

Consolidated Financial Statements

Lakeview Hotel Real Estate Investment Trust

June 30, 2008

(Unaudited)

**LAKEVIEW HOTEL REAL ESTATE
INVESTMENT TRUST**

Supplement to Consolidated Financial Statements
for the Six Months ended June 30, 2008 and 2007

**NOTICE OF NO AUDITOR REVIEW OF INTERIM FINANCIAL
STATEMENTS**

Under National Instrument 51-109 Part 4 Subsection 4.3 (3)(a), if an auditor has not performed a review of interim financial statements, the statements must be accompanied by a notice indicating that they have not been reviewed by an auditor.

The unaudited interim financial statements of the Lakeview Hotel Real Estate Investment Trust for the six months ended June 30, 2008 and 2007 were prepared by, and are the responsibility of, the Trust's management.

The Lakeview Hotel Real Estate Investment Trust's independent auditor did not perform a review of these financial statements in accordance with the standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statements by an entity's auditor.

Lakeview Hotel Real Estate Investment Trust

CONSOLIDATED BALANCE SHEETS

Unaudited

	June 30 2008 \$	December 31 2007 \$
		(audited)
ASSETS		
Current		
Cash and cash equivalents	2,533,443	3,883,533
Reserve fund <i>[note 3]</i>	1,571,344	1,237,214
Accounts receivable	2,499,901	2,030,665
Inventory	197,296	142,103
Prepaid expenses	1,197,787	301,449
Total current assets	7,999,771	7,594,964
Deposits held in trust	400,000	—
Mortgages receivable <i>[note 4]</i>	4,038,429	—
Franchise fees, licenses and pre-opening costs <i>[note 5]</i>	162,434	156,432
Income properties <i>[notes 2,6,8,10, and 14]</i>	153,026,860	144,810,596
Investment in Lakeview Flag Licensing General Partnership <i>[note 7]</i>	59,275	40,367
	165,686,769	152,602,359
LIABILITIES AND UNITHOLDERS' EQUITY		
Current		
Accounts payable and accrued liabilities <i>[note 14]</i>	3,047,047	2,772,776
Distributions payable	707,384	707,188
Current portion of mortgages payable <i>[note 10]</i>	2,290,985	2,211,080
Total current liabilities	6,045,416	5,691,044
Debentures <i>[note 8]</i>	9,434,360	—
Convertible debentures <i>[note 9]</i>	22,991,176	14,318,230
Mortgages payable <i>[note 10]</i>	79,095,977	80,158,092
Future income tax liability <i>[note 17]</i>	730,000	734,000
Total liabilities	118,296,929	100,901,366
Unitholders' equity	47,389,840	51,700,993
	165,686,769	152,602,359

See accompanying notes

On behalf of the Board of Trustees:

"Gary Coleman"
Trustee

"Keith Levit"
Trustee

Lakeview Hotel Real Estate Investment Trust

CONSOLIDATED BALANCE SHEETS COMPREHENSIVE LOSS

Unaudited

	Three Months Ended		Six Months Ended	
	June 30		June 30	
	2008	2007	2008	2007
	\$	\$	\$	\$
REVENUE				
Rooms	8,321,629	5,400,496	16,283,839	11,204,415
Food, beverage and gift shop	939,012	950,650	2,043,748	1,893,261
Interest and miscellaneous	276,913	150,765	503,694	307,182
	9,537,554	6,501,911	18,831,281	13,404,858
EXPENSES				
Amortization				
Franchise fees, licenses and pre-opening costs	11,617	4,949	23,938	9,899
Income properties	1,522,152	1,016,596	2,939,962	1,889,914
Food, beverage and gift shop	381,441	409,770	829,967	801,587
General and administration <i>[note 14]</i>	1,859,314	1,645,921	3,545,893	2,875,830
Insurance	73,370	55,789	151,979	109,079
Interest				
Loan and other	6,127	46,831	9,983	59,060
Mortgages and debentures	2,188,627	921,815	3,998,228	1,612,790
Maintenance	241,705	135,960	476,771	264,532
Marketing <i>[note 14]</i>	624,093	383,177	1,264,879	703,233
Property taxes	479,680	347,465	838,710	583,030
Salaries and benefits	2,435,399	1,676,576	4,805,690	3,167,400
Supplies	218,184	204,349	445,481	347,913
Utilities	358,924	220,589	785,878	498,106
	10,400,633	7,069,787	20,117,359	12,922,373
Income (loss) before the following	(863,079)	(567,876)	(1,286,078)	482,485
Income from Lakeview Flag Licensing General Partnership <i>[note 7]</i>	156,913	114,737	318,298	233,253
Income (loss) before income taxes	(706,166)	(453,139)	(967,780)	715,738
(Provision for) recovery of income taxes - future	—	(1,184,100)	4,000	(1,184,100)
Net loss and comprehensive loss for the period	(706,166)	(1,637,239)	(963,780)	(468,362)
Basic and diluted net loss and comprehensive loss per Unit <i>[note 13]</i>	(0.037)	(0.086)	(0.050)	(0.025)

See accompanying notes

Lakeview Hotel Real Estate Investment Trust

**CONSOLIDATED BALANCE SHEETS
UNITHOLDERS' EQUITY**

Unaudited

	Three Months Ended		Six Months Ended	
	June 30		June 30	
	2008	2007	2008	2007
	\$	\$	\$	\$
Unitholders' capital <i>[note 11]</i>				
Balance, beginning of period	59,021,720	57,097,038	59,021,720	55,901,339
Conversion of debentures	18,438	1,519,032	18,438	2,714,731
Balance, end of period	59,040,158	58,616,070	59,040,158	58,616,070
Equity portion of convertible debentures				
Balance, beginning of period	2,883,536	529,231	2,883,536	823,836
Issuance of convertible debentures <i>[note 9]</i>	954,268	3,062,813	954,268	3,062,813
Conversion of debentures	(1,759)	(383,863)	(1,759)	(678,468)
Issuance costs	(74,997)	(213,693)	(74,997)	(213,693)
Balance, end of period	3,761,048	2,994,488	3,761,048	2,994,488
Contributed capital				
Balance, beginning of period	345,900	45,000	345,900	45,000
Issuance of Unit options <i>[note 12]</i>	—	304,500	—	304,500
Balance, end of period	345,900	349,500	345,900	349,500
Accumulated earnings				
Balance, beginning of period	2,555,403	3,725,483	2,813,017	2,556,606
Net loss and comprehensive loss for the period	(706,166)	(1,637,239)	(963,780)	(468,362)
Balance, end of period	1,849,237	2,088,244	1,849,237	2,088,244
Accumulated distributions				
Balance, beginning of period	(15,484,743)	(7,029,265)	(13,363,180)	(5,011,551)
Distributions declared <i>[note 11]</i>	(2,121,760)	(2,090,788)	(4,243,323)	(4,108,502)
Balance, end of period	(17,606,503)	(9,120,053)	(17,606,503)	(9,120,053)
Unitholders' equity, end of period	47,389,840	54,928,249	47,389,840	54,928,249

