



InnVest
R · E · I · T

2006 Third Quarter Report to Unitholders

for the three and nine months ended
September 30, 2006

LETTER TO UNITHOLDERS

InnVest achieved significant growth in distributable income in the third quarter. This growth has been fuelled by acquisitions, improvements in RevPAR and cost controls which have generated higher operating profits.

In the third quarter we acquired two full service Hilton Hotels, in addition to the acquisition of the five hotels acquired in the first half of 2006. The 571 room Hilton Quebec City and the 197 room Hilton Saint John, New Brunswick were acquired on September 19, 2006 for \$62.7 million plus transaction costs bringing the total year-to-date acquisitions to \$140.4 million plus transaction costs. The acquisitions in the quarter were financed with \$49.8 million of first mortgage debt and cash on hand. Management expects that these acquisitions will be immediately accretive to distributable income on an absolute and per unit basis.

We continue to have significant unutilized capacity to make acquisitions that are accretive to cash flow and demonstrate long-term value. The REIT has unused operating loan availability of \$25 million at September 30, 2006 and eight hotel properties including the two Deltas acquired in the second quarter, which remain unencumbered. The REIT estimates that the unencumbered hotels could generate approximately \$45 million in mortgage proceeds. The REIT also has an unused acquisition facility of \$40 million available to acquire hotel properties and an unused loan facility of \$21.7 million available to fund 50% of capital expenditures.

Continuing with its strategy of investing in its hotels, InnVest deployed approximately \$8.0 million for capital asset improvements during the third quarter.

FINANCIAL REVIEW

For the third quarter, InnVest's revenue per available room ("RevPAR") improved by 5.1% as RevPAR increased to \$75.84. Average daily rates increased by 5.2% to \$103.69. As in the first half of 2006, this was primarily due to the nature of the hotels we acquired at the end of the second quarter of 2005, which typically yield higher rates than our base portfolio of hotels. On a same hotel basis the REIT's RevPAR improved by 3.3% in the quarter, mainly as the result of improvements in room rates.

Room revenues for the three months ended September 30, 2006 were \$103.3 million, 9.8% higher than the \$94.1 million generated for the same period in 2005. The increase of \$9.2 million reflects the \$6.0 million in revenues from the hotels acquired after the end of the second quarter in 2005 and in 2006. The balance of the improvement reflects an overall increase in room revenue of 3.5% in the base portfolio of hotels. There were increases in all geographical regions with the largest dollar increases experienced in Ontario and the largest percentage increase experienced in the Western region.

Hotel expenses for the three months ended September 30, 2006 increased by \$7.9 million or 12.3% when compared to the same period in 2005. This reflects \$5.5 million in expenses incurred in the hotels acquired after the end of the second quarter in 2005 and in 2006, which were not owned for all of comparative period. The remaining \$2.4 million that relates to the base portfolio represents a 3.7% increase over 2005. In the base portfolio, operating expenses increased \$2.3 million or 4.4%, which is higher than the 3.5% increase in room revenue because of further implementation of the free continental breakfast program at the Choice branded hotels.

Distributable income grew to \$31.5 million for the three months ended September 30, 2006, an improvement of \$4.1 million over the distributable income of \$27.4 million experienced in the same period in 2005. Distributable income per unit on a diluted basis grew \$0.010 or 2.0% to \$0.519 in the quarter.

At September 30, 2006, InnVest's cash totalled \$11.2 million. Financial leverage is at 39.6% debt to gross asset value excluding convertible debentures and 49.9% including convertible debentures. For the trailing twelve months ended September 30, 2006 the REIT's pay-out ratio of distributions to distributable income was 95.0%.

In 2005, 47.23% of the distributions made during that year were not taxable to unitholders. For calendar 2006, the REIT estimates that over 40% of unitholder distributions will not be taxable to unitholders.

OUTLOOK

In the third quarter, the REIT continued to benefit from the hotels acquired in 2005 and 2006, which were not owned in the prior year. This contributed \$2.8 million to hotel operating income during the third quarter. The base portfolio of hotels achieved a \$4.3 million increase in hotel operating income for the nine months ended September 30, 2006.

All regions in InnVest's portfolio are experiencing growth, with the strongest region being the West. Ontario, the REIT's largest concentration of hotels, continues to see sustained growth in the top line and is expected to experience strong hotel operating income growth. Continued top line growth contributed to stabilized operating margins in the quarter.

Growth within its base portfolio and its 2006 acquisitions are expected to positively impact the REIT's operating results for the balance of 2006 and into 2007.

Kenneth Gibson
President and Chief Executive Officer
November 8, 2006

INTRODUCTION

The following is a discussion of the results of operations and financial condition of InnVest Real Estate Investment Trust ("InnVest" or the "REIT") for the three and nine months ended September 30, 2006, with a comparison to the results of operations of InnVest for the three and nine months ended September 30, 2005.

The following management's discussion and analysis ("MD&A") is dated November 8, 2006 and should be read in conjunction with the unaudited consolidated financial statements of the REIT and the notes thereto as at and for the three and nine months ended September 30, 2006 and the audited consolidated financial statements of the REIT and the notes thereto as at and for the year ended December 31, 2005.

The financial statements of InnVest are prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and are presented in Canadian dollars. Monetary data in tabular form and in the text, unless otherwise indicated, are in thousands of dollars, except for per unit, Average Daily Rate ("ADR") and Revenue per Available Room ("RevPAR") amounts.

Additional information relating to the REIT, including the REIT's annual information form, can be found at www.sedar.com.

OVERVIEW OF INNVEST REIT

InnVest holds Canada's largest hotel portfolio with 137 hotels and 15,661 rooms located in every province of Canada. InnVest also owns a 50% interest in Choice Hotels Canada Inc. ("Choice Canada"), the largest franchisor of hotels in Canada. The portfolio consists of limited service and mid-scale with food and beverage hotel properties operated under several internationally recognized franchise brands such as Comfort Inn®, Quality Suites®, Quality Hotels®, Holiday Inn®, Radisson Hotels®, Radisson Suites®, Delta®, Hilton Hotels®, Hilton Garden Inn®, Hilton Homewood Suites® and Travelodge®.

InnVest is an unincorporated open-ended real estate investment trust governed by the laws of Ontario and constituted pursuant to a Declaration of Trust ("Declaration") and is publicly traded and listed on the Toronto Stock Exchange under the symbol INN.UN.

THIRD QUARTER HIGHLIGHTS

- On a same hotel basis, RevPAR growth was 3.3% during the third quarter of 2006 for the REIT's portfolio of hotels;
- Distributable income grew to \$31.5 million for the three months ended September 30, 2006, an improvement of \$4.1 million over the same period in 2005. Distributable income per unit on a diluted basis grew \$0.010 to \$0.519, an increase of 2.0%;
- In September, the REIT acquired the 571 room Hilton Quebec City and the 197 room Hilton Saint John, New Brunswick for a total of \$62.7 million plus transaction costs; and
- \$8.0 million was invested in our hotels, funded from restricted cash reserves or funds set aside for acquired hotels.

REGIONAL HOTEL MARKETS

OVERVIEW AND KEY PERFORMANCE DRIVERS

The overview and key performance drivers of the Canadian hotel market remain substantially unchanged from the description provided in the MD&A for the year ended December 31, 2005.

RECENT INDUSTRY PERFORMANCE

Canadian hotel industry fundamentals continued to post improvements in the third quarter of 2006. According to PKF Consulting, advisors to the hotel industry, occupancy and ADR's for the nine months ended September 30, 2006 for Canadian hotels experienced 1.4 points and 4.1% growth respectively resulting in RevPAR growth of 6.5% for the period. On a same hotel basis, InnVest experienced above average RevPAR growth in western Canada at 14.8%, with Alberta (20.6%) posting the highest gains. The Atlantic region hotels posted a RevPAR improvement of 5.2%. Ontario and Quebec, where the majority of the REIT's hotels are located, posted a RevPAR gain of 3.8% and a slight decline of 0.1% respectively.

InnVest's hotels on a same hotel basis outperformed the Canadian market for the nine months ended September 30, 2006 in two out of its four regions as follows:

REVPAR % GROWTH BY GEOGRAPHICAL REGIONS

	InnVest Portfolio	Canadian Market	Variance
Ontario	3.8%	4.9%	-1.1%
Quebec	-0.1%	1.7%	-1.8%
Atlantic	5.2%	3.9%	1.3%
Western	14.8%	10.2%	4.6%
Total	4.3%	6.5%	-2.2%

InnVest under performed the market in Ontario as the market growth was influenced by strong growth in the Niagara Falls region where InnVest does not own any hotels.

The growth in the Quebec market was primarily due to increased revenues in downtown Montreal where InnVest is not heavily represented. The rural Quebec markets experienced a modest increase in RevPAR of 0.3% and InnVest outperformed the market in these regions.

PORTFOLIO SUMMARY

InnVest operates under ten different brands with Comfort Inn representing 43.7% of the portfolio based on number of guest rooms. As of September 30, 2006, InnVest owned 137 internationally branded limited service and mid-scale with food and beverage hotels located in every province of Canada (the "hotel portfolio").

MANAGEMENT'S DISCUSSION AND ANALYSIS

HOTEL OWNERSHIP

Brands	No. of Hotels	No. of Guest Rooms	% of Guest Rooms
Comfort Inn	85	6,849	43.7%
Holiday Inn	15	2,608	16.7%
Travelodge	11	1,839	11.7%
Quality Suites/Inn	8	1,096	7.0%
Quality Hotel	5	796	5.1%
Radisson Hotel/Suites	4	707	4.5%
Delta Hotel	3	582	3.8%
Hilton Hotels	2	768	4.9%
Best Western	1	130	0.8%
Hilton Garden Inn	1	120	0.8%
Hilton Homewood Suites	1	83	0.5%
Independent	1	83	0.5%
	137	15,661	100.0%

Over 76% of the REIT's guest rooms are in Ontario and Quebec. The geographic distribution of hotels and rooms by brand as at September 30, 2006 is as follows:

	Ontario			Quebec			Atlantic			Western		
	No. of Hotels	Guest Rooms	% of Total Guest Rooms	No. of Hotels	Guest Rooms	% of Total Guest Rooms	No. of Hotels	Guest Rooms	% of Total Guest Rooms	No. of Hotels	Guest Rooms	% of Total Guest Rooms
Comfort Inn	38	3,155	20.1%	22	1,754	11.2%	16	1,195	7.6%	9	745	4.8%
Holiday Inn	13	2,260	14.4%	-	-	-	1	196	1.3%	1	152	1.0%
Travelodge	7	943	6.0%	-	-	-	-	-	-	4	896	5.7%
Quality Suites/Inn	4	604	3.9%	4	492	3.1%	-	-	-	-	-	-
Quality Hotel	1	212	1.4%	2	298	1.9%	1	160	1.0%	1	126	0.8%
Radisson Hotel/Suites	3	532	3.4%	1	175	1.1%	-	-	-	-	-	-
Delta Hotel	1	245	1.6%	2	337	2.2%	-	-	-	-	-	-
Hilton Hotels	-	-	-	1	571	3.6%	1	197	1.3%	-	-	-
Best Western	1	130	0.8%	-	-	-	-	-	-	-	-	-
Hilton Garden Inn	1	120	0.8%	-	-	-	-	-	-	-	-	-
Homewood Suites	1	83	0.5%	-	-	-	-	-	-	-	-	-
Independent	1	83	0.5%	-	-	-	-	-	-	-	-	-
	71	8,367	53.4%	32	3,627	23.1%	19	1,748	11.2%	15	1,919	12.3%

The REIT's hotels are typically located near major thoroughfares in urban and suburban areas as well as demand generators such as business centres, government and manufacturing facilities, universities, airports and tourist attractions. The hotels have a diverse customer base, including business travelers, leisure travelers, groups, organizations and corporate clients.

OTHER BUSINESS AND COMPETITIVE STRENGTHS

The REIT's franchise business and competitive strengths remain substantially unchanged from the description provided in the MD&A for the year ended December 31, 2005; however the REIT, as part of the Quebec Delta transaction has acquired office, retail real estate and a retirement home. These assets are classified as other real estate properties on the balance sheet. The operating results are included along with the franchise business income in the consolidated statements of income in other business income.

STRATEGY AND OBJECTIVES

OBJECTIVES AND OPERATING STRATEGY

The REIT's objectives and operating strategy remain substantially unchanged from the description provided in the MD&A for the year ended December 31, 2005.

ACQUISITION STRATEGY AND 2006 ACTIVITY

InnVest continues to execute on its strategy of increasing cash flow and enhancing the long-term value of the REIT through selective acquisitions that are expected to be accretive to earnings and cash flow. In addition to the acquisition of the Leamington Comfort Inn in the first quarter, the REIT, through two separate transactions acquired four hotels with a total of 540 rooms for a combined purchase price of \$74.5 million plus transaction costs during the second quarter. Two of the hotels are branded Delta hotels and located in Sherbrooke and Trois Rivieres, Quebec (the "Deltas"). These hotels operate in the full-service segment and include convention centres, office and retail space, which account for \$16.8 million of the all-in purchase price. The Trois Rivieres location also includes a retirement home. The remaining two hotels are newly built hotels located in Burlington, Ontario, one of which is branded a Hilton Garden Inn and the other a Homewood Suites. In the third quarter, the REIT acquired the 571 room Hilton Quebec City and the 197 room Hilton Saint John, New Brunswick (the "Hiltons") for \$62.7 million plus transaction costs. The transaction for the Hiltons closed on September 19, 2006.

