# Condensed Consolidated Interim Financial Statements

## For the three and nine months ended September 30, 2015 and 2014

## (Unaudited)

# Condensed Consolidated Interim Statements of Financial Position

***In thousands of Canadian dollars,***
***(Unaudited)***

| | Note | **September 30, 2015** | December 31, 2014 |
|---|---|---|---|
| **ASSETS** | | | |
| **Non-current assets** | | | |
| Investment properties | [3] | **$1,822,090** | $1,733,895 |
| Property and equipment | [4] | **4,852** | 4,854 |
| Loans receivable | | **4,950** | 4,000 |
| Other non-current assets | | **18** | - |
| | | **1,831,910** | 1,742,749 |
| **Current assets** | | | |
| Cash | | **15,740** | 18,847 |
| Rent and other receivables | | **5,141** | 1,954 |
| Inventory | | **300** | 139 |
| Other current assets | | **16,868** | 11,545 |
| | | **38,049** | 32,485 |
| **TOTAL ASSETS** | | **$1,869,959** | $1,775,234 |
| **EQUITY AND LIABILITIES** | | | |
| Shareholders' equity | | **$669,755** | $648,029 |
| Accumulated other comprehensive loss ("AOCL") | [16] | **(167)** | (198) |
| Non-controlling interest | | **14,853** | 14,852 |
| **Total Equity** | | **684,441** | 662,683 |
| **Non-current liabilities** | | | |
| Mortgages and loans payable | [6] | **796,834** | 729,474 |
| Convertible debentures | [8] | **99,199** | 97,967 |
| Other liabilities | | **5,582** | 1,916 |
| Deferred tax | | **116,764** | 105,958 |
| | | **1,018,379** | 935,315 |
| **Current liabilities** | | | |
| Mortgages and loans payable | [6] | **120,235** | 115,248 |
| Construction loans | [7] | **19,977** | 31,944 |
| Accounts payable and accrued liabilities | | **26,927** | 30,044 |
| | | **167,139** | 177,236 |
| **Total Liabilities** | | **1,185,518** | 1,112,551 |
| **TOTAL EQUITY AND LIABILITIES** | | **$1,869,959** | $1,775,234 |

*See accompanying notes to the condensed consolidated interim financial statements.*

Approved on Behalf of the Board

(signed) "G. Wayne Watson"
Director

(signed) "Philip D. Fraser"
Director

# Condensed Consolidated Interim Statements of Income and Comprehensive Income

***In thousands of Canadian dollars (except per share amounts), (Unaudited)***

| | Note | Three months ended | | Nine months ended | |
|---|---|---|---|---|---|
| | | **September 30, 2015** | September 30, 2014 | **September 30, 2015** | September 30, 2014 |
| Property revenue | | **$43,193** | $37,777 | **$124,181** | $109,360 |
| Property operating expenses | | **(16,015)** | (14,004) | **(51,152)** | (46,526) |
| **Net operating income** | | **27,178** | 23,773 | **73,029** | 62,834 |
| **Other income** | | | | | |
| Equity income | [5] | - | 166 | - | 500 |
| Home sales | [11] | **19** | 40 | **29** | 76 |
| Corporate income | | **359** | 363 | **1,076** | 746 |
| | | **378** | 569 | **1,105** | 1,322 |
| **Other expenses** | | | | | |
| Financing costs | [12] | **(9,396)** | (8,618) | **(27,718)** | (25,908) |
| Depreciation | | **(196)** | (169) | **(566)** | (467) |
| Amortization of deferred financing costs | | **(480)** | (430) | **(1,409)** | (1,261) |
| Administration | | **(2,474)** | (1,980) | **(7,356)** | (6,028) |
| | | **(12,546)** | (11,197) | **(37,049)** | (33,664) |
| **Income before fair value gain, gain (loss) on disposition and income taxes** | | **15,010** | 13,145 | **37,085** | 30,492 |
| Fair value gain | [3] | **1,368** | 13,382 | **1,548** | 21,582 |
| Gain (loss) on disposition | | **74** | - | **(109)** | 94 |
| **Income before income taxes** | | **16,452** | 26,527 | **38,524** | 52,168 |
| Current tax recovery | | **-** | - | - | 327 |
| Deferred tax expense | | **(4,831)** | (5,061) | **(10,793)** | (11,274) |
| **Net income** | | **$11,621** | $21,466 | **$27,731** | $41,221 |
| **Other comprehensive loss** | | | | | |
| **Item that may be reclassified subsequently to net income** | | | | | |
| Amortization of loss in AOCL to finance costs (net of tax - $5 and $14) | [16] | **10** | - | **31** | - |
| Unrealized loss on forward interest rate hedge (net of tax - $16 and $86) | [16] | **-** | (40) | **-** | (209) |
| **Comprehensive income** | | **$11,631** | $21,426 | **$27,762** | $41,012 |
| | | | | | |
| **Net income attributable to:** | | | | | |
| Common shareholders | | **11,462** | 20,491 | **27,137** | 39,031 |
| Non-controlling interest | | **159** | 975 | **594** | 2,190 |
| | | **$11,621** | $21,466 | **$27,731** | $41,221 |
| **Comprehensive income attributable to:** | | | | | |
| Common shareholders | | **11,472** | 20,451 | **27,168** | 38,822 |
| Non-controlling interest | | **159** | 975 | **594** | 2,190 |
| | | **$11,631** | $21,426 | **$27,762** | $41,012 |
| | | | | | |
| Net income per share attributable to common shareholders: | | | | | |
| -basic | [13] | **$0.18** | $0.37 | **$0.44** | $0.71 |
| -diluted | [13] | **$0.17** | $0.33 | **$0.42** | $0.66 |

# Condensed Consolidated Interim Statements of Changes in Equity

***In thousands of Canadian dollars,***
***(Unaudited)***

**Nine months ended September 30, 2015**

| | **Share Capital** | **Contributed Surplus** | **Other Paid-in Capital** | **Retained Earnings** | **AOCL** | **Non-Controlling Interest** | **Total Equity** |
|---|---|---|---|---|---|---|---|
| At January 1, 2015 | **$459,138** | **$2,417** | **$5,681** | **$180,793** | **$ (198)** | **$14,852** | **$662,683** |
| Net income | **-** | **-** | **-** | **27,137** | **-** | **594** | **27,731** |
| Amortization of loss on forward interest rate hedge | **-** | **-** | **-** | **-** | **31** | **-** | **31** |
| Dividends | **-** | **-** | **-** | **(28,013)** | **-** | **-** | **(28,013)** |
| Distributions to non-controlling interest | **-** | **-** | **-** | **-** | **-** | **(593)** | **(593)** |
| Dividend reinvestment plan | **4,858** | **-** | **-** | **-** | **-** | **-** | **4,858** |
| Stock options exercised | **3,458** | **(486)** | **-** | **-** | **-** | **-** | **2,972** |
| Restricted share units issued | **-** | **662** | **-** | **-** | **-** | **-** | **662** |
| Issuance of shares for acquisitions | **14,489** | **-** | **-** | **-** | **-** | **-** | **14,489** |
| Repurchase through normal course issuer bid | **(167)** | **(48)** | **-** | **-** | **-** | **-** | **(215)** |
| Restricted share units redeemed | **157** | **(322)** | **-** | **-** | **-** | **-** | **(165)** |
| **At September 30, 2015** | **$481,933** | **$2,223** | **$5,681** | **$179,917** | **$(167)** | **$14,853** | **$684,440** |

