for financial liabilities were added to IFRS 9. IFRS 9 will replace IAS 39 – *Financial Instruments: Recognition and Measurement* in its entirety. IFRS 9 uses a single approach to determine whether a financial asset or liability is measured at amortized cost or fair value, replacing the multiple rules in IAS 39. For financial assets, the approach in IFRS 9 is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. The new standard also requires a single impairment method to be used, replacing the multiple impairment methods in IAS 39. For financial liabilities measured at fair value, fair value changes due to changes in a company's credit risk are presented in other comprehensive income, instead of net income, unless this would create an accounting mismatch. An accounting mismatch may occur when financial liabilities that are measured at fair value are managed with assets that are measured at fair value through profit and loss. A mismatch could arise because the entire change in the fair value of the financial assets would be presented in net income but a portion of the change in the fair value of the related financial liabilities would not. IFRS 9 is effective for annual periods beginning on or after January 1, 2013. Earlier application is permitted. InnVest is currently evaluating the impact of IFRS 9 on its condensed consolidated financial statements.

IAS 28 and IFRS 11 – Joint ventures

IAS 28 was amended in 2011 which prescribes the accounting for investments in associates and sets out the requirements for the application of the equity method when accounting for investments in associates and joint ventures. This will affect the accounting for jointly controlled entities which InnVest currently proportionately consolidates under IFRS. IFRS 11 was issued in 2011 and establishes principles for financial reporting by parties to a joint arrangement. IAS 28 and IFRS 11 ares effective for annual periods beginning on or after January 1, 2013. Earlier application is permitted. InnVest is currently evaluating the impact of IAS 28 and IFRS 11 on its condensed consolidated financial statements.

IFRS 10 – Consolidated financial statements

IFRS 10 establishes principles for the presentation and preparation of consolidated financial statements when an entity controls one or more other entities. IFRS 10 supersedes IAS 27 "Consolidated and Separate Financial Statements" and SIC-12 "Consolidation — Special Purpose Entities" and is effective for annual periods beginning on or after January 1, 2013. Earlier application is permitted. InnVest is currently evaluating the impact of this standard on its condensed consolidated financial statements.

IFRS 12 – Disclosure of interests in other entities

IFRS 12 applies to entities that have an interest in a subsidiary, a joint arrangement, an associate or an unconsolidated structured entity. IFRS 12 is effective for annual periods beginning on or after January 1, 2013. Earlier application is permitted. InnVest is currently evaluating the impact of this standard on its condensed consolidated financial statements.

IFRS 13 – Fair value measurements

IFRS 13 defines fair value, sets out a single IFRS framework for measuring fair value and requires disclosures about fair value measurements. The IFRS 13 applies to IFRSs that require or permit fair value measurements or disclosures about fair value measurements (and measurements, such as fair value less costs to sell, based on fair value or disclosures about those measurements), except in specified circumstances. IFRS 13 is to be applied for annual periods beginning on or after January 1, 2013. Earlier application is permitted. InnVest is currently evaluating the impact of this standard on its condensed consolidated financial statements.

IAS 1 – Presentation of financial statements

IAS 1 prescribes the basis for presentation of financial statements. Recent amendments retain the option to present profit or loss and other comprehensive income either in one continuous statement or in two separate but consecutive statements. Items of other comprehensive income are required to be grouped into those that will and will not be subsequently reclassified to profit or loss. Tax on items of other comprehensive income is required to be allocated on the same basis. The measurement and recognition of items of profit or loss and other comprehensive income are not affected by the amendments.

These amendments are to be applied for annual periods beginning on or after January 1, 2013 with retroactive applicable required with certain exceptions. Earlier application is permitted. InnVest is currently evaluating the impact of this standard on its condensed consolidated financial statements.

IAS 19 – Employee benefits

IAS 19 sets out the accounting and disclosure requirements for employee benefits. Recent amendments require the recognition of changes in the defined benefit obligation and in the plan assets when those changes occur, eliminating the corridor approach and accelerating the recognition of past service costs. Changes in the defined benefit obligation and plan assets are disaggregated into three components: service costs, net interest on the net defined benefit liabilities (assets) and remeasurements of the net defined benefit liabilities (assets). Service costs and net interest are recorded in the statement of operations and remeasurements are a component of other comprehensive income.

These amendments are to be applied for annual periods beginning on or after January 1, 2012. Earlier application is permitted. InnVest is currently evaluating the impact of this standard on its condensed consolidated financial statements.

Controls and procedures

Management of InnVest is responsible for establishing and maintaining adequate internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external reporting purposes in accordance with IFRS. In accordance with National Instrument 52-109 – *Certification of Disclosure in Issuers' Annual and Interim Filings*, the President and Chief Executive Officer and the Chief Financial Officer and Corporate Secretary have assessed, or caused an assessment to be made under their direct supervision, of the design and operating effectiveness of InnVest's internal controls over financial reporting as at September 30, 2011, and based on that assessment have concluded that InnVest's internal controls over financial reporting were appropriately designed and were operating effectively.

During the three months ended September 30, 2011 there were no changes in InnVest's internal controls over financial reporting which have significantly affected, or are reasonably likely to significantly affect, InnVest's internal controls over financial reporting. Significant changes implemented effective January 1, 2011 included the following:

Conversion to IFRS

The conversion to IFRS from Canadian GAAP as at January 1, 2011 impacts the way InnVest presents its financial results and the accompanying disclosures. Management has evaluated the impact of the conversion on its financial reporting systems, processes and controls. The most significant updates to internal control processes address senior management oversight on the development of key assumptions for impairment testing, changes to PP&E component accounting and the compilation of data for new disclosure requirements.

Maintenance of qualifying REIT status under the SIFT rules

Effective January 1, 2011, internal control processes were put in place to maintain InnVest's status as a qualifying REIT under the SIFT rules.

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/or (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.

Condensed consolidated balance sheets

(in thousands of Canadian dollars) (unaudited)	**September 30, 2011**	December 31, 2010	January 1, 2010
		(Note 3)	(Note 3)
ASSETS			
Current assets			
Cash	**$ 24,391**	$ 9,001	$ 101,054
Accounts receivable	**36,589**	28,992	26,181
Prepaid expenses and other assets	**14,535**	8,345	7,962
	75,515	46,338	135,197
Restricted cash	**4,626**	3,831	3,815
Hotel properties (Note 4)	**1,456,810**	1,498,485	1,565,564
Other real estate properties (Note 5)	**18,203**	15,666	14,482
Intangible assets (Note 6)	**15,892**	17,529	18,528
Deferred income tax asset (Note 12)	**18,527**	16,988	–
	$ 1,589,573	$ 1,598,837	$ 1,737,586
LIABILITIES			
Current liabilities			
Bank indebtedness (Note 7)	**$ 4,500**	$ –	$ –
Accounts payable and accrued liabilities	**77,548**	78,236	67,764
Distributions payable	**3,901**	3,731	3,649
Current portion of long-term debt (Note 8)	**83,784**	82,808	21,326
	169,733	164,775	92,739
Long-term debt (Note 8)	**724,519**	758,122	931,685
Other long-term obligations (Note 9)	**14,626**	12,335	11,129
Convertible debentures (Note 10)	**287,878**	241,472	225,918
Deferred income tax liability (Note 12)	**3,239**	3,515	227,052
	1,199,995	1,180,219	1,488,523
Future distributions liability (Note 3)	**–**	–	467,912
Unitholders and other liabilities (Note 14)	**43,331**	111,501	3,990
	43,331	111,501	471,902
UNITHOLDERS' EQUITY (DEFICIT)	**346,247**	307,117	(222,839)
	$ 1,589,573	$ 1,598,837	$ 1,737,586

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

Condensed consolidated statements of net income (loss) and comprehensive income (loss)

(in thousands of Canadian dollars, except per unit amounts) (unaudited)	Three months ended September 30, 2011	Three months ended September 30, 2010	Nine months ended September 30, 2011	Nine months ended September 30, 2010
		(Note 3)		*(Note 3)*
Total revenues (Note 19)	$ 178,463	$ 176,951	$ 475,724	$ 471,474
Hotel revenues	$ 174,832	$ 173,022	$ 465,703	$ 461,727
Hotel expenses				
Operating expenses (Note 17)	104,396	102,277	299,368	293,580
Property taxes, rent and insurance	13,268	13,512	39,834	41,005
Management fees (Note 17)	6,394	6,410	17,031	17,119
	124,058	122,199	356,233	351,704
Hotel operating income	50,774	50,823	109,470	110,023
Other expenses (income)				
Interest on mortgages and other debt	12,120	14,447	38,441	43,281
Convertible debentures interest and accretion	5,550	5,157	16,031	14,236
Corporate and administrative (Note 17)	1,447	1,556	4,136	4,826
Other business income, net (Note 20)	(1,548)	(1,649)	(3,596)	(3,739)
Other income	(121)	(469)	(366)	(648)
Depreciation and amortization	22,668	24,125	71,134	70,719
Writedown of hotel properties (Note 4)	7,711	–	7,711	–
	47,827	43,167	133,491	128,675
Income (loss) before the undernoted:	2,947	7,656	(24,021)	(18,652)
Finance costs – distributions	(46)	(45)	(2,392)	(18,383)
Unrealized gain (loss) on liabilities presented at fair value (Note 21)	71,434	(17,486)	73,677	(115,898)
Income (loss) before income tax expense (recovery)	74,335	(9,875)	47,264	(152,933)
Income tax expense (recovery) (Note 12)				
Current	220	–	220	–
Deferred	7,186	(5,443)	(1,815)	(8,475)
	7,406	(5,443)	(1,595)	(8,475)
Net income (loss) and comprehensive income (loss)	$ 66,929	$ (4,432)	$ 48,859	$ (144,458)
Net income per unit (Note 16)				
Basic	$ 0.716	–	$ 0.529	–
Diluted	$ 0.581	–	$ 0.508	–

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

Condensed consolidated statements of unitholders' equity (deficit)