	Ontario		Quebec		Atlantic	
	No. of Hotels	No. of Guest Rooms	No. of Hotels	No. of Guest Rooms	No. of Hotels	No. of Guest Rooms
Comfort Inn	1	62	–	–	–	–
Hilton Garden Inn	1	120	–	–	–	–
Homewood Suites	1	83	–	–	–	–
Delta Hotels	–	–	2	337	–	–
Hilton Hotels	–	–	1	571	1	197
	3	265	3	908	1	197

Based on 2005 results, the Comfort Inn, Delta Hotels and the Hilton Hotels and related assets acquisitions are expected to be immediately accretive to distributable income. The two new build hotels are expected to be accretive within the first 12–24 months of operations. These acquisitions will continue to increase the REIT's participation in the mid-scale with food and beverage segment and launch the REIT into the extended stay segment of the market with the Hilton Homewood Suites brand. These acquisitions support the REIT's objective of providing long-term benefits to unitholders through value appreciation and further diversification. The acquisitions were financed through the assumption of \$14.3 million in mortgages, a vendor-take-back loan of \$2.0 million, new mortgage financing proceeds of \$49.8 million and cash.

DIVESTITURE STRATEGY

When assets are identified that do not support certain primary objectives of the REIT, an analysis is conducted to decide if the divestiture of such assets is in the best interest of unitholders. Such an analysis will take into consideration the implications for distributable income and overall diversification, market conditions and numerous other factors.

Effective April 17, 2006, the REIT classified one hotel as discontinued operations as prescribed by CICA Handbook Section 3475, Disposal of Long-Lived Assets and Discontinued Operations and effective September 30, 2006, the REIT classified an additional hotel as discontinued operations. This section requires that long-lived assets held for sale be classified, for both the current and comparative periods as discontinued operations and the results of operations and cash flows associated with the assets be reported separately as discontinued operations in the financial statements. The REIT wrote down the book value of this hotel by \$1.0 million in the second quarter, and no further amortization and depreciation will be recorded by the REIT for each hotel after the respective effective dates. No write down in book value is required for the hotel classified as discontinued operations in the third quarter.

MANAGEMENT'S DISCUSSION AND ANALYSIS

FINANCIAL PERFORMANCE REVIEW

Below is a comparison of the operating results for the three and nine months ended September 30, 2006 to the results of operations for the comparable periods of 2005.

	Three Months Ended Sept. 30, 2006	Three Months Ended Sept. 30, 2005	Nine Months Ended Sept. 30, 2006	Nine Months Ended Sept. 30, 2005
Hotel revenues	\$ 117,119	\$ 105,539	\$ 290,265	\$ 243,449
Hotel expenses	72,372	64,468	196,167	162,716
Hotel operating income	44,747	41,071	94,098	80,733
Net income from continuing operations	\$ 23,304	\$ 21,388	\$ 40,145	\$ 20,782
Net income from continuing operations				
per unit – basic	\$ 0.425	\$ 0.449	\$ 0.775	\$ 0.447
per unit – diluted	\$ 0.395	\$ 0.412	\$ 0.763	\$ 0.446
Net income (loss) from discontinued operations	\$ 232	\$ 135	\$ (804)	\$ (1,634)
Net income	\$ 23,536	\$ 21,523	\$ 39,341	\$ 19,148
Add / (deduct)				
Depreciation, amortization and accretion ⁽¹⁾	12,972	10,446	36,200	29,544
Future income tax recovery	(1,265)	(1,444)	(14,171)	(1,479)
Non-cash executive and trustee compensation	86	91	261	273
Writedown of assets held for sale	–	211	1,000	1,682
Funds from operations ⁽²⁾	\$ 35,329	\$ 30,827	\$ 62,631	\$ 49,168
Amortization of deferred financing	710	559	1,939	1,614
Reserve for replacement of furniture, fixtures and equipment and capital improvements (“FF&E Reserve”)	(4,746)	(4,275)	(11,688)	(9,927)
Convertible debentures accretion	211	257	595	775
Deferred land lease expense and retail lease income, net	34	17	84	17
Distributable income ⁽²⁾	\$ 31,538	\$ 27,385	\$ 53,561	\$ 41,647
Distributable income per unit ⁽³⁾				
– basic	\$ 0.575	\$ 0.575	\$ 1.034	\$ 0.895
– diluted	\$ 0.519	\$ 0.509	\$ 0.972	\$ 0.856
Distributions ⁽⁴⁾	\$ 15,417	\$ 13,422	\$ 44,150	\$ 39,404
Distributions – per unit ⁽⁴⁾	\$ 0.2813	\$ 0.2813	\$ 0.8438	\$ 0.8438
Reconciliation of Cash flow from operating activities to Distributable income				
Cash flow from operating activities	\$ 36,460	\$ 34,296	\$ 64,083	\$ 56,091
Changes in non-cash working capital	(156)	(2,704)	1,108	(4,744)
Changes in non-cash working capital – discontinued operations	(54)	51	(26)	210
Reserve for replacement of furniture, fixtures and equipment and capital improvements (“FF&E Reserve”)	(4,746)	(4,275)	(11,688)	(9,927)
Deferred land lease expense and retail lease income, net	34	17	84	17
Distributable income ⁽²⁾	\$ 31,538	\$ 27,385	\$ 53,561	\$ 41,647

- (1) For purposes of the calculation of funds from operations, amortization of deferred financing is excluded from depreciation, amortization and accretion.
- (2) Funds from operations and distributable income are measures of earnings and cash flow commonly used by industry analysts that are not required under GAAP, and accordingly, may not be comparable to similar measures used by other organizations.
- (3) Distributable income per unit amounts have been calculated on a basis consistent with that prescribed by GAAP for calculating earnings per unit.
- (4) Distributions and distributions per unit include cash distributions and distributions arising from the Distribution Reinvestment Plan.

KEY PERFORMANCE MEASURES

There are several key metrics that are used to measure the performance of the hotel industry and the relative strength of participants in the industry: occupancy, average daily rates (“ADR”), revenue per available room (“RevPAR”), gross operating profit (“GOP”), hotel operating income (“HOI”), funds from operations (“FFO”) and distributable income (“DI”).

The key performance measures related to room revenues for the REIT’s portfolio of hotels on a same hotel basis, excluding the hotels that have been classified as discontinued operations and the hotels acquired in the second and third quarters of 2006 for which comparative data is not available are as follows:

	Three months ended September 30			Nine months ended September 30		
	2006	2005	Var %	2006	2005	Var %
Occupancy						
Ontario	71.5%	71.2%	0.4%	64.7%	64.6%	0.2%
Quebec	74.8%	77.2%	(3.1%)	65.4%	66.6%	(1.8%)
Atlantic	81.1%	81.1%	–	65.2%	65.1%	0.2%
Western	75.9%	71.6%	6.0%	65.2%	60.6%	7.6%
Total	73.8%	73.5%	0.4%	64.9%	64.5%	0.6%
ADR						
Ontario	\$ 106.73	\$ 103.61	3.0%	\$ 103.26	\$ 99.55	3.7%
Quebec	\$ 96.72	\$ 95.59	1.2%	\$ 93.11	\$ 91.41	1.9%
Atlantic	\$ 103.82	\$ 99.43	4.4%	\$ 93.62	\$ 89.17	5.0%
Western	\$ 84.30	\$ 80.85	4.3%	\$ 79.83	\$ 74.78	6.8%
Total	\$ 101.33	\$ 98.51	2.9%	\$ 97.09	\$ 93.67	3.7%
RevPAR						
Ontario	\$ 76.36	\$ 73.79	3.5%	\$ 66.76	\$ 64.33	3.8%
Quebec	\$ 72.37	\$ 73.77	(1.9%)	\$ 60.85	\$ 60.91	(0.1%)
Atlantic	\$ 84.19	\$ 80.60	4.5%	\$ 61.05	\$ 58.02	5.2%
Western	\$ 64.01	\$ 57.91	10.5%	\$ 52.02	\$ 45.31	14.8%
Total	\$ 74.79	\$ 72.39	3.3%	\$ 63.02	\$ 60.42	4.3%

On a same hotel basis, the REIT’s hotels, posted a RevPAR improvement of 3.3% for the three months ended September 30, 2006 over the same period in the previous year. This increase was achieved through a 2.9% or \$2.82 increase in ADR and a 0.4% increase in occupancy.

The REIT’s hotels, posted a RevPAR improvement of 4.3% for the nine months ended September 30, 2006 over the same period in the previous year. This increase was achieved through a 3.7% or \$3.42 increase in ADR and a 0.6% increase in occupancy.

OPERATING RESULTS REVIEW - THREE MONTHS ENDED SEPTEMBER 30, 2006

InnVest's operations are seasonal and as such its results are not consistent throughout the year. Revenue earned from hotel operations fluctuate throughout the year, with the third quarter being the highest due to the increased level of leisure travel in the summer months and the first quarter being the lowest because leisure travel tends to be lower. The results from operations vary materially from quarter to quarter because of the seasonal nature of the revenue stream and the fact that certain costs such as property taxes, insurance, interest, depreciation and amortization, corporate and administrative are fixed or virtually fixed.

HOTEL OPERATING RESULTS COMPARISON

In summarizing the hotel operating results for the three months ended September 30, 2006 and comparing those results to the three months ended September 30, 2005, the REIT has categorized 127 of its 129 hotels owned for the entire current and comparative period as its "Base Portfolio" with the remaining two hotels being classified as discontinued operations. The hotel acquired after the end of the second quarter of 2005 have been categorized as the "2005 Acquisition" and the seven hotels acquired year-to-date in 2006 as the "2006 Acquisitions."

HOTEL REVENUES

Hotel revenues consist primarily of revenue generated from room occupancy. Non-room revenue from food and beverage services and other miscellaneous revenue streams associated with hotel operations such as space leases, vending commissions, movie rentals, parking and telephone are also included. Departmental expenses are those expenses which are directly related to generating both room revenue and non-room revenue.

A summary of the hotel revenue categorized by room revenue and non-room revenue for the three months ended September 30, 2006 and 2005 are stated below:

	2006	2005	Variance
Room Revenue			
Base Portfolio	\$ 96,605	\$ 93,339	\$ 3,266
2005 Acquisition	1,045	749	296
2006 Acquisitions	5,668	-	5,668
Sub-total	\$ 103,318	\$ 94,088	\$ 9,230
Non-Room Revenue			
Base Portfolio	\$ 11,804	\$ 11,425	\$ 379
2005 Acquisition	33	26	7
2006 Acquisitions	1,964	-	1,964
Sub-total	\$ 13,801	\$ 11,451	\$ 2,350
Hotel Revenue			
Base Portfolio	\$ 108,409	\$ 104,764	\$ 3,645
2005 Acquisition	1,078	775	303
2006 Acquisitions	7,632	-	7,632
Total	\$ 117,119	\$ 105,539	\$ 11,580

OVERALL HOTEL PORTFOLIO

In the third quarter hotel revenue increased by \$11.6 million, and as in the first two quarters the majority of the increase was due to the hotels acquired in 2005 and 2006. The majority of the 2005 Acquisitions (seven of nine) were completed in June 2005 with one acquisition in March 2005 and one in August 2005. The one hotel acquired in the first quarter of 2006 closed on March 3, 2006, while two Hiltons were acquired April 28, 2006, two Deltas were acquired on May 25, 2006 and two additional Hiltons were acquired on September 19, 2006. The base portfolio of 127 hotels owned for the current and comparative period experienced an increase in revenue of \$3.6 million or 3.5%.

The increase of \$9.2 million in room revenues for the three months ended September 30, 2006 reflects \$6.0 million in revenues from the hotels acquired in 2005 after the end of the second quarter and 2006. The balance of the improvement reflects an overall increase in room revenue of 3.5% in the Base Portfolio. There were increases in all geographical regions with the exception of Quebec, with the largest dollar increase experienced in Ontario and the largest percentage increase experienced in the Western region.

ROOM REVENUES

A geographical comparison of the room revenue variance between the three months ended September 30, 2006 and 2005, excluding the hotels classified as discontinued operations are as follows:

	Hotels	Rooms	As a % of total	Room revenue variance	As a % of total	Var % over 2005
Base Portfolio						
Ontario	66	7,846	50.7%	\$ 2,030	22.0%	3.8%
Quebec	29	2,719	17.6%	(353)	(3.8%)	(1.9%)
Atlantic	17	1,482	9.6%	512	5.5%	4.5%
Western	15	1,919	12.4%	1,077	11.7%	10.5%
Sub-total	127	13,966	90.3%	3,266	35.4%	3.5%
2005 Acquisition	1	140	0.9%	296	3.2%	100.0%
2006 Acquisitions	7	1,370	8.8%	5,668	61.4%	100.0%
Total	135	15,476	100.0%	\$ 9,230	100.0%	9.8%

InnVest's base portfolio of Western hotels achieved the largest percentage growth of 10.5%, which equated to a \$1.1 million increase in room revenue, while the Ontario hotels achieved the largest dollar growth of \$2.0 million or 3.8% in room revenues relative to the same period in 2005. The Ontario hotels located in the Greater Toronto Area ("GTA") posted room revenue increases of 4.1%, while the Ontario hotels outside of the GTA achieved an increase of 3.7% over the same period in 2005. The Ontario markets which contributed positively to the results for the three-month period were the Burlington, Hamilton and Oakville (\$502 or 12.3%), North Bay (\$221 or 13.0%), and London (\$178 or 5.0%). The market that contributed negatively to the room revenue results in the period was Windsor, which posted a decline of \$156 or 10.9%, mainly as the result of a decline in occupancy caused by a slow down in the auto industry.

