Condensed Consolidated Interim Financial Statements

[unaudited]

For the three and six months ended June 30, 2017 and 2016

Condensed Consolidated Interim Statements of Financial Position

In thousands of Canadian dollars,
[unaudited]

	Note	**June 30, 2017**	December 31, 2016
ASSETS			
Non-current assets			
Investment properties	[3]	**$2,076,027**	$1,942,809
Property and equipment		**5,065**	4,787
Other non-current assets		**950**	950
		$2,082,042	$1,948,546
Current assets			
Cash		**$17,706**	$24,652
Rent and other receivables		**3,694**	2,895
Other current assets		**15,245**	11,540
		36,645	39,087
TOTAL ASSETS		**$2,118,687**	$1,987,633
EQUITY AND LIABILITIES			
Unitholders' equity	[9]	**$859,300**	$750,450
Accumulated other comprehensive loss ("AOCL")		**(67)**	(97)
Non-controlling interest		**119**	113
Total Equity		**$859,352**	$750,466
Non-current liabilities			
Mortgages and loans payable	[5]	**$934,628**	$885,652
Convertible debentures	[7]	**—**	46,690
Other liabilities		**11,312**	12,563
Exchangeable units	[8]	**49,219**	46,158
Deferred income tax	[13]	**92,489**	84,547
Deferred unit-based compensation	[11]	**4,189**	2,988
		$1,091,837	$1,078,598
Current liabilities			
Mortgages and loans payable	[5]	**$110,156**	$111,862
Construction loans	[6]	**22,405**	18,509
Accounts payable and accrued liabilities		**34,937**	28,198
		167,498	158,569
Total Liabilities		**$1,259,335**	$1,237,167
TOTAL EQUITY AND LIABILITIES		**$2,118,687**	$1,987,633
Commitments and contingencies	[18]		
Financial guarantees	[19]		

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

Approved on behalf of the Board of Trustees

(signed) "G. Wayne Watson "
Trustee

(signed) "Philip D. Fraser "
Trustee

Condensed Consolidated Interim Statements of Income and Comprehensive Income

In thousands of Canadian dollars, [unaudited]

	Note	Three months ended June 30, 2017	Three months ended June 30, 2016	Six months ended June 30, 2017	Six months ended June 30, 2016
Property revenue		**$45,898**	$43,847	**$90,203**	$86,054
Property operating expenses					
Operating expenses		**(7,106)**	(6,866)	**(14,783)**	(13,912)
Utility and fuel expenses		**(4,505)**	(4,630)	**(10,785)**	(11,341)
Property taxes		**(5,502)**	(5,081)	**(10,908)**	(10,101)
		(17,113)	(16,577)	**(36,476)**	(35,354)
Net operating income		**$28,785**	$27,270	**$53,727**	$50,700
Other income		**217**	410	**402**	699
Financing costs	[12]	**(8,021)**	(9,700)	**(16,789)**	(19,280)
Depreciation		**(191)**	(219)	**(356)**	(427)
Amortization of deferred financing costs		**(441)**	(369)	**(845)**	(733)
Administration		**(2,755)**	(3,069)	**(5,675)**	(6,667)
Income before fair value adjustments, loss on disposition and income taxes		**$17,594**	$14,323	**$30,464**	$24,292
Fair value adjustment on convertible debentures		**221**	(1,151)	**690**	762
Fair value adjustment on unit-based compensation		**(35)**	(948)	**(322)**	(1,160)
Fair value adjustment on exchangeable units	[8]	**(232)**	(4,609)	**(3,093)**	(10,782)
Fair value adjustment on investment properties		**22,173**	(2,032)	**32,718**	(2,032)
Loss on disposition		**(238)**	(291)	**(238)**	(265)
Income before income taxes		**39,483**	5,292	**60,219**	10,815
Deferred tax (expense) recovery	[13]	**(4,872)**	(1,626)	**(7,959)**	38,018
Net income		**$34,611**	$3,666	**$52,260**	$48,833
Other comprehensive income loss					
Item that may be reclassified subsequently to net income					
Amortization of loss in AOCL to financing costs		**15**	15	**30**	30
Comprehensive income		**$34,626**	$3,681	**$52,290**	$48,863
Net income attributable to:					
Unitholders		**34,609**	458	**52,254**	45,371
Non-controlling interest		**2**	3,208	**6**	3,462
		$34,611	$3,666	**$52,260**	$48,833
Comprehensive income attributable to:					
Unitholders		**34,624**	473	**52,284**	45,401
Non-controlling interest		**2**	3,208	**6**	3,462
		$34,626	$3,681	**$52,290**	$48,863

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

Condensed Consolidated Interim Statements of Changes in Equity

In thousands of Canadian dollars, [unaudited]

Six months ended June 30, 2017	**Trust Units**	**Contributed Surplus**	**Retained Earnings**	**AOCL**	**Non-controlling Interest**	**Total Equity**
As at January 1, 2017	**$560,197**	**$795**	**$189,458**	**($97)**	**$113**	**$750,466**
Exchange of exchangeable units	**32**	—	—	—	—	**32**
Distribution reinvestment plan	**5,098**	—	—	—	—	**5,098**
Restricted trust unit plan	**202**	—	—	—	—	**202**
Issued for cash	**73,569**	—	—	—	—	**73,569**
Net income	—	—	**52,254**	—	**6**	**52,260**
Amortization of loss on forward interest rate hedge	—	—	—	**30**	—	**30**
Distributions declared and paid	—	—	**(18,430)**	—	—	**(18,430)**
Distributions payable	—	—	**(3,875)**	—	—	**(3,875)**
At June 30, 2017	**$639,098**	**$795**	**$219,407**	**($67)**	**$119**	**$859,352**