See accompanying notes

Lakeview Hotel Real Estate Investment Trust

CONSOLIDATED STATEMENTS OF CASH FLOWS

Unaudited	Three Months Ended		Six Months Ended	
	June 30		June 30	
	2008	2007	2008	2007
	\$	\$	\$	\$
OPERATING ACTIVITIES				
Net loss for the period	(706,166)	(1,637,239)	(963,780)	(468,362)
Add (deduct) items not involving cash				
Amortization of income properties	1,522,152	1,016,596	2,939,962	1,889,914
Amortization of franchise fees, licenses and pre-opening costs	11,617	4,949	23,938	9,899
Compensation costs of Unit options <i>[note 12]</i>	—	304,500	—	304,500
Income from Lakeview Flag Licensing General Partnership	(156,913)	(114,737)	(318,298)	(233,253)
Accretion on debt component of convertible debentures	189,198	64,054	354,807	106,090
Accretion of debentures	38,462	—	39,481	—
Accretion of mortgages payable	51,005	29,146	101,043	53,475
Decretion of mortgages receivable <i>[note 4]</i>	2,296	—	2,296	—
Future income tax expense (recovery)	—	1,184,100	(4,000)	1,184,100
	951,651	851,369	2,175,449	2,846,363
Net change in non-cash working capital balances related to operations	(1,598,746)	(447,496)	(1,475,756)	(539,793)
Cash provided by (used in) operating activities	(647,095)	403,873	699,693	2,306,570
INVESTING ACTIVITIES				
Acquisition of income properties, cash consideration <i>[note 2]</i>	(10,028,181)	(45,492,961)	(10,028,181)	(55,689,077)
Additions to income properties	(668,475)	(740,886)	(1,132,720)	(1,475,024)
Deposits held in trust for hotel acquisition	9,918,683	—	(400,000)	—
Increase in franchise fees, licenses and pre-opening costs	(29,940)	(33,684)	(29,940)	(33,684)
Advance of mortgages receivable <i>[note 4]</i>	(4,000,000)	—	(4,000,000)	—
Transaction costs on advance of mortgages receivable <i>[note 4]</i>	(40,725)	—	(40,725)	—
Distributions from Lakeview Flag Licensing General Partnership	154,840	129,850	299,390	215,600
Cash used in investing activities	(4,693,798)	(46,137,681)	(15,332,176)	(56,982,185)
FINANCING ACTIVITIES				
Unitholders' distributions				
Class A	(2,066,710)	(2,035,738)	(4,133,223)	(3,998,435)
Exchangeable Units	(55,050)	(55,050)	(110,100)	(110,067)
Proceeds from loan	2,800,000	1,750,000	2,800,000	2,500,000
Repayment of loan	(2,800,000)	(1,800,000)	(2,800,000)	(1,800,000)
Proceeds from mortgages	—	32,670,000	—	32,670,000
Repayment of mortgages	(551,003)	(272,995)	(1,083,253)	(511,342)
Proceeds of debentures <i>[note 8]</i>	—	—	10,250,000	—
Proceeds of convertible debentures <i>[notes 9 [c] and [d]]</i>	10,000,000	18,000,000	10,000,000	18,000,000
Financing costs on mortgages and debentures	(815,047)	(1,629,961)	(1,641,031)	(1,638,343)
Cash provided by financing activities	6,512,190	46,626,256	13,282,393	45,111,813
Net increase (decrease) in cash and cash equivalents during the period	1,171,297	892,448	(1,350,090)	(9,563,802)
Cash and cash equivalents, beginning of period	1,362,146	775,351	3,883,533	11,231,601
Cash and cash equivalents, end of period	2,533,443	1,667,799	2,533,443	1,667,799
Supplemental cash flow information				
Cash paid for interest	2,092,543	783,646	3,390,346	1,383,964

See accompanying notes

Lakeview Hotel Real Estate Investment Trust

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2008

Unaudited

1. ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Organization and principles of consolidation

Lakeview Hotel Real Estate Investment Trust ["Lakeview Hotel REIT"] is a closed-end real estate investment trust that was created pursuant to the Declaration of Trust dated February 11, 2004. Lakeview Hotel REIT was established under the laws of the Province of Manitoba and the laws of Canada applicable therein. Lakeview Hotel REIT issued Trust Units pursuant to a Qualifying Transaction, including a Plan of Arrangement which was completed on April 15, 2004. The Qualifying Transaction consisted of a private offering of Lakeview Hotel REIT Units, a public offering of Lakeview Hotel REIT subordinate convertible debentures, the acquisition of the Lakeview Inn & Suites, Fredericton, New Brunswick [the "Initial Property"] and the acquisition of a 49% interest in the Lakeview Flag Licensing General Partnership and a 50% interest in the Lakeview Flag Management General Partnership as described below. The principal purpose of Lakeview Hotel REIT is to provide Unitholders with an opportunity to participate in a diversified portfolio of hotel and extended-stay properties, and commercial and office properties ancillary thereto, located throughout Canada and the United States.

These consolidated financial statements include the accounts of Lakeview Hotel REIT's subsidiaries as follows: Lakeview Hotel REIT Operating Trust, Lakeview Flag Operating LP General Partner Inc., Lakeview Flag Operating Limited Partnership, 2330407 Manitoba Ltd., 1164656 Alberta Ltd., 1184720 Alberta Ltd., 1208406 Alberta Ltd., 1208417 Alberta Ltd., Vaughan Steeles Super 8 Ltd., 1227671 Alberta Ltd., 1236406 Alberta Ltd., 1236412 Alberta Ltd., 0759566 B.C. Ltd., 0760018 B.C. Ltd., 0760024 B.C. Ltd., 1312258 Alberta Ltd., 1317639 Alberta Ltd., 1323785 Alberta Ltd., 1360841 Alberta Ltd. and 0816064 B.C. Ltd. Transactions within the consolidated group are eliminated upon consolidation.

The 50% interest in the Lakeview Flag Management General Partnership is proportionately consolidated as the partners jointly control this partnership. The 49% interest in the Lakeview Flag Licensing General Partnership is accounted for using the equity method.

Significant accounting policies

These unaudited consolidated interim financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles. They have also been prepared on a basis consistent with the December 31, 2007 audited financial statements and should be read in conjunction with the audited financial statements and the notes thereto.

Lakeview Hotel Real Estate Investment Trust

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2008

Unaudited

[a] Cash and cash equivalents

Cash and cash equivalents consist of cash and guaranteed investment certificates with maturities of less than 90 days from the date of issuance and are readily convertible to cash.

[b] Inventory

Inventory is recorded at the lower of cost, on a first in, first out basis, and net realizable value.

[c] Franchise fees, licenses and pre-opening costs

Franchise fees include the application and initial fees associated with the transfer of membership of hotel franchises to Lakeview Hotel REIT. Franchise fees are stated at cost less accumulated amortization. Amortization is recorded using the straight-line method over the shorter of the term of the franchise agreement or the period over which management estimates the franchise will be retained.

Licenses include the costs associated with the purchase of the right to continue operation of existing video lottery terminals. Licenses are stated at cost less accumulated amortization. Amortization is recorded using the straight-line method over five years.

Pre-opening costs were incurred with respect to the opening of the Local Heroes restaurant at the Lakeview Inn & Suites - Fort Saskatchewan on June 15, 2007 and include training, travel and salaries. Pre-opening costs are stated at cost less accumulated amortization. Amortization is recorded using the straight-line method over three years.

[d] Income properties

Income properties include land, buildings, parking lots, signs and furniture, fixtures and equipment.

Income properties are stated at the lower of cost less accumulated amortization or estimated net recoverable amount. Impairment of income properties is recognized when an event or change in circumstances causes the asset's carrying value to exceed the total undiscounted cash flows expected from its use and eventual disposition. The impairment loss is calculated by deducting the fair value of the asset from its carrying value.