InnVest's base portfolio of hotels in Quebec experienced a room revenue decrease of \$353 million or 1.9%. The REIT's rural Quebec hotels improved by \$287 or 5.2%, while the REIT's Quebec City and Montreal hotels posted declines of \$182 or 5.4% and \$458 or 4.8% respectively. Both the Quebec City and Montreal markets were negatively affected by the decline in travelers from the United States.

InnVest's base portfolio of Atlantic region hotels experienced a \$512 million or 4.5% growth over 2005, with all four Provinces contributing.

InnVest's base portfolio of Western hotels continued to experience significant revenue growth posting an increase of \$1.1 million or 10.5% over the prior year. The majority of the gains were posted by the hotels located in Alberta (\$892 or 14.1%). As in the first two quarters, this increase was attributable to occupancy improvements and room rate increases related to economic activity generated by the oil and gas industry.

NON-ROOM REVENUES

Non-room revenues increased by \$3.4 million, primarily reflecting the non-room revenues generated by the hotels the REIT acquired in 2005 and 2006, which were not owned for any of the comparative period. The majority of the hotels acquired in 2005 and 2006 compete in the mid-scale with food and beverage sector and earn a higher proportion of total revenues from non-room revenues.

MANAGEMENT'S DISCUSSION AND ANALYSIS

HOTEL OPERATING INCOME MARGIN ANALYSIS

The following chart illustrates the REIT's margins for the base portfolio and the 2005 Acquisition and the 2006 Acquisitions, excluding the assets classified as discontinued operations, for the three months ended September 30, 2006 and 2005:

2006	Base Portfolio	2005 Acquisition ⁽¹⁾	2006 Acquisitions ⁽²⁾	Total
Hotel revenues	\$ 108,409	\$ 1,078	\$ 7,632	\$ 117,119
Hotel expenses				
Operating expenses	54,476	503	4,694	59,673
Property taxes, rent and insurance	8,283	94	370	8,747
Management fees	3,658	36	258	3,952
	66,417	633	5,322	72,372
Hotel operating income	\$ 41,992	\$ 445	\$ 2,310	\$ 44,747
HOI margin	38.7%	41.2%	30.3%	38.2%

2005	Base Portfolio	2005 Acquisition ⁽¹⁾		Total
Hotel revenues	\$ 104,764	\$ 775	\$ –	\$ 105,539
Hotel expenses				
Operating expenses	52,164	326	–	52,490
Property taxes, rent and insurance	8,354	63	–	8,417
Management fees	3,535	26	–	3,561
	64,053	415	–	64,468
Hotel operating income	\$ 40,711	\$ 360	\$ –	\$ 41,071
HOI margin	38.9%	46.4%		38.9%

Variance	Base Portfolio	2005 Acquisition ⁽¹⁾	2006 Acquisitions ⁽²⁾	Total
Hotel revenues	\$ 3,645	\$ 303	\$ 7,632	\$ 11,580
Hotel expenses				
Operating expenses	2,312	177	4,694	7,183
Property taxes, rent and insurance	(71)	31	370	330
Management fees	123	10	258	391
	2,364	218	5,322	7,904
Hotel operating income	\$ 1,281	\$ 85	\$ 2,310	\$ 3,676
HOI margin	(0.2%)	(5.2%)		(0.7%)

(1) The 2005 Acquisition represents a hotel acquired in 2005 and was not owned for the entire comparative period.

(2) The 2006 Acquisitions represent hotels acquired in 2006 and were not owned for any of the comparative period.

Total hotel operating income margin decreased by 0.7 points, which can be mainly attributed to the lower margin experienced for the seven hotels included in the 2006 Acquisitions. The 2006 Acquisitions generate a larger portion of their business in the non-room categories that typically yield lower margins. The decline in the margin for the one hotel included in the 2005 Acquisition is related to the hotel being owned for a less than a full quarter in the comparative period. The Base Portfolio's operating margin decreased by 0.2 points as the result of the percentage increases in operating expenses being slightly higher than the percentage revenue increases partially offset by the successful appeal of property taxes in certain municipalities.

HOTEL EXPENSES

Hotel expenses for the three months ended September 30, 2006 increased by \$7.9 million or 12.3% when compared to the same period in 2005. This increase reflects \$218 in expenses incurred in the hotel acquired in the third quarter of 2005 and \$5.3 million in expenses incurred in the hotels acquired in 2006, which were not owned for any of the comparative period. The remaining \$2.4 million related to the base portfolio represents a 3.7% increase over 2005. In the base portfolio, operating expenses increased \$2.3 million or 4.4%, which was modestly higher than the increase in room and total revenue as the result of the continued implementation of the free continental breakfast program at the Choice branded hotels.

HOTEL OPERATING INCOME

Hotel operating income ("HOI") for the three months ended September 30, 2006 improved by \$3.7 million to \$44.7 million. This was a result of an increase in hotel revenues of \$11.6 million partially offset by an overall increase in hotel expenses of \$7.9 million. The Base Portfolio achieved \$1.3 million or 34.9% of this increase, with the balance attributed to the hotels acquired in 2005 after June 30, 2005 and in 2006.

A geographical comparison of the HOI variance between the three months ended September 30, 2006 and 2005 is as follows:

	Hotels	Rooms	As a % of total	HOI variance	As a % of total	Var % over 2005
Base Portfolio						
Ontario	66	7,846	50.7%	\$ 1,167	31.8%	5.5%
Quebec	29	2,719	17.6%	(661)	(18.0%)	(7.6%)
Atlantic	17	1,482	9.6%	146	4.0%	2.4%
West	15	1,919	12.4%	629	17.1%	13.5%
Sub-total	127	13,966	90.3%	1,281	34.9%	3.1%
2005 Acquisition	1	140	0.9%	85	2.3%	100.0%
2006 Acquisitions	7	1,370	8.8%	2,310	62.8%	100.0%
Total	135	15,476	100.0%	\$ 3,676	100.0%	9.0%

The increase of \$2.4 million in HOI arising from the acquired hotels contributed 65.1% of the overall HOI increase of \$3.7 million. In the base portfolio, increases in HOI were experienced in three out of four regions with the largest dollar increase achieved in Ontario at \$1.2 million and the largest percentage increase achieved in the Western region at 13.5%.

OTHER INCOME AND EXPENSES

The net amount of other income and expenses for the three months ended September 30, 2006 was \$22.8 million, \$1.8 million or 8.4% more than the same period in 2005. The main contributors to this increase were a \$2.7 million increase in depreciation, amortization and accretion, a \$387 increase in interest on mortgages, an \$813 decrease in convertible debenture interest and accretion and a \$713 increase in other business income. The increases were mainly related to the hotels acquired during 2006, while the reduction in convertible debentures interest and accretion was the result of a conversion of \$14.2 million and \$52.9 million of the Initial Series – 9.75% Debentures during the first and second quarters respectively and the redemption of \$4.5 million of the Initial Series – 9.75% Debentures on June 1, 2006.

INCOME TAXES

Current income tax recovery for the three months ended September 30, 2006 was \$59, a decrease of \$177 from the same period expense in 2005. This decrease is attributable to refunds received in the current period as the result of taxable losses generated in corporate subsidiaries of the REIT. Further, InnVest experienced a \$1.3 million future income tax recovery, which is consistent with the same period of the prior year.

In 2005, 47.23% of the distributions made during that year were not taxable to unitholders. For calendar 2006, the REIT estimates that over 40% of unitholder distributions will not be taxable to unitholders.

NET INCOME

InnVest's net income for the three months ended September 30, 2006 was \$23.5 million compared to \$21.5 million for the same period in 2005.

InnVest's net income from continuing operations was \$23.3 million or \$0.425 per unit basic (\$0.395 – diluted), compared with a net income in the prior year period of \$21.4 million or \$0.449 per unit basic (\$0.412 – diluted). The improvement of \$1.9 million is the net result of improvements in hotel operating income, a net decrease in interest expense on mortgages and convertible debentures, increases in other business income, partially offset by increases in depreciation, amortization and accretion.

FUNDS FROM OPERATIONS

Funds from operations ("FFO") is not a measure defined under GAAP but it is widely used in the real estate industry. The Real Property Association of Canada generally defines FFO as net income adjusted for extraordinary items, gains or losses on the sale of assets, provisions for impairment against property values, capital items and depreciation and amortization relating to capital items. As an indicator of performance, FFO should not be considered a substitute for net income or funds from operating activities determined in accordance with GAAP. The REIT's method of calculating FFO may be different from that of other organizations.

The REIT currently calculates FFO by using net income and adjusting for:

- i) Depreciation, amortization and accretion, excluding amortization of deferred financing costs,
- ii) Future income tax expense or recovery,
- iii) Non-cash executive and trustee compensation expense, and
- iv) Write down of assets held for sale.

FFO is a meaningful measure of operating performance for investors. It assumes that the value of real estate investments does not necessarily decrease on a systematic basis over time, an assumption inherent in GAAP, and it adjusts for items included in GAAP net income that do not necessarily provide the best indicator of operating performance, such as gains or losses on the sale of, and provisions for impairment against, hotel properties.

FFO for the three months ended September 30, 2006 increased \$4.5 million to \$35.3 million over the same period in 2005. The increase is mainly attributable to the \$3.7 million increase in hotel operating income and an \$813 decrease in convertible debentures interest and accretion.

DISTRIBUTABLE INCOME

Distributable income is not a measure defined under GAAP, however it is commonly used in the real estate investment trust industry to measure performance.

Distributable income is intended to approximate cash earnings. It is defined in the REIT's Declaration of Trust to mean net income of the REIT and its consolidated subsidiaries as reported in its consolidated financial statements adjusted for:

- i) Depreciation, amortization and accretion and future income tax expense,
- ii) Any gains or losses on the disposition of any real property and any future income tax benefits,
- iii) The reserve for replacement of furniture, fixtures and equipment and capital improvements ("FF&E reserve"), and
- iv) Any other adjustment determined by a majority of the Trustees of the REIT in their discretion.

The calculation of distributable income and the amounts of each adjustment from net income are disclosed in the notes to the financial statements. Distributable income is one measure used by industry analysts in the determination of the Trust's per unit value, the ability of the Trust to fund distributions and investment returns for current or potential investors. As outlined in the Declaration of Trust, the REIT is required to distribute monthly to unitholders not less than one-twelfth of 80% of the estimated annualized distributable income of the Trust for the calendar year. Distributable income is not only used by management and the Board of Trustees to determine the level of distributions to unitholders, it also serves as an important measure for investors in their evaluation of the performance of management.

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

Distributable income for the three months ended September 30, 2006 was \$31.5 million or \$0.575 per unit basic (\$0.519 – diluted). This reflects a \$4.1 million improvement over the distributable income experienced for the same period in the prior year of \$27.4 million or \$0.575 per unit basic (\$0.509 – diluted). This increase is consistent with the increase in funds from operations discussed above.

CHANGES IN FINANCIAL CONDITION

The following discussion evaluates the cash flo/w results of InnVest from operating, financing and investing activities for the three months ended September 30, 2006.

Operating Activities

Funds generated from operating activities increased \$2.2 million to \$36.5 million for the three months ended September 30, 2006. The increase is mainly attributable to an increase in hotel operating income of \$3.7 million plus a net decrease in interest expense on mortgages and convertible debentures of \$380 and combined improvements in other business income and other income and current income taxes of \$985, net of a decrease of \$2.5 million in changes in non-cash working capital.

Financing Activities

Funds generated in financing activities were \$32.6 million for the period compared to funds used of \$21.9 million for the same period in 2005. The majority of the change relates to:

- Net proceeds from long-term debt in excess of cash used to repay bank indebtedness and loan payable of \$51.0 million;
- A decrease in the repayment of debt on discontinued operations of \$4.8 million;
- Decrease in deferred financing costs incurred of \$454; and
- Increase in cash distributions of \$1.8 million.

Investing Activities

Funds used for investing activities were \$79.5 million during the three months ended September 30, 2006 compared to \$9.2 million in the same period in 2005. The majority of the change relates to:

- Increase in cash used in hotel acquisitions, other assets and related working capital of \$59.1 million;
- Decrease in sale of discontinued operations of \$9.4 million;
- Decrease in capital expenditures of \$2.9 million; and
- Use of \$5.7 million in cash restricted for future furniture, fixtures and equipment and capital expenditures versus \$338 in the prior period.

In the three months ended September 30, 2006, InnVest spent \$8.0 million on capital items (2005 – \$10.9 million).

As part of the regular refurbishment program, InnVest sets aside 4% of revenue for the replacement of furniture, fixture and equipment and capital improvements (“FF&E reserve”) shown as restricted cash in the financial statements. The FF&E reserve is managed over the longer term to maintain the hotel properties to ensure they remain competitive in their markets.