Six months ended June 30, 2016	Trust Units	Capital Stock	Contributed Surplus	Other Paid-in Capital	Retained Earnings	AOCL	Non-controlling Interest	Total Equity
As at January 1, 2016	$—	$484,133	$2,150	$5,681	$177,863	$ (157)	$15,658	$685,328
REIT conversion	447,566	(484,133)	(1,355)	(5,681)	(12,463)	—	—	(56,066)
Exchange of exchangeable units	549	—	—	—	—	—	—	549
Distribution reinvestment plan	3,460	—	—	—	—	—	—	3,460
Restricted trust unit plan	99	—	—	—	—	—	—	99
Issued for cash	93,623	—	—	—	—	—	—	93,623
Net income	—	—	—	—	45,371	—	3,462	48,833
Amortization of loss on forward interest rate hedge	—	—	—	—	—	30	—	30
Distributions on non-controlling interest	—	—	—	—	—	—	(505)	(505)
Acquisition of non-controlling interest	—	—	—	—	(5,598)	—	(18,495)	(24,093)
Distributions declared and paid	—	—	—	—	(14,662)	—	—	(14,662)
Distributions payable	—	—	—	—	(3,349)	—	—	(3,349)
At June 30, 2016	$545,297	$—	$795	$—	$187,162	$ (127)	$120	$733,247

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

Condensed Consolidated Interim Statements of Cash Flows

In thousands of Canadian dollars, [unaudited]

	Note	Three months ended June 30, 2017	Three months ended June 30, 2016	Six months ended June 30, 2017	Six months ended June 30, 2016
OPERATING ACTIVITIES					
Net income		**$34,611**	$3,666	**$52,260**	$48,833
Add (deduct) items not affecting cash					
Fair value adjustments		**(22,127)**	8,740	**(29,993)**	13,212
Depreciation and amortization		**632**	588	**1,201**	1,160
Non-cash compensation expense		**372**	874	**482**	1,044
Deferred income taxes		**4,872**	1,625	**7,959**	(38,018)
Loss on disposition		**238**	291	**238**	265
Net change in non-cash operating activities	[15]	**(3,166)**	(6,419)	**(704)**	(3,845)
Cash provided by operating activities		**$15,432**	$9,365	**$31,443**	$22,651
FINANCING ACTIVITIES					
Deferred financing costs paid		**(1,382)**	(1,226)	**(2,592)**	(2,268)
Net proceeds on issuance of units		**(4)**	93,761	**73,563**	93,700
Cash paid on vesting of restricted units		**(19)**	(12)	**(221)**	(184)
Redemption of convertible debentures		**(46,000)**	—	**(46,000)**	—
Mortgage financing		**55,320**	74,658	**114,267**	102,696
Mortgages repaid on maturity		**(43,726)**	(39,431)	**(47,753)**	(51,744)
Mortgage principal repayments		**(8,744)**	(7,728)	**(17,267)**	(15,385)
Proceeds from construction loans		**9,164**	1,514	**13,613**	3,561
Construction loans repaid on maturity		**—**	—	**(9,717)**	—
Distributions paid to non-controlling interest		**—**	(24,429)	**—**	(24,610)
Distributions to unitholders		**(8,464)**	(6,566)	**(16,746)**	(14,354)
Cash provided by (used in) financing activities		**($43,855)**	$90,541	**$61,147**	$91,412
INVESTING ACTIVITIES					
Decrease (increase) in restricted cash		**1,650**	(55,124)	**1,582**	(56,745)
Acquisition of investment properties, net of debt assumed		**(16,155)**	(32,468)	**(80,284)**	(32,832)
Disposition of investment property		**16,616**	(34)	**16,616**	8
Development of investment properties		**(19,167)**	(5,581)	**(25,401)**	(9,680)
Capital expenditures		**(6,463)**	(9,072)	**(12,049)**	(13,630)
Cash used in investing activities		**($23,519)**	(102,279)	**($99,536)**	($112,879)
Net (decrease) increase in cash		**(51,942)**	(2,373)	**(6,946)**	1,184
Cash, beginning of period		**69,648**	17,855	**24,652**	14,298
Cash, end of period		**$17,706**	$15,482	**$17,706**	$15,482

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

1. Organization of the Trust

Killam Apartment Real Estate Investment Trust ("Killam" or the "Trust") is an unincorporated open-ended mutual fund trust created pursuant to the amended and restated Declaration of Trust ("DOT"), dated November 27, 2015, under the laws of the Province of Ontario. Killam specializes in the acquisition, management and development of multi-residential apartment buildings and manufactured home communities ("MHCs") in Canada.

The condensed consolidated interim financial statements comprise the financial statements of Killam and its subsidiaries as at and for the six months ended June 30, 2017. Killam's head office operations are located at 3700 Kempt Road, Halifax, Nova Scotia, B3K 4X8 and the Trust's registered office is located at 2571 Windsor Street, Halifax, Nova Scotia, B3K 5C4.

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 disclosures 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.

The condensed consolidated interim financial statements of the Trust for the period ended June 30, 2017, were authorized for issue in accordance with a resolution of the Board of Trustees of Killam on August 9, 2017.

