Management's Responsibility for Financial Reporting

The consolidated financial statements, management's discussion and analysis (MD&A) and all financial information contained in the annual report are the responsibility of management. The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards and, where appropriate, have incorporated estimates based on the best judgment of management.

To discharge its responsibility for financial reporting, management is responsible for implementing and maintaining adequate internal controls to provide reasonable assurance that the Company's assets are safeguarded, that transactions are properly authorized and that reliable financial information is relevant, accurate and available on a timely basis.

The consolidated financial statements have been examined by PricewaterhouseCoopers LLP, the Company's external auditors. The external auditors are responsible for examining the consolidated financial statements and expressing their opinion on the fairness of the financial statements in accordance with International Financial Reporting Standards. The auditor's report outlines the scope of their audit examination and states their opinion.

The Board of Directors, through the Audit Committee, is responsible for ensuring management fulfills its responsibilities for financial reporting and internal controls. The Audit Committee is comprised of three financially literate and independent directors. This committee meets regularly with management and the external auditors to review significant accounting, financial reporting and internal control matters. PricewaterhouseCoopers LLP have unrestricted access to the Audit Committee with and without the presence of management. The Audit Committee reviews the financial statements, the auditor's report, and MD&A and submits its report to the Board of Directors for formal approval. The Audit Committee is also responsible for reviewing and recommending the annual appointment of external auditors and approving the external audit plan. These consolidated financial statements and Management's Discussion and Analysis have been approved by the Board of Directors for inclusion in the Annual Report based on the review and recommendation of the Audit Committee.

Brian Baker
President &Chief Executive Officer

Naomi Stefura, CA
Chief Financial Officer

Edmonton, Alberta
March 15, 2017

March 15, 2017

Independent Auditor's Report

To the Shareholders of
Melcor Developments Ltd.

We have audited the accompanying consolidated financial statements of Melcor Developments Ltd. and its subsidiaries, which comprise the consolidated statements of financial position as at December 31, 2016 and December 31, 2015 and the consolidated statements of income, comprehensive income, changes in equity and cash flows for the years then ended, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

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

Auditor's responsibility
Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

PricewaterhouseCoopers LLP
TD Tower, 10088 102 Avenue NW, Suite 1501, Edmonton, Alberta, Canada T5J 3N5
T: +1 780 441 6700, F: +1 780 441 6776

"PwC" refers to PricewaterhouseCoopers LLP, an Ontario limited liability partnership.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Melcor Developments Ltd. and its subsidiaries as at December 31, 2016 and December 31, 2015 and their financial performance and their cash flows for the years then ended in accordance with International Financial Reporting Standards.

PricewaterhouseCoopers LLP

Chartered Professional Accountants

MELCOR DEVELOPMENTS LTD.

Consolidated Financial Statements

December 31, 2016

Consolidated Statement of Income

For the years ended December 31 ($000s)	2016	2015
Revenue (note 21)	242,461	263,309
Cost of sales (note 21)	(134,047)	(142,662)
Gross profit	108,414	120,647
General and administrative expense (note 21)	(20,757)	(23,691)
Fair value adjustment on investment properties (note 10, 21 and 28)	15,795	9,574
Adjustments related to REIT units (note 25)	(21,466)	17,679
Gain on sale of assets	37	58
Operating earnings	82,023	124,267
Interest income	1,178	2,427
Foreign exchange gains (loss)	(412)	1,008
Finance costs (note 20)	(25,814)	(27,178)
Net finance costs	(25,048)	(23,743)
Income before income taxes	56,975	100,524
Income tax expense (note 22)	(22,542)	(24,566)
Net income for the year	34,433	75,958
Earnings per share attributable to Melcor's shareholders (note 17):		
Basic earnings per share	1.04	2.29
Diluted earnings per share	1.04	2.29

See accompanying notes to the consolidated financial statements.

On behalf of Melcor's Board of Directors

Gordon J. Clanachan, FCA
Audit Committee Chair

Timothy C. Melton
Executive Chairman

Consolidated Statement of Comprehensive Income

For the years ended December 31 ($000s)	2016	2015
Net income for the year	**34,433**	75,958
Other comprehensive income		
Items that may be reclassified subsequently to net income:		
Currency translation differences (note 18)	**(3,515)**	18,682
Comprehensive income	**30,918**	94,640

See accompanying notes to the consolidated financial statements.