(in thousands of Canadian dollars) *(unaudited)*	Cumulative net loss	Cumulative distributions	Deficit	Units in $	Total
Balance January 1, 2010 (Note 3)	$ (222,839)	$ –	$ (222,839)	$ –	$ (222,839)
CHANGES DURING THE PERIOD					
Reclassification to equity (Note 3)	–	–	–	568,550	568,550
Net loss and comprehensive loss	(144,458)	–	(144,458)	–	(144,458)
Distributions to unitholders	–	(14,791)	(14,791)	–	(14,791)
Redemption and cancellation of debentures	2,094	–	2,094	–	2,094
Distribution reinvestment plan units issued	–	–	–	283	283
Conversion of debentures	–	–	–	152	152
Trustee compensation	–	–	–	38	38
Balance September 30, 2010	**$ (365,203)**	**$ (14,791)**	**$ (379,994)**	**$ 569,023**	**$ 189,029**
Balance December 31, 2010 (Note 3)	**$ (187,679)**	**$ (25,930)**	**$ (213,609)**	**$ 520,726**	**$ 307,117**
CHANGES DURING THE PERIOD					
Net income and comprehensive income	**48,859**	**–**	**48,859**	**–**	**48,859**
Distributions to unitholders	**–**	**(32,510)**	**(32,510)**	**–**	**(32,510)**
Distribution reinvestment plan units issued	**–**	**–**	**–**	**273**	**273**
Conversion of debentures	**–**	**–**	**–**	**1,803**	**1,803**
Issue of new units, net	**–**	**–**	**–**	**20,405**	**20,405**
Vested executive compensation	**–**	**–**	**–**	**186**	**186**
Trustee compensation	**–**	**–**	**–**	**114**	**114**
Balance September 30, 2011	**$ (138,820)**	**$ (58,440)**	**$ (197,260)**	**$ 543,507**	**$ 346,247**

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

Condensed consolidated statements of cash flows

(in thousands of Canadian dollars) *(unaudited)*	**Nine months ended September 30, 2011**	Nine months ended September 30, 2010
		(Note 3)
OPERATING ACTIVITIES		
Net income (loss)	**$ 48,859**	$ (144,458)
Add (deduct)		
Depreciation and amortization	**71,134**	70,719
Writedown of hotel properties	**7,711**	–
Finance costs – distributions	**2,392**	18,383
Unrealized (gain) loss on liabilities presented at fair value (Note 20)	**(73,677)**	115,898
Interest on mortgages and other debt	**38,441**	43,281
Convertible debentures interest and accretion	**16,031**	14,236
Interest expense paid	**(51,925)**	(53,438)
Deferred income tax recovery	**(1,815)**	(8,475)
Non-cash executive and trustee compensation	**300**	38
Changes in non-cash working capital	**(17,620)**	(5,426)
Cash generated from operations	**39,831**	50,758
FINANCING ACTIVITIES		
Repayment of long-term debt	**(21,572)**	(117,948)
Proceeds from long-term debt	**–**	3,100
Issue of new stapled units, net of issuance costs	**23,942**	–
Issue of convertible debentures, net of issuance costs	**47,725**	71,688
Redemption and cancellation of convertible debentures	**–**	(45,678)
Unit distributions	**(32,032)**	(31,536)
Repayment of operating loan	**(7,200)**	–
Repayment of bridge loan	**(1,500)**	(1,000)
Cash generated (utilized) from financing activities	**9,363**	(121,374)
INVESTING ACTIVITIES		
Capital expenditures on hotel properties	**(35,597)**	(24,190)
Change in intangible assets	**(112)**	(662)
Proceeds from mortgage receivable	**2,700**	–
Deposit on lease arrangement	**–**	2,013
Proceeds from sale of discontinued asset, net of costs and mortgage receivable	**–**	6,031
(Increase) decrease in restricted cash	**(795)**	137
Cash utilized in investing activities	**(33,804)**	(16,671)
Increase (decrease) in cash during the period	**15,390**	(87,287)
Cash, beginning of the period	**9,001**	101,054
Cash, end of the period	**$ 24,391**	$ 13,767

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

Notes to condensed consolidated financial statements

September 30, 2011 (all Canadian dollar amounts are in thousands, except unit and per unit amounts) (unaudited)

Note 1 | Basis of presentation

InnVest Real Estate Investment Trust (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. As at September 30, 2011, the REIT owned 144 Canadian hotels operated under international brands. Effective December 31, 2010, the REIT leased its hotels to InnVest Operations Trust ("IOT"), an unincorporated open-ended taxable investment trust. IOT directly and indirectly holds all of the hotel operating assets, earns revenues from hotel customers and pays rent to the REIT. IOT also indirectly holds a 50% interest in Choice Hotels Canada Inc. ("CHC"). The REIT and IOT are collectively referred to as "InnVest". Each issued and outstanding unit of the REIT trades together with a non-voting unit of IOT as a stapled unit ("InnVest Unit") on the Toronto Stock Exchange (the "TSX") under the symbol INN.UN. All non-voting units of IOT are owned by the unitholders of the REIT. The REIT owns all of the voting units of IOT, representing 1.5% of total units of IOT.

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 year.

Note 2 | Significant accounting policies

a) Statement of compliance

Beginning January 1, 2011, InnVest prepares its annual consolidated financial statements in accordance with International Financial Reporting Standards ("IFRS"). These financial statements reflect part of the period covered by InnVest's first financial statements for the year ending December 31, 2011 and are covered by IFRS 1 – *First-Time Adoption of IFRS ("IFRS 1")*. These interim consolidated financial statements have been prepared in accordance with International Accounting Standard ("IAS") 34 – *Interim Financial Reporting* as issued by the International Accounting Standards Board ("IASB") using the accounting policies InnVest expects to adopt in its consolidated financial statements for the year ending December 31, 2011. These interim consolidated financial statements may not include all of the information required in annual financial statements in accordance with IFRS. InnVest's consolidated financial statements for the year ending December 31, 2011 will be its first annual financial statements prepared in compliance with IFRS.

Note 3 summarizes the changes resulting from the transition to IFRS affecting the previously reported balance sheet, equity, net income (loss) and comprehensive income (loss) and cash flows.

b) Principles of consolidation

The consolidated financial statements include the accounts of the REIT and IOT and their subsidiaries, and the proportionate share of the assets, liabilities, revenues and expenses of a joint venture, IOT's 50% interest in CHC and a co-tenancy that owns one of the REIT's hotels.

c) Comprehensive income (loss)

InnVest recognizes comprehensive income (loss) which represents changes in the unitholders' equity during a period arising from transactions and other events with non-owner sources. For the three and nine months ended September 30, 2011 and 2010, there is no difference between InnVest's Condensed Consolidated Statement of Net Income (Loss) and its Statement of Comprehensive Income (Loss) and there is no accumulated other comprehensive income (loss) as at September 30, 2011 and 2010.

d) Hotel properties

Hotel properties, consisting of land, buildings and furniture, fixtures and equipment, are stated at deemed cost and cost less accumulated depreciation. Hotel properties are reviewed periodically for impairment as described in Note 2 (g). In accordance with IFRS 1's Fair Value as Deemed Cost Election (refer to Note 3), land and buildings were re-valued at January 1, 2010 at fair value.

e) Other real estate properties

Other real estate properties include office and retail properties as well as a retirement residence. Office and retail properties include land and buildings. The retirement residence includes land, buildings and furniture, fixtures and equipment.

The buildings and furniture, fixtures and equipment are stated at deemed cost and cost less accumulated depreciation and are reviewed periodically for impairment as described in Note 2 (g). In accordance with the IFRS 1's Fair Value as Deemed Cost Election (refer to Note 3), land and buildings were re-valued at January 1, 2010 at fair value.

f) Depreciation

Depreciation for Hotel Properties and Other Real Estate Properties is provided on a straight-line basis over their estimated useful life:

Buildings	40 years
Furniture, fixtures and equipment	7 years
Finishes	15 years
Electrical and mechanical	30 years

g) Impairment of long-lived assets

Management reviews long-lived assets on a quarterly basis for impairment triggers and impairment to determine if any events or changes in circumstances exist that would indicate that the carrying amount of an asset may not be recoverable over time. Impairment assessments are conducted at the level of cash generating units ("CGUs"), with each hotel or other real estate property representing a separate CGU.

If the carrying value exceeds the estimated recoverable amount, the asset is written down to its recoverable amount. Recoverable amount is the greater of fair value less costs to sell and value in use. Value in use is assessed based on estimated future cash flows discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Impairments are reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation, if no impairment had been recognized.

h) Intangible assets

Intangible Assets include licence contracts related to the joint venture interest in CHC, and are recorded at the value attributed to the discounted cash flow of the expected earnings stream under the contract terms at the time of acquisition of CHC. This amount is amortized on a straight-line basis over the average life or expected renewal life of the contracts, which is estimated to be twenty years.

Intangible assets also include franchise rights with various brands, which are amortized on a straight-line basis over the term of the agreement.

i) Provisions

Provisions are recognized on the balance sheet when InnVest has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of economic benefits will be required and a reliable estimate of the amount payable can be made. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, when appropriate, the risks specific to the liability.

InnVest recognises decommissioning and restoration provisions related to various environmental obligations for certain properties where the quantum of such costs and the timing for settlement are reasonably determinable. The obligations relate to the eventual removal of asbestos, underground storage tanks and polychlorinated biphenyls ("PCBs") and eventual remediation of land contamination. InnVest has recorded a liability and corresponding asset for the estimated future decommissioning and restoration costs, discounted to present value. Such estimates are subject to revisions based on changes in laws and regulations or changes in inputs to the decommissioning model.

j) Guarantees

InnVest is required to disclose its obligations undertaken in issuing certain guarantees. Where InnVest expects to make a payment in respect of any guarantee, a liability will be recognized to the extent that one has not yet been recognized. At September 30, 2011, December 31, 2010 and January 1, 2010, there were no such obligations.

k) Financial instruments

Financial assets and financial liabilities are initially recognized at fair value. Measurement in subsequent periods depends on whether the financial instrument has been classified as fair value through profit or loss ("FVTPL"), available-for-sale, held-to-maturity, loans and receivables, or other liabilities. Subsequent measurement for financial assets and liabilities is based on either fair value or amortized cost using the effective interest method ("EIM"), depending upon their classification. Any financial asset or financial liability can be classified at FVTPL as long as the fair value is reliably determinable.

The following summarizes the classification and measurement InnVest has elected to apply to each of its significant categories of financial instruments:

	Classification	Measurement
Financial assets		
Cash and restricted cash	Loans and receivables	Amortized cost
Accounts receivable	Loans and receivables	Amortized cost
Mortgages receivable	Loans and receivables	Amortized cost
Financial liabilities		
Bank indebtedness	Other liabilities	Amortized cost
Accounts payable and accrued liabilities	Other liabilities	Amortized cost
Operating line	Other liabilities	Amortized cost
Mortgages payable	Other liabilities	Amortized cost
Convertible debentures – host instrument	Other liabilities	Amortized cost
Unitholders and other liabilities	FVTPL	Fair value
Future distributions liability	FVTPL	Fair value

Transaction costs, other than those related to financial instruments measured at fair value (expensed as incurred), are added to the fair value of the financial asset or financial liability on initial recognition and amortized using the EIM.