Maintenance and repair costs are expensed against operations as incurred, while significant improvements, replacements and major renovations are capitalized to income properties.

Lakeview Hotel Real Estate Investment Trust

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2008
Unaudited

Amortization is recorded as follows:

Buildings	Straight-line over 40 years
Parking lots	Straight-line over 10 years
Signs	Straight-line over 10 years
Furniture, fixtures and equipment	Straight-line over 3 - 10 years

[e] Revenue recognition

Room revenue is recognized when the services are performed and collection is reasonably assured, which is generally on the night the rooms are rented.

Food and beverage revenue is recognized when the services are performed.

[f] Related parties

During 2008 and 2007, Lakeview Hotel REIT had transactions with the following related parties:

<u>Related parties</u>	<u>Nature of relationship</u>
Lakeview Management Inc. ["LMI"]	Unitholder and administrator
Free to Guest Movies Ltd.	A company related to LMI
Lakeview Flag Licensing General Partnership	Equity investee
Lakeview Flag Management General Partnership	Joint venture investee
XYZ Design Inc.	A company related to LMI
Keith Levit Photography	A business owned by the President and Trustee

[g] Lakeview Perks Loyalty Program

In 2006, LMI introduced the Lakeview Perks Loyalty Program. Members of the Lakeview Perks Loyalty Program earn points based on their spending at Lakeview Inn & Suites hotels and Lakeview Resorts. Points can be redeemed for hotel stays at participating hotels or other services or merchandise. The future redemption liability is included in accounts payable and accrued liabilities and is estimated based on points awarded and management's assessment of anticipated point redemptions and point value.

Management will adjust the estimated liability based on redemption experience and additional points awarded and such adjustments will be recorded in the results of operations.

Lakeview Hotel Real Estate Investment Trust

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2008
Unaudited

[h] Income taxes

In June 2007, the Government of Canada enacted new legislation imposing additional income taxes upon publicly traded income trusts classified as Specified Investment Flow-Throughs ["SIFT"], which include a real estate investment trust ["REIT"] that carries on Canadian hotel operations effective January 1, 2011. Prior to June 2007, Lakeview Hotel REIT estimated the future income tax on certain temporary differences between amounts recorded on its balance sheet for book and tax purposes at a nil effective tax rate. Under the legislation, Lakeview Hotel REIT now estimates the effective tax rate on the post 2010 reversal of these temporary differences to be 27.2% in 2011 and 25.7% thereafter. Temporary differences reversing before 2011 will still give rise to nil future income taxes.

While Lakeview Hotel REIT believes it will be subject to additional tax under the new legislation, the estimated effective tax rate on temporary difference reversals after 2011 may change in future periods. As the legislation is new, future technical interpretations of the legislation could occur and could materially affect management's estimate of the future income tax liability.

The amount and timing of reversals of temporary differences will also depend on Lakeview Hotel REIT's future operating results, acquisitions and dispositions of assets and liabilities, and distribution policy. A significant change in any of the preceding assumptions could materially affect Lakeview Hotel REIT's estimate of the future tax liability.

[i] Net loss and comprehensive loss per unit

Net loss and comprehensive loss per unit is based on the consolidated net loss for the period divided by the weighted average number of units outstanding during the period. Diluted loss per unit is computed in accordance with the treasury stock method and based on the weighted average number of units and dilutive unit equivalents.

[j] Stock-based compensation plan

Lakeview Hotel REIT has a unit purchase plan as described in note 12. The fair value method is used to determine the expense for stock-based awards granted to employees and non-employees. Under the fair value method, compensation cost is measured at fair value at the date of grant using the Black-Scholes option pricing model. The compensation expense is expensed over the vesting period with a corresponding credit to contributed surplus. Consideration paid on the exercise of unit options plus the amount of previously recognized expense is credited to unitholders' capital when the options are exercised.

Lakeview Hotel Real Estate Investment Trust

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2008

Unaudited

[k] Use of estimates

The preparation of financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingencies at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

[l] Financial Instruments

Lakeview Hotel REIT has the following financial assets and liabilities:

- Cash and cash equivalents, reserve fund and deposits held in trust are classified as "assets held-for-trading" and are measured at fair value. Gains and losses resulting from the periodic revaluation are recorded in net loss.
- Accounts receivable and mortgages receivable are classified as "loans and receivables" and are recorded at cost, which upon their initial measurement is equal to their fair value. Subsequent measurements are recorded at amortized cost using the effective interest rate method. Under the effective interest rate method, transaction costs are added to the receivable to which they relate. Over its term, the long-term receivable will decrease to its face value with the decrement being applied against interest income earned on the mortgages receivable. The reduced interest income is reflected on the consolidated statements of loss and comprehensive loss.
- Accounts payable and accrued liabilities, distributions payable, debentures, convertible debentures and mortgages payable are classified as "other financial liabilities" and are initially measured at their fair value. Subsequent measurements are recorded at amortized cost using the effective interest rate method. Under the effective interest rate method, financing costs must be applied against the debt to which they relate. Over the term of the debt the long-term liability will increase to the face value of the debt, with the accretion being included in interest on mortgages or interest on debentures and convertible debentures on the consolidated statements of loss and comprehensive loss.

Fair value is based on quoted market prices when available. However, when financial instruments lack an available trading market, fair value is determined using management's estimates and is calculated using market factors with similar characteristics and risk profiles.

[m] New accounting standards adopted in 2008

Capital Disclosures and Financial Instruments – Presentation and Disclosure

Lakeview Hotel Real Estate Investment Trust

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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Unaudited

The CICA issued three new accounting standards: Section 1535, "Capital Disclosures"; Section 3862, "Financial Instruments – Disclosures"; and Section 3863, "Financial Instruments – Presentation". These new standards are effective for fiscal years beginning on or after October 1, 2007 and Lakeview Hotel REIT has adopted them on January 1, 2008.

Section 1535 establishes disclosure requirements about an entity's capital and how it is managed. The purpose is to enable users of the financial statements to evaluate the entity's objectives, policies and processes for managing capital *[note 18]*.

Sections 3862 and 3863 replaced Section 3861, "Financial Instruments – Disclosure and Presentation", revising and enhancing its disclosure requirements, and carrying forward the presentation requirements. These new sections place increased emphasis on disclosures about the nature and extent of risk arising from financial instruments and how the entity manages those risks *[note 16]*.

[n] Future accounting changes

International Financial Reporting Standards ["IFRS"]

In 2005, the Accounting Standards Board [AcSB] announced that the accounting standards in Canada are to converge with IFRS. On February 13, 2008, the CICA had confirmed that the use of IFRS will be required by January 1, 2011, with appropriate comparative data from the prior year. Under IFRS, the primary audience is capital markets and as a result, there is significantly more disclosure required, specifically for quarterly reporting. Further, while IFRS uses a conceptual framework similar to Canadian GAAP, there are significant differences in accounting policy that must be addressed. While Lakeview Hotel REIT has begun assessing the adoption of IFRS for 2011, the financial impact of the transition to IFRS cannot be reasonably estimated at this time.

