



**FOR IMMEDIATE RELEASE**

**SYMBOL: "RYL.UN"**

**ROYAL HOST REAL ESTATE INVESTMENT TRUST ANNOUNCES  
FOURTH QUARTER AND YEAR END DECEMBER 31, 2003 RESULTS**

**Calgary, Alberta March 24th, 2004** - Royal Host, a diversified hotel Real Estate Investment Trust (REIT), today announced financial results for the fourth quarter and year ended December 31, 2003.

Contrary to industry trends, Royal Host announced a 2.7% increase in revenue per available room (RevPAR) in the fourth quarter of 2003 compared to the same quarter of 2002. Royal Host also recorded a 12% improvement year over year in operating profit during the quarter.

In the last quarter of 2003, cash available for distribution improved to \$0.11 per unit (basic) from \$0.09 per unit in the same quarter of 2002.

During 2003, the hospitality industry experienced some of the most difficult conditions on record including: the impact of the war in Iraq; the outbreak of Sudden Acute Respiratory Syndrome (SARS) in Toronto; and the impact of a strengthening Canadian dollar, to name a few.

"This past year has been extremely challenging for the hospitality industry," said Greg Royer, CEO of Royal Host REIT. "Our operating trends were negative for the first three quarters of 2003. However, in the fourth quarter of 2003, we were able to turn things around and recorded a year over year improvement in both revenues and operating profit."

**Highlights for 2003**

During 2003 Royal Host:

- Outperformed the industry in RevPAR per Pannell Kerr Forster, in each of the four quarters of the year;

- Began a process of restructuring its operations and reducing costs and took steps towards exiting non-core businesses;
- Maintained a record of uninterrupted cash distributions to unitholders, albeit at a reduced rate;
- Acquired the Calgary Best Western Village Park Inn;
- Continued to benefit from the successful acquisition and integration of focused service hotels in Belleville, Trenton and Calgary; and
- Invested approximately \$14 million in capital improvements to maintain the quality of its hotel properties.

### **Fourth Quarter Results**

Total hospitality revenues increased by \$1.4 million to \$35.1 million in the fourth quarter of 2003, an increase of 4.2% from revenues of \$33.7 million in the same quarter of 2002. The increase in total revenues primarily reflects the impact of the acquisition of the Calgary Best Western hotel in the second quarter of 2003 and to a lesser degree, the take-over of the operations of the Yellowknife hotel in November of 2002.

Year over year, 2003 fourth quarter room revenues increased by almost 9.5% or \$2.0 million; food and beverage revenues increased by \$0.2 million; while other hospitality revenues were \$0.7 million lower than the same quarter of 2002. Other hospitality revenues were lower primarily due to the recognition of a one time revenue item related to the franchise business in the fourth quarter of 2002.

Hospitality expenses increased to \$26.4 million in the fourth quarter of 2003 from \$25.9 million in 2002. This \$0.5 million increase in expenses is minor considering that the fourth quarter of 2003 included two additional hotel operations compared to the same quarter of 2002.

Due to management's ability to control costs in the fourth quarter of 2003, the gross operating margin increased by 7.5% to 24.8% compared to the same quarter of 2002. This improvement was significant in that it reversed a year long trend of increased costs and deteriorating margins.

For the fourth quarter of 2003, Royal Host recorded a loss of \$1.4 million compared to positive earnings of \$1.3 million in 2002. This decrease is largely due to changes in future income taxes, a non-cash item. However, cash available for distribution of \$4.3 million in 2003 was unchanged from the same quarter in 2002.

## **Year end Results**

For the twelve months ended December 31, 2003, total revenues increased by \$5.4 million, a 4.0% increase from the same period in 2002. Total hospitality expenses for the 12 months ended December 31, 2003, were \$10.2 million or 10.5% higher than the same period in 2002. The increase in revenues and expenses is primarily attributable to the addition of the Belleville, Trenton and Calgary hotels, as well as the take-over of the Yellowknife operations.

Due to a misinterpretation of documentation pertaining to a complex co-tenancy arrangement, Royal Host's financial statements for the years ended December 31, 1998 through 2002, overstated other hospitality revenue and net earnings by a cumulative total of approximately \$2.0 million. While not material in any single year, the miscalculation has been corrected by recording a prior period adjustment with retroactive restatement. Where appropriate, all references and comparisons to prior periods in this communication relate to the restated numbers.

For the year ended December 31, 2003, increased costs exceeded increased revenues, resulting in a \$4.8 million reduction in gross margin from \$39.7 million (29.1% operating margin) in 2002 to \$34.9 million (24.6% operating margin) in 2003. For the year, on a same property basis, operating margins also declined due to lower revenues while costs remained relatively unchanged.

For 2003, other income and expenses were \$34.9 million, an increase of \$2.6 million compared to the same 12 months of 2002. This increase is primarily due to: increased interest expense from additional debt required to finance acquisitions and other capital expenditures; higher year-over-year trust administration expenses resulting from increased compliance and insurance costs; and changes in future income taxes, a non-cash item.

Reduced annual same store revenues and lower operating margins in the high volume second and third quarters of 2003, contributed to a year-over-year reduction in net earnings of \$7.3 million for the year ended December 31, 2003 compared to 2002. During 2003, Royal Host generated \$11.7 million in basic adjusted cash available for distribution or \$0.48 per unit compared to an adjusted \$0.74 per unit in 2002.

While net earnings calculated in accordance with Canadian generally accepted accounting principles (GAAP) is an important measure of an organization's health and performance, given our significant levels of non-cash items such as amortization, we focus more on our calculation of adjusted cash available for distribution. This measure, which is not recognized under GAAP, indicates the amount of cash generated by our operations that is available for distribution to unitholders, repayment of debt or for further investment in capital assets.

## OUTLOOK

“We are relieved to get 2003 and its challenges behind us. While we experienced increased costs and lower operating margins during the first three quarters of 2003, through the dedication and hard work of our management and staff, we completely changed the dynamics and recorded improvements in both revenues and margins in the fourth quarter,” added Royer. “Looking forward, we are also encouraged because our January and February 2004 monthly revenue per available room (RevPAR) is up over both last year and the comparative months of 2002. We believe that a market recovery, combined with improving operating margins will result in superior returns for our unitholders.”

