

# **Madison Pacific Properties Inc.**

Consolidated Financial Statements  
For the Years Ended August 31, 2019 and 2018

(expressed in thousands of Canadian dollars)



## *Independent auditor's report*

To the Shareholders of Madison Pacific Properties Inc.

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### *Our opinion*

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of Madison Pacific Properties Inc. and its subsidiaries (together, the Company) as at August 31, 2019 and 2018, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards (IFRS).

#### **What we have audited**

The Company's consolidated financial statements comprise:

- the consolidated balance sheets as at August 31, 2019 and 2018;
- the consolidated statements of changes in equity for the years then ended;
- the consolidated statements of income and comprehensive income for the years then ended;
- the consolidated statements of cash flows for the years then ended; and
- the notes to the consolidated financial statements, which include a summary of significant accounting policies.

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### *Basis for opinion*

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

#### **Independence**

We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Canada. We have fulfilled our other ethical responsibilities in accordance with these requirements.

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*PricewaterhouseCoopers LLP*  
*PricewaterhouseCoopers Place, 250 Howe Street, Suite 1400, Vancouver, British Columbia, Canada V6C 3S7*  
*T: +1 604 806 7000, F: +1 604 806 7806*



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### *Other information*

Management is responsible for the other information. The other information comprises the Management's Discussion and Analysis and Annual Information Form.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

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### *Responsibilities of management and those charged with governance for the consolidated financial statements*

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRS, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

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### *Auditor's responsibilities for the audit of the consolidated financial statements*

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.



As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Company to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.



We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

The engagement partner on the audit resulting in this independent auditor's report is John Paul Pressey.

**(signed) PricewaterhouseCoopers LLP**

Chartered Professional Accountants

Vancouver, British Columbia  
November 26, 2019

# Madison Pacific Properties Inc.

## Consolidated Balance Sheets

As at August 31, 2019 and 2018

(expressed in thousands of Canadian dollars)

	2019 \$	2018 \$
<b>Assets</b>		
<b>Non-current assets</b>		
Investment properties (note 5)	498,456	464,285
Other non-current assets (note 6)	70,300	59,215
	<u>568,756</u>	<u>523,500</u>
<b>Current assets</b>		
Cash and cash equivalents	56,955	46,207
Amounts receivable and other current assets (note 7)	3,157	4,699
Income taxes receivable (note 15)	262	261
	<u>60,374</u>	<u>51,167</u>
<b>Total assets</b>	<u>629,130</u>	<u>574,667</u>
<b>Liabilities</b>		
<b>Non-current liabilities</b>		
Debt on investment properties (note 8)	148,921	173,264
Deferred income tax liabilities (note 15)	37,036	31,584
	<u>185,957</u>	<u>204,848</u>
<b>Current liabilities</b>		
Current portion of debt on investment properties (note 8)	81,429	36,946
Accounts payable and accrued liabilities (note 9)	9,082	9,644
	<u>90,511</u>	<u>46,590</u>
<b>Total liabilities</b>	<u>276,468</u>	<u>251,438</u>
<b>Equity</b>		
<b>Equity attributable to shareholders of the Company</b>		
Share capital (note 11)	67,472	67,472
Contributed surplus	1,105	1,105
Retained earnings	272,482	243,882
	<u>341,059</u>	<u>312,459</u>
<b>Non-controlling interests</b>	<u>11,603</u>	<u>10,770</u>
<b>Total equity</b>	<u>352,662</u>	<u>323,229</u>
<b>Total liabilities and equity</b>	<u>629,130</u>	<u>574,667</u>

Approved by the Board of Directors

“Sam Grippo” Director

“Marvin Haasen” Director

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

**Madison Pacific Properties Inc.**  
**Consolidated Statements of Changes in Equity**  
**For the Years Ended August 31, 2019 and 2018**

(expressed in thousands of Canadian dollars)

	Attributable to shareholders of the Company			Total \$	Non- controlling interests \$	Total equity \$
	Share capital \$	Contributed surplus \$	Retained earnings \$			
<b>Balance – August 31, 2017</b>	67,472	1,093	208,051	276,616	9,143	285,759
Share-based compensation	-	12	-	12	-	12
Net income and comprehensive income	-	-	41,981	41,981	2,016	43,997
Dividends (note 12)	-	-	(6,150)	(6,150)	-	(6,150)
Distributions to non-controlling interests	-	-	-	-	(389)	(389)
<b>Balance – August 31, 2018</b>	67,472	1,105	243,882	312,459	10,770	323,229
Net income and comprehensive income	-	-	34,750	34,750	1,488	36,238
Dividends (note 12)	-	-	(6,150)	(6,150)	-	(6,150)
Distributions to non-controlling interests	-	-	-	-	(638)	(638)
Purchase of subsidiary shares from non-controlling interest	-	-	-	-	(17)	(17)
<b>Balance – August 31, 2019</b>	<b>67,472</b>	<b>1,105</b>	<b>272,482</b>	<b>341,059</b>	<b>11,603</b>	<b>352,662</b>

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

# Madison Pacific Properties Inc.

## Consolidated Statements of Income and Comprehensive Income

For the Years Ended August 31, 2019 and 2018

(expressed in thousands of Canadian dollars, except per share data)

	2019	2018
	\$	\$
Property revenues (note 13 and 17)	31,117	31,228
Property operating expenses (note 14 and 17)	8,530	8,380
	<u>22,587</u>	<u>22,848</u>
General and administrative expenses (note 14 and 17)	3,198	2,911
	<u>19,389</u>	<u>19,937</u>
Net gain on fair value adjustment on investment properties (note 5)	29,404	37,450
Equity earnings of associate and joint ventures (note 6)	1,238	1,530
	<u>50,031</u>	<u>58,917</u>
Interest income	1,201	478
Interest expense	7,942	7,465
(Losses) gains on fair value adjustment on interest rate swaps (note 8)	<u>(1,071)</u>	<u>712</u>
Income before income taxes	42,219	52,642
Income taxes (note 15)	<u>5,981</u>	<u>8,645</u>
Net income and comprehensive income	<u>36,238</u>	<u>43,997</u>
<b>Net income and comprehensive income attributable to:</b>		
Shareholders of the Company	34,750	41,981
Non-controlling interests	1,488	2,016
	<u>36,238</u>	<u>43,997</u>
<b>Income per share (note 16)</b>		
Basic	\$0.59	\$0.72
Diluted	<u>\$0.59</u>	<u>\$0.72</u>

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

**Madison Pacific Properties Inc.**  
**Consolidated Statements of Cash Flows**  
For the Years Ended August 31, 2019 and 2018

(expressed in thousands of Canadian dollars)