2. ACQUISITION OF HOTELS

In 2008, Lakeview Hotel REIT acquired the Four Points by Sheraton hotel located in Prince George, British Columbia. The acquisition has been accounted for by the purchase method with the results of operations from the hotel included in Lakeview Hotel REIT's earnings from the date of acquisition. The assets and liabilities acquired at fair value were as follows:

Lakeview Hotel Real Estate Investment Trust

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2008

Unaudited

2008

	Acquisition Date	Land \$	Building \$	Furniture, fixtures and equipment \$	Working capital \$	Cash consider- ation \$
British Columbia						
Four Points by Sheraton - Prince George	2008-04-03	1,030,474	8,218,032	775,000	4,675	10,028,181

Cash consideration for the purchase of the hotel in 2008 was financed from proceeds from the public offering of debentures on March 28, 2008 (*note 8*) and working capital.

In 2007, Lakeview Hotel REIT acquired certain hotels. The acquisitions have been accounted for by the purchase method with the results of operations from the acquired hotels included in the Lakeview Hotel REIT's earnings from the date of their respective acquisitions. The assets and liabilities acquired at fair value were as follows:

2007

(audited)

	Acquisition date	Land \$	Building \$	Parking lot \$	Furniture, fixtures and equipment \$	Working capital \$	Cash consider- ation \$
Alberta							
Lakeview Inn & Suites - Edson Airport West	2007-04-16	604,909	6,633,839	—	600,000	(2,042)	7,836,706
Lakeview Inn & Suites - Brooks	2007-05-15	796,065	9,446,644	—	600,000	(14,414)	10,828,295
Lakeview Signature Inn - Calgary	2007-06-22	2,690,246	22,098,577	181,074	1,850,338	(6,941)	26,813,294
Lakeview Inn & Suites - Slave Lake*	2007-11-15	523,380	9,390,654	—	450,000	7,421	10,371,455
British Columbia							
Lakeview Inn & Suites - Fort Nelson	2007-01-08	763,082	8,795,788	—	647,235	(4,948)	10,201,157
		<u>5,377,682</u>	<u>56,365,502</u>	<u>181,074</u>	<u>4,147,573</u>	<u>(20,924)</u>	<u>66,050,907</u>

* Converted to a Lakeview Inn & Suites hotel on January 1, 2008.

Cash consideration for the purchase of the hotels in 2007 was financed by a combination of proceeds from private placements of Class A Units, first mortgages [*note 10*], a Pre-Approved Line of Credit, proceeds from a public offering of convertible debentures on June 20, 2007 [*note 9*] and working capital.

Lakeview Hotel Real Estate Investment Trust

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2008
Unaudited

3. RESERVE FUND

Pursuant to the Hotel Management Agreements with Lakeview Flag Management General Partnership, the Lakeview Hotel REIT properties are required to reserve funds in a separate account for on-going capital repairs, replacements and/or improvements of the property including but not limited to the regular repair, replacement and maintenance of the furniture, fixtures and equipment. Under the terms of the Hotel Management Agreements, the properties are required to make monthly deposits into the reserve account equal to not less than 2% of monthly gross revenue.

	Six Months Ended June 30 2008	Year Ended December 31 2007
	\$	\$
		(audited)
Reserve fund, beginning of period	1,237,214	622,779
Allocations to reserve fund	570,772	951,428
Use of reserve fund	(236,642)	(336,993)
Reserve fund, end of period	1,571,344	1,237,214

4. MORTGAGES RECEIVABLE

The mortgages receivable represent amounts advanced under a mezzanine loan arrangement with an independent hotel developer and its related parties for a number of hotels in British Columbia and Alberta. The mortgages receivable earn interest at 12% per annum compounded and payable monthly. Payments of interest only are received on the mortgages. The principal is due no later than the maturity of the mortgages, which is on the third anniversary of the date upon which the last advance under the loan is made. Lakeview Hotel REIT made a further advance of \$1,000,000 on August 1, 2008. Details of the mortgages are as follows:

	June 30 2008	December 31 2007
	\$	\$
		(audited)
Principal	4,000,000	—
Transaction costs	40,725	—
Decretion of mortgages receivable	(2,296)	—
	4,038,429	—

Lakeview Hotel Real Estate Investment Trust

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2008

Unaudited

As Lakeview Hotel REIT invests in mortgages to facilitate acquisitions, credit risks arise in the event that the borrowers default on the repayment of their mortgages to Lakeview Hotel REIT. The maximum exposure to credit risk associated with mortgages receivable occurs if all borrowers default on repayment of their mortgages to Lakeview Hotel REIT. Therefore, the carrying value of the mortgages receivable balance represents Lakeview Hotel REIT's maximum exposure to related credit risk without taking into account any collateral held or any other credit enhancements. Lakeview Hotel REIT has mitigated this risk by registering first and/or second mortgage charges against two different hotel properties owned by the borrower which are in various stages of development as well as against other collateral security. The mortgages receivable are also secured by an assignment of leases and material contracts on three properties and corporate and personal guarantees from the borrowers. There were no impairments or impairment provisions recorded for mortgages receivable as at June 30, 2008. Therefore, the credit quality of these financial assets is considered adequate.

Lakeview Hotel REIT has been granted the option to purchase three hotel properties from the borrowers at any time prior to the later of (a) the second anniversary of the date on which the last advance of mortgage funds under the loan was made to the owners or (b) the date the mortgages are repaid in full by the owners. The purchase price for the lands and hotel businesses upon exercise of the option will range from \$115,000 to \$130,000 per room/suite in the hotels. The purchase price will be reduced by any amounts owing to Lakeview Hotel REIT by the owners under the mortgages for each hotel purchased pursuant to the options. Prior to purchase and upon completion, all three hotels will be licensed and operated as Lakeview Inns & Suites and will be paying license fees to Lakeview Flag Licensing General Partnership. Effective January 1, 2009, management fees will also be paid to Lakeview Flag Management General Partnership.

5. FRANCHISE FEES, LICENSES AND PRE-OPENING COSTS

	June 30 2008	December 31 2007
	\$	\$
		(audited)
Cost	233,029	203,089
Less accumulated amortization	(70,595)	(46,657)
	162,434	156,432

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6. INCOME PROPERTIES

	June 30 2008			December 31 2007 (audited)		
	Cost \$	Accumulated amortization \$	Net book value \$	Cost \$	Accumulated amortization \$	Net book value \$
Land	15,492,009	—	15,492,009	14,388,297	—	14,388,297
Buildings	133,543,656	5,677,381	127,866,275	124,902,646	4,064,291	120,838,355
Parking lots	413,045	65,593	347,452	389,197	46,130	343,067
Signs	484,138	54,352	429,786	406,865	39,481	367,384
Furniture, fixtures and equipment	13,481,717	4,590,379	8,891,338	12,181,200	3,307,707	8,873,493
	163,414,565	10,387,705	153,026,860	152,268,205	7,457,609	144,810,596

Effective March 1, 2007, Lakeview Hotel REIT acquired approximately 2/3 of an acre of land adjacent to the Lakeview Inn & Suites in Edson, Alberta for total consideration including closing adjustments of \$365,753. Lakeview Hotel REIT intends to add up to 36 rooms to the Edson property at a time justified by market conditions. The cash consideration for the purchase was financed out of working capital.