### Operating Results

	Three Months Ended		Years Ended	
	December 31, 2003	December 31, 2002	December 31, 2003	December 31, 2002
<b>ADR</b>	<b>\$85.83</b>	<b>\$85.07</b>	<b>\$87.95</b>	<b>\$89.91</b>
<b>Occupancy</b>	<b>61.2%</b>	<b>60.1%</b>	<b>64.2%</b>	<b>63.9%</b>
<b>RevPAR</b>	<b>\$52.51</b>	<b>\$51.11</b>	<b>\$56.45</b>	<b>\$57.43</b>
<b>Available Room Nights</b>	<b>469,000</b>	<b>416,000</b>	<b>1,761,000</b>	<b>1,613,000</b>

Royal Host will host a conference call on Thursday, March 25, 2004 at 11.30 am EST to discuss these results. Please dial 1-888-334-9269 or 1-416-695-9714 to access the call. You will be required to identify yourself and whether you are participating on behalf of an organization. Media will be in listen-only mode for the duration of the call. A recording of this conference call will be made available beginning March 25, 2004 through to April 1, 2004. To access the recording please dial 1-866-518-1010 or 1-416-695-5275.

Royal Host REIT owns 39 hotels, manages 75 properties and franchises 117 locations for over 15,500 guestrooms in the mid-market to upscale segments. Royal Host also owns the master franchise rights for Travelodge in Canada and provides hotel and resort management services for its portfolio and to third party owned properties.

Royal Host's objective is to maximize earnings while balancing risk for its unitholders through efficient operations, strong marketing and a focus on providing travelers with superior accommodations and travel experiences. Royal Host units and convertible debentures are traded on the Toronto Stock Exchange under the trading symbols "RYL.UN" and "RYL.DB", respectively.

This press release contains certain forward-looking statements relating, but not limited to, Royal Host's operations, anticipated financial performance, business prospects and strategies. Forward-looking information typically contains statements with words such as "anticipate", "believe", "expect", "plan", or similar words suggesting future outcomes. Such forward-looking statements are subject to risks, uncertainties and other factors, which could cause actual results to differ materially from future results expressed, projected or implied by such forward-looking statements. Such factors include, but are not limited to economic, competitive and lodging industry conditions. Royal Host disclaims any responsibility to update any such forward-looking statements.

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# **ROYAL HOST REAL ESTATE INVESTMENT TRUST**

## **Consolidated Financial Statements**

**For the years ended December 31, 2003 and December 31, 2002**

**ROYAL HOST REAL ESTATE INVESTMENT TRUST**  
**Consolidated Balance Sheets**  
*\$000's*

	As At	
	December 31, 2003	December 31, 2002
		<i>(Restated - Note 4)</i>
<b>ASSETS</b>		
<b>Current Assets</b>		
Cash and short-term investments <i>(Note 2(l))</i>	5,183	16,106
Accounts and notes receivable	8,609	9,172
Deposits and prepaid expenses	3,453	3,783
Inventories	3,739	3,885
Property under development <i>(Note 7)</i>	2,068	340
Future income tax <i>(Note 9)</i>	583	195
	<b>23,635</b>	<b>33,481</b>
<b>Restricted Cash <i>(Note 5)</i></b>	<b>4,247</b>	<b>4,159</b>
<b>Capital Assets <i>(Note 10)</i></b>	<b>338,336</b>	<b>327,818</b>
<b>Long-term Notes Receivable and Other Assets <i>(Note 8)</i></b>	<b>3,297</b>	<b>3,562</b>
	<b>369,515</b>	<b>369,020</b>
<b>LIABILITIES AND EQUITY</b>		
<b>Current Liabilities</b>		
Accounts payable and accrued liabilities	18,330	18,631
Current portion of mortgages and other debt <i>(Note 11)</i>	39,515	36,307
Current portion of capital leases <i>(Note 12)</i>	864	1,208
Distributions payable	558	1,667
Other current liabilities	1,929	2,118
	<b>61,196</b>	<b>59,931</b>
<b>Mortgages and Other Debt <i>(Note 11)</i></b>	<b>121,650</b>	<b>104,933</b>
<b>Capital Leases <i>(Note 12)</i></b>	<b>1,490</b>	<b>1,125</b>
<b>Future Income Taxes <i>(Note 9)</i></b>	<b>1,350</b>	<b>792</b>
<b>Deferred Revenue</b>	<b>963</b>	<b>1,478</b>
<b>Equity <i>(Note 13)</i></b>	<b>182,866</b>	<b>200,761</b>
	<b>369,515</b>	<b>369,020</b>

*See accompanying Notes to Consolidated Financial Statements*

**ROYAL HOST REAL ESTATE INVESTMENT TRUST**  
**Consolidated Statements of Net Earnings**  
**For the years ended December 31, 2003 and December 31, 2002**  
*\$000's*

	Three Months Ended		Years Ended	
	December 31, 2003	December 31, 2002	December 31, 2003	December 31, 2002
		<i>(Restated Note 4)</i>		<i>(Restated Note 4)</i>
<b>Hospitality Revenues</b>				
Rooms	22,957	20,971	97,790	92,051
Food and beverage	7,657	7,493	26,523	24,056
Other hospitality revenues	4,453	5,187	17,231	20,033
	<b>35,067</b>	<b>33,651</b>	<b>141,544</b>	<b>136,140</b>
<b>Hospitality Expenses</b>	<b>26,362</b>	<b>25,881</b>	<b>106,655</b>	<b>96,486</b>
<b>Gross Margin</b>	<b>8,705</b>	<b>7,770</b>	<b>34,889</b>	<b>39,654</b>
<b>Other (Income) and Expenses</b>				
Interest income	105	(146)	(29)	(490)
Interest on mortgages and other debt	3,557	3,212	13,622	12,787
Trust administration	521	437	2,125	1,692
Capital and other taxes	204	44	488	261
Future income tax	1,113	(1,908)	671	(286)
Amortization	4,462	4,816	17,779	18,340
Loss (gain) on foreign currency translation (Note 3(b))	109	(10)	214	(10)
	<b>10,071</b>	<b>6,445</b>	<b>34,870</b>	<b>32,294</b>
<b>Net Earnings (Note 6)</b>	<b>(1,366)</b>	<b>1,325</b>	<b>19</b>	<b>7,360</b>
<b>Per unit net earnings</b>				
- basic (Note 6)	<b>(0.12)</b>	<b>(0.03)</b>	<b>(0.28)</b>	<b>0.01</b>
- diluted (Note 6)	<b>(0.12)</b>	<b>(0.03)</b>	<b>(0.29)</b>	<b>0.01</b>

*See accompanying Notes to Consolidated Financial Statements*

**ROYAL HOST REAL ESTATE INVESTMENT TRUST**  
**Consolidated Statements of Cash Flows**  
**For the years ended December 31, 2003 and December 31, 2002**  
*\$000's*