Consolidated Statement of Financial Position

($000s)	2016	2015
ASSETS		
Cash and cash equivalents	**39,892**	48,674
Restricted cash (note 3b)	**—**	2,288
Accounts receivable	**16,918**	18,744
Income taxes recoverable	**1,909**	2,455
Agreements receivable (note 8)	**116,244**	152,183
Land inventory (note 9)	**680,260**	696,802
Investment properties (note 10 and 28)	**970,693**	904,348
Property and equipment (note 11)	**15,507**	16,269
Other assets (note 12)	**50,565**	50,206
	1,891,988	1,891,969
LIABILITIES		
Accounts payable and accrued liabilities (note 13)	**35,274**	40,534
Income taxes payable	**—**	1,342
Provision for land development costs (note 14)	**91,584**	93,839
General debt (note 15)	**608,611**	631,008
Deferred income tax liabilities (note 22)	**67,458**	66,875
REIT units (note 25 and 28)	**94,340**	80,401
	897,267	913,999
SHAREHOLDERS' EQUITY		
Equity attributable to Melcor's shareholders		
Share capital (note 16a)	**72,137**	70,061
Contributed surplus	**2,594**	2,743
Accumulated other comprehensive income (AOCI) (note 18)	**25,190**	28,705
Retained earnings	**894,800**	876,461
	994,721	977,970
	1,891,988	1,891,969

See accompanying notes to the consolidated financial statements.

Consolidated Statement of Changes in Equity

($000s)	Share capital	Contributed surplus	AOCI	Retained earnings	Total equity
	Equity attributable to Melcor's shareholders				
Balance at January 1, 2016	**70,061**	**2,743**	**28,705**	**876,461**	**977,970**
Net income for the year	**—**	**—**	**—**	**34,433**	**34,433**
Cumulative translation adjustment (note 18)	**—**	**—**	**(3,515)**	**—**	**(3,515)**
Transactions with equity holders					
Dividends	**—**	**—**	**—**	**(15,967)**	**(15,967)**
Share repurchase (note 16a)	**(26)**	**—**	**—**	**(127)**	**(153)**
Employee share options					
Value of services recognized	**—**	**302**	**—**	**—**	**302**
Share issuance	**2,102**	**(451)**	**—**	**—**	**1,651**
Balance at December 31, 2016	**72,137**	**2,594**	**25,190**	**894,800**	**994,721**

($000s)	Share capital	Contributed surplus	AOCI	Retained earnings	Total equity
	Equity attributable to Melcor's shareholders				
Balance at January 1, 2015	67,767	2,947	10,023	820,598	901,335
Net income for the year	—	—	—	75,958	75,958
Cumulative translation adjustment (note 18)	—	—	18,682	—	18,682
Transactions with equity holders					
Dividends	—	—	—	(19,914)	(19,914)
Share repurchase (note16a)	(34)	—	—	(181)	(215)
Employee share options					
Value of services recognized	—	339	—	—	339
Share issuance	2,328	(543)	—	—	1,785
Balance at December 31, 2015	70,061	2,743	28,705	876,461	977,970

See accompanying notes to the consolidated financial statements.