<b>Cash flows from (used in):</b>	<b>2019</b>	<b>2018</b>
	<b>\$</b>	<b>\$</b>
<b>Operating activities</b>		
Net income	36,238	43,997
Items not affecting cash		
Net gain on fair value adjustment on investment properties	(29,404)	(37,450)
Amortization	1,097	1,012
Equity earnings of associate and joint ventures	(1,238)	(1,530)
Share-based compensation	-	12
Losses (gains) on fair value adjustment on interest rate swaps	1,071	(712)
Recognition of rental revenue on a straight-line basis	36	(110)
Deferred income taxes	5,452	8,497
	<u>13,252</u>	<u>13,716</u>
Increase in amounts receivable and other assets	(3,767)	(1,338)
Increase in income taxes receivable	(1)	(46)
Increase in accounts payable and accrued liabilities	350	723
	<u>9,834</u>	<u>13,055</u>
<b>Investing activities</b>		
Additions to investment properties and property development costs	(5,195)	(3,160)
Other investment property expenditures	(1,443)	(701)
Net proceeds from disposition of investment properties	-	24,676
Investments in joint ventures net of cash drawn (note 6(b))	(5,701)	(1,352)
Repayment of loans receivable	92	52
	<u>(12,247)</u>	<u>19,515</u>
<b>Financing activities</b>		
Net proceeds from debt on investment properties (note 8)	51,892	40,907
Repayment of debt on investment properties (note 8)	(31,926)	(31,968)
Distributions to non-controlling interests	(638)	(389)
Purchase of subsidiary shares from non-controlling interest	(17)	-
Dividends paid	(6,150)	(6,150)
	<u>13,161</u>	<u>2,400</u>
Increase in cash and cash equivalents	10,748	34,970
Cash and cash equivalents - beginning of year	46,207	11,237
Cash and cash equivalents - end of year	<u>56,955</u>	<u>46,207</u>
<b>Supplemental cash flow information</b>		
Interest received	1,200	478
Interest paid	7,711	7,407

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

# Madison Pacific Properties Inc.

## Notes to the Consolidated Financial Statements

For the Years Ended August 31, 2019 and 2018

(expressed in thousands of Canadian dollars, except number of shares and per share amounts)

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### 1. General information

Madison Pacific Properties Inc. (the “Company”) owns, develops and operates office, industrial, and commercial real estate properties located in British Columbia, Alberta, and Ontario. The Company also has investments in joint ventures that intend to develop residential properties. The Company is incorporated and domiciled in Canada. The head office of the Company is located at 389 West 6<sup>th</sup> Avenue, Vancouver, British Columbia, V5Y 1L1, and its registered office is located at 25<sup>th</sup> Floor, Toronto-Dominion Bank Tower, 700 West Georgia Street, Vancouver, British Columbia, V7Y 1B3.

### 2. Summary of significant accounting policies and critical accounting estimates

#### a. Basis of presentation

The Company prepares its consolidated financial statements in accordance with International Financial Reporting Standards (“IFRS”), as issued by the International Accounting Standards Board (“IASB”). IFRS comprises IFRS, International Accounting Standards (“IAS”), and interpretations issued by the IFRS Interpretations Committee (“IFRIC”) and the former Standing Interpretations Committee (“SIC”).

These consolidated financial statements were approved by the Board of Directors on November 21, 2019.

#### b. Basis of measurement

These consolidated financial statements have been prepared on the historical cost basis except for investment properties and financial derivatives, which are measured at fair value.

#### c. New accounting standards

During the year ended August 31, 2019, the Company implemented new accounting policies to comply with the new accounting standards: IFRS 15, *Revenue from Contracts with Customers* (“IFRS 15”) and IFRS 9, *Financial Instruments* (“IFRS 9”). The nature and impact of the new standards are described in note 3 and the related accounting policies are described in note 2(h), 2(i) and 2(j).

#### d. Principles of consolidation

##### *Subsidiaries*

These consolidated financial statements incorporate the assets and liabilities of all entities controlled by the Company and the results of all controlled entities. Controlled entities are those entities over which the Company has i) the power to govern the financial and operating policies, ii) the right to receive benefits from that entity, and iii) the ability to use its operating decisions to alter the benefits received. These criteria are met by having a shareholding of more than one-half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Company controls another entity. In addition, for consolidation purposes, factors may exist where an entity may consolidate without having more than 50% of the voting power through ownership or agreements, or in the circumstances of enhanced minority rights, as a consequence of *de facto* control. *De facto* control is control without the legal right to exercise unilateral control, and involves decision-making abilities that are

# Madison Pacific Properties Inc.

## Notes to the Consolidated Financial Statements

For the Years Ended August 31, 2019 and 2018

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(expressed in thousands of Canadian dollars, except number of shares and per share amounts)

not shared with others and the ability to give direction with respect to the operating and financial policies of the entity concerned. Where control of a subsidiary ceases during a financial year, its results are included up to the point in the year when control ceases. Where control of an entity is acquired during a financial year, its results are included in the consolidated statement of income and comprehensive income from the date on which control commences.

The Company's subsidiaries are Metro Vancouver Properties Corp. ("Metro"), MP Western Properties Inc., 1073774 Properties Inc., 3530639 Canada Inc., 801325 B.C. Ltd., the MPW Properties Partnership, Madison Silverdale Developments Corp., Madison Developments 2800 Barnet Ltd., the MT Properties Limited Partnership, and MT Management Inc. The Company holds a 100% interest in MP Western Properties Inc., 1073774 Properties Inc., 3530639 Canada Inc., Madison Silverdale Developments Corp. and a 99.8% interest in Metro which holds a 100% interest in the MPW Properties Partnership, 801325 B.C. Ltd., and Madison Developments 2800 Barnet Ltd., a 60.9% interest in the MT Properties Limited Partnership, and a 75% interest in MT Management Inc.

All inter-company balances, transactions, and unrealized profits resulting from inter-company transactions are eliminated.

### *Non-controlling interests*

Non-controlling interests represent equity interests in subsidiaries owned by outside parties. The share of net assets of subsidiaries attributable to non-controlling interests is presented as a component of equity. Changes in the parent company's ownership interest in subsidiaries that do not result in a loss of control are accounted for as equity transactions.

### *Joint arrangements*

The Company classifies its interests in joint arrangements as either a joint venture or a joint operation. A joint arrangement is a contractual arrangement whereby the Company and other parties undertake an economic activity that is subject to joint control. A joint arrangement is classified as a joint venture when the parties to the joint arrangement have rights over the net assets of the joint arrangement, whereas a joint arrangement is classified as a joint operation when the arrangement provides rights to assets and obligations for liabilities for the parties sharing joint control. Joint operations are accounted for using the proportionate consolidation method whereby the Company's share of assets, liabilities, income, expenses and cash flows of jointly controlled operations are combined with the equivalent items in the results on a line-by-line basis. Joint ventures are accounted for using the equity method as follows:

- Investments are initially recognized at cost.
- Investments in joint ventures include goodwill and intangible assets identified on acquisition, net of any accumulated impairment loss.
- The Company's share of its joint ventures' post-acquisition profits or losses is recognized in the consolidated statement of income and comprehensive income.
- Dividends and distributions receivable from joint ventures reduce the carrying amount of the investment.
- The Company's liability with respect to its joint ventures is limited to its net investment where it has no obligation to fund any subsequent losses should they arise. There is no obligation beyond the initial investment.

# Madison Pacific Properties Inc.

## Notes to the Consolidated Financial Statements

### For the Years Ended August 31, 2019 and 2018

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(expressed in thousands of Canadian dollars, except number of shares and per share amounts)

- Joint ventures are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

#### *Associates*

Associates are entities over which the Company has significant influence but not control. Investments in associates are accounted for using the equity method as follows:

- Investments are initially recognized at cost.
- Investments in associates include goodwill and intangible assets identified on acquisition, net of any accumulated impairment loss.
- The Company's share of its associates' post-acquisition profits or losses is recognized in the consolidated statement of income and comprehensive income.
- Dividends and distributions receivable from associates reduce the carrying amount of the investment.
- The Company's liability with respect to its associates is limited to its net investment where it has no obligation to fund any subsequent losses should they arise. There is no obligation beyond the initial investment.
- Associates are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

#### **e. Investment properties**

Investment properties are held to earn rental income, for capital appreciation, or for both. Investment properties also include properties being constructed or developed for future use, including existing investment properties which undergo redevelopment for continued future use. Property interests held under operating leases are not treated as investment properties.

An investment property is initially measured at cost, which includes the cost of the acquisition, property transfer taxes, due diligence costs, and standard closing costs.