Unitholders and other liabilities consist of the fair value of the non-voting units of IOT, the fair value of InnVest's exchangeable units, the fair value of the conversion feature associated with InnVest's convertible debentures and the fair value of the unvested executive compensation, which are further defined below and in Note 2 (o), (p) and (q).

Derivatives embedded in other financial instruments or contracts are separated from their host contracts and are measured at fair values, with changes therein recognized in the consolidated statement of income (loss) and comprehensive income (loss). InnVest has concluded that its convertible debentures include embedded derivatives under IFRS. InnVest has separated the conversion option component for each of its series of convertible debentures and measures such component at fair value at each reporting date.

The fair value of a financial instrument is the amount of consideration that could be agreed upon in an arm's-length transaction between knowledgeable, willing parties who are under no compulsion to act. In certain circumstances, however, the initial fair value may be based on other observable current market transactions in the same instrument, without modification, or on a valuation technique using market based inputs.

Except as noted below, the carrying value of InnVest's financial assets and financial liabilities approximate their fair values because of the short period until receipt or payment of cash. The fair values of long-term debt are based on the current market conditions for mortgages with similar terms and conditions. The fair value of the convertible debentures is based on the market rates for the convertible debentures at each reporting period.

Fair value measurements recognized in the balance sheet are categorized using a fair value hierarchy that reflects the significance of inputs used in determining the fair values:

i) Level 1 – derived from quoted prices (unadjusted) in active markets for identical assets or liabilities that InnVest has the ability to access at the measurement date;

ii) Level 2 – derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e.: as prices) or indirectly (i.e.: derived from prices); and

iii) Level 3 – derived from inputs for the asset or liability that is not based on observable market data (unobservable inputs).

Each type of fair value is categorized based on the lowest level input that is significant to the fair value measurement in its entirety.

l) Defined benefit pension plans

InnVest maintains defined benefit pension plans for the benefit of management employees and non-union non-management employees of certain hotels acquired in 2006 and 2007.

The cost of pensions and other retirement benefits earned by employees is actuarially determined using the projected benefit method pro-rated on service and management's best estimate of expected plan investment performance, salary escalation, retirement ages of employees and expected health care costs.

For the purpose of calculating the expected return on plan assets, those assets are valued at fair value. The excess of the net actuarial gain or loss over 10% of the greater of the benefit obligation and the fair value of plan assets, at the beginning of the year, is amortized over the remaining service period of active employees. The average remaining service periods of the active employees covered by the pension plan for the benefit of management employees and non-union non-management employees are 14 years and 16 years, respectively.

m) Revenue recognition

Hotel revenue

Revenues from hotel operations are recognized when services are provided and ultimate collection is reasonably assured.

Franchise revenue

Monthly revenues from licence contracts are based on gross room revenue as reported by the franchisees and are recorded when earned with an appropriate provision for estimated uncollectible amounts. Initial franchise fees are recorded as income when the cash has been received and upon execution of binding contracts.

Retail, office and retirement residence revenue

InnVest retains all the risks and benefits of ownership of its other real estate properties and therefore accounts for leases with its tenants as operating leases. Rental revenue from retail, office and retirement residence leases includes all amounts earned from tenants related to lease agreements and revenue is recognized on a straight-line basis.

n) Deferred income taxes

For InnVest's taxable subsidiary entities, income taxes are accounted for using the liability method, whereby deferred income tax assets and liabilities are determined based on differences between the carrying amount of the balance sheet items and their corresponding tax values as well as unused tax losses and tax credits. Deferred income taxes are computed using enacted or substantively enacted income tax rates for the years in which deferred tax balances are expected to reverse.

A deferred tax asset is recognized only to the extent that it is probable that future taxable profits will be available against which the asset can be utilized. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and InnVest intends to settle its current assets and liabilities on a net basis.

o) Executive compensation plan

The senior executives participate in an incentive plan that involves the grant of InnVest Units which vest over time. A unit granted entitles the holder to receive, on the vesting date, the then current fair market value of the InnVest 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 InnVest Units. The payment will be satisfied through the issuance of InnVest Units.

The benefit resulting from the issuance of InnVest Units under this plan is recorded as compensation expense, on a straight-line basis over the vesting period. Units granted (based on vesting schedule accrual) are initially presented as liabilities based on the fair value of the InnVest Units on the date of grant and are subsequently measured at each reporting date at their fair value with changes in the carrying amount recognized as compensation expense in net income (loss) for the period. Upon issuance of InnVest Units (following the satisfaction of all vesting conditions), the liability is reclassified to equity at the then-current fair value.

p) Exchangeable units

InnVest has Exchangeable Units, exchangeable into InnVest Units on a one-for-one basis. The Exchangeable Units largely have the same features as InnVest's Units but their features are not identical. The Exchangeable Units are classified as liabilities. The distributions on the Exchangeable Units are recognized in the consolidated statements of income (loss) and comprehensive income (loss) as finance costs under IFRS. The Exchangeable Units are measured at each reporting date at their fair value with changes in the carrying amount recognized in net income (loss) for the period.

q) IOT non-voting units

After giving effect to the reorganization of InnVest on December 31, 2010, InnVest unitholders' hold an interest in IOT through ownership of the IOT non-voting units. Refer to Note 1. Under IFRS, this ownership position is presented as a liability. Subsequent to initial measurement, IOT non-voting units are measured at fair value at each reporting date with changes in the carrying amount recognized in net income (loss) for the period. The distributions to IOT unitholders are recognized in the consolidated statements of income (loss) as finance costs.

r) Significant accounting judgments, estimates and assumptions

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

Significant accounting judgments:

Identification of impairment indicators

Management is required to test for impairment when there is an indicator of impairment whereby the carrying value of a property may not be recoverable. Management has established a methodology for identifying indicators of impairment which includes looking at changes in net operating performance, occupancy levels and other factors on a property-by-property basis. The identification of impairment indicators will affect whether management will test for the impairment of a property at each balance sheet date.

Degree of componentization of hotel property

Each component of a hotel property with a cost that is significant in relation to the total cost of the hotel property must be depreciated separately. Upon conversion to IFRS, management undertook a process to (i) identify hotel property components, (ii) allocate the deemed cost of the hotel property to each component and (iii) determine the appropriate depreciation period for each component. The identification, allocation and depreciation period chosen for each component of hotel properties affects the depreciation expense in each accounting period.

Significant accounting estimates and assumptions:

Impairment

Impairment testing of hotel properties requires management to assess the property's ability to recover its book value through the normal course of operations and evaluate the value in use of the property. Significant assumptions are used in the assessment of fair value and impairment including estimates of future operating cash flows, the time period over which they will occur, an appropriate discount rate, appropriate growth rates (revenues and costs) and changes in market valuation parameters. Management considers various factors in its assessment including the historical performance of hotel properties, expected trends in each specific market including new or expected new hotel supply as well as local and macroeconomic conditions.

Fair value of hotel properties

Management was required to make a number of assumptions and estimates in calculating the deemed cost of hotel properties at conversion to IFRS. Management's valuation methodology included the use of discounted cash flow models, the direct capitalization approach and a per room valuation approach.

Determination of useful lives of hotel property components

Management determines the estimated useful lives and related depreciation charge for each hotel property component. InnVest depreciates these assets using the straight-line method over their estimated economic or useful lives. The depreciation method and estimates of useful life selected impacts the level of depreciation expense recognized in InnVest's operating results. In establishing useful lives, management considered its capital maintenance plans and consulted with third party and internal construction experts.

Valuation of financial instruments and liabilities

Management makes estimates and assumptions relating to the fair value measurement of its Exchangeable Units, unit executive incentive plans, the convertible debenture conversion feature, the IOT units and the fair value disclosed of the convertible debentures, and mortgages payable. The critical assumptions and estimates underlying the fair value measurements and disclosures include current market interest rates and credit spreads reflected in comparable financial instruments and InnVest's own credit risk.

In determining the fair value of mortgages and convertible debentures, management uses internally developed models to discount future payments based upon a current market rate for debt instruments with similar terms and risks. The selection of the applicable market rate is based on management experience in obtaining similar financing as well as current credit market conditions. Changing credit market conditions, including movements in interest rates and credit spreads, may impact underlying estimates and, in turn, the fair value of debt instruments.

The fair value of exchangeable units, unit executive incentive plans and the convertible debenture conversion feature use quoted market prices based on the price of InnVest Units.

The determination of the fair value of the IOT units requires significant judgement and estimation. In performing this valuation, InnVest assesses the value of IOT based on the values of its assets and liabilities, with consideration given to the net asset value on a consolidated basis, the trading price of the stapled unit and various other factors. In determining the allocation of the net asset value between the REIT and IOT entities, the judgements and estimates include:

- Currents assets, restricted cash, current liabilities, other long-term obligations and future income taxes are valued at book values, which approximate their fair values.
- The inter-entity balances of outstanding lease payments between REIT and IOT is adjusted to take into account the expected net cash flows for IOT to June 30, 2012 at which time the current stapled structure is expected to change.
- The components of hotel properties and non-hotel real estate under the REIT, which excludes the hotel chattels that are owned by IOT, are estimated using current trends in the market for capitalization rates, hotels sales comparatives and previously determined discounted cash flows adjusted for the change in conditions as at the reporting date.
- The fair value of chattels is estimated at their book values as the declines from cost are fairly represented by the accounting depreciation rates.
- The interest in CHC is valued at its expected annual cash flow generated divided by a market capitalization rate for similar businesses.
- The fair value of long-term debt is determined by discounting the contractual cash flow streams at current interest rates for similar debts for their respective remaining terms.
- Convertible debentures are adjusted to reflect the difference between book values and the closing prices at the reporting date for the various series.

The resulting allocation of IOT's net assets as a percentage of the consolidated net assets of InnVest (adjusted for the 1.5% of IOT owned by a subsidiary of the REIT) multiplied by the number of Stapled Units outstanding at the reporting date and the closing price of the Stapled Units, is recorded as a liability.

Defined benefit pension plans

InnVest maintains defined benefit pension plans for the benefit of management employees and non-union non-management employees of certain hotels acquired in 2006 and 2007. The cost of defined benefit pension plans and other post-employment benefits is determined using actuarial valuations. The actuarial valuation involves making assumptions about expected plan investment performance, salary escalation, the retirement ages of employees and expected health care costs as at the date of its actuarial valuation. Changes in estimates about plan investment performance, as impacted by current market conditions, may impact future pension costs.

s) Future accounting changes

Financial instruments – classification and measurement ("IFRS 9")

In November 2009, IFRS 9 was issued which contained requirements for financial assets. In October 2010, requirements for financial liabilities were added to IFRS 9. IFRS 9 will replace IAS 39 – *Financial Instruments: Recognition and Measurement* in its entirety. IFRS 9 uses a single approach to determine whether a financial asset or liability is measured at amortized cost or fair value, replacing the multiple rules in IAS 39. For financial assets, the approach in IFRS 9 is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. The new standard also requires a single impairment method to be used, replacing the multiple impairment methods in IAS 39.