7. INVESTMENT IN LAKEVIEW FLAG LICENSING GENERAL PARTNERSHIP

On April 15, 2004, Lakeview Hotel REIT indirectly acquired a 49% interest in Lakeview Flag Licensing General Partnership with nominal initial capitalization of \$49 and issuance of the Lakeview Flag Operating Limited Partnership Class E Units [exchangeable into 500,000 Units, the "Exchangeable Units"] and 500,000 Class V Special Trust Units and 1 Class T Special Trust Unit of Lakeview Hotel REIT. The principal purpose of the Lakeview Flag Licensing General Partnership is to hold the trademarks, trade names, operating procedures, systems, related items and goodwill associated therewith of the hotel flags known as "Lakeview Inn & Suites" and "Lakeview Resorts" ["Lakeview Flag"]. Although the exchange amount was \$1,000,000, the transaction was recorded at the carrying value of \$1 in accordance with Canadian generally accepted accounting principles applicable to related party transactions because the 49% interest in Lakeview Flag Licensing General Partnership was acquired from a company controlled by certain Unitholders of Lakeview Hotel REIT and the exchange amount was not supported by independent evidence.

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Lakeview Flag Licensing General Partnership earns income, pursuant to the Sub-franchise Agreement and the License Agreements with the respective hotels, through the payment to it of a license fee equal to 4% of gross room revenue received from the following Lakeview Inn & Suites hotels which are owned by LMI and located as follows:

Bathurst, New Brunswick [Canada]
Brandon, Manitoba [Canada]
Grand Forks, North Dakota [United States of America]
Halifax, Nova Scotia [Canada]
Miramichi, New Brunswick [Canada]

In addition, pursuant to the Sub-franchise Agreement and License Agreement, Lakeview Flag Licensing General Partnership earns a license fee of 4% of gross room revenue from each Lakeview Hotel REIT property that has opened as or has been converted to a Lakeview Inn & Suites hotel or Lakeview Signature Inn. The license fees are earned effective as of the date of opening or conversion.

Gross room revenue is the gross income resulting from all room sales made to customers or guests of the respective hotels and does not include any sales tax which is collected and remitted to the appropriate tax authority by the hotels.

Investment in Lakeview Flag Licensing General Partnership:

	Six Months Ended June 30 2008 \$	Year Ended December 31 2007 \$
		(audited)
Investment, beginning of period	40,367	30,090
Equity income	318,298	547,807
Distribution received	(299,390)	(537,530)
Investment, end of period	59,275	40,367

8. DEBENTURES

Effective March 28, 2008, Lakeview Hotel REIT, through a public offering, issued \$10,250,000 Series A Senior Secured Debentures [the "Debentures"]. The Debentures mature on June 20, 2012

Lakeview Hotel Real Estate Investment Trust

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and bear interest at an annual rate of 8.125% payable monthly, in cash, with the first payment occurring on April 30, 2008. The debentures are secured by a first charge on the Four Points by Sheraton – Prince George hotel, an assignment of the insurance policy on the property, an assignment of rents and leases of the property and an assignment of material contracts and agreements [note 2]. The debentures are redeemable, in full from time to time at Lakeview Hotel REIT's sole option on not less than 30 days' prior written notice, at a price equal to 110% of the principal amount plus accrued and unpaid interest up to, but excluding the date of redemption.

	June 30 2008	December 31 2007
	\$	\$
		(audited)
Principal	10,250,000	—
Financing costs	(855,121)	—
Accretion of debentures	39,481	—
	9,434,360	—

9. CONVERTIBLE DEBENTURES

At initial measurement, the debentures were allocated to debt and equity components based on the estimated cost of borrowing without the conversion option as follows:

	Debt	Equity	Total
	\$	\$	\$
10% Subordinated Convertible Debentures	3,344,822	1,155,178	4,500,000
9% Subordinated Convertible Debentures	1,066,282	433,718	1,500,000
6.5% Series C Convertible Redeemable Subordinated Debentures	14,937,187	3,062,813	18,000,000
8.5 % Series D Convertible Redeemable Subordinated Debentures	9,045,732	954,268	10,000,000
	28,394,023	5,605,977	34,000,000

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The details of the four series of convertible debentures are outlined in the tables below:

Debenture	June 30, 2008			
	Effective interest rate %	Original face amount \$	Converted to trust units \$	Face amount outstanding \$
10% Subordinated Convertible Debentures	18%	4,500,000	4,398,000	102,000
9% Subordinated Convertible Debentures	18%	1,500,000	1,460,000	40,000
6.5% Series C Convertible Redeemable Subordinated Debentures	11%	18,000,000	—	18,000,000
8.5 % Series D Convertible Redeemable Subordinated Debentures	11%	10,000,000	20,000	9,980,000
		34,000,000	5,878,000	28,122,000

Debenture	June 30, 2008				
	Face amount outstanding \$	Holders' conversion option \$	Accretion \$	Financing costs \$	June 30 2008 \$
10% Subordinated Convertible Debentures	102,000	(26,184)	27,536	(9,724)	93,628
9% Subordinated Convertible Debentures	40,000	(11,566)	7,487	(3,610)	32,311
6.5% Series C Convertible Redeemable Subordinated Debentures	18,000,000	(3,062,813)	644,982	(1,058,428)	14,523,741
8.5% Series D Convertible Redeemable Subordinated Debentures	9,980,000	(952,360)	23,347	(709,491)	8,341,496
	28,122,000	(4,052,923)	703,352	(1,781,253)	22,991,176

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December 31, 2007 (audited)				
Debenture	Effective interest rate %	Original face amount \$	Converted to trust units \$	Face amount outstanding \$
10% Subordinated Convertible Debentures	18%	4,500,000	4,398,000	102,000
9% Subordinated Convertible Debentures	18%	1,500,000	1,460,000	40,000
6.5% Series C Convertible Redeemable Subordinated Debentures	11%	18,000,000	—	18,000,000
		24,000,000	5,858,000	18,142,000

December 31, 2007 (audited)					
Debenture	Face amount outstanding \$	Holders' conversion option \$	Accretion \$	Financing costs \$	December 31 2007 \$
10% Subordinated Convertible Debentures	102,000	(26,184)	22,876	(9,724)	88,968
9% Subordinated Convertible Debentures	40,000	(11,566)	5,930	(3,610)	30,754
6.5% Series C Convertible Redeemable Subordinated Debentures	18,000,000	(3,062,813)	319,749	(1,058,428)	14,198,508
	18,142,000	(3,100,563)	348,555	(1,071,762)	14,318,230

The accretion of the debt component, which increases the debt component from the initial carrying amount, is included in interest expense and totalled \$354,807 and \$106,090 respectively for the six months ended June 30, 2008 and 2007 and \$189,198 and \$64,054 respectively for the three months ended June 30, 2008 and 2007.

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[a] 10% Subordinated Convertible Debentures

On April 15, 2004, under a public offering, Lakeview Hotel REIT issued \$4,500,000 of 10% Subordinate Convertible Debentures.

The debentures bear interest at 10%, mature in five years from date of issue and are subordinate only to property specific conventional mortgage financing and any vendor take-back mortgage financing. The debentures were/are convertible by the holder at any time during the third year after the date of issue at the following conversion price per Unit: \$2.50 in year three; \$3.00 in year four; and \$3.50 in year five. At any time after three years from the issue date, Lakeview Hotel REIT had/has the right to redeem all, but not less than all, debentures at par plus accrued interest. On maturity, the debentures are repayable at par plus any accrued and unpaid interest in cash, or at the option of Lakeview Hotel REIT, in Units [based on a Unit conversion price equal to 95% of the weighted average of the trading price of the Units during the preceding 20 trading day period], or in any other combination thereof.