After initial recognition, investment properties are carried at fair value. Fair value represents the estimated amount at which the properties could be exchanged between a knowledgeable and willing buyer and seller in an arm's length transaction at the date of valuation. Valuations are prepared by management based primarily on assumptions relating to cash flow from current leases, rental income from future leases in light of current market conditions, and capitalization rates. The capitalization rates used are generally based on ranges provided by external valuers. These assumptions are further compared against information obtained from independent industry experts. Adjustments are made to the fair values of the investment properties when changes in the underlying valuation assumptions occur. Changes in fair values are recognized in the consolidated statement of income and comprehensive income.

Fair value measurement on property under construction is only applied if the fair value is considered to be reliably measurable.

# **Madison Pacific Properties Inc.**

## **Notes to the Consolidated Financial Statements**

### **For the Years Ended August 31, 2019 and 2018**

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(expressed in thousands of Canadian dollars, except number of shares and per share amounts)

Subsequent expenditures are capitalized to the asset's carrying amount only when it is probable that the Company will receive future economic benefits associated with the expenditures and the fair value of the investment property exceeds its carrying amount plus subsequent expenditures. All other repair and maintenance costs are expensed when incurred.

For investment properties being constructed, developed or redeveloped for future use, all direct expenditures incurred in connection with the construction or development are capitalized during the development period. This period begins from the date that activities commence to prepare the property for its intended use and ends when such activities are substantially complete.

Depreciation is not taken on investment properties.

Investment properties are derecognized either when they have been disposed of or when the investment property is permanently withdrawn from use and no future economic benefit is expected from its disposal. Any gain or loss arising on the derecognition of an investment property is recognized as a net gain in the fair value adjustment on investment properties in the consolidated statement of income and comprehensive income in the period in which the investment property is derecognized.

Investment properties are classified as held for sale when the criteria in IFRS 5, *Non-current Assets Held for Sale and Discontinued Operations*, are met. The resulting sale is recognized when title passes to the purchaser, all or substantially all of the proceeds have been received or are receivable, and all material conditions of the sales agreement have been met.

#### **f. Leases**

The Company has retained substantially all of the risks and benefits of ownership of its revenue properties and therefore accounts for leases with its tenants as operating leases. Properties leased out under operating leases are included in investment properties in the consolidated balance sheet.

When a tenant lease provides for free rent periods and/or periodic increases in base rent over the lease term, the total amount of net rental revenue to be received from these leases is accounted for on a straight-line basis over the term of the applicable lease. Accordingly, an asset is recorded for the current difference between the straight-line rent recorded as rental revenue and the rent that is contractually due from the tenant. As the lease term progresses and the step-rate increase is received, the asset is drawn down. The asset is included in the carrying amount of the related investment property.

Tenant incentives comprise costs incurred to make leasehold improvements to tenants' space and are included in the carrying amount of the related investment property. Such incentives are recognized as a reduction of rental income on a straight-line basis over the term of the applicable lease.

Leasing commissions are fees paid in connection with negotiating lease contracts with lessees. Such fees are included in the carrying amount of the related investment property and are amortized on a straight-line basis over the term of the applicable lease.

# Madison Pacific Properties Inc.

## Notes to the Consolidated Financial Statements

For the Years Ended August 31, 2019 and 2018

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(expressed in thousands of Canadian dollars, except number of shares and per share amounts)

### **g. Cash and cash equivalents**

Cash and cash equivalents include cash on hand, deposits held with banks, and other short-term highly liquid investments with original maturities of three months or less.

### **h. Financial instruments**

Financial assets and liabilities are recognized when the Company becomes a party to the contractual provisions of the financial instrument. Financial assets are derecognized when the rights to receive cash flows from the assets have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership. Financial liabilities are derecognized when the obligation specified in the contract is discharged, cancelled or expires.

At initial recognition, the Company classifies its financial instruments in the following categories depending on the purpose for which the financial instruments were acquired:

- i. Financial assets and liabilities at fair value through profit or loss (“FVTPL”): A financial asset or liability is classified in this category if acquired principally for the purpose of selling or repurchasing in the short term. Derivatives, including interest rate swaps, are also included in this category unless they are designated as hedges.
- ii. Financial assets at fair value through other comprehensive income (“FVOCI”): A financial asset is classified in this category if the asset is held for both the collection of contractual cash flows, where those cash flows represent solely payments of principal and interest, and to sell the financial asset. The Company currently has no financial instruments classified as financial assets at FVOCI.

Financial assets at FVOCI are initially recognized at fair value plus transaction costs and are subsequently carried at fair value. Gains or losses arising from changes in fair value are recognized in other comprehensive income. These financial assets are classified as non-current, unless the financial asset matures within 12 months, or management expects to dispose of it within 12 months. When these financial assets are derecognized, the accumulated gains or losses are moved from accumulated other comprehensive income to the consolidated statement of income and comprehensive income.

- iii. Financials assets at amortized cost: The Company’s financial assets at amortized cost comprise loans receivable, cash and cash equivalents, and amounts receivable. Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest are measured at amortized cost. These financial assets are initially recognized at the amount expected to be received net of any transaction costs incurred, and less, when material, a discount to reduce the amount to fair value. Subsequently, these financial assets are measured at amortized cost using the effective interest method. At each reporting period, each financial asset measured at amortized cost is assessed for impairment. The expected credit loss impairment is based on the difference in cash flows the Company expects to receive and the contractual cash flows due in accordance with the contract, discounted at the asset’s original effective interest rate. Impairment losses are recognized in the consolidated statement of income and comprehensive income.

# **Madison Pacific Properties Inc.**

## Notes to the Consolidated Financial Statements

### For the Years Ended August 31, 2019 and 2018

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(expressed in thousands of Canadian dollars, except number of shares and per share amounts)

The current portions of loans receivable, cash and cash equivalents, and amounts receivable are included in current assets due to their short-term nature. The balance of loans receivable that is not current is included in non-current assets.

- iv. Financial liabilities at amortized cost: Financial liabilities at amortized cost include accounts payable and accrued liabilities, bank indebtedness drawn on the line of credit, and debt on investment properties. Accounts payable and accrued liabilities and bank indebtedness drawn on the line of credit are recognized at the amount required to be paid. Debt on investment properties is recognized initially at fair value, net of any transaction costs incurred, and subsequently at amortized cost using the effective interest method.

Financial liabilities are classified as current liabilities if payment is due within 12 months. Otherwise, they are presented as non-current liabilities.

#### **i. Derivative financial instruments**

The Company enters into interest rate swaps from time to time to manage interest rate risk. Interest rate swaps are financial derivatives and are classified as carried at FVTPL. The fair value of an interest rate swap is included in the consolidated balance sheet within accounts payable and accrued liabilities if the fair value of the interest rate swap results in an unrealized loss, and the fair value of an interest rate swap is included within other current assets if the fair value of the interest rate swap results in an unrealized gain. Gains and losses on re-measurement are included in the consolidated statement of income and comprehensive income (note 8).

#### **j. Revenue recognition**

Property revenues include rental revenue and property management revenue.

Rental revenue from operating leases is recognized on a straight-line basis over the applicable lease term. The cost of tenant incentives is recognized over the term of the applicable lease as a reduction in rental revenue.

Rental revenue includes the recovery of certain operating expenses and property taxes.

Unearned revenue represents deposits received in advance of rent being earned and property taxes recovered prior to their due date.

Property management revenue is recorded monthly as earned.

#### **k. Stock-based compensation**

The Company determines the fair value of stock-based awards at the date of grant using the Black-Scholes option pricing model and recognizes the fair value over the vesting period as stock-based compensation expense with a corresponding adjustment to contributed surplus (note 11(b)).