OPERATING RESULTS REVIEW – NINE MONTHS ENDED SEPTEMBER 30, 2006**HOTEL OPERATING RESULTS COMPARISON**

In summarizing the hotel operating results for the nine months ended September 30, 2006 and comparing those results to the nine months ended September 30, 2005, the REIT has categorized 119 of its 121 hotels owned for the entire current and comparative period as its “Base Portfolio” with the remaining two hotels classified as discontinued operations, the nine hotels acquired in 2005 as the “2005 Acquisitions” and the seven hotels acquired year-to-date in 2006 as the “2006 Acquisitions.”

HOTEL REVENUES

A summary of the hotel revenue categorized by room revenue and non-room revenue for the nine months ended September 30, 2006 and 2005 are stated below:

	2006	2005	Variance
Room Revenue			
Base Portfolio	\$ 212,170	\$ 201,865	\$ 10,305
2005 Acquisitions	32,359	12,063	20,296
2006 Acquisitions	7,892	–	7,892
Sub-total	\$ 252,421	\$ 213,928	\$ 38,493
Non-Room Revenue			
Base Portfolio	\$ 27,692	\$ 26,993	\$ 699
2005 Acquisitions	7,370	2,528	4,842
2006 Acquisitions	2,782	–	2,782
Sub-total	\$ 37,844	\$ 29,521	\$ 8,323
Hotel Revenue			
Base Portfolio	\$ 239,862	\$ 228,858	\$ 11,004
2005 Acquisitions	39,729	14,591	25,138
2006 Acquisitions	10,674	–	10,674
Total	\$ 290,265	\$ 243,449	\$ 46,816

OVERALL HOTEL PORTFOLIO

Hotel revenue increased by \$46.8 million, with the majority of the increase attributable to the hotels acquired in 2005 and 2006. The majority of the 2005 Acquisitions (seven of nine) were completed in June 2005 with one acquisition in

March 2005 and one in August 2005. The base portfolio of 119 hotels owned for the current and comparative period experienced an increase in revenue of \$11.0 million or 4.8%.

The increase of \$38.5 million in room revenues for the nine months ended September 30, 2006 reflects the \$28.2 million in revenues from the hotels acquired in 2005 and 2006 and \$10.3 million or 5.1% improvement in the Base Portfolio. There were increases in all geographical regions with the largest dollar increase experienced in Ontario and the largest percentage increase experienced in the Western region.

The increase in non-room revenues is mainly attributable to the food and beverage revenue in the acquired hotels since the hotels acquired in 2005 and 2006 compete in the mid-scale with food and beverage sector and earn a higher proportion of total revenues from non-room revenues.

ROOM REVENUES

A geographical comparison of the room revenue variance between the nine months ended September 30, 2006 and 2005, excluding the hotels classified as discontinued operations are as follows:

	Hotels	Rooms	As a % of total	Room revenue variance	As a % of total	Var % over 2005
Base Portfolio						
Ontario	59	6,681	43.2%	\$ 5,292	13.8%	4.7%
Quebec	28	2,544	16.4%	213	0.6%	0.5%
Atlantic	17	1,482	9.6%	1,283	3.3%	5.2%
Western	15	1,919	12.4%	3,517	9.1%	14.8%
Sub-total	119	12,626	81.6%	10,305	26.8%	5.1%
2005 Acquisitions	9	1,480	9.5%	20,296	52.7%	168.3%
2006 Acquisitions	7	1,370	8.9%	7,892	20.5%	100.0%
Total	135	15,476	100.0%	\$ 38,493	100.0%	18.0%

InnVest's base portfolio of Ontario hotels experienced the largest dollar growth of \$5.3 million or 4.7% in room revenues relative to the same period in 2005. The Ontario hotels outside of the Greater Toronto Area ("GTA") posted room revenue increases of 4.4%, while the GTA hotels achieved an increase of 5.6% over the same period in 2005. The Ontario markets which contributed positively to the results for the nine-month period were Ottawa (\$1.2 million or 9.5%), northern Ontario (\$512 or 8.3%) and North Bay (\$442 or 10.5%). The market that contributed negatively to the room revenue results in the period was Oshawa, which posted a decline of \$398 or 3.8%, mainly as the result of a decline in occupancy caused by a slow down in the auto industry.

InnVest's base portfolio of hotels in Quebec generated a modest room revenue increase of \$213 or 0.6%. The REIT's rural Quebec hotels improved by \$765 or 5.9%, while the REIT's Montreal and Quebec City hotels posted declines of \$398 or 1.8% and \$154 or 2.1% respectively.

InnVest's base portfolio of Atlantic region hotels experienced a \$1.3 million or 5.2% growth over 2005, with increases being experienced in all four provinces.

InnVest's base portfolio of Western hotels continues to benefit from economic activity related to the oil and gas industry posting an increase of \$3.5 million or 14.8% over the prior year. The majority of the gains were posted by the hotels located in Alberta (\$2.9 million or 20.6%) and Saskatchewan (\$361 or 6.9%). The Regina market benefited from hosting the Canadian Men's Curling Championships in the first quarter, while the Saskatoon market benefited from an increase in City wide events and additional crew business in the second and third quarters.

NON-ROOM REVENUES

Non-room revenues increased by \$8.3 million, primarily reflecting the non-room revenues generated by the hotels the REIT acquired in 2005 and 2006, which were not owned for all of the comparative period. The majority of the hotels acquired in 2005 and 2006 compete in the mid-scale with food and beverage sector and earn a higher proportion of total revenues from non-room revenues.

MANAGEMENT'S DISCUSSION AND ANALYSIS

HOTEL OPERATING INCOME MARGIN ANALYSIS

The following chart illustrates the REIT's margins for the base portfolio and the hotels acquired in 2005 and 2006, excluding the assets classified as discontinued operations, for the nine months ended September 30, 2006 and 2005:

2006	Base Portfolio	2005 Acquisitions ⁽¹⁾	2006 Acquisitions ⁽²⁾	Total
Hotel revenues	\$ 239,862	\$ 39,729	\$ 10,674	\$ 290,265
Hotel expenses				
Operating expenses	129,846	24,157	6,275	160,278
Property taxes, rent and insurance	21,127	4,466	531	26,124
Management fees	8,064	1,341	360	9,765
	159,037	29,964	7,166	196,167
Hotel operating income	\$ 80,825	\$ 9,765	\$ 3,508	\$ 94,098
HOI margin	33.7%	24.6%	32.9%	32.4%

2005	Base Portfolio	2005 Acquisitions ⁽¹⁾		Total
Hotel revenues	\$ 228,858	\$ 14,591	\$ –	\$ 243,449
Hotel expenses				
Operating expenses	123,167	8,450	–	131,617
Property taxes, rent and insurance	21,402	1,481	–	22,883
Management fees	7,724	492	–	8,216
	152,293	10,423	–	162,716
Hotel operating income	\$ 76,565	\$ 4,168	\$ –	\$ 80,733
HOI margin	33.5%	28.6%		33.2%

Variance	Base Portfolio	2005 Acquisitions ⁽¹⁾	2006 Acquisitions ⁽²⁾	Total
Hotel revenues	\$ 11,004	\$ 25,138	\$ 10,674	\$ 46,816
Hotel expenses				
Operating expenses	6,679	15,707	6,275	28,661
Property taxes, rent and insurance	(275)	2,985	531	3,241
Management fees	340	849	360	1,549
	6,744	19,541	7,166	33,451
Hotel operating income	\$ 4,260	\$ 5,597	\$ 3,508	13,365
HOI margin	0.2%	(4.0%)		(0.8%)

(1) The 2005 Acquisitions represent hotels acquired in 2005 and were not owned for the entire comparative period.

(2) The 2006 Acquisitions represent hotels acquired in 2006 and were not owned for any of the comparative period.

Total hotel operating income margin decreased by 0.8 points, which can be attributed to the eight hotels acquired in 2005 after March 31, 2005 that were not owned for the entire comparative period. Eight of the nine hotels included in the 2005 Acquisitions were acquired on or after June 30, 2005 and therefore the higher margins achieved in the comparative period were the direct result of the higher margins typically experienced in the summer months.

HOTEL EXPENSES

Hotel expenses for the nine months ended September 30, 2006 increased by \$33.5 million or 20.6% when compared to the same period in 2005. This reflects \$19.5 million in expenses incurred in the hotels acquired in 2005 after March 31, 2005, which were not owned for the entire comparative period and \$7.2 million in expenses incurred in the hotels acquired in 2006 that were not owned for any of the comparative period. The remaining \$6.7 million that relates to the base portfolio represents a 4.4% increase over 2005. In the base portfolio, operating expenses increased \$6.6 million or 5.4%, which is slightly higher than the 5.1% increase in room revenue because of further implementation of the free continental breakfast program at the Choice branded hotels.

HOTEL OPERATING INCOME

Hotel operating income (“HOI”) for the nine months ended September 30, 2006 improved by \$13.4 million to \$94.1 million. This was a result of an increase in hotel revenues of \$46.8 million partially offset by an overall increase in hotel expenses of \$33.4 million. The Base Portfolio achieved \$4.3 million or 31.9% of this increase, with the balance attributed to the hotels acquired in 2005 and 2006.

A geographical comparison of the HOI variance between the nine months ended September 30, 2006 and 2005 is as follows:

	Hotels	Rooms	As a % of total	HOI variance	As a % of total	Var % over 2004
Base Portfolio						
Ontario	59	6,681	43.2%	\$ 2,164	16.2%	5.3%
Quebec	28	2,544	16.4%	(687)	(5.1%)	(4.1%)
Atlantic	17	1,482	9.6%	407	3.0%	3.9%
Western	15	1,919	12.4%	2,376	17.8%	27.5%
Sub-total	119	12,626	81.6%	4,260	31.9%	5.6%
2005 Acquisitions	9	1,480	9.5%	5,597	41.9%	100.0%
2006 Acquisitions	7	1,370	8.9%	3,508	26.2%	100.0%
Total	135	15,476	100.0%	\$ 13,365	100.0%	16.6%

The increase of \$9.1 million in HOI arising from the acquired hotels contributed 68.1% of the overall HOI increase of \$13.4 million. In the base portfolio, increases in HOI were experienced in all regions with the exception of the Quebec region which posted a decrease of \$687. The Western hotels posted the largest dollar and percentage increases of \$2.4 million and 27.5%.

OTHER INCOME AND EXPENSES

The net amount of other income and expenses for the nine months ended September 30, 2006 was \$68.3 million, \$7.4 million or 12.2% more than the same period in 2005. The main contributors to this change were a \$7.2 million increase in depreciation, amortization and accretion, a \$2.2 million increase in interest on mortgages, a \$1.6 million decrease in convertible debenture interest and accretion, a \$627 increase in corporate and administrative expenses and \$991 increase in other business income. The increases were mainly related to the hotels acquired during 2005 and 2006, while the reduction in convertible debentures interest and accretion was the result of the conversion of \$14.2 million and \$52.9 million of the Initial Series – 9.75% Debentures during the first and second quarters respectively and the redemption of \$4.5 million of the Initial Series – 9.75% Debentures on June 1, 2006.

INCOME TAXES

Current income tax recovery for the nine months ended September 30, 2006 was \$186, a decrease of \$711 from the expense recorded for the same period in 2005. This decrease is attributable to refunds of \$228 received in the period as the result of taxable losses generated in corporate subsidiaries of the REIT and the reversal of the large corporation tax recorded in the first quarter resulting from the elimination of the large corporation tax by the Federal Government. Further, InnVest experienced a \$12.7 million increase in future income tax recovery recorded over the same period in the prior year, mainly from using a lower blended income tax rate as the result of a change in the federal income tax rate in June 2006 for the corporate subsidiaries of the REIT.

NET INCOME

InnVest's net income for the nine months ended September 30, 2006 was \$39.3 million compared to \$19.1 million for the same period in 2005.

InnVest's net income from continuing operations was \$40.1 million or \$0.775 per unit basic (\$0.763 – diluted), compared with net income in the same period of the prior year period of \$20.8 million or \$0.447 per unit basic (\$0.446 – diluted). The improvement of \$19.3 million was the net result of improvements in hotel operating income, partially offset by a net increase in interest expense on mortgages and convertible debentures, increases in depreciation, amortization and accretion, an increase in other business income, corporate and administrative expense and an increase in the income tax recovery amount.

FUNDS FROM OPERATIONS

FFO for the nine months ended September 30, 2006 increased \$13.5 million to \$62.6 million from \$49.1 million in the same period in 2005. The increase is mainly attributable to the \$13.4 million increase in hotel operating income.

DISTRIBUTABLE INCOME

Distributable income for the nine months ended September 30, 2006 was \$53.6 million or \$1.034 per unit basic (\$0.972 – diluted). This reflects an \$11.9 million improvement over the distributable income experienced for the same period in the prior year of \$41.7 million or \$0.895 per unit basic (\$0.856 – diluted). This increase is consistent with the increase in funds from operations discussed above.

CHANGES IN FINANCIAL CONDITION

The following discussion evaluates the cash flow results of InnVest from operating, financing and investing activities for the nine months ended September 30, 2006.

Operating Activities

Funds generated from operating activities increased \$8.0 million to \$64.1 million for the nine months ended September 30, 2006. The increase is mainly attributable to an increase in hotel operating income of \$13.4 million less a net increase in interest expense on mortgages and convertible debentures of \$712, plus combined improvements in other business income and other income and current income and capital taxes of \$1.7 million. Additionally, there was a decrease of \$5.9 million in changes in non-cash working capital.