(B) Basis of Presentation

The condensed consolidated interim financial statements of Killam have been prepared on a historical cost basis, except for investment properties, deferred unit-based compensation, convertible debentures and exchangeable units, which 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 per unit 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 Trust's business and financial statement presentation. In particular, Killam's significant accounting policies were presented in note 2 to the consolidated financial statements for the year ended December 31, 2016, and have been consistently applied in the preparation of these condensed consolidated interim financial statements.

The operating results for the three and six months ended June 30, 2017, are not necessarily indicative of results that may be expected for the full year ended December 31, 2017, due to seasonal variations in property expenses and other factors.

Dollar amounts in thousands of Canadian dollars

3. Investment Properties

As at June 30, 2017

Segment	Apartments	MHCs	Other	IPUC	Total
Balance, beginning of period	**$1,721,399**	**$133,634**	**$32,269**	**$55,507**	**$1,942,809**
Fair value adjustment on investment properties	**33,221**	**(214)**	**(289)**	**—**	**32,718**
Acquisitions	**64,385**	**—**	**3,849**	**12,050**	**80,284**
Dispositions	**(16,616)**	**—**	**—**	**—**	**(16,616)**
Capital expenditure on investment properties	**10,296**	**949**	**186**	**—**	**11,431**
Capital expenditure on IPUC	**—**	**—**	**—**	**24,678**	**24,678**
Interest capitalized on IPUC	**—**	**—**	**—**	**723**	**723**
Balance, end of period	**$1,812,685**	**$134,369**	**$36,015**	**$92,958**	**$2,076,027**

As at December 31, 2016

Segment	Apartments	MHCs	Other	IPUC	Total
Balance, beginning of year	$1,636,744	$125,648	$32,188	$45,676	$1,840,256
Fair value adjustment on investment properties	(9,188)	5,896	(457)	—	(3,749)
Acquisitions	48,214	—	—	—	48,214
Dispositions	—	(8)	—	—	(8)
Transfer from IPUC	15,490	—	—	(15,490)	—
Capital expenditure on investment properties	30,139	2,098	538	—	32,775
Capital expenditure on IPUC	—	—	—	24,411	24,411
Interest capitalized on IPUC	—	—	—	910	910
Balance, end of year	$1,721,399	$133,634	$32,269	$55,507	$1,942,809

During the six months ended June 30, 2017, Killam acquired the following properties:

Property	**Location**	**Acquisition Date**	**Year Built**	**Units**	**Purchase Price[(1)]**
Apartments					
Spruce Grove	Calgary	16-Jan-17	1978	66	$12,800
Southport condominium units	Halifax	16-Feb-17	2016	5	1,070
Kanata Lakes IV & V [(2)]	Ottawa	01-Mar-17	2016	134	49,240
Other				205	$63,110
Vacant Land	Edmonton	13-Apr-17 / 23-Jun-17			4,050
1459 Hollis Street[(3)]	Halifax	19-Apr-17			4,600
Gloucester - Land[(4)]	Ottawa	21-Apr-17			8,000
Total Acquisitions					$79,760

(1) Purchase price does not include transaction costs.
(2) Purchase price represents 50% ownership in two buildings with a cumulative total of 268-units; in addition, it includes 35% interest in a shared clubhouse. This building is part of a five-building complex; with this acquisition Killam and its 50/50 partner now own the entire complex.
(3) Included in the acquisition is $0.85 million in land value relating to adjacent development projects - The Alexander & The Governor.
(4) Purchase price represents 50% interest in a multi-phase development site project.

During the three and six months ended June 30, 2017, Killam capitalized salaries of $0.8 million and $1.6 million (three and six months ended June 30, 2016 - $0.8 million and $1.5 million), as part of its project improvement, suite renovation and development programs. For the three and six months ended June 30, 2017, interest costs associated with the general corporate borrowings used to fund development were capitalized to the respective development projects using Killam's weighted average borrowing rate of 2.94% (June 30, 2016 - 3.38%). Interest costs associated with construction loans were capitalized to the respective developments using the actual borrowing rate associated with the loan.

Dollar amounts in thousands of Canadian dollars

3. Investment Properties (continued)

Investment properties with a fair value of $2.0 billion as at June 30, 2017, (December 31, 2016 - $1.9 billion) have been pledged as collateral against Killam's mortgages, construction loan and credit facilities.

Valuation Basis

Using the direct income capitalization method, the apartment properties were valued using cap-rates in the range of 4.12% to 8.00%, applied to a stabilized net operating income ("NOI") of $98.1 million (December 31, 2016 - 4.12% to 8.00% and $96.1 million), resulting in an overall weighted average cap-rate of 5.35% (December 31, 2016 - 5.49%). The stabilized occupancy rates used in the calculation of NOI were in the range of 93.0% to 98.1% (December 31, 2016 - 93.0% to 98.1%).

Using the direct income capitalization method, the MHC properties were valued using cap-rates in the range of 5.75% to 8.00%, applied to a stabilized NOI of $9.0 million (December 31, 2016 - 5.75% to 8.00% and $9.0 million), resulting in an overall weighted average cap-rate of 6.79% (December 31, 2016 - 6.81%). The stabilized occupancy rate used in the calculation of NOI was 97.9% (December 31, 2016 - 97.9%).