Condensed Consolidated Statement of Cash Flows

For the years ended December 31 ($000s)	2016	2015
CASH FLOWS FROM (USED IN)		
OPERATING ACTIVITIES		
Net income for the year	34,433	75,958
Non cash items:		
Amortization of tenant incentives (note 12)	6,344	6,045
Depreciation of property and equipment (note 11)	1,571	1,705
Stock based compensation expense (note 16f)	302	339
Non cash financing costs	1,179	1,627
Straight-line rent adjustment	(2,302)	(1,949)
Fair value adjustment on investment properties (note 10, 21 and 28)	(15,795)	(9,574)
Fair value adjustment on REIT units (note 25 and 28)	13,939	(25,261)
Gain on sale of assets	(37)	(58)
Deferred income taxes (note 22)	628	3,490
Cash provided by operating activities before changes in non-cash working capital	40,262	52,322
Agreements receivable	33,729	15,590
Development activities (note 3u)	15,010	(4,794)
Payment of tenant incentives and direct leasing costs	(6,362)	(6,797)
Change in restricted cash (note 3d)	1,041	64
Purchase of raw land (note 9)	(9,754)	(2,500)
Operating assets and liabilities (note 3u)	(4,929)	(23,349)
	68,997	30,536
INVESTING ACTIVITIES		
Purchase of investment properties	(38,720)	(18,620)
Additions to investment properties (note 10)	(14,768)	(31,254)
Net proceeds from disposal of investment properties (note 10)	38,961	84,241
Purchase of property and equipment (note 11)	(829)	(1,139)
Proceeds from disposal of asset	57	71
	(15,299)	33,299
FINANCING ACTIVITIES		
Revolving credit facilities	(54,019)	17,561
Proceeds from general debt	86,467	91,371
Repayment of general debt	(80,589)	(124,800)
Change in restricted cash (note 3d)	1,247	593
Repurchase of REIT units	—	(1,000)
Dividends paid	(15,967)	(19,914)
Common shares repurchased (note 16a)	(153)	(215)
Share capital issued	1,651	1,785
	(61,363)	(34,619)
FOREIGN EXCHANGE GAIN (LOSS) ON CASH HELD IN A FOREIGN CURRENCY	(1,117)	447
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS DURING THE YEAR	(8,782)	29,663
CASH AND CASH EQUIVALENTS, BEGINNING OF THE YEAR	48,674	19,011
CASH AND CASH EQUIVALENTS, END OF THE YEAR	39,892	48,674

See accompanying notes to the consolidated financial statements.

1. DESCRIPTION OF THE BUSINESS

We are a real estate development company with community development, property development, investment property, REIT and recreational property divisions. We develop, manage and own mixed-use residential communities, business and industrial parks, office buildings, retail commercial centres, and golf courses.

Melcor Developments Ltd. ("Melcor" or "we") is incorporated in Canada. The registered office is located at Suite 900, 10310 Jasper Avenue Edmonton, AB T5J 1Y8. We operate in Canada and the United States ("US"). Our shares are traded on the Toronto Stock Exchange under the symbol "MRD". As at December 31, 2016 Melton Holdings Ltd. holds approximately 47.2% of the outstanding shares and pursuant to IAS 24, Related party disclosures, is the ultimate controlling shareholder of Melcor.

As at March 15, 2017, Melcor, through an affiliate, holds an approximate 56.7% effective interest in Melcor REIT ("REIT" or "the REIT") through ownership of all Class B LP Units of the Partnership and is the ultimate controlling party. Melcor continues to manage, administer and operate the REIT and its properties under an asset management agreement and property management agreement. Trust units of the REIT are traded on the Toronto Stock Exchange under the symbol "MR.UN".

2. BASIS OF PRESENTATION

We prepare our consolidated financial statements in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") as set out in Part I of the Chartered Professional Accountants ("CPA") Handbook.

Our consolidated financial statements have been prepared in accordance with IFRS. These consolidated financial statements were authorized for issue by the Board of Directors on March 15, 2017.

3. SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies used in the preparation of these consolidated financial statements are described below.

a. Basis of measurement

Our consolidated financial statements have been prepared under the historical cost convention, except for investment properties, derivatives and REIT units which are measured at fair value.

We prepare our financial statements in conformity with IFRS which requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying our accounting policies. Changes in assumptions may have a significant impact on the consolidated financial statements in the period the assumptions change. We believe that the underlying assumptions are appropriate. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in notes 6 and 5 respectively.

b. Basis of consolidation

These consolidated financial statements include:

I. The accounts of Melcor Developments Ltd. and its wholly-owned subsidiaries:

- Melcor Developments Arizona, Inc.
- Melcor Lakeside Inc.
- Stanley Investments Inc.
- Melcor REIT Holdings GP Inc.
- Melcor REIT Holdings Limited Partnership
- Melcor Homes Ltd.
- Lethcentre Inc.

II. The accounts of Melcor REIT Limited Partnership (the Partnership) (56.7% owned by Melcor Developments Ltd). The remaining 43.3% publicly held interest in the REIT is presented as a liability in our consolidated financial statements. Refer to notes 7 and 25 for details related to our interest in the REIT.