For financial liabilities measured at fair value, fair value changes due to changes in a company's credit risk are presented in other comprehensive income, instead of net income, unless this would create an accounting mismatch. An accounting mismatch may occur when financial liabilities that are measured at fair value are managed with assets that are measured at fair value through profit and loss. A mismatch could arise because the entire change in the fair value of the financial assets would be presented in net income but a portion of the change in the fair value of the related financial liabilities would not. IFRS 9 is effective for annual periods beginning on or after January 1, 2013. Earlier application is permitted. InnVest is currently evaluating the impact of IFRS 9 on its condensed consolidated financial statements.

Consolidated financial statements ("IFRS 10")

IFRS 10 establishes principles for the presentation and preparation of consolidated financial statements when an entity controls one or more other entities. IFRS 10 supersedes IAS 27 – *Consolidated and Separate Financial Statements* and the Standing Interpretations Committee's ("SIC") *SIC-12 Consolidation – Special Purpose Entities* and is effective for annual periods beginning on or after January 1, 2013. Earlier application is permitted under certain circumstances. InnVest is currently evaluating the impact of this standard on its condensed consolidated financial statements.

Joint ventures ("IAS 28" and "IFRS 11")

IAS 28 which was amended in 2011 prescribes the accounting for investments in associates and sets out the requirements for the application of the equity method when accounting for investments in associates and joint ventures. This will affect the accounting for jointly controlled entities which InnVest currently proportionately consolidates under IFRS. IFRS 11 was issued in 2011 and establishes principles for financial reporting by parties to a joint arrangement. IAS 28 and IFRS 11 are effective for annual periods beginning on or after January 1, 2013. Earlier application is permitted. InnVest is currently evaluating the impact of IAS 28 and IFRS 11 on its consolidated financial statements.

Disclosure of interests in other entities ("IFRS 12")

IFRS 12 applies to entities that have an interest in a subsidiary, a joint arrangement, an associate or an unconsolidated structured entity. IFRS 12 is effective for annual periods beginning on or after January 1, 2013. Earlier application is permitted. InnVest is currently evaluating the impact of this standard on its condensed consolidated financial statements.

Fair value measurements ("IFRS 13")

IFRS 13 defines fair value, sets out a single IFRS framework for measuring fair value and requires disclosures about fair value measurements. The IFRS 13 applies to IFRSs that require or permit fair value measurements or disclosures about fair value measurements (and measurements, such as fair value less costs to sell, based on fair value or disclosures about those measurements), except in specified circumstances. IFRS 13 is to be applied for annual periods beginning on or after January 1, 2013. Earlier application is permitted. InnVest is currently evaluating the impact of this standard on its condensed consolidated financial statements.

Presentation of financial ftatements ("IAS 1")

IAS 1 prescribes the basis for presentation of financial statements. Recent amendments retain the option to present profit or loss and other comprehensive income either in one continuous statement or in two separate but consecutive statements. Items of other comprehensive income are required to be grouped into those that will and will not be subsequently reclassified to profit or loss. Tax on items of other comprehensive income is required to be allocated on the same basis. The measurement and recognition of items of profit or loss and other comprehensive income are not affected by the amendments.

These amendments are to be applied for annual periods beginning on or after January 1, 2013 with retroactive applicable required with certain exceptions. Earlier application is permitted. InnVest is currently evaluating the impact of this standard on its condensed consolidated financial statements.

Employee benefits ("IAS 19")

IAS 19 sets out the accounting and disclosure requirements for employee benefits. Recent amendments require the recognition of changes in the defined benefit obligation and in the plan assets when those changes occur, eliminating the corridor approach and accelerating the recognition of past service costs. Changes in the defined benefit obligation and plan assets are disaggregated into three components: service costs, net interest on the net defined benefit liabilities (assets) and re-measurements of the net defined benefit liabilities (assets). Service costs and net interest are recorded in the statement of operations and re-measurements are a component of other comprehensive income.

These amendments are to be applied for annual periods beginning on or after January 1, 2013 with retroactive applicable required with certain exceptions. Earlier application is permitted. InnVest is currently evaluating the impact of this standard on its condensed consolidated financial statements.

Note 3 | Transition to IFRS

InnVest adopted IFRS effective January 1, 2010 (the "transition date") and has prepared its opening IFRS balance sheet as at that date. Prior to the adoption of IFRS, InnVest prepared its financial statements in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"). InnVest's consolidated financial statements for the year ending December 31, 2011 will be the first annual financial statements that comply with IFRS.

The accounting policies referenced in Note 2 have been applied in preparing the financial statements for the three and nine months ended September 30, 2011; the comparative information presented in these financial statements for the three and nine months ended September 30, 2010; the opening IFRS balance sheet as at January 1, 2010; and the comparable balance sheet as at December 31, 2010. An explanation of how the transition from Canadian GAAP to IFRS has affected InnVest's balance sheet, financial performance and cash flows is set out below.

IFRS 1 – First-time adoption of IFRS

IFRS generally requires an entity to apply all IFRS retrospectively, as though IFRS had been in place since inception. However, IFRS 1 provides certain mandatory exceptions and permits limited optional exemptions. The following are the optional exemptions applied by InnVest in the preparation of its first financial statements under IFRS.

i. **Fair value as deemed cost**
InnVest has elected to measure its hotel properties and other real estate properties, excluding furniture, fixtures and equipment, at fair value as at the transition date and to use that amount as its deemed cost in the opening IFRS balance sheet.

ii. **Business combinations**
InnVest has applied the exemption for business combinations (IFRS 3 – *Business Combinations*), such that IFRS 3 was not applied to past business combinations. As a result, the opening balance sheet was not restated for business combinations that took place prior to the transition date.

iii. **Employee benefits**
InnVest has applied the employee benefits exemption to recognize all cumulative actuarial gains and losses in equity in the opening IFRS balance sheet.

Other elections

InnVest has applied the exemption allowing it not to restate decommissioning liabilities, unit based compensation and compound financial instruments that were settled prior to the date of transition.

In preparing these consolidated financial statements in accordance with IFRS 1, InnVest applied the following mandatory exception from full retrospective application of IFRS.

i. **Estimates**
Hindsight was not used to create or revise estimates and accordingly the estimates previously made by InnVest under Canadian GAAP are consistent with their application under IFRS.

Reconciliation of unitholders' equity and net (loss) income and comprehensive (loss) income

The following is a reconciliation of InnVest's unitholders' equity reported in accordance with Canadian GAAP to its unitholders' equity in accordance with IFRS as at January 1, 2010 (transition date), September 30, 2010 and December 31, 2010.

	Note	December 31, 2010	September 30, 2010	January 1, 2010
Unitholders' equity as reported under Canadian GAAP		$ 573,374	$ 469,109	$ 506,989
Differences increasing (decreasing) reported amounts				
Opening cumulative adjustments		(729,828)	(729,828)	–
Fair value adjustment of hotel properties	(i)	–	–	(214,996)
Fair value adjustment of other real estate properties	(ii)	–	–	(2,000)
Decommissioning and restoration provision	(iii)	–	–	(510)
Depreciation and amortization	(iv)	563	324	–
Reclassification of units	(v)	568,550	568,550	(467,912)
Fair value adjustments of units classified as liabilities	(vi)	(140,210)	(104,000)	–
Conversion feature of convertible debentures	(vii)	(15,107)	(21,642)	(3,990)
Defined benefit pension plans	(viii)	250	(42)	202
Deferred income taxes	(ix)	51,030	6,558	(40,622)
Writedown of hotel property	(x)	(1,505)	–	–
		(266,257)	(280,080)	(729,828)
Unitholders' equity (deficit) as reported under IFRS		$ 307,117	$ 189,029	$ (222,839)

The following is a reconciliation of InnVest's net (loss) income and comprehensive (loss) income reported in accordance with Canadian GAAP to its net (loss) income and comprehensive (loss) income in accordance with IFRS for the three and nine months ended September 30, 2010 and the year ended December 31, 2010.

		For the three months ended September 30, 2010	For the nine months ended September 30, 2010	For the year ended December 31, 2010
As reported under Canadian GAAP		$ 8,555	$ (16,626)	$ 147,458
Differences increasing (decreasing) reported amounts:				
Depreciation and amortization	(iv)	599	323	563
Valuation of units classified as liabilities	(v)(vi)	(583)	(95,524)	(131,707)
Distributions on units classified as liabilities	(v)(vi)	(58)	(18,396)	(18,454)
Conversion feature of convertible debentures	(vii)	(17,022)	(20,751)	(14,568)
Defined benefit pension plans	(viii)	(10)	(42)	250
Deferred income taxes	(ix)	4,087	6,558	51,030
Writedown of hotel property	(x)	–	–	(1,505)
As reported under IFRS		$ (4,432)	$ (144,458)	$ 33,067

i) Hotel properties

In accordance with IFRS 1, InnVest elected to use the fair value as deemed cost election for its hotel properties at transition. The impact of this election was a reduction in the carrying value of its opening balance sheet hotel properties as at January 1, 2010 of $214,996. In addition, certain intangible assets recognized on the acquisition of hotel properties under Canadian GAAP do not qualify as intangible assets under IFRS. Accordingly, upon conversion to IFRS, intangible assets were derecognized, effectively by reclassifying them to hotel properties.

ii) Other real estate

In accordance with IFRS 1, InnVest elected to use the fair value as deemed cost election for its other real estate properties. The impact of this election was a reduction in the carrying value of its opening balance sheet other real estate properties as at January 1, 2010 of $2,000.

iii) Decommissioning and restoration provision

In accordance with IAS 37 – *Provisions, Contingent Liabilities and Contingent Assets*, the measurement of InnVest's decommissioning and restoration provision was adjusted as at the transition date based on differences in discount rates used as compared to Canadian GAAP.

iv) Depreciation and amortization

The transition to IFRS has resulted in a difference in depreciation expense resulting from changes to the opening cost base of hotel properties and other real estate properties (refer to deemed cost election as described in (i) and (ii) above). In addition, changes were made to the asset componentization resulting in differences in useful lives and, accordingly, the depreciation charge.

v) Reclassification of InnVest units

Under IFRS, a trust unit may be considered a liability when a financial instrument has a contractual obligation feature to deliver cash or another financial asset to another entity. Prior to June 16, 2010, the mandatory requirement to distribute taxable income under InnVest's Declaration of Trust constituted such a contractual obligation and, accordingly, components of InnVest units are presented as a liability under IFRS.