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 by region:

	June 30, 2017			December 31, 2016		
	Low	**High**	**Effective Weighted Average**	Low	High	Effective Weighted Average
Apartments			**5.35%**			5.49%
Halifax	4.85%	7.25%	5.35%	4.85%	7.33%	5.51%
Moncton	5.15%	7.00%	5.88%	5.15%	8.00%	6.00%
Fredericton	5.15%	6.50%	5.93%	5.15%	6.50%	5.98%
Saint John	6.00%	6.75%	6.41%	6.00%	6.75%	6.41%
St. John's	5.00%	6.00%	5.63%	5.00%	6.00%	5.68%
Charlottetown	5.50%	6.25%	5.94%	5.50%	6.25%	5.94%
Ontario	4.12%	5.02%	4.51%	4.12%	5.02%	4.63%
Alberta	4.52%	4.75%	4.69%	4.75%	4.75%	4.75%
Other Atlantic	5.75%	8.00%	6.83%	5.75%	8.00%	6.83%
MHCs			**6.79%**			6.81%
Ontario	7.00%	8.00%	7.49%	7.00%	8.00%	7.49%
Nova Scotia	5.75%	7.00%	6.14%	5.75%	7.00%	6.17%
New Brunswick	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%
Newfoundland	7.00%	7.00%	7.00%	7.25%	7.25%	7.25%

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

Class of property	**Capitalization rate**	
	10 basis points increase	*10 basis points decrease*
Apartments	$(33,629)	$34,910
MHCs	$(1,927)	$1,984

The investment property segment defined as "other" consists of five commercial properties.

Dollar amounts in thousands of Canadian dollars

4. Joint Operations and Investments in Joint Venture

Killam has interests in seven properties that are subject to joint control and are joint operations. Accordingly, the condensed consolidated interim statements of financial position and consolidated statements of income and comprehensive income include Killam's rights to and obligations for the related assets, liabilities, revenue and expenses.

5. Mortgages and Loans Payable

As at	June 30, 2017		December 31, 2016	
	Weighted Average Interest	Debt Balance	Weighted Average Interest	Debt Balance
Mortgages and loans payable				
Fixed rate	**2.93%**	**$1,030,950**	3.01%	$989,638
Variable rate	**4.28%**	**7,826**	4.28%	7,863
Vendor financing	**5.00%**	**6,008**	4.43%	13
Total		**$1,044,784**		$997,514
Current		**110,156**		111,862
Non-current		**934,628**		885,652
		$1,044,784		$997,514

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

As at June 30, 2017, unamortized deferred financing costs of $24.7 million (December 31, 2016 - $22.9 million) and mark-to-market premiums on mortgages assumed on acquisitions of $0.1 million (December 31, 2016 - $0.3 million) are netted against mortgages and loans payable.

Estimated future principal payments and maturities required to meet mortgage obligations by twelve-month periods as at June 30, 2017, are as follows:

	Principal Amount	% of Total Principal
2018	$110,156	10.3%
2019	177,607	16.6%
2020	188,601	17.6%
2021	142,543	13.3%
2022	164,396	15.4%
Subsequent to 2022	286,060	26.8%
	$1,069,363	100.0%
Unamortized deferred financing costs	(24,693)	
Unamortized mark-to-market adjustments	114	
	$1,044,784	

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

I. A $30 million revolving demand credit facility to be used for Killam’s acquisition and development program, as well as general business purposes. The interest rate on the credit facility is prime plus 75 bps on prime rate advances or 175 bps over Banker's Acceptance. Killam has assets with an aggregate carrying value of $46.3 million pledged to the line. As at June 30, 2017, there was no balance drawn on the credit facility. The agreement includes certain covenants and undertakings with which Killam is in compliance.

Dollar amounts in thousands of Canadian dollars

5. Mortgages and Loans Payable (Continued)

II. A $1.5 million revolving demand facility that can be used for Killam'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 June 30, 2017, Killam had assets with a carrying value of $1.8 million (December 31, 2016 - $1.6 million) pledged as collateral and letters of credit total $1.2 million outstanding against the facility (December 31, 2016 - $1.2 million). The agreement includes certain covenants and undertakings of which Killam is in compliance.

6. Construction Loans

As at June 30, 2017, Killam had access to two floating rate non-revolving demand construction loans for the purpose of financing development projects including a $51.8 million construction loan commitment related to The Alexander, where Killam has a 50% ownership interest, and a $18.8 million construction loan commitment related to the Saginaw Gardens II development project. Payments are to be made monthly on an interest only basis. The construction loans have interest rates of prime plus 0.625%. Once construction is complete and rental targets achieved, the construction loans will be repaid in full and replaced with conventional mortgages.

As at June 30, 2017, $22.4 million (December 31, 2016 - $18.5 million) was drawn on The Alexander and Saginaw Gardens II construction loans, at a weighted average interest rate of 3.33% (December 31, 2016 - 3.39%).

7. Convertible Debentures

Face Interest Rate %	Conversion Price	Face Amount	Maturity Date	June 30, 2017	December 31, 2016(1)
5.45%	$14.60	$46,000	June 30, 2018	—	$46,690

(1) Recorded at fair value based on closing market trading prices of the debentures.

Killam redeemed its $46.0 million, 5.45% convertible debentures on April 13, 2017.

8. Exchangeable Units

	Number of Exchangeable Units	Value
Balance, December 31, 2016	3,865,836	$46,158
Exchangeable units exchanged	(2,500)	(32)
Fair value adjustment	—	3,093
Balance, June 30, 2017	**3,863,336**	**$49,219**

The exchangeable units are non-transferable, but are exchangeable, on a one-for-one basis, into Killam trust units at any time at the option of the holder. Prior to such exchange, distributions will be made on these exchangeable units in an amount equivalent to the distributions that would have been made had the units been exchanged for Killam trust units.