III. Investments in 28 joint arrangements (2015 – 29) with interests ranging from 7% to 60%. These arrangements are undivided interests in the assets, liabilities, revenue and expenses and we record our proportionate share in accordance with the agreements. Refer to note 23 for details on joint arrangements.

All intercompany transactions and balances are eliminated on consolidation.

c. Cash and cash equivalents

Cash and cash equivalents are comprised of cash and short-term deposits with maturity dates of less than three months from the date they were acquired.

d. Restricted cash

Restricted cash can only be used for specified purposes. Our restricted cash represents subsidies funded by Melcor as part of the formation of the REIT to subsidize finance costs on assumed debt and Class C LP Units, and to fund capital expenditures, environmental expenditures, tenant incentives and lease costs. On May 1, 2016 the term of the covenant elapsed, at which point the remaining restricted cash was re-classified to cash and cash equivalents.

e. Land inventory

Land inventory is recorded at the lower of cost and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less costs to complete the development and selling costs. Cost includes all costs incurred to purchase development land, capitalized carrying costs related to holding the land under development, and development costs to build infrastructure. The estimated unexpended portion of costs to complete building the infrastructure, which are classified as "provision for land development costs" (refer to note 3j), are recorded as a liability upon the approval of the development plan with the municipality.

The cost of land and carrying costs are allocated to each phase of development based on a prorated acreage of the total land parcel at the time a plan is registered with a municipality. The cost of sale of a lot is allocated on the basis of the estimated total cost of the project prorated by the anticipated selling price of the lot over the anticipated selling price of the entire project at the date of plan registration.

Where we acquire land subject to deferred payments greater than one year, it is initially recognized at the fair value of the future estimated contractual obligations.

f. Investment properties

Investment properties include commercial, industrial, and residential properties, and a manufactured home community held for the long term to earn rental income or for capital appreciation, or both. It also includes properties under development for future use as investment properties.

Acquired investment properties are measured initially at cost, including related transaction costs associated with the acquisition when the acquisition is accounted for as an asset purchase. Costs capitalized to properties under development include direct development and construction costs, borrowing costs, and property taxes.

After initial recognition, investment properties are recorded at fair value, determined based on the accepted valuation methods of direct income capitalization or discounted future cash flows.

Melcor Developments Ltd. has an internal valuation team consisting of individuals who are knowledgeable and have experience in the fair value techniques applied in valuing investment property. At least once every two years, the valuations are performed by qualified external valuators who hold recognized and relevant professional qualifications and have recent experience in the location and category of the investment property being valued. Changes in fair value are recognized in the consolidated statements of income and comprehensive income in the period in which they arise.

Fair value measurement of an investment property under development is only applied if the fair value is considered to be reliably measurable. In rare circumstances, investment property under development is carried at cost until its fair value becomes reliably measurable. It may sometimes be difficult to determine reliably the fair value of an investment property under development. In order to evaluate whether the fair value of an investment property under development can be determined reliably, management considers the following factors, among others:

- the provisions of the construction contract;
- the stage of completion;
- whether the project or property is standard (typical for the market) or non-standard;
- the level of reliability of cash inflows after completion;

- the development risk specific to the property;
- past experience with similar construction; and
- status of construction permits.

Subsequent expenditures are capitalized to the asset's carrying amount only when it is probable that future economic benefits associated with the expenditure will flow to Melcor and the cost of the item can be measured reliably. All repairs and maintenance costs are expensed when incurred.

Initial direct leasing costs incurred in negotiating and arranging tenant leases are added to the carrying amount of investment properties. All direct leasing costs are external expenditures and no amounts for internal allocations are capitalized with respect to the negotiation or arranging of tenant leases.

g. Property and equipment

Property and equipment is initially measured at cost, which includes expenditures that are directly attributable to the acquisition of the asset. Subsequent to its initial recognition, property and equipment is carried at cost less accumulated depreciation and any accumulated impairment losses.

The major categories of property and equipment are depreciated using the declining balance method of depreciation as follows:

Buildings	4%
Golf course greens and tees	6%
Golf course equipment	20-30%
Corporate assets	20-50%

Property and equipment is tested for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable. For the purpose of measuring recoverable amounts, assets are grouped at the lowest levels for which there are separately identifiable cash inflows. The recoverable amount is the higher of an asset's fair value less costs to sell and the discounted expected future cash flows of the relevant asset or group of assets. An impairment loss is recognized for the amount by which the asset or group of assets' carrying amount exceeds its recoverable amount.

