

BPO Properties

2008 Annual Report

Dear Shareholders:

We are pleased to report that 2008 was another strong year for BPO Properties. We met our financial targets and made significant advancements to our developments. We generated FFO from continuing operations of \$154 million, or \$4.92 per common share, an increase of 5.8% over 2007. Although we were disappointed by the performance of our share price — which was greatly affected by the general slowing of the global economy — we remain confident in our strategy of investing in premier-quality office properties located in high-growth Canadian markets. We also remain confident in our long-term lease profile with high-credit-quality tenants. These strategies keep us well-positioned to ride out the economic downturn and to look for opportunities to grow our business once market conditions become more favorable.

In last year's letter to shareholders, we outlined our major business objectives for 2008. We have made meaningful progress in: generating capital, development and leasing. The following are some of our accomplishments.

Financial Highlights

All amounts expressed in Canadian dollars unless otherwise noted

(Millions, except per share information)	2008	2007	2006
Results of Operations			
Net income	\$ 65.5	\$ 138.8	\$ 72.7
Commercial property net operating income ⁽¹⁾	195.5	187.4	174.1
Funds from operations excluding gains	154.0	159.3	155.0
Funds from operations and gains	154.0	250.5	170.9
Per Diluted Common Share			
Net income	\$ 1.80	\$ 4.23	\$ 1.99
Funds from operations	4.92	4.95	4.88
Funds from operations and gains	4.92	8.15	5.43
Dividends paid	0.60 ⁽²⁾	0.60	0.60
Book value	16.94	23.12	19.55
Closing market price — TSX	24.00	60.30	69.92
Financial Position			
Total assets	\$ 2,352.5	\$ 2,235.7	\$ 2,098.6
Shareholders' equity	861.1	1,040.5	939.0

⁽¹⁾ Excludes net operating income from discontinued operations

⁽²⁾ Excludes a special dividend of \$7.25 per common share paid in 2008.

Capital Generation

Over the course of the year we were able to arrange financing or refinancing for eight properties, totaling approximately \$700 million.

In 2008, we completed the disposition program for the non-core portfolio from O&Y with the sale of Acres House in Niagara Falls for \$13.4 million on a 100% basis. Proceeds generated from the disposition program following the 2005 O&Y acquisition totaled approximately \$207 million for the company's 25% ownership interest from the sale of 15 properties totaling 2.2 million square feet in Toronto, Calgary and Winnipeg.

Leasing

Capitalizing on consistently favorable fundamentals in all of our markets, we had another strong year, leasing a total of 3.3 million square feet. Our portfolio-wide occupancy stands at 98.7% percent, an improvement of 30 basis points over last year. We executed 441,000 square feet in lease take-backs in which we captured significant increases in rental rates; our mark-to-market across the portfolio represents an uptick of \$16 per square foot.

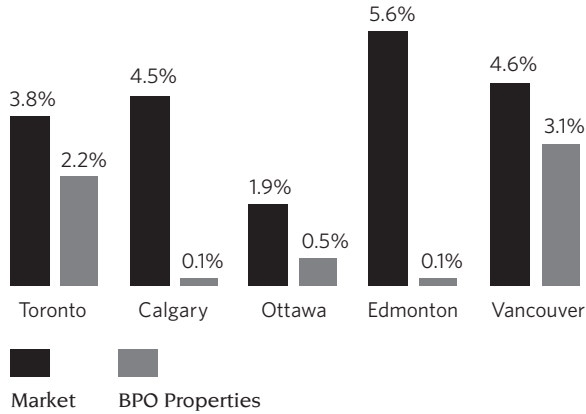
Some of the most notable transactions for the year included: a 15-year renewal and expansion with Petro-Canada at Petro-Canada Centre in Calgary for one million square feet; a five-year renewal and expansion with Imperial Oil at Fifth Avenue Place in Calgary for 717,000 square feet; a seven-year lease renewal with Bennett Jones at First Canadian Place in Toronto for 145,000 square feet; an eight-year renewal with Crescent Point General Partner Corp. at Petro-Canada Centre in Calgary for 140,000 square feet; and a new, 10-year lease with Citco Inc at Hudson's Bay Centre in Toronto for 99,000 square feet.

Development

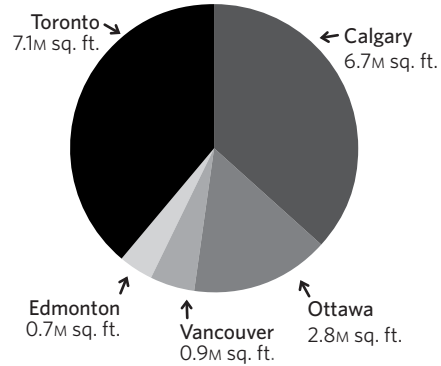
We reached two major development milestones in September 2008: the topping-off ceremonies for both Bay Adelaide Centre West in Toronto and Bankers Court in Calgary. Both properties are on schedule to be completed and begin welcoming tenants in 2009.

Bay Adelaide Centre West, being built to a LEED — Gold standard, is 72% leased to five tenants and substantial completion is expected in July

BPO Properties Vs. Market Vacancy



Markets By Square Feet



2009. Bankers Court is 100% pre-leased and will be completed in the first quarter of 2009.

Outlook

Moving into 2009, our core strategies remain intact, and our efforts will focus around generating capital, advancing our developments, and capitalizing on lease take-back opportunities.

Our 5.6-million-square-foot development pipeline represents a significant opportunity to grow future income streams. We plan to make significant headway within our development pipeline in 2009, including the second tower of the Bay Adelaide Center and 300 Queen Street in Ottawa.

Finally, we will continue our strategy of proactive leasing, and will look for lease take-back opportunities where available — especially in the Calgary market.

In Closing

With stable operating income, well-occupied buildings and a solid asset management platform, we are excited by our future prospects as we grow through

development and leasing of new properties and continued efforts in proactive asset management. On behalf of all BPO Properties employees and our Board of Directors, I'd like to thank you for your continued support.

Sincerely,

Thomas F. Farley
President & Chief Executive Officer

March 6, 2009

Portfolio by City

BPO Properties Ltd., one of Canada's largest commercial real estate companies, owns, develops and manages premier office properties. BPO Properties' portfolio comprises 27 commercial properties totalling 18.1 million square feet, and includes 3.3 million square feet of parking. The development portfolio consists of eight sites totalling over five million square feet in the downtown cores of Toronto, Calgary and Ottawa. Landmark properties include First Canadian Place in Toronto and Bankers Hall in Calgary.

December 31, 2008	Number of Properties	Leased %	Office 000's Sq. Ft.	Retail 000's Sq. Ft.	Parking 000's Sq. Ft.	Leasable Area 000's Sq. Ft.	Effective Ownership Interest %	BPO's Effective Interest 000's Sq. Ft.
Commercial								
Toronto, Ontario								
First Canadian Place	1	96.5%	2,379	232	170	2,781	25%	695
Exchange Tower	1	98.7%	963	66	131	1,160	50%	580
Hudson's Bay Centre	1	99.3%	536	261	295	1,092	100%	1,092
2 Queen St. E.	1	98.6%	448	16	81	545	25%	136
Queens Quay Terminal	1	94.6%	429	75	—	504	100%	504
151 Yonge St.	1	94.7%	289	10	72	371	25%	93
105 Adelaide St. W.	1	100.0%	176	7	49	232	100%	232
HSBC Building	1	97.1%	188	6	31	225	100%	225
20-22 Front St.	1	99.2%	136	8	—	144	100%	144
	9	97.5%	5,544	681	829	7,054		3,701
Ottawa, Ontario								
Place de Ville I	2	99.4%	569	18	502	1,089	25%	272
Place de Ville II	2	99.3%	591	19	433	1,043	25%	261
Jean Edmonds Towers	2	100.0%	540	13	95	648	25%	162
	6	99.5%	1,700	50	1,030	2,780		695
Calgary, Alberta								
Bankers Hall	3	100.0%	1,944	224	525	2,693	50%	1,347
Petro Canada Centre	2	100.0%	1,708	24	220	1,952	50%	976
Fifth Avenue Place	2	99.9%	1,430	45	206	1,681	50%	841
Altius Centre	1	98.1%	303	3	72	378	25%	95
	8	99.9%	5,385	296	1,023	6,704		3,259
Edmonton, Alberta								
Canadian Western Bank	1	99.8%	371	36	91	498	25%	125
Enbridge Tower	1	100.0%	179	4	30	213	25%	53
	2	99.9%	550	40	121	711		178
Vancouver, B.C.								
Royal Centre	1	96.9%	494	95	264	853	100%	853
Other								
Merivale Place, Nepean	1	100.0%	—	3	—	3	100%	3
Total Commercial	27	98.7%	13,673	1,165	3,267	18,105		8,689
Development								
Toronto, Ontario								
Bay Adelaide Centre	3	—	2,600	—	—	2,600	100%	2,600
Brookfield Place III	1	—	800	—	—	800	54%	432
	4	—	3,400	—	—	3,400		3,032
Ottawa, Ontario								
300 Queen Street	1	—	577	—	—	577	25%	144
			577	—	—	577		144
Calgary, Alberta								
Herald Block	1	—	1,200	—	—	1,200	100%	1,200
Bankers Court	2	—	500	—	—	500	50%	250
	3	—	1,700	—	—	1,700		1,450
Total Development	8	—	5,677	—	—	5,677		4,626
Total Portfolio	35	98.7%	19,350	1,165	3,267	23,782	—	13,315

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FORWARD-LOOKING STATEMENTS

This annual report to shareholders, particularly the “Business Environment and Outlook” section, contains forward-looking statements and information within the meaning of applicable securities legislation. These forward-looking statements reflect management’s current beliefs and are based on assumptions and information currently available to the management of BPO Properties. In some cases, forward-looking statements can be identified by terminology such as “may”, “will”, “expect”, “plan”, “anticipate”, “believe”, “intend”, “estimate”, “predict”, “forecast”, “outlook”, “potential”, “continue”, “should”, “likely”, or the negative of these terms or other comparable terminology. Although management believes that the anticipated future results, performance, or achievements expressed or implied by the forward-looking statements and information are based upon reasonable assumptions and expectations, the reader should not place undue reliance on forward-looking statements and information, because they involve assumptions, known and unknown risks, uncertainties, and other factors that may cause the actual results, performance or achievements of the Company to differ materially from anticipated future results, performance, or achievements expressed or implied by such forward-looking statements and information. Factors that could cause actual results to differ materially from those set forth in the forward-looking statements and information include general economic conditions; local real estate conditions, including the development of properties in close proximity to the Company’s properties; timely leasing of newly developed properties and re-leasing of occupied square footage upon expiration; dependence on tenants’ financial condition; the uncertainties of real estate development and acquisition activity; the ability to effectively integrate acquisitions; interest rates; availability of equity and debt financing; the impact of newly adopted accounting principles on the Company’s accounting policies and on period-to-period comparisons of financial results; and other risks and factors described from time to time in the documents filed by the Company with the securities regulators in Canada including in the Annual Information Form under the heading “Business of BPO Properties – Company and Real Estate Industry Risks.” The Company undertakes no obligation to publicly update or revise any forward-looking statements or information, whether as a result of new information, future events or otherwise, except as required by securities laws.

Management's Discussion and Analysis of Financial Results

March 6, 2009

PART I – OBJECTIVES AND FINANCIAL HIGHLIGHTS

BASIS OF PRESENTATION

Financial data included in Management's Discussion and Analysis ("MD&A") for the year ended December 31, 2008, includes material information up to March 6, 2009. Financial data provided has been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") with non-GAAP measures such as net operating income and funds from operations have been reconciled to appropriate Canadian GAAP measures. All dollar references, unless otherwise stated, are in millions of Canadian dollars except per-share amounts. Amounts in U.S. dollars are identified as "US\$."

The following discussion and analysis is intended to provide readers with an assessment of the performance of BPO Properties Ltd. ("BPO Properties" or "the Company") over the past two years as well as our financial position and future prospects. It should be read in conjunction with the consolidated financial statements and appended notes, which begin on page 39 of this report. In our discussion of operating performance, we refer to net operating income and funds from operations on a total and per-share basis. Net operating income is defined as income from property operations after operating expenses have been deducted, but prior to deducting financing, administration, depreciation and amortization, and income tax expenses. Funds from operations is defined as net income prior to extraordinary items, one-time transaction costs, depreciation and amortization, income taxes, and certain other non-cash items. We use net operating income and funds from operations to assess the operating results of the Company. Net operating income is an important measure in assessing operating performance and funds from operations is a relevant measure in analyzing real estate, as commercial properties generally appreciate rather than depreciate. We provide the components of net operating income and a full reconciliation from net income to funds from operations on page 23. Net operating income and funds from operations are both non-GAAP measures that do not have any standardized meaning prescribed by GAAP and therefore may not be comparable to similar measures presented by other companies.

Additional information, including our Annual Information Form, is available on our Web site at www.bpoproperties.com or at www.sedar.com.

OVERVIEW OF THE BUSINESS

BPO Properties is a publicly traded Canadian commercial real estate company listed on the Toronto stock exchange under the symbol BPP. We own, develop, and manage premier commercial office properties in select cities in Canada. At December 31, 2008, the book value of BPO Properties' total assets was \$2,352.5 million. During 2008, we generated \$65.5 million of net income (\$1.80 per common share) and \$154.0 million of funds from operations (\$4.92 per common share).

FINANCIAL HIGHLIGHTS

BPO Properties' financial results are as follows:

(Millions, except per-share amounts)	2008	2007	2006
Results of operations			
Net income	\$ 65.5	\$ 138.8	\$ 72.7
Net income per share	1.80	4.23	1.99
Common share dividends paid per share ⁽¹⁾	0.60	0.60	0.60
Funds from operations	154.0	159.3	155.0
Funds from operations per share	4.92	4.95	4.88

⁽¹⁾ Excludes a special common share dividend of \$7.25 per share in 2008

(Millions)	2008	2007	2006
Balance sheet data			
Total assets	\$ 2,352.5	\$ 2,235.7	\$ 2,098.6
Commercial properties	1,338.7	1,351.6	1,370.5
Commercial and development property debt	1,255.3	965.5	887.2
Shareholders' equity	861.1	1,040.5	939.0
Book value per common share	16.94	23.12	19.55

COMMERCIAL PROPERTY OPERATIONS

Our strategy of owning, pro-actively managing, and developing premier properties in high-growth, and in many instances supply-constrained markets with high barriers to entry has created one of Canada's most distinguished portfolios of office properties. Our commercial property portfolio consists of interests in 27 properties totaling 18.1 million square feet, including 3.3 million square feet of parking. Our development portfolio comprises five development sites totaling 5.7 million square feet. Our primary markets are the financial, energy, and government sectors in the cities of Toronto, Ottawa, Calgary, Edmonton, and Vancouver. We intend to continue our strategy of concentrating operations within a select number of gateway cities with attractive tenant bases in order to maintain a meaningful presence and build on the strength of our tenant relationships within these markets.

We remain focused on the following strategic priorities:

- Surfacing value from our properties through proactive leasing and select redevelopment initiatives;
- Prudent capital management including the refinancing of mature properties and investing in joint venture opportunities with institutional partners who seek to benefit from the depth of our expertise;
- Monetizing development assets when the economy rebounds and supply constraints create opportunities; and
- Expanding our asset management platform through the establishment of new joint venture opportunities or funds.

The following table summarizes our investment by market:

Region	Number of Properties	Leasable Area (000's Sq. Ft.)	BPO Properties' Owned Interest (000's Sq. Ft.)	Book Value (Millions)	Debt (Millions)	Net Book Equity (Millions)
Toronto, Ontario	9	7,054	3,701	\$ 597.8	\$ 370.8	\$ 227.0
Ottawa, Ontario	6	2,780	695	99.4	24.6	74.8
Calgary, Alberta	8	6,704	3,259	511.6	391.2	120.4
Edmonton, Alberta	2	711	178	17.4	37.1	(19.7)
Vancouver, B.C.	1	853	853	109.7	120.0	(10.3)
Other	1	3	3	2.8	—	2.8
Continuing operations	27	18,105	8,689	1,338.7	943.7	395.0
Office developments	8	5,677	4,626	689.1	311.6	377.5
Total	35	23,782	13,315	\$ 2,027.8	\$ 1,255.3	\$ 772.5

We have historically explored property-level joint-venture opportunities with strategic institutional partners. Although we plan to continue with this endeavor, we also pursue acquisitions of individual assets and portfolios through joint venture fund vehicles. In 2005, we formed our Canadian Office Fund (the "Fund") to acquire the O&Y portfolio. Of our 27 properties, seven are wholly owned, eight are held in property-level joint ventures or co-tenancies, and twelve were acquired through the O&Y portfolio acquisition. The Fund consists of a consortium of institutional investors that we lead and manage. Affiliates of the consortium members own direct interests in property-level joint ventures and have entered into several agreements relating to property management, fees, transfer rights, and other material issues related to the operation of the properties. We proportionately consolidate our interest in the Fund.

We believe that investing our liquidity with these partners in fund formats enables us to enhance returns. The Fund and associated asset-management fees represent an important area of growth as we expand our assets under management. Purchasing properties or portfolios of properties in fund formats allows us to earn the following categories of fees:

- **Asset Management** Stable base fee for providing regular, ongoing services.
- **Transaction** Development, redevelopment, and leasing activities conducted on behalf of these funds.
- **Performance** Earned when certain predetermined benchmarks are exceeded. Performance fees, which can add considerably to fee revenue, typically arise later in a fund's life cycle and are therefore not fully reflected in current results.

An important characteristic of our portfolio is the strong credit quality of our tenants. We direct special attention to credit quality particularly in these markets in order to ensure the long-term sustainability of rental revenues through economic cycles. Major tenants with over 500,000 square feet of space in the portfolio include Public Works and Government Services Canada, Bank of Montreal/Nesbitt Burns, Petro-Canada, Imperial Oil, and Talisman Energy. A detailed list of major tenants is included in Part III ("Risks and Uncertainties") of this MD&A, beginning on page 27.

Our strategy is to sign long-term leases in order to mitigate risk and reduce our overall retenanting costs. We typically commence discussions with tenants regarding their space requirements well in advance of the contractual expiration, and although each market is different, the majority of our leases, when signed, extend between 5 and 10-year terms. As a result of this strategy, approximately 9.3% (the majority of which is in 2013) of our leases mature annually over the next five years.

The following is a breakdown of lease maturities by region with associated expiring net rental rates:

Year of Expiry	Total Portfolio			Toronto, Ontario			Ottawa, Ontario			Calgary, Alberta		
	000's Sq. Ft.	%	Net Rent per Sq. Ft. ⁽¹⁾	000's Sq. Ft.	%	Net Rent per Sq. Ft. ⁽¹⁾	000's Sq. Ft.	%	Net Rent per Sq. Ft. ⁽¹⁾	000's Sq. Ft.	%	Net Rent per Sq. Ft. ⁽¹⁾
Currently available	191	1.3		157	2.5		8	0.5		7	0.1	
2009	527	3.6	\$ 18	393	6.3	\$ 17	35	2.0	\$ 17	61	1.1	\$ 29
2010	1,019	6.9	24	491	7.9	26	7	0.4	33	346	6.1	26
2011	1,115	7.5	27	298	4.8	26	8	0.5	16	680	12.0	29
2012	1,230	8.3	27	694	11.1	26	6	0.3	31	461	8.1	30
2013	3,001	20.2	26	1,273	20.4	28	1,131	64.6	20	502	8.8	33
2014	376	2.5	31	223	3.6	29	9	0.5	25	111	2.0	40
2015	2,187	14.7	25	514	8.3	28	542	31.0	15	1,016	17.9	30
2016 & beyond	5,192	35.0	26	2,182	35.1	22	4	0.2	30	2,497	43.9	33
Parking	3,267	—	—	829	—	—	1,030	—	—	1,023	—	—
	18,105	100.0		7,054	100.0		2,780	100.0		6,704	100.0	
Average market net rent			\$ 29			\$ 27			\$ 22			\$ 40

Year of Expiry	Edmonton, Alberta			Vancouver, B.C.			Other		
	000's Sq. Ft.	%	Net Rent per Sq. Ft. ⁽¹⁾	000's Sq. Ft.	%	Net Rent per Sq. Ft. ⁽¹⁾	000's Sq. Ft.	%	Net Rent per Sq. Ft. ⁽¹⁾
Currently available	1	0.1		18	3.1		—	—	
2009	14	2.4	\$ 9	24	4.1	\$ 22	—	—	\$ —
2010	136	23.1	14	39	6.6	18	—	—	—
2011	55	9.3	13	74	12.6	24	—	—	—
2012	7	1.2	21	62	10.5	22	—	—	—
2013	9	1.5	21	84	14.3	22	2	66.7	32
2014	28	4.7	16	5	0.8	27	—	—	—
2015	81	13.7	17	34	5.8	24	—	—	—
2016 & beyond	259	44.0	15	249	42.2	12	1	33.3	28
Parking	121	—	—	264	—	—	—	—	—
	711	100.0		853	100.0		3	100.0	
Average market net rent			\$ 27			\$ 30			\$ 27

⁽¹⁾ Net rent at expiration of lease

COMMERCIAL DEVELOPMENT

We hold interests in 5.7 million square feet of high-quality, centrally located development sites at various stages of planning and construction. We will seek to monetize these sites through development only when our risk-adjusted return hurdles are met and when pre-leasing targets (in excess of 50%) with one or more lead tenants have been achieved. We currently have two projects under development which are outlined on page 12 of this MD&A.