9. Unitholders' Equity

By virtue of Killam being an open-ended mutual fund trust, unitholders of trust units are entitled to redeem their trust units at any time at prices determined and payable in accordance with the conditions specified in Killam's DOT. As a result, under IFRS, trust units are defined as financial liabilities; however, for the purposes of financial statement classification and presentation, the trust units may be presented as equity instruments as they meet the puttable instrument exemption under IAS 32.

All trust units outstanding are fully paid, have no par value and are voting trust units. The DOT authorizes the issuance of an unlimited number of trust units. Trust units represent a unitholder's proportionate undivided beneficial interest in Killam. No trust unit has any preference or priority over another. No unitholder has or is deemed to have any right of ownership in any of the assets of Killam. Each unit confers the right to one vote at any meeting of unitholders and to participate pro rata in any distributions and, on liquidation to a pro rata share of the residual net assets remaining after preferential claims thereon of debtholders.

Dollar amounts in thousands of Canadian dollars

9. Unitholders' Equity (continued)

Unitholders have the right to redeem their units at the lesser of (i) 90% of the market price of the trust unit (market price is defined as the weighted average trading price of the previous 10 trading days) and (ii) the most recent closing market price (closing market price is defined as the weighted average trading price on the specified date) at the time of the redemption. The redemption price will be satisfied by cash, up to a limit of $50 thousand for all redemptions in a calendar month, or a note payable. For the six months ended June 30, no unitholders redeemed units.

The units issued and outstanding are as follows:

	Number of Trust Units	Value
December 31, 2016	67,869,802	$560,197
Distribution reinvestment plan	407,575	5,098
Restricted trust units redeemed	26,447	202
Units issued on exchange of exchangeable units	2,500	32
Units issued for cash	6,088,500	73,569
June 30, 2017	**74,394,824**	**$639,098**

Equity Raise

On March 13, 2017, Killam closed its public offering of 6,088,500 trust units, at a price of $12.65, for gross proceeds of $77.0 million.

Distribution Reinvestment Plan ("DRIP")

Killam's DRIP allows unitholders to acquire additional units of the Trust through the reinvestment of distributions on their units. Unitholders who participate in the DRIP receive additional units equal to 3% of the units reinvested. Units issued with the DRIP are issued directly from the Trust at a price based on the 10-day volume weighted average closing price of the TSX preceding the relevant distribution date, which typically is on or about the 15th day of the month following the distribution declaration.

10. Distributions

Killam paid distributions to its unitholders in accordance with its DOT. Distributions declared by the Board of Trustees were paid monthly, on or about the 15th day of each month.

For the three and six months ended June 30, 2017, the distributions declared related to the trust units were $11.6 million and $22.3 million (three and six months ended June 30, 2016 - $9.2 million and $18.0 million), respectively. For the three and six months ended June 30, 2017, distributions declared related to the exchangeable units were $0.6 million and $1.2 million (three and six months ended June 30, 2016 - $0.7 million and $1.4 million). The distribution on the exchangeable units are recorded in financing costs.

11. Deferred Unit-based Compensation

Restricted Trust Units (RTUs), governed through Killam's RTU Plan, are awarded to members of the senior executive team and director-level employees as a percentage of their variable compensation. Non-executive members of the Board of Trustees have the right to receive a percentage of their annual retainer in the form of RTUs.

The RTUs have a value equal to the volume weighted average price of all trust units traded on the TSX for the five trading days immediately preceding the date on which the compensation is awarded. The RTUs earn distributions based on the same distributions paid on the trust units, and such distributions are used to acquire additional RTUs. The initial RTUs, and RTUs acquired through distribution reinvestment, are credited to each person's account and are not issued to the employee or Board member until they redeem such RTUs. The RTUs will be redeemed and paid out in trust units by December 31 of the year in which the RTUs have vested.

Dollar amounts in thousands of Canadian dollars

11. Deferred Unit-based Compensation (continued)

The RTUs are considered a financial liability because there is a contractual obligation for the Trust to deliver trust units (which are accounted for as liabilities, but presented as equity instruments under IAS 32) upon conversion of the RTUs. The RTUs are measured at fair value with changes flowing through the condensed consolidated interim statements of income and comprehensive income. The fair value of the vested RTUs for the six month period ended June 30, 2017, is $4.2 million (June 30, 2016 - $3.5 million).

For the three and six months ended June 30, 2017, compensation expense of $0.4 million and $0.5 million (three and six months ended June 30, 2016 - $0.9 million and $1.0 million) has been recognized in respect of the RTUs.

The details of the RTUs issued under the RTU Plan are shown below:

For the six months ended June 30,	**2017**		2016	
	Number of RTUs	**Weighted Average Issue Price**	Number of RTUs	Weighted Average Issue Price
Outstanding, beginning of period	**263,736**	**$10.78**	184,106	$10.40
Granted	**234,975**	**12.76**	143,244	10.83
Redeemed	**(40,875)**	**10.79**	(37,952)	10.48
Forfeited	**—**	**—**	(517)	10.88
Additional restricted trust unit distributions	**8,086**	**12.56**	6,727	11.45
Outstanding, end of period	**465,922**	**$11.89**	295,608	$10.62