Financing Activities

Funds generated through financing activities were \$80.3 million for the period compared to funds generated of \$28.6 million for the same period in 2005. The majority of the change relates to:

- Net proceeds from long-term debt in excess of cash used to repay bank indebtedness and loan payable of \$52.7 million;
- A decrease in the repayment of debt on discontinued operations of \$4.9 million;
- Increase in deferred financing costs incurred of \$2.5 million; and
- Increase in cash distributions of \$3.9 million.

Investing Activities

Funds used for investing activities were \$147.7 million during the nine months ended September 30, 2006 compared to \$104.2 million in the same period in 2005. The majority of the change relates to:

- Increase in hotel and other real estate acquisitions, other assets and related working capital of \$29.0 million;
- Decrease in sale of discontinued operations of \$9.4 million;
- Decrease in capital expenditures of \$5.1 million; and
- Net increase of \$2.5 million in cash restricted for future furniture, fixtures and equipment and capital expenditures versus \$7.8 million used in the prior period.

In the nine months ended September 30, 2006, InnVest spent \$19.4 million on capital items (2005 – \$24.5 million).

LIQUIDITY AND CAPITAL RESOURCES

FINANCIAL COMMITMENTS

The following chart summarizes InnVest's future contractual obligations as at September 30, 2006:

	Remainder of 2006	2007	2008	2009	2010	2011 and thereafter	Total
Mortgages payable – principal	\$ 2,148	\$ 11,479	\$ 151,412	\$ 8,109	\$ 149,099	\$ 182,495	\$ 504,742
Mortgages payable – interest	7,865	31,109	26,271	19,837	16,077	31,186	132,345
Capital lease – principal	208	116	122	129	142	1,484	2,201
Capital lease – interest	24	129	123	116	103	408	903
Convertible debentures – principal	–	–	–	–	–	132,190	132,190
Convertible debentures – interest	4,037	8,074	8,074	8,074	8,074	12,278	48,611
Long-term land leases	544	2,179	2,183	2,203	2,203	85,632	94,944
Operating equipment leases	164	531	420	354	221	69	1,759
	\$ 14,990	\$ 53,617	\$ 188,605	\$ 38,822	\$ 175,919	\$ 445,742	\$ 917,695

The next material refinancing to occur will be in 2008 when \$145.4 million of long-term debt with a weighted average interest rate of 7.4% matures.

The long-term land leases require minimum annual average lease payments as outlined above and expire between 2023 and 2088. There are also future rental charges determined as a percentage of revenue that are not included in the amounts reflected above.

The REIT issued a redemption notice on April 26, 2006 to redeem the \$57.5 million of outstanding convertible debenture from the initial series due July 26, 2007 (“Initial Series – 9.75% Debentures”) on June 1, 2006. Prior to June 1, 2006 a total of \$53 million of the Initial Series – 9.75% Debentures were converted to 4,923,996 units of the REIT at the conversion price of \$10.75. The remaining Initial Series – 9.75% Debentures of \$4.5 million were redeemed at 95% of the volume-weighted average trading price of the Units on the TSX for the 20 consecutive trading days ending five trading days prior to the date of redemption. A total of 392,307 units were issued at the redemption price of \$11.57.

Also on April 26, 2006 the REIT entered into a bought deal term sheet to issue \$75 million of convertible unsecured subordinated debentures (“Series B – 6.00% Debentures”). These debentures were issued on May 16, 2006 and are convertible into trust units at a strike price of \$14.90, bear interest at 6.00% per annum payable semi-annually on May 31 and November 30 of each year and are due May 31, 2013. The trust units to be issued upon conversion of the Series B – 6.00% Debentures are 5,033,557.

DISTRIBUTIONS TO UNITHOLDERS

The following chart illustrates the distributable income that the REIT has generated relative to cash distributions paid to unitholders for the twelve months ended September 30, 2006 and for the years ended December 31, 2005, 2004 and 2003, the period ended December 31, 2002 and the cumulative period from the REIT's inception on July 26, 2002 to September 30, 2006:

	Year ended September 30, 2006	Year ended December 31, 2005	Year ended December 31, 2004	Year ended December 31, 2003	Period ended December 31, 2002 ⁽¹⁾	Cumulative since inception to September 30, 2006
Distributable income ⁽²⁾	\$ 60,635	\$ 48,721	\$ 44,269	\$ 39,455	\$ 25,263	\$ 211,269
Distributions	57,630	52,884	50,164	46,280	20,000	213,481
Distributable income in excess of (less than) distributions	3,005	(4,163)	(5,895)	(6,825)	5,263	(2,212)
Non-cash distributions made through the distribution reinvestment plan ("DRIP")	3,575	3,303	3,168	1,367	–	10,580
Distributable income in excess of (less than) cash distributions	\$ 6,580	\$ (860)	\$ (2,727)	\$ (5,458)	\$ 5,263	\$ 8,368
Payout ratios:						
Total distributions	95.0%	108.5%	113.3%	117.3%	79.2%	101.0%
Cash distributions (total distributions minus DRIP)	89.1%	101.8%	106.2%	113.8%	79.2%	96.0%

(1) For the period from July 26, 2002 to December 31, 2002

(2) Distributable income is calculated after deducting 4% of total hotel revenues as a reserve for future furniture, fixtures and equipment and capital improvements.

The REIT's payout ratio was 95.0% for the twelve months ended September 30, 2006 or 89.1% on a cash basis. On a cumulative basis from the inception of the REIT on July 26, 2002, the payout ratio has been 101.0% or 96.0% on a cash basis. Liquidity to fund distributions is generated from cash flow from operations, cash on hand, bank operating lines available and by the ability to finance certain unencumbered or under-leveraged assets.

Distributions to unitholders are approved by the REIT's Board of Trustees. In exercising their discretion to approve the level of distributions, the Trustees use forecasts prepared by management and other financial information to determine if sufficient cash flow will be available to fund distributions. Such financial information is subject to change due to the nature of the Canadian hotel industry which can be difficult to predict even in the short-run. This is due to the following factors:

1. Its exposure to the overall cyclical effects of the Canadian business environment,
2. The seasonal nature of the REIT's business,
3. The REIT's geographical diversity. InnVest's hotels are located in numerous regions throughout Canada each with its own unique characteristics,
4. Changing customer sentiment toward brands which the REIT's hotel properties use,
5. Changes in customer segmentation due to changing social, economic and political conditions, and
6. Numerous other macroeconomic, social and geopolitical factors which are beyond the control of the REIT.

All of these factors can have a material effect on the REIT's revenue and cost structure. An example is the significant impact of SARS on the Canadian hotel industry in 2003. As a result of the REIT's exposure to numerous factors which are beyond its control, it is difficult for management of the REIT to make predictions concerning distribution levels for future quarters therefore management asserts that it would not be prudent to provide investors or potential investors with forward-looking information regarding distribution levels.

CAPITAL RESOURCES

The REIT's cash position at September 30, 2006 was \$11.2 million, of which \$8.6 million is restricted under the REIT's trust indenture for the replacement of furniture, fixtures, and equipment and for capital improvements.

InnVest sets aside 4% of total hotel revenue for replacing furniture, fixtures and equipment and capital improvements. Capital expenditures committed and yet to be incurred at September 30, 2006 were \$1.1 million. The current expectation is that capital spending on the hotel portfolio will be approximately \$22 million for the year ending December 31, 2006.

The following chart shows the changes in the restricted cash balance for the three and nine months ended September 30, 2006 along with the comparable period:

	Three Months Ended Sept. 30, 2006	Three Months Ended Sept. 30, 2005	Nine Months Ended Sept. 30, 2006	Nine Months Ended Sept. 30, 2005
Opening balance	\$ 2,870	\$ 8,893	\$ 6,079	\$ 17,024
4% of revenues	4,685	4,275	11,688	9,927
Adjustment re discontinued operations	61	-	-	-
Transferred from operating cash	-	993	-	-
Initial reserve – Hotels Acquired	9,000	6,000	10,200	6,750
Capital expenditures	(8,021)	(10,930)	(19,372)	(24,470)
Closing balance	\$ 8,595	\$ 9,231	\$ 8,595	\$ 9,231

InnVest is not permitted to exceed certain financial leverage amounts under the terms of the Declaration of Trust. The REIT is permitted to hold indebtedness excluding convertible debentures up to a level of 50% of gross book value. InnVest calculates indebtedness in accordance with GAAP excluding non-interest bearing indebtedness, trade accounts payable, and any future income tax liability. We calculate gross book value as the total book value of assets on the REIT's balance sheet, plus the amount of accumulated depreciation and amortization, less any future income tax liabilities. Further, the REIT is permitted to have indebtedness and convertible debentures up to a level of 60% of gross asset value. At September 30, 2006, the REIT's leverage excluding and including convertible debentures was 39.6% and 49.9% respectively.

The REIT also had unused operating loan availability of \$25 million at September 30, 2006 and eight hotel properties which remained unencumbered. The REIT estimates that the unencumbered hotels could generate approximately \$45 million in mortgage proceeds. The REIT also has an unused acquisition facility of \$40 million available to acquire hotel properties and an unused loan facility of \$21.7 million available to fund 50% of capital expenditures.

During the nine months ended September 30, 2006, the REIT distributed \$44.2 million or \$1.125 per unit, of which \$2.7 million was distributed in units as part of the Distribution Reinvestment Plan ("DRIP"), at the rate of \$0.09375 per unit per month. A regular monthly distribution of \$0.09375 per unit for the month of September 2006 was paid on October 13, 2006.

InnVest expects to make cash distributions based on cash flow to be generated from operations and its borrowing capacity. Future growth is expected to be funded from borrowing capacity and through the issuance of trust units.

EQUITY

At September 30, 2006 a total of 54,849,502 units of the REIT were outstanding. There is only one class of trust units, with each unit eligible for one vote. For the nine months ended September 30, 2006 and subsequent, units of the REIT were issued as follows:

	Units	Amount
Balance at December 31, 2005	47,961,163	\$ 464,164
<i>First quarter activity of Units issued</i>		
DRIP	73,444	881
Executive compensation plan	14,636	182
Conversion of debentures	1,318,416	14,173
Balance at March 31, 2006	49,367,659	\$ 479,400
<i>Second quarter activity of Units issued</i>		
DRIP	76,922	907
Executive compensation plan	1,760	23
Conversion of debentures	4,931,996	54,815
Redemption of debentures	392,307	4,719
Balance at June 30, 2006	54,770,644	\$ 539,864
<i>Third quarter activity of Units issued</i>		
DRIP	76,929	954
Trustee compensation plan	1,929	28
Balance at September 30, 2006	54,849,502	\$ 540,846
<i>Activity subsequent to September 30, 2006</i>		
DRIP	25,442	322
Trustee compensation plan	1,741	27
Balance at November 8, 2006	54,876,685	\$ 541,195

At March 31, 2006 a total of \$57.5 million of the Initial Series – 9.75% Debentures remained outstanding. Of this amount \$53 million were converted to units of the REIT during the second quarter with the balance of \$4.5 million redeemed on June 1, 2006. A total of 5,316,303 were issued through the conversions and redemption in the second quarter.

A total of \$57.2 million of the Series A – 6.25% Debentures remained outstanding at September 30, 2006. These debentures are convertible into trust units at a strike price of \$12.50, bear interest at 6.25% per annum payable semi-annually on April 15 and October 15 of each year and are due April 15, 2011. The trust units to be issued upon conversion of the Series A – 6.25% Debentures are 4,575,200. A total of \$100 in Series A – 6.25% Debentures was converted into 8,000 units during the third quarter.

A total of \$75 million of the Series A – 6.00% Debentures remained outstanding at September 30, 2006. The Series B – 6.00% Debentures are convertible into trust units at a strike price of \$14.90, bear interest at 6.00% per annum payable semi-annually on May 31 and November 30 of each year and are due May 31, 2013. The trust units to be issued upon conversion of the Series B – 6.00% Debentures are 5,033,557.

RISKS AND UNCERTAINTIES

The REIT's risks and uncertainties remain substantially unchanged from the description provided in the MD&A for the year ended December 31, 2005, except as follows:

PROPOSED TAX CHANGES TO INCOME TRUSTS

On October 31, 2006, the Finance Minister proposed tax changes relating to income trusts. Indications are that real estate investment trusts will be excluded from this proposed legislation if they meet a number of tests. At this time, it

is too early to determine the impact, if any that the proposed legislation will have on InnVest. InnVest will review the detailed legislation when it becomes available and we will take necessary actions which are in the best interests of its Unitholders in order to qualify as a REIT under the proposed changes.

ANTICIPATED REORGANIZATION AND PROPOSED TAX CHANGES TO INCOME TRUSTS

The REIT obtained the approval of unitholders to effect a proposed reorganization (the "Reorganization"). The purpose of the Reorganization is to reorganize the REIT and its subsidiaries in order to achieve a more efficient and integrated operational structure that will position the REIT to pursue additional hotel acquisitions in accordance with its long-term objectives. It is anticipated that the REIT will achieve operating and other cost reductions and a more tax-efficient structure by virtue of the Reorganization.

In the third quarter, the REIT received an advanced ruling from the Canada Revenue Agency in respect of the Reorganization. The REIT obtained the requisite approval of unitholders at the annual and special meeting of unitholders held on May 17, 2006. In light of the October 31, 2006 announcement, the REIT intends to make certain changes to its reorganization plan and re-submit its request for an advanced ruling in the fourth quarter, and upon receipt of the advance ruling complete the Reorganization within the next six months.