The following table summarizes our commercial development projects at December 31, 2008:

	Location	Number of Properties	Number of Sites	Ownership	Total Sq. Ft.
Toronto, Ontario					
Bay Adelaide Centre	Bay and Adelaide Streets	3	1	100%	2,600,000
Brookfield Place III	Third phase of Brookfield Place project	1	1	54%	800,000
Ottawa, Ontario					
Place de Ville III	Third phase of Place de Ville project	1	1	25%	577,000
Calgary, Alberta					
Herald Block	1 st Street and 7 th Avenue, within one block from our existing Calgary assets	1	1	100%	1,200,000
Bankers Court	East and West Parkades adjacent to Bankers Hall	2	1	50%	500,000
		8	5		5,677,000

PERFORMANCE MEASUREMENT

The key indicators by which we measure our performance are:

- Net income per share;
- Net operating income;
- Funds from operations per share;
- Overall indebtedness level;
- Weighted-average cost of debt; and
- Occupancy levels.

Although we monitor and analyze our financial performance using a number of indicators, our primary business objective of generating reliable and growing cash flow is monitored and analyzed using net income, net operating income, and funds from operations. Although net income is calculated in accordance with GAAP, net operating income and funds from operations are both non-GAAP financial measures that do not have any standardized meaning prescribed by GAAP and are therefore unlikely to be comparable to similar measures presented by other companies. We provide the components of net operating income and a full reconciliation from net income to funds from operations on page 23 of this MD&A.

Net Income

Net income is calculated in accordance with GAAP. Net income is used as a key indicator in assessing the profitability of the Company.

Net Operating Income

Net operating income is defined as income from property operations after operating expenses have been deducted, but prior to deducting financing, administration, depreciation and amortization, and income tax expenses. Net operating income is used as a key indicator of performance as it represents a measure over which management has control. We measure the performance of management by comparing the performance of the property portfolio adjusted for the effect of current and prior-year sales and acquisitions.

Funds from Operations

Funds from operations is defined as net income prior to extraordinary items, one-time transaction costs, depreciation and amortization, income taxes, and certain other non-cash items. Although we believe that funds from operations is the most relevant measure to analyze real estate as commercial properties generally appreciate rather than depreciate, we believe that funds from operations, net operating income, and net income are all relevant measures. We compute funds from operations substantially in accordance with the definition provided by the Real Property Association of Canada ("Real Pac"). Under this definition, funds from operations does not represent or approximate cash generated from operating activities determined in accordance with Canadian GAAP and should not be considered an alternative to GAAP measures. Accordingly, we provide a reconciliation of funds from operations to net income, consistent with the definition as set out above. A reconciliation is not provided to cash flow from operating activities, as it is often subject to fluctuations based on the timing of working capital payments.

KEY PERFORMANCE DRIVERS

In addition to monitoring and analyzing performance in terms of net income, net operating income, and funds from operations, we consider the following items to be important drivers of our current and anticipated financial performance:

- Increases in occupancies by leasing vacant space;
- Increases in rental rates as market conditions permit; and
- Reduction in occupancy costs through achieving economies of scale and diligently managing contracts.

We also believe that the key external performance drivers are:

- The availability of equity capital at a reasonable cost;
- The availability of debt capital at a cost and on terms conducive to our goals; and
- The availability of new property acquisitions that fit into our strategic plan.

PART II – FINANCIAL STATEMENT ANALYSIS

ASSET PROFILE

Our total asset book value was \$2,352.5 million at December 31, 2008 (compared to \$2,235.7 million on December 31, 2007). The following is a summary of our assets:

(Millions)	December 31, 2008	December 31, 2007
Commercial properties	\$ 1,338.7	\$ 1,351.6
Commercial developments	689.1	452.5
Loans receivable	150.6	283.5
Intangible assets	30.3	40.2
Tenant receivables and other assets	82.3	66.0
Cash and cash equivalents	61.5	37.7
Assets related to discontinued operations	—	4.2
Total	\$ 2,352.5	\$ 2,235.7

COMMERCIAL PROPERTIES

The book value of our commercial properties from continuing operations was \$1,338.7 million as of December 31, 2008 (compared to \$1,351.6 million on December 31, 2007). The decrease in commercial properties is primarily attributable to depreciation, offset by capital additions during the year ended December 31, 2008. There were no commercial properties held for sale at December 31, 2008. The consolidated carrying value of our properties is approximately \$154 per square foot, significantly less than the estimated replacement cost of these assets.

A breakdown of our commercial properties by region is as follows:

Region	Leasable Area (000's Sq. Ft.)	BPO Properties' Owned Interest (000's Sq. Ft.)	Book Value	Book Value
			December 31, 2008 (Millions)	December 31, 2007 (Millions)
Toronto, Ontario	7,054	3,701	\$ 597.8	\$ 603.9
Ottawa, Ontario	2,780	695	99.4	101.7
Calgary, Alberta	6,704	3,259	511.6	519.6
Edmonton, Alberta	711	178	17.4	17.6
Vancouver, B.C.	853	853	109.7	106.9
Other	3	3	2.8	1.9
Total	18,105	8,689	\$ 1,338.7	\$ 1,351.6

TENANT INSTALLATION COSTS AND CAPITAL EXPENDITURES

Upon the signing of the majority of our leases, we provide tenant improvements for leased space in order to accommodate the specific space requirements of the tenant. In addition to these capital expenditures, leasing commissions are paid to third-party brokers representing tenants in lease negotiations. Tenant improvements and leasing commissions are capitalized in the year incurred, amortized over the term of the lease, and recovered through rental payments. Expenditures for tenant installation costs for the year ended December 31, 2008, totaled \$11.0 million (compared to \$10.8 million in 2007). The increase was a result of tenant installation costs incurred on the lease-up of space throughout our portfolio.

Tenant installation costs are summarized as follows:

(Millions)	2008	2007
Leasing commissions	\$ 3.7	\$ 3.7
Tenant improvements	7.3	7.1
Total	\$ 11.0	\$ 10.8

We also invest in ongoing maintenance and capital-improvement projects to sustain the high quality of the infrastructure and tenant service amenities in our properties. Capital expenditures for the year ended December 31, 2008, totaled \$20.5 million (compared to \$15.6 million in 2007). These expenditures exclude repairs and maintenance costs, which are recovered through contractual tenant cost-recovery payments.

Capital expenditures include revenue-enhancing capital expenditures, which represent improvements to an asset or reconfiguration of space to increase rentable area or increase current rental rates, and non-revenue-enhancing expenditures, which are those required to extend the service life of an asset. The increase is primarily attributed to an increase in revenue-enhancing capital expenditures for improvements and space build out at Hudson's Bay Centre in Toronto and reconfiguration of space at Royal Centre in Vancouver.

The details of our capital expenditures are summarized as follows:

(Millions)	2008	2007
Revenue enhancing	\$ 15.4	\$ 13.1
Non-revenue-enhancing	5.1	2.5
Total	\$ 20.5	\$ 15.6

Capital expenditures continue to be a primary use of cash for the Company. Consistent with prior years, the Company will continue to focus on the prudent use of cash in 2009, primarily undertaking projects that are mandatory in nature and provide an immediate return and benefit to the Company.

COMMERCIAL DEVELOPMENTS

The details of the commercial developments portfolio and related book values are as follows:

(Millions, except square feet)	Buildable Sq. Ft.	Sq. Ft. Currently Under Construction	Dec. 31, 2008	Dec. 31, 2007
Current developments				
Bay Adelaide Centre, Toronto	2,600,000	1,160,000	\$ 578.9	\$ 374.2
Bankers Court, Calgary	500,000	265,000	49.1	21.7
Planning				
Herald Block, Calgary	1,200,000	—	57.5	52.5
<i>Others:</i>				
Brookfield Place III, Toronto	800,000	—		
Place de Ville III, Ottawa	577,000	—		
	<u>1,377,000</u>		3.6	4.1
Total	5,677,000	1,425,000	\$ 689.1	\$ 452.5

Commercial developments consist of commercial property development sites, density rights, and related infrastructure. The total book value of this development land and infrastructure was \$689.1 million at December 31, 2008, an increase of \$236.6 million from \$452.5 million at December 31, 2007. The increase is a result of the ongoing active construction at two of our development sites during the year ended December 31, 2008. The following is a brief description of our construction in progress:

- Bay Adelaide Centre in Toronto represents one of our largest development projects. Ground-breaking on Phase I of this project took place in July of 2006 and construction is actively underway and continues to be on budget. Phase I, which is expected to be completed in July 2009, represents 1.2 million square feet of a three-phase project that is expected to total 2.6 million square feet. Due to the continuous construction on Phase I the book value of this site has increased by \$204.7 million since December 31, 2007. The building is currently 72% leased.
- Construction on Bankers Court in Calgary, a 500,000-square-foot, two-building project, commenced in the third quarter of 2006. Active development of the first building, totaling 265,000 square feet, is on track and is expected to be completed in the first quarter of 2009. The building is 100% leased. As a result of the continuous development, the book value of this site has increased by \$27.4 million since December 31, 2007.

We continue to expand the Herald Block development site in Calgary. Last year we acquired the Heagle building for \$5.0 million, adding 100,000 square feet of additional density to the site, and in the fourth quarter of this year, we acquired the laneway bisecting the site from the City of Calgary for \$2.7 million and successfully rezoned the consolidated site. The combined site has a capacity of 1.2 million rentable square feet and links to existing skybridge connections.

Although we are not a speculative developer, we are a full-service real estate company with in-house development expertise. With over five million square feet of high-quality, centrally located development properties in Toronto, Ottawa and Calgary, we will undertake developments when our risk-adjusted returns and pre-leasing targets (in excess of 50%) have been achieved.

The details of development expenditures are as follows:

(Millions)	2008	2007
Construction costs	\$ 195.4	\$ 97.0
Interest capitalized	27.3	23.3
Property taxes and other	15.7	15.3
Total	\$ 238.4	\$ 135.6

LOANS RECEIVABLE

Loans receivable decreased to \$150.6 million at December 31, 2008 (compared to \$283.5 million on December 31, 2007). The decrease primarily relates to the repayment of a \$41.8 million loan receivable from one of our joint venture partners and a net repayment of \$95.3 million of an on-demand deposit with our parent company, Brookfield Properties Corporation (“BPC”) in the second quarter of 2008. At December 31, 2008, the on-demand deposit of \$125.0 million outstanding from BPC earns interest at the bank overnight lending rate plus 100 basis points. Subsequent to year-end, the full amount of the on-demand deposit was repaid to the Company (see note 21 of the consolidated financial statements).

INTANGIBLE ASSETS

Pursuant to Emerging Issues Committee Abstract 140, “Accounting for Operating Leases Acquired in Either an Asset Acquisition or a Business Combination,” an enterprise that acquires real estate should allocate a portion of the purchase price to in-place operating leases, based on their fair value that the enterprise acquires in connection with the real estate property. We assess the fair value of acquired intangible assets and liabilities, including tenant improvements, above- and below-market in-place operating leases, origination costs, and other identified intangible assets and assumed liabilities. Net intangible assets decreased to \$30.3 million at December 31, 2008, from \$40.2 million at December 31, 2007, primarily due to amortization during the year ended December 31, 2008. Approximately \$18.1 million of fully amortized intangible assets and their corresponding accumulated amortization were written off during the year ended December 31, 2008.

The components of intangible assets are as follows:

(Millions)	2008	2007
Intangible assets		
Lease-origination costs	\$ 40.4	\$ 57.1
Tenant relationships	6.5	7.6
Above-market in-place operating leases	2.0	2.3
	48.9	67.0
Less accumulation amortization		
Lease-originations costs	(16.2)	(24.6)
Tenant relationships	(1.6)	(1.4)
Above-market in-place operating leases	(0.8)	(0.8)
Total	\$ 30.3	\$ 40.2

TENANT RECEIVABLES AND OTHER ASSETS

Tenant receivables and other assets increased to \$82.3 million at December 31, 2008, from \$66.0 million at December 31, 2007, primarily due to the increase in tenant and other receivables as a result of the timing of accrued receivables.

The components of tenant receivables and other assets are as follows:

(Millions)	2008	2007
Tenant and other receivables	\$ 44.4	\$ 32.0
Straight-line rent receivable	18.3	16.5
Prepaid expenses and other assets	18.5	16.4
Restricted cash	1.1	1.1
Total	\$ 82.3	\$ 66.0

CASH AND CASH EQUIVALENTS

We endeavor to maintain high levels of liquidity to ensure that we can react quickly to changes in market conditions and to potential investment opportunities.

As of December 31, 2008, cash balances increased to \$61.5 million from \$37.7 million at December 31, 2007. The increase is primarily due to funds from our operating activities and financing activities; offset by development expenditures and dividend payments during the year.

The full repayment of the on-demand deposit with BPC subsequent to year-end, further increases our liquidity position by an additional \$125.0 million (see note 21 of the consolidated financial statements).

DISCONTINUED OPERATIONS

Properties that meet the criteria of the Canadian Institute of Chartered Accountants (“CICA”) issued Handbook Section 3475, “Disposal of Long-Lived Assets and Discontinued Operations,” are classified as discontinued operations. Any long-lived assets related to the property are recorded at the lower of carrying amount or fair value less estimated costs to sell and are not depreciated while classified as held for sale. The results of operations and balance sheet items of any property that has been identified as discontinued operations are reported separately if

the operations of the property will be eliminated as a result of the disposal and we will not have any significant continuing involvement in the operations of the property after the disposal transaction. Comparative amounts are also reclassified.

During the second quarter of 2008, the Company sold its 25% interest in 4342 Queen Street in Niagara Falls which was classified as a discontinued operation in the fourth quarter of 2007, resulting in a gain of \$nil.

Net income, including gains on disposition, attributable to discontinued operations was \$nil as of December 31, 2008, compared to \$80.0 million in 2007. The decrease in net income is the result of the sale of the following properties in 2007, which includes Atrium on Bay, 18 King Street, 2 St. Clair West and 40 St. Clair West in Toronto, 2200 Walkey Road and 2204 Walkley Road in Ottawa and Gulf Canada Square in Calgary. There were no properties classified as held for sale as of December 31, 2008.

The components of assets and liabilities related to discontinued operations are as follows:

(Millions)	2008	2007
Assets related to discontinued operations		
Commercial properties	\$ —	\$ 3.2
Intangible assets	—	0.1
Tenant receivables and other assets	—	0.9
Total assets related to discontinued operations	\$ —	\$ 4.2
Liabilities related to discontinued operations		
Accounts payable and other liabilities	—	3.0
Total liabilities related to discontinued operations	\$ —	\$ 3.0

The following table summarizes the income and gains from discontinued operations:

(Millions, except per-share amounts)	2008	2007
Revenue	\$ 0.1	\$ 18.2
Operating expenses	(0.1)	(6.2)
Interest expense	—	12.0
Depreciation and amortization	—	(2.2)
Income from discontinued operations prior to gains and taxes	—	9.8
Gains on sale of discontinued operations	—	(3.2)
Income taxes related to discontinued operations	—	6.6
Net income from discontinued operations	\$ —	\$ 91.2
Net income from discontinued operations – per share	\$ —	\$ (17.8)
	\$ —	\$ 80.0
	\$ —	\$ 2.81

LIABILITIES AND SHAREHOLDERS' EQUITY

Our asset base of \$2,352.5 million is financed with a combination of debt, preferred, and common equity. The components of our liabilities and shareholders' equity are as follows:

(Millions)	2008	2007
Liabilities		
Commercial and development property debt	\$ 1,255.3	\$ 965.5
Intangible liabilities	71.9	85.0
Accounts payable and other liabilities	105.6	100.4
Future income tax liabilities	58.6	41.3
Liabilities related to discontinued operations	—	3.0
Shareholders' equity		
Preferred shares	381.7	381.7
Common shares	78.4	78.8
Retained earnings and AOCI	401.0	580.0
Total	\$ 2,352.5	\$ 2,235.7

COMMERCIAL AND DEVELOPMENT PROPERTY DEBT

Commercial and development property debt totaled \$1,255.3 million at December 31, 2008 (compared to \$965.5 million on December 31, 2007). The increase is primarily attributed to additional advances on the development loans for Bay Adelaide Centre in Toronto and Bankers Court in Calgary, as well as net new proceeds on financing various properties throughout the year. The details and terms for new financing transactions for 2008 are as follows:

(Millions)			New Proceeds at Ownership	Repayments at Ownership	Net Proceeds Generated	Interest Rate (%)	Mortgage details	Maturity
105 Adelaide Street West	Q1	Refinancing	\$ 23.1	\$ (23.1)	\$ —	5.32%	Nonrecourse	February 2013
2 Queen Street East	Q2	New financing	28.6	—	28.6	5.64%	Nonrecourse	December 2017
Altius Centre	Q2	New financing	20.5	—	20.5	5.64%	Nonrecourse	December 2017
Canadian Western Bank Place	Q2	New financing	14.5	—	14.5	5.64%	Nonrecourse	December 2017
Royal Centre	Q2	New financing	122.0	(132.0)	(10.0)	4.96%	Nonrecourse	May 2012
Hudson's Bay Centre	Q2	New financing	110.0	(100.0)	10.0	5.20%	Limited recourse ⁽¹⁾⁽²⁾	May 2013
20-22 Front Street	Q3	New financing	20.0	(6.3)	13.7	6.24%	Nonrecourse	October 2020
Petro Canada Centre	Q4	Bridge financing	150.0	(121.5)	28.5	5.01% ⁽³⁾	Nonrecourse	October 2009

⁽¹⁾ Limited recourse up to \$15.0 million

⁽²⁾ Two-year extension option that extends the maturity to May 2015 is available to the Company provided that certain debt service and loan-to-value thresholds are met

⁽³⁾ Interest rate is based on Bankers Acceptance plus 225 bps and will increase by 25 bps if the facility remains outstanding at March 13, 2009

Commercial and development property debt at December 31, 2008, had a weighted-average interest rate of 5.6% and an average term to maturity of four years. Debt on our commercial properties, with the exception of Hudson's Bay Centre and Bay Adelaide Centre, are nonrecourse, thereby reducing overall financial risk to the Company.

We will continue to make efforts to match the maturity of our commercial and development property debt portfolio with the average lease term of our properties. The Company has debt totaling \$217.6 million maturing in year 2009, representing 17.3% of the Company's total debt outstanding at December 31, 2008, of which \$2.2 million matures in the second quarter and the remainder matures in the fourth quarter of 2009. Management expects these debts will be refinanced in the normal course.