12. Financing Costs

	Three months ended June 30,		**Six months ended June 30,**	
	2017	2016	**2017**	2016
Mortgage, loan and construction loan interest	**$8,031**	$7,770	**$15,934**	$15,542
Interest on exchangeable units	**599**	705	**1,185**	1,416
Amortization of fair value adjustments on assumed debt	**(164)**	(122)	**(231)**	(267)
Amortization of loss on interest rate hedge	**15**	15	**30**	30
Unrealized (gain) loss on derivative liability	**(147)**	131	**(121)**	131
Convertible debenture interest	**81**	1,441	**715**	2,892
Capitalized interest	**(394)**	(240)	**(723)**	(464)
	$8,021	$9,700	**$16,789**	$19,280

13. Deferred Income Tax

Trusts that satisfy the REIT Exemption are excluded from the specified investment flow-through ("SIFT") definition and therefore will not be subject to taxation under the SIFT Rules. Effective December 31, 2016, Killam qualified for the REIT Exemption and continues to meet the REIT Exemption as at June 30, 2017, and is therefore not subject to taxation to the extent that income is distributed to unitholders. However, this exemption does not extend to the corporate subsidiaries of Killam that are taxable legal entities. For the six months ended June 30, 2017, the deferred tax expense relates to the corporate subsidiary entity of the REIT.

Dollar amounts in thousands of Canadian dollars

14. Segmented Information

For investment properties, discrete financial information is provided on a property-by-property basis to members of executive management, which collectively comprise the chief operating decision maker. The individual properties are aggregated into segments with similar economic characteristics such as the nature of the property, vacancy rates, long-term growth rates and other characteristics. Management considers that this is best achieved by aggregating into apartments, MHC and other segments. Consequently, Killam is considered to have three reportable segments, as follows:

- Apartment segment - acquires, operates, manages and develops multi-family residential properties across Canada;
- MHC segment - acquires and operates MHC communities in Ontario and Eastern Canada; and
- Other segment - includes five commercial properties.

Killam's administration costs, other income, financing costs, depreciation and amortization, fair value adjustments, loss on disposition and deferred tax expense are not reported to the members of executive management on a segment basis.

The accounting policies of these reportable segments are the same as those described in the summary of significant accounting policies described in note 2 of the consolidated financial statements for the year ended December 31, 2016. Reportable segment performance is analyzed based on NOI. The operating results, and assets and liabilities, of the reportable segments are as follows:

Three months ended June 30, 2017	**Apartments**	**MHCs**	**Other**	**Total**
Property revenue	**$40,864**	**$3,890**	**$1,144**	**$45,898**
Property operating expenses	**(15,108)**	**(1,308)**	**(697)**	**(17,113)**
Net operating income	**$25,756**	**$2,582**	**$447**	**$28,785**

Three months ended June 30, 2016	Apartments	MHCs	Other	Total
Property revenue	$38,850	$3,759	$1,238	$43,847
Property operating expenses	(14,568)	(1,312)	(697)	(16,577)
Net operating income	$24,282	$2,447	$541	$27,270

Six months ended June 30, 2017	**Apartments**	**MHCs**	**Other**	**Total**
Property revenue	**$81,135**	**$6,808**	**$2,260**	**$90,203**
Property operating expenses	**(32,409)**	**(2,656)**	**(1,411)**	**(36,476)**
Net operating income	**$48,726**	**$4,152**	**$849**	**$53,727**

Six months ended June 30, 2016	Apartments	MHCs	Other	Total
Property revenue	$77,013	$6,608	$2,433	$86,054
Property operating expenses	(31,393)	(2,600)	(1,361)	(35,354)
Net operating income	$45,620	$4,008	$1,072	$50,700

As at June 30, 2017	**Apartments**	**MHCs**	**Other**	**Total**
Total assets	**$1,929,258**	**$142,059**	**$47,370**	**$2,118,687**
Total liabilities	**$1,097,077**	**$78,614**	**$83,644**	**$1,259,335**

As at December 31, 2016				
Total assets	$1,802,855	$142,071	$42,707	$1,987,633
Total liabilities	$1,036,995	$77,634	$122,538	$1,237,167

Dollar amounts in thousands of Canadian dollars

15. Supplemental Cash Flow Information

	Three months ended June 30,		Six months ended June 30,	
	2017	2016	**2017**	2016
Net income items related to investing and financing activities				
Interest paid on mortgages payable and other	**$8,045**	$7,454	**$15,763**	$15,137
Interest paid on convertible debentures	**715**	2,878	**715**	2,878
	$8,760	$10,332	**$16,478**	$18,015
Net change in non-cash operating assets and liabilities				
Rent and other receivables	**($192)**	$790	**($799)**	$11
Other current assets	**(2,603)**	(2,528)	**(5,288)**	(7,927)
Accounts payable and other liabilities	**(371)**	(4,681)	**5,383**	4,071
	($3,166)	($6,419)	**($704)**	($3,845)

16. Financial Instruments and Financial Risk Management Objectives and Policies

Killam’s principal financial liabilities consist of mortgages, construction loans and trade payables. The main purpose of these financial liabilities is to finance investment properties and operations. Killam has various financial assets, such as trade receivables and cash, which arise directly from its operations.

Killam 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. It is, and has been, Killam’s policy that no speculative trading in derivatives shall be undertaken. The main risks arising from Killam’s financial instruments are interest rate risk, credit risk and liquidity risk. These risks are managed as follows:

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

As at June 30, 2017, no mortgages or vendor debt had floating interest rates, except for two construction loan for $22.4 million, four demand loans totaling $7.8 million and two revolving demand facilities. These loans and facilities have interest rates of prime plus 0.63% - 2.0% (December 31, 2016 - prime plus 0.63% - 2.0%) and consequently, Killam is exposed to short-term interest rate risk on these loans.