	Three Months Ended		Years Ended	
	December 31, 2003	December 31, 2002	December 31, 2003	December 31, 2002
		<i>(Restated Note 4)</i>		<i>(Restated Note 4)</i>
<b>CASH PROVIDED BY (USED IN)</b>				
<b>Operating Activities</b>				
Net earnings	(1,366)	1,325	19	7,360
Items not affecting cash:				
Amortization of capital assets	4,306	4,549	17,119	17,566
Future income tax (recovery) expense	1,113	(1,908)	671	(286)
Funds from operations <i>(Note 2(k))</i>	4,053	3,966	17,809	24,640
<b>Change in non-cash working capital:</b>				
Decrease (increase) in accounts and notes receivable	1,234	(102)	563	(1,082)
Decrease (increase) in deposits and prepaid expenses	1,369	483	330	(1,002)
Decrease (increase) in inventories	116	(302)	146	(414)
(Decrease) increase in accounts payable and accrued liabilities	(1,623)	716	(802)	2,575
(Decrease) increase in other current liabilities and deferred revenue	56	570	(704)	221
Amortization of deferred finance costs	156	267	660	774
	<b>5,361</b>	<b>5,598</b>	<b>18,002</b>	<b>25,712</b>
<b>Financing Activities</b>				
Additions to mortgages and other debt	400	-	32,240	11,100
Principal repayments on mortgages and other debt and capital leases	(3,332)	(1,181)	(13,816)	(23,454)
Issuance of trust units plan under employee unit purchase	(78)	36	8	95
Contributed surplus <i>(Note 13(g))</i>	89	-	89	-
Issuance of convertible debenture	-	-	-	40,000
Equity financing issue costs	-	(4)	-	(1,892)
Equity distributions <i>(Note 13(b))</i>	(2,812)	(6,150)	(19,120)	(24,062)
	<b>(5,733)</b>	<b>(7,299)</b>	<b>(599)</b>	<b>1,787</b>
<b>Investing Activities</b>				
Restricted cash <i>(Note 5)</i>	51	(462)	(88)	(965)
Capital expenditures	(2,478)	(3,426)	(26,115)	(18,011)
Property under development	(648)	(340)	(1,728)	(340)
Increase in long-term notes receivable and other assets	(140)	419	(395)	(1,084)
	<b>(3,215)</b>	<b>(3,809)</b>	<b>(28,326)</b>	<b>(20,400)</b>
<b>Net Change in Cash and Short-term Investments</b>	<b>(3,587)</b>	<b>(5,510)</b>	<b>(10,923)</b>	<b>7,099</b>
<b>Cash and Short-term Investments, beginning of year</b>	<b>8,770</b>	<b>21,616</b>	<b>16,106</b>	<b>9,007</b>
<b>Cash and Short-term Investments, end of year</b>	<b>5,183</b>	<b>16,106</b>	<b>5,183</b>	<b>16,106</b>

*See accompanying Notes to Consolidated Financial Statements*

**ROYAL HOST REAL ESTATE INVESTMENT TRUST**  
**Notes to Consolidated Financial Statements**  
**As at December 31, 2003 and December 31, 2002**

**1. GENERAL INFORMATION**

Royal Host Real Estate Investment Trust ("Royal Host" or the "Trust") was created pursuant to the Declaration of Trust dated August 27, 1997. Royal Host is an unincorporated closed-end mutual fund trust established for the purpose of investing in hotel properties and hospitality businesses, under specified guidelines as defined under the Declaration of Trust.

**2. SIGNIFICANT ACCOUNTING POLICIES**

**a) Basis of Accounting**

The Royal Host accounting policies and standards of financial disclosure are in accordance with Canadian generally accepted accounting principles ("GAAP") as prescribed by the Canadian Institute of Chartered Accountants ("CICA") and industry specific accounting principles as published by the Canadian Institute of Public and Private Real Estate Companies ("CIPPREC").

**b) Use of Estimates**

The preparation of the consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and revenue and expenses for the reported periods. Actual results could differ from those estimates.

**c) Principles of Consolidation**

These consolidated financial statements include the accounts of Royal Host and its wholly-owned subsidiaries, and the accounts of all partnerships, joint ventures and co-tenancies to the extent of the Royal Host proportionate interest in their respective assets, liabilities, revenues, expenses and cash flows. All inter-company transactions and balances have been eliminated.

**d) Revenue Recognition**

Revenues consisting of rooms, food and beverage and other hospitality revenues are recognized when services are provided and collection is reasonably assured. Other hospitality revenues include management fees, franchise royalties, parking, tenant leases, health club and spa, timeshare maintenance fees and sales and other. Ongoing credit evaluations are performed and an allowance for potential credit losses is provided against the portion of accounts receivable which is estimated to be uncollectible.

Timeshare revenues are recorded when the purchaser has complied with all major conditions of the sale, including the payment of the full purchase price or the arrangement of appropriate financing. Certain portions of timeshare revenue are deferred until earned by Royal Host.

**e) Capital Assets**

Hotel properties are recorded at the lower of cost less accumulated amortization or net recoverable amount. The net recoverable amount represents the estimated undiscounted projected future net cash flow generated from the property throughout its useful life, including its residual value, and is intended to determine the recovery of an investment and is not an expression of a property's fair market value.

Hotel properties are amortized using the straight-line method over their estimated useful lives ranging between 25 and 40 years. Each individual property is evaluated quarterly and a useful life is estimated based on certain factors including construction materials used, location, condition of the property and the particular capital maintenance program and requirements of the property.

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Maintenance and repair costs are expensed against operations as incurred, while significant improvements, replacements and major renovations are capitalized to hotel properties. Furniture, equipment and certain improvements are amortized on a straight-line basis over periods of up to ten years.

Intangible assets are amortized using the straight-line method based on their estimated useful lives over the following periods:

- i) Franchise rights and management contracts – 3-10 years,
- ii) Customer lists and intellectual and human capital – 1-7 years.

Property under development consists of properties under construction and are recorded at the lower of cost, including pre-development expenditures, and their net recoverable amount.

**f) Capitalized Costs**

Costs associated with the acquisition of hotel properties are capitalized to the respective hotel property. These costs typically include realty agent commissions, property transfer taxes, legal fees, environmental studies, engineering and other direct expenses.

The cost of hotel properties under development includes all expenditures incurred in connection with the activities of acquiring, developing and constructing these properties. These expenditures consist of all direct costs including interest on debt and an appropriate allocation of general and administrative costs incurred.

**g) Inventory**

Inventory consists of food, beverages, china, silverware, glassware, linen and general supplies. These items are recorded at lower of cost or net replacement value and are determined on a first-in, first-out basis.

**h) Financing Costs**

Debt financing costs are deferred and amortized on a straight-line basis over the terms of the related loans.

**i) Income Taxes**

Royal Host is taxed as a “mutual fund trust” for income tax purposes. Pursuant to the Declaration of Trust, the Trustees intend to distribute all taxable income directly earned by Royal Host to its Unitholders and to deduct such distributions and designations for income tax purposes.