On June 16, 2010, InnVest modified its Declaration of Trust, to eliminate the mandatory distribution and leave distributions to the discretion of the Trustees. For periods subsequent to June 16, 2010, InnVest units are presented as equity. For the equity reconciliation at January 1, 2010 (opening balance sheet), InnVest has presented InnVest Units as a liability. This will impact the comparative balance sheet presentation.

Given its presentation as a liability, distributions made on InnVest Units prior to June 16, 2010 are recorded as finance charges in the consolidated statement of net loss as compared to distributions through the equity statement under Canadian GAAP.

Under IFRS, InnVest Units classified as financial liabilities were re-measured at each reporting date prior to June 16, 2010 using the fair value of InnVest Units at such date. The resulting non-cash charges are recorded as fair value gains (losses) in the condensed consolidated statements of net income (loss).

vi) Financial instruments classified as liabilities

Under Canadian GAAP, InnVest accounted for certain financial instruments as a component of unitholders equity. Under IFRS, these instruments have been reclassified to liabilities because they are not the least subordinated instrument of units and because there is a redemption feature at the option of the holder. This treatment applies to InnVest's exchangeable units and units granted to executives under a compensation program. In addition, IOT Units reflected as non-controlling interest under Canadian GAAP are presented as a liability under IFRS.

Subsequent to initial measurement at cost, these financial liabilities are remeasured to fair value using the market value of InnVest Units at each reporting date. For InnVest's exchangeable shares and the IOT units, the resulting non-cash charges are recorded as unrealized fair value gains (losses). For the units granted to executives under a compensation program, the resulting non-cash charge at each reporting date is recorded as compensation expense.

Distributions made on equity based instruments classified as liabilities are recorded on the income statement as compared to distributions on the statement of equity under Canadian GAAP. Distributions paid on exchangeable shares and the IOT units are recorded as finance costs. Distributions paid on units granted under a compensation program are recorded as compensation expense.

vii) Conversion feature of convertible debentures

In accordance with IAS 32 – *Financial Instruments*, the conversion feature of convertible debentures is presented as a liability as compared to a component of equity under Canadian GAAP. The conversion feature is re-measured each reporting period with changes in the fair value being recorded as fair value gains (losses) in the consolidated statements of net income (loss). Under IFRS, the conversion feature will be adjusted to unitholders' equity upon conversion of a debenture with respect to the REIT's debentures, and to the IOT unitholders' liability with respect to the debentures of IOT.

viii) Pension accounting

InnVest elected to recognize all cumulative actuarial gains and losses at the date of transition to IFRS in deficit in accordance with IFRS 1. InnVest applied this election to all its pension plans. The adoption of IAS 19 – *Employee Benefits* also resulted in changes in the pension obligation relating to differences in the attribution period for certain pension plans as well as differences in the asset ceiling.

ix) Deferred income taxes

On January 1, 2010, the deferred income tax liability was impacted by changes made to the carrying value of hotel properties and other real estate properties and components to the properties.

As discussed in Note 3 (v), from January 1, 2010 to June 16, 2010 InnVest's units were classified as a future distribution liability and accordingly, deferred taxes were reflected at the tax rate applicable for a Specified Investment Flow-through entity ("SIFT"), of approximately 27% for such entities who distribute their taxable income.

On June 16, 2010, the mandatory distribution feature was removed from InnVest's Declaration of Trust, with the impact that InnVest's units were reclassified to equity. Under IFRS, as the units no longer represents a future distribution liability, deferred taxes were then required to be recorded at the "undistributed" rate of approximately 45%.

On December 31, 2010, InnVest completed a corporate restructuring to become a Qualifying REIT. Prior to this transaction, IFRS required InnVest to recognize deferred income taxes and liabilities on temporary differences expected to reverse after January 1, 2011. As a result of the completion of its restructuring, the non-cash deferred tax liability that arose primarily as a result of the introduction of the SIFT legislation in 2007, reversed in the fourth quarter of 2010.

x) Writedown of hotel property
InnVest's impairment review resulted in an incremental impairment under IFRS based on changes to the opening deemed cost value and corresponding depreciation for one leasehold asset at December 31, 2010.

Statement of cash flow

As a result of changes in accounting presentation, certain items on the statement of cash flow have been affected. Most notably, certain distributions to unitholders, previously recognized in financial activities are now recognized as finance costs on the statement of net income (loss) and comprehensive income (loss) and therefore flow through operating activities.

Note 4 | Hotel properties

InnVest's ongoing review of the hotel properties for impairment of value identified three Ontario hotels and one Alberta hotel which required a writedown of $7,711 to their estimated fair value less costs to sell or value in use ("recoverable amount"). The impairment was triggered by InnVest's long-term holding expectation for these assets.

	Land, building and leaseholds	Building finishes	Electrical and mechanical	Furniture, fixtures and equipment	Total
Cost (Including deemed cost)					
Opening balance January 1, 2011	$ 978,286	$ 286,491	$ 231,443	$ 146,239	$ 1,642,459
Derecognition of assets	–	–	–	(12,922)	(12,922)
Adjustment – decommissioning and restoration provision	2,332	–	–	–	2,332
Additions	8,840	9,603	5,063	9,372	32,878
Writedown of assets to recoverable amount	(7,711)	–	–	–	(7,711)
Balance at September 30, 2011	981,747	296,094	236,506	142,689	1,657,036
Accumulated depreciation and amortization					
Opening balance January 1, 2011	20,616	39,443	7,532	76,383	143,974
Derecognition of assets	–	–	–	(12,922)	(12,922)
Depreciation and amortization	14,761	31,383	5,824	17,206	69,174
Balance at September 30, 2011	35,377	70,826	13,356	80,667	200,226
Carrying value, September 30, 2011	$ 946,370	$ 225,268	$ 223,150	$ 62,022	$ 1,456,810

The land amount included in land, building and leaseholds is $171,389 at September 30, 2011, December 31, 2010 and January 1, 2010. This amount is not depreciated.

	Land, building and leaseholds	Building finishes	Electrical and mechanical	Furniture, fixtures and equipment	Total
Cost (including deemed cost)					
Opening balance January 1, 2010	$ 977,247	$ 277,524	$ 228,666	$ 147,223	$ 1,630,660
Sale of hotel	(5,532)	–	–	(153)	(5,685)
Fair value decommissioning and restoration adjustment	1,767	–	–	–	1,767
Proceeds from lease arrangement	(1,509)	–	–	(1,050)	(2,559)
Additions	12,716	8,967	2,777	13,333	37,793
Derecognition of assets	–	–	–	(10,049)	(10,049)
Writedown of asset to recoverable amount	(6,403)	–	–	(3,065)	(9,468)
Balance at December 31, 2010	978,286	286,491	231,443	146,239	1,642,459
Accumulated depreciation and amortization					
Opening balance at January 1, 2010	–	–	–	65,096	65,096
Proceeds from lease arrangement	–	–	–	(546)	(546)
Depreciation and amortization	20,850	39,443	7,532	23,704	91,529
Derecognition of assets	–	–	–	(10,049)	(10,049)
Writedown of asset to recoverable amount	(234)	–	–	(1,822)	(2,056)
Balance at December 31, 2010	20,616	39,443	7,532	76,383	143,974
Carrying value, December 31, 2010	$ 957,670	$ 247,048	$ 223,911	$ 69,856	$ 1,498,485
Carrying value, January 1, 2010	$ 977,247	$ 277,524	$ 228,666	$ 82,127	$ 1,565,564

In 2010, InnVest's ongoing review of hotel properties for impairment of value identified one Ontario leasehold hotel which required a writedown of its carrying value to its estimated recoverable amount.

Note 5 | Other real estate properties

Other real estate properties include office and retail properties and a retirement residence.

	Land and building	Furniture, fixtures and equipment	Total
Cost (including deemed cost)			
Opening balance January 1, 2011	$ 16,066	$ 100	$ 16,166
Derecognition of assets	–	(56)	(56)
Additions	2,701	18	2,719
Balance at September 30, 2011	18,767	62	18,829
Accumulated depreciation and amortization			
Opening balance January 1, 2011	438	62	500
Derecognition of assets	–	(56)	(56)
Depreciation and amortization	174	8	182
Balance at September 30, 2011	612	14	626
Carrying value, September 30, 2011	$ 18,155	$ 48	$ 18,203

The land amount included in land and building is $1,624 at September 30, 2011, December 31, 2010 and January 1, 2010. This amount is not depreciated.

	Land and building	Furniture, fixtures and equipment	Total
Cost (including deemed cost)			
Opening balance January 1, 2010	$ 14,430	$ 96	$ 14,526
Additions	1,636	4	1,640
Balance at December 31, 2010	16,066	100	16,166
Accumulated depreciation and amortization			
Opening balance at January 1, 2010	–	44	44
Depreciation and amortization	438	18	456
Balance at December 31, 2010	438	62	500
Carrying value, December 31, 2010	$ 15,628	$ 38	$ 15,666
Carrying value, January 1, 2010	$ 14,430	$ 52	$ 14,482

Note 6 Intangible assets

	Licence contracts	Franchise rights	Total
Cost			
Opening balance January 1, 2011	$ 26,320	$ 3,853	$ 30,173
Derecognition of assets	–	(1,329)	(1,329)
Additions	–	112	112
Balance at September 30, 2011	26,320	2,636	28,956
Accumulated depreciation and amortization			
Opening balance January 1, 2011	11,099	1,545	12,644
Derecognition of assets	–	(1,329)	(1,329)
Depreciation and amortization	987	762	1,749
Balance at September 30, 2011	12,086	978	13,064
Carrying value, September 30, 2011	$ 14,234	$ 1,658	$ 15,892

	Licence contracts	Franchise rights	Total
Cost			
Opening balance January 1, 2010	$ 26,320	$ 3,280	$ 29,600
Additions	–	1,005	1,005
Derecognition of assets	–	(432)	(432)
Balance at December 31, 2010	26,320	3,853	30,173
Accumulated depreciation and amortization			
Opening balance at January 1, 2010	9,783	1,289	11,072
Derecognition of assets	–	(432)	(432)
Depreciation and amortization	1,316	688	2,004
Balance at December 31, 2010	11,099	1,545	12,644
Carrying value, December 31, 2010	$ 15,221	$ 2,308	$ 17,529
Carrying value, January 1, 2010	$ 16,537	$ 1,991	$ 18,528

Note 7 | Bank indebtedness

As at September 30, 2011, the bridge loan amount was $4,500 (December 31, 2010 – $6,000 classified as long-term debt). In 2011, InnVest extended the bridge loan to March 1, 2012, which required a $1,250 principal payment in the second quarter of 2011, and quarterly principal payments of $250 thereafter. The extension bears interest at the Canadian Bankers' Acceptance rate plus 3.5%.