The tightening of the credit markets has posed a significant challenge to property owners and managers. However, in spite of these conditions, we have had success in various financings throughout 2008 by completing eight financing deals at eight different properties, allowing for a more manageable 2009 debt maturity exposure. We believe completing these financings in this tough credit environment is a validation of our strategy of owning high-quality assets in Canada's top markets.

The details of commercial and development property debt at December 31, 2008, are as follows:

Commercial Property	Location	Interest Rate %	Maturity Date	BPO Properties'	
				Consolidated Share (Millions)	Mortgage Details
Enbridge Tower	Edmonton	6.7	June 2009	\$ 2.2	Nonrecourse - fixed rate
Petro-Canada Centre	Calgary	5.0	October 2009	150.0	Nonrecourse - variable rate
Place de Ville I	Ottawa	7.8	November 2009	5.9	Nonrecourse - fixed rate
First Canadian Place	Toronto	8.1	December 2009	60.2	Nonrecourse - fixed rate
Bay Adelaide Centre ⁽¹⁾⁽³⁾	Toronto	3.5	July 2010	277.5	Limited recourse-variable rate
Bankers Court	Calgary	3.5	October 2010	36.3	Nonrecourse - variable rate
Queen's Quay Terminal	Toronto	7.3	March 2011	34.0	Nonrecourse - fixed rate
Fifth Avenue Place	Calgary	7.6	August 2011	71.5	Nonrecourse - fixed rate
Exchange Tower	Toronto	6.8	April 2012	61.2	Nonrecourse - fixed rate
Royal Centre	Vancouver	5.0	May 2012	120.8	Nonrecourse - fixed rate
151 Yonge Street	Toronto	6.0	June 2012	11.1	Nonrecourse - fixed rate
HSBC Building	Toronto	8.2	October 2012	22.8	Nonrecourse - fixed rate
105 Adelaide	Toronto	5.3	February 2013	22.8	Nonrecourse - fixed rate
Hudson's Bay Centre ⁽²⁾⁽⁴⁾	Toronto	5.2	May 2013	110.0	Limited recourse - fixed rate
Bankers Hall	Calgary	7.2	November 2013	160.4	Nonrecourse - fixed rate
Bankers Hall	Calgary	6.7	November 2013	11.3	Nonrecourse - fixed rate
Jean Edmonds Tower	Ottawa	5.6	January 2014	1.4	Nonrecourse - fixed rate
2 Queen Street	Toronto	5.6	December 2017	28.6	Nonrecourse - fixed rate
Altius Centre	Calgary	5.6	December 2017	20.5	Nonrecourse - fixed rate
Canadian Western Bank Place	Edmonton	5.6	December 2017	14.5	Nonrecourse - fixed rate
20-22 Front St.	Toronto	6.2	October 2020	19.9	Nonrecourse - fixed rate
Jean Edmonds Tower	Ottawa	6.8	January 2024	15.6	Nonrecourse - fixed rate
Premium on assumed mortgages	Various	—	—	4.1	
Continuing operations		5.6		1,262.6	
Deferred financing costs				(7.3)	
Total				\$ 1,255.3	

⁽¹⁾ This loan has limited recourse to the Company for up to \$60.0 million

⁽²⁾ This loan has limited recourse to the Company for up to \$15.0 million

⁽³⁾ Two one-year extension options available at maturity. The criteria to extend the first option to 2011 has been met as of December 31, 2008

⁽⁴⁾ Two-year extension option which extends the maturity to May 2015 is available to the Company provided that certain debt service and loan-to-value thresholds are met

Commercial and development property debt maturities for the next five years and thereafter are as follows:

(Millions, except interest data)	Scheduled			Total	Weighted-Average Interest Rate (%) at Dec. 31, 2008
	Amortization	Maturities			
2009	\$ 12.6	\$ 217.6	\$ 230.2	5.9%	
2010	14.1	312.5	326.6	3.5%	
2011	14.4	97.3	111.7	7.5%	
2012	10.3	195.6	205.9	5.9%	
2013	5.7	276.8	282.5	6.3%	
2014 and thereafter	4.9	93.5	98.4	5.9%	
Total	\$ 62.0	\$ 1,193.3	\$ 1,255.3	5.6%	

CONTRACTUAL OBLIGATIONS

The following table presents our contractual obligations over the next five years and beyond:

(Millions)	Payments Due By Period			
	Total	1 - 3 Years	4 - 5 Years	After 5 Years
Commercial and development property debt	\$ 1,255.3	\$ 668.5	\$ 488.4	\$ 98.4
Interest expense ⁽¹⁾ - Commercial and development property debt	215.2	134.2	48.5	32.5
Ground leases ⁽²⁾	2,216.5	14.7	9.8	2,192.0
	\$ 3,687.0	\$ 817.4	\$ 546.7	\$ 2,322.9

⁽¹⁾ Represents aggregate interest expense expected to be paid over the term of the debt, on an undiscounted basis, based on current interest rates

⁽²⁾ Represents minimum rental payments, on an undiscounted basis, on land leases or other agreements largely expiring on or before the year 2891

CORPORATE GUARANTEES AND CONTINGENT OBLIGATIONS

We may be contingently liable with respect to litigation and claims that arise in the normal course of business. In addition, we may execute agreements that provide for indemnifications and guarantees to third parties. Disclosure of commitments, guarantees, and contingencies can be found in Note 16 to the consolidated financial statements.

INTANGIBLE LIABILITIES

Intangible liabilities are below-market in-place operating leases and above-market ground leases assumed on acquisitions, net of related accumulated amortization. Net intangible liabilities decreased to \$71.9 million at December 31, 2008, from \$85.0 million at December 31, 2007, primarily due to amortization during the year ended December 31, 2008. Approximately \$11.5 million of fully amortized intangible liabilities and their corresponding accumulated amortization were written off during the year ended December 31, 2008.

The composition of intangible liabilities is as follows:

(Millions)	2008	2007
Intangible liabilities		
Below-market in-place operating leases	\$ 56.8	\$ 68.3
Above-market ground lease obligations	45.8	45.8
	102.6	114.1
Less accumulated depreciation		
Below-market in-place operating leases	(22.6)	(23.6)
Above-market ground lease obligations	(8.1)	(5.5)
Total	\$ 71.9	\$ 85.0

ACCOUNTS PAYABLE AND OTHER LIABILITIES

Accounts payable and other liabilities totaled \$105.6 million at December 31, 2008 (compared to \$100.4 million on December 31, 2007). The increase is primarily related to the timing of accrued liabilities, higher deferred income, and accrued construction costs as a result of advancements in our two development projects, Bay Adelaide Centre in Toronto and Bankers Court in Calgary.

A summary of the components of accounts payable and other liabilities is as follows:

(Millions)	2008	2007
Accounts payable and accrued liabilities	\$ 101.3	\$ 95.3
Accrued interest	4.3	5.1
Total	\$ 105.6	\$ 100.4

INCOME TAXES

At December 31, 2008, we had net future income tax liabilities of \$58.6 million (compared to \$41.3 million on December 31, 2007). The increase of \$17.3 million is due to a decrease of future income tax assets related to operating and capital losses.

The components of future income tax liabilities are as follows:

(Millions)	2008	2007
Future income tax assets related to operating and capital losses	\$ (7.6)	\$ (16.6)
Future income tax liabilities related to differences between tax and book basis	66.2	57.9
Total	\$ 58.6	\$ 41.3

At December 31, 2008, we had net operating loss carryforwards of approximately \$34.7 million (compared to \$54.7 million on December 31, 2007), which are available to reduce taxable income in future years. The benefit of the tax losses, net of a valuation allowance, has been reflected in the future income tax assets.

The components of income tax expense are as follows:

Continuing operations

(Millions)	2008	2007
Income tax expense at the Canadian federal and provincial income tax rate of 32.0% (2007 – 34.0%)	\$ 32.1	\$ 29.6
Increase (decrease) in income tax expense due to the following:		
De-recognition of tax asset (tax assets previously not recognized)	1.6	(4.7)
Change in statutory tax rates	—	2.9
Other	1.1	0.4
Total	\$ 34.8	\$ 28.2

Discontinued operations

(Millions)	2008	2007
Income tax expense at the Canadian federal and provincial income tax rate of 32.0% (2007 – 34.0%)	\$ —	\$ 33.3
Decrease in income tax expense due to the following:		
Nontaxable portion of capital gain	—	(15.5)
Total	—	17.8

Total income tax expense	\$ 34.8	\$ 46.0
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The major components of income tax expense include the following:

(Millions)	2008	2007
Current tax expense	\$ 16.5	\$ 12.0
Future tax expense	18.3	34.0
Total	\$ 34.8	\$ 46.0

PREFERRED SHARES

At December 31, 2008, we had \$381.7 million of preferred equity outstanding consistent with the balance at December 31, 2007. These preferred shares represent low-cost capital to us, without dilution to our common equity base. Dividends paid on these preferred shares are accounted for as capital distributions.

We have the following preferred shares outstanding:

(Millions, except share information)	Shares Outstanding	Cumulative Dividend Rate	2008	2007
Series G	1,805,489	70% of bank prime	\$ 45.1	\$ 45.1
Series J	3,816,527	70% of bank prime	95.4	95.4
Series K	300	30-day BA + 0.4%	150.0	150.0
Series M	2,847,711	70% of bank prime	71.2	71.2
Series N	800,000	30-day BA + 0.4%	20.0	20.0
Total			\$ 381.7	\$ 381.7

The redemption terms of the preferred shares issued by BPO Properties are as follows:

(i) Series G preferred shareholders are entitled to cumulative dividends at an annual rate equal to 70% of the average bank prime rate. The Company may, at its option, redeem the shares at a price of \$25 per share plus arrears on any accrued and unpaid dividends.

(ii) Series J and M preferred shareholders are entitled to cumulative dividends at an annual rate equal to 70% of the average bank prime rate for the previous quarter. The Company may, at its option, redeem the shares at a price of \$25 per share plus arrears on any accrued and unpaid dividends.

(iii) Series K preferred shareholders are entitled to cumulative dividends at the 30-day bankers' acceptance rate plus 0.4%. The Company may, at its option, redeem the shares at a price of \$500,000 per share plus an amount equal to all accrued and unpaid dividends.

(iv) Series N preferred shareholders are entitled to cumulative dividends at the 30-day bankers' acceptance rate plus 0.4%. The Company may, at its option, redeem the shares at \$25 per share plus arrears on any accrued and unpaid dividends.

During the year ended December 31, 2008, we paid preferred dividends of \$14.3 million (compared to \$18.2 million in 2007), due to a decrease in interest rates on which the dividend rates are based.

COMMON EQUITY

Total common shares issued and outstanding at December 31, 2008, totaled 28.3 million (compared to 28.5 million on December 31, 2007) shares, which included 21.7 million non-voting equity shares (compared to 21.7 million on December 31, 2007).

During 2008, we repurchased 147,900 common shares for \$7.0 million. The book value of the common shares was \$0.4 million; as a result, the \$6.6 million paid in excess of the book value was recorded as a reduction to retained earnings.

We paid common share dividends of \$223.6 million for the year ended December 31, 2008 (compared to \$17.1 million in 2007). The increase is due to a special common share dividend that was paid during the second quarter of 2008 for \$206.5 million or \$7.25 per common share.

The book value per common share at December 31, 2008, was \$16.94 (compared to \$23.12 on December 31, 2007).

At December 31, 2008, the book value of our common equity was \$479.4 million (December 31, 2007 – \$658.8 million), compared with a market equity capitalization of approximately \$679.2 million (December 31, 2007 – \$1,718.6 million), calculated as total common shares outstanding multiplied by \$24.00 per share, the closing price per common share on the Toronto Stock Exchange on December 31, 2008 (December 31, 2007 – \$60.30 per share).

Like most commercial real estate companies within our peer group, our share price traded down materially. Compounding a decline in 2008 across most major indices, commercial real estate was hit particularly hard as a result of perceived pressures on balance sheet liquidity from financing risk. In addition, companies with tenant exposure concentrated in financial service focused markets, like Toronto, experienced additional share price pressure. However, despite this, at December 31, 2008, our market value per common share of \$24.00 was in excess of our book value per common share of \$16.94.

CAPITAL RESOURCES AND LIQUIDITY

We employ a broad range of financing strategies to facilitate growth and manage financial risk, with particular emphasis on the overall reduction of the weighted-average cost of capital, in order to enhance returns for common shareholders. Our principal liquidity needs for the next twelve months are to:

- fund recurring expenses;
- meet debt service requirements;
- make dividend payments;
- fund those capital expenditures deemed mandatory, including tenant improvements;
- fund current development costs not covered under construction loans; and
- fund investing activities which could include:
 - discretionary capital expenditures;
 - repurchase of our stock; and
 - property acquisitions.

We believe that our liquidity needs will be satisfied using cash on hand, cash flows generated from operating and financing activities, as well as proceeds from new joint venture opportunities or funds. Rental revenue, recoveries from tenants, interest and other income, available cash balances, draws on our credit facilities and refinancings, including upward refinancings of maturing indebtedness are our principal sources of capital used to pay operating expenses, dividend payments, debt service, and recurring capital and leasing costs in our commercial property portfolio. We seek to increase income from our existing properties by maintaining quality standards for our properties that promote high occupancy rates and support increases in rental rates while reducing tenant turnover and by controlling operating expenses. Another source of cash flow includes third-party fees generated by our asset management, leasing and development businesses. In addition, our tax status as a corporation and tax loss pools allow us to reinvest and retain cash generated by our operations without incurring significant cash taxes. Consequently, we believe our revenue along with proceeds from financing activities will continue to provide the necessary funds for our short-term liquidity needs. However, material changes in these factors may adversely affect our net cash flows.

Our principal liquidity needs for periods beyond the next twelve months are for development costs, potential property acquisitions, scheduled debt maturities and non-recurring capital expenditures. We plan to meet these needs with one or more of the following:

- cash flows from operations;
- construction loans;
- investment in new funds;
- proceeds from sales of partial interests in our wholly-owned assets; and
- financings, including upward refinancings.

Our commercial property debt is primarily fixed-rate and nonrecourse to the Company. These investment-grade financings are typically structured on a loan-to-appraised-value basis of between 55% and 65% as market conditions permit. In addition, in certain circumstances where a building is leased almost exclusively to a high-credit-quality tenant, a higher loan-to-value financing, based on the tenant's credit quality, is put in place at rates commensurate with the cost of funds for the tenant. This reduces our equity requirements to finance commercial property, and enhances equity returns.

Most of our borrowings are in the form of long-term property-specific financings with recourse only to the specific assets. Limiting recourse to specific assets ensures that poor performance within one area does not compromise our ability to finance the balance of our operations. Our maturity schedule is fairly diversified so that financing requirements in any given year are manageable.

Our focus on structuring financings with investment grade characteristics ensures that debt levels on any particular asset can typically be maintained throughout a business cycle, and so enables us to limit covenants and other performance requirements, thereby reducing the risk of early payment requirements or restrictions on the distribution of cash from the assets being financed.

The sustainability of our capital strategy has been demonstrated by the \$488.7 million in debt financings at our ownership, completed in 2008, from which new proceeds were used to fund existing obligations, including a one-time special dividend of \$206.5 million paid to common shareholders in the second quarter of this year.

To help ensure we are able to react to investment opportunities quickly and on a value basis, we attempt to maintain a high level of liquidity. Our primary sources of liquidity consist of cash and cash equivalents. In addition, we structure our affairs to facilitate monetization of longer-duration assets through financings, co-investor participations or refinancings.

At December 31, 2008, we had approximately \$186.5 million of liquidity consisting of \$61.5 million of cash and a \$125.0 million on-demand deposit from BPC. Subsequent to the year ended December 31, 2008, we received the full balance of the loan receivable outstanding from BPC in the amount of \$125.0 million.

Cost of capital

We continually strive to reduce our weighted-average cost of capital and improve common shareholders' equity returns through value-enhancement initiatives and the consistent monitoring of the balance between debt and equity financing.

As of December 31, 2008, our weighted-average cost of capital, assuming a 12.0% return on equity, was 6.2% (December 31, 2007 – 8.8%). Our cost of capital is lower than many of our peers because of the greater amount of investment-grade financing that can be placed on our assets, which is a function of the high-quality nature of both the assets and the tenant base that compose our portfolio. The decrease over the prior year is due to a decrease in our market capitalization.

The following schedule details the capitalization of the Company at the end of 2008 and 2007 and the related costs thereof:

(Millions, except cost of capital data)	Cost of Capital ⁽¹⁾		Underlying Value ⁽²⁾	
	Dec. 31, 2008	Dec. 31, 2007	Dec. 31, 2008	Dec. 31, 2007
Liabilities				
Commercial and development property debt	5.6%	6.9%	\$ 1,255.3	\$ 965.5
Shareholders' equity				
Preferred shares	3.8%	4.8%	381.7	381.7
Common shares ⁽³⁾	12.0%	12.0%	679.2	1,718.6
Total⁽⁴⁾	6.2%	8.8%	\$ 2,316.2	\$ 3,065.8

⁽¹⁾ As a percentage of average book value

⁽²⁾ Underlying value of liabilities represents the cost to retire on maturity. Underlying value of common equity is based on the closing stock price of BPO Properties' common shares at December 31, 2008. Underlying value of preferred equity is based on the book value of preferred shares

⁽³⁾ Determined on a market-value basis and assumes a 12% return on equity

⁽⁴⁾ In calculating the weighted-average cost of capital, the cost of debt has been tax-effected

OPERATING RESULTS

Net Income

Our net income for the year ended December 31, 2008, was \$65.5 million (\$1.80 per common share) compared to \$138.8 million (\$4.23 per common share) in 2007.

The net decrease from the year ended December 31, 2007 to the year ended December 31, 2008, is largely a result of the following:

- an \$80.0 million decrease in net income from discontinued operations, net of taxes (\$2.81 per share), as there was no net income generated from the sale of one property during 2008;
- a \$6.5 million increase in interest expense, net of taxes (\$0.23 per share) due to overall higher debt balances this year than the previous year, as a result of new financings and refinancing, primarily at Petro-Canada Centre and Royal Centre, offset by;
- a \$5.5 million growth in same-property net operating income, net of taxes (\$0.19 per share), primarily due to continued growth in same-property revenues as a result of new leases and expansions;
- a \$5.6 million increase in loans and investment income, net of taxes (\$0.20 per share), primarily due to interest income from the on-demand deposit with BPC, sales of miscellaneous non-core investments, and investment income from a residential joint venture business;
- a \$3.3 million decrease in depreciation and amortization, net of taxes (\$0.11 per share); and
- a \$2.6 million transaction-cost write-off, net of taxes (\$0.09 per share) during 2007.

Set out below is a summary of the various components of our net income and funds from operations. Discussion of each of these components is provided on the following pages.

(Millions, except per-share amounts)	2008	2007	2006
Commercial properties			
Revenue	\$ 345.1	\$ 328.2	\$ 310.6
Expenses	149.6	140.8	136.5
Net operating income	195.5	187.4	174.1
Loans and investment income	20.5	12.3	21.3
	216.0	199.7	195.4
Expenses			
Interest	39.5	30.0	41.4
General and administrative expenses	22.5	20.2	16.9
Funds from operations ⁽¹⁾	154.0	149.5	137.1
Transaction costs	—	4.0	—
Depreciation and amortization	53.7	58.5	56.3
Income taxes	34.8	28.2	27.5
Net income from continuing operations	65.5	58.8	53.3
Discontinued operations ⁽²⁾	—	80.0	19.4
Net income	\$ 65.5	\$ 138.8	\$ 72.7
Net income per common share			
Continuing operations	\$ 1.80	\$ 1.42	\$ 1.31
Property-disposition gains	—	2.66	0.46
Discontinued operations	—	0.15	0.22
	\$ 1.80	\$ 4.23	\$ 1.99
Funds from operations and gains per common share			
Continuing operations	\$ 4.92	\$ 4.61	\$ 4.25
Property-disposition gains	—	3.20	0.55
Discontinued operations	—	0.34	0.63
	\$ 4.92	\$ 8.15	\$ 5.43

⁽¹⁾ Represents funds from continuing operations

⁽²⁾ Refer to page 14 for further details on discontinued operations

It should be noted that challenges of comparability of net income exist among various real estate companies, as those entities structured as corporations, such as the Company, are required to charge their earnings with tax expense despite the presence of tax losses, which reduce our cash tax obligation. This differs from those entities which operate as real estate investment trusts (“REITs”), as REITs are not subject to taxation provided they remain in compliance with specific tax codes.