OUTLOOK

In the third quarter, the REIT continued to benefit from the hotels acquired in 2005 and 2006, which were not owned in the prior year. This contributed \$2.8 million to hotel operating income during the third quarter. The base portfolio of hotels achieved a \$4.3 million increase in hotel operating income for the nine months ended September 30, 2006.

All regions in InnVest's portfolio are experiencing growth, with the strongest region being the West. Ontario, the REIT's largest concentration of hotels, continues to see sustained growth in top line and is expected to experience strong hotel operating income growth. Continued top line growth contributed to stabilized operating margins in the quarter.

Growth within its base portfolio and its 2006 acquisitions are expected to positively impact the REIT's operating results for the balance of 2006 and into 2007.

ACCOUNTING POLICIES

RELATED PARTY TRANSACTIONS

Franchise Business

The REIT's related party transactions between itself and its franchise business remain substantially unchanged from the description provided in the MD&A for the year ended December 31, 2005. Royalty payments paid to Choice Canada by the REIT on a net basis for the nine months ended September 30, 2006 totaled \$405.

Hotel Management

The REIT's related party transactions between itself and its hotel manager remain substantially unchanged from the description provided in the MD&A for the year ended December 31, 2005. Total fees paid under the management agreement to the hotel manager for the nine months ended September 30, 2006 were \$12.2 million. No management incentive fees were paid in the nine months ended September 30, 2006.

The manager of the hotel portfolio is Westmont, one of the largest privately held managers of hotels in the world. Westmont has approximately 5.75 years remaining on a 10-year master hotel management agreement to manage InnVest's hotel portfolio and is subject to non-competitive arrangements for limited service hotels in Canada.

HEDGING TRANSACTIONS

The REIT's hedging transactions remain substantially unchanged from the description provided in the MD&A for the year ended December 31, 2005.

CRITICAL ACCOUNTING ESTIMATES

There have been no changes in accounting policies since December 31, 2005 and management is not anticipating any significant changes for the remainder of the year. Effective January 1, 2007, the REIT will adopt the new CICA recommendations related to accounting for Financial Instruments. At this time, The REIT has not determined the impact, if any, to its consolidated financial statements.

CHANGES IN ACCOUNTING POLICIES

The REIT's changes in accounting policies remain substantially unchanged from the description provided in the MD&A for the year ended December 31, 2005 except as follows:

Other Real Estate Properties

Office and Retail properties include land, buildings and improvements are stated at cost less accumulated depreciation. Depreciation on the buildings is provided on a straight-line basis over their estimated useful life not to exceed 40 years.

The Retirement residence includes land, buildings and chattels. The building and chattels are stated at cost less accumulated depreciation. Depreciation on the buildings is provided on a straight-line basis over their estimated useful life not to exceed 40 years. Chattels are depreciated on a straight-line basis not to exceed seven years.

Asset Retirement Obligation

Effective April 1, 2006 the REIT adopted the guidelines contained in the CICA Emerging Issues Committee Abstract 159 Conditional Asset Retirement Obligations, and accordingly has retroactively recorded a conditional asset retirement obligation in accordance with Section 3110 Asset Retirement Obligations of the CICA Handbook. The REIT recorded a liability in the amount of \$1.3 million, a net increase in hotel properties of \$906 and a decrease in unitholders' equity of \$415 related to various environmental obligations for certain properties where the quantum of such costs and the timing for settlement is reasonably determinable. The obligation relates to the eventual removal of asbestos, underground storage tanks and Polychlorinated Biphenyls ("PCB's") and eventual remediation of land contamination. The asset will be amortized over the remaining life of the building. The liability will be accreted over the term of the obligations and accretion will be included in depreciation, amortization and accretion expense in the consolidated income statement.

Effectiveness of Internal Disclosure Controls

In accordance with Multilateral Instrument 52-109 respecting certification of disclosure in issuers' annual and interim filings, the Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of the REIT's internal disclosure controls as of and for the nine months ended September 30, 2006. The CEO and CFO concluded that the REIT's control procedures provide reasonable assurance that (i) information required to be disclosed by the REIT in its annual filings, interim filings or other reports filed or submitted by it under applicable securities legislation is recorded, processed, summarized and reported within the prescribed time periods, and (ii) material information regarding the REIT is accumulated and communicated to the REIT's management, especially its Chief Executive Officer and Chief Financial Officer, in a timely manner.

Forward-looking information

The preceding management's discussion and analysis contains forward looking or outlook information with respect to InnVest. Because forward-looking information addresses future events and conditions, it involves risk and uncertainties that could cause actual results to differ materially from those contemplated by the forward-looking information. These risks and uncertainties are discussed earlier in management's discussion and analysis, as well as the REIT's annual information form.

InnVest disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, unless required to do so by applicable securities laws.

CONSOLIDATED BALANCE SHEETS

(in thousands of dollars) (unaudited)	September 30, 2006	December 31, 2005
		Restated (Note 2)
ASSETS		
Current Assets		
Cash	\$ 2,634	\$ 5,893
Accounts receivable	17,801	10,122
Prepaid expenses and other assets	10,578	4,929
Assets held for sale (Note 17)	119	69
	31,132	21,013
Restricted cash	8,595	6,079
Hotel properties (Note 4)	1,140,378	1,036,309
Other real estate properties (Note 5)	16,715	-
Licence contracts (accumulated amortization \$5,506; December 31, 2005 – \$4,520)	20,814	21,800
Deferred financing and other assets (Note 6)	20,865	10,560
Assets held for sale (Note 17)	5,566	6,729
	\$ 1,244,065	\$ 1,102,490
LIABILITIES		
Current Liabilities		
Bank indebtedness (Note 7)	\$ -	\$ 7,100
Accounts payable and accrued liabilities	44,777	29,432
Distributions payable	5,139	4,496
Current portion of long-term debt (Note 8)	11,569	8,498
Liabilities related to assets held for sale (Note 17)	233	160
	61,718	49,686
Long-term debt and other obligations (Note 8)	496,733	426,625
Convertible debentures (Note 9)	127,133	125,917
Future income tax liability (Note 10)	126,061	140,386
Long-term debt related to assets held for sale (Note 17)	2,201	2,233
	813,846	744,847
UNITHOLDERS' EQUITY	430,219	357,643
	\$ 1,244,065	\$ 1,102,490

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

CONSOLIDATED STATEMENTS OF NET INCOME

(in thousands of dollars, except per unit amounts) (unaudited)	Three Months Ended Sept. 30, 2006	Three Months Ended Sept. 30, 2005	Nine Months Ended Sept. 30, 2006	Nine Months Ended Sept. 30, 2005
		Restated (Notes 2 and 17)		Restated (Notes 2 and 17)
Hotel revenues	\$ 117,119	\$ 105,539	\$ 290,265	\$ 243,449
Hotel expenses				
Operating expenses (Note 14)	59,704	52,490	160,278	131,617
Property taxes, rent and insurance	8,747	8,417	26,124	22,883
Management fees (Note 14)	3,921	3,561	9,765	8,216
	72,372	64,468	196,167	162,716
Hotel operating income	44,747	41,071	94,098	80,733
Other (income) and expenses				
Interest on mortgages	7,619	7,232	22,116	19,939
Convertible debentures interest and accretion	2,147	2,960	7,181	8,827
Corporate and administrative (Note 14)	1,071	923	3,444	2,817
Capital tax	327	218	1,149	1,005
Other business income, net (Note 16)	(1,904)	(1,191)	(3,255)	(2,264)
Other income	(152)	(57)	(275)	(165)
Depreciation, amortization and accretion	13,659	10,924	37,950	30,746
	22,767	21,009	68,310	60,905
Income before income tax (recovery) expense	21,980	20,062	25,788	19,828
Income tax (recovery) expense				
Current	(59)	118	(186)	525
Future	(1,265)	(1,444)	(14,171)	(1,479)
	(1,324)	(1,326)	(14,357)	(954)
Net income from continuing operations	23,304	21,388	40,145	20,782
Write down of assets held for sale (Note 17)	-	(211)	(1,000)	(1,682)
Income from discontinued operations (Note 17)	232	346	196	48
	232	135	(804)	(1,634)
Net income	\$ 23,536	\$ 21,523	\$ 39,341	\$ 19,148
Net income from continuing operations, per unit (Note 12)				
Basic	\$ 0.425	\$ 0.449	\$ 0.775	\$ 0.447
Diluted	\$ 0.395	\$ 0.412	\$ 0.763	\$ 0.446
Net income per unit (Note 12)				
Basic	\$ 0.429	\$ 0.452	\$ 0.760	\$ 0.411
Diluted	\$ 0.398	\$ 0.414	\$ 0.750	\$ 0.411
Net income (loss) from discontinued operations, per unit				
Basic	\$ 0.004	\$ 0.003	\$ (0.015)	\$ (0.036)
Diluted	\$ 0.003	\$ 0.002	\$ (0.013)	\$ (0.035)

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

CONSOLIDATED STATEMENTS OF UNITHOLDERS' EQUITY

(in thousands of dollars) (unaudited)	Units in \$	Net Income	Distributions	Executive Compen- sation	Holders' Conversion Option	Total
		Restated (Note 2)				
Balance December 31, 2004	\$ 438,652	\$ 40,499	\$ (116,444)	\$ 226	\$ 5,705	\$ 368,638
CHANGES DURING THE PERIOD						
Net income	–	19,148	–	–	–	19,148
Unit distributions (Note 13)	–	–	(39,404)	–	–	(39,404)
Issue of new units	18,870	–	–	–	–	18,870
Costs incurred regarding issue of new units	(100)	–	–	–	–	(100)
Distribution reinvestment						
plan units issued (Note 11)	2,470	–	–	–	–	2,470
Conversion of debentures	2,833	–	–	–	(108)	2,725
Vested executive compensation	283	–	–	(283)	–	–
Executive and trustee compensation (Note 11)	91	–	–	182	–	273
Balance September 30, 2005	\$ 463,099	\$ 59,647	\$ (155,848)	\$ 125	\$ 5,597	\$ 372,620
Balance December 31, 2005	\$ 464,164	\$ 57,033	\$ (169,328)	\$ 186	\$ 5,588	\$ 357,643
CHANGES DURING THE PERIOD						
Net income	–	39,341	–	–	–	39,341
Unit distributions (Note 13)	–	–	(44,150)	–	–	(44,150)
Distribution reinvestment						
plan units issued (Note 11)	2,742	–	–	–	–	2,742
Conversion of debentures	68,988	–	–	–	(2,556)	66,432
Redemption of debentures	4,719	–	–	–	(172)	4,547
Issue of new debentures	–	–	–	–	3,400	3,400
Vested executive compensation	152	–	–	(152)	–	–
Executive and trustee compensation (Note 11)	81	–	–	183	–	264
Balance September 30, 2006	\$ 540,846	\$ 96,374	\$ (213,478)	\$ 217	\$ 6,260	\$ 430,219

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands of dollars) (unaudited)	Three Months Ended Sept. 30, 2006	Three Months Ended Sept. 30, 2005	Nine Months Ended Sept. 30, 2006	Nine Months Ended Sept. 30, 2005
		Restated (Notes 2 and 17)		Restated (Notes 2 and 17)
OPERATING ACTIVITIES				
Net income from continuing operations	\$ 23,304	\$ 21,388	\$ 40,145	\$ 20,782
Add (deduct) items not affecting operations				
Depreciation, amortization and accretion	12,339	10,365	34,949	29,132
Amortization of deferred financing and other assets	1,320	559	3,001	1,614
Future income tax recovery	(1,265)	(1,444)	(14,171)	(1,479)
Non-cash executive and trustee compensation	89	91	264	273
Convertible debentures accretion	211	257	594	775
Discontinued operations	306	376	408	250
Changes in non-cash working capital	156	2,704	(1,107)	4,744
	36,460	34,296	64,083	56,091
FINANCING ACTIVITIES				
Repayment of long-term debt	(2,184)	(1,970)	(6,476)	(43,956)
Proceeds from long-term debt	49,800	23,790	63,300	126,933
Issue convertible debentures	-	-	75,000	-
Unit distributions	(14,459)	(12,665)	(40,765)	(36,878)
Decrease in bank indebtedness and loan payable	-	(25,200)	(7,100)	(11,000)
Discontinued operations repayment of debt	(11)	(4,857)	(32)	(4,931)
Deferred financing	(568)	(1,022)	(3,983)	(1,520)
Changes in non-cash working capital related to financing activities	16	-	381	(13)
	32,594	(21,924)	80,325	28,635
INVESTING ACTIVITIES				
Capital expenditures on hotel properties	(8,021)	(10,916)	(19,346)	(24,437)
Discontinued operations capital expenditures	-	(14)	(26)	(33)
Sale of discontinued assets	-	9,424	-	9,424
Other assets	(84)	(582)	(260)	(669)
Acquisition of hotel properties (Note 3)	(65,035)	(5,766)	(127,845)	(96,344)
Changes in restricted cash	(5,725)	(338)	(2,516)	7,793
Collection of vendor-take-back mortgage	-	-	200	-
Changes in non-cash working capital related to investing activities	(660)	(1,017)	2,126	66
	(79,525)	(9,209)	(147,667)	(104,200)
(Decrease) increase in cash during the period	(10,471)	3,163	(3,259)	(19,474)
Cash, beginning of period	13,105	-	5,893	22,637
Cash, end of period	\$ 2,634	\$ 3,163	\$ 2,634	\$ 3,163
Supplemental disclosure of cash flow information:				
Cash paid for interest	\$ 7,655	\$ 7,061	\$ 26,410	\$ 19,959
Cash paid for income taxes (including capital tax)	\$ 318	\$ 453	\$ 828	\$ 1,794

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

September 30, 2006 (all dollar amounts are in thousands, except unit and per unit amounts) (unaudited)

1. BASIS OF PRESENTATION

InnVest Real Estate Investment Trust (“InnVest” or the “REIT”) is an unincorporated open-ended real estate investment trust governed by the laws of Ontario. The REIT began operations on July 26, 2002. As at September 30, 2006, the REIT owns 137 Canadian hotels with 15,661 guest rooms operated under international brands and has a 50% interest in Choice Hotels Canada Inc. (“CHC”).