InnVest has a $40,000 operating line that is a term facility which bears interest at either, the Canadian bank prime rate plus 2.5% or the Canadian Bankers' Acceptance rate plus 3.5%. It is secured by 13 properties and is due August 31, 2012. The amount of the operating line is subject to a mortgageability test which is based on the operating results of the secured properties, calculated quarterly on a trailing four quarters basis. Based on the operating results of the secured properties for the four quarters ended September 30, 2011, InnVest qualifies for $39,212 of the maximum amount of $40,000. The amount drawn on the operating line as at September 30, 2011 was $ nil (December 31, 2010 – $7,200 classified as long-term debt).

Note 8 | Long-term debt

	September 30, 2011	December 31, 2010	January 1, 2010
Mortgages payable	**$ 812,645**	$ 834,029	$ 952,158
Operating line	**–**	7,200	–
Bank indebtedness	**–**	6,000	7,000
	812,645	847,229	959,158
Less debt issuance costs	**(4,342)**	(6,299)	(6,147)
Total long-term debt	**808,303**	840,930	953,011
Less current portion	**(83,784)**	(82,808)	(21,326)
Net long-term debt	**$ 724,519**	$ 758,122	$ 931,685

Substantially all of InnVest's assets have been pledged as security under debt agreements. At September 30, 2011, long-term debt had a weighted average interest rate of 5.6% (December 31, 2010 – 6.0%) and a weighted average effective interest rate of 6.0% (December 31, 2010 – 6.3%). The long-term debt is repayable in average monthly payments of principal and interest totalling $6,399 (December 31, 2010 – $6,241) and matures at various dates from November 20, 2011 to March 21, 2018.

Scheduled repayment of long-term debt is as follows:

	Regular amortization	Due on maturity	Total
Remainder of 2011	$ 7,769	$ 50,722	$ 58,491
2012	24,355	176,526	200,881
2013	13,245	148,740	161,985
2014	7,132	294,033	301,165
2015	2,812	70,088	72,900
2016 and thereafter	1,976	15,247	17,223
	$ 57,289	$ 755,356	$ 812,645

The current portion of long-term debt on the balance sheet is based on the twelve months ending September 30, 2012, whereas the repayment schedule above reflects the fiscal year.

The estimated fair value of InnVest's mortgages payable at September 30, 2011 was approximately $809,805 (December 31, 2010 – $872,679). This estimate was determined by discounting expected cash flows at interest rates that reflect current market conditions for debt with similar terms, maturities and risk.

Long-term debt includes $82,251 (December 31, 2010 – $96,443) which is subject to floating interest rates. Annual interest expense will increase by $823 for every 1% increase in the base Bankers' Acceptance rate.

Interest expense on mortgages and other debt, interest on operating and bridge loans and convertible debentures interest are considered operating items in the statements of cash flows.

Note 9 | Other long-term obligations

	September 30, 2011	December 31, 2010	January 1, 2010
Capital lease	$ 1,291	$ 1,428	$ 1,549
Other lease obligations	275	272	319
	1,566	1,700	1,868
Less current portion	(189)	(189)	(276)
Total lease obligations	1,377	1,511	1,592
Pension liability	2,599	2,623	3,102
Decommissioning and restoration obligations	10,650	8,201	6,435
Total other long-term obligations	$ 14,626	$ 12,335	$ 11,129

The current portion of lease obligations is included in accounts payable and accrued liabilities.

Defined benefit pension plans

The defined benefit pension plans are for specific employees of certain hotels in InnVest and are closed plans. The most recent actuarial valuation with respect to the funding of InnVest's pension plans was prepared on December 31, 2010.

The pension plan liability as at September 30, 2011 consists of the following:

	Management pension benefit plans	Non-union non-management pension benefit plans	September 30, 2011 benefit plans	December 31, 2010 benefit plans	January 1, 2010 benefit plans
Accrued benefit obligation	$ 5,215	$ 1,590	$ 6,805	$ 6,568	$ 5,850
Fair value of plan assets	2,831	1,575	4,406	4,049	3,432
Funded status – plan deficit	2,384	15	2,399	2,519	2,418
Liability arising from minimum funding requirement	222	170	392	392	684
Unamortized net actuarial loss	(192)	–	(192)	(288)	–
Accrued employee future benefit liability	$ 2,414	$ 185	$ 2,599	$ 2,623	$ 3,102

The pension expense recognized for the nine months ended September 30, 2011 is $261 (September 30, 2010 – $307).

Note 10 | Convertible debentures

The details of the convertible debentures outstanding as at the periods presented are outlined in the tables below:

Debenture	Original face amount	Maturity date	Interest rate	Effective interest rate	Conversion strike price	Outstanding principal September 30, 2011	Outstanding principal December 31, 2010
Series B	$ 75,000	May 31, 2013	6.00%	7.53%	$ 14.90	$ 74,980	$ 74,980
Series C	$ 70,000	August 1, 2014	5.85%	7.42%	14.70	$ 70,000	$ 70,000
Series D	$ 50,000	March 31, 2016	6.75%	9.41%	$ 5.70	$ 36,358	$ 38,474
Series E	$ 75,000	September 30, 2017	6.00%	7.75%	$ 8.00	$ 75,000	$ 75,000
Series F	$ 50,000	March 30, 2018	5.75%	7.40%	$ 9.45	$ 50,000	$ –

	September 30, 2011	December 31, 2010	January 1, 2010
Convertible debentures	**$ 306,338**	$ 258,454	$ 240,744
Less financing costs and accretion	**(3,248)**	(3,801)	(2,184)
Less allocation of conversion feature value	**(15,212)**	(13,181)	(12,642)
	$ 287,878	$ 241,472	$ 225,918

The conversion feature of the convertible debentures is recorded as a liability under Unitholders' liabilities and measured at fair value (see Note 13).

The fair value of InnVest's convertible debentures, estimated based on the market rates for convertible debentures as at September 30, 2011, is $272,212 (December 31, 2010 – $267,435).

Conversions

During the three and nine months ended September 30, 2011, $nil and $2,116, respectively, of Series D – 6.75% Debentures were converted to nil and 371,221 units, respectively (September 30, 2010 – $152 converted to 18,458 units and $7,216 converted to 1,257,754 units, respectively).

Series F debentures

On March 8, 2011, InnVest closed a bought deal of $50,000, 5.75% convertible unsecured subordinated debentures ("Series F – 5.75% Debentures"). These debentures are convertible into InnVest Units at a conversion price of $9.45 per unit, bear interest at 5.75% per annum payable semi-annually on March 30 and September 30 of each year and will mature March 30, 2018. Upon conversion, the Series F – 5.75% Debentures are convertible into 5,291,005 units. The Series F – 5.75% Debentures are not redeemable prior to March 30, 2014.

The scheduled convertible debentures maturities are as follows:

	Due on maturity
Remainder of 2011	$ –
2012	–
2013	74,980
2014	70,000
2015	–
2016 and thereafter	161,358
	$ 306,338
Financing costs and allocation of conversion feature value	(18,460)
	$ 287,878

Note 11 | Capital management

InnVest manages its capital, which is defined as the aggregate of unitholders' equity and debt, under the terms of the Declarations of Trust for the REIT and IOT, collectively referred to as the "DOT". InnVest's capital management objectives are (i) to ensure compliance with debt and investment restrictions outlined in its DOT as well as external existing debt covenants, (ii) to allow for the implementation of its acquisition strategy and hotel property refurbishment program, and (iii) to build long-term unitholder value. Issuances of equity and debt are approved by the Board of Trustees (the "Board") through their review and approval of InnVest's strategic plan and annual budget plan, along with changes to the approved plans periodically throughout each year.

At September 30, 2011, InnVest's primary contractual obligations consisted of long-term mortgage obligations and convertible debentures. InnVest is not permitted to exceed certain financial leverage amounts under the terms of the DOT. InnVest is permitted to hold indebtedness excluding convertible debentures up to a level of 60% of gross asset value. Further, InnVest is permitted to have indebtedness and convertible debentures up to a level of 75% of gross asset value. Indebtedness is computed as of the last day of each financial year excluding any indebtedness under any operating line, non-interest bearing indebtedness, trade accounts payable and for greater certainty, deferred income tax liability.

Under the terms of the DOT individual property mortgages, or mortgages on a pool of properties, cannot exceed 75% of the fair value of the underlying property.

At September 30, 2011, InnVest's leverage excluding and including convertible debentures was 45.8% and 63.0%, respectively, calculated as follows:

	September 30, 2011		December 31, 2010	
Total assets per consolidated balance sheet		**$ 1,589,573**		$ 1,598,837
Accumulated depreciation and amortization		**214,410**		157,118
Deferred income tax asset and liability		**(21,766)**		(20,503)
Gross asset value		**$ 1,782,217**		$ 1,735,452
Book value of mortgages and other indebtedness[1]	**$ 817,145**	**45.8%**	$ 847,229	48.8%
Convertible debentures[2]	**306,338**	**17.2%**	258,454	14.9%
	$ 1,123,483	**63.0%**	$ 1,105,683	63.7%

1. *Adjusted to eliminate financing issuance costs.*
2. *Adjusted to face value.*

The DOT also includes guidelines that limit capital expended to, among other items, the following:

(a) Direct and indirect investments in real property on which hotels are situated and the hotel business conducted thereon, primarily in Canada, and in entities whose activities consist primarily of franchising hotels;

(b) Temporary investments held in cash, deposits with a Canadian chartered bank or trust company, short-term government debt securities or in money market instruments of, or guaranteed by, a Schedule 1 Canadian bank, short-term commercial paper, notes, bonds of other debt securities of a Canadian entity having a rating of at least R-1 (Mid) by Dominion Bond Rating Service or A-1 (Mid) by Standard & Poor's Corporation maturing prior to one year from the date of issue; and

(c) Investments in mortgages or mortgage bonds, where the related security is a first mortgage on income producing real property which otherwise complies with (a) above and is subject to certain leverage limits and debt service coverage. The aggregate value of such investments shall not exceed 20% of the unitholders' equity.

InnVest is in compliance with these guidelines.

InnVest maintains an operating line of up to $40,000 with a Canadian chartered bank (the “Bank”) with the following covenants in addition to the leverage limits under the DOT:

(a) Trailing 12 months consolidated earnings before interest, taxes, depreciation and amortization (“EBITDA”) to consolidated interest expense of not less than 2.0 times (actual being 2.0 times at September 30, 2011 and 1.9 times at December 31, 2010);

(b) Trailing 12 months consolidated EBITDA to consolidated debt service of not less than 1.5 times (actual being 1.6 times at September 30, 2011 and 1.5 times at December 31, 2010); and

(c) Unitholders’ Equity, which includes the unitholders’ equity of IOT shown as a financial liability on the consolidated balance sheet, of not less than $300,000 (actual being $386,845 at September 30, 2011 and $396,351 at December 31, 2010).