Our net income per common share and weighted-average common shares outstanding are calculated as follows:

(Millions)	2008	2007	2006
Net income	\$ 65.5	\$ 138.8	\$ 72.7
Preferred share dividends	(14.3)	(18.2)	(16.0)
Net income available to common shareholders	\$ 51.2	\$ 120.6	\$ 56.7
Weighted-average shares outstanding	28.4	28.5	28.5

RECONCILIATION OF NET INCOME TO FUNDS FROM OPERATIONS

(Millions)	2008	2007	2006
Net income	\$ 65.5	\$ 138.8	\$ 72.7
Depreciation and amortization ⁽¹⁾	53.7	61.7	64.8
Income taxes ⁽²⁾	34.8	46.0	33.4
Transaction costs	—	4.0	—
Funds from operations and gains	154.0	250.5	170.9
Property disposition gains	—	(91.2)	(15.9)
Funds from operations	\$ 154.0	\$ 159.3	\$ 155.0

⁽¹⁾ Includes depreciation and amortization from discontinued operations of \$nil, \$3.2 million, and \$8.5 million for the years ended December 31, 2008, 2007, and 2006, respectively

⁽²⁾ Includes income taxes from discontinued operations of \$nil, \$17.8 million, and \$5.9 million for the years ended December 31, 2008, 2007, and 2006, respectively

After providing for preferred-share dividends, our funds from operations per diluted share, excluding property disposition gains, is calculated as follows:

(Millions, except per-share amounts)	2008	2007	2006
Funds from operations	\$ 154.0	\$ 159.3	\$ 155.0
Preferred share dividends	(14.3)	(18.2)	(16.0)
	139.7	141.1	139.0
Weighted-average shares outstanding	28.4	28.5	28.5
Funds from operations per share	\$ 4.92	\$ 4.95	\$ 4.88

Funds from operations slightly decreased to \$4.92 per share during the year ended December 31, 2008 (compared to \$4.95 per share in 2007). The decrease during the year is primarily due to funds generated from discontinued operations in 2007, which were subsequently sold in 2007, offset by an increase in same-property commercial rental revenue, loans and investment income, and lower preferred share dividends declared due to lower interest rates in which the dividends are based.

REVENUE

Revenue from commercial properties includes rental revenues earned from tenant leases, straight-line rent, percentage rent, and additional rent from the recovery of operating costs, property taxes and fee income. Revenue from commercial properties totaled \$345.1 million during 2008 (compared to \$346.4 million in 2007). The components of revenue are as follows:

(Millions)	2008	2007	2006
Revenue from continuing operations	\$ 331.8	\$ 315.6	\$ 298.6
Fee income	13.3	12.6	12.0
Revenue from discontinued operations	—	18.2	42.4
Total commercial property revenue	345.1	346.4	353.0
Loans and investment income	20.5	12.3	21.3
Total	\$ 365.6	\$ 358.7	\$ 374.3

COMMERCIAL PROPERTY OPERATIONS

Commercial property net operating income totaled \$195.5 million in 2008 (compared to \$187.4 million in 2007). The components of commercial property net operating income from continuing operations are as follows:

(Millions)	2008	2007	2006
Revenue from continuing operations and fee income	\$ 345.1	\$ 328.2	\$ 310.6
Operating expenses	149.6	140.8	136.5
Total	\$ 195.5	\$ 187.4	\$ 174.1

(Millions)	2008	2007	2006
Net operating income – same property	\$ 177.8	\$ 169.8	\$ 161.3
Net operating income – properties acquired	14.2	12.0	8.8
Nonrecurring fees and other income	3.5	5.6	4.0
Total	\$ 195.5	\$ 187.4	\$ 174.1

The components of commercial property net operating income from discontinued operations are as follows:

(Millions)	2008	2007	2006
Revenue from discontinued operations	\$ 0.1	\$ 18.2	\$ 42.4
Property operating expenses	(0.1)	(6.2)	(18.3)
Net operating income from discontinued operations	\$ —	\$ 12.0	\$ 24.1

Our strategy of owning, proactively managing and developing premier properties in high-growth, and in many instances supply-constrained, markets with high barriers to entry, along with our focus on executing long-term leases with strong credit rated tenants, has created one of Canada's most distinguished portfolios of office properties. In the past, this strategy has reduced our exposure to the cyclical nature of the real estate business, however, considering the severity of the global economic slowdown, we are at risk that major tenants are succumbing to financial pressures and are no longer having a need for all of their space, leading to increased supply through sublets or tenant defaults. To date, we've not been materially impacted by those financial institutions and professional service firms that have filed for bankruptcy or dissolved in recent months, though we are aware that this could be the beginning of a trend, and we are concerned about the financial stress that is facing many of our tenants across our portfolio. Despite this, we were successful in 2008 in largely reducing our lease expiry profile in the upcoming years, specifically in our energy sector markets which was a goal for us due to drastic reduction in price of oil compared to the beginning of the year. We feel confident with our current rollover risk exposure and are focused on working towards renewals on large expiries in the upcoming months, as well as continuing to manage our rollover exposure in the future years.

Our leases generally have clauses that provide for the collection of rental revenues in amounts that increase every five years, with these increases negotiated at the signing of the lease. The large number of high-credit-quality tenants in our portfolio lowers the risk of not realizing these increases. GAAP requires that these increases be recorded on a straight-line basis over the life of the lease. For the year ended December 31, 2008, we recognized \$2.1 million straight-line rental revenue (compared to \$2.9 million in 2007).

Commercial property operating costs, which include real estate taxes, utilities, insurance, repairs and maintenance, cleaning, and other property-related expenses, were \$149.6 million in 2008 (compared to \$140.8 million in 2007). The increase was the result of an increase in utilities and general property maintenance costs.

Substantially all of our leases are net leases in which the lessee is required to pay its proportionate share of the property's operating expenses such as utilities, repairs, insurance, and taxes. Consequently, leasing activity is the principal contributor to the change in same-property net operating income. Our total portfolio rate increased by 30 basis points to 98.7% at December 31, 2008, compared to 98.4% at December 31, 2007, primarily due to lease-ups in Edmonton and Ottawa. At December 31, 2008, average in-place net rent throughout the portfolio was \$22 per square foot, compared to \$21 per square foot at December 30, 2007.

The following table shows the average in-place rents and estimated current market rents for similar space in each of our markets as of December 31, 2008:

	Gross Leasable Area (000's Sq. Ft.)	Avg. Lease Term (Years)	Avg. In-Place Net Rent (\$ per Sq. Ft.)	Avg. Market Net Rent (\$ per Sq. Ft.)
Toronto, Ontario	7,054	6	\$ 23	\$ 27
Ottawa, Ontario	2,780	5	17	22
Calgary, Alberta	6,704	9	24	40
Edmonton, Alberta	711	6	12	27
Vancouver, B.C.	853	10	16	30
Other	3	8	31	27
Total ⁽¹⁾	18,105	7	\$ 22	\$ 29

⁽¹⁾ Excludes developments

A summary of current and historical occupancy levels at December 31 for the past two years is as follows:

	December 31, 2008		December 31, 2007	
	Total Sq. Ft.	% Leased	Total Sq. Ft.	% Leased
Toronto, Ontario	7,054	97.5	7,054	97.5
Ottawa, Ontario	2,780	99.5	2,780	99.3
Calgary, Alberta	6,704	99.9	6,704	99.8
Edmonton, Alberta	711	99.9	710	99.1
Vancouver, B.C.	853	96.9	853	97.4
Other	3	100.0	212	68.6
Total ⁽¹⁾	18,105	98.7	18,313	98.4

⁽¹⁾ Excludes developments

During 2008, we leased 3,300,000 square feet of space, which is equivalent to approximately four times the amount of space contractually expiring during the year. This included 3,032,000 square feet of new leasing and renewals, and 268,000 square feet of development leasing, compared to expiries of 753,000 square feet and accelerated expiries of 2,271,000 square feet. For the year ended December 31, 2008, the average leasing net rent is \$31, which is an increase of 48% over the average expiring net rent of \$21.

The details of our leasing activity for 2008 are as follows:

(000's Sq. Ft.)	Dec. 31, 2007		Activities during the year ended Dec. 31, 2008						Dec. 31, 2008	
	GLA ⁽¹⁾	Leased	Expiries	Average Expiring Net Rent	Year One ⁽²⁾⁽⁴⁾ Leasing Net Rent	Average ⁽³⁾⁽⁴⁾ Leasing Net Rent	Acq. (Disp.)	GLA ⁽¹⁾	Leased	
Toronto, Ontario	7,054	6,901	(662)	\$ 22	658	\$ 28	\$ 28	—	7,054	6,897
Ottawa, Ontario	2,780	2,769	(75)	15	78	21	21	—	2,780	2,772
Calgary, Alberta	6,704	6,690	(2,190)	21	2,197	31	33	—	6,704	6,697
Edmonton, Alberta	710	705	(74)	9	79	24	24	1	711	710
Vancouver, B.C.	853	838	(22)	22	19	31	33	—	853	835
Other	212	164	(1)	—	1	—	—	(209)	3	3
Total ⁽¹⁾	18,313	18,067	(3,024)	\$ 21	3,032	\$ 30	\$ 31	(208)	18,105	17,914
Development Pre-leasing					268					
Total Leasing					3,300					

⁽¹⁾ Excludes developments

⁽²⁾ Represents net rent in the first year

⁽³⁾ Represents average net rent over lease term

⁽⁴⁾ Excludes noncore properties sold

INTEREST AND OTHER INCOME

Loans and investment income totaled \$20.5 million in 2008 (compared to \$12.3 million in 2007). The increase primarily relates to interest income earned on the on-demand deposits with BPC and income from non-core investments, offset by a decrease in third-party loan interest income as a result of the repayment of the Atrium on Bay and Exchange Tower loan receivables during 2007.

INTEREST EXPENSE

Interest expense was \$39.5 million in 2008 (compared to \$30.0 million in 2007). The increase is due to new financings for 105 Adelaide Street West in Toronto during the first quarter of 2008; 2 Queen Street East and Hudson's Bay Centre in Toronto, Altius Centre in Calgary, Canadian Western Bank Place in Edmonton and Royal Centre in Vancouver during the second quarter of 2008; 20-22 Front Street in Toronto during the third quarter of 2008, Petro Canada Centre in Calgary in the fourth quarter of 2008; as well as amortization of deferred financing fees using the effective-interest-rate method.

GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses were \$22.5 million for year ended December 31, 2008 (compared to \$20.2 million in 2007). The increase is largely due to general inflationary pressures in addition to an increase in advisory fees, and certain one-time expenditures relating to upgrading and improving our budgeting and leasing systems as well as overall systems security.

DEPRECIATION AND AMORTIZATION EXPENSE

Depreciation and amortization expense includes amortization of the value of buildings over their useful lives and the accelerated amortization of lease-origination and tenant-relationship costs over the average life of the lease portfolio. Depreciation and amortization expense for the year ended December 31, 2008, was \$53.7 million (compared to \$58.5 million in 2007).

QUARTERLY RESULTS

The 2008 and 2007 results by quarter are as follows:

(Millions, except per-share amounts)	2008				2007			
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Total Revenue	\$ 98.5	\$ 88.6	\$ 91.2	\$ 87.4	\$ 90.6	\$ 86.9	\$ 90.2	\$ 91.0
Net operating income								
Operating income from commercial properties	49.8	49.2	48.8	47.7	47.6	46.0	48.8	45.0
Loans and investment income	8.1	4.0	4.8	3.6	5.1	2.3	2.0	2.9
	57.9	53.2	53.6	51.3	52.7	48.3	50.8	47.9
Expenses								
Interest expense	11.4	9.5	9.8	8.8	6.1	8.2	7.4	8.3
General and administrative expenses	7.1	5.1	5.2	5.1	4.8	4.5	5.1	5.8
Transaction costs	—	—	—	—	—	4.0	—	—
	39.4	38.6	38.6	37.4	41.8	31.6	38.3	33.8
Depreciation and amortization	14.8	13.3	13.0	12.6	15.6	13.6	14.4	14.9
Income taxes	9.6	9.9	7.8	7.5	5.7	7.9	8.1	6.5
Net income from continuing operations	15.0	15.4	17.8	17.3	20.5	10.1	15.8	12.4
Discontinued operations	—	—	—	—	22.5	5.3	5.3	46.9
Net income	\$ 15.0	\$ 15.4	\$ 17.8	\$ 17.3	\$ 43.0	\$ 15.4	\$ 21.1	\$ 59.3
Net income per common share								
Continuing operations	\$ 0.42	\$ 0.43	\$ 0.49	\$ 0.46	\$ 0.55	\$ 0.19	\$ 0.40	\$ 0.28
Discontinued operations	—	—	—	—	0.79	0.19	0.19	1.64
	\$ 0.42	\$ 0.43	\$ 0.49	\$ 0.46	\$ 1.34	\$ 0.38	\$ 0.59	\$ 1.92
Funds from operations and gains per common share								
Continuing operations	\$ 1.29	\$ 1.24	\$ 1.22	\$ 1.16	\$ 1.30	\$ 1.09	\$ 1.19	\$ 1.03
Discontinued operations	—	—	—	—	0.05	0.06	0.11	0.12
Property-disposition gains	—	—	—	—	0.92	0.20	0.17	1.91
	\$ 1.29	\$ 1.24	\$ 1.22	\$ 1.16	\$ 2.27	\$ 1.35	\$ 1.47	\$ 3.06

Operating income from current properties has increased since 2007 due to higher occupancy and rental rates.

Loans and investment income increased in the fourth quarter of 2008 compared to the previous quarters in 2008 primarily due to income from a non-core investment.

Interest expense increased in the fourth quarter of 2008 compared to the previous quarters in 2008 primarily due to a \$0.6 million prepayment fee incurred on the repayment of the Petro-Canada Centre bonds in Calgary.

PART III – RISKS AND UNCERTAINTIES

BPO Properties' financial results are affected by the performance of our operations and various external factors influencing the specific sectors and geographic locations in which we operate, as well as macroeconomic factors such as economic growth, inflation, and interest rates; regulatory requirements and initiatives; and litigation and claims that arise in the normal course of business.

Our strategy is to invest in premier assets that generate sustainable streams of cash flow. Although high-quality assets may initially generate lower returns on capital, we believe that the sustainability and future growth of their cash flows is more ensured over the long term, and as a result, warrant higher valuation levels. We also believe that the high quality of our asset base protects the Company against future uncertainty and enables us to invest with confidence when opportunities arise.

The following is a review of the material factors and the potential impact these factors may have on our business operations. A more detailed description of the business environment and risks is contained in our Annual Information Form which is posted on our Web site at www.bpoproperties.com or at www.sedar.com.

PROPERTY-RELATED RISKS

Our strategy is to invest in high-quality core office properties as defined by the physical characteristic of the asset and, more importantly, the certainty of receiving rental payments from large corporate tenants (with investment-grade credit ratings – see "Credit Risk" below) that these properties attract. Nonetheless, we remain exposed to certain risks inherent in the core office-property business.

Commercial property investments are generally subject to varying degrees of risk depending on the nature of the property. These risks include changes in general economic conditions (such as the availability and costs of mortgage funds), local conditions (such as an oversupply of space or a reduction in demand for real estate in the markets in which we operate), the attractiveness of the properties to tenants, competition from other landlords with competitive space, and our ability to provide adequate maintenance at an economical cost.

Certain significant expenditures, including property taxes, maintenance costs, mortgage payments, insurance costs, and related charges, must be made regardless of whether a property is producing sufficient income to service these expenses. Our core office properties are subject to mortgages that require substantial debt service payments. If we become unable or unwilling to meet mortgage payments on any property, losses could be sustained as a result of the mortgagee's exercise of its rights of foreclosure or of sale. We believe the stability and long-term nature of our contractual revenues effectively mitigates these risks.

As owners and managers of premier office properties, lease rollovers also present a risk factor, as continued growth of rental income is dependent on strong leasing markets to ensure expiring leases are renewed and new tenants are found promptly to fill vacancies. Refer to "Lease Rollover Risk" on page 28 of this MD&A for further details.

INTEREST RATE AND FINANCING RISK

We attempt to stagger the maturities of our mortgage portfolio evenly over a 10-year time horizon. We believe that this strategy will most effectively manage interest rate risk.

As outlined under "Capital Resources and Liquidity," on page 19 of this MD&A, we have an ongoing obligation to access debt markets to refinance maturing debt as it comes due. There is a risk that lenders will not refinance such maturing debt on terms and conditions acceptable to us, or on any terms at all. Our strategy is to stagger the maturities of our mortgage portfolio attempts to mitigate our exposure to excessive amounts of debt maturing in any one year.

Approximately 37% of our outstanding commercial and development property debt at December 31, 2008 is floating-rate debt (December 31, 2007 – 36%) and subject to fluctuations in interest rates. The effect of a 100-basis-point increase in interest rates on interest expense relating to our floating-rate debt, all else being equal, is an increase in interest expense, net of taxes of \$3.1 million on an annual basis or approximately \$0.11 per share. In addition, we have \$125.0 million (compared to \$262.1 million on December 31, 2007) of our loan receivable balances at December 31, 2008, subject to variable interest rates. The effect of a 100-basis-point decrease in interest rates on interest income relating to our variable-rate loan receivable, all else being equal, is a decrease in interest income, net of taxes of \$0.9 million on an annual basis or approximately \$0.03 per share. The analysis does not reflect the impact a changing interest rate environment could have on our overall performance, and as a result, it does not reflect the actions management may take in such an environment.

We currently have a level of indebtedness for the Company of 53% of gross book value. This level of indebtedness is considered by the Company to be conservative and, based on this, the Company believes that all debts will be financed or refinanced as they come due in the foreseeable future.

CREDIT RISK

Credit risk arises from the possibility that tenants may be unable to fulfill their lease commitments. We mitigate this risk by ensuring that our tenant mix is diversified and by limiting our exposure to any one tenant. We also maintain a portfolio that is diversified by property type so

that exposure to a business sector is lessened. Currently, no one tenant represents more than 12.8% of total leasable area or 8.3% of tenant receivables.

We attempt to mitigate our credit risk by signing long-term leases with tenants who have investment-grade credit ratings. Additional discussion of this strategy is discussed on page 8 of this MD&A.

The following list shows the largest tenants by leasable area in our portfolio and their respective lease commitments:

Tenant	Location	Year of Expiry ⁽¹⁾	000's Sq. Ft. ⁽²⁾	% of Sq. Ft. ⁽²⁾	Credit Rating ⁽³⁾
Rated					
Government of Canada	Various	2013	1,896	12.8	AAA
Bank of Montreal/Nesbitt Burns	Toronto, Ottawa, Calgary	2018	1,134	7.6	A+
Petro-Canada	Calgary	2028	1,015	6.8	BBB
Imperial Oil	Calgary	2016	717	4.8	AAA
Talisman Energy	Calgary	2015	539	3.6	BBB
Enbridge Inc.	Calgary, Edmonton	2015	449	3.0	A-
RBC Financial Group	Toronto, Calgary, Vancouver	2023	438	3.0	AA-
Canadian Natural Resources	Calgary	2011	305	2.1	BBB
CIBC	Toronto, Calgary	2034	281	1.9	A+
EnCana Corporation	Calgary	2014	241	1.6	A-
Manufacturers Life Insurance	Toronto	2013	169	1.1	AAA
Lombard Insurance	Toronto	2012	134	0.9	A-
Westcoast Energy	Calgary, Vancouver	2012	132	0.9	BBB+
HSBC Of Canada	Toronto	2011	109	0.7	AA
National Bank of Canada	Toronto, Ottawa	2013	93	0.6	A
Xstrata (Falconbridge)	Toronto	2017	81	0.5	BBB
Other investment-grade	Various	Various	546	3.7	BBB- or higher
			8,279	55.6%	BBB- or higher
Bennett Jones	Toronto, Calgary	2013	306	2.1	
Osler, Hoskin & Harcourt	Toronto	2015	270	1.8	
The Hudson's Bay Company	Toronto	2009	209	1.4	
CI Investments Inc.	Toronto	2012	195	1.3	
Toronto Stock Exchange	Toronto	2018	179	1.2	
Gowlings Canada Inc.	Toronto	2020	170	1.1	
Crescent Point Resources	Calgary	2020	140	0.9	
Fraser Milner Casgrain	Toronto, Calgary	2010	138	0.9	
Davies Ward Philips Vineberg	Toronto	2013	119	0.8	
Citco (Canada) Inc.	Toronto	2018	99	0.7	
PriceWaterhouseCoopers	Calgary	2015	95	0.6	
Precision Drilling Corp.	Calgary	2011	93	0.6	
Other government agencies	Various	Various	203	1.4	
Total			10,495	70.4%	

⁽¹⁾ Weighted average based on square feet

⁽²⁾ Prior to considering partnership interests in partially owned properties and excludes parking

⁽³⁾ From Standard & Poor's, Moody's, or Dominion Bond Rating Service

Because we invest in mortgages from time to time, further credit risks arise in the event that borrowers default on the repayment of their mortgages to us. We endeavor to ensure that adequate security has been provided in support of such mortgages.