Nine months ended September 30, 2014

| | Share Capital | Contributed Surplus | Other Paid-in Capital | Retained Earnings | AOCL | Non-Controlling Interest | Total Equity |
|---|---|---|---|---|---|---|---|
| At January 1, 2014 | $398,181 | $2,302 | $5,681 | $184,560 | $- | $13,336 | $604,060 |
| Net income | - | - | - | 39,031 | - | 2,190 | 41,221 |
| Other comprehensive loss | - | - | - | - | (209) | - | (209) |
| Dividends | - | - | - | (24,728) | - | - | (24,728) |
| Distributions to non-controlling interest | - | - | - | - | - | (675) | (675) |
| Acquisition of non-controlling interest | - | - | - | 12 | - | (469) | (457) |
| Dividend reinvestment plan | 1,923 | - | - | - | - | - | 1,923 |
| Stock options exercised | 849 | (101) | - | - | - | - | 748 |
| Restricted share units issued | - | 632 | - | - | - | - | 632 |
| Issuance of shares for cash | 7,000 | - | - | - | - | - | 7,000 |
| Issuance of shares for acquisitions | 800 | - | - | - | - | - | 800 |
| Restricted share units redeemed | 85 | (101) | - | - | - | - | (16) |
| At September 30, 2014 | $408,838 | $2,732 | $5,681 | $198,875 | $(209) | $14,382 | $630,299 |

*See accompanying notes to the condensed consolidated interim financial statements.*

# Condensed Consolidated Interim Statements of Cash Flows

***In thousands of Canadian dollars,***
***(Unaudited)***

| | | Three months ended | | Nine months ended | |
|---|---|---|---|---|---|
| | | **September 30, 2015** | September 30, 2014 | **September 30, 2015** | September 30, 2014 |
| **OPERATING ACTIVITIES** | | | | | |
| Net income | | **$11,621** | $21,466 | **$27,731** | $41,221 |
| **Add (deduct) items not affecting cash** | | | | | |
| Fair value (gain) | [3] | **(1,368)** | (13,382) | **(1,548)** | (21,582) |
| Depreciation and amortization | | **676** | 599 | **1,975** | 1,729 |
| Non-cash compensation expense | | **128** | 121 | **265** | 260 |
| Equity income | | **-** | (166) | **-** | (500) |
| Deferred income taxes | | **4,831** | 5,061 | **10,793** | 11,274 |
| Current tax recovery | | **-** | - | **-** | (327) |
| (Gain) loss on disposition | | **(74)** | **-** | **109** | (94) |
| Financing costs | [12] | **9,396** | 8,618 | **27,718** | 25,908 |
| Interest paid | [15] | **(7,802)** | (7,291) | **(26,356)** | (23,339) |
| Net change in non-cash operating activities | [15] | **(3,909)** | 2,874 | **(12,836)** | (2,196) |
| **Cash provided by operating activities** | | **$13,499** | $17,900 | **$27,851** | $32,354 |
| **FINANCING ACTIVITIES** | | | | | |
| Increase in deferred financing | | **(603)** | (1,459) | **(3,167)** | (4,963) |
| Proceeds on issuance of common shares | | **-** | 7,022 | **2,941** | 7,830 |
| Repurchase common shares through normal course issuer bid | | **(162)** | **-** | **(162)** | - |
| Mortgage financing | | **52,312** | 56,921 | **157,658** | 181,096 |
| Mortgages repaid on maturity | | **(32,919)** | (31,701) | **(77,014)** | (101,330) |
| Mortgage principal repayments | | **(7,323)** | (5,884) | **(21,496)** | (17,232) |
| Proceeds from construction loans | | **4,090** | 8,589 | **13,242** | 13,982 |
| Construction loans repaid on maturity | | **-** | **-** | **(25,206)** | - |
| Distributions paid to non-controlling interest | | **(186)** | (225) | **(593)** | (675) |
| Dividends | | **(7,404)** | (7,730) | **(22,996)** | (22,651) |
| **Cash provided by financing activities** | | **$7,805** | $25,533 | **$23,207** | $56,057 |
| **INVESTING ACTIVITIES** | | | | | |
| Increase in restricted cash | | **(296)** | (428) | **(214)** | 764 |
| Acquisition of non-controlling interest | | **-** | (457) | **-** | (457) |
| Increase in loan receivable | | **-** | - | **-** | (4,000) |
| Increase in investment in joint venture, net of distributions | | **-** | (281) | **-** | (131) |
| Net proceeds on sale of land | | **-** | **-** | **50** | 134 |
| Acquisition and development of investment properties, net of debt assumed | | **(9,177)** | (34,011) | **(30,383)** | (83,806) |
| Capital expenditures | | **(9,873)** | (9,555) | **(23,618)** | (21,280) |
| **Cash used in investing activities** | | **$(19,346)** | $(44,732) | **$(54,165)** | $(108,776) |
| **Net increase (decrease) in cash** | | **1,958** | (1,299) | **(3,107)** | (20,365) |
| Cash, beginning of the period | | **13,782** | 8,612 | **18,847** | 27,678 |
| **Cash, end of period** | | **$15,740** | $7,313 | **$15,740** | $7,313 |

*See accompanying notes to the condensed consolidated interim financial statements.*

## 1. Corporate Information

Killam Properties Inc. ("Killam" or the "Company") is a real estate company specializing in the acquisition, management and development of multi-residential apartment buildings and manufactured home communities ("MHCs") in Canada. Killam is incorporated under the Canada Business Corporations Act. Killam's common shares are publicly traded and listed on the Toronto Stock Exchange under the symbol "KMP". The condensed consolidated interim financial statements comprise the financial statements of Killam and its subsidiaries as at September 30, 2015**.** The Company's head office operations are located at 3700 Kempt Road, Halifax, Nova Scotia, B3K 4X8 and the Company's registered office is located at 2571 Windsor Street, Halifax, Nova Scotia, B3K 5C4.

The condensed consolidated interim financial statements of the Company for the period ended September 30, 2015, were authorized for issue in accordance with a resolution of the Board of Directors on November 3, 2015.

## 2. Significant Accounting Policies

### (A) Statement of Compliance

These condensed consolidated interim financial statements have been prepared in accordance with *IAS 34 Interim Financial Reporting* (IAS 34) as issued by the International Accounting Standards Board ("IASB"). Accordingly, certain information and footnote disclosure normally included in annual financial statements prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the IASB, have been omitted or condensed.