Killam’s fixed mortgage and vendor debt, which matures in the next 12 months, totals $69.7 million. Assuming these mortgages are refinanced at similar terms, except at a 100 bps increase in interest rates, financing costs would increase by $0.7 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. Killam 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 for all prospective tenants and Killam also obtains a security deposit to assist in potential recoveries. In addition, receivables balances are monitored on an ongoing basis. Killam's bad debt expense experience has historically been less than 0.4% of revenue. None of Killam’s tenants account for more than 1% of the tenant receivables as at June 30, 2017, or 2016. The maximum exposure to credit risk is the carrying amount of each class of financial assets as disclosed in this note.

Dollar amounts in thousands of Canadian dollars

16. Financial Risk Management Objectives and Policies (continued)

(iii) Liquidity Risk

Management manages Killam's cash resources based on financial forecasts and anticipated cash flows. Killam structures its financing so as to stagger the maturities of its debt, thereby minimizing Killam's exposure to liquidity risk in any one year. In addition, Killam's apartments qualify for CMHC insured debt, reducing the refinancing risk upon mortgage maturities. Killam's MHCs do not qualify for CMHC insured debt; however, MHCs have access to conventional 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 six months ended June 30, 2017, Killam refinanced $39.4 million of maturing apartment mortgages with new mortgages totaling $55.9 million generating net proceeds of $16.5 million. As well, Killam refinanced $1.7 million of maturing MHC mortgages with new mortgages totaling $2.2 million for net proceeds of $0.5 million. The following table presents the principal payments (excluding interest) and maturities of Killam's liabilities for the next five years and thereafter:

For the twelve months ending June 30,	Mortgage and loans payable	Construction loans	Total
2018	$110,156	$16,442	$126,598
2019	177,607	5,963	183,570
2020	188,601	—	188,601
2021	142,543	—	142,543
2022	164,396	—	164,396
Thereafter	286,060	—	286,060
	$1,069,363	$22,405	$1,091,768

Capital Management

The primary objective of Killam's capital management is to ensure a healthy capital structure to support the business and maximize unitholder value. Killam manages its capital structure and makes adjustments to it in light of changes in economic conditions. To maintain or adjust the capital structure, Killam may adjust the distribution payment to unitholders, issue additional units, issue debt securities or adjust mortgage financing on properties.

Killam's primary measure of capital management is the total debt to total assets ratio. Killam's strategy, as outlined in the operating policies of its DOT, is for its overall indebtedness not to exceed 70% of total assets. However Killam's long-term target is to manage overall indebtedness to not exceed 50%. The calculation of the total debt to total assets is summarized as follows:

As at	June 30, 2017	December 31, 2016
Mortgages, loans payables and construction loans(1)	**$1,058,989**	$1,011,623
Convertible debentures	**—**	$46,000
Total debt	**$1,058,989**	$1,057,623
Total assets(1)	**$2,102,787**	$1,976,133
Total debt as a percentage of assets	**50.4%**	53.5%

(1) Total assets adjusted for Killam's non-controlling interest related to The Alexander - $15.9 million (December 31, 2016 - total assets adjusted for Killam's non-controlling interest related to The Alexander - $11.5 million). Total mortgages, loans payables and construction loans adjusted for Killam's non-controlling interest related to The Alexander - $8.2 million (December 31, 2016 - $4.4 million).

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 June 30, 2017, would increase the debt as a percentage of assets by 80 bps.

Dollar amounts in thousands of Canadian dollars

17. Fair Value Measurement

Fair Value of Financial Instruments

Fair value is the amount that would be received in the sale of an asset or would be paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value of interest-bearing financial assets and liabilities is determined by discounting the contractual principal and interest payments at estimated current market interest rates for the instrument. Current market rates are determined by reference to current benchmark rates for similar term and current credit spreads for debt with similar terms and risks. The fair values of the Trust's financial instruments were determined as follows:

(i) the fair values of the loans receivable 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 Killam might receive or pay in actual market transactions;

(ii) the fair values of the mortgages payable are estimated 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 Killam might pay or receive in actual market transactions;

(iii) the fair value of the convertible debentures is based on a quoted market price as at the reporting date;

(iv) the fair value of the deferred unit-based compensation and the exchangeable units is estimated at the reporting date, based on the closing market price of the trust units listed on the TSX. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and, therefore, cannot be determined with precision. Changes in estimates could significantly affect fair values;

(v) the fair value of the derivative liability is calculated based on an estimate of the mid-market arbitrage-free price of the swap. The arbitrage-free price comprises the present value of the future rights and obligations between two parties to receive or deliver future cash flows or exchange other assets or liabilities. Future obligations are valued as the sum of the present values as of the valuation date of contractually fixed future amounts and expected variable future amounts, the expected size of which is calculated from the projected levels of underlying variables. Future rights are valued as the sum of the present values of the expected values of contingent future amounts, the existence and size of which are calculated from the projected levels of underlying variables.

The significant financial instruments of Killam and their carrying values as at June 30, 2017, and December 31, 2016, are as follows:

As at	**June 30, 2017**		December 31, 2016	
Classification	**Carrying Value**	**Fair Value**	Carrying Value	Fair Value
Financial assets carried at amortized cost:				
Loans[1]	**$950**	**$955**	$950	$955
Financial liabilities carried at amortized cost:				
Mortgages payable	**$1,044,784**	**$1,086,870**	$997,514	$1,036,288
Financial liabilities carried at FVTPL:				
Exchangeable units	**$49,219**	**$49,219**	$46,158	$46,158
Convertible debentures	**$—**	**$—**	$46,690	$46,690
Deferred unit-based compensation	**$4,189**	**$4,189**	$2,988	$2,988
Derivative liability[2]	**$418**	**$418**	$296	$296

(1) The $1.0 million loan receivable is included in the other non-current assets within the condensed consolidated interim financial statements of financial position.