LEASE ROLLOVER RISK

Lease rollover risk arises from the possibility that we may experience difficulty renewing leases as they expire or in re-leasing space vacated by tenants upon early lease expiry. We attempt to stagger the lease expiry profile so that we are not faced with disproportionate amounts of space expiring in any one year; approximately 9.3% (the majority of which is in 2013) of our leases mature annually over the next five years. Our portfolio has a weighted-average lease life of seven years. We further mitigate this risk by maintaining a diversified portfolio mix by geographic location and by proactively leasing space in advance of its contractual expiry.

The following table sets out lease expiries, by square footage, for our portfolio at December 31, 2008:

(000's Sq. Ft.)	Currently								2016		Parking	Total
	Available	2009	2010	2011	2012	2013	2014	2015	& Beyond	Subtotal		
Toronto, Ontario	157	393	491	298	694	1,273	223	514	2,182	6,225	829	7,054
Ottawa, Ontario	8	35	7	8	6	1,131	9	542	4	1,750	1,030	2,780
Calgary, Alberta	7	61	346	680	461	502	111	1,016	2,497	5,681	1,023	6,704
Edmonton, Alberta	1	14	136	55	7	9	28	81	259	590	121	711
Vancouver, B.C	18	24	39	74	62	84	5	34	249	589	264	853
Other	—	—	—	—	—	2	—	—	1	3	—	3
Total	191	527	1,019	1,115	1,230	3,001	376	2,187	5,192	14,838	3,267	18,105
% of total	1.3%	3.6%	6.9%	7.5%	8.3%	20.2%	2.5%	14.7%	35.0%	100.0%		

ENVIRONMENTAL RISKS

As an owner of real property, we are subject to various federal, provincial, state, and municipal laws relating to environmental matters. Such laws provide that we could be liable for the costs of removing certain hazardous substances and remediating certain hazardous locations. The failure to remove or remediate such substances or locations, if any, could adversely affect our ability to sell such real estate or to borrow using such real estate as collateral and could potentially result in claims against us. We are not aware of any material noncompliance with environmental laws at any of our properties nor are we aware of any pending or threatened investigations or actions by environmental regulatory authorities in connection with any of our properties or any pending or threatened claims relating to environmental conditions at our properties.

We will continue to make the necessary capital and operating expenditures to ensure that we are compliant with environmental laws and regulations. Although there can be no assurances, we do not believe that costs relating to environmental matters will have a materially adverse effect on our business, financial condition, or results of operations. However, environmental laws and regulations can change and we may become subject to more stringent environmental laws and regulations in the future, which could have an adverse effect on our business, financial condition, or results of operations.

OTHER RISKS AND UNCERTAINTIES

Real estate is relatively illiquid. Such illiquidity may limit our ability to vary our portfolio promptly in response to changing economic or investment conditions. Also, financial difficulties of other property owners resulting in distressed sales could depress real estate values in the markets in which we operate.

Our commercial properties generate a relatively stable source of income from contractual tenant rent payments. Continued growth of rental income is dependent on strong leasing markets to ensure expiring leases are renewed and new tenants are found promptly to fill vacancies.

Taking into account the current state of the economy, 2009 likely will not provide the same level of increases in rental rates on renewal as compared to previous years. We are, however, substantially protected against short-term market conditions, as most of our leases are long-term in nature with an average term of seven years. As we face the onset of a severe recession, it is possible we will see downward pressure on overall occupancy levels and net effective rents.

The Company has insurance covering certain acts of terrorism for up to \$1.0 billion of damage and resulting business interruption costs. The Company continues to seek additional coverage equal to the full replacement cost of its assets; however, until this type of coverage becomes commercially available on an economically reasonable basis, any damage or business interruption costs as a result of uninsured acts of terrorism could result in a material cost to the Company. The Company believes it is in compliance with all of its loan covenants despite not being able to acquire terrorism coverage for the full replacement cost of all our properties.

DERIVATIVE FINANCIAL INSTRUMENTS

We utilize derivative financial instruments from time to time, primarily to manage financial risks, including interest rate, commodity, and foreign-exchange risks. Hedge accounting is applied where the derivative is designated as a hedge of a specific exposure and there is reasonable assurance the hedge will be effective in offsetting an identified risk. Realized and unrealized gains and losses on derivative financial instruments designated as hedges of financial risks are included in income as an offset to the hedged item in the period the underlying asset, liability, or anticipated transaction to which they relate.

Financial instruments that are not designated as hedges are carried at estimated fair values, and gains and losses arising from changes in fair values are recognized in income as a component of interest and other income in the period the changes occur. The use of nonhedging derivative contracts is governed by documented risk-management policies and approved limits.

During the year ended December 31, 2008, our use of derivative financial instruments was limited to foreign-exchange contracts and forward gas contracts. Unrealized gains and losses, representing the fair value of such contracts, are determined in reference to the appropriate forward exchange rate for each contract at December 31, 2008 and are reflected in receivables and other assets or accounts payable and other liabilities, as appropriate, on the consolidated balance sheet.

At December 31, 2008, the Company had foreign-exchange contracts to sell a notional amount of US\$21.0 million (December 31, 2007 – US\$21.0 million) at an exchange rate of US\$1.00 = C\$1.22, maturing in March 2009, which have not been designated as hedges for financial reporting purposes. The aggregate fair value of these contracts at December 31, 2008, was \$nil and is reflected in loans receivable in the consolidated balance sheets and in loans and investment income in the consolidated statements of income and comprehensive income.

The Company has entered into fixed gas-purchase contracts with a third party gas supplier, which covers the period November 1, 2008, to October 31, 2009. As of December 31, 2008, the remaining commitment for the Company to purchase gas for its facilities was \$2.9 million.

The primary risks associated with our use of derivatives are credit risk and price risk. Credit risk is the risk that losses will be incurred from the default of the counterparty on its contractual obligations. The use of derivative contracts is governed by documented risk-management policies and approved limits, which includes an evaluation of the creditworthiness of counterparties, as well as managing the size, diversification, and maturity of the portfolio. Price risk is the risk that we will incur losses from derivatives from adverse changes in foreign-exchange rates and gas prices. We mitigate price risk by entering only into derivative transactions where we have determined a significant offset exists between changes in the fair value of, or the cash flows attributable to, the hedged item and the hedging item.

PART IV – CRITICAL ACCOUNTING POLICIES AND ESTIMATES

CHANGES IN ACCOUNTING POLICIES

We adopted the following new accounting policies, none of which individually or collectively had a material impact on our consolidated financial statements, unless otherwise noted. These changes were the result of changes to the Canadian Institute of Chartered Accountants ("CICA") Handbook, Accounting Guidelines ("AcG"), or Emerging Issues Committee Abstracts ("EIC").

Capital Disclosures

Effective January 1, 2008, the Company adopted the CICA issued Handbook Section 1535, "Capital Disclosures." Section 1535 requires the disclosure of (i) an entity's objectives, policies and process for managing capital; (ii) quantitative data about an entity's managed capital; (iii) whether an entity has complied with capital requirements; and (iv) if an entity has not complied with such capital requirements, the consequences of such non-compliance. The Company adopted the requirements of Section 1535 on January 1, 2008 and the required disclosures are included in Note 19 of these consolidated financial statements.

Financial Instruments – Disclosures and Presentation

Effective January 1, 2008, the Company adopted the two CICA issued Handbook Sections 3862, "Financial Instruments – Disclosures," and Section 3863, "Financial Instruments – Presentation." These standards replace Section 3861, "Financial Instruments – Disclosure and Presentation" and require additional disclosure of the nature and extent of risks arising from financial instruments and how the entity manages those risks. Disclosures required by Section 3862 have been made in the notes to these consolidated financial statements. The adoption of Section 3863 did not have any impact on the Company's consolidated financial statements.

FUTURE ACCOUNTING POLICY CHANGES

Goodwill and Intangible Assets

In February 2008, the CICA issued a new accounting standard, Section 3064, "Goodwill and Intangible Assets." Section 3064 replaces Sections 3062, "Goodwill and Other Intangible Assets" and 3450, "Research and Development Costs." The section establishes standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. Standards concerning goodwill are unchanged from those included in the previous Section 3062. Various changes have been made to other sections of the CICA Handbook for consistency purposes. As a result of related amendments to Section 100, "Financial Statement Concepts," any expenses deferred pursuant to previously existing "matching" concepts and which do not otherwise meet the definition of an asset, will no longer be eligible for capitalization as an asset. The new section and related amendments will be applicable to financial statements relating to fiscal years beginning on or after October 1, 2008. Accordingly, the Company will adopt the new standards for fiscal year beginning January 1, 2009. Consistent with transition provisions in Section 3064, the Company will adopt the standards retrospectively with restatement. The Company is still assessing the impact of the adoption of this standard but expects that the effect of adopting Section 3064 and its related amendments will be a reduction in commercial properties with a corresponding charge against retained earnings.

International Financial Reporting Standards ("IFRS")

In 2006, the Canadian Accounting Standards Board ("AcSB") published a new strategic plan that will significantly affect financial reporting requirements for Canadian companies. The AcSB strategic plan outlines the convergence of Canadian GAAP with IFRS over an expected five-year transitional period. In February 2008, the AcSB announced that 2011 is the changeover date for publicly accountable companies to use IFRS, replacing Canadian GAAP. The date is for interim and annual financial statements relating to the fiscal years beginning on or after January 1, 2011. The transition date of January 1, 2011 will require the restatement for comparative purposes of amounts reported by the Company for the year ended December 31, 2010. Though the Company has begun assessing the adoption of IFRS for 2011, the financial reporting impact of the transition to IFRS cannot be reasonably estimated at this time. The Company continues to monitor and assess the impact of the convergence of Canadian GAAP and IFRS as new standard changes are introduced over the transitional period.

USE OF ESTIMATES

The preparation of financial statements, in conformity with Canadian generally accepted accounting principles, requires estimates and assumptions that affect the carried amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from estimates. Significant estimates are required in the determination of future cash flows and probabilities in assessing net recoverable amounts and net realizable values, the allocation of the purchase prices to components of commercial properties and businesses acquired, the useful lives for depreciation and amortization, the Company's ability to utilize tax losses and the rates at which those losses will be realized, the effectiveness of hedges, and fair value of financial instruments for disclosure purposes.

Our critical accounting policies are those that we believe are the most important in portraying our financial condition and results and require the most subjective judgment and estimates on the part of management. A summary of our significant accounting policies, including the critical accounting policies discussed below, is set forth in Note 1 to our consolidated financial statements.

Property Acquisitions

Upon acquisition of rental properties, we determine the fair value of acquired tangible and intangible assets, including land, buildings, tenant improvements, above- and below-market in-place operating leases, origination costs related to acquired in-place leases, other identified intangible assets, and assumed liabilities and allocate the purchase price to the acquired assets and assumed liabilities, including land at appraised value and buildings at depreciated replacement cost. We assess and consider fair values based on estimated cash flow projections that utilize appropriate discount rates, as well as available market information. Estimates of future cash flows are based on a number of factors including the historical operating results, known and anticipated trends, and market conditions. We also consider an allocation of purchase price to other acquired intangibles, including acquired in-place leases that may have intangible value with regard to the customer relationship, including (but not limited to) the nature and extent of the existing relationship with the tenant, the tenant's credit quality, and expectations of renewals. We record acquired above- and below-market in-place operating leases at their fair values, using a discount rate that reflects the risks associated with the leases acquired. The fair values are equal to the difference between (1) the contractual amounts to be paid pursuant to each in-place lease, and (2) management's estimate of fair-market lease rates for each corresponding in-place lease, measured over a period equal to the remaining term of the leases for above-market leases and the initial term plus the term of any below-market fixed-rate renewal options for below-market leases. Recorded amounts for in-place lease-origination values are based on our evaluation of the specific characteristics of each tenant's lease. Factors to be considered include estimates of carrying costs during expected lease-up periods considering current market conditions and costs to execute similar leases. Building is stated at a depreciated replacement cost.

The cost of buildings and improvements includes the purchase price of property, legal fees, and other acquisition costs.

Depreciation and amortization on rental properties is based on the allocation of the acquisition cost to land, building, tenant improvements, and intangibles and their estimated useful lives, based on management's estimates. The allocation of the acquisition cost and the determination of the estimated useful lives of the components significantly affect the computation of depreciation and amortization recorded over future periods and, accordingly, net income.

Our lease agreements generally provide tenant improvements, in which lease agreements generally provide for payments by the landlord to the tenant in the form of tenant improvement allowances, are amounts paid by the Company pursuant to such lease provisions and are characterized as either the purchase of tenant improvements owned by the landlord, or tenant inducements. When the payment is determined to be for tenant improvements owned by the Company, then the improvements are accounted for as an addition to commercial property and depreciated over their estimated useful life. If the Company determines that it is not the owner of the tenant improvements, then the property subject to the lease is the unimproved space and any payments made to the tenant under the lease are treated as tenant inducements, which reduce revenue over the term of the lease.

Depreciation

We apply the straight-line method of depreciation. Under this method, depreciation is charged to income on a straight-line basis over the remaining estimated useful life of the property. A significant portion of the acquisition cost of each property is allocated to building. The allocation of the acquisition cost to building and the determination of the useful life are based upon management's estimates. In the event the allocation to building is inappropriate or the estimated useful life of buildings proves incorrect, the computation of depreciation will not be appropriately reflected over future periods.

Impairment of Assets

We review the long-lived assets used in operations for impairment when there is an event or change in circumstances that indicates a potential impairment in value. An asset is considered impaired when the undiscounted future cash flows are not sufficient to recover the asset's carrying value. If such impairment is present, an impairment loss is recognized based on the excess of the carrying amount of the asset over its fair value. The evaluation of anticipated cash flows is based in part on assumptions regarding future occupancy, rental rates, and capital requirements that could differ materially from actual results in future periods.

There were no impairments recorded for the years ended December 31, 2008, or December 31, 2007.

Revenue Recognition

Base rental revenue, representing the total amount of contractual rent to be received from a lease, is reported on a straight-line basis over the term of each lease. Revenue recognition under a lease begins when the tenant takes possession of, or controls, the physical use of the property subject to the lease. Generally, this occurs on the lease commencement date or, where we are required to make additions to the property in the form of tenant improvements, upon substantial completion of those improvements. A free-rent or straight-line rent receivable is recorded for rental income recognized in excess of rent payments actually received pursuant to the terms of the individual lease agreements. An allowance for doubtful accounts is recorded, if necessary, for estimated losses resulting from the inability of tenants to make required rent payments. The computation of this allowance is based on the tenants' payment history and current credit status.

In accordance with EIC-140, we also recognize rental revenue of acquired in-place above- and below-market leases at their fair value over the terms of the respective leases.

Recoveries from tenants, consisting of amounts due from tenants for common area maintenance, real estate taxes, and other recoverable costs, are recognized as revenue in the period the expenses are incurred. Tenant reimbursements are recognized and presented in accordance with EIC Abstract No. 123 "Reporting Revenue Gross as a Principal versus Net as an Agent," which requires that these reimbursements be recorded on a gross basis, as we are generally the primary obligor with respect to purchasing goods and services from third-party suppliers, having discretion in selecting suppliers and taking credit risk.

Revenue and expenses related to commercial developments are recognized in income when the development is substantially complete. This is also the point at which the property is reclassified from commercial developments to commercial properties. The Company considers a commercial development to be substantially complete upon the earlier of attaining an occupancy that results in break-even income after debt servicing or the expiration of a reasonable maximum period of time, but no later than one year after completion of major construction. Prior to substantial completion, revenues and expenses related to commercial developments are capitalized to the property. To the extent a development or redevelopment property is leased and the tenant begins to occupy the space as construction is substantially complete in phases, we would recognize revenue and expenses in accordance with those respective phases.

Fair Value of Financial Instruments

The fair values of commercial and development property debt are calculated based on the discount spread between the future contractual interest payments and future interest payments on mortgage debt based on a current market rate. In determining the current market rate, market spread is added to the quoted yields on federal government bonds with similar maturity dates similar to debt in place. Because valuations of the financial instruments are based on these types of estimates, the fair values of financial instruments may change if the estimates do not prove to be accurate.

The fair values of derivative instruments are calculated using generally accepted pricing models.

Tax

In accordance with Canadian GAAP, we use the liability method of accounting for future income taxes and provide for future income taxes for all significant income-tax temporary differences.

Preparation of the financial statements requires an estimate of income taxes in the jurisdictions in which we operate. The process involves an estimate of our actual current tax exposure and an assessment of temporary differences resulting from differing treatment of items, such as depreciation and amortization, for tax and accounting purposes. These differences result in future tax assets and liabilities, which are included in our balance sheet. An assessment must also be made to determine the likelihood that our future tax assets will be recovered from future taxable income. To the extent that recovery is not considered more likely than not, a valuation allowance must be provided.

Judgment is required in determining the provision for income taxes, future income tax assets and liabilities, and any related valuation allowance. To the extent a valuation allowance is created or revised, current-period earnings will be affected. Judgment is required to assess tax interpretations, regulations, and legislation, which are continually changing, to ensure liabilities are complete and to ensure assets net of valuation allowances are realizable. The impact of different interpretations and applications could potentially be material.

During the year, we released \$nil (compared to \$1.0 million in 2007) of tax-valuation allowances following the completion of certain reviews by taxation authorities, and de-recognized \$1.6 million (compared to \$8.2 million in 2007) in previously recognized tax assets in connection with a strategic tax review undertaken by the Company and determination of the necessary plans to realize such assets. Both these changes are reflected in our income tax provision.

RELATED-PARTY TRANSACTIONS

In the normal course of operations, the Company enters into various transactions on market terms with related parties which have been measured at exchange value and are recognized in the consolidated financial statements.

The Company has entered into two service-support agreements with Brookfield Properties Ltd. ("BPL"), a subsidiary of BPC (one agreement dated October 21, 2005, relating to the former O&Y properties and the other dated January 1, 2006, in relation to the other properties owned by the Company as of such date). The purpose of the agreements is to provide the services of certain personnel and consultants as well as such facilities of BPL as are necessary to help the Company provide the services and facilities required of it pursuant to property-management services to which it is a party. The fees paid to BPL are on a cost-recovery basis and totaled \$13.0 million during 2008 (compared to \$11.4 million in 2007). The service-support agreements also permit the Company to charge costs and expenses payable by the Company, which are attributable to BPL on a cost-recovery basis. Total costs charged to BPL during 2008 totaled \$0.8 million (compared to \$0.6 million in 2007).