### (B) Basis of Presentation

The condensed consolidated interim financial statements of the Company have been prepared on a historical cost basis, except for investment properties and derivative financial instruments that have been measured at fair value. Historical cost is generally based on the fair value of the consideration given in exchange for assets. The condensed consolidated interim financial statements have been prepared on a going concern basis and are presented in Canadian dollars, which is Killam's functional currency, and all values are rounded to the nearest thousand ($000), except share, per share or as noted amounts.

The condensed consolidated interim financial statements should be read in conjunction with the most recently issued Annual Report of Killam, which includes information necessary or useful to understanding the Company's business and financial statement presentation. In particular, the Company's significant accounting policies were presented in Note 2 to the consolidated financial statements for the year ended December 31, 2014, and, after the changes described in Note 2(c), have been consistently applied in the preparation of these condensed consolidated interim financial statements.

The operating results for the three and nine months ended September 30, 2015, are not necessarily indicative of results that may be expected for the full year ended December 31, 2015, due to seasonal variations in property expenses and other factors.

### (C) Basis of Consolidation

On March 31, 2015, the Company acquired 50% of the shares of a Corporation which owns vacant land for future development. The Company has determined that it controls the Corporation, and therefore consolidates the Corporation's assets, liabilities and the results of its operations. As the Company will purchase the remaining 50% of the shares in the Corporation upon completion of the development, the non-controlling interest is recorded as a liability, and is included in other non-current long-term liabilities.

***Tabular amounts in thousands of Canadian dollars (except share, per share or as noted amounts)***

## 3. Investment Properties

**As at and for the nine month period ended September 30, 2015**

| **Segment** | **Apartments** | **MHCs** | **Other** | **IPUC** | **Total** |
|---|---|---|---|---|---|
| **Level** | **3** | **3** | **3** | **3** | |
| **Balance, beginning of period** | **$1,568,203** | **$122,629** | **$2,223** | **$40,840** | **$1,733,895** |
| *Fair value gain (loss) included in net income* | | | | | |
| Fair value gain (loss) on investment property | **2,032** | **(484)** | **-** | **-** | **1,548** |
| *Acquisitions and dispositions* | | | | | |
| Acquisitions | **10,791** | **-** | **28,924** | **10,700** | **50,415** |
| Dispositions | **-** | **-** | **-** | **(1,143)** | **(1,143)** |
| *Other movements* | | | | | |
| Transfer from IPUC | **36,147** | **-** | **-** | **(36,147)** | **-** |
| Transfer to IPUC | **(2,300)** | **-** | **-** | **2,300** | **-** |
| Capital expenditure on investment property | **20,403** | **1,705** | **946** | **-** | **23,054** |
| Capital expenditure on IPUC | **-** | **-** | **-** | **13,396** | **13,396** |
| Interest capitalized on IPUC | **-** | **-** | **-** | **925** | **925** |
| **Balance, end of period** | **$1,635,276** | **$123,850** | **$32,093** | **$30,871** | **$1,822,090** |

As at and for the year ended December 31, 2014

| Segment | Apartments | MHCs | Other | IPUC | Total |
|---|---|---|---|---|---|
| Level | 3 | 3 | 3 | 3 | |
| Balance, beginning of year | $1,334,153 | $115,414 | $2,176 | $24,373 | $1,476,116 |
| *Fair value (loss) gain included in net income* | | | | | |
| Fair value (loss) gain on investment property | (298) | 4,730 | - | 336 | 4,768 |
| *Acquisitions and dispositions* | | | | | |
| Acquisitions | 231,618 | - | - | - | 231,618 |
| Dispositions | (41,464) | (40) | - | - | (41,504) |
| *Other movements* | | | | | |
| Transfer from IPUC | 14,098 | - | - | (14,098) | - |
| Capital expenditure on investment property | 30,096 | 2,525 | 47 | - | 32,668 |
| Capital expenditure on IPUC | - | - | - | 29,013 | 29,013 |
| Interest capitalized on IPUC | - | - | - | 1,216 | 1,216 |
| Balance, end of year | $1,568,203 | $122,629 | $2,223 | $40,840 | $1,733,895 |

During the three and nine months ended September 30, 2015, the Company capitalized salaries of $0.8 million and $2.2 million (three and nine months ended September 30, 2014 - $0.8 million and $2.3 million), as part of its project improvement, suite renovation and development programs.

For the three and nine months ended September 30, 2015, interest costs associated with the general corporate borrowings used to fund development have been capitalized to the respective development using the Company's weighted average borrowing rate of 3.65% (December 31, 2014 - 3.93%). Interest costs associated with construction loans are capitalized to the respective development using the actual borrowing rate associated with the loan.

***Tabular amounts in thousands of Canadian dollars (except share, per share or as noted amounts)***

## 3. Investment Properties (continued)

Investment properties with a fair value of $1,783.8 million at September 30, 2015, (December 31, 2014 - $1,683.4 million) are pledged as collateral against the Company's mortgages payable.

| Class of property | Fair value at September 30, 2015 | Fair value at December 31, 2014 | Valuation technique | Unobservable inputs | 2015 Inputs | 2014 Inputs |
|---|---|---|---|---|---|---|
| **Apartments** -Level 3 | **$1,635,276** | $1,568,203 | Capitalization of stabilized net income approach | - Capitalization rate (weighted average)<br>- Vacancy rate (weighted average)<br>- Management fee rate | **5.58%**<br>**3.60%**<br>**3.50%** | 5.63%<br>3.60%<br>3.50% |
| **MHCs** -Level 3 | **$123,850** | $122,629 | Capitalization of stabilized net income approach | - Capitalization rate (weighted average)<br>- Vacancy rate<br>- Management fee rate | **6.64%**<br>**1.70%**<br>**3.00%** | 6.69%<br>1.70%<br>3.00% |

The investment property segment defined as Other (level 3) consists of three commercial properties.

IPUC includes properties under construction and land held for future development and is recorded at cost of $30.9 million (December 31, 2014 - $40.8 million) as fair value cannot be reliably determined.