The lender waived compliance with the trailing 12 month minimum interest coverage ratio and debt service coverage ratio for the fourth quarter of 2010.

Note 12 | Income taxes and deferred income tax

On July 20, 2011, the Minister of Finance (the “Minister”) announced changes in, among other things, the tax treatment of real estate investment trusts that have issued “stapled” securities. If the Minister’s announcement is enacted as proposed and no changes are made to the existing structure of the REIT and IOT, then rents (and certain other amounts) paid by IOT to the REIT after the applicable transition date (expected to be July 20, 2012) (the “Transition Period”) would cease to be deductible in computing the income of IOT for Canadian income tax purposes. InnVest is restricted from issuing stapled securities during the Transition Period, subject to certain exceptions. As a consequence, InnVest has decided to suspend its distribution reinvestment plan (“DRIP”) until further notice (see note 15).

Note 13 | Financial instruments

Risk management

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

Interest rate risk

The average term to maturity of InnVest’s long-term debt and convertible debentures combined is approximately three years. This strategy reduces InnVest’s exposure to re-pricing risk resulting from short-term interest rate fluctuations in any one year. Management is of the view that such a strategy will provide the most effective interest rate risk management for debt.

InnVest’s floating rate debt balance is monitored by management to minimize InnVest’s exposure to interest rate fluctuations. As at September 30, 2011, InnVest’s floating rate debt balance of $82,251 (December 31, 2010 – $96,443) is approximately 10.1% (December 31, 2010 – 11.4%) of total long-term debt, excluding convertible debentures.

Credit risk

Credit risk relates to the possibility that hotel guests, either individual or corporate, do not pay the amounts owed to InnVest. InnVest mitigates this risk by limiting its exposure to customers allowed to pay by invoice after check out (“direct bill”). Accounts receivable as at September 30, 2011 are $36,589 (December 31, 2010 – $28,992). InnVest reviews accounts receivable regularly and the allowance for doubtful accounts is adjusted for any balances which are determined by management to be uncollectable. This provision adjustment is expensed in the hotel operating income. The allowance as at September 30, 2011 is $406 or 1.1% (December 31, 2010 – $538 or 1.9%) of total receivables. Bad debt expense included in hotel expenses is $21 for the nine months ended September 30, 2011 (September 30, 2010 – $60). Accounts receivable amounts outstanding for over 90 days, which have not been provided for, total $357 at September 30, 2011 (December 31, 2010 – $196). Mortgages receivable are secured by mortgages on the assets sold.

Liquidity risk

Liquidity risk arises from the possibility of not having sufficient cash available to InnVest to fund its growth and capital maintenance programs and refinance its obligations as they arise. There is a risk that lenders will not refinance maturing debt on terms and conditions acceptable to InnVest or on any terms at all. There is also a risk that bank lenders will not refinance the operating and bridge loan facilities on terms and conditions acceptable to InnVest or on any terms at all.

Estimated maturities of InnVest's financial liabilities, excluding Unitholder liabilities, are:

	Remainder of 2011	2012	2013	2014	2015	2016 and thereafter	Contractual cash flows[1]
Accounts payable and accrued liabilities	$ 77,548	$ –	$ –	$ –	$ –	$ –	$ 77,548
Mortgage payable – principal[2]	58,491	200,881	161,985	301,165	72,900	17,223	812,645
Mortgage payable – interest[3]	10,713	42,437	22,617	10,900	3,335	1,779	91,781
Bridge loan – principal	250	4,250	–	–	–	–	4,500
Bridge loan – interest	49	33	–	–	–	–	82
Convertible debentures – principal	–	–	74,980	70,000	–	161,358	306,338
Convertible debentures – interest	2,250	18,424	15,799	13,924	9,829	17,415	77,641
Long-term land leases	1,200	4,826	4,826	4,826	4,826	83,225	103,729
Total	$ 150,501	$ 270,851	$ 280,207	$ 400,815	$ 90,890	$ 281,000	$1,474,264

1. Contractual cash flows include principal and interest payments and include extension options available to InnVest.
2. Mortgage principal includes regular amortization and repayments at maturity.
3. Interest for floating rate debt is based on interest rates prevailing at September 30, 2011.

Fair values

The fair values of InnVest's financial assets and current liabilities approximate their recorded values at September 30, 2011 and December 31, 2010 due to their short-term nature.

The fair value of InnVest's long-term debt is less than the carrying value by approximately $2,840 at September 30, 2011 (December 31, 2010 – $25,450 greater than the carrying value) due to changes in interest rates since the dates on which the individual mortgages were arranged. The fair value of long-term debt has been estimated based on the current market rates for mortgages with similar terms and conditions.

The fair value of InnVest's convertible debentures is less than the carrying value by approximately $36,601 at September 30, 2011 (December 31, 2010 – $10,493 greater than the carrying value). The fair value of convertible debentures is based on the market rates for similar convertible debentures as at each reporting date.

The fair value hierarchy of financial instruments measured at fair value on the balance sheet is as follows:

	Level 1	Level 2	Level 3	Total
Financial liabilities:				
InnVest operations trust	$ –	$ –	$ 40,598	$ 40,598
Exchangeable units	1,568	–	–	1,568
Convertible debentures holders' conversion option	–	–	853	853
Unvested executive compensation	312	–	–	312
Total financial liabilities	$ 1,880	$ –	$ 41,451	$ 43,331

Letters of credit

As at September 30, 2011, InnVest has letters of credit totalling $3,638 (December 31, 2010 – $3,638) held on behalf of security deposits for various utility companies and liquor licences, and additional security for the pension liabilities.

Note 14 | Unitholders and other liabilities

	September 30, 2011	December 31, 2010	January 1, 2010
InnVest operations trust	$ 40,598	$ 89,234	$ –
Exchangeable units	1,568	2,449	–
Convertible debentures holders' conversion option	853	19,097	3,990
Unvested executive compensation	312	721	–
Balance, end of period	$ 43,331	$ 111,501	$ 3,990

InnVest operations trust

InnVest Operations Trust represents the InnVest unitholders' interest in IOT through ownership of the IOT non-voting units after giving effect to the reorganization of InnVest on December 31, 2010. Each non-voting unit of IOT trades together with each issued and outstanding unit of the REIT as an InnVest Unit. IOT indirectly holds the hotel operating assets along with a 50% interest in CHC.

The IOT holdings are presented as liabilities at their fair value. During the nine months ended September 30, 2011, distributions totalling $2,256 were paid on the IOT units and are included as financing costs in the consolidated statement of net income (loss).

For every 1% absolute change in the IOT's relative value allocation of the consolidated entities (see Note 2 (r)), the liability changes by approximately $4,000.

In the quarter ended September 30, 2011, changes in assumptions directly resulting from the expected termination of the current stapled structure caused a reduction in the IOT liability, and a corresponding increase in income before tax, of approximately $18,000.

Exchangeable units

As part of an acquisition made in 2005, InnVest granted 362,869 exchangeable units ("Exchangeable Units") to a third party. The Exchangeable Units receive a monthly cash payment equal to the value of the cash distributions that would have been paid on the InnVest Units if they had been issued on the date of grant. The Exchangeable Units are exchangeable into InnVest Units with three business days of prior written notice to InnVest.

The Exchangeable Units are presented as liabilities at their fair value. During the nine months ended September 30, 2011, distributions totaling $135 (September 30, 2010 – $135) were paid on the Exchangeable Units and are included as financing costs in the condensed consolidated statement of net income (loss).

Convertible debenture holders' conversion option

InnVest has separated the conversion option component for each of its series of convertible debentures which are presented as liabilities. InnVest measures the conversion option component at fair value at each reporting date.

Executive compensation plan

The senior executives participate in the executive compensation plan under which InnVest Units are granted by the Board of Trustees from time to time. InnVest has reserved a maximum of 1,000,000 InnVest Units for issuance under the plan. The balance in this reserve account at September 30, 2011 is 707,303 InnVest Units. An InnVest Unit granted through the plan entitles the holder to receive, on the vesting date, the then current fair market value of the InnVest Unit plus the value of the cash distributions that would have been paid on the InnVest Unit if it had been issued on the date of grant assuming the reinvestment of the distribution into InnVest Units. The payment will be satisfied through the issuance of InnVest Units.

At September 30, 2011, there were 113,566 (December 31, 2010 – 106,869) unvested executive units granted under the plan. The unvested units are presented as liabilities over the vesting periods.

The Board of Trustees approved the granting of 27,815 units during the nine months ended September 30, 2011. All granted units vest equally on the third and fourth anniversaries of the effective date of grant.

Given current restrictions on the issuance of stapled securities during the Transition Period (see Note 12), executive compensation units which vest during the Transition Period will be satisfied in cash as opposed to the issuance of units.

Note 15 | Units outstanding

Each issued and outstanding unit of the REIT trades together with a non-voting unit of IOT as a stapled unit ("InnVest Unit") on the TSX. An unlimited number of InnVest Units have been authorized, each of which represents an equal undivided beneficial interest in any distributions from InnVest. Per the DOT, InnVest Units cannot be issued from treasury unless the Trustees consider it not to be dilutive to ensuing annual distributions of distributable income to existing unitholders.

Units issued and outstanding:

	September 30, 2011	September 30, 2010
Balance, beginning of the period	**89,474,691**	87,498,354
Units issued	**3,600,000**	–
Units issued on conversion of debentures	**371,221**	1,257,754
Units issued under distribution reinvestment plan	**47,609**	261,626
Units issued under trustee and executive plans	**44,501**	28,574
Balance, end of the period	**93,538,022**	89,046,308

Trustee compensation plan

The members of the Board of Trustees are meant to receive 50% of their annual retainer in units (based on the then current market price of the InnVest Units). InnVest has set aside 350,000 InnVest Units in reserve for this purpose. The balance in this reserve account at September 30, 2011 is 221,964 InnVest Units. Given current restrictions on the issuance of stapled securities during the Transition Period (see Note 12), 100% of the Board of Trustees' compensation will be paid in cash through the end of the Transition Period.

Distribution reinvestment plan ("DRIP")

InnVest had a DRIP whereby eligible Canadian unitholders may have elected to have their distributions of income from InnVest automatically reinvested in additional InnVest Units. On August 12, 2011 InnVest suspended its DRIP until further notice (see Note 12).