The Company has certain arrangements with an affiliate of Brookfield Asset Management Inc. ("BAM"), the ultimate parent of the Company, and BPC to provide various information technology services and with BPC to provide various administrative services including accounts payable processing and accounts receivable collection. The costs for these services amounted to \$8.2 million for the year ended December 31, 2008, and are charged to the Company on a cost recovery basis and replaced similar costs that were incurred directly by the Company in the prior year when these services were performed internally.

Included in loans receivable at December 31, 2008, is a \$125.0 million (December 31, 2007 - \$220.3 million) on-demand deposit placed with BPC. In two separate transactions during the second quarter of 2008, BPC repaid the original \$220.3 million on-demand deposit that was issued in December 2007 and a new \$125.0 million on-demand deposit was placed with BPC. For the year ended December 31, 2008, interest income of \$7.0 million was recorded on these deposits (compared to \$0.2 million in 2007). Subsequent to year-end, the full amount of the on-demand deposit was repaid to the Company (see note 21 of the consolidated financial statements).

Included in rental revenues during the year ended December 31, 2008, are amounts received from BAM, and its affiliates of \$0.4 million (December 31, 2007 - \$0.4 million). In addition, the Company has certain arrangements with BAM and its affiliates to acquire insurance in the normal course and at market rates or at cost. These fees are based on a percentage of the annual premiums paid.

PART V – BUSINESS ENVIRONMENT AND OUTLOOK

OPERATING ENVIRONMENT AND OUTLOOK

The consequences of the current downturn in the economy, including a rise in unemployment, a drop in consumer and business confidence and spending, and nearly non-existent debt markets, are having an adverse effect on the real estate industry as a whole. Leasing demand in most of our markets has tempered and we are beginning to see increasing direct and sublease availabilities and associated downward pressure on rents and economic fundamentals. Our occupancy levels, however, are at 98.7% across our portfolio and only 2.2% (including the 194,000 square foot lease renewal with Hudson's Bay at Hudson's Bay Centre, completed subsequent to the year-end) of the space within our portfolio is scheduled to come off lease in 2009. The high quality of our properties relative to others in our markets should enable us to attract new tenants if we are unsuccessful in extending leases with existing tenants. Furthermore, our in-place rents continue to be below market. In our portfolio, the average expiring rates in 2009 are \$18 per square foot compared with a current market rate of \$29 per square foot, representing a 61% discount. Our average in-place net rent of \$22 increased by 4.8% as compared with the prior year notwithstanding the difficult environment. Our strong tenant lease profile, low vacancies and rental rates that in most properties are substantially below current market rates, give us a high level of confidence that we can achieve our operating targets in 2009. Furthermore, the general lack of development, especially in the central business districts, has created stability from a supply perspective.

While we remain committed to commercial property development and redevelopment opportunities in these current market conditions, our focus is on completing the construction of our underway development pipeline on time and budget and continuing to make progress on leasing. Any new development will have to provide appropriate risk-adjusted returns, have substantial pre-lease commitments and be financeable before we would be willing to proceed.

Looking longer term, with a solid platform consisting of a strong balance sheet, a well-leased portfolio with below-market net rents, a 5.7 million square foot development and redevelopment pipeline and financial flexibility, BPO Properties is well-positioned to continue to deliver on its commitments to shareholders.

DISCLOSURE CONTROLS AND PROCEDURES

Management, including the Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as defined in the Canadian Securities Administrators Multilateral Instrument 52-109) as of December 31, 2008. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that such disclosure controls and procedures as of December 31, 2008, are effective in providing reasonable assurance that material information relating to the Company and our consolidated subsidiaries would be made known to us by others within those entities.

INTERNAL CONTROLS OVER FINANCIAL REPORTING

Management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is a process designed by, or under the supervision of, the President and Chief Executive Officer and the Chief Financial Officer and effected by the Board of Directors, management and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP.

Management assessed both the design and operating effectiveness of the Company's internal control over financial reporting as at December 31, 2008, based on criteria established by the COSO control framework and Multilateral Instrument 52-109. Based on this assessment, management believes that, as at December 31, 2008, the Company's internal control over financial reporting is effective.

Due to its inherent limitations, internal controls over financial reporting may not prevent or detect misstatements on a timely basis. Also, projections of any evaluation to the effectiveness of internal control over the financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management took appropriate steps that enabled it to conclude that during the fiscal year ended December 31, 2008, no changes were made to internal controls over financial reporting that would have materially affected or would be reasonably considered to materially affect these controls.

OUTLOOK

Despite this period of financial market volatility and illiquidity, as well as the significant stress put on common stocks such as ours, BPO Properties is in secure economic health as evidenced by our positive earnings and low vacancy. With high occupancy, low rollover exposure, and manageable near-term debt maturities, we are optimistic about our performance prospects for 2009.



Bryan Davis

*Senior Vice President and Chief Financial Officer
March 6, 2009*

DISTRIBUTIONS

Distributions paid by the Company during the year ended December 31, 2008, and the past three fiscal years are as follows:

	December 31, 2008	December 31, 2007	December 31, 2006	December 31, 2005
Common shares ⁽¹⁾	\$ 0.60	\$ 0.60	\$ 0.60	\$ 0.60
Preferred shares				
Series G	0.97	1.05	0.92	0.73
Series J	0.94	1.06	0.95	0.74
Series K	19,202.33	24,662.88	22,194.65	15,646.94
Series M	0.94	1.06	0.95	0.74
Series N	0.96	1.23	1.11	0.78

⁽¹⁾ Excludes a special common share dividend of \$7.25 per share in 2008

ADDITIONAL INFORMATION

Quarterly supplementary information packages with more detailed financial information is posted on BPO Properties' website at www.bpoproperties.com and should be read in conjunction with this annual report.

Management's Responsibility for the Financial Statements

The consolidated financial statements and management's financial analysis and review contained in this annual report are the responsibility of the management of the Company. To fulfill this responsibility, the Company maintains a system of internal controls to ensure that its reporting practices and accounting and administrative procedures are appropriate and provide assurance that relevant and reliable financial information is produced. The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles and, where appropriate, reflect estimates based on management's best judgment in the circumstances. The financial information presented throughout this annual report is consistent with the information contained in the consolidated financial statements.

Deloitte & Touche LLP, the independent auditors appointed by the shareholders, have audited the consolidated financial statements in accordance with Canadian generally accepted auditing standards to enable them to express to the shareholders their opinion on the consolidated financial statements. Their report as auditors is set out below.

The consolidated financial statements have been further examined by the Board of Directors and by its Audit Committee, which meets with the auditors and management to review the activities of each and reports to the Board of Directors. The auditors have direct and full access to the Audit Committee and meet with the committee both with and without management present. The Board of Directors, directly and through its Audit Committee, oversees management responsibilities and is responsible for reviewing and approving the financial statements.



Thomas F. Farley
President and Chief Executive Officer
March 6, 2009



Bryan Davis
Senior Vice President and Chief Financial Officer

Auditors' Report

To the Shareholders of BPO Properties Ltd.,

We have audited the consolidated balance sheets of BPO Properties Ltd. as at December 31, 2008, and 2007, and the consolidated statements of income and comprehensive income, changes in shareholders' equity, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2008, and 2007, and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Toronto, Canada
March 6, 2009



Chartered Accountants
Licensed Public Accountants

Consolidated Balance Sheets

December 31 (Millions)	Notes	2008	2007
Assets			
Commercial properties	4	\$ 1,338.7	\$ 1,351.6
Commercial developments	5	689.1	452.5
Loans receivable	6	150.6	283.5
Intangible assets	7	30.3	40.2
Tenant receivables and other assets	8	82.3	66.0
Cash and cash equivalents	9	61.5	37.7
Assets related to discontinued operations	10	—	4.2
		\$ 2,352.5	\$ 2,235.7
Liabilities			
Commercial and development property debt	11	\$ 1,255.3	\$ 965.5
Intangible liabilities	12	71.9	85.0
Accounts payable and other liabilities	13	105.6	100.4
Future income tax liabilities	14	58.6	41.3
Liabilities related to discontinued operations	10	—	3.0
Shareholders' equity			
	15	861.1	1,040.5
		\$ 2,352.5	\$ 2,235.7

See accompanying notes to the consolidated financial statements

On behalf of the Board,



Richard B. Clark
Chairman



Thomas F. Farley
President and Chief Executive Officer

Consolidated Statements of Income and Comprehensive Income

December 31 (Millions, except per-share amounts)	Notes	2008	2007
Commercial Properties			
Revenue		\$ 345.1	\$ 328.2
Expenses		149.6	140.8
		195.5	187.4
Loans and investment income		20.5	12.3
		216.0	199.7
Expenses			
Interest expense	11	39.5	30.0
General and administrative expenses		22.5	20.2
Transaction costs		—	4.0
		154.0	145.5
Depreciation and amortization		53.7	58.5
Income taxes	14	34.8	28.2
Net income from continuing operations		65.5	58.8
Discontinued operations	10	—	80.0
Net income and comprehensive income		\$ 65.5	\$ 138.8
Net income per common share			
Continuing operations		\$ 1.80	\$ 1.42
Discontinued operations		—	2.81
Total	15	\$ 1.80	\$ 4.23

See accompanying notes to the consolidated financial statements

Consolidated Statements of Changes in Shareholders' Equity

December 31 (Millions)	Notes	2008	2007
Preferred shares			
Balance at beginning and end of year		\$ 381.7	\$ 381.7
Common shares			
Balance at beginning of year		78.8	78.9
Share repurchases	15	(0.4)	(0.1)
Balance at end of year		78.4	78.8
Retained earnings			
Balance at beginning of year		580.0	478.6
Net income		65.5	138.8
Preferred share dividends		(14.3)	(18.2)
Common share dividends		(223.6)	(17.1)
Amount paid in excess of the book value of common shares repurchased	15	(6.6)	(2.1)
Balance at end of year		401.0	580.0
Accumulated other comprehensive income ("AOCI")			
		—	—
Retained earnings and AOCI		401.0	580.0
Shareholders' equity at end of year		\$ 861.1	\$ 1,040.5

See accompanying notes to the consolidated financial statements

Consolidated Statements of Cash Flows

December 31 (Millions)	Notes	2008	2007
Operating activities			
Net income		\$ 65.5	\$ 138.8
Add (deduct):			
Depreciation and amortization		53.7	61.7
Future income taxes		18.3	34.0
Property disposition gains		—	(91.2)
Amortization of above/below market in-place operating leases		(12.9)	(14.6)
Amortization of deferred debt financing costs		3.7	1.6
Loan discount amortization and foreign exchange		(4.7)	3.0
Deferred leasing costs		(3.7)	(3.7)
Increase in receivables		(12.7)	(11.2)
Increase in other assets		(2.4)	(1.2)
Increase in accounts payable and other liabilities		5.4	28.0
Cash flows provided by operating activities		110.2	145.2
Investing activities			
Development and redevelopment expenditures		(237.8)	(135.6)
Capital expenditures		(20.5)	(15.6)
Commercial property tenant improvements		(7.3)	(7.1)
Acquisition of properties		—	(5.0)
Dispositions of properties, net	20	3.3	181.4
Restricted cash and deposits		—	0.3
Advances to related parties	6	(125.0)	(220.3)
Repayments from related parties	6	220.3	—
Loans receivable – collections		41.8	112.4
Loans receivable – advances, net		—	(76.0)
Cash flows used in investing activities		(125.2)	(165.5)
Financing activities			
Commercial and development property debt amortization		(15.6)	(16.9)
Commercial and development property debt repayments		(358.9)	(151.9)
Commercial and development property debt arranged		660.5	239.0
Advances from related parties	6	—	43.0
Repayments to related parties		—	(43.0)
Amortization of debt premiums		(2.3)	(2.4)
Repurchase of common shares	15	(7.0)	(2.2)
Common share dividends paid		(223.6)	(17.1)
Preferred share dividends paid		(14.3)	(18.2)
Cash flows provided by financing activities		38.8	30.3
Increase in cash and cash equivalents		23.8	10.0
Cash and cash equivalents, beginning of year		37.7	27.7
Cash and cash equivalents, end of year		\$ 61.5	\$ 37.7

See accompanying notes to the consolidated financial statements

Notes to the Consolidated Financial Statements

NOTE 1: SUMMARY OF ACCOUNTING POLICIES

(a) General

The consolidated financial statements of BPO Properties Ltd. ("the Company") are prepared in accordance with generally accepted accounting principles ("GAAP") as prescribed by the Canadian Institute of Chartered Accountants ("CICA").

(b) Principles of consolidation

The consolidated financial statements include the accounts of all of the Company's subsidiaries and its proportionate share of assets, liabilities, revenues, and expenses of joint ventures.

(c) Properties

(i) Commercial properties

Commercial properties held for investment are carried at cost less accumulated depreciation. Upon acquisition, the Company allocates the purchase price to the components of the commercial properties acquired. The amount allocated to land is based on its estimated fair value; buildings and existing tenant improvements are recorded at depreciated replacement cost; the values of above- and below-market in-place operating leases are determined based on the present value of the difference between the rents payable under the contractual terms of the leases and estimated market rents; lease-origination costs for in-place operating leases are determined based on the estimated costs that would be incurred to put the existing leases in place under the same terms and conditions; and tenant relationships are measured based on the present value of the estimated avoided net costs if a tenant were to renew its lease at expiry, discounted by the probability of such renewal. Direct acquisition fees and costs, which exclude general and administrative costs, are capitalized until the acquisition is completed, or the acquisition is abandoned and the costs are written off.

Depreciation on buildings is provided on a straight-line basis over the useful lives of the properties to a maximum of 60 years. Depreciation is determined with reference to each rental property's carried value, remaining estimated useful life and residual value. Depreciation on buildings is recorded in depreciation and amortization expense.

Properties are reviewed for impairment whenever events or changes in circumstances indicate the carrying value may not be recoverable. For commercial properties, an impairment loss is recognized when a property's carrying value exceeds its undiscounted future net cash flow. The impairment is measured as the amount by which the carrying value exceeds the estimated fair value. Projections of future cash flow take into account the specific business plan for each property and management's best estimate of the most probable set of economic conditions anticipated to prevail in the market.

(ii) Commercial developments

Commercial developments consist of properties for which a major repositioning program is being conducted and properties that are under construction. These properties are recorded at cost, including predevelopment expenditures. The impairment is measured as the amount by which the carrying value exceeds the estimated fair value. For commercial developments, an impairment loss is recognized when a property's carrying value exceeds its undiscounted future net cash flow. Properties are reviewed for impairment whenever events or changes in circumstances indicate the carrying value may not be recoverable. Projections of future cash flow take into account the specific business plan for each property and management's best estimate of the most probable set of economic conditions anticipated to prevail in the market.

(iii) Discontinued operations

Commercial properties that qualify as "held for sale" pursuant to the criteria of CICA Handbook Section 3475, "Disposal of Long-Lived Assets and Discontinued Operations," are classified as discontinued operations. Such properties are recorded at the lower of carrying amount or fair value less estimated cost to sell and are not depreciated while classified as held for sale. The results of operations and balance sheet items related to any property that has been identified as a discontinued operation are reported separately if the Company will not have any significant continuing involvement in the operations of the property after the disposal transaction. Comparative amounts are also reclassified.

(d) Capitalized costs

Costs capitalized to commercial developments include all direct and directly attributable expenditures incurred in connection with the acquisition, to the extent that such costs are incremental to a specific acquisition, development, construction, and initial predetermined leasing period. Costs directly attributable to commercial developments include interest and salaries and benefits for employees directly associated with the development projects, such as architects, engineers, designers, and development project managers. Ancillary income relating specifically to such properties during the development period is treated as a reduction of capitalized costs.

(e) Leasing costs

Leasing costs include the following:

- Tenant improvements, in which lease agreements generally provide for payments by the landlord to the tenant in the form of tenant improvement allowances, are amounts paid by the Company pursuant to such lease provisions and are characterized as either the purchase of tenant improvements owned by the landlord or as tenant inducements. When the payment is determined to be for tenant improvements owned by the Company, then the improvements are accounted for as an addition to commercial property and depreciated over their estimated useful life. If the Company determines that it is not the owner of the tenant improvements, then the property subject to the lease is the unimproved space and any payments made to the tenant under the lease are treated as tenant inducements, which reduce revenue over the term of the lease; and
- Leasing fees, which are included in commercial properties. These fees are amortized on a straight-line basis over the term of the applicable lease to amortization expense.

(f) Intangible assets and liabilities

Intangible assets and liabilities include the value of above- and below-market in-place operating leases, lease-origination costs, tenant relationships, and above-market ground-lease obligations. Intangible assets and liabilities are stated at historic cost less accumulated amortization and impairment charges, if any.

The values of above- and below-market in-place operating leases are amortized on a straight-line basis to commercial properties revenue over the remaining term of the associated lease. Lease-origination costs are amortized on a straight-line basis to amortization expense over the remaining term of the applicable lease. The value of tenant relationships is amortized on a straight-line basis to amortization expense over the remaining term of the lease plus an estimated renewal term. In the event that a tenant vacates the leased space prior to the contractual termination of the lease or does not exercise their renewal and no rental payments are being made on the lease, any unamortized balance of the related intangible will be expensed.

(g) Revenue recognition**i) Commercial properties**

The Company has retained substantially all of the risks and benefits of ownership of its rental properties and therefore accounts for leases with its tenants as operating leases. Revenue recognition under a lease begins when the tenant takes possession of, or controls, the physical use of the property subject to the lease. Generally, this occurs on the lease commencement date or, where the Company is required to make additions to the property in the form of tenant improvements, upon substantial completion of those improvements. The total amount of contractual rent to be received from operating leases is recognized on a straight-line basis over the term of the lease; a straight-line or free-rent receivable, as applicable, is recorded for the difference between the rental revenue recorded and the contractual amount received. Rental revenue also includes percentage participating rents and recoveries of operating expenses, including property and capital taxes. Percentage participating rents are recognized when tenants' specified sales targets have been met. Operating expense recoveries are recognized in the period that recoverable costs are chargeable to tenants.

Revenue and expenses related to commercial developments are recognized in income when the development is substantially complete. This is also the point at which the property is reclassified from commercial developments to commercial properties. The Company considers a commercial development to be substantially complete upon the earlier of attaining an occupancy that results in break-even income after debt servicing or the expiration of a reasonable maximum period of time, but no later than one year after completion of major construction. Prior to substantial completion, revenues and expenses related to commercial developments are capitalized to the property.

ii) Performance and management fee revenue

The Company is entitled to management fees and performance fees on the management of properties for third parties. The Company recognizes performance fees in revenue when the amount receivable from its fund partners is determinable at the end of a contractually specified term.

(h) Income taxes

The Company accounts for income taxes under the liability method. Under this method, future income tax assets and liabilities are calculated based on (i) the temporary differences between the carrying values and the tax bases of assets and liabilities, and (ii) unused income tax losses, measured using substantively enacted income tax rates and laws that are expected to apply in the future as temporary differences reverse and income tax losses are used.

(i) Reporting currency and foreign currency translation

The consolidated financial statements have been presented in Canadian dollars as the Company's principal investments and cash flow are influenced primarily by the Canadian dollar. Assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the rate in effect at the balance sheet date. Revenues and expenses are translated at the weighted-average rate in effect for the period presented.

(j) Use of estimates

The preparation of financial statements, in conformity with Canadian generally accepted accounting principles, requires estimates and assumptions that affect the carried amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from estimates. Significant estimates are required in the determination of future cash flows and probabilities in assessing net recoverable amounts and fair values, the allocation of the purchase prices to components of commercial properties and businesses acquired, the useful lives for depreciation and amortization, the Company's ability to utilize tax losses and the rates at which those losses will be realized, the selection of discount and capitalization rates used to fair value assets, the effectiveness of hedges, and the fair value of financial instruments for disclosure purposes.

(k) Financial instruments and derivatives

Financial assets and financial liabilities, including derivatives, are measured at fair value on initial recognition in the consolidated balance sheets. Measurement subsequent to initial recognition depends on the financial instruments classification which is determined by the purpose for which the instrument was acquired or issued, the instrument's characteristics and the Company's designation of the instrument. Financial instruments are classified as held for trading, available for sale, held to maturity, loans and receivables, or other financial liabilities.