# **Madison Pacific Properties Inc.**

## **Notes to the Consolidated Financial Statements**

### **For the Years Ended August 31, 2019 and 2018**

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(expressed in thousands of Canadian dollars, except number of shares and per share amounts)

#### **l. Provisions**

Provisions for restructuring costs, warranties and legal claims, where applicable, are recognized in other liabilities when the Company has a present legal or constructive obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated. Provisions are measured at management's best estimate of the expenditure required to settle the obligation at the end of the reporting period and are discounted to present value where the effect is material.

#### **m. Income taxes**

The Company follows the asset and liability method of accounting for income taxes whereby deferred income tax assets and liabilities are recognized for differences between the bases of assets and liabilities used for financial statement and income tax purposes. Deferred income tax assets and liabilities are calculated using substantively enacted tax rates for the period in which the differences are expected to reverse. Deferred income tax assets are recognized only to the extent that management determines that it is more likely than not that the deferred income tax assets will be realized. Deferred income tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment or substantive enactment.

#### **n. Income per share**

Basic income per share is calculated by dividing the net income or loss for the year attributable to shareholders of the Company by the weighted average number of Class B voting common shares and Class C non-voting shares outstanding during the year.

Diluted income per share is calculated by adjusting the weighted average number of Class B voting common shares and Class C non-voting shares outstanding for dilutive instruments.

#### **o. Fair value**

Fair value measurements recognized in the consolidated balance sheet are categorized in accordance with the following levels:

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3: Inputs for the asset or liability that are not based on observable market data (unobservable inputs).

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

#### **p. Critical accounting estimates and judgements**

The preparation of consolidated financial statements requires management to use judgement in applying its accounting policies and to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period.

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Significant areas requiring the use of management judgements, estimates, and assumptions relate to:

i. Fair value of investment properties

After initial recognition, valuations of investment properties are prepared by management based primarily on assumptions relating to cash flows from current leases, rental income from future leases in light of current market conditions, and capitalization rates. The capitalization rates used are generally based on ranges provided by external valuers. These assumptions are further compared against information obtained from independent industry experts. Adjustments are made to the carrying values of the investment properties when changes in the underlying valuation assumptions occur.

ii. Income taxes

Management has estimated the income tax provision and deferred income tax balances in accordance with its interpretation of the various income tax laws and regulations. It is possible, due to the complexity inherent in estimating income taxes, that the tax provision and deferred income tax balances could change.

In accordance with IAS 12, *Income Taxes*, the Company has recognized income tax losses and undeducted expenditures as deferred income tax assets. At this time, management has estimated that there will be sufficient future taxable income to utilize the losses and expenditures.

The Company has unrecognized investment tax credits. At this time, management has estimated that the recoverability is still in doubt as the Company has not established when it will be in a taxable position.

Management uses judgement based on underlying facts and assumptions when determining whether a provision for a tax liability or derecognition of a deferred income tax asset is required for tax positions in dispute with tax authorities (note 15).

iii. Allocation of purchase price on investment property acquisitions

On the acquisition of an investment property, the Company is required to make an allocation for the building component of the property in order to calculate depreciation for income tax purposes.

iv. Stock-based compensation

The Company determines the fair value of the stock options and other stock awards at the date of grant using the Black-Scholes option pricing model.

v. Assets held for sale

The Company makes estimates and assumptions about the fair values and selling costs of assets held for sale in determining their carrying amounts. The classification of an investment property as an asset held for sale requires the use of judgement regarding whether the criteria are met for this classification as at the date of the consolidated financial statements.

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### 3. New accounting standards and amendments to standards

The Company has applied, for the first time, certain standards and amendments, which are effective for annual periods beginning on or after September 1, 2018. The nature and the impact of the new standards and amendments are described below:

#### **IFRS 15, *Revenue from Contracts with Customers***

Effective September 1, 2018, the Company adopted IFRS 15 using the modified retrospective basis with no restatement of comparative periods. IFRS 15 replaces IAS 18, *Revenue* (“IAS 18”), and establishes a five-step model to account for revenue arising from contracts with customers. Under IFRS 15, revenue is recognized at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. The standard requires entities to exercise judgement, taking into consideration all of the relevant facts and circumstances when applying each step of the model to contracts with customers. The standard also specifies the accounting for the incremental costs of obtaining a contract and the costs directly related to fulfilling a contract.

The Company’s assessment included a review of relevant contracts for the following key areas that are in scope of IFRS 15: common area maintenance recoveries and property management fees.

The Company has concluded that there is no material impact in revenue recognition for these revenue streams between the point of transfer of risks and rewards under IAS 18 and the point of transfer of control under IFRS 15. No transitional adjustment has been recorded as at September 1, 2018.

The Company has adopted each of the accounting policies noted below on September 1, 2018:

#### i. Rental revenue

Rental revenue comprises the majority of the Company’s revenue and is generated through operating leases, which create a legally enforceable right to use the underlying asset by the tenant and require the Company to provide other services. Base rent, property taxes and insurance recoveries are accounted for pursuant to IAS 17, *Leases* (“lease components”), and are therefore outside the scope of IFRS 15, while common area maintenance (“CAM”) recoveries (“non-lease components”) are within the scope of IFRS 15.

CAM services are integrated property management services provided to tenants in exchange for CAM recoveries and property management fees. CAM services are considered to be a single performance obligation delivered to tenants over time. The Company receives variable consideration for the CAM recoveries and recognizes this as revenue over the period those services are provided.

#### ii. Property management fees

The Company has interests in various investment properties through joint arrangements and partnerships. The Company provides property management services, and construction and development services to co-owners, and partners for which it earns market-based fees.

Property management services and construction and development services are each considered a single performance obligation for which fees are recognized as revenue over the periods those services are provided.

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Revenue is recognized at the agreed transaction price in each contract.

**IFRS 9, Financial Instruments**

Effective September 1, 2018, the Company adopted IFRS 9 using the modified retrospective basis with no restatement of comparative periods. IFRS 9 replaces IAS 39, *Financial Instruments: Recognition and Measurement* (“IAS 39”), and all previous versions of IFRS 9. The standard introduces new requirements for: (i) classification and measurement of financial assets and financial liabilities, (ii) impairment of financial assets and (iii) hedge accounting.

i. Classification and measurement

Under IFRS 9, financial assets are classified and measured on the basis of both the business model in which the assets are managed and the contractual cash flow characteristics of the asset. Financial assets after initial recognition are classified and measured based on three categories: (i) amortized cost, (ii) FVOCI with fair value gains or losses recycled to net income on de-recognition, or (iii) FVTPL. Financial liabilities are classified and measured on two categories: (i) amortized cost or (ii) FVTPL.

Financial assets and liabilities are recognized at fair value at initial recognition, adjusted in some cases for transaction costs (i.e. when financial assets and liabilities are carried at amortized cost). The exception is for trade receivables that do not contain a significant financing component, as defined by IFRS 15. These are measured at the transaction price. Financial assets are recorded at amortized cost when financial assets are held with the objective of collecting contractual cash flows and those cash flows represent solely payments of principal and interest and are not designated as FVTPL.