Royal Host utilizes the future income tax asset and liability method of accounting for future income taxes. This method requires recording a future income tax amount for the Trust’s subsidiaries based on differences between the carrying amounts of balance sheet items and their corresponding tax basis. In addition, the future tax benefits of income tax assets, including unused tax losses, are recognized to the extent that it is more likely than not that such losses will be ultimately utilized by the Trust’s subsidiaries. Future income tax assets and liabilities are measured using the enacted tax rates and laws that are expected to apply when the tax assets or liabilities are to be either realized or settled.

**j) Unit Option Plan**

Royal Host has a unit option plan as described in Note 13(d). No compensation expense is recognized for the plan when options are granted. Consideration received on exercise of options is credited to Unitholders' equity. See Note 3 (a) for changes in accounting policy related to Stock Based Compensation Plans.

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**k) Non-GAAP Measures Reporting**

Funds from operations are calculated as the equivalent of earnings before the amortization of capital assets and future income tax (recovery) expense. This amount is determined in accordance with the Canadian Institute of Public and Private Real Estate Companies ("CIPREC") guidelines and is intended to present the funds generated before changes in the non-cash balance sheet operating accounts. It essentially displays the funds generated using the accrual basis of accounting. Readers are cautioned that funds from operations are not a defined measure of performance under Canadian generally accepted accounting principles ("GAAP"). Royal Host's calculation of funds from operations may be different than the calculation used by other entities.

**l) Cash and Cash Equivalents**

Cash and short-term investments include all cash and highly liquid investments with an original maturity of less than three months and exclude restricted cash.

**m) Foreign Currency Translation**

The Trust's foreign operations are conducted through integrated subsidiaries and financial statements are translated using the temporal method. Accordingly, monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at rates of exchange in effect at the date of the consolidated financial statements. Non-monetary assets, liabilities and other items recorded in the net earnings arising from transactions denominated in foreign currencies are translated at rates of exchange in effect at the date of the transaction. The Trust discloses exchange gains and losses as part of net earnings.

**3. CHANGES IN ACCOUNTING POLICIES**

**a) Stock Based Compensation Plans**

Effective January 1, 2002, the Trust adopted Section 3870 - Stock Based Compensation Plans of the CICA Handbook with respect to the accounting and disclosure of stock based compensation plans, which recommends that awards to employees be valued using the fair-value method of accounting.

Under CICA Section 3870, companies that elect a method other than the fair-value method of accounting are required to disclose pro forma net income and earnings per share information, using a pricing model such as the Black-Scholes model, as if the fair-value method of accounting had been used. These new rules do not apply to pre-existing awards except for those awards that call for settlement in cash and other assets.

The adoption of Handbook Section 3870 has no financial impact to the Trust on the issued unit options, under the existing unit option plan, as they were issued prior to the date of adoption.

**b) Foreign Currency Translation**

Effective January 1, 2002, the Trust adopted the amendments to Section 1650 - Foreign Currency Translation of the CICA Handbook. These amendments deal with elimination of the deferral and amortization of unrealized translation gains and losses on non-current monetary assets and liabilities and the requirement to disclose the exchange gains and losses included in net earnings. The Trust had no material deferred unrealized translation gains or losses on non-monetary assets and liabilities and therefore required no adjustments to net earnings at January 1, 2002.

**c) Goodwill & Intangible Assets**

Effective January 1, 2002, the Trust adopted Section 3062 - Goodwill and Other Intangible Assets of the CICA Handbook. In accordance with the changes provided in this section, Management evaluated the goodwill balance at January 1, 2002, totaling approximately \$21.7 million, for reclassification to intangible assets versus the traditional classification of goodwill. Upon evaluating goodwill, Management reclassified goodwill to two categories of intangible assets: (1) franchise rights and management contracts, and (2) customer lists and intellectual and

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human capital. Management evaluated the estimated useful lives of the corresponding intangible assets to ensure the amortization periods being used appropriately reflected the period of remaining benefit (Note 2(e)).

Intangible assets are recorded at the lower of net book value or net recoverable amount. Any permanent impairment would be written down in the period identified and charged against earnings.

**4. RESTATEMENT OF PRIOR PERIODS**

Royal Host's financial statements for the years ended December 31, 1998 through 2002 overstated other hospitality revenue and net earnings, resulting from the misinterpretation of documentation pertaining to the complex calculation of a priority return Royal Host receives in relation to its 50% interest in a co-tenancy hotel operation. The miscalculation has been corrected by recording a prior period adjustment with retroactive restatement. The effects of this restatement are as follows:

i) Equity (Note 13) as at January 1, 2002 decreased by \$1,197,000 to \$129,791,000. With respect to the balance sheet at December 31, 2002, Current Accounts and Notes Receivable decreased by \$258,000 to \$9,172,000; Long-term Notes Receivable and Other Assets decreased by \$1,450,000 to \$3,562,000; and Accounts Payable and Accrued Liabilities increased by \$265,000 to \$18,631,000.

ii) Other Hospitality Revenue for the year ended December 31, 2002 decreased by \$776,000 to \$20,033,000. Accordingly, Net Earnings for the year ended December 31, 2002 also decreased by \$776,000 to \$7,360,000.

iii) Other Hospitality Revenue for the three months ended December 31, 2002 decreased by \$685,000 to \$5,187,000. Accordingly, Net Earnings for the three months ended December 31, 2002 also decreased by \$685,000 to \$1,325,000.

**5. RESTRICTED CASH**

Restricted cash is \$4,247,000 (2002 - \$4,159,000) representing funds on deposit with lenders for future planned capital expenditures within the next 12 months.

**6. PER UNIT COMPUTATIONS**

There were 24,762,344 trust units outstanding as at December 31, 2003 (2002 - 24,634,976). Per unit computations are based on the weighted average number of trust units outstanding for the year, after adjusting the net earnings for payments on the convertible debentures of \$5,460,000 (2002 - \$4,933,000) and payments on the redeemable partnership units of \$1,513,000 (2002 - \$2,269,000).

For the twelve months ended:	December 31, 2003			December 31, 2002 (Restated - Note 4)		
	(\$000's)	Weighted Average Units (000's)	Per Unit	(\$000's)	Weighted Average Units (000's)	Per Unit
<b>Earnings</b>						
Net earnings	19			7,360		
Less:						
Distributions on redeemable partnership units	(1,513)			(2,269)		
Interest on 8% convertible debentures	(1,760)			(1,760)		
Interest on 9.25% convertible debentures	(3,700)			(3,173)		
<b>Basic (loss) earnings</b>	<b>(6,954)</b>	<b>24,550</b>	<b>(0.28)</b>	<b>158</b>	<b>24,454</b>	<b>0.01</b>
Unit options		852			-	
Unit option repurchase		(1,774)			-	
<b>Diluted (loss) earnings</b>	<b>(6,954)</b>	<b>23,628</b>	<b>(0.29)</b>	<b>158</b>	<b>24,454</b>	<b>0.01</b>

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In computing the diluted earnings per unit in fiscal 2003 and 2002, the convertible debentures and redeemable partnership units had an anti-dilutive impact on earnings and therefore did not impact the calculation. In computing the diluted earnings per unit in fiscal 2002, the unit options had an anti-dilutive impact on earnings and therefore did not impact the calculation.