Financial assets and financial liabilities classified as trading are measured at fair value with changes in those fair values recognized in net income. Financial assets classified as held to maturity, loans and receivables, and other financial liabilities are measured at amortized cost, net of associated transaction costs, using the effective-interest method. The Company includes transaction costs associated with the origination of interest-bearing financial assets and liabilities as a component of the initial carrying amount of the instrument. Available-for-sale financial assets are measured at fair value with changes therein, together with foreign currency translation gains and losses, recognized in Other Comprehensive Income ("OCI"). The Company does not hold any financial instruments that are classified as available for sale or held to maturity for the year ended December 31, 2008.

Derivative instruments are recorded on the consolidated balance sheet at fair value, including those derivatives that are embedded in financial or non-financial contracts and that are not closely related to the host contract. Changes in the fair value of derivative instruments are recognized in net income with the exception of derivatives designated in an effective cash flow.

The Company presents financial assets on the consolidated balance sheets in tenant and other receivables; loans receivable; and cash and cash equivalents. Non-derivative financial assets presented in tenant and other receivables and loans receivable are classified as loans and receivables and are carried at amortized cost. Derivatives and embedded derivatives with a favorable fair value to the Company are presented in tenant and other receivables and loans receivable at fair value. Cash and cash equivalents are classified as trading and measured at fair value at the balance sheet date.

The Company presents financial liabilities in commercial and development property debt, accounts payable and other liabilities. All of the Company's non-derivative financial liabilities are classified as other liabilities and measured at amortized cost following the effective-interest method. Derivatives and embedded derivatives with an unfavorable fair value to the Company are presented in accounts payable and other liabilities at fair value.

The Company utilizes derivative financial instruments primarily to manage financial risks, including interest rate, commodity, and foreign-exchange risks. The use of derivative contracts is governed by documented risk-management policies and approved limits.

The Company applies hedge accounting to derivative financial instruments in cash flow hedging relationships. Hedge accounting is discontinued prospectively when the hedge relationship is terminated or no longer qualifies as a hedge, or when the hedged or hedging item is sold or terminated.

In cash flow hedging relationships, the effective portion of the change in the fair value of the hedging derivative is recognized in OCI while the ineffective portion is recognized in net income. When hedge accounting is discontinued, the amounts previously recognized in Accumulated Other Comprehensive Income ("AOCI") are reclassified to net income in the periods when the variability in the cash flows of the hedged item affects net income. Gains and losses on derivatives are reclassified immediately to net income when the hedged item is sold or terminated.

Derivative financial instruments that are not designated as hedges are carried at estimated fair values, and gains and losses arising from changes in fair values are recognized in net income in the period the changes occur. Realized and unrealized gains and losses on other derivatives not designated as hedges are recorded in interest and other income.

(I) Cash and cash equivalents

Cash and cash equivalents include cash and short-term investments with original maturities of three months or less.

NOTE 2: CHANGES IN ACCOUNTING POLICIES

Capital Disclosures

Effective January 1, 2008, the Company adopted the CICA issued Handbook Section 1535, "Capital Disclosures." Section 1535 requires the disclosure of (i) an entity's objectives, policies and process for managing capital; (ii) quantitative data about an entity's managed capital; (iii) whether an entity has complied with capital requirements; and (iv) if an entity has not complied with such capital requirements, the consequences of such non-compliance. The Company adopted the requirements of Section 1535 on January 1, 2008 and the required disclosures are included in Note 19 of these consolidated financial statements.

Financial Instruments – Disclosures and Presentation

Effective January 1, 2008, the Company adopted the two CICA issued Handbook Sections 3862, "Financial Instruments – Disclosures," and Section 3863, "Financial Instruments – Presentation." These standards replace Section 3861, "Financial Instruments – Disclosure and Presentation" and require additional disclosure of the nature and extent of risks arising from financial instruments and how the entity manages those risks. Disclosures required by Section 3862 have been made in the notes to these consolidated financial statements. The adoption of Section 3863 did not have any impact on the Company's consolidated financial statements.

NOTE 3: FUTURE ACCOUNTING POLICY CHANGES

Goodwill and Intangible Assets

In February 2008, the CICA issued a new accounting standard, Section 3064, "Goodwill and Intangible Assets." Section 3064 replaces Sections 3062, "Goodwill and Other Intangible Assets" and 3450, "Research and Development Costs." The section establishes standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. Standards concerning goodwill are unchanged from those included in the previous Section 3062. Various changes have been made to other sections of the CICA Handbook for consistency purposes. As a result of related amendments to Section 100, "Financial Statement Concepts," any expenses deferred pursuant to previously existing "matching" concepts and which do not otherwise meet the definition of an asset, will no longer be eligible for capitalization as an asset. The new section and related amendments will be applicable to financial statements relating to fiscal years beginning on or after October 1, 2008. Accordingly, the Company will adopt the new standards for fiscal year beginning January 1, 2009. Consistent with transition provisions in Section 3064, the Company will adopt the standards retrospectively with restatement. The Company is still assessing the impact of the adoption of this standard but expects that the effect of adopting Section 3064 and its related amendments will be a reduction in commercial properties with a corresponding charge against retained earnings.

NOTE 4: COMMERCIAL PROPERTIES

A breakdown of commercial properties is as follows:

(Millions)	2008	2007
Commercial properties		
Land	\$ 153.5	\$ 153.5
Building and improvements	1,400.1	1,412.2
Total commercial properties	1,553.6	1,565.7
Less: Accumulated depreciation	(214.9)	(214.1)
Total	\$ 1,338.7	\$ 1,351.6

(a) At December 31, 2008, commercial properties with a net book value of approximately \$539.7 million (compared to \$547.8 million on December 31, 2007), are situated on land held under leases or other agreements largely expiring after the year 2099. Minimum rental payments in respect of ground leases related to commercial real estate properties are approximately \$4.9 million annually for the next five years and \$24.5 million in total on an undiscounted basis. Amounts payable under ground leases ranging from 3 to 883 years are included in the above amounts.

(b) Depreciation and amortization on commercial properties for the year ended December 31, 2008 was \$53.7 million (compared to \$58.5 million in 2007).

(c) During the year ended December 31, 2008, approximately \$42.3 million of fully amortized building and improvements and the corresponding accumulated amortization were written off.

(d) The following amounts represent the Company's proportionate interest in incorporated and unincorporated joint ventures and partnerships, reflected in the Company's commercial and development properties:

(Millions)	2008	2007
Assets	\$ 1,104.5	\$ 1,100.0
Liabilities	773.6	680.6
Operating revenues	233.8	235.9
Operating expenses	104.0	102.8
Net income ⁽¹⁾	64.1	137.9
Cash flows from operating activities	81.7	97.4
Cash flows provided by (used in) financing activities	108.6	(90.1)
Cash flows (used in) provided by investing activities	(41.0)	154.6

⁽¹⁾ Income taxes are not reflected here as they are recorded at the corporate level

NOTE 5: COMMERCIAL DEVELOPMENTS

Commercial developments includes commercial land, developable land, and construction costs. At December 31, 2008, commercial developments had a book value of \$689.1 million (compared to \$452.5 million on December 31, 2007). The Company capitalizes interest, development costs and property taxes and other to commercial developments. During 2008, the Company capitalized costs totaling \$238.4 million (compared to \$137.5 million in 2007). Included in this amount is \$195.4 million of construction and related costs (compared to \$112.3 million in 2007), \$27.3 million of interest capitalized (compared to \$23.3 million in 2007) and \$15.7 million of property taxes and other (compared to \$1.9 million in 2007) related to commercial developments for the year ended December 31, 2008.

NOTE 6: LOANS RECEIVABLE

The components of loans receivable are as follows:

(Millions)	2008	2007
Loans receivable	\$ 150.5	\$ 282.9
Accrued interest	0.1	0.6
Total	\$ 150.6	\$ 283.5

At December 31, 2008, loans receivable includes the following:

- \$25.5 million (December 31, 2007 – \$20.8 million) loan repayable in U.S. dollars of US\$20.9 million (December 31, 2007 – US\$20.9 million). For the year ended December 31, 2008, interest income related to this loan of \$2.6 million was recorded, compared to \$2.5 million in 2007. This loan receivable bears interest at 11.2% per annum and matures in 2011. As of December 31, 2008, accrued interest income of \$nil (December 31, 2007 - \$nil) was recorded.
- \$125.0 million (December 31, 2007 - \$220.3 million) on-demand deposit with the Company's parent, Brookfield Properties Corporation ("BPC"). This deposit bears interest at 100 basis points over short-term government paper rates. In two separate transactions during the second quarter of 2008, BPC repaid the original \$220.3 million on-demand deposit that was issued in December 2007 and a new \$125.0 million on-demand deposit was placed with BPC. During the year ended December 31, 2008, interest income of \$7.0 million was recorded on these deposits (compared to \$0.2 million in 2007). Subsequent to year-end, the full amount of the on-demand deposit was repaid to the Company (see note 21 of the consolidated financial statements).

During 2008, the Company received payment of the full outstanding balance of the loan receivable from a joint venture for \$41.8 million. During the year ended December 31, 2008, interest income of \$0.7 million was recorded on these deposits (compared to \$1.6 million in 2007).

For the year ended December 31, 2008, interest income of \$10.3 million (compared to \$6.4 million in 2007), was recorded on loans receivable, of which \$0.1 million was accrued for on December 31, 2008 (compared to \$0.6 million on December 31, 2007).

At December 31, 2008, the Company had \$125.0 million (December 31, 2007 – \$262.1 million) of its loan receivable balances subject to variable interest rates. The effect of a 100-basis-point decrease in interest rates on interest income relating to our variable-rate loan receivable, all else being equal, is a decrease in interest income, net of taxes of \$0.9 million on an annual basis or approximately \$0.03 per share. The analysis does not reflect the impact a changing interest rate environment could have on our overall performance, and as a result, it does not reflect the actions management may take in such an environment.

Credit risk related to loans receivables arises from the possibility that borrowers may default on the repayment of their loans. Because the Company invests in loans and mortgages from time to time, credit risks arise in the event that borrowers default on the repayment of their loans and mortgages to the Company.

Market risk is the risk of loss that may arise from changes in market factors such as interest rates, foreign exchange rates, and commodity prices. The Company utilizes derivative financial instruments primarily to manage these risks. Hedge accounting is applied where the derivative is designated as a hedge of a specific exposure and there is reasonable assurance the hedge will be effective. Realized and unrealized gains and losses on derivative financial instruments designated as hedges of financial risks are included in income as an offset to the hedged item in the period the underlying asset, liability, or anticipated transaction to which they relate arise.

At December 31, 2008, the Company had foreign-exchange contracts to sell a notional amount of US\$21.0 million (December 31, 2007 – US\$21.0 million) at a weighted-average exchange rate of US\$1.00 = C\$1.22, maturing in March 2009, which have not been designated as hedges for financial reporting purposes. The aggregate fair value of these contracts at December 31, 2008, was \$nil and is reflected in loans receivable in the consolidated balance sheets and in loans and investment income in the consolidated statements of income and comprehensive income. The Company believes that it is not exposed to significant currency risk as a result of having the foreign-exchange contracts.

The fair value of the loan receivable repayable in U.S. dollars is determined by reference to current market rates for receivables with similar terms. At December 31, 2008, the fair value of the loan receivable repayable in U.S. dollars was \$24.3 million (compared to \$21.2 million on December 31, 2007).

NOTE 7: INTANGIBLE ASSETS

The components of intangible assets are as follows:

(Millions)	2008	2007
Intangible assets		
Lease-origination costs	\$ 40.4	\$ 57.1
Tenant relationships	6.5	7.6
Above-market in-place operating leases	2.0	2.3
	48.9	67.0
Less accumulated amortization		
Lease-origination costs	(16.2)	(24.6)
Tenant relationships	(1.6)	(1.4)
Above-market in-place operating leases	(0.8)	(0.8)
Total	\$ 30.3	\$ 40.2

Amortization on intangible assets for the year ended December 31, 2008 was \$9.9 million (compared to \$11.4 million on December 31, 2007). Approximately \$18.1 million of fully amortized intangible assets, and the corresponding accumulated amortization were written off during the year ended December 31, 2008.

NOTE 8: TENANT RECEIVABLES AND OTHER ASSETS

The components of tenant receivables and other assets are as follows:

(Millions)	2008	2007
Tenant and other receivables	\$ 44.4	\$ 32.0
Straight-line rent receivable	18.3	16.5
Prepaid expenses and other assets	18.5	16.4
Restricted cash	1.1	1.1
Total	\$ 82.3	\$ 66.0

These receivables are generally short-term receivables of a trade nature. The carrying value of tenant and other receivables approximates fair value due to their short-term nature.

During the year ended December 31, 2008, the Company recorded \$0.6 million (compared to \$0.6 million on December 31, 2007) as a reserve against uncollectible tenant receivables.

As of December 31, 2008, approximately \$0.8 million of the Company's balance of accounts receivables is over 90 days due (compared to approximately \$0.5 million on December 31, 2007).

Credit risk related to tenant and other receivables, including straight-line rent receivable, arises from the possibility that tenants may be unable to fulfill their lease commitments. The Company mitigates this risk by ensuring that its tenant mix is diversified and by limiting its exposure to any one tenant. Currently no one tenant represents more than 12.8% of total leasable area and 8.3% of tenant receivables. This risk is further mitigated by signing long-term leases with tenants who have investment-grade credit ratings. Over the next few years, the Company has a highly manageable lease expiry profile of 3.6% in 2009, 6.9% in 2010, 7.5% in 2011 and 8.3% in 2012.

Cash and deposits are considered restricted when they are subject to contingent rights of third parties. As of December 31, 2008, restricted cash was \$1.1 million (compared to \$1.1 million on December 31, 2007).

NOTE 9: CASH AND CASH EQUIVALENTS

For the year ended December 31, 2008, interest income of \$2.5 million was recorded on cash and cash equivalents (compared to \$3.3 million in 2007). Cash and cash equivalents invested in overnight term deposits earned an average interest rate of 3.03% during the year.

NOTE 10: DISCONTINUED OPERATIONS

During the second quarter of 2008, the Company sold its 25% interest in 4342 Queen Street in Niagara Falls, which was classified as a discontinued operation in the fourth quarter of 2007, resulting in a gain of \$nil.

Net income, including gains on disposition, attributable to discontinued operations was \$nil as of December 31, 2008 (compared to \$80.0 million in 2007). The decrease in net income is the result of the sale of the following properties in 2007, which includes Atrium on Bay, 18 King Street, 2 St. Clair West and 40 St. Clair West in Toronto, 2200 Walkey Road and 2204 Walkley Road in Ottawa and Gulf Canada Square in Calgary. There were no properties classified as held for sale as of December 31, 2008.

The components of assets and liabilities related to discontinued operations are as follows:

(Millions)	2008	2007
Assets related to discontinued operations		
Commercial properties	\$ —	\$ 3.2
Intangible assets	—	0.1
Tenant receivables and other assets	—	0.9
Total assets related to discontinued operations	—	4.2
Liabilities related to discontinued operations		
Accounts payable and other liabilities	—	3.0
Total liabilities related to discontinued operations	\$ —	\$ 3.0

The following table summarizes the income and gains from discontinued operations:

(Millions, except per-share amounts)	2008	2007
Revenue	\$ 0.1	\$ 18.2
Operating expenses	(0.1)	(6.2)
Interest expense	—	12.0
Depreciation and amortization	—	(2.2)
Income from discontinued operations prior to gains and taxes	—	9.8
Gains on sale of discontinued operations	—	(3.2)
Income taxes related to discontinued operations	—	6.6
Net income from discontinued operations	\$ —	\$ 80.0
Net income from discontinued operations – per share	\$ —	\$ 2.81

NOTE 11: COMMERCIAL AND DEVELOPMENT PROPERTY DEBT

Commercial property mortgages are secured by individual properties generally without recourse to the Company. Approximately 82% of the Company's commercial and development property debt is due after 2009.

Commercial and development property debt maturities and scheduled principal repayments for the next five years and thereafter are as follows:

(Millions, except interest rate data)	Scheduled Amortization	Maturities	Total	Weighted-Average Interest Rate (%) at Dec. 31, 2008
2009	12.6	217.6	230.2	5.9%
2010	14.1	312.5	326.6	3.5%
2011	14.4	97.3	111.7	7.5%
2012	10.3	195.6	205.9	5.9%
2013	5.7	276.8	282.5	6.3%
2014 and thereafter	4.9	93.5	98.4	5.9%
Total	\$ 62.0	\$ 1,193.3	\$ 1,255.3	5.6%

The weighted-average interest rate at December 31, 2008, was 5.6% (compared to 6.9% on December 31, 2007). Approximately 63% of the Company's outstanding debt at December 31, 2008, is fixed-rate debt (compared to 64% on December 31, 2007). The details and terms for new financing transactions for 2008 are as follows:

(Millions)			New Proceeds	Repayments	Net Proceeds	Interest	Mortgage	
			at Ownership	at Ownership	Generated	Rate (%)	details	Maturity
105 Adelaide Street West	Q1	Refinancing	\$ 23.1	\$ (23.1)	\$ —	5.32%	Nonrecourse	February 2013
2 Queen Street East	Q2	New financing	28.6	—	28.6	5.64%	Nonrecourse	December 2017
Altius Centre	Q2	New financing	20.5	—	20.5	5.64%	Nonrecourse	December 2017
Canadian Western Bank Place	Q2	New financing	14.5	—	14.5	5.64%	Nonrecourse	December 2017
Royal Centre	Q2	New financing	122.0	(132.0)	(10.0)	4.96%	Nonrecourse	May 2012
Hudson's Bay Centre	Q2	New financing	110.0	(100.0)	10.0	5.20%	Limited recourse ⁽¹⁾⁽²⁾	May 2013
20-22 Front Street	Q3	New financing	20.0	(6.3)	13.7	6.24%	Nonrecourse	October 2020
Petro Canada Centre	Q4	Bridge financing	150.0	(121.5)	28.5	5.01% ⁽³⁾	Nonrecourse	October 2009

⁽¹⁾ Limited recourse up to \$15.0 million

⁽²⁾ Two-year extension option that extends the maturity to May 2015 is available to the Company provided that certain debt service and loan-to-value thresholds are met

⁽³⁾ Interest rate is based on Bankers Acceptance plus 225 bps and will increase by 25 bps if the facility remains outstanding at March 13, 2009

Included in commercial and development property debt at December 31, 2008 are \$7.3 million of net deferred financing costs (compared to \$8.8 million on December 31, 2007) and \$4.1 million of premiums related to mortgages assumed upon acquisition (compared \$6.3 million on December 31, 2007).

For the year ended December 31, 2008, interest expense of \$66.8 million (compared to \$53.3 million in 2007) was recorded on commercial and development property debt, of which \$27.3 million (compared to \$23.3 million in 2007) was capitalized to commercial developments.

Approximately 37% of the Company's outstanding commercial and development property debt at December 31, 2008 is floating-rate debt (compared to 36% on December 31, 2007). The effect of a 100-basis-point increase in interest rates on interest expense relating to floating rate debt, all else being equal, is an increase in interest expense, net of taxes of \$3.1 million on an annual basis or approximately \$0.11 per share.

The fair value of commercial and development property debt is determined by discounting contractual principal and interest payments at estimated current market interest rates for the instrument. Current market interest rates are determined with reference to current benchmark rates for a similar term and current credit spreads for debt with similar terms and risk. As of December 31, 2008, the fair value of commercial and development property debt exceeds the principal loan value of these obligations by \$30.3 million (compared to an excess of \$29.8 million on December 31, 2007).

Interest rate risk arises when the fair value or future cash flows of commercial and development property debt fluctuate because of changes in market interest rates. Financing risk arises when lenders will not refinance maturing debt on terms and conditions acceptable to the Company, or on any terms at all. The Company attempts to stagger the maturities of its borrowings, as well as obtain fixed-rate debt as the means of managing interest rate risk. The Company has an ongoing obligation to access debt markets to refinance maturing debt as it comes due. The Company's strategy to stagger its borrowing maturities also helps to mitigate the Company's exposure to excessive amounts of debt maturing in any one year. The Company has debt totaling \$217.6 million maturing in 2009, representing 17.3% of the Company's total debt outstanding at December 31, 2008, of which \$2.2 million matures in the second quarter and the remainder matures in the fourth quarter of 2009.