### *Sensitivity Analysis*

The significant unobservable inputs used in the fair value measurements categorized within Level 3 of the fair value hierarchy include cap-rates, vacancy rates and management fee rates. Investment property valuations are most sensitive to changes in the cap-rate. The cap-rate assumptions for the investment properties are included in the following table:

| | **September 30, 2015** | | | December 31, 2014 | | |
|---|---|---|---|---|---|---|
| | **Low** | **High** | **Effective Weighted Average** | Low | High | Effective Weighted Average |
| **Apartments** | | | **5.58%** | | | 5.63% |
| Halifax | 5.00% | 7.06% | 5.59% | 5.00% | 7.00% | 5.60% |
| Moncton | 5.15% | 8.00% | 5.91% | 5.15% | 8.00% | 5.95% |
| Fredericton | 5.15% | 6.25% | 5.89% | 5.15% | 6.25% | 5.89% |
| Saint John | 6.00% | 6.75% | 6.42% | 6.25% | 6.75% | 6.53% |
| St. John's | 5.00% | 6.00% | 5.75% | 5.15% | 6.00% | 5.83% |
| Charlottetown | 5.50% | 6.20% | 5.93% | 5.50% | 6.20% | 5.89% |
| Ontario | 4.50% | 5.00% | 4.85% | 4.50% | 5.10% | 4.96% |
| Alberta | 5.00% | 5.00% | 5.00% | 5.00% | 5.00% | 5.00% |
| Other Atlantic | 5.75% | 7.00% | 6.50% | 5.75% | 7.00% | 6.83% |
| **MHCs** | | | **6.64%** | | | 6.69% |
| Ontario | 7.00% | 8.00% | 7.21% | 7.00% | 8.00% | 7.25% |
| Nova Scotia | 5.75% | 7.00% | 6.18% | 5.75% | 7.50% | 6.25% |
| New Brunswick | 8.00% | 8.00% | 8.00% | 8.00% | 8.00% | 8.00% |
| Newfoundland | 7.25% | 7.25% | 7.25% | 7.25% | 7.25% | 7.25% |

***Tabular amounts in thousands of Canadian dollars (except share, per share or as noted amounts)***

## 3. Investment Properties (continued)

The quantitative sensitivity analysis shown below illustrates the value increase or decrease in the Company's portfolio of properties given the change in the noted input.

| Class of property | Capitalization rate | | Vacancy rate | Management fee rate |
|---|---|---|---|---|
| | *10 basis points increase* | *10 basis points decrease* | *1% increase/ decrease in vacancy* | *1% increase/ decrease in management fees* |
| Apartments | $(28,816) | $29,869 | $22,708 | $25,999 |
| MHCs | $(1,838) | $1,894 | $1,602 | $2,080 |

## 4. Property and Equipment

| | **September 30, 2015** | | December 31, 2014 | |
|---|---|---|---|---|
| **As at** | **Cost** | **Accumulated Depreciation** | Cost | Accumulated Depreciation |
| Land | **$270** | **$ -** | $270 | $ - |
| Building | **1,824** | **192** | 1,824 | 156 |
| Heavy equipment | **225** | **89** | 222 | 81 |
| Vehicles | **1,314** | **435** | 1,271 | 399 |
| Furniture, fixtures and equipment | **4,519** | **3,315** | 4,080 | 2,885 |
| Leaseholds | **882** | **151** | 803 | 95 |
| | **9,034** | **4,182** | 8,470 | 3,616 |
| Less: accumulated depreciation | **(4,182)** | | (3,616) | |
| | **$4,852** | | $4,854 | |

Land and building represents the Company’s ownership of a 50% interest in the land and building that its head office occupies. Under IFRS, owner-occupied property is required to be accounted for as property and equipment and not investment property.

Property with a carrying value of $1.9 million (December 31, 2014 - $1.9 million ) is pledged as collateral against the Company's mortgage payable.

## 5. Investments in Joint Venture

A joint venture, previously accounted for using the equity method, was dissolved on December 9, 2014, and Killam purchased the remaining 75% ownership interest in the properties. Subsequent to the purchase, Killam sold a 50% interest in two of the properties to a third-party and these properties are now accounted for as joint operations.

***Tabular amounts in thousands of Canadian dollars (except share, per share or as noted amounts)***

## 6. Mortgages and Loans Payable

| As at | **September 30, 2015** | | December 31, 2014 | |
|---|---|---|---|---|
| | **Weighted Average Interest** | **Debt Balance** | Weighted Average Interest | Debt Balance |
| Mortgages and loans payable | | | | |
| Fixed rate | **3.32%** | **$904,470** | 3.60% | $839,813 |
| Variable rate | **4.27%** | **7,445** | 4.14% | 4,760 |
| Vendor financing | **3.03%** | **5,154** | 6.81% | 149 |
| **Total** | | **$917,069** | | $844,722 |
| Current | | **120,235** | | 115,248 |
| Non-current | | **796,834** | | 729,474 |
| | | **$917,069** | | $844,722 |

Mortgages are collateralized by a first charge on the properties of the Company and vendor mortgages are collateralized by either a second charge on the property and/or a general corporate guarantee.

As of September 30, 2015, unamortized deferred financing costs of $19.4 million (December 31, 2014 - $17.2 million) and mark-to-market premiums on mortgages assumed on acquisitions of $0.9 million (December 31, 2014 – $1.2 million) are netted against mortgages and loans payable.

Estimated future principal payments required to meet mortgage obligations as at September 30, 2015, are as follows:

| | **Principal repayments by 12 month periods ended September 30,** |
|---|---|
| 2016 | $120,235 |
| 2017 | 139,562 |
| 2018 | 116,310 |
| 2019 | 154,282 |
| 2020 | 190,757 |
| Subsequent | 214,438 |
| | 935,584 |
| Unamortized deferred financing costs | (19,416) |
| Unamortized mark-to-market adjustments | 901 |
| | $917,069 |

The Company has two credit facilities with major financial institutions, which are set out as follows:

I. A $2.0 million revolving demand facility that can be used for the Company's acquisition program and general business purposes. The interest rate on the debt is prime plus 125 bps on prime rate advances or 225 bps over Banker's Acceptances (BAs). Killam has the right to choose between prime rate advances and BAs based on available rates and timing requirements. As at September 30, 2015, the Company had assets with a carrying value of $1.9 million pledged to the line and a balance outstanding of $Nil (December 31, 2014 - $Nil). The agreement includes certain covenants and undertakings of which the Company is in compliance.

II. A $1.5 million revolving demand facility that can be used for the Company's acquisition program and for general business purposes. The interest rate on the debt is prime plus 175 bps on advances and 135 bps on issuance of letters of credit in addition to 50 bps per annum. As at September 30, 2015, the Company had assets with a carrying value of $1.8 million pledged as collateral and letters of credit totaling $1.5 million outstanding against the facility (December 31, 2014 - $1.5 million). The agreement includes certain covenants and undertakings of which the Company is in compliance.

*Tabular amounts in thousands of Canadian dollars (except share, per share or as noted amounts)*

## 7. Construction Loans

At September 30, 2015, the Company had access to two floating rate non-revolving demand construction loans totaling $28.1 million for the purpose of financing the development projects. Payments are made monthly on an interest only basis. The construction loans have interest rates ranging from prime to prime plus 0.75%. Once construction has been completed and rental targets achieved, the construction loans will be repaid in full and converted into conventional mortgages. As at September 30, 2015, $20.0 million (December 31, 2014 - $31.9 million) was drawn at a weighted average interest rate of 3.60% (December 31, 2014 - 3.84%).