During 2007, \$1,896,000 of the debentures were converted at a price of \$2.50 into 758,400 Class A Units and \$175,000 of the debentures were converted at a price of \$3.00 into 58,331 Class A Units.

[b] 9% Subordinated Convertible Debentures

On May 30, 2005, under a private offering, the Lakeview Hotel REIT issued \$1,500,000 of 9% Subordinated Convertible Debentures.

The debentures bear interest at 9%, mature in five years from date of issue and are subordinate only to property specific conventional mortgage financing and any vendor take-back mortgage financing. The debentures are convertible by the holder at any time after the date of issue at \$2.90 per Unit.

During 2007, \$880,000 of the debentures were converted at a price of \$2.90 into 303,440 Class A Units.

[c] 6.5% Series C Convertible Redeemable Subordinated Debentures

On June 20, 2007, under a public offering, Lakeview Hotel REIT issued \$18,000,000 of Series C Convertible Redeemable Subordinated Debentures.

The debentures bear interest at 6.5%, mature June 30, 2012 and are subordinate only to property specific conventional mortgage financing and any vendor take-back mortgage financing. The debentures are convertible by the holder at any time after the date of issue at \$5.55 per Unit.

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At any time after three years from the issue date but prior to four years from the issue date, Lakeview Hotel REIT has the right to redeem all, but not less than all, debentures at par plus accrued interest provided that the volume-weighted average trading price of the Units during a 20 consecutive trading day period ending five trading days before notice of redemption is given is not less than 125% of the conversion price. On maturity, the debentures are repayable at par plus any accrued and unpaid interest in cash, or at the option of Lakeview Hotel REIT, in Units [based on a Unit conversion price equal to 95% of the weighted average of the trading price of the Units during the preceding 20 trading day period], or in any other combination thereof.

[d] 8.5% Series D Convertible Redeemable Subordinated Debentures

On May 8, 2008, under a public offering, Lakeview Hotel REIT issued \$10,000,000 of Series D Convertible Redeemable Subordinated Debentures.

The debentures bear interest at 8.5 %, mature May 31, 2013 and are subordinate only to property specific conventional mortgage financing, any vendor take-back mortgage financing and the Series A Senior Secured Debentures issued March 28, 2008 (note 8). The debentures are convertible by the holder at any time prior to maturity at \$3.75 per unit.

The debentures will not be redeemable prior to May 31, 2011. On and after May 31, 2011, but prior to May 31, 2012, the debentures will be redeemable, in whole or in part from time to time at Lakeview Hotel REIT's sole option on not more than 60 days and not less than 30 days notice at a price, payable in cash, equal to the principal amount plus accrued and unpaid interest, provided that the volume-weighted average trading price of the Units on the TSXV during the 20 consecutive trading days ending on the fifth trading day preceding the date on which notice of redemption is given is not less than 150% of the Conversion Price.

On and after May 31, 2012, but prior to the Maturity Date, the debentures will be redeemable, in whole or in part from time to time at Lakeview Hotel REIT's sole option on not more than 60 days and not less than 30 days notice at a price, payable in cash, equal to the principal amount thereof, plus accrued and unpaid interest, provided that the Current Market Price is not less than 125% of the Conversion Price.

On maturity, the debentures are repayable at par plus any accrued and unpaid interest in cash.

During 2008, \$20,000 of the debentures were converted at a price of \$3.75 into 5,333 Class A Units.

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10. MORTGAGES PAYABLE

	June 30 2008	December 31 2007
	\$	\$
		(audited)
Mortgages payable, bearing interest at 5.88% to 6.74% per annum, due February 1, 2011 to July 1, 2014, collateralized by first charges on certain income properties, an assignment of the insurance policy on the income properties, an assignment of rents and leases of the income properties and an assignment of material contracts and agreements. The mortgages are cross-collateralized by each of the underlying properties with the exception of the Four Points by Sheraton – Prince George <i>[note 8]</i>	81,386,962	82,369,172
Less current portion	2,290,985	2,211,080
	79,095,977	80,158,092

Estimated future principal repayments over the next five years and thereafter are as follows:

	\$
Remainder of 2008	1,127,827
2009	2,362,752
2010	2,513,112
2011	29,087,884
2012	30,460,243
Thereafter	16,635,990
Total principal outstanding	82,187,808
Financing costs	(1,097,242)
Accretion of mortgages	296,396
	81,386,962

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11. UNITHOLDERS' CAPITAL

	Class A Units \$	Class V Special Trust Units and Exchangeable Units \$	Class T Special Trust Units \$	Total Unitholders' capital \$
Balance, December 31, 2006	55,901,338	1	—	55,901,339
Conversion of debentures <i>[note 9]</i>	3,100,531	—	—	3,100,531
Issuance of Units on exercise of Unit options <i>[note 12]</i>	19,850	—	—	19,850
Balance, December 31, 2007 (audited)	59,021,719	1	—	59,021,720
Conversion of debentures <i>[note 9]</i>	18,438	—	—	18,438
Balance, June 30, 2008	59,040,157	1	—	59,040,158

Units issued during 2008 and 2007 are summarized as follows:

	Class A Units #	Class V Special Trust Units and Exchangeable Units #	Class T Special Trust Units #
Balance, December 31, 2006	17,644,252	500,000	1
Conversion of debentures <i>[note 9]</i>	1,120,171	—	—
Issuance of Units on exercise of Unit options <i>[note 12]</i>	5,000	—	—
Balance, December 31, 2007 (audited)	18,769,423	500,000	1
Conversion of debentures <i>[note 9]</i>	5,333	—	—
Balance June 30, 2008	18,774,756	500,000	1

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The beneficial interest in the Lakeview Hotel REIT is divided into interests of one class and of equal value, referred to as Class A Units, of unlimited number. All Class A Units participate pro rata in any distribution declared on Class A Units and have one vote per Unit.

Exchangeable Units were issued by Lakeview Flag Operating Limited Partnership [note 7]. The Exchangeable Units are exchangeable into 500,000 Class A Units of Lakeview Hotel REIT at the option of the holder. The Exchangeable Units entitle the holders to cash distributions equivalent to the amount of cash distributions that would be allocated to 500,000 Class A Units. In addition, the following were issued in conjunction with the issuance of the Exchangeable Units:

- 500,000 Class V Special Trust Units, one vote per Unit, excluding the right to vote in respect of the election of Trustees, no entitlement to any distribution declared payable on Class A Units, except as declared by Trustees subject to certain restrictions, cancelled proportionately upon exchange of securities exchangeable into Class A Units.
- One Class T Special Trust Unit, non-transferable, non-voting, right to appoint one-third of the total number of Trustees, no right to any distributions or economic interest in Lakeview Hotel REIT.

Distributions to Unitholders

For both the three-month periods ended June 30, 2008 and 2007, distributions of \$0.11 per Class A Unit and per Exchangeable Unit were declared, totalling \$2,121,760 and \$2,090,788 respectively.

For both the six-month periods ended June 30, 2008 and 2007, distributions of \$0.22 per Class A Unit and per Exchangeable Unit were declared, totaling \$4,243,323 and \$4,108,502 respectively.