The following table compares the classification of financial instruments under IFRS 9 and IAS 39, and reconciles the IAS 39 and IFRS 9 carrying amounts as at September 1, 2018:

	Classification Category		Changes due to:			
	IAS 39	IFRS 9	IAS 39	Reclassification	Remeasurement	IFRS 9
<b>Financial Assets</b>						
Cash and cash equivalents	Held for trading	Amortized cost	\$ 46,207	\$ -	\$ -	\$ 46,207
Amounts receivable and other current financial assets	Loans and receivables	Amortized cost	447	-	-	447
Other non-current financial assets	Loans and receivables	Amortized cost	12,628	-	-	12,628
Interest rate swap assets	FVTPL	FVTPL	1,260	-	-	1,260
<b>Financial Liabilities</b>						
Debt on investment properties	Other liabilities	Amortized cost	\$ 210,210	\$ -	\$ -	\$ 210,210
Accounts payable and other liabilities	Other liabilities	Amortized cost	9,644	-	-	9,644

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The Company does not currently have any financial assets classified as FVOCI.

#### ii. Impairment of financial assets measured at amortized cost

IFRS 9 introduces a new single expected credit loss (“ECL”) impairment model for the Company’s financial assets measured at amortized cost. The ECL model results in an allowance for credit losses being recorded on financial assets regardless of whether there has been an actual loss event. ECLs are based on the difference in cash flows the Company expects to receive and the contractual cash flows due in accordance with the contract, discounted at the asset’s original effective interest rate.

At each reporting date, each financial asset measured at amortized cost is assessed for impairment under the ECL model.

The adoption of the ECL model did not have a material impact on the Company’s financial assets carried at amortized cost.

#### iii. Hedging

IFRS 9 introduces a new hedge accounting model that expands the scope of hedged items and risks eligible for hedge accounting and aligns hedge accounting more closely with risk management. The new model no longer specifies quantitative measures for effectiveness testing and does not permit hedge de-designation.

The Company uses fixed-for-floating interest rate swaps to manage interest rate risk. At the date of the initial application, none of the interest rate swaps were eligible to be treated as hedging relationships. As such, the adoption of the hedge accounting requirements of IFRS 9 had no material impact to the Company’s consolidated financial statements.

## 4. Accounting standards and interpretations issued but not effective

In January 2016, the IASB issued IFRS 16, *Leases* (“IFRS 16”). The new standard replaces IAS 17, *Leases*, and its associated interpretative guidance. IFRS 16 applies a control model to the identification of leases, distinguishing between a lease and a service contract on the basis of whether the customer controls the asset being leased. For those assets determined to meet the definition of a lease, IFRS 16 introduces significant changes to the accounting by lessees, introducing a single, on-balance sheet accounting model that is similar to current finance lease accounting, with limited exceptions for short-term leases or leases of low value assets. Lessor accounting remains similar to current accounting practice. The standard is effective for annual periods beginning on or after January 1, 2019. The Company has substantially completed its assessment of the effect of IFRS 16, and has determined that the new standard will not have a material effect on its consolidated financial statements.

In June 2017, the IASB issued IFRIC Interpretation 23, *Uncertainty over Income Tax Treatments* (“IFRIC 23”), to clarify the application of recognition and measurement requirements in IAS 12, *Income Taxes*, when there is uncertainty over income tax treatments. The interpretation is effective for annual periods beginning on or after January 1, 2019. The Company has substantially completed its assessment of the effect of IFRIC 23, and has determined that the new interpretation will not have a material effect on its consolidated financial statements.

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**5. Investment properties**

	<b>August 31, 2019</b>	<b>August 31, 2018</b>
	<b>\$</b>	<b>\$</b>
Balance at beginning of year	464,285	480,544
Other additions and property development costs	4,303	4,111
Dispositions (note 5(c))	-	(23,330)
Transfer to investment in joint ventures (note 6(b))	-	(32,174)
Recognition of rental revenue on a straight-line basis	(36)	110
Tenant improvements	1,254	349
Amortization of tenant improvements	(673)	(636)
Leasing commissions	169	214
Amortization of leasing commissions	(250)	(271)
Net gain on fair value adjustment	29,404	35,368
	<hr/>	<hr/>
Balance at end of year	498,456	464,285

**a. Valuations**

After initial recognition, valuations are prepared by management based primarily on assumptions relating to cash flows from current leases, rental income from future leases in light of current market conditions, and capitalization rates. The capitalization rates used are generally based on ranges provided by external valuers. These assumptions are further compared against information obtained from independent industry experts. Adjustments are made to the carrying values of the investment properties when changes in the underlying valuation assumptions occur.

The fair value of the Company's investment properties is considered to be at Level 3 in the fair value hierarchy (note 2(o)), as significant unobservable inputs are required to determine fair value.

**b. Investment property acquisitions**

For the years ended August 31, 2019 and August 31, 2018, the Company had no acquisitions of investment properties.

**c. Investment property dispositions**

For the year ended August 31, 2019, the Company had no dispositions of investment properties.

For the year ended August 31, 2018, the Company sold one industrial property and a 50% interest in a commercial property, both located in British Columbia, for net proceeds of \$24,676. Concurrent with the sale of a 50% interest in the commercial property, the Company entered into a 50/50 joint venture with a residential developer to rezone and redevelop the property for residential and commercial use. The Company's 50% interest retained in the investment property was transferred to the 2798 Barnet Development Limited Partnership (the "Barnet LP") and is accounted for as an investment in joint venture (note 6(b)).

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Rezoning and redevelopment of the property is subject to receipt of all necessary approvals, none of which are certain.

**d. Sensitivity**

The following table provides a sensitivity analysis for the weighted average capitalization rate applied at August 31, 2019, excluding properties under development:

<b>Capitalization rate increase (decrease)</b>	<b>Weighted average capitalization rate</b>	<b>Fair value of investment properties (at Company's ownership)</b>	<b>Fair value variance</b>	<b>% change</b>
		<b>\$</b>	<b>\$</b>	
(0.75%)	3.70%	614,868	116,412	23.4%
(0.50%)	4.00%	568,065	69,609	14.0%
(0.25%)	4.29%	530,437	31,981	6.4%
August 31	4.56%	498,456	-	-
0.25%	4.83%	470,605	(27,851)	(5.6%)
0.50%	5.10%	445,983	(52,473)	(10.5%)
0.75%	5.36%	423,990	(74,466)	(14.9%)

**6. Other non-current assets**

	<b>August 31, 2019</b>	<b>August 31, 2018</b>
	<b>\$</b>	<b>\$</b>
Deposits (note 15)	16,248	12,184
Investment in associate (note 6(a))	13,937	12,946
Investments in joint ventures (note 6(b))	39,474	33,526
Loans receivable and other	641	559
	<u>70,300</u>	<u>59,215</u>

Deposits include amounts paid for income reassessments in dispute (note 15).

**a. Investment in associate**

The investment in associate includes an equity investment in Grant Street Properties Inc. ("GSP"), a related private company that owns and manages commercial and industrial properties. The Company holds an ownership interest of 33.83% in GSP. This investment has been accounted for using the equity method and include equity earnings for the year ended August 31, 2019 of \$991 (year ended August 31, 2018 - \$1,530). The Company's share of assets, liabilities, revenue and other income, and expenses as at and for the year ended August 31, 2019 is \$20,030, \$6,211, \$1,625 and \$634, respectively (August 31, 2018 - \$18,283, \$5,456, \$2,345 and \$815, respectively).

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**b. Investments in joint ventures**

The investment in joint ventures includes equity investments in the Silverdale Hills Limited Partnership (the “Silverdale Hills LP”) and the Barnet LP (note 5(c)). During the year ended August 31, 2018, real estate properties previously presented as investment properties on the consolidated balance sheet, were transferred to investments in joint ventures on the consolidated balance sheet as a result of the transfer of the investment properties into development partnerships and related events and circumstances. These investments have been accounted for using the equity method and includes equity earnings for the year ended August 31, 2019 of \$247 (year ended August 31, 2018 – \$nil). The Company’s share of assets, liabilities, revenue and other income, and expenses as at and for the year ended August 31, 2019 is \$54,359, \$14,816, \$604 and \$357, respectively (August 31, 2018 - \$48,274, \$14,748, \$nil and \$nil, respectively).