## 8. Convertible Debentures

| Face Interest Rate % | Effective Interest Rate % | Conversion Price | Face Amount | Maturity | September 30, 2015 | December 31, 2014 |
|---|---|---|---|---|---|---|
| 5.65% | 7.30% | $13.40 | $57,500 | November 30, 2017 | **$55,678** | $55,108 |
| 5.45% | 6.30% | $14.60 | $46,000 | June 30, 2018 | **45,082** | 44,859 |
| | | | | | **100,760** | 99,967 |
| Less: Deferred financing charges | | | | | **(1,561)** | (2,000) |
| | | | | | **$99,199** | $97,967 |

*Tabular amounts in thousands of Canadian dollars (except share, per share or as noted amounts)*

# 9. Capital Stock and Contributed Surplus

## Capital Stock

Authorized:
Unlimited number of common shares, with no par value
Unlimited number of preferred shares, issuable in series, with no par value

Issued:
The following table summarizes the changes in issued common shares of the Company:

| | **2015** | | 2014 | |
|---|---|---|---|---|
| | **Number of Shares** | **Value** | Number of Shares | Value |
| **Balance, January 1** | **60,475,978** | **$459,138** | 54,458,774 | $398,181 |
| Dividend reinvestment plan | **96,438** | **1,010** | 64,575 | 671 |
| Stock options exercised | **234,917** | **2,191** | 102,500 | 561 |
| Stock issued for acquisitions | **1,092,548** | **12,000** | 75,330 | 800 |
| Restricted share units redeemed | **12,566** | **147** | 2,733 | 32 |
| **Balance, March 31** | **61,912,447** | **$474,486** | 54,703,912 | $400,245 |
| Dividend reinvestment plan | **174,157** | **1,839** | 72,539 | 746 |
| Stock options exercised | **132,990** | **1,267** | 31,250 | 260 |
| Restricted share units redeemed | **-** | **-** | 1,401 | 17 |
| **Balance, June 30** | **62,219,594** | **$477,592** | 54,809,102 | $401,268 |
| Dividend reinvestment plan | **198,846** | **2,009** | 48,775 | 506 |
| Stock options exercised | **-** | **-** | 3,000 | 28 |
| Stock issued for acquisitions | **249,311** | **2,489** | - | - |
| Restricted share units redeemed | **6,316** | **10** | 3,668 | 36 |
| Issued for cash | **-** | **-** | 691,488 | 7,000 |
| Repurchase through normal course issuer bid | **(21,000)** | **(167)** | - | - |
| **Balance, September 30** | **62,653,067** | **$481,933** | 55,556,033 | $408,838 |

## Normal Course Issuer Bid

In July 2015, the Company announced that the Toronto Stock Exchange (the "TSX") had accepted Killam's notice of intention to make a normal course issuer bid for its common shares. Under the normal course issuer bid, Killam may acquire up to 1,500,000 common shares commencing on July 30, 2015, and ending July 29, 2016. All purchases of common shares will be made through the facilities of the TSX at the market price of the shares at the time of the acquisition. Daily repurchases by Killam are limited to 23,698 common shares, other than block purchase exemptions. Any shares acquired will be cancelled.

For the three and nine months ended September 30, 2015, 21,000 common shares were purchased and cancelled. The shares were purchased at an average price of $9.98.

*Tabular amounts in thousands of Canadian dollars (except share, per share or as noted amounts)*

## 9. Capital Stock and Contributed Surplus (Continued)

### Contributed Surplus

| | 2015 | 2014 |
|---|---|---|
| **Balance, January 1** | **$2,417** | $2,302 |
| Stock options expensed | **-** | 3 |
| Stock options exercised | **(274)** | (67) |
| Restricted share units issued | **409** | 390 |
| Restricted share units redeemed | **(229)** | (32) |
| **Balance, March 31** | **$2,323** | $2,596 |
| Stock options expensed | **-** | 1 |
| Stock options exercised | **(212)** | (31) |
| Restricted share units issued | **125** | 117 |
| Restricted share units redeemed | **-** | (23) |
| **Balance, June 30** | **$2,236** | $2,660 |
| Stock options exercised | **-** | (3) |
| Restricted share units issued | **128** | 121 |
| Restricted share units redeemed | **(93)** | (46) |
| Normal course issuer bid | **(48)** | - |
| **Balance, September 30** | **$2,223** | $2,732 |

## 10. Share-Based Compensation

Share-based compensation expense for the three and nine months ended September 30, 2015 and 2014 is as follows:

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | **2015** | 2014 | **2015** | 2014 |
| Stock option plan | **$-** | $- | **$-** | $4 |
| Restricted share unit plan | **128** | 121 | **361** | 347 |
| **Total share-based compensation expense** | **$128** | $121 | **$361** | $351 |

***Tabular amounts in thousands of Canadian dollars (except share, per share or as noted amounts)***

## 10. Share-Based Compensation (Continued)

Options exercised during the three and nine months ended September 30 are as follows:

| | **2015** | | 2014 | |
|---|---|---|---|---|
| | **Number of Options** | **Weighted Average Exercise Price** | Number of Options | Weighted Average Exercise Price |
| **Outstanding, January** | **367,907** | **$8.16** | 550,407 | $7.66 |
| Exercised | **(234,917)** | **8.16** | (102,500) | 5.71 |
| **Outstanding, March 31** | **132,990** | **$8.16** | 447,907 | $8.10 |
| Exercised | **(132,990)** | **8.16** | (31,250) | 7.34 |
| **Outstanding, June 30** | **-** | **-** | 416,657 | $8.16 |
| Exercised | **-** | **-** | (3,000) | 8.16 |
| **Outstanding, September 30** | **-** | **-** | 413,657 | $8.16 |

The following table summarizes the stock options outstanding:

| **As at** | **September 30, 2015** | | | December 31, 2014 | | |
|---|---|---|---|---|---|---|
| **Exercise Price** | **Number of Options Outstanding** | **Remaining Contractual Life** | **Options Exercisable** | Number of Options Outstanding | Remaining Contractual Life | Options Exercisable |
| **$8.16** | - | - | - | 367,907 | 0.40 years | 367,907 |
| | - | | - | 367,907 | | 367,907 |

All outstanding stock options were exercised as of May 28, 2015.