NOTE 12: INTANGIBLE LIABILITIES

Included in intangible liabilities are below-market tenant leases and above-market ground leases assumed on acquisitions, net of related accumulated amortization. The components of intangible liabilities are as follows:

(Millions)	2008	2007
Intangible liabilities		
Below-market in-place operating leases	\$ 56.8	\$ 68.3
Above-market ground lease obligations	45.8	45.8
	102.6	114.1
Less accumulated amortization		
Below-market in-place operating leases	(22.6)	(23.6)
Above-market ground lease obligations	(8.1)	(5.5)
Total	\$ 71.9	\$ 85.0

Amortization on intangible liabilities for the year ended December 31, 2008, was \$13.2 million (compared to \$14.1 million on December 31, 2007). Approximately \$11.5 million of fully amortized intangible liabilities and the corresponding accumulated amortization were written off during the year ended December 31, 2008.

NOTE 13: ACCOUNTS PAYABLE AND OTHER LIABILITIES

The components of the Company's accounts payable and other liabilities are as follows:

(Millions)	2008	2007
Accounts payable and accrued liabilities	\$ 101.3	\$ 95.3
Accrued interest	4.3	5.1
Total	\$ 105.6	\$ 100.4

These payables are generally short-term payables of a trade nature. The carrying value of accounts payable and other liabilities approximates fair value due to their short-term nature.

NOTE 14: INCOME TAXES

Future income tax liabilities consist of the following:

(Millions)	2008	2007
Future income tax assets related to operating and capital losses	\$ (7.6)	\$ (16.6)
Future income tax liabilities related to differences between tax and book basis	66.2	57.9
Total	\$ 58.6	\$ 41.3

At December 31, 2008, the Company had net operating loss carryforwards of \$34.7 million (compared to \$54.7 million on December 31, 2007), which are available to reduce taxable income in future years. The benefit of the tax losses, net of a valuation allowance, has been reflected in the future income tax assets.

The components of income tax expense are as follows:

Continuing operations

(Millions)	2008	2007
Income tax expense at the Canadian federal and provincial income tax rate of 32.0% (2007 – 34.0%)	\$ 32.1	\$ 29.6
Increase (decrease) in income tax expense due to the following:		
De-recognition of tax asset (tax assets previously not recognized)	1.6	(4.7)
Change in statutory tax rates	—	2.9
Other	1.1	0.4
Total	\$ 34.8	\$ 28.2

Discontinued operations

(Millions)	2008	2007
Income tax expense at the Canadian federal and provincial income tax rate of 32.0% (2007 – 34.0%)	\$ —	\$ 33.3
Decrease in income tax expense due to the following:		
Nontaxable portion capital gain	—	(15.5)
Total	—	17.8
Total income tax expense	\$ 34.8	\$ 46.0

The major components of income tax expense include the following:

(Millions)	2008	2007
Current tax expense	\$ 16.5	\$ 12.0
Future tax expense	18.3	34.0
Total	\$ 34.8	\$ 46.0

NOTE 15: SHAREHOLDERS' EQUITY

The components of shareholders' equity are as follows:

(Millions)	2008	2007
Preferred shares	\$ 381.7	\$ 381.7
Common shares	78.4	78.8
Retained earnings	401.0	580.0
AOCI	—	—
Total	\$ 861.1	\$ 1,040.5

Authorized share capital consists of 300,000 senior preferred shares, unlimited priority preferred shares, unlimited preferred shares issuable in series, unlimited common shares, and unlimited non-voting equity shares. No senior preferred shares or priority preferred shares are issued and outstanding.

(a) Preferred shares

Details of the preferred shares issued by the Company are as follows:

(Millions, except share information)	Shares Outstanding	Cumulative Dividend Rate	2008	2007
Series G	1,805,489	70% of bank prime	\$ 45.1	\$ 45.1
Series J	3,816,527	70% of bank prime	95.4	95.4
Series K	300	30-day BA + 0.4%	150.0	150.0
Series M	2,847,711	70% of bank prime	71.2	71.2
Series N	800,000	30-day BA + 0.4%	20.0	20.0
Total			\$ 381.7	\$ 381.7

The redemption terms of the preferred shares issued by the Company are as follows:

(i) Series G preferred shareholders are entitled to cumulative dividends at an annual rate equal to 70% of the average bank prime rate. The Company may, at its option, redeem the shares at a price of \$25 per share plus arrears on any accrued and unpaid dividends.

(ii) Series J and M preferred shareholders are entitled to cumulative dividends at an annual rate equal to 70% of the average bank prime rate for the previous quarter. The Company may, at its option, redeem the shares at a price of \$25 per share plus arrears on any accrued and unpaid dividends.

(iii) Series K preferred shareholders are entitled to cumulative dividends at the 30-day bankers' acceptance rate plus 0.4%. The Company may, at its option, redeem the shares at a price of \$500,000 per share plus an amount equal to all accrued and unpaid dividends.

(iv) Series N preferred shareholders are entitled to cumulative dividends at the 30-day bankers' acceptance rate plus 0.4%. The Company may, at its option, redeem the shares at \$25 per share plus arrears on any accrued and unpaid dividends.

During 2008, preferred dividends of \$14.3 million were paid, compared to \$18.2 million in 2007.

(b) Common equity

Total common shares issued and outstanding at December 31, 2008, totaled 28.3 million (compared to 28.5 million on December 31, 2007) shares, which included 21.7 million non-voting equity shares (compared to 21.7 million on December 31, 2007).

During 2008, the Company repurchased 147,900 common shares (compared to 32,900 common shares in 2007) for \$7.0 million (compared to \$2.2 million in 2007). The book value of the common shares was \$0.4 million (compared to \$0.1 million in 2007); as a result, the \$6.6 million paid in excess of the book value was recorded as a reduction to retained earnings (compared to \$2.1 million in 2007).

The Company paid common share dividends of \$223.6 million for year ended December 31, 2008 (compared to \$17.1 million in 2007). A special common share dividend was paid during the second quarter of 2008 for \$206.5 million or \$7.25 per common share.

(c) Earnings per share

Net income available to common shareholders and weighted-average common shares outstanding are calculated as follows:

(Millions)	2008	2007
Net income from continuing operations	\$ 65.5	\$ 58.8
Net income	65.5	138.8
Preferred share dividends	(14.3)	(18.2)
Net income from continuing operations available to common shareholders	\$ 51.2	\$ 40.6
Net income available to common shareholders	51.2	120.6
Weighted-average shares outstanding	28.4	28.5
Net income from continuing operations per common share	\$ 1.80	\$ 1.42
Net income per common share	\$ 1.80	\$ 4.23

There were no dilutive instruments outstanding.

NOTE 16: GUARANTEES, CONTINGENCIES, AND OTHER

(a) In the normal course of operations, the Company and its consolidated subsidiaries execute agreements that provide for indemnification and guarantees to third parties in transactions such as business dispositions, business acquisitions, lease-up of development properties, sales of assets, sales of services, securitization agreements, and underwriting and agency agreements.

(b) As of December 31, 2008, the Company has commitments totaling \$93.3 million to third parties for the development projects of Bay Adelaide Centre, Toronto and Bankers Court, Calgary.

(c) The Company has previously entered into fixed gas-purchase contracts with a third-party gas supplier, which covers the period November 1, 2008 to October 31, 2009. As of December 31, 2008, the remaining commitment for the Company to purchase gas for its facilities was \$2.9 million.

(d) The Company currently has guaranteed up to \$60.0 million of a \$420.0 million credit facility related to construction financing for the Bay Adelaide Centre.

(e) The Company currently has limited recourse for up to \$15.0 million related to the Hudson's Bay Centre debt.

(f) The Company and its operating subsidiaries are contingently liable with respect to litigation and claims that arise from time to time in the normal course of business. The outcome of litigation and claims currently being pursued against the Company is not determinable. In the opinion of management, any liability that may arise from such contingencies would not have a materially adverse effect on the consolidated financial statements of the Company.

(g) The Company has insurance covering certain acts of terrorism for up to \$1.0 billion of damage and resulting business interruption costs. The Company continues to seek additional coverage equal to the full replacement cost of its assets; however, until this type of coverage becomes commercially available on an economically reasonable basis, any damage or business interruption costs as a result of uninsured acts of terrorism could result in a material cost to the Company. The Company believes it is in compliance with all of its loan covenants, despite not being able to acquire terrorism coverage for the full replacement cost of all the Company's properties.

NOTE 17: SEGMENTED INFORMATION

The Company has only one business segment: the ownership, development, and management of commercial properties.

NOTE 18: RELATED-PARTY TRANSACTIONS

In the normal course of operations, the Company enters into various transactions on market terms with related parties. These transactions have been measured at exchange value and are recognized in the consolidated financial statements.

The Company has entered into two service-support agreements with Brookfield Properties Ltd. ("BPL"), a subsidiary of BPC (one agreement dated October 21, 2005, relating to the former O&Y properties and the other dated January 1, 2006, in relation to the other properties owned by the Company as of such date). The purpose of the agreements is to provide the services of certain personnel and consultants as well as such facilities of BPL as are necessary to help the Company provide the services and facilities required of it pursuant to property-management services to which it is a party. The fees paid to BPL are on a cost-recovery basis and totaled \$13.0 million during 2008 (compared to \$11.4 million in 2007). The service-support agreements also permit the Company to charge costs and expenses payable by the Company, which are attributable to BPL on a cost-recovery basis. Total costs charged to BPL during 2008 totaled \$0.8 million (compared to \$0.6 million in 2007).

The Company has certain arrangements with an affiliate of Brookfield Asset Management Inc. ("BAM"), the ultimate parent of the Company, and BPC to provide various information technology services and with BPC to provide various administrative services including accounts payable processing and accounts receivable collection. The costs for these services amounted to \$8.2 million for the year ended December 31, BPO Properties Ltd.

2008, and are charged to the Company on a cost recovery basis and replaced similar costs that were incurred directly by the Company in the prior year when these services were performed internally.

Included in loans receivable at December 31, 2008, is a \$125.0 million (compared to \$220.3 million on December 31, 2007) on-demand deposit placed with BPC. In two separate transactions during the second quarter of 2008, BPC repaid the original \$220.3 million on-demand deposit and a new \$125.0 million on-demand deposit was placed with BPC. For the year ended December 31, 2008, interest income of \$7.0 million was recorded on these deposits (compared to \$0.2 million in 2007).

Included in rental revenues during the year ended December 31, 2008, are amounts received from BAM, and its affiliates of \$0.4 million (compared to \$0.4 million in 2007). In addition, the Company has certain arrangements with BAM and its affiliates to acquire insurance in the normal course and at market rates or at cost. These fees are based on a percentage of the annual premiums paid.

NOTE 19: CAPITAL MANAGEMENT AND LIQUIDITY

The Company employs a broad range of financing strategies to facilitate growth and manage financial risk.

The Company continually strives to reduce its weighted-average cost of capital and improve common shareholders' equity returns through value enhancement initiatives and the consistent monitoring of the balance between debt and equity financing. As of December 31, 2008, the Company's weighted-average cost of capital, assuming a 12.0% return on equity, was 6.2%. The following schedule details the components of the Company's capital as of December 31, 2008 and the related costs thereof:

(Millions, except cost of capital data)	Cost of Capital ⁽¹⁾		Underlying Value ⁽²⁾	
	Dec. 31, 2008	Dec. 31, 2007	Dec. 31, 2008	Dec. 31, 2007
Liabilities				
Commercial and development property debt	5.6%	6.9%	\$ 1,255.3	\$ 965.5
Shareholders' equity				
Preferred shares	3.8%	4.8%	381.7	381.7
Common shares ⁽³⁾	12.0%	12.0%	679.2	1,718.6
Total⁽⁴⁾	6.2%	8.8%	\$ 2,316.2	\$ 3,065.8

⁽¹⁾ As a percentage of average book value

⁽²⁾ Underlying value of liabilities represents the cost to retire on maturity. Underlying value of common equity is based on the closing stock price of the Company's common shares at December 31, 2008. Underlying value of preferred equity is based on the book value of preferred shares

⁽³⁾ Determined on a market-value basis and assumes a 12% return on equity

⁽⁴⁾ In calculating the weighted-average cost of capital, the cost of debt has been tax-effected

At December 31, 2008, a 1.0% decrease in return on equity results in a weighted-average cost of capital decrease of 0.3% (compared to 0.6% on December 31, 2007).

Commercial and development property debt

The Company's commercial property debt is primarily fixed-rate and nonrecourse to the Company, thereby reducing the overall financial risk to the Company. These financings are typically structured on a loan-to-appraised value basis of between 55% and 65% when the market permits. In addition, in certain circumstances where a building is leased almost exclusively to a high-credit quality tenant, a higher loan-to-value financing, based on the tenant's credit quality, is put in place at rates commensurate with the cost of funds for the tenant. This reduces equity requirements to finance commercial property, and enhances equity returns. The Company currently has a level of indebtedness of 53% of gross book value. This level of indebtedness is considered by the Company to be within its target and, based on this, the Company believes that all debts will be financed or refinanced as they come due in the foreseeable future.

The Company is subject to certain covenants on its borrowings including debt service coverage and loan to value thresholds. As of December 31, 2008, the Company was in compliance with all of its covenants.

The Company's strategy is to satisfy its liquidity needs using cash on hand, cash flows generated from operating activities and provided by financing activities, as well as proceeds from asset sales. Rental revenue, recoveries from tenants, interest and other income, available cash balances, draws on credit facilities and refinancings, including upward refinancings, of maturing indebtedness are the Company's principal sources of capital used to pay operating expenses, dividends, debt service and recurring capital and leasing costs in its commercial property portfolio. The Company finances its development operations and on-going working capital requirements with development debt and accounts payable. Another source of cash flow includes third-party fees generated by the Company's asset management, leasing and development businesses. Consequently, the Company's plans to meet its short-term liquidity needs with revenue along with proceeds from financing activities.

The principal liquidity needs for periods beyond the next twelve months are for development costs, potential property acquisitions, scheduled debt maturities and non-recurring capital expenditures. The Company's strategy to meet these needs with one or more of the following:

- cash flow from operations;
- construction loans;
- investment in new funds;
- proceeds from sales of assets; and
- credit facilities and refinancing opportunities

The Company attempts to match the maturity of its commercial and development property debt portfolio with the average lease terms of its properties. At December 31, 2008, the average term to maturity of the Company's commercial and development property debt portfolio was four years and the Company's average lease term of its properties was approximately seven years. Excluding development debt, the Company's average term to maturity was also four years. The Company will continue to make efforts to match the maturity of the commercial property debt portfolio with the average lease term of its properties.

The following table presents the contractual payments of the Company's financial debt:

(Millions)	Payments Due By Period			
	Total	1 - 3 Years	4 - 5 Years	After 5 Years
Commercial and development property debt ⁽¹⁾	\$ 1,255.3	\$ 668.5	\$ 488.4	\$ 98.4

⁽¹⁾Net of transaction costs

NOTE 20: OTHER INFORMATION

Supplemental cash flow information

(Millions)	2008	2007
Dispositions of real estate	\$ 3.3	\$ 256.0
Mortgage repaid upon disposition	—	(74.6)
Net dispositions	\$ 3.3	\$ 181.4
Cash taxes paid ⁽¹⁾	\$ 18.0	\$ 0.1
Cash interest paid	\$ 69.9	\$ 62.3

⁽¹⁾Included in cash taxes paid is \$14.0 million reimbursed to BPC for taxes paid to the tax authorities on its behalf

NOTE 21: SUBSEQUENT EVENTS

Subsequent to the year ended December 31, 2008, the Company received the full balance of the loan receivable outstanding from BPC in the amount of \$125.0 million.

Selected Financial Information

December 31 (Millions, except for share information)	2008	2007	2006	2005	2004
Financial results					
Commercial property net operating income ⁽¹⁾	\$ 195.5	\$ 199.7	\$ 197.9	\$ 121.8	\$ 113.2
Funds from operations ⁽²⁾	154.0	159.3	155.0	104.4	102.2
Net income	65.5	138.8	72.7	68.2	63.0
Total assets	2,352.5	2,235.7	2,098.6	2,026.3	1,562.4
Shareholders' equity	861.1	1,040.5	939.0	899.4	861.0
Per diluted common share					
Common shares outstanding	28.3	28.5	28.5	28.5	28.5
Funds from operations and gains	\$ 4.92	\$ 8.15	\$ 5.43	\$ 3.25	\$ 3.20
Funds from operations excluding gains	4.92	4.95	4.88	3.25	2.99
Net income	1.80	4.23	1.99	1.98	1.83
Dividends paid ⁽³⁾	0.60	0.60	0.60	0.60	0.60
Shareholders' equity – book value	30.43	36.51	32.95	31.56	30.21
Common share price at year end	24.00	60.30	69.92	39.70	39.00
Operating data					
Number of commercial properties	27	36	43	50	17
Rentable area (millions of sq. ft.)	23.8	24.0	27.1	27.2	14.1
Effective interest (millions of sq. ft.)	13.3	13.5	14.4	12.8	7.8
Average occupancy (%) ⁽⁴⁾	98.7	98.4	97.2	96.1	94.8

⁽¹⁾ Includes net operating income from discontinued operations

⁽²⁾ Includes funds from operations from discontinued operations

⁽³⁾ Excludes the special common share dividend of \$7.25 per share in 2008 and \$15.00 per share in 2004

⁽⁴⁾ The 2004 occupancy numbers have been restated to include Hudson's Bay Centre, which was transferred to commercial properties in the first quarter of 2005

Board of Directors

Richard B. Clark
Chairman of the Board
Chief Executive Officer
Brookfield Properties Corporation

Thomas F. Farley
President and Chief Executive Officer
BPO Properties Ltd.

The Hon. William G. Davis, P.C., C.C., Q.C.
Counsel, Torys LLP

Robert J. McGavin
Corporate Director

Michael F.B. Nesbitt
Chairman, Montrose Mortgage Corporation Ltd.

Officers

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President and Chief Executive Officer

T. Jan Sucharda
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Vice President, Investor Relations and Communications

Ricky Tang
Vice President and Controller

Elliott Feintuch
Associate Counsel

Brett M. Fox
Assistant Secretary

Michelle Campbell
Assistant Secretary

BPO Properties Corporate Information

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Stock Exchange Listing

Stock Symbol	Exchange	Record Date	Payment Date	
Common shares	BPP	TSX	First day of March, June, September and December	Last business day of March, June, September and December
Series G	BPP.PR.G	TSX	Last business day of January, April, July and October	Fourteenth day of February, May, August and November
Series J	BPP.PR.J	TSX	Last business day of January, April, July and October	Fourteenth day of February, May, August and November
Series K	Not listed	TSX	First business day preceding payment date	The day after the third Wednesday of every month
Series M	BPP.PR.M	TSX	Last business day of January, April, July and October	Fourteenth day of February, May, August and November
Series N	Not listed	TSX	Six business days preceding payment date	The day after the third Wednesday of every month

Shareholder Information

BPO Properties welcomes inquiries from shareholders, analysts, media representatives and other interested parties. Questions relating to investor relations or media inquiries can be directed to Melissa Coley, Vice President, Investor Relations at 416.359.8593 or via e-mail at mcoley@bpoproperties.com. Inquiries regarding financial results should be directed to Bryan Davis, Senior Vice President and Chief Financial Officer at 416.956.5170 or via e-mail at bdavis@bpoproperties.com.

Shareholder questions relating to dividends, address changes and share certificates should be directed to the company's Transfer Agent, CIBC Mellon Trust, as listed above.

Annual General Meeting

The Annual General Meeting of shareholders will be held in Toronto, Ontario, at the Hockey Hall of Fame, Brookfield Place, 181 Bay Street, May 4, 2009 at 1:30 p.m. Shareholders may also participate in the meeting by webcast through BPO Properties' Web site at www.bpoproperties.com.

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