(2) The $0.4 million derivative liability is included in other liabilities within the condensed consolidated interim statements of financial position.

Dollar amounts in thousands of Canadian dollars

17. Fair Value Measurement (continued)

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

As at	**June 30, 2017**	December 31, 2016
Mortgages - Apartments	**2.38%**	2.34%
Mortgages - MHCs	**3.93%**	3.76%

Assets and Liabilities Measured at Fair Value

The fair value hierarchy of assets and liabilities measured at fair value on a recurring basis in the condensed consolidated interim statements of financial position is as follows:

As at		**June 30, 2017**			December 31, 2016	
	Level 1	**Level 2**	**Level 3**	Level 1	Level 2	Level 3
Assets						
Investment properties	—	—	**$2,076,027**	—	—	$1,942,809
Liabilities						
Exchangeable units	—	**$49,219**	—		$46,158	—
Convertible debentures	—	—	—	$46,690	—	—
Deferred unit-based compensation	—	**$4,189**	—		$2,988	—
Derivative liability	—	**$418**	—	—	$296	—

The three levels of the fair value hierarchy are described in note 2 to the audited consolidated financial statements for the year ended December 31, 2016. Transfers between levels in the fair value hierarchy are recognized on the date of the event or change in circumstances that caused the transfer. There were no transfers of assets or liabilities between Level 1, Level 2 and Level 3 during the six months ended June 30, 2017.

18. Commitments and Contingencies

Killam has entered into commitments for acquisitions (net of assumed debt) and development costs of $52.3 million as at June 30, 2017 (December 31, 2016 - $26.9 million).

Killam is subject to various legal proceedings and claims that arise in the ordinary course of business. These matters are generally covered by insurance. Management believes that the final outcome of such matters will not have a material adverse effect on the financial position, results of operations or liquidity of Killam. However, actual outcomes may differ from Management's expectations.

Killam and its 50% partner began construction in downtown Halifax on a 240-unit building, The Alexander, in late 2015. This project is scheduled to be completed in Q1-2018. The cost to develop is approximately $72 million. At the completion of construction and following the achievement of certain leasing conditions, Killam has a commitment in place to purchase the other 50% interest in this development.

Killam entered into a physical supply contract for natural gas to hedge its own usage, which is summarized below:

Area	**Usage Coverage**	**Term**	**Cost**
Ontario	70%	November 01, 2016 - October 31, 2017	$12.60/m3

19. Financial Guarantees

Killam is the guarantor on a joint and several basis for mortgage debt held through its joint operations. As at June 30, 2017, the maximum potential obligation resulting from these guarantees is $119.4 million, related to long-term mortgage financing (December 31, 2016 - $87.9 million). These loans are secured by a first ranking mortgage over the associated investment properties. Half of the total mortgages for these properties are recorded as a mortgage liability on the condensed consolidated interim financial statement of financial position. Killam is also the guarantor on a joint and several basis for the construction loan related to The Alexander development project. As at June 30, 2017, the maximum potential obligation resulting from this guarantee is $16.4 million (December 31, 2016 - $8.8 million).

Management has reviewed the contingent liability associated with its financial guarantee contracts and, as at June 30, 2017, determined that a provision is not required to be recognized in the condensed consolidated interim statements of financial position (December 31, 2016 - $nil).

20. Comparative Figures

Certain comparative figures have been reclassified to conform with the financial statement presentation adopted for the current year. Killam reclassified, on the condensed consolidated interim statements of cash flows, a portion of cash related to security deposits from "other current assets" to "cash" as these deposits are not required to be held in a restricted account.

21. Related Party Transactions

For the three and six months ended June 30, 2017, Killam paid a commercial leasing placement fee to a property management company controlled by an executive and Trustee of Killam, in the amount of $17 thousand (for the three and six months ended June 30, 2016 - $nil).

During the three and six months ended June 30, 2017, Killam paid a sales commission, totaling $0.3 million, to a property management company that is 50% owned by an executive and Trustee of Killam (for the three and six months ended June 30, 2016 - $nil).

Halkirk Properties Limited ("Halkirk") is a company that is partially owned by a Trustee of Killam. During 2016 and year-to-date in 2017, Killam and Halkirk have been developing a 240-unit building adjacent to the Brewery Market in Halifax, Nova Scotia. Construction of the development is managed by Killam and the cost of construction is funded 50/50 by each partner.

22. Subsequent Events

On July 4, 2017, Killam acquired a two-building, 134-unit property located in Halifax, Nova Scotia. The purchase price of $31.6 million was funded with two assumed mortgages of $10.8 million and $11.7 million with interest rates of 1.8% and 1.98%, and the balance with cash on hand.

On July 18, 2017, Killam announced a distribution of $0.05167 per unit, payable on August 15, 2017, to unitholders of record on July 31, 2017.

Subsequent to June 30, 2017, Killam agreed to acquire 296 units in two properties in Edmonton, Alberta. The purchase price of $67.5 million is expected to be satisfied with cash and new CMHC 10-year mortgage debt. The first property, consisting of 124 units, is scheduled to close August 18, 2017, and the remaining property, consisting of 172 units, is scheduled to close in Q4-2017.