Distribution policy

The following is a summary of the Lakeview Hotel REIT distribution policy, the full provisions of which are contained in the Declaration of Trust:

Subject to the obligations of the Trustees in respect of the Class V Units, the Trustees may, on or before each Distribution Record Date, and shall on or before the December 31 Distribution Record Date, declare payable, to the Unitholders of record on such Distribution Record Date, all or any part of the Distributable Cash of the Trust for the Distribution Period ending on such Distribution Record Date determined in accordance with the Declaration of Trust, and the proportionate share of each Unit of the amount so payable shall be determined by dividing such amount by the number of Units outstanding on that Distribution Record Date. Each Unitholder's share thereof shall be equal to the proportionate share per Unit multiplied by the number of Units owned of record by the Unitholder

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on that Distribution Record Date and shall be paid to each such Unitholder on the Distribution Payment Date next following the Distribution Record Date.

"Distributable Cash of the Trust" for the period ending on a Distribution Record Date shall be the amount calculated, for the period commencing immediately following the preceding Distribution Record Date and ending on such Distribution Record Date [each, a "Distribution Period"], as all revenues received or receivable, including net realized capital gains and such other amounts as Lakeview Hotel REIT may receive from time to time in the applicable period, less:

- [a] Administrative and operational expenses and other obligations;
- [b] Amounts which may be used for acquisitions or other business purposes;
- [c] Amounts required for replacement reserves; and
- [d] Such other amounts as the Trustees deem appropriate and necessary.

Items of income or expense not provided for above shall be included in such calculation on such basis as may be considered appropriate by the Trustees.

12. UNIT PURCHASE PLAN

The Trustees have established a Unit Purchase Plan to provide incentives to Trustees, management and other participants to carry out the business of Lakeview Hotel REIT. The aggregate number of Units reserved for issuance under this plan shall not exceed five percent [5%] of the total number of issued and outstanding units.

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The Unit options outstanding and exercisable under the Unit Purchase Plan are summarized as follows:

	Six Months Ended June 30 2008		Year Ended December 31 2007 (audited)	
	Number of options	Weighted average exercise price \$	Number of options	Weighted average exercise price \$
Unit options outstanding, beginning of period	232,500	4.28	62,500	3.25
Unit options granted	-	-	175,000	4.62
Unit options exercised	-	-	(5,000)	3.25
Unit options outstanding, end of period	232,500	4.28	232,500	4.28
Range of exercise price of Unit options outstanding, end of period	-	3.25 to 4.62	-	3.25 to 4.62
Unit options vested, end of period	232,500	4.28	232,500	4.28
Expiry date	2011 to 2012		2011 to 2012	

The fair values of the options were estimated using the Black-Scholes option pricing model with the following assumptions and results:

	2007 Options (audited)
Distribution yield	8.8 %
Expected volatility	52.7 %
Risk-free interest rate	4.8 %
Estimated compensation costs	\$304,500

The compensation costs were expensed at the date of grant.

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13. BASIC AND DILUTED LOSS PER UNIT

The basic and diluted loss per Unit is calculated based on the following:

	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
Weighted average Units	19,271,064	18,939,039	19,270,243	18,597,808

The effect of the options under the Unit Purchase Plan issued to certain Trustees and management [note 12] and conversion of the convertible debentures [note 9] are not presented as they would have an anti-dilutive effect on the loss per Unit.

14. RELATED PARTY TRANSACTIONS

In addition to the related party transactions disclosed elsewhere in these consolidated financial statements, during the normal course of business, Lakeview Hotel REIT had the following transactions and balances recorded at their exchange value with related parties:

	June 30 2008	December 31 2007
	\$	\$
		(audited)
Accounts payable and accrued liabilities to		
LMI	159,360	83,277
Lakeview Flag Licensing General Partnership [note 7]	101,220	61,503
Lakeview Flag Management General Partnership [note 15]	128,216	83,686
XYZ Design Inc.	15,452	6,906

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	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
	\$	\$	\$	\$
Marketing expenses paid to				
Free to Guest Movies Ltd.	53,457	42,645	101,318	81,470
LMI	93,984	41,616	195,527	88,343
Included in general and administration expense				
Accounting fees paid to				
LMI	131,167	101,743	255,850	192,698
Asset management fees paid to				
LMI	108,100	74,867	216,303	140,644
Reservation fees paid to				
LMI	93,809	62,468	195,352	132,557
License fees paid to				
Lakeview Flag Licensing				
General Partnership <i>[note 7]</i>	250,461	166,608	521,149	353,517
Management fees paid to				
Lakeview Flag Management				
General Partnership <i>[note 15]</i>	339,222	235,400	666,480	484,218
Professional fees paid to				
XYZ Design Inc.	-	2,711	-	5,336
Capitalized to income properties				
Professional fees paid to				
XYZ Design Inc.	19,593	12,603	34,510	19,780
Keith Levit Photography	22,695	8,825	22,695	8,825

Under the License Agreement *[note 7]*, the following annual fees are paid by Lakeview Hotel REIT to LMI for accounting services, marketing services and access to the on-line reservation system.

Accounting fee	\$30,000 per annum per hotel
Reservation fee	1.5% of gross room revenue
Marketing fee	1.5% (1% - 2007) of gross room revenue

[Gross room revenue is defined in note 7]

The reservation and marketing fees are paid to LMI when properties have been converted to Lakeview Inn & Suites hotels.

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The accounting fee shall be increased annually by the year over year increase in the Consumer Price Index for the province in which the hotel is located.

Pursuant to a Services Agreement between Lakeview Hotel REIT and LMI, LMI has been engaged as the administrator of Lakeview Hotel REIT, to administer the affairs of the Lakeview Hotel REIT on a day-to-day basis and perform the record keeping and reporting functions of the Trustees. The initial term of the Services Agreement is 5 years expiring on April 14, 2009. In consideration, Lakeview Hotel REIT issued to LMI, at the inception of the agreement, options to acquire 50,000 Units, fully vested and exercisable upon issuance at \$1.00 per Unit. LMI exercised its options concurrently with the closing of the Qualifying Transaction.

Effective October 1, 2006, LMI began to charge an asset management fee based on 0.3% of the net book value of income properties. The fee is paid monthly on the last day of every month and is based on the net book value of income properties at the end of the previous month.

15. INVESTMENT IN LAKEVIEW FLAG MANAGEMENT GENERAL PARTNERSHIP

Lakeview Hotel REIT indirectly acquired a 50% interest in the Lakeview Flag Management General Partnership with initial nominal capitalization of \$50, entitling it to 25% of Lakeview Flag Management General Partnership's net income.

Pursuant to a Property Management Agreement, Lakeview Flag Management General Partnership provides hotel management services to each limited service Lakeview Hotel REIT property for a fee equal to 5% of gross revenue and to each full service Lakeview Hotel REIT property for a fee equal to 4% of gross revenue. Gross revenue includes all income derived from the properties and their operations.

Lakeview Hotel REIT's 25% share of the assets, liabilities, revenues, expenses and cash flows are as follows:

	June 30 2008	December 31 2007
	\$	\$
		(audited)
Assets - current	42,862	28,890
Liabilities - current	2,012	1,577

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	Three Months Ended June 30		Six Months Ended June 30	
	2008 \$	2007 \$	2008 \$	2007 \$
Revenue	113,142	78,552	222,306	161,537
Expenses	9	11	19	54
Net income	113,133	78,541	222,287	161,483
Cash flows				
Cash provided by operating activities	112,702	88,175	207,878	150,875
Cash used in financing activities	(112,750)	(88,250)	(208,750)	(152,000)
Decrease in cash	(48)	(75)	(872)	(1,125)

16. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Financial instruments include cash and cash equivalents, reserve fund, deposits held in trust, accounts receivable, mortgages receivable, accounts payable and accrued liabilities, distributions payable, debentures, convertible debentures and mortgages payable.