**For the three months ended:**

	December 31, 2003			December 31, 2002 <i>(Restated - Note 4)</i>		
	(\$000's)	Weighted Average Units (000's)	Per Unit	(\$000's)	Weighted Average Units (000's)	Per Unit
<b>Earnings</b>						
Net earnings	(1,366)			1,325		
Less:						
Distributions on redeemable partnership units	(189)			(567)		
Interest on 8% convertible debentures	(444)			(444)		
Interest on 9.25% convertible debentures	(932)			(932)		
<b>Basic (loss) earnings</b>	<b>(2,931)</b>	<b>24,549</b>	<b>(0.12)</b>	<b>(618)</b>	<b>24,611</b>	<b>(0.03)</b>
Unit options		852			907	
Unit option repurchase		(1,917)			(1,564)	
<b>Diluted (loss) earnings</b>	<b>(2,931)</b>	<b>23,484</b>	<b>(0.12)</b>	<b>(618)</b>	<b>23,954</b>	<b>(0.03)</b>

In computing the diluted earnings per unit in three months ended December 31, 2003 and 2002, the convertible debentures and redeemable partnership units had an anti-dilutive impact on earnings and therefore did not impact the calculation.

**7. PROPERTY UNDER DEVELOPMENT**

A subsidiary of Royal Host is participating in a joint venture to develop a portion of the property at the Grand Okanagan Resort and Conference Center in Kelowna, British Columbia for resale. Property under development reflects Royal Host's proportionate share of the costs incurred to date to develop the property. Construction of the first phase of the project, a parkade, commenced January 2004. Revenue from the sale of land or property is recorded on closing or, where sold by way of an agreement of purchase and sale, when the agreement is duly executed and delivered. Profit from the sale of land or property is recorded on closing or, where sold by way of an agreement of purchase and sale, when the collection of the sale proceeds is reasonably assured and all other material conditions are met.

**8. LONG-TERM NOTES RECEIVABLE AND OTHER ASSETS**

	<i>(in \$000's)</i>	
	December 31, 2003	December 31, 2002 <i>(Restated - Note 4)</i>
Notes receivable	685	686
Deferred financing costs (net of accumulated amortization)	2,612	2,876
	<b>3,297</b>	<b>3,562</b>

The notes receivable mature between January 1, 2004 and March 18, 2009, require monthly payments of principal and interest based on individual customer amortization schedules, and bear interest at rates of between 8.0% and 16.9%. The carrying value of the notes receivable approximates fair value.

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**9. FUTURE INCOME TAXES**

The Trust has tax losses of approximately \$1,541,000 (2002 - \$600,000) available to reduce future taxable income. The losses will begin to expire in 2008, but the majority of the losses will expire in 2009 and 2010. The adjustment for the change in effective tax rates reflects the benefit from the reduction of the currently substantially enacted federal rate resulting in combined federal and provincial rates of between 34.1% and 39.1%, depending on the province.

The net future income tax liability is calculated as follows:

	<i>(in \$000's)</i>	
	<u>December 31, 2003</u>	<u>December 31, 2002</u>
Tax assets relating to operating losses	583	195
Tax assets (liabilities) relating to differences in tax and book basis and other items	<u>(1,350)</u>	<u>(792)</u>
Net future tax liability	<u><b>(767)</b></u>	<u><b>(597)</b></u>

**10. CAPITAL ASSETS**

	<i>(in \$000's)</i>		
	<u>Gross Book Value</u>	<u>Accumulated Amortization</u>	<u>Net Book Value</u>
<b>December 31, 2003</b>			
Land	41,433	-	41,433
Buildings	315,680	50,201	265,479
Furniture, fixtures and equipment	39,221	30,179	9,042
Furniture, fixtures and equipment under capital leases	7,292	3,126	4,166
Paving and other	1,319	400	919
	<u><b>404,945</b></u>	<u><b>83,906</b></u>	<u><b>321,039</b></u>
Capital assets under development	1,164	-	1,164
Intangible assets <i>(Note 3(c))</i>			
Franchise rights and management contracts	27,612	12,679	14,933
Customer lists and intellectual and human capital	7,270	6,070	1,200
	<u><b>440,991</b></u>	<u><b>102,655</b></u>	<u><b>338,336</b></u>

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	<i>(in \$000's)</i>		
	<u>Gross Book Value</u>	<u>Accumulated Amortization</u>	<u>Net Book Value</u>
<b>December 31, 2002</b>			
Land	38,233	-	38,233
Buildings	294,237	42,185	252,052
Furniture, fixtures and equipment	35,486	25,758	9,728
Furniture, fixtures and equipment under capital leases	5,679	2,062	3,617
Paving and other	1,239	333	906
	<u><b>374,874</b></u>	<u><b>70,338</b></u>	<u><b>304,536</b></u>
Capital assets under development	4,051	-	4,051
Intangible assets <i>(Note 3(c))</i>			
Franchise rights and management contracts	27,655	10,196	17,459
Customer lists and intellectual and human capital	7,270	5,498	1,772
	<u><b>413,850</b></u>	<u><b>86,032</b></u>	<u><b>327,818</b></u>

All hotel properties are wholly-owned by Royal Host, except one hotel property representing less than 5% of total capital assets, which is jointly owned by Royal Host and the vendor. Pursuant to the Exchange Agreement dated September 11, 1998, the vendor has an option to exchange its 50% ownership interest for units of Royal Host. The valuation of such exchange is to be determined based on a specified industry average historic capitalization rate and the units of Royal Host are to be priced based on a 20 day weighted average trading price per unit. This specified capitalization rate is not determined with reference to a base-lending rate such as prime rate. This calculation has been taken into consideration in the diluted per unit calculations in Note 6 and determined to be anti-dilutive.

On April 1, 2003, Royal Host acquired the Calgary Best Western Village Park Inn adding 160 guestrooms, for an aggregate purchase price of \$12,786,000.

On July 12, 2002, Royal Host acquired 2 hotel properties from a single vendor, adding 233 guestrooms, for an aggregate purchase price of \$11,726,000. Cash consideration was paid from the net proceeds of the 9.25% Convertible Unsecured Subordinated Debenture issued February 21, 2002.