In the year ended August 31, 2019, the Company made additional equity investments of \$5,701 in the Silverdale Hills LP. The additional equity was required to fund development costs and the acquisition of additional parcels of undeveloped residential land. In March 2018, the Barnet LP obtained a bank loan of \$29,250 for which the Company has provided a guarantee of \$14,625. The Barnet LP bank loan of \$29,250 is payable on demand and matures in 2020. During the year ended August 31, 2018, the Company drew \$14,030 of cash from the Barnet LP.

**7. Amounts receivable and other current assets**

	<b>August 31, 2019</b>	<b>August 31, 2018</b>
	\$	\$
Accounts receivable	342	284
Interest receivable and current portion of loans receivable	198	163
Prepaid expenses, deposits and other	2,428	2,992
Fair value assets on interest rate swaps (note 8)	189	1,260
	<u>3,157</u>	<u>4,699</u>

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**8. Debt on investment properties**

	<b>August 31, 2019</b>	<b>August 31, 2018</b>
	\$	\$
Balance at beginning of year	210,210	201,166
Net proceeds from debt issuances	51,892	40,907
Amortization of deferred financing costs	265	227
Amortization of acquisition date fair value adjustments on assumed debt	(91)	(122)
Repayment of debt	(31,926)	(31,968)
	<hr/>	<hr/>
Balance at end of year	230,350	210,210
Less: current portion	81,429	36,946
Non-current portion	<hr/> <u>148,921</u>	<hr/> <u>173,264</u>

Mortgage and construction loans are secured by charges against the related properties and corporate guarantees. Of the total mortgage and construction loans (before netting of deferred financing costs and fair value adjustments to assumed debt), \$230,920 (August 31, 2018 - \$206,023) bears interest at fixed rates ranging from 2.40% to 4.83% (August 31, 2018 - 2.40% to 5.39%) per annum and \$nil (August 31, 2018 - \$4,744) bears interest at variable rates (August 31, 2018 - bank prime rate plus 0.70% to 0.75%) per annum. The weighted average interest rate on fixed rate debt as at August 31, 2019 was 3.38% (August 31, 2018 - 3.40%).

See note 20 for minimum principal repayments.

**Interest rate swaps**

The Company has entered into interest rate swaps with Canadian chartered banks on five mortgages to fix the Company's interest rates on those mortgages. The swaps had notional amounts as at August 31, 2019 totalling \$65,478 (August 31, 2018 - \$64,654), fixed swap rates ranging from 2.92% to 3.90%, and maturity dates ranging from June 2020 to August 2024. The total notional amount of the interest rate swaps represented 28.4% as at August 31, 2019 (August 31, 2018 - 30.7%) of the total debt on investment properties (before netting of deferred financing costs and fair value adjustments on assumed debt). The Company anticipates holding the mortgages and interest rate swap contracts until maturity.

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The total fair value of the interest rate swaps and net unrealized (losses) gains on those contracts are as follows:

	Fair value assets		Net unrealized (losses) gains on interest rate swaps	
	2019 \$	2018 \$	2019 \$	2018 \$
Interest rate swaps	189	1,260	(1,071)	712

### 9. Accounts payable and accrued liabilities

	August 31, 2019 \$	August 31, 2018 \$
Trade payables	745	850
Dividends payable	3,075	3,075
Accrued interest payable	506	456
Other accrued liabilities	1,369	1,977
Tenant deposits	1,099	1,089
Unearned revenue	2,288	2,197
	<u>9,082</u>	<u>9,644</u>

### 10. Bank indebtedness

The Company has a line of credit of up to \$20,000 (August 31, 2018 - \$20,000) bearing interest at bank prime rate plus 1% or the Bankers Acceptance rate (August 31, 2018 - bank prime rate plus 1% or the Bankers Acceptance rate) with a Canadian chartered bank. As at August 31, 2019, \$nil (August 31, 2018 - \$nil) had been drawn against this line of credit. The amount available under this line of credit varies with the fair value of investment properties pledged, up to a maximum of \$20,000. Second mortgages against certain of the Company's investment properties, assignments of rents and insurance, as well as general security agreements creating floating charges over all of the Company's assets, have been provided as security. Amounts advanced under this line of credit are repayable on demand.

The line of credit agreement contains the following financial ratios that must be maintained, with which the Company was in compliance as at August 31, 2019:

- Not permit the debt service coverage ratio to be less than 1.25 to 1.00;
- Not permit the ratio of EBITDA to interest expense on all debt secured by the investment properties pledged to be less than 1.50 to 1.00;

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- Not permit the aggregate amount of all outstanding borrowings secured by the investment properties pledged to exceed 65% of their appraised values; and
- Not permit the tangible net worth of the Company to be at any time less than \$125,000.

**11. Share capital**

**a. Authorized and issued shares**

The authorized share capital of the Company consists of an unlimited number of Class A non-voting preferred shares without par value, an unlimited number of Class B voting common shares without par value (“Class B Shares”), and an unlimited number of Class C non-voting shares without par value (“Class C Shares”).

The following table summarizes the issued share capital as at August 31, 2019 and August 31, 2018:

	Class B Shares		Class C Shares		Total	
	Number	Amount \$	Number	Amount \$	Number	Amount \$
Balance – August 31, 2019 and August 31, 2018	7,255,500	7,720	51,315,089	59,752	58,570,589	67,472

No shares were issued or cancelled during the years ended August 31, 2019 and August 31, 2018.

**b. Share option plan**

The Company implemented a share option plan (the “Plan”) effective January 1, 2019. Under the Plan, the Company reserves Class B Shares equal to 2% of aggregate outstanding Class B Shares and Class C Shares for issuance upon the exercise of share options granted under the Plan. As at November 21, 2019, 1,171,411 Class B Shares are reserved for the issuance under the Plan. The Plan provides that share options may be issued only to executives, employees and outside directors of the Company or of any of its subsidiaries and that options granted to insiders (as defined by Toronto Stock Exchange rules) shall not exceed 10% of the outstanding Class B Shares.

The Plan and the terms of options granted, including the exercise price, the expiry time, the vesting period and other terms and conditions relating to such options, shall be administered by the Board of Directors or any committee to which such authority is delegated by the Board of Directors.

As at November 21, 2019, no share options had been granted under the Plan.

**12. Dividends**

On July 11, 2019, the Company declared a dividend of \$0.0525 per Class B Share and Class C Share payable on September 6, 2019.

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On January 14, 2019, the Company declared a dividend of \$0.0525 per Class B Share and Class C Share payable on February 22, 2019.

On July 12, 2018, the Company declared a dividend of \$0.0525 per Class B Share and Class C Share payable on September 6, 2018.

On January 11, 2018, the Company declared a dividend of \$0.0525 per Class B Share and Class C Share payable on February 22, 2018.

**13. Property revenues**

The following table summarizes the components of property revenues for the years ended:

	<b>August 31, 2019</b>	<b>August 31, 2018</b>
	\$	\$
Rental revenue	30,267	30,127
Property management revenue	850	1,101
	<u>31,117</u>	<u>31,228</u>

Future minimum rental commitments on non-cancellable tenant operating leases on a calendar year basis beginning January 1, 2020 are summarized in the following table:

Not later than 1 year	\$ 22,045
Later than 1 year and not later than 5 years	56,812
Later than 5 years	<u>17,278</u>
	<u>96,135</u>

**14. Property operating and general and administrative expenses**

For the year ended August 31, 2019, property operating expenses consisted of property taxes of \$5,599 (year ended August 31, 2018 - \$5,570) and other property-related expenses of \$2,931 (year ended August 31, 2018 - \$2,810). Property operating expenses that relate to investment property vacancies amounted to \$118 for the year ended August 31, 2019 (year ended August 31, 2018 - \$104).