***Tabular amounts in thousands of Canadian dollars (except share, per share or as noted amounts)***

## 10. Share-Based Compensation (Continued)

The details of the restricted share units issued under the restricted share unit plan are shown below:

| | **2015** | | 2014 | |
|---|---|---|---|---|
| | **Number of RSUs** | **Weighted Average Issue Price** | Number of RSUs | Weighted Average Issue Price |
| **Outstanding, January 1** | **140,513** | **$11.01** | 94,345 | $12.29 |
| Granted | **61,228** | **10.87** | 62,672 | 10.37 |
| Redeemed | **(20,420)** | **12.64** | (2,847) | 12.14 |
| Additional restricted share distributions | **1,937** | **10.74** | 1,428 | 10.42 |
| **Outstanding, March 31** | **183,258** | **$10.78** | 155,598 | $11.53 |
| Granted | **6,000** | **10.41** | 5,918 | 10.56 |
| Redeemed | **-** | **-** | (2,044) | 12.68 |
| Additional restricted share distributions | **2,604** | **10.60** | 2,272 | 10.32 |
| **Outstanding, June 30** | **191,862** | **$10.77** | 161,744 | $11.46 |
| Granted | **7,920** | **10.15** | 6,016 | 10.39 |
| Redeemed | **(9,084)** | **11.78** | (4,644) | 11.54 |
| Additional restricted share distributions | **2,867** | **10.11** | 2,338 | 10.43 |
| **Outstanding, September 30** | **193,565** | **$10.60** | 165,454 | $11.41 |

## 11. Home Sales

| | **Three months ended September 30,** | | **Nine months ended September 30,** | |
|---|---|---|---|---|
| | **2015** | 2014 | **2015** | 2014 |
| Home sales revenues | **$193** | $396 | **$506** | $1,216 |
| Cost of home sales | **(164)** | (343) | **(448)** | (1,094) |
| New home placement fees | **-** | - | **8** | - |
| Operating expenses | **(10)** | (13) | **(37)** | (46) |
| Income from home sales | **$19** | $40 | **$29** | $76 |

## 12. Financing Costs

| | **Three months ended September 30,** | | **Nine months ended September 30,** | |
|---|---|---|---|---|
| | **2015** | 2014 | **2015** | 2014 |
| Mortgage, loan and construction loan interest | **$7,991** | $7,391 | **$23,905** | $21,957 |
| Amortization of fair value adjustments on assumed debt | **(153)** | (125) | **(429)** | (376) |
| Amortization of loss on interest rate hedge | **15** | - | **45** | - |
| Convertible debenture interest | **1,706** | 1,691 | **5,122** | 5,059 |
| Capitalized interest | **(163)** | (339) | **(925)** | (732) |
| | **$9,396** | $8,618 | **$27,718** | $25,908 |

*Tabular amounts in thousands of Canadian dollars (except share, per share or as noted amounts)*

## 13. Per Share Information

The following is the weighted average number of shares outstanding for the three and nine months ended September 30, 2015, and 2014.

| For the three months ended September 30, | 2015 | 2014 |
|---|---|---|
| Weighted average number of shares outstanding - basic | **62,469,801** | 54,916,532 |
| Unexercised dilutive options | **-** | 92,034 |
| Restricted share units | **192,177** | 163,476 |
| Convertible debentures | **10,402,010** | 10,000,000 |
| Weighted average number of shares outstanding - diluted | **73,063,988** | 65,172,042 |

| For the nine months ended September 30, | 2015 | 2014 |
|---|---|---|
| Weighted average number of shares outstanding - basic | **61,874,398** | 54,759,217 |
| Unexercised dilutive options | **109,621** | 125,434 |
| Restricted share units | **176,887** | 145,769 |
| Convertible debentures | **10,402,010** | 10,000,000 |
| Weighted average number of shares outstanding - diluted | **72,562,916** | 65,030,420 |

The following is the adjustment to net income applicable to common shareholders used in the diluted earnings per share calculation.

| For the three months ended September 30, | 2015 | 2014 |
|---|---|---|
| Net income applicable to common shareholders | **$11,462** | $20,491 |
| Adjustment for dilutive effect of convertible debentures | **1,195** | 1,184 |
| Adjusted net income for diluted per share amounts | **$12,657** | $21,675 |

| For the nine months ended September 30, | 2015 | 2014 |
|---|---|---|
| Net income applicable to common shareholders | **$27,137** | $39,031 |
| Adjustment for dilutive effect of convertible debentures | **3,585** | 3,541 |
| Adjusted net income for diluted per share amounts | **$30,722** | $42,572 |

***Tabular amounts in thousands of Canadian dollars (except share, per share or as noted amounts)***

## 14. Segmented Information

The Company operates in two rental segments of the multi-family residential industry: apartments and MHCs, all located in Canada. The Other segment includes three commercial properties and head office administration costs. The accounting policies of these segments are the same as those described in Note 2 of the consolidated financial statements for the year ended December 31, 2014. The segments are analyzed based on net operating. The operating results, assets and liabilities, and capital expenditures of the segments are as follows:

| **For the three months ended September 30, 2015** | **Apartments** | **MHCs** | **Other** | **Total** |
|---|---|---|---|---|
| Property revenue | **$37,459** | **$4,629** | **$1,105** | **$43,193** |
| Property operating expenses | **(13,865)** | **(1,599)** | **(551)** | **(16,015)** |
| Net operating income | **$23,594** | **$3,030** | **$554** | **$27,178** |
| Home sales & corporate income | - | - | **378** | **378** |
| Financing costs | **(6,959)** | **(624)** | **(1,813)** | **(9,396)** |
| Depreciation and amortization | **(314)** | **(51)** | **(311)** | **(676)** |
| Administration | **(472)** | **(87)** | **(1,915)** | **(2,474)** |
| Income before fair value gain, gain (loss) on disposition and income taxes | **$15,849** | **$2,268** | **$(3,107)** | **$15,010** |
| | | | | |
| Capital expenditures on investment properties | **$8,459** | **$707** | **$577** | **$9,743** |

| For the three months ended September 30, 2014 | **Apartments** | **MHCs** | **Other** | **Total** |
|---|---|---|---|---|
| Property revenue | $33,232 | $4,407 | $138 | $37,777 |
| Property operating expenses | (12,378) | (1,512) | (114) | (14,004) |
| Net operating income | $20,854 | $2,895 | $24 | $23,773 |
| Home sales, equity income & corporate income | - | - | 569 | 569 |
| Financing costs | (6,452) | (632) | (1,534) | (8,618) |
| Depreciation and amortization | (282) | (46) | (271) | (599) |
| Administration | (366) | (83) | (1,531) | (1,980) |
| Income before fair value gain and income taxes | $13,754 | $2,134 | $(2,743) | $13,145 |
| | | | | |
| Capital expenditures on investment properties | $8,564 | $792 | $7 | $9,363 |