Under the Royal Host capital replacement reserve policy, 3% of total hotel revenue is reserved to allow for the upkeep and renovation of the hotel properties. This policy may be amended from time to time at the discretion of the Trustees. On this basis, the reserve provided for the year ended December 31, 2003 would have been \$4,066,000 (2002 - \$3,736,000). As Royal Host has spent \$13,999,000 (2002 - \$6,285,000) to renovate and reposition the hotel properties, excluding capital lease additions totaling \$1,522,000 (2002 - \$123,000) and the net purchases of hotel property for an aggregate purchase price of \$12,116,000 (2002 - \$11,726,000), the Trustees have determined that no reserve would be provided for in 2003 and 2002.

As at December 31, 2003, Royal Host has no commitments to complete capital assets under development (2002 - \$550,000).

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**11. MORTGAGES AND OTHER DEBT**

	<i>(in \$000's)</i>	
	<b>December 31, 2003</b>	<b>December 31, 2002</b>
Mortgages and other debt secured by hotel properties	161,165	141,240
Less current portion	39,515	36,307
<b>Long-term obligations</b>	<b>121,650</b>	<b>104,933</b>
Principal repayments required for the years ending December 31:		
2004	39,515	
2005	28,083	
2006	3,377	
2007	20,768	
2008	2,905	
Subsequent	66,517	
	<b>161,165</b>	
<b>Supplementary Information:</b>	<b>December 31, 2003</b>	<b>December 31, 2002</b>
Cash interest paid in the years ended	13,697	12,680

On July 3, 2002, Royal Host completed financing arrangements in the amount of \$5,000,000, the proceeds to be used to renovate certain hotel properties. The loan is interest bearing at the bank's floating base rate. The loan is secured by first mortgages on the land and general security registered against certain hotel properties. As at December 31, 2003, Royal Host had received net advances of funds in the amount of \$4,848,000 related to the arranged financing.

On February 6, 2003, Royal Host completed financing in the form of a revolving operating loan, repayable on demand, available to the Trust at prime rate plus 2.0% per annum payable monthly in arrears or as a First Bank Acceptance with a Stamping Fee of 3.0% per annum. The proceeds of this loan are to be used for general working capital purposes. The loan is secured by a certain hotel property. As at December 31, 2003, Royal Host had no outstanding balance owing from net advances of funds related to the arranged financing. Currently, the maximum amount available for borrowing is \$4.0 million.

On February 5, 2003, Royal Host completed financing in the amount of \$6.2 million, the proceeds to be used for working capital and corporate purposes. This is an operating loan, repayable on demand, bearing interest at prime plus 1.0% per annum, with interest payable monthly. The loan is secured by a certain hotel property. As at December 31, 2003, Royal Host had received net advances of funds in the amount of \$3,740,000 related to the arranged financing.

On March 27, 2003, Royal Host completed two financings with one lender in the amounts of \$2.4 and \$3.7 million, the proceeds to be used for working capital and corporate purposes. These are 20 year term mortgage loans, secured by certain hotel properties. The interest is adjusted semi-annually and is the greater of:

- a) 3.2% over the yield on the Government of Canada mortgage benchmark bond; and
- b) A floor of 7.9% per annum.

All funds have been advanced by the lender.

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On September 29, 2003, Royal Host completed financing in the amount of \$8.7 million, of which the proceeds were used to pay down short-term debt and for working capital and general corporate purposes. This is a 10 year term mortgage, secured by a certain hotel property. The interest is 7.37% compounded semi-annually, and all funds have been advanced by the lender.

The current portion of the long-term debt includes a \$30.0 million portfolio loan, which becomes due March 31, 2004. Royal Host is in the process of negotiating a one year extension with the current lender under the same terms and conditions, subject to the lender's loan committee final approval.

Mortgages and other debt bear interest at rates ranging from 5.25% to 9.47% per annum (2002 – 5.25% to 9.47%) with a weighted average year-end rate of 8.62% per annum (2002 – 8.84%) and mature between 2003 and 2018. The mortgages and other debt are secured by fixed charges over specified hotel properties. Monthly principal and interest payments pursuant to the indebtedness total \$1,405,000 at December 31, 2003 (2002 - \$1,413,000).

Financing charges are deferred and amortized over the term of the related debt. In 2003, \$660,000 was included in amortization (2002 - \$774,000).

**12. OBLIGATIONS UNDER CAPITAL LEASES**

Royal Host has entered into various capital lease obligations to acquire computers and hotel furniture, fixtures and equipment. The present values of minimum lease payments under capital lease as of December 31, 2003 are as follows:

	<i>(in \$000's)</i>	
	<u>December 31, 2003</u>	<u>December 31, 2002</u>
Present value of future minimum lease payments	2,354	2,333
Less current portion	864	1,208
<b>Long-term obligations</b>	<b><u>1,490</u></b>	<b><u>1,125</u></b>
Years ending December 31		
2004	1,032	
2005	686	
2006	451	
2007	324	
2008	<u>222</u>	
Future minimum lease payments	2,715	
Amounts representing interest	<u>361</u>	
Present value of future minimum lease payments	<b><u>2,354</u></b>	

The leases outstanding at December 31, 2003 bear interest at a weighted average annual rate of 8.42% per annum (2002 – 9.99%).

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**13. EQUITY**

	<i>(in \$000's)</i>	
	<b>December 31, 2003</b>	<b>December 31, 2002</b> <i>(Restated - Note 4)</i>
<b>Balance, beginning of year, as previously reported</b>	<b>111,261</b>	<b>130,988</b>
Prior period adjustment <i>(Note 4)</i>	-	(1,197)
<b>Adjusted balance, beginning of year</b>	<b>111,261</b>	<b>129,791</b>
Net earnings	19	7,360
Issuance of trust units		
Distribution reinvestment plan	629	720
Employee unit purchase program <i>(Note 13(g))</i>	-	2,320
Employee loans pursuant to employee unit purchase program <i>(Note 13(g))</i>	8	(2,225)
Equity financing issue costs	-	(1,892)
Contributed surplus	89	-
Equity distributions		
Trust units	(11,667)	(17,611)
Redeemable partnership units	(1,513)	(2,269)
Interest paid on convertible debentures	(5,460)	(4,933)
	<b>93,366</b>	<b>111,261</b>
<b>Convertible Equity</b>		
Redeemable partnership units	27,500	27,500
Convertible debentures	62,000	62,000
	<b>89,500</b>	<b>89,500</b>
<b>Balance, end of year</b>	<b>182,866</b>	<b>200,761</b>

**a) Unit Capital**

	<b>Number of units</b>	<i>(in \$000's)</i>
<b>Balance, December 31, 2001</b>	<b>24,115,846</b>	<b>219,868</b>
Issuance of trust units		
Employee unit purchase program <i>(Note 13(g))</i>	400,000	2,320
Distribution reinvestment plan	119,130	720
<b>Balance, December 31, 2002</b>	<b>24,634,976</b>	<b>222,908</b>
Issuance of trust units		
Distribution reinvestment plan	127,368	629
<b>Balance, December 31, 2003</b>	<b>24,762,344</b>	<b>223,537</b>

As is common with REITs and other income trusts, Royal Host distributes cash in excess of the net earnings, and accordingly an accumulated deficit results, which at December 31, 2003 amounts to \$130,171,000 (2002 - \$111,647,000).