For the year ended August 31, 2019, general and administrative expenses consisted of employee compensation and benefits of \$2,049 (year ended August 31, 2018 - \$1,723), professional fees of \$482 (year ended August 31, 2018 - \$660), and other administrative expenses of \$667 (year ended August 31, 2018 - \$528).

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The following table summarizes employee compensation and benefits expense for the years ended:

	<b>August 31, 2019</b>	<b>August 31, 2018</b>
	\$	\$
Salaries and short-term employee benefits	2,049	1,711
Stock-based compensation	-	12
	<u>2,049</u>	<u>1,723</u>

**15. Income taxes**

The following table provides the components of income taxes for years ended:

	<b>August 31, 2019</b>	<b>August 31, 2018</b>
	\$	\$
Current income tax expense	529	148
Deferred income tax expense	5,452	8,497
	<u>5,981</u>	<u>8,645</u>

Income taxes vary from the amount that would be expected if computed by applying the Canadian federal and provincial statutory income tax rates to the Company's income before income taxes as shown in the following table for years ended:

	<b>August 31, 2019</b>		<b>August 31, 2018</b>	
	\$		\$	
Income before income taxes	42,219		52,642	
	\$	%	\$	%
Expected income taxes at statutory rates	11,390	27.0	14,052	26.7
Adjustments				
Non-taxable portion of realized and unrealized capital gains	(4,398)	(10.4)	(4,751)	(9.0)
Recognition of previously unrecognized tax assets	(439)	(1.0)	(428)	(0.8)
Adjustment in respect of prior years	93	0.2	63	0.1
Effect of future income tax rate changes	(297)	(0.7)	721	1.4
Equity earnings in investee	(334)	(0.8)	(408)	(0.8)
Other items	(34)	(0.1)	(604)	(1.1)
Income taxes	<u>5,981</u>	<u>14.2</u>	<u>8,645</u>	<u>16.5</u>

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Deferred income tax liabilities (assets) comprise the following:

	<b>August 31, 2019</b>	<b>August 31, 2018</b>
	\$	\$
Benefit of non-capital losses carried forward	(1,244)	(861)
Benefit of capital losses carried forward	(942)	(942)
Undeducted expenditures	(1,896)	(3,497)
Deferred income tax assets not recognized	946	946
Investment properties	37,963	33,838
Tenant improvements and leasing costs	1,348	1,222
Straight-line rental revenue in excess of base rents	861	878
	<u>37,036</u>	<u>31,584</u>

The entire change in deferred income tax liabilities for the years ended August 31, 2019 and August 31, 2018 has been recognized in net income for those respective years.

As at August 31, 2019, the Company has approximately \$7,031 of scientific research and development expenditures available for unlimited carryforward and approximately \$4,134 of non-capital losses which begin to expire in 2037, which may be used to reduce future Canadian income taxes otherwise payable. The Company also has approximately \$6,807 of unrecognized federal investment tax credits which begin to expire in 2020, and can also be carried forward to be used to reduce future Canadian income taxes otherwise payable.

The federal investment tax credits and non-capital losses expire as follows:

	<b>Federal investment tax credits</b>	<b>Non-capital losses carried forward</b>
	\$	\$
2020	679	-
2021	625	-
2022	880	-
2023	1,048	-
2024	934	-
2025	865	-
2026	727	-
2027	689	-
2028	360	-
2037	-	417
2038	-	2,383
2039	-	1,334
	<u>6,807</u>	<u>4,134</u>

In addition, the Company has capital losses carried forward of approximately \$6,974 which may be used to reduce future taxable capital gains in Canada and do not expire.

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#### Contingencies

The Company and certain subsidiaries have received from the Canada Revenue Agency (“CRA”) and Alberta Tax and Revenue Administration (“ATRA”) tax notices of reassessment for various taxation years. The reassessments deny the application and usage of certain non-capital losses, capital losses, deductions and investment tax credits arising from prior years. In addition, the CRA and ATRA are disallowing unclaimed carryforward non-capital losses of \$417, carryforward capital losses of \$6,974, carryforward scientific research and development expenditures of \$12,991, and investment tax credits of \$7,409. As a result, additional taxes payable for the reassessed years, including interest, total \$33,601. The Company and its subsidiaries have filed notices of objection to the reassessments with the CRA and ATRA. To object to the reassessments, the Company and its subsidiaries were required to make deposits totalling \$16,248 for a portion of the taxes and interest the CRA and ATRA have claimed are owed. The Company and its subsidiaries have made these deposits and they are included in other non-current assets. Additional estimated interest accruing on the unpaid portion of the reassessments was approximately \$3,307 as at August 31, 2019.

The Company and its counsel believe that its filing positions for the Company and subsidiaries described above are appropriate and in accordance with the law. It intends to vigorously defend such positions as required. Accordingly, the Company has not recorded a liability in these consolidated financial statements for the reassessed taxes payable and related interest described above nor has it reduced the carrying value of deferred income tax assets recorded for unused carryforward amounts. If the Company is ultimately successful in defending its positions, deposits made plus applicable interest will be refunded to the Company. There is no assurance that the Company’s objections and appeals will be successful. If the CRA and ATRA are successful, the Company will be required to pay the balance of taxes reassessed plus applicable interest and derecognize deferred income tax assets related to the carryforward amounts.

#### 16. Income per share

	2019	2018
Net income attributable to shareholders of the Company	\$34,750	\$41,981
Weighted average number of shares outstanding	<u>58,570,589</u>	<u>58,570,589</u>
Basic and diluted income per share	<u>\$0.59</u>	<u>\$0.72</u>

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**17. Related party transactions**

The following transactions occurred in the normal course of operations and are measured at the exchange amounts, which are the amounts agreed upon by the related parties:

**a. Transactions and balances with related parties**

The Company has engaged the services of a landscaping and building services company owned by a related party. During the year ended August 31, 2019, landscaping, maintenance, and construction management services paid to this company totalled \$370 (year ended August 31, 2018 - \$341).

**b. Transactions and balances with affiliates**

During the year ended August 31, 2019, the Company engaged the services of an electrical contractor controlled by a shareholder of the Company for which it paid fees of \$39 (year ended August 31, 2018 - \$15).

During the year ended August 31, 2019, rental revenues of \$1,966 (year ended August 31, 2018 - \$1,941) were received from a shareholder of the Company and from tenants that are companies related to a shareholder of the Company.

During the year ended August 31, 2019, the Company paid management consulting fees of \$147 to a shareholder of the Company (year ended August 31, 2018 - \$390).

The Company has provided a limited guarantee of \$16,830 on the MT Properties Limited Partnership mortgage debt. During the year ended August 31, 2019, a guarantee fee of \$50 (year ended August 31, 2018 - \$50) was paid to the Company.

On December 11, 2017, the Silverdale Hills LP, of which the Company owns a 50% interest, acquired 459 acres of undeveloped residential lands in Mission, British Columbia for \$29,514. The vendor in the transaction is a party related to a significant shareholder of the Company.