***Tabular amounts in thousands of Canadian dollars (except share, per share or as noted amounts)***

## 14. Segmented Information (continued)

| For the nine months ended September 30, 2015 | Apartments | MHCs | Other | Total |
|---|---|---|---|---|
| Property revenue | **$110,819** | **$11,092** | **$2,270** | **$124,181** |
| Property operating expenses | **(45,786)** | **(4,193)** | **(1,173)** | **(51,152)** |
| Net operating income | **65,033** | **6,899** | **1,097** | **73,029** |
| Home sales, equity income & corporate income | **-** | **-** | **1,105** | **1,105** |
| Financing costs | **(20,861)** | **(1,868)** | **(4,989)** | **(27,718)** |
| Depreciation and amortization | **(924)** | **(148)** | **(903)** | **(1,975)** |
| Administration | **(1,239)** | **(278)** | **(5,839)** | **(7,356)** |
| Income before fair value gain, loss on disposition and income taxes | **$42,009** | **$4,605** | **$(9,529)** | **$37,085** |
| Capital expenditures on investment properties | **$20,403** | **$1,705** | **$946** | **$23,054** |

| For the nine months ended September 30, 2014 | Apartments | MHCs | Other | Total |
|---|---|---|---|---|
| Property revenue | $98,096 | $10,835 | $429 | $109,360 |
| Property operating expenses | (42,232) | (4,000) | (294) | (46,526) |
| Net operating income | 55,864 | 6,835 | 135 | 62,834 |
| Home sales, equity income & corporate income | - | - | 1,322 | 1,322 |
| Financing costs | (19,300) | (1,927) | (4,681) | (25,908) |
| Depreciation and amortization | (792) | (148) | (788) | (1,728) |
| Administration | (1,089) | (262) | (4,677) | (6,028) |
| Income before fair value gain, gain on disposition and income taxes | $34,683 | $4,498 | $(8,689) | $30,492 |
| Capital expenditures on investment properties | $18,836 | $1,539 | $16 | $20,391 |

| As at September 30, 2015 | Apartments | MHCs | Other | Total |
|---|---|---|---|---|
| Total assets | **$1,623,507** | **$153,996** | **$92,456** | **$1,869,959** |
| Total liabilities | **$884,150** | **$59,497** | **$241,871** | **$1,185,518** |

| As at December 31, 2014 | Apartments | MHCs | Other | Total |
|---|---|---|---|---|
| Total assets | $1,572,049 | $149,058 | $54,127 | $1,775,234 |
| Total liabilities | $842,283 | $58,395 | $211,873 | $1,112,551 |

There are no transactions with a single tenant that account for 10% or more of the Company's revenues.

***Tabular amounts in thousands of Canadian dollars (except share, per share or as noted amounts)***

## 15. Supplemental Cash Flow Information

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | **2015** | 2014 | **2015** | 2014 |
| **Net income items related to investing and financing activities** | | | | |
| Interest paid on mortgages payable and other | **$7,802** | $7,291 | **$23,478** | $21,591 |
| Interest paid on convertible debentures | **-** | - | **2,878** | 1,748 |
| | **$7,802** | $7,291 | **$26,356** | $23,339 |
| **Changes in non-cash operating assets and liabilities** | | | | |
| Rent and other receivables | **$(596)** | $(207) | **$(3,187)** | $(154) |
| Income tax receivable | **-** | - | **-** | (1,450) |
| Inventory | **(142)** | 109 | **(161)** | 337 |
| Other current assets | **1,436** | 1,314 | **(5,115)** | (5,160) |
| Accounts payable and accrued liabilities | **(4,607)** | 1,658 | **(4,373)** | 4,231 |
| | **$(3,909)** | $2,874 | **$(12,836)** | $(2,196) |

## 16. Accumulated Other Comprehensive Loss

| | Three months ended September 30 | | Nine months ended September 30 | |
|---|---|---|---|---|
| | **2015** | 2014 | **2015** | 2014 |
| Balance, beginning of period | **$(177)** | $- | **$(198)** | $- |
| Amortization of loss in AOCL to finance costs (net of tax $5 and $14)(1) | **10** | - | **31** | - |
| Unrealized loss of forward interest rate hedge (net of tax $16 and $86) | **-** | (40) | **-** | (209) |
| **Balance, end of period** | **$(167)** | $(40) | **$(167)** | $(209) |

(1) The cumulative aggregate loss of $198 thousand on the forward interest rate hedge will be amortized into net income as financing costs over the mortgage term, which ends in September 2020.

## 17. Financial Risk Management Objectives and Policies

The Company's principal financial liabilities are comprised of mortgages, construction loans, debentures and trade payables. The main purpose of these financial liabilities is to finance the Company's investment properties and operations. The Company has various financial assets such as trade receivables and cash, which arise directly from its operations.

The Company may also enter into derivative transactions, primarily interest rate swap contracts to manage interest rate risk arising from fluctuations in bond yields, as well as natural gas and oil swap contracts to manage price risk arising from fluctuations in these commodities. The Company entered into one derivative contract during 2014 and has not entered into any derivative transactions in 2015. It is, and has been, the Company's policy that no speculative trading in derivatives shall be undertaken.

The main risks arising from the Company's financial instruments are interest rate risk, credit risk and liquidity risk. These risks are managed as follows:

**(i) Interest rate risk**

The Company is exposed to interest rate risk as a result of its mortgages and loans payable, however this risk is mitigated through the Company's strategy to have the majority of its mortgages payable in fixed-term arrangements, as well as, at times, entering into cash flow hedges. The Company also structures its financings so as to stagger the maturities of its debt, minimizing the Company's exposure to interest rate volatility in any one year.

As at September 30, 2015, no mortgages or vendor debt had floating interest rates except for four demand loans totaling $7.4 million and two revolving demand facilities. These loans and facilities have interest rates of prime plus 1.0% - 2.0% (December 31, 2014 - prime plus 1.0% - 2.0%). Killam also has two construction loans totaling $20.0 million with floating interest rates ranging from prime to prime plus 0.75% and consequently, Killam is exposed to short-term interest rate risk on these loans.

An annualized 100 bps change in the interest rate on Killam's entire mortgage and vendor debt at September 30, 2015, would affect financing costs by approximately $9.3 million per year. However, only $93.0 million of Killam's fixed mortgage and vendor debt matures in the next twelve months. Assuming these mortgages are refinanced at similar terms, except at a 100 bps increase in interest rates, financing costs would increase by $0.9 million per year.

**(ii) Credit risk**

Credit risk arises from the possibility that tenants may experience financial difficulty and be unable to fulfill their lease term commitments. The Company mitigates the risk of credit loss through the diversification of its existing portfolio and limiting its exposure to any one tenant. Credit assessments are conducted with respect to all new leasing and the Company also obtains a security deposit to assist in potential recovery requirements. In addition, the receivable balances are monitored on an ongoing basis with the result that the Company's exposure to bad debt is not significant. The Company's bad debt expense experience has historically been less than 0.4% of revenues. None of Killam's tenants account for more than 1% of the tenant receivables as at each of the period-ends presented in these financial statements. The maximum exposure to credit risk is the carrying amount of each class of financial assets as disclosed in this note.

***Tabular amounts in thousands of Canadian dollars (except share, per share or as noted amounts)***

## 17. Financial Risk Management Objectives and Policies (continued)

**(iii) Liquidity risk**

Management manages the Company's cash resources based on financial forecasts and anticipated cash flows. The Company structures its financings so as to stagger the maturities of its debt, thereby minimizing the Company's exposure to liquidity risk in any one year. In addition, the Company's apartments qualify for CMHC insured debt, thereby reducing the refinancing risk on mortgage maturities. The Company's MHCs do not qualify for CMHC insured debt, however, they continue to have access to mortgage debt. Management does not anticipate liquidity concerns on the maturity of its mortgages as funds continue to be accessible in the multi-residential sector.