The accompanying unaudited interim consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles (“GAAP”). The accounting principles used in these financial statements are consistent with those used in the annual consolidated financial statements for the year ended December 31, 2005, except as disclosed in Note 2. These financial statements do not include all the information and disclosure required by GAAP for annual financial statements, and should be read in conjunction with the annual consolidated financial statements.

Revenues earned from hotel operations fluctuate throughout the year, with the third quarter being the highest due to the increased level of leisure travel in the summer months, and the first quarter being the lowest as leisure travel tends to be lower at that time of the year.

2. CHANGES IN ACCOUNTING POLICIES

The accounting policies followed in preparation of these financial statements are consistent with those as set out in the audited financial statements for the year ended December 31, 2005 except as follows:

OTHER REAL ESTATE PROPERTIES

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

Office and retail properties include land and buildings. The buildings are stated at cost less accumulated depreciation. Depreciation on the buildings is provided on a straight-line basis over their estimated useful life not to exceed 40 years.

The Retirement residence includes land, buildings and furniture, fixtures and equipment. The building and furniture, fixtures and equipment are stated at cost less accumulated depreciation. Depreciation on the buildings is provided on a straight-line basis over their estimated useful life not to exceed 40 years. Furniture, fixtures and equipment are depreciated on a straight-line basis not to exceed seven years.

ASSET RETIREMENT OBLIGATION

Effective April 1, 2006 the REIT adopted the guidelines contained in the Emerging Issues Committee Abstract No. 159 “Conditional Asset Retirement Obligations” and accordingly has retroactively recorded a conditional asset retirement obligation in accordance with Section 3110 Asset Retirement Obligations of the CICA Handbook. The REIT recorded a liability in the amount of \$1,343, a net increase in hotel properties of \$906 and a decrease in unitholders’ equity of \$415 related to various environmental obligations for certain properties where the quantum of such costs and the timing for settlement is reasonably determinable. The obligation relates to the eventual removal of asbestos, underground storage tanks and Polychlorinated Biphenyls (PCB’s) and eventual remediation of land contamination. The asset will be amortized over the remaining life of the building. The liability will be accreted over the term of the obligations and accretion will be included in depreciation, amortization and accretion expense in the consolidated statement of net income.

3. ASSET ACQUISITIONS

On March 3, 2006, the REIT purchased the Comfort Inn Leamington, Ontario for cash consideration of \$3,275.

During the second quarter, the REIT entered into two separate agreements to acquire four hotels with a total of 540 rooms for a combined purchase price of \$74,500 plus transaction costs. Two of the hotels are branded Delta hotels and are city centre located hotels in Sherbrooke and Trois Rivières, Quebec. These hotels operate in the full-service segment and include convention centres, office and retail space. The Trois Rivières location also includes a retirement home. The remaining two hotels are newly built hotels located in Burlington, Ontario, one of which is branded a Hilton Garden Inn and the other a Homewood Suites. The acquisitions were financed through the

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

assumption of \$14,327 of mortgages, a vendor-take-back loan of \$2,000 and cash. The two Burlington hotels' transaction closed on April 28, 2006, while the Delta hotels closed on May 25, 2006.

On September 19, 2006, the REIT acquired two Hiltons, a 571 room hotel in Quebec City and a 197 room hotel in Saint John. The purchase price of \$62,656 plus transaction costs was financed with the REIT's main lender for \$49,800 and cash for the remainder.

As at September 30, 2006, the REIT is continuing to evaluate the fair value of the net assets acquired, and based on this ongoing evaluation, the purchase price allocation may be adjusted in future periods.

	Leamington Comfort Inn	Burlington Hiltons	Quebec Deltas	Quebec City & Saint John Hiltons	Total
Cash	\$ 1	\$ 3	\$ 22	\$ 100	\$ 126
Current assets	21	112	195	1,985	2,313
Hotel properties	3,150	28,186	26,601	61,060	118,997
Other real estate	–	–	16,849	–	16,849
Other assets	110	56	4,850	4,076	9,092
	3,282	28,357	48,517	67,221	147,377
Assumption of existing long-term debt	–	(14,327)	–	–	(14,327)
Current liabilities	(7)	–	(1,019)	(2,053)	(3,079)
	\$ 3,275	\$ 14,030	\$ 47,498	\$ 65,168	\$ 129,971

The consideration paid consists of the following:

Cash	\$ 3,275	\$ 12,030	\$ 47,498	\$ 15,368	\$ 78,171
New mortgage debt	–	–	–	49,800	49,800
Loan payable	–	2,000	–	–	2,000
	\$ 3,275	\$ 14,030	\$ 47,498	\$ 65,168	\$ 129,971

4. HOTEL PROPERTIES

	Cost	Accumulated Depreciation	September 30, 2006 Net Book Value	December 31, 2005 Net Book Value
Land	\$ 93,681	\$ –	\$ 93,681	\$ 83,371
Buildings	1,080,381	92,070	988,311	898,390
Furniture, fixtures and equipment	112,636	54,250	58,386	54,548
	\$ 1,286,698	\$ 146,320	\$ 1,140,378	\$ 1,036,309

5. OTHER REAL ESTATE PROPERTIES

	Cost	Accumulated Depreciation	September 30, 2006 Net Book Value	December 31, 2005 Net Book Value
Land	\$ 1,385	\$ –	\$ 1,385	\$ –
Buildings	15,305	118	15,187	–
Furniture, fixtures and equipment	159	16	143	–
	\$ 16,849	\$ 134	\$ 16,715	\$ –

Other real estate includes the office and retail properties and retirement residence which was acquired along with the two hotels as part of the Quebec Deltas acquisition which closed May 25, 2006 (Note 3).

6. DEFERRED FINANCING AND OTHER ASSETS

	Cost	Accumulated Amortization	September 30, 2006 Net Book Value	December 31, 2005 Net Book Value
Deferred financing	\$ 16,528	\$ 7,893	\$ 8,635	\$ 6,589
Other assets	13,797	1,567	12,230	3,971
	\$ 30,325	\$ 9,460	\$ 20,865	\$ 10,560

7. BANK INDEBTEDNESS

The REIT has a \$25,000 operating loan facility that bears interest at Canadian bank prime plus 0.5% or Canadian Bankers' Acceptance rate plus 1.5%. It is secured by nine properties and is payable on demand. At September 30, 2006, the REIT had drawn \$nil on this facility (December 31, 2005 – \$7,100).

8. LONG-TERM DEBT AND OTHER OBLIGATIONS

	September 30, 2006	December 31, 2005
		Restated (Note 2)
Mortgages payable	\$ 504,742	\$ 431,680
Capital lease and other obligations	2,201	2,113
	506,943	433,793
Less current portion	11,569	8,498
Total long-term debt	495,374	425,295
Asset retirement obligation	1,359	1,330
Total long-term debt and other obligations	\$ 496,733	\$ 426,625

Substantially all of the REIT's assets have been pledged as security under various debt agreements. At September 30, 2006, long-term debt had a weighted average interest rate of 6.5% (December 31, 2005 – 6.3%). The long-term debt is repayable in average monthly payments of principal and interest totalling \$3,514 (December 31, 2005 – \$2,982) per month, and matures at various dates from July 26, 2008 to October 1, 2017.

Scheduled repayment of long-term debt is as follows:

2006 (remainder of the year)	\$ 2,356
2007	11,595
2008	151,534
2009	8,238
2010	149,241
2011 and thereafter	183,979
	\$ 506,943

The current portion of long-term debt on the balance sheet is based on the year ending September 30, 2007, whereas the repayment schedule above reflects the fiscal year.

The estimated fair value of the REIT's long-term debt at September 30, 2006 was approximately \$513,358 (December 31, 2005 – \$440,904). This estimate was determined by discounting expected cash flows at the interest rates currently being offered to the REIT for debt of the same remaining maturities.

Long-term debt includes \$68,671 (December 31, 2005 – \$69,896) of mortgages payable, which are subject to floating interest rates. Interest expense will increase by \$687 for every 1% increase in the base Bankers' Acceptance rate.

9. CONVERTIBLE DEBENTURES

The details of the three series of convertible debentures are outlined in the table below:

	Issue Date	Maturity Date	Interest Rate	Original Face Amount	Converted to Trust Units	Face Amount Outstanding	Holders' Conversion Options	Accretion	Sept. 30, 2006	Dec. 31, 2005
Initial										
Debtentures	July 26, 2002	June 30, 2007	9.75%	\$ 75,000	\$ 75,000	\$ -	\$ -	\$ -	\$ -	\$ 70,773
Series A										
Debtentures	April 2, 2004	April 15, 2011	6.25%	57,500	310	57,190	2,860	1,022	55,352	55,144
Series B										
Debtentures	May 16, 2006	May 31, 2013	6.00%	75,000	-	75,000	3,400	181	71,781	-
				\$ 207,500	\$ 75,310	\$ 132,190	\$ 6,260	\$ 1,203	\$ 127,133	\$ 125,917

On April 26, 2006 the REIT issued a redemption notice for all issued and outstanding Initial Series Debentures. The redemption was effective June 1, 2006. There was no gain or loss on the redemption of the outstanding Initial Series Debentures.

On May 16, 2006 the REIT announced the closing on a bought deal basis of \$75,000 6% convertible unsecured subordinated debentures ("Series B – 6.00% Debentures"). These debentures are convertible into trust units at a strike price of \$14.90, bear interest at 6.00% per annum payable semi-annually on May 31 and November 30 of each year and are due May 31, 2013. The trust units to be issued upon conversion of the Series B – 6.00% Debentures are 5,033,557.

10. FUTURE INCOME TAX LIABILITY

Future income taxes are the result of temporary differences between tax bases of assets and liabilities and their carrying amounts for accounting purposes. Such temporary differences are then measured using substantively enacted tax rates that will be in effect when these differences are expected to reverse. In June 2006, the federal general corporate income tax rate reductions, among other things, were enacted. The federal corporate income tax rate reductions were as follows: 20.5% effective January 1, 2008; 20% effective January 1, 2009; and 19% effective January 1, 2010. Since the majority of InnVest REIT's temporary differences are expected to reverse in 2010 and onward, a future income tax recovery of \$11,575 relating to these federal rate reductions was recognized in the consolidated statement of net income at the end of June 30, 2006.

11. UNITHOLDERS' EQUITY

The REIT is authorized to issue an unlimited number of units, each of which represents an equal undivided beneficial interest in any distributions from the REIT. All units are of the same class with equal rights and privileges.

	Units	Amount
Balance as at December 31, 2004	45,815,071	\$ 438,652
New units issued, net of costs	1,553,345	18,770
Units issued under distribution reinvestment plan	208,929	2,470
Units issued on conversion of debentures	262,876	2,833
Units issued for vested executive compensation	22,681	283
Units issued under trustee compensation plan	7,789	91
Balance at September 30, 2005	47,870,691	\$ 463,099
Balance as at December 31, 2005	47,961,163	\$ 464,164
Units issued under distribution reinvestment plan	227,295	2,742
Units issued on conversion of debentures	6,250,412	68,988
Units issued on redemption of debentures	392,307	4,719
Units issued for vested executive compensation	12,218	152
Units issued under trustee compensation plan	6,107	81
Balance at September 30, 2006	54,849,502	\$ 540,846

TRUSTEE COMPENSATION PLAN

The members of the Board of Trustees receive 50% of their annual retainer in units (based on the then current market price of the units). The REIT has set aside 100,000 units in reserve for this purpose. The balance in this reserve account at September 30, 2006 is 55,502 units. Under the Trustee Compensation Plan, 6,107 units were issued during the nine months ended September 30, 2006 (nine months ended September 30, 2005 – 7,789 units).

EXECUTIVE COMPENSATION PLAN

The senior executives participate in the executive compensation plan under which units are granted by the Board of Trustees from time to time. The REIT has reserved a maximum of 1,000,000 units for issuance under the plan. The balance in this reserve account at September 30, 2006 is 870,432 units. A unit granted through the plan entitles the holder to receive, on the vesting date, the then current fair market value of the unit plus the value of the cash distributions that would have been paid on the unit if it had been issued on the date of grant assuming the reinvestment of the distribution into REIT units. The payment will be satisfied through the issuance of units.

The following table summarizes the status of the executive compensation plan at September 30, 2006, excluding granted units which have fully vested:

	Unvested Executive units	Units Accumulated from Distributions	Total Units
January 1, 2003 – granted	17,846	7,440	25,286
January 1, 2004 – granted	10,218	3,060	13,278
January 1, 2005 – granted	13,118	2,278	15,396
January 1, 2006 – granted	12,968	905	13,873
January 1, 2006 – units vested	(8,923)	(3,295)	(12,218)
	45,227	10,388	55,615

On March 5, 2006, the Board of Trustees approved the granting of 12,968 units effective as of January 1, 2006. These units vest equally on the third and fourth anniversary of the effective date of grant.