Lakeview Hotel REIT's carrying value of accounts receivable, accounts payable and accrued liabilities and distributions payable approximates their fair value due to the immediate or short-term nature of these instruments.

The carrying value of the mortgages receivable approximates its fair value due to its recent advance.

The carrying value of the debentures, convertible debentures and mortgages payable approximates the fair value as interest rates are consistent with current rates.

Management's involvement in operations helps identify risks and variations from expectations. The Lakeview Hotel REIT does not manage risk through the use of hedging transactions. As part of the overall operation of the Trust, management considers the avoidance of undue concentrations of risk.

It is management's opinion that Lakeview Hotel REIT is not exposed to significant currency risks arising from these financial instruments.

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Interest rate risk

Lakeview Hotel REIT is exposed to interest risk as it relates to the renewal or refinancing of its long-term debts as they become due.

Fluctuations in interest rates create a cash flow risk which is minimized by obtaining long-term mortgages. There is a risk that interest rates will fluctuate subsequent to the date the Trust commits to a fixed interest rate with the lender. Obtaining long-term mortgages with fixed interest rates minimizes cash flow risk.

Credit risk

The amount of accounts receivable disclosed in the balance sheet of \$2,499,901 as at June 30, 2008 and \$2,030,665 as at December 31, 2007 is net of allowances for bad debts, estimated by management based on prior experience and their assessment of the current economic environment. No customer accounts for more than 10% of the accounts receivable balance.

Historically there have been no collection issues with respect to accounts receivable and Lakeview Hotel REIT does not believe it is subject to any significant concentration of credit risk.

See Note 4 for management's assessment of the credit risk relating to the mortgages receivable and the actions taken to mitigate it.

Liquidity risk

Lakeview Hotel REIT's objective is to have sufficient liquidity to meet liabilities when due as well as to maintain compliance with liquidity covenants on financing contracts. Lakeview Hotel REIT monitors its cash balances and cash flows generated from operations to meet requirements. Based on overall cash generation capacity and overall financial position, while there can be no assurance, management believes Lakeview Hotel REIT will be able to meet financial obligations as they come due while maintaining compliance with all financial covenants.

17. INCOME TAXES

In accordance with new legislation enacted by the Government of Canada in June 2007 that imposed additional income taxes upon publicly traded trusts effective January 1, 2011 and as based on its assets and liabilities as at June 30, 2008, Lakeview Hotel REIT has estimated the amount of its temporary differences which were previously not subject to tax and has estimated the periods in which these differences will reverse. Lakeview Hotel REIT estimates that approximately

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\$2,684,000 net taxable temporary differences will reverse after January 1, 2011, resulting in a \$730,000 future income tax liability, a reduction of \$4,000 from the amount recorded at December 31, 2007. The taxable temporary differences related principally to Lakeview Hotel REIT's income properties and financing costs relating to long-term debt.

18. CAPITAL MANAGEMENT

Lakeview Hotel REIT defines capital as the aggregate of unitholders' equity and interest-bearing debt. The objectives of Lakeview Hotel REIT's capital management program are to maintain a level of capital that complies with the debt restrictions according to Lakeview Hotel REIT's Declaration of Trust, complies with existing debt service coverage ratio covenants, provides a return to unitholders by delivering monthly cash distributions, optimizes the cost of capital, funds its business strategies and builds long-term unitholder value.

In managing its capital structure, Lakeview Hotel REIT monitors performance throughout the year to ensure anticipated cash distributions, working capital requirements and capital expenditures are funded from operations, available cash on deposit and, where applicable, borrowing on the Pre-Approved Line of Credit. Lakeview Hotel REIT will make adjustments to its capital structure to meet the objectives of the broader corporate strategy or in response to changes in economic conditions and risk. In order to maintain or adjust the capital structure, Lakeview Hotel REIT may issue debt and/or issue or redeem units.

Lakeview Hotel REIT monitors its capital by the following methods, including (but not limited to):

- Maintaining a Debt Service Coverage ratio defined as earnings before interest, income taxes, depreciation and amortization (earnings base) to mortgage interest and principal payments (debt service) of no less than 1.10.
- Restricting the total of all mortgage loans on all income properties from being greater than 75% of the appraised value of the income properties in accordance with the Declaration of Trust. As at June 30, 2008 and December 31, 2007 respectively, the total of mortgage loans payable is 49.8% and 54.1% of the total estimated current value of income properties.

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	June 30 2008	December 31 2007
	\$	\$
Capital Structure		
Debentures	9,434,360	—
Convertible debentures	22,991,176	14,318,230
Mortgages payable	81,386,962	82,369,172
Total debt	<u>113,812,498</u>	<u>96,687,402</u>
Unitholders' equity	47,389,840	51,700,993
Total Capital	<u>161,202,338</u>	<u>148,388,395</u>

Debt Service Coverage Ratio	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
	\$	\$	\$	\$
Earnings base	3,022,357	1,537,052	6,004,331	4,287,401
Debt service	1,835,526	925,139	3,671,052	1,702,900
Debt service coverage ratio	<u>1.65</u>	1.66	<u>1.64</u>	2.52

Lakeview Hotel REIT is also subject to financial covenants in its mortgages payable, which are measured on an annual basis and include customary terms and conditions for borrowings of this nature. These include the Debt Service Coverage ratio presented above. Lakeview Hotel REIT is in compliance with all of its financial covenants.

For the three-month and six-month periods ended June 30, 2008 and 2007, cash distributions to unitholders exceed Lakeview Hotel REIT's distributable income, as defined in the Declaration of Trust.

19. SUBSEQUENT EVENTS

[a] Effective August 1, 2008, Lakeview Hotel REIT acquired the Days Inn hotel located in Ottawa, Ontario for total consideration of \$10,500,000 plus closing adjustments. The cash consideration for this purchase was financed by a vendor take-back mortgage, proceeds received under the Pre-Approved Line of Credit plus working capital.

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- [b] Effective August 6, 2008, Lakeview Hotel REIT issued 109,500 options to purchase Lakeview Hotel REIT Units to the senior management and executives of the Trust. The options are exercisable for a period of five years expiring August 1, 2013 at an exercise price of \$3.50.
- [c] Effective August 1, 2008, the Board of Trustees and the Compensation and Governance Committee of Lakeview Hotel REIT resolved that the compensation payable to the Independent Trustees of Lakeview Hotel REIT for services rendered to or on behalf of Lakeview Hotel REIT would be as follows:
- a. annual retainer of \$12,000, payable quarterly in advance;
 - b. Committee Chair retainer of \$2,000 per year, payable quarterly in advance.
 - c. meeting fee;
 - i. \$1,000 per Board or Committee meeting if in person; payable within 30 days of each such meeting;
 - ii. \$500 per Board or Committee meeting if other than in person, payable within 30 days of each such meeting;
- provided that no payment in excess of \$1,000 will be paid for any Board or Committee meetings held in sequence at one identifiable period of time,

and that the compensation payable to the Lakeview Trustee of Lakeview Hotel REIT for services rendered to or on behalf of Lakeview Hotel REIT would be by way of the issuance of options of Lakeview Hotel REIT in an amount equal to the monetary compensation paid to the Independent Trustees of Lakeview Hotel REIT based on an estimated fair value of the options using the Black-Scholes option pricing model.