Note 16 | Per unit information

			Three months ended September 30, 2011			Nine months ended September 30, 2011
			Weighted average units			Weighted average units
Net income – basic	$	**66,929**	**93,532,175**	$	**48,859**	**92,420,163**
Net income – diluted	$	**72,479**	**124,841,890**	$	**57,024**	**112,142,501**

The impact of the equity-based instruments which are presented as liabilities has been excluded from the diluted per unit calculations for the three and nine months ended September 30, 2011. The impact of all of the debentures has been included for the three months ended September 30, 2011, but Series B and Series C have been excluded from the diluted per unit calculations for the nine months ended September 30, 2011 because the conversions would not be dilutive.

InnVest had no equity instruments prior to June 16, 2010 as a result of the classification of all units as financial liabilities. Refer to Note 3 – *Transition to IFRS*. Consequently, InnVest has not reported per unit measures in the comparative periods.

Note 17 | Management agreements

Westmont Hospitality Canada Limited

InnVest has a Management Agreement for hotel management and accounting services and an Administrative Services Agreement (the "Agreements") with Westmont Hospitality Canada Limited ("Westmont"). Westmont is considered a related party to InnVest as a result of its ability to exercise significant influence through the Agreements. Westmont manages all but 15 of InnVest's hotels.

The current terms for the Agreements expire July 25, 2017 and include an additional renewal term for a five-year extension, subject to the consent of Westmont and approval of InnVest. 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 InnVest achieves distributable income 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. For assets sold which are managed by Westmont, InnVest pays a termination fee equal to the fees paid based on trailing 12 months revenues. InnVest recorded termination fees of $ nil during the nine months ended September 30, 2011 (September 30, 2010 – $135).

In addition to the base management fee and incentive fee, Westmont is entitled to 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 or a fixed percentage of hotel operating income, after the reserve for replacement of furniture, fixtures and equipment and capital improvements, subject to an annual minimum fee.

During the three and nine months ended September 30, 2011 and 2010, the fees charged to InnVest pursuant to the Agreements were as follows:

	Three months ended September 30, 2011	Three months ended September 30, 2010	**Nine months ended September 30, 2011**	Nine months ended September 30, 2010
Management fees	**$ 3,408**	$ 3,452	**$ 8,847**	$ 8,870
Asset management fees (included in management fee expense)	**503**	495	**1,510**	1,510
Accounting services (included in hotel operating expenses)	**596**	588	**1,788**	1,776
Administrative services (included in corporate and administrative expenses)	**107**	113	**335**	339
Project management and general contractor services (capitalized to hotel properties)	**272**	274	**720**	666
Termination fees (included in hotel operating expenses)	**–**	39	**–**	135
	$ 4,886	$ 4,961	**$ 13,200**	$ 13,296

In addition, salaries of InnVest employees paid by Westmont and reimbursed by InnVest were $68 and $249 for the three and nine months ended September 30, 2011 (September 30, 2010 – $52 and $269 respectively). Included in accounts payable and accrued liabilities are amounts owed to Westmont at September 30, 2011 totalling $1,745 (December 31, 2010 – $1,230).

Other management agreements

Hilton Canada Co. ("Hilton") manages two Hilton hotel properties for InnVest. The hotel management agreements provide for the payment of an annual management fee to Hilton in an amount equal to 3.0% of gross revenues until the agreements mature on December 31, 2026. For the three and nine months ended September 30, 2011, total management fees paid to Hilton were $344 and $889 respectively (September 30, 2010 – $311 and $850 respectively).

Delta Hotels Limited ("Delta") manages 10 Delta hotel properties for InnVest. The hotel management agreements provide for the payment of an annual management fee to Delta in an amount of 2% to 3% of total revenues from the hotel. For the two hotels purchased by InnVest in 2006, Delta can qualify for an incentive management fee of 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 incentive management fees for the other eight hotels are calculated based on net operating income from hotel operations plus amortization less the capital replacement reserve, in excess of a threshold. The agreements mature from December 31, 2011 to December 31, 2047. For the three and nine months ended September 30, 2011, total management fees paid to Delta were $1,231 and $3,305 respectively (2010 – $1,245 and $3,378 respectively).

Fairmont Hotels and Resorts ("Fairmont") manages three hotel properties for InnVest. The hotel management agreements provide for the payment of a base management fee and an incentive management fee to Fairmont. The base management fee is equal to 3% of total hotel revenues. The incentive management fees are calculated based on net operating income from hotel operations plus amortization less the capital replacement reserve, in excess of a threshold. The agreements mature from December 31, 2023 to December 31, 2047. For the three and nine months ended September 30, 2011, the total management fees paid to Fairmont were $908 and $2,480 respectively (2010 – $908 and $2,512 respectively).

Fairmont may also receive a portfolio incentive fee for which two Fairmont properties and four Delta properties participate. The portfolio incentive fees are calculated based on net operating income from hotel operations plus amortization less the capital replacement reserve, in excess of a threshold. There were no portfolio incentive fees for the three and nine months ended September 30, 2011 and 2010.

Note 18 | Segmented financial information

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

	Western	Ontario	Quebec	Atlantic	Total
Three months ended September 30, 2011					
Hotel revenues	**$ 42,862**	**$ 62,627**	**$ 39,628**	**$ 29,715**	**$ 174,832**
Hotel expenses	**30,049**	**45,848**	**28,392**	**19,769**	**124,058**
Hotel operating income	**$ 12,813**	**$ 16,779**	**$ 11,236**	**$ 9,946**	**$ 50,774**
Three months ended September 30, 2010					
Hotel revenues	$ 40,802	$ 64,110	$ 38,049	$ 30,061	$ 173,022
Hotel expenses	28,507	46,455	27,462	19,775	122,199
Hotel operating income	$ 12,295	$ 17,655	$ 10,587	$ 10,286	$ 50,823
Nine months ended September 30, 2011					
Hotel revenues	**$ 118,050**	**$ 172,826**	**$ 104,036**	**$ 70,791**	**$ 465,703**
Hotel expenses	**86,253**	**133,943**	**81,505**	**54,532**	**356,233**
Hotel operating income	**$ 31,797**	**$ 38,883**	**$ 22,531**	**$ 16,259**	**$ 109,470**
Nine months ended September 30, 2010					
Hotel revenues	$ 115,578	$ 172,913	$ 102,261	$ 70,975	$ 461,727
Hotel expenses	83,909	134,265	79,935	53,595	351,704
Hotel operating income	$ 31,669	$ 38,648	$ 22,326	$ 17,380	$ 110,023
Capital expenditures on hotel properties					
Three months ended September 30, 2011	**$ 1,610**	**$ 5,917**	**$ 4,347**	**$ 2,069**	**$ 13,943**
Three months ended September 30, 2010	$ 2,610	$ 3,820	$ 2,779	$ 1,196	$ 10,405
Capital expenditures on hotel properties					
Nine months ended September 30, 2011	**$ 7,890**	**$ 10,647**	**$ 11,733**	**$ 5,327**	**$ 35,597**
Nine months ended September 30, 2010	$ 5,062	$ 8,491	$ 7,569	$ 3,068	$ 24,190
Hotel Properties					
September 30, 2011	**$ 421,606**	**$ 544,250**	**$ 305,412**	**$ 185,542**	**$ 1,456,810**
December 31, 2010	$ 432,930	$ 566,333	$ 309,418	$ 189,804	$ 1,498,485

Note 19 | Total revenues

	Three months ended September 30, 2011	Three months ended September 30, 2010	**Nine months ended September 30, 2011**	Nine months ended September 30, 2010
Hotel revenues	**$ 174,832**	$ 173,022	**$ 465,703**	$ 461,727
Other business income	**3,631**	3,929	**10,021**	9,747
	$ 178,463	$ 176,951	**$ 475,724**	$ 471,474

Note 20 | Other business income

Other business income includes franchise business income, which is InnVest's 50% share of CHC's operations, and the income from the other real estate properties.

	Franchise business	Retail/ office	Retirement residence	Three months ended September 30, 2011	Three months ended September 30, 2010
Revenues	$ 2,843	$ 590	$ 198	$ 3,631	$ 3,929
Expenses	1,595	294	194	2,083	2,280
Other business income, net	$ 1,248	$ 296	$ 4	$ 1,548	$ 1,649

	Franchise business	Retail/ office	Retirement residence	Nine months ended September 30, 2011	Nine months ended September 30, 2010
Revenues	$ 7,418	$ 1,973	$ 630	$ 10,021	$ 9,747
Expenses	4,876	917	632	6,425	6,008
Other business income, net	$ 2,542	$ 1,056	$ (2)	$ 3,596	$ 3,739

Note 21 | Unrealized gain (loss) on liabilities presented at fair value

Fair value (gain) loss recorded for the three and nine months ended September 30, 2011 and 2010 are as follows:

	Three months ended September 30, 2011	Three months ended September 30, 2010	Nine months ended September 30, 2011	Nine months ended September 30, 2010
InnVest operations trust (Note 3)	$ 53,08	$ –	$ 52,520	$ –
Unit reclassification (Note 3)	–	–	–	(94,469)
Exchangeable units	893	(464)	882	(678)
Convertible debentures holders' conversion option	17,457	(17,022)	20,275	(20,751)
Gain (loss) for the period	$ 71,434	$ (17,486)	$ 73,677	$ (115,898)

Note 22 | Subsequent events

Proposed reorganization

In response to changes to recent changes to the tax treatment of real estate investment trusts that have issued "stapled securities" (see Note 12), subsequent to the end of the quarter, the Board of Trustees of InnVest announced its recommendation to pursue a merger of IOT into the REIT effective on June 30, 2012. This reorganization would result in all the former stapled unitholders and stapled debenture holders of the REIT and IOT holding only units or convertible debentures, as the case may be, of the REIT. The merged entity would be governed as a trust. The proposed merger will be subject to unitholder approval. InnVest intends to schedule a special meeting of unitholders in the first quarter of 2012.

Reduction in distributions

Subsequent to the end of the quarter, InnVest announced a reduction in distributions paid to unitholders to $0.400 per unit annually, as compared to the prior distribution level of $0.50 per unit annually. This equates to a monthly distribution of approximately $0.033 per unit beginning in November 2011. The board of Trustees unanimously approved the reduction of distributions after careful consideration of the environment faced by the REIT and its desire to conserve liquidity to fund profit-improving capital investments throughout the portfolio.

Litigation settlement

Subsequent to the end of the quarter, InnVest settled an outstanding construction lawsuit in which it was the plaintiff. As a result, InnVest expects to record a gain of $2,900, less legal and associated costs in the fourth quarter of 2011.

Note 23 | Approval of the condensed consolidated financial statements

These condensed consolidated financial statements were authorized for issue by the Board of Trustees of InnVest on November 9, 2011.