DISTRIBUTION REINVESTMENT PLAN ("DRIP")

The REIT has a DRIP whereby eligible Canadian unitholders may elect to have their distributions of income from the REIT automatically reinvested in additional units. Unitholders who so elect will receive a further bonus distribution of units equal in value to 3% of each distribution that was reinvested.

12. PER UNIT INFORMATION

Net income per unit calculations are based on the following:

	Three Months Ended September 30, 2006		Three Months Ended September 30, 2005	
		Weighted Average Units		Weighted Average Units
Net income from continuing operations – basic	\$ 23,304	54,811,022	\$ 21,388	47,655,770
Convertible debentures interest and accretion	2,148	9,608,757	2,960	11,406,615
Dilutive effect of executive compensation plan	–	55,033	–	56,416
Net income from continuing operations – diluted	\$ 25,452	64,474,812	\$ 24,348	59,118,801

	Nine Months Ended September 30, 2006		Nine Months Ended September 30, 2005	
		Weighted Average Units		Weighted Average Units
Net income from continuing operations – basic	\$ 40,145	51,777,943	\$ 20,782	46,539,533
Convertible debentures interest and accretion	4,848	7,105,464	–	–
Dilutive effect of executive compensation plan	–	53,824	–	68,056
Net income from continuing operations – diluted	\$ 44,993	58,937,231	\$ 20,782	46,607,589

	Three Months Ended September 30, 2006		Three Months Ended September 30, 2005	
		Weighted Average Units		Weighted Average Units
Net income – basic	\$ 23,536	54,811,022	\$ 21,523	47,655,770
Convertible debentures interest and accretion	2,148	9,608,757	2,960	11,406,615
Dilutive effect of executive compensation plan	–	55,033	–	56,416
Net income – diluted	\$ 25,684	64,474,812	\$ 24,483	59,118,801

	Nine Months Ended September 30, 2006		Nine Months Ended September 30, 2005	
		Weighted Average Units		Weighted Average Units
Net income – basic	\$ 39,341	51,777,943	\$ 19,148	46,539,533
Convertible debentures interest and accretion	4,848	7,105,464	–	–
Dilutive effect of executive compensation plan	–	53,824	–	68,056
Net income – diluted	\$ 44,189	58,937,231	\$ 19,148	46,607,589

Distributable income per unit calculations are based on the following (Note 13):

	Three Months Ended September 30, 2006		Three Months Ended September 30, 2005	
		Weighted Average Units		Weighted Average Units
Distributable income – basic	\$ 31,538	54,811,022	\$ 27,385	47,655,770
Convertible debentures interest	1,937	9,608,757	2,703	11,406,615
Dilutive effect of executive compensation plan	–	55,033	–	56,416
Distributable income – diluted	\$ 33,475	64,474,812	\$ 30,088	59,118,801

	Nine Months Ended September 30, 2006		Nine Months Ended September 30, 2005	
		Weighted Average Units		Weighted Average Units
Distributable income – basic	\$ 53,561	51,777,943	\$ 41,647	46,539,533
Convertible debentures interest	6,586	10,072,664	8,052	11,432,690
Dilutive effect of executive compensation plan	–	53,824	–	68,056
Distributable income – diluted	\$ 60,147	61,904,431	\$ 49,699	58,040,279

The impact of some of the convertible debentures has been excluded from some of the calculations because the impact of the conversion would not be dilutive.

13. DISTRIBUTABLE INCOME

Distributions to unitholders are computed based on distributable income as defined by the Declaration of Trust.

Distributable income is a measure of cash flow that is not defined under Canadian GAAP, and accordingly, may not be comparable to similar measures used by other issuers. Distributable income per unit has been calculated on a basis consistent with that prescribed by Canadian GAAP for calculating earnings per unit.

Distributable income is defined as net income in accordance with Canadian GAAP, subject to certain adjustments as set out in the Declaration of Trust, including adding back depreciation and amortization, amortization of fair value debt adjustment and future income tax (recovery) expense, excluding any gains or losses on the disposition of real property and future income taxes, deducting the amount calculated, at 4% of hotel revenues, for the reserve for the replacement of furniture, fixtures and equipment and capital improvements, the accretion on convertible debentures that is included in the computation of net income, and making any other adjustments determined by the trustees of the REIT in their discretion.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005
Net income	\$ 23,536	\$ 21,523
Add (deduct)		
Depreciation, amortization and accretion	13,682	11,005
Future income tax recovery	(1,265)	(1,444)
Reserve for replacement of furniture, fixtures and equipment and capital improvements	(4,746)	(4,275)
Convertible debentures accretion	211	257
Non-cash executive and trustee compensation	86	91
Deferred land lease expense and retail lease income, net	34	17
Writedown of asset held for sale	–	211
	8,002	5,862
Distributable income	31,538	27,385
Distributable income in excess of distributions	16,121	13,963
Distributions	\$ 15,417	\$ 13,422
Distributable income per unit – basic	\$ 0.575	\$ 0.575
– diluted	\$ 0.519	\$ 0.509

	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005
Net income	\$ 39,341	\$ 19,148
Add (deduct)		
Depreciation, amortization and accretion	38,139	31,158
Future income tax recovery	(14,171)	(1,479)
Reserve for replacement of furniture, fixtures and equipment and capital improvements	(11,688)	(9,927)
Convertible debentures accretion	595	775
Non-cash executive and trustee compensation	261	273
Deferred land lease expense and retail lease income, net	84	17
Writedown of asset held for sale	1,000	1,682
	14,220	22,499
Distributable income	53,561	41,647
Distributions in excess of distributable income	9,411	2,243
Distributions	\$ 44,150	\$ 39,404
Distributable income per unit – basic	\$ 1.034	\$ 0.895
– diluted	\$ 0.972	\$ 0.856

14. MANAGEMENT AGREEMENTS

On July 26, 2002, the REIT entered into a Management Agreement for hotel management and accounting services and an Administrative Services Agreement (the “Agreements”) with Westmont Hospitality Management Canada Limited (“Westmont”).

The Agreements have an initial term of 10 years with two successive five-year renewal terms, subject to the consent of Westmont and approval of the REIT. The Agreements will expire July 25, 2012. The Agreements provide for the payment of an annual management fee to Westmont in an amount equal to 3.375% of gross revenues during the term of the Agreements, including renewal periods. In addition, Westmont may receive an annual incentive fee if the REIT achieves distributable income (see Note 13) in excess of \$1.25 per unit. No management incentive fees were paid during the periods presented. Accounting fees are calculated based on a fixed charge per room which increases by the Consumer Price Index change annually.

In addition to the base management fee and incentive fee, Westmont is entitled to reasonable fees based on a percentage of the cost of purchasing certain goods and supplies and certain construction costs and capital expenditures, fees for accounting services, reasonable out-of-pocket costs and expenses (other than general and administrative expenses or overhead costs except as otherwise provided in the Administrative Services Agreement) and project management and general contractor service fees related to hotel renovations managed by Westmont. During the three and nine months ended September 30, 2006 and 2005, the fees charged to the REIT pursuant to the Agreements were as follows:

	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005
Fees from continuing operations:		
Management fees	\$ 3,754	\$ 3,561
Accounting services (included in hotel operating expenses)	575	540
Administrative services (included in corporate and administrative expenses)	144	126
Project management and general contractor services (capitalized to hotel properties)	125	230
Fees from discontinued operations	35	233
	\$ 4,633	\$ 4,690

	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005
Fees from continuing operations:		
Management fees	\$ 9,570	\$ 8,216
Accounting services (included in hotel operating expenses)	1,708	1,522
Administrative services (included in corporate and administrative expenses)	419	385
Project management and general contractor services (capitalized to hotel properties)	419	513
Fees from discontinued operations	87	402
	\$ 12,203	\$ 11,038

In addition, salaries of REIT employees paid by Westmont and reimbursed by the REIT were \$157 (September 30, 2005 – \$154). Included in accounts payable and accrued liabilities are amounts outstanding at September 30, 2006 totalling \$1,479 (December 31, 2005 – \$977).

15. SEGMENTED FINANCIAL INFORMATION

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

	Western	Ontario	Quebec	Atlantic	Total
Three months ended September 30, 2006					
Hotel revenues	\$ 12,140	\$ 67,539	\$ 24,247	\$ 13,193	\$ 117,119
Hotel expenses	6,852	44,037	14,769	6,714	72,372
Hotel operating income	\$ 5,288	\$ 23,502	\$ 9,478	\$ 6,479	\$ 44,747
Three months ended September 30, 2005					
Hotel revenues	\$ 11,065	\$ 62,712	\$ 19,559	\$ 12,203	\$ 105,539
Hotel expenses	6,406	41,192	10,845	6,025	64,468
Hotel operating income	\$ 4,659	\$ 21,520	\$ 8,714	\$ 6,178	\$ 41,071
Nine months ended September 30, 2006					
Hotel revenues	\$ 29,612	\$ 177,489	\$ 54,629	\$ 28,535	\$ 290,265
Hotel expenses	18,603	124,195	35,886	17,483	196,167
Hotel operating income	\$ 11,009	\$ 53,294	\$ 18,743	\$ 11,052	\$ 94,098
Nine months ended September 30, 2005					
Hotel revenues	\$ 25,975	\$ 145,124	\$ 45,509	\$ 26,841	\$ 243,449
Hotel expenses	17,342	100,683	28,339	16,352	162,716
Hotel operating income	\$ 8,633	\$ 44,441	\$ 17,170	\$ 10,489	\$ 80,733
Capital expenditures					
Three months ended					
September 30, 2006	\$ 373	\$ 6,398	\$ 688	\$ 560	\$ 8,019
Three months ended					
September 30, 2005	\$ 692	\$ 6,890	\$ 909	\$ 2,425	\$ 10,916
Capital expenditures					
Nine months ended					
September 30, 2006	\$ 926	\$ 14,791	\$ 2,129	\$ 1,500	\$ 19,346
Nine months ended					
September 30, 2005	\$ 2,098	\$ 15,773	\$ 1,810	\$ 4,756	\$ 24,437
Hotel properties					
September 30, 2006	\$ 73,903	\$ 682,221	\$ 267,745	\$ 116,509	\$ 1,140,378
December 31, 2005	\$ 75,969	\$ 657,390	\$ 194,056	\$ 108,894	\$ 1,036,309

16. OTHER BUSINESS INCOME

	Franchise Business	Retail/ Office	Retirement Residence	Three months Ended Sept. 30, 2006	Three months Ended Sept. 30, 2005
Revenues	\$ 1,876	\$ 696	\$ 272	\$ 2,844	\$ 1,759
Expenses	569	241	129	939	568
Other business income, net	\$ 1,306	\$ 454	\$ 143	\$ 1,904	\$ 1,191

	Franchise Business	Retail/ Office	Retirement Residence	Nine months Ended Sept. 30, 2006	Nine months Ended Sept. 30, 2005
Revenues	\$ 3,962	\$ 947	\$ 384	\$ 5,294	\$ 3,622
Expenses	1,493	350	195	2,038	1,358
Other business income, net	\$ 2,470	\$ 597	\$ 188	\$ 3,255	\$ 2,264

Other business income includes Franchise Business Income, which is InnVest's 50% share of Choice Canada's operations and the net income from the non-hotel properties acquired as part of the Quebec Deltas acquisition (Note 3).

17. ASSETS HELD FOR SALE AND DISCONTINUED OPERATIONS

On April 18, 2006, the REIT reclassified one Ontario hotel property to assets held for sale. At September 30, 2006, the REIT reclassified a second hotel property, in Atlantic Canada, to assets held for sale. The long-term debt of \$2,201 for these assets is with the REIT's main mortgage lender and can be repaid at any time without penalty. This debt matures on July 26, 2008.

Discontinued operations for the three and nine months ended September 30, 2006 and 2005 are as follows:

	Three Months Ended Sept. 30, 2006	Three Months Ended Sept. 30, 2005	Nine Months Ended Sept. 30, 2006	Nine Months Ended Sept. 30, 2005
Hotel revenues	\$ 815	\$ 1,343	\$ 1,916	\$ 4,753
Hotel expenses				
Operating expenses	445	755	1,207	3,282
Property taxes, rent and insurance	47	23	146	405
Management fees	28	43	65	160
	520	821	1,418	3,847
Hotel operating income	295	522	498	906
Interest on mortgages	40	95	113	446
Depreciation and amortization	23	81	189	412
	63	176	302	858
Income from discontinued operations	232	346	196	48
Write down of assets held for sale	–	(211)	(1,000)	(1,682)
Net income from discontinued operations	\$ 232	\$ 135	\$ (804)	\$ (1,634)

18. SUBSEQUENT EVENT

On October 31, 2006, the Minister of Finance, Canada proposed tax changes relating to income trusts under a Tax Fairness Plan for Canadians. Indications are that real estate investment trusts will be excluded from this proposed legislation if they meet a number of conditions relating to the nature of their income and investments. The Minister of Finance did not announce a release date for detailed legislation to implement the Tax Fairness Plan. Until the detail of the proposed legislation is made public, it is not possible to determine the impact, if any on the REIT.

19. COMPARATIVE INFORMATION

Certain prior period amounts have been reclassified to conform to the current period presentation.

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