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**b) Distributions to Unitholders**

For the year ended December 31, 2003, distributions declared to Unitholders, excluding distributions on redeemable partnership units, aggregated \$11,667,000 (2002 - \$17,611,000). The distributions to holders of redeemable partnership units for fiscal 2003 were \$1,513,000 (2002 - \$2,269,000) and interest on convertible debentures was \$5,460,000 (2002 - \$4,933,000).

On the consolidated statements of cash flows, distributions paid are net of distribution reinvestment plan contributions of \$629,000 for the year ended December 31, 2003 (2002 - \$720,000). Accordingly, gross distributions for the year were \$19,749,000 (2002 - \$24,782,000).

**c) Distribution Reinvestment Plan**

Royal Host has established a Distribution Reinvestment Plan ("DRIP") that is administered by its transfer agent and has reserved 500,000 units for issue under this Plan. For the period January 2001 to July 2001, the transfer agent purchased DRIP units on the open market. Subsequent to July 2001, Royal Host has issued new units for DRIP participants out of the previously authorized reserved units.

**d) Unit Options**

Royal Host has reserved 1,883,000 units under its unit option plan. As at December 31, 2003, Royal Host has unit options outstanding to certain directors, employees and consultants to purchase an aggregated total of 852,500 units (2002 - 907,500 units), at amounts ranging from \$10.00 to \$10.50 per unit. In 2003 and 2002, the weighted average exercise price is \$10.03. All unit options were issued prior to 1999 and were fully vested and exercisable at the end of December 31, 2003 and 2002. Of these options, 797,500 options expire on October 31, 2007 (2002 - 852,500) and 55,000 options expire on March 23, 2008 (2002 - 55,000). During 2003 and 2002, no options were issued or exercised and 55,000 options expired in 2003 (2002 - Nil).

The adoption of Handbook Section 3870 - Stock Based Compensation Plans has no financial impact on the unit options under the existing unit option plan, which were issued prior to the date of adoption (see Note 3(a)).

**e) Redeemable Partnership Units**

Holders of redeemable partnership units ("Holders") are entitled to receive distributions indirectly from Royal Host equivalent to the distributions paid by Royal Host to its Unitholders, commencing on January 1, 1999. Each partnership unit is redeemable by the Holders after January 1, 2000 at a cash price equal to the market value of a Royal Host unit, or at the option of Royal Host and subject to regulatory approval, one Royal Host unit or a combination thereof.

Under certain circumstances, including a change of control ("Trigger Event"), the Holders have the right to redeem the partnership units for cash proceeds of \$27.5 million. If the Trigger Event occurs after the issuance of redeemable units but prior to January 1, 2004, then the Holders may redeem the then outstanding redeemable partnership units for cash, at the greater of \$9.00 per unit or the market price of the Royal Host units. Change in control is defined as ownership by any one entity or a group of related entities of more than 20% of the outstanding units of Royal Host. As at December 31, 2003, no Trigger Event occurred and therefore this option to the holders of the redeemable partnership units has expired.

For accounting purposes, the redeemable partnership units have equity characteristics and accordingly they are classified as equity instruments.

**f) Convertible Debentures**

**i) 8.00% Convertible Secured Debentures**

The convertible debentures of \$22,000,000 bear interest at 8% per annum and are payable monthly, at Royal Host's option, in either cash or Royal Host units of an equivalent value. In addition, upon maturity in 2003, Royal Host has the option to repay the debentures in either cash or in equivalent units of Royal Host

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on the basis that one unit has a value equal to the weighted average trading price of a unit on the Toronto Stock Exchange ("TSE") for the twenty (20) trading days immediately preceding the maturity date.

With respect to these debentures which matured on September 30, 2003, an amending agreement has been obtained that extends the maturity date of the debenture to May 31, 2004, with no changes to the interest rate, settlement options or any other condition of the initial debentures. This amending agreement anticipates a further extension of the maturity date to September 30, 2005, pending finalization of a development agreement at the Yorkdale Travelodge hotel. Accordingly, the convertible debentures have continued to be recorded as an equity instrument based on the aforementioned intended terms of extension.

**ii) 9.25% Convertible Unsecured Subordinated Debentures**

The convertible debentures of \$40,000,000 bear interest at 9.25% per annum and are payable semi-annually in arrears on March 1 and September 1 in each year commencing September 1, 2002.

On redemption or at maturity on March 1, 2007, Royal Host has the option to repay the debentures in either cash or in equivalent units of Royal Host. The number of units to be issued will be determined by dividing the principal amount of the debentures by 95% of the current market price of the units. The term "current market price" is defined in the Indenture to mean the weighted average trading price of the units on the TSE for the twenty (20) consecutive trading days ending on the fifth (5) trading day preceding the date of maturity.

The debentures will not be redeemable on or before March 1, 2005. Thereafter, the debentures will be redeemable, in whole at any time or in part from time to time, at the option of Royal Host on at least 30 days prior notice at a price equal to the principal amount thereof, plus accrued and unpaid interest, provided that the current market price preceding the date upon which notice of redemption is given is at least 125% of the conversion price of \$7.00 per unit.

Based on certain conditions, the debentures are convertible, at the holders' discretion, at \$7.00 per trust unit from date of issue to maturity at March 1, 2007.

For accounting purposes, the convertible debentures have equity characteristics and accordingly they are classified as equity instruments.

**g) Employee Unit Purchase Program**

During 2000, the Trustees approved the issuance of up to 400,000 units from treasury for an employee unit purchase program. Under this program, certain approved Royal Host employees (excluding certain senior executives) were eligible to finance the purchase of units from treasury at a prescribed per unit rate based on current market values.

As at December 31, 2003, 182,500 units were allocated under this plan. The employee unit purchase program represents a financing program for selected employees to purchase units of Royal Host. Royal Host has outstanding employee loans receivable, net of additions and terminations, of \$913,000 with respect to the program. These loans bear interest at a fixed rate of 3.0% per annum (2002 – 5.0%), a rate established based on consideration of existing institutional rates and Canada Revenue Agency ("CRA") guidelines for employee loan rates. This plan structure does not meet the definition of stock based compensation plans, and therefore does not fall under the new Handbook Section 3870 – Stock Based Compensation Plans (Note 3(a)).

In accordance with EIC ("Emerging Issues Committee") 44, for accounting purposes, these employee loans receivable have been offset against the corresponding trust units equity.