During the three and nine months ended September 30, 2015, the Company refinanced $32.0 million and $74.7 million of maturing apartment mortgages with new mortgages totaling $43.8 million and $109.4 million for net proceeds of $11.8 million and $34.7 million. As well, during the three and nine months ended September 30, 2015, the Company refinanced $1.0 million and $2.4 million of a maturing MHC mortgage for net proceeds of $1.1 million and $2.6 million.

The following table presents the principal payments and maturities of the Company's liabilities over the next five years as at September 30,2015:

| For the twelve months ended September 30, | Mortgage and loans payable | Construction loans | Convertible debentures | Total |
|---|---|---|---|---|
| 2016 | $120,235 | $19,977 | $ - | **$140,212** |
| 2017 | 139,562 | - | - | **139,562** |
| 2018 | 116,310 | - | 57,500 | **173,810** |
| 2019 | 154,282 | - | 46,000 | **200,282** |
| 2020 | 190,757 | - | - | **190,757** |
| Thereafter | 214,438 | - | - | **214,438** |
| | $935,584 | $19,977 | $103,500 | **$1,059,061** |

### Capital Management

The primary objective of the Company's capital management is to ensure that it maintains a healthy capital ratio in order to support its business and maximize shareholder value. The Company manages its capital structure and makes adjustments to it in light of changes in economic conditions. To maintain or adjust the capital structure, the Company may adjust the dividend payment to shareholders, issue new shares, issue debt securities or adjust mortgage financing on properties.

The Company monitors capital using a total debt to total assets ratio. The Company's strategy is for its total debt to total assets ratio to not exceed 65%. The calculation of the total debt to total assets is summarized as follows:

| As at | September 30, 2015 | December 31, 2014 |
|---|---|---|
| Mortgages, loans payables and construction loans | **$937,046** | $876,666 |
| Convertible debentures | **99,199** | 97,967 |
| Total debt | **$1,036,245** | $974,633 |
| Total assets | **$1,869,959** | $1,775,234 |
| Total debt as a percentage of total assets | **55.4%** | 54.9% |

The above calculation is sensitive to changes in the fair value of investment properties, in particular, cap-rate changes. A 10 bps increase in the weighted average cap-rate as at September 30, 2015, would increase the debt as a percentage of assets by 90 bps.

***Tabular amounts in thousands of Canadian dollars (except share, per share or as noted amounts)***

## 17. Financial Risk Management Objectives and Policies (continued)

### Fair Value Measurement

Financial instruments are defined as a contractual right or obligation to receive or deliver cash or another financial asset. The following table presents the classification, subsequent measurement, carrying values and fair values of the Company's financial assets and liabilities:

| | | **September 30, 2015** | | December 31, 2014 | |
|---|---|---|---|---|---|
| **Classification** | **Subsequent Measurement** | **Carrying Value** | **Fair Value** | Carrying Value | Fair Value |
| **Financial Assets:** | | | | | |
| Loans receivable (a) | Amortized cost | **$4,950** | **$4,980** | $4,000 | $4,027 |
| **Financial Liabilities:** | | | | | |
| Mortgages (b) | Amortized cost | **$917,069** | **$975,242** | $844,722 | $941,158 |
| Convertible debentures (c) | Amortized cost | **$99,199** | **$103,669** | $97,967 | $103,996 |

The fair value of cash and cash equivalents, as well as the Company's short-term financial instruments, comprising accounts receivable, restricted cash, accounts payable and accrued liabilities, security deposits, loans and construction loans, which approximate carrying value due to their short-term nature or because they are based on current market rates.

(a) The fair value of the loan receivable is based upon discounted future cash flows using discount rates that reflect current market conditions for instruments with similar terms and risks. Such fair value estimates are not necessarily indicative of the amounts the Company might receive or pay in actual market transactions (level 2).

(b) The fair value of mortgages are based upon discounted future cash flows using discount rates that reflect current market conditions for instruments with similar terms and risks. Such fair value estimates are not necessarily indicative of the amounts the Company might pay or receive in actual market transactions (level 2).

(c) The fair value of the convertible debentures are based on a quoted market price as at the reporting date (level 1).

The interest rates used to discount the estimated cash flows, when applicable, are based on the 5-year government yield curve at the reporting date, plus an adequate credit spread, and were as follows:

| **As at** | **September 30, 2015** | December 31, 2014 |
|---|---|---|
| Mortgages - Apartments | **1.63%** | 2.11% |
| Mortgages - MHCs | **3.43%** | 3.91% |

As at September 30, 2015, and December 31, 2014, the Company did not have any financial assets or liabilities measured at fair value on the consolidated statements of financial position.

## 18. Related Party Transactions

Killam contracted APM Construction Services Inc. ("APM") to act as Project Manager on a development project in St. John's, NL, which was completed in March 2015. APM is an entity controlled by a director of Killam. APM was paid an industry standard management fee of approximately 4% of the construction costs. For the three and nine months ended September 30, 2015, Killam paid APM $18 thousand and $0.1 million for construction management services (September 30, 2014 - $0.1 million and $0.2 million). As of September 30 2015, Killam does not have any construction projects on-going with APM.

Killam has a 50% interest in a commercial complex that houses its head office. The remaining 50% interest is owned by a company controlled by an executive and director of Killam. In addition, the property manager for the commercial complex is controlled by the executive and director and is paid an industry standard property management fee. Occasionally, Killam will also pay market leasing placement fees, to the company controlled by an executive and director of Killam, for placement of a commercial tenant in a property owned by Killam. Killam paid $90 thousand in project manager fees during Q3-2015 related to leasehold improvements completed for a commercial tenant.

On March 31, 2015, Killam acquired the Brewery Market, located in Halifax, NS, from Halkirk Properties Limited, for $22.3 million, which is partially owned by a director of Killam. Killam also acquired a 50% interest in a Corporation, which owns vacant land adjacent the Brewery Market for future development. The remaining 50% is also owned by Halkirk Properties Limited ("Halkirk").

During Q3-2015, Killam and Halkirk commenced development of a 240-unit building on the vacant land adjacent to the Brewery Market. Construction of the development is managed by Killam and cost of construction will be funded 50/50 by each partner.

## 19. Subsequent Events

On October 15, 2015, the Company announced a dividend of $0.05 per share, payable on November 16, 2015, to shareholders of record on October 31, 2015.

On October 6, 2015, Killam's Board of Directors unanimously approved the proposed reorganization of Killam into a real estate investment trust. The reorganization will be accomplished by way of plan of arrangement, and among other approvals, will be subject to shareholder approval at a special meeting to be held on or about December 8, 2015.