**Key management personnel**

Key management personnel include the Company's directors and officers. The following table summarizes compensation awarded to key management personnel for the years ended:

	<b>August 31, 2019</b>	<b>August 31, 2018</b>
	<b>\$</b>	<b>\$</b>
Salaries and short-term employee benefits	1,641	1,358
Share-based compensation	-	12
	<u>1,641</u>	<u>1,370</u>

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### 18. Interest in joint operations

The Company's interests in investment properties owned through joint operations accounted for using proportionate consolidation are as follows:

Location	Description	Ownership interest as at	
		August 31, 2019	August 31, 2018
<b>Richmond, British Columbia</b>			
3351 Jacombs Road	Industrial	50%	50%
11388 No. 5 Road	Industrial	50%	50%
<b>Burnaby, British Columbia</b>			
7700 Riverfront Gate	Industrial	50%	50%
4750 Tillicum Street	Industrial	50%	50%
8155 North Fraser Way	Industrial	50%	50%
<b>Vancouver, British Columbia</b>			
1625 West 3 <sup>rd</sup> Avenue & 1855 Fir Street	Retail	50%	50%
148 West 6 <sup>th</sup> Avenue	Industrial	50%	50%
110-122 West 2 <sup>nd</sup> Avenue	Industrial	50%	50%

For these joint operations, the fair value of investment properties and carrying value of debt on those investment properties, at 50%, as at August 31, 2019 were \$52,276 and \$22,540, respectively (August 31, 2018 - \$46,660 and \$19,877, respectively). The Company is contingently liable for the obligations of its joint operations. Management believes that the assets of its joint operations are available and sufficient for the purpose of satisfying such obligations.

### 19. Segment information

The Company's chief executive officer and chief financial officer examined the Company's performance and have concluded that the Company has one reportable segment - that being the rental of office, industrial, and commercial real estate properties located in Canada. Although properties are in different Canadian regions and in different asset classes, they have reasonably similar returns and risks.

# Madison Pacific Properties Inc.

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### 20. Financial instruments

#### Financial assets and liabilities

The Company classifies its financial instruments as follows:

	<b>Financial assets at amortized cost</b>	<b>Financial liabilities at amortized cost</b>	<b>Financial assets at fair value through profit or loss</b>
<b>August 31, 2019</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>
Other non-current financial assets	16,599	-	-
Cash and cash equivalents	56,955	-	-
Amounts receivable and other current financial assets	540	-	-
Debt on investment properties	-	(230,350)	-
Accounts payable and accrued liabilities	-	(9,082)	-
Fair value assets on interest rate swaps	-	-	189
<b>Total</b>	<b>74,094</b>	<b>(239,432)</b>	<b>189</b>

	<b>Financial assets at amortized cost</b>	<b>Financial liabilities at amortized cost</b>	<b>Financial assets at fair value through profit or loss</b>
<b>August 31, 2018</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>
Other non-current financial assets	12,628	-	-
Cash and cash equivalents	46,207	-	-
Amounts receivable and other current financial assets	447	-	-
Debt on investment properties	-	(210,210)	-
Accounts payable and accrued liabilities	-	(9,644)	-
Fair value assets on interest rate swaps	-	-	1,260
<b>Total</b>	<b>59,282</b>	<b>(219,854)</b>	<b>1,260</b>

#### Credit risk

The Company's credit risk is limited to the carrying amount of its cash and cash equivalents, amounts receivable, and long-term receivables.

##### a. Cash and cash equivalents

Deposits of cash are made with major Canadian banks and only with counterparties meeting certain credit criteria.

# **Madison Pacific Properties Inc.**

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#### **b. Amounts receivable**

Credit risk arises from the possibility that tenants may experience financial difficulty and be unable to fulfill their lease commitments or repay loans advanced to assist them with leasehold improvements.

The Company follows a program of credit evaluations of tenants and limits the amount of credit extended when deemed necessary. The Company maintains provisions for potential credit losses, and any such losses to date have been within management's expectations.

Additionally, the Company mitigates tenant credit risk through staggered lease maturities and diversification of revenue sources resulting from a large tenant base and avoids dependence on any single tenant by ensuring no individual tenant contributes a significant percentage of the Company's gross revenue.

As at August 31, 2019, excluding revenue and leases related to properties under development and assets held for sale:

- No one tenant accounted for more than 13.85% (August 31, 2018 - 14.60%) of the Company's rental revenue.
- Lease maturities were staggered such that no more than 21.26% (August 31, 2018 - 21.04%) of the rental space was subject to renewal in any one year.

#### **Interest rate risk**

Borrowings under the Company's operating line of credit bear interest at variable rates. The Company's mortgages bear interest at fixed rates, and therefore, the Company is not exposed to interest rate risk on those fixed rate mortgages. As at August 31, 2019, \$nil (August 31, 2018 - \$nil) had been drawn on the line of credit and the Company had \$nil (August 31, 2018 - \$4,744) in variable rate mortgages and construction loans. These variable rate borrowings represent nil% (August 31, 2018 - 2.25%) of the Company's total borrowings. The impact of a 1% change in the Company's variable rate borrowings would increase or decrease interest expense and pre-tax earnings for the year by \$nil (year ended August 31, 2018 - \$47). Additionally, the Company earns interest on its cash and cash equivalent balances at variable rates.

#### **Liquidity risk**

The Company manages liquidity by maintaining adequate cash balances and by having an appropriate line of credit available. In addition, the Company regularly monitors and reviews both actual and forecasted cash flows. Refinancing risks are minimized by ensuring debt on investment properties has a balanced maturity schedule. Management does not anticipate any difficulty in refinancing debt on investment properties under similar terms as the debt matures.

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The following table details the minimum principal repayments for debt on investment properties:

	\$
2020	81,686
2021	23,627
2022	35,763
2023	50,346
2024	39,498
	<u>230,920</u>

**Fair value**

Cash and cash equivalents, amounts receivable, and accounts payable and accrued liabilities have fair values that approximate their carrying values. The estimated fair value of debt on investment properties as at August 31, 2019 is \$231,201 (August 31, 2018 - \$208,076). The fair value of outstanding interest rate swaps is disclosed in note 8.

The estimated fair values of debt on investment properties and interest rate swaps are based on values derived using market interest rates of similar instruments and incorporate assumptions regarding current market interest rates, terms, and the related risk. Accordingly, changes in these assumptions would result in a variance in the fair value estimates.

**21. Commitments**

At August 31, 2019, future minimum commitments with respect to a land lease are as follows:

	<b>Direct commitment on land lease \$</b>
2020	94
2021	94
2022	94
2023	94
2024	94
2025 and thereafter	2,402

**22. Capital management**

The primary objective of the Company's capital management is to ensure that it maintains adequate capital resources in order to support its business and maximize shareholder value. The Company manages its capital structure with the goal of minimizing risk to the stability of cash flows from properties. Other goals include maintaining debt service coverage, interest coverage, and debt to equity ratios as well as maintaining minimum amounts of shareholders' equity as required by the Company's line of credit agreement. The Company's capital includes mortgage loans, construction loans, a line of credit, and equity.

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The Company's principal source of financing is from mortgage loans. The ability to obtain a mortgage loan is dependent on the value of a specific property and the cash flows the property generates and the availability of funds from time to time from lending institutions. The Company expects to renew mortgage loans under similar terms as they become due.

There have been no changes in the Company's approach to capital management in the year ended August 31, 2019.

The calculation of the total capital, excluding the undrawn line of credit, is summarized as follows:

	<b>August 31, 2019</b>	<b>August 31, 2018</b>
	\$	\$
Fixed rate mortgage loans	230,920	206,023
Variable rate mortgages and construction loans	-	4,744
	<hr/> 230,920	<hr/> 210,767
Equity	<hr/> 341,059	<hr/> 312,459
	<hr/> <hr/> 571,979	<hr/> <hr/> 523,226