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**14. COMMITMENTS**

**a) Energy Contracts**

Royal Host has entered into long-term supply arrangements with two electrical utility companies and a natural gas provider to supply electricity and natural gas requirements for certain properties.

i. Electricity

The electricity contracts are for a term of five years at a blended rate of approximately 7.12 cents per kilowatt-hour, excluding delivery, for annual usage of approximately 14.9 million kilowatt-hours in 2004 (2003 – approximately 6.98 cents per kilowatt-hour for approximately 14.8 million kilowatt-hours).

ii. Natural Gas

The natural gas contract is for a term of five years, at a rate of approximately 26.90 cents per cubic meter, excluding delivery, on annual usage of approximately 569,000 cubic meters for 2004 (2003 – 23.22 cents per cubic meter for approximately 3.99 million cubic meters). Royal Host is not required to guarantee usage levels for any contracts.

**b) Contractual Guarantee**

Effective December 18, 2001, Royal Host management, acting in its capacity as manager of an unincorporated, independent vacation club society (“Society”) entered into a lease agreement with a party to secure, on behalf of the Society, the right to use a vacation property. The Society is not owned or controlled by Royal Host. The lease agreement temporarily obligates a Royal Host subsidiary to lease the particular vacation property for three successive 15-year terms followed by a final 5-year term. The renewal terms are automatic and substantially obligate the lessee to renew the lease for a full term of 50 years.

Effective July 8, 2003, Royal Host management fully transferred the entitlements and obligations associated with the aforementioned lease agreement to the Society. The Society has agreed to accept the entitlements and obligations associated with the lease.

Royal Host has agreed to guarantee the lease obligations of the Society for a period of five years, effective from the lease commencement date of January 1, 2002, should the Society default on any obligations. Royal Host has avenues to pursue recourse with the Society for the full extent of any default on the lease payments. The maximum potential amount of future payments for the period from January 1, 2004 to December 31, 2006 is approximately \$664,000. The estimated fair value of this obligation is \$587,000. As at December 31, 2003, the Society has not defaulted on any lease payments.

**c) Other Guarantees and Indemnifications**

In the normal course of business, the Trust may provide indemnification to counterparties in transactions such as credit facilities, leasing transactions, service arrangements, director and officer indemnification agreements and sales of assets. These indemnification agreements may require the Trust to compensate the counterparties for costs incurred as a result of changes in laws and regulations (including tax legislation) or as a result of litigation claims or statutory sanctions that may be suffered by counterparties as a consequence of the transaction. The terms of these indemnification agreements may vary based on the contract and do not provide any limit on the maximum potential liability. To date, the Trust has not made any significant payments under such indemnifications and no amount has been accrued in the financial statements with respect to these indemnification agreements.

In the normal course of business, the Trust may enter into various agreements that may meet the AcG-14 definition of a guarantee. AcG-14 defines a guarantee to be a contract (including an indemnity) that contingently requires the Trust to make payments to the guaranteed party based on (i) changes in an underlying interest rate, foreign exchange rate, equity or commodity instrument, index or other variable, that is related to an asset, a liability or an equity security of the counterparty, (ii) failure of another party to perform under an obligating agreement or, (iii) failure of a third party to pay its indebtedness when due.

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**15. OTHER HOSPITALITY REVENUES**

In 2002, other hospitality revenues included rental income from one hotel property in Yellowknife, Northwest Territories that was leased to the previous owner for a fixed fee of \$2,015,000 per annum. The lease had a renewal option to the tenant for a further three additional 5-year terms, commencing October 31, 2002. The tenant did not exercise the renewal option.

On November 1, 2002, Royal Host commenced operation of the Yellowknife property after expiration of the aforementioned tenant lease contract. The property is a 130 room full-service hotel and is connected to a shopping mall, containing 24,752 net leasable square feet, in which the hotel maintains an approximate 1/3 interest.

**16. FRANCHISE AND MEMBERSHIP AGREEMENTS**

Under the terms of the hotel franchise agreements expiring at various dates commencing October 31, 2007 through to December 12, 2021, annual payments for franchise expenses (including fees, reservation and advertising services) are due to external parties for 35 of the 39 hotels owned by Royal Host (2002 - 35 of the 38 hotels). In 2002, Royal Host acquired two hotel properties for which the franchise fees are paid to an external party.

In 2003, Royal Host acquired a hotel property (see Note 10) that required it to enter into a membership agreement for which the member fees are paid to an external party. The membership agreement is for one-year terms, renewable annually at the end of the membership organization's fiscal year (November 30).

The franchise royalties and membership fees paid to external parties are calculated based upon percentages of defined revenues and amounted to \$2,233,000 for the year (2002 - \$2,010,000).

**17. OPERATING LEASES**

Certain property and equipment is leased under operating lease agreements expiring at varying intervals. The following is a five-year schedule for future minimum rental payments required under these leases as at December 31, 2003:

**Years ending December 31 (\$000's)**

2004	743
2005	427
2006	245
2007	148
2008	82
Total future minimum rental payments	<u>1,645</u>

**18. RISK MANAGEMENT**

Royal Host's key financial risk exposures include credit risks arising from receivables from corporate accounts and amounts owed by purchasers of timeshares, commodity price risk on utilities and interest rate risk arising from fluctuations in interest rates.

Credit risks are minimized, as amounts due from any one debtor are not significant and routine credit assessments are carried out prior to credit being granted. The accounts receivable from timeshare owners are secured by the timeshares purchased.

Commodity price risk is managed through the use of fixed price contracts, where available, for the stable supply of natural gas and electricity in the jurisdictions where such commodities have been de-regulated.

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Interest rate risk is continually monitored and managed through limiting the amount of variable rate debt as well as the total amount of debt. The amount of variable rate debt aggregated \$9,157,000 or 4.1% of the Royal Host total debt portfolio as at December 31, 2003 (2002 - \$1,660,000 or 1.2%). Variable rates for 2003 ranged from prime plus 3/4% to prime plus 2.0% (2002 - prime plus 3/4% to prime plus 1.5%).

**19. FAIR VALUES**

Current assets and liabilities approximate their carrying values at December 31, 2003, due to their short-term nature. The fair values of the non-current portion of mortgages and other debt and convertible equity instruments are as follows:

<i>(in \$000's)</i>	<b>Carrying Values</b>	<b>Fair Values</b>
Mortgages and other debt	121,650	127,043
Capital leases	1,490	1,493
Redeemable partnership units and convertible debentures	89,500	88,845

Fair value estimates are made at a specific point in time based on relevant market information. These are estimates and involve uncertainties and matters of significant judgment and cannot be determined with precision. Changes in assumptions and estimates could significantly affect fair values.

**20. COMPARATIVE FIGURES**

Certain prior year's figures have been reclassified to conform to the presentation adopted for 2003. In addition, for 2002 Royal Host adopted the practice of classifying restricted cash held by lenders (see Note 5) as a non-current item.