We evaluate impairment losses for potential reversals when events or circumstances warrant such consideration.

h. Other assets

Other assets include prepaid expenses, inventory, deposits, straight-line rent adjustments and tenant incentives incurred in respect of new or renewed leases. Tenant incentives are amortized on a straight-line basis over the lease term and are recorded as a reduction of revenue.

i. Borrowing costs

General and specific borrowing costs attributable to the acquisition, construction or production of qualifying assets are added to the cost of those assets. Borrowing costs are capitalized while acquisition or construction is actively underway and ceases once the asset is substantially complete, or suspended if the development of the asset is suspended. The amount of borrowing cost capitalized is determined by applying a weighted average cost of borrowings to qualifying assets. Qualifying assets include our land under development and investment properties under development assets. All other borrowing costs are recognized as finance costs in the consolidated statement of income in the period in which they are incurred.

j. Provision for land development costs

We recognize a provision for land development related to the construction, installation and servicing of municipal improvements related to subdivisions under development once we have an approved development agreement with the municipality, as this is the point in time when an obligation arises. The provision is recognized as a liability with an equal amount capitalized to land inventory. Provisions for land development are measured at management's best estimate of the expenditure required to complete the approved development plan at the end of the reporting period. Adjustments are made to the liability with a corresponding adjustment to cost of sales as actual costs are incurred. Provisions are discounted, where material, by discounting the expected future cash flows at a rate that reflects risk specific to the provision and the time value of money.

k. Provision for decommissioning obligations

Decommissioning obligations are measured at the present value of the expected cost to settle the obligation. Subsequent to the initial measurement, the obligation is adjusted at the end of each period to reflect the passage of time and changes in the estimated future cash flows as well as any changes in the discount rate. Increases or decreases in the provision are recognized as an expense or income. Actual costs incurred upon settlement of the decommissioning obligation are recorded against the provision.

l. Recognition of revenue

Revenue is generated from the sale of developed land, rental of investment properties, management fees, and the operation of golf courses.

Revenue from the sale of developed land is recognized when a minimum of 15% of the sale price has been received, the sale is unconditional and possession has been granted.

Management fee revenue is comprised of fees paid by our joint arrangement partners based on development and/or sales activities, which fluctuates period to period depending on the stage of various projects.

Revenue from rental of investment properties includes base rents, recoveries of operating expenses including property taxes, parking revenue and incidental income. Tenant leases are accounted for as operating leases given that we have retained substantially all of the risks and benefits of the ownership of our investment properties. Revenue recognition under a lease commences when the tenant has a right to use the leased asset. The total amount of contractual rent to be received from operating leases is recognized on a straight-line basis over the term of the lease; a straight-line rent receivable, which is included in other assets, is recorded for the difference between the rental revenue recognized and the contractual amount received. When incentives are provided to our tenants, the cost of these incentives is recognized over the lease term, on a straight-line basis, as a reduction to rental revenue. Recoveries from tenants are recognized as revenues in the period in which the corresponding costs are incurred.

Revenue from golf courses is recognized in the accounting period in which the services are provided.

m. Income taxes

Current income tax is the expected amount of tax payable to the taxation authorities, using tax rates enacted, or substantively enacted, at the end of the reporting period, and any adjustment to tax payable in respect of previous years.

Deferred income tax is recognized using the liability method based on the temporary differences between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax assets are the result of recognizing the benefit associated with deductible temporary differences, unused tax credits, and tax loss carryforwards. The carrying amount of the deferred tax liabilities and assets is determined on a non-discounted basis using tax rates and laws that have been enacted or substantively enacted at the reporting period date and are expected to apply when the deferred tax asset or liability is settled. Deferred tax assets are recognized to the extent that it is probable that the assets can be recovered.

We presume that investment property measured at fair value will be recovered entirely through sale. Measurement of the related deferred taxes reflects the tax consequences of recovering the carrying amount through sale.

The REIT qualifies as a mutual fund trust within the meaning of the Income Tax Act (Canada) (“Tax Act”) and as a real estate investment trust eligible for the ‘REIT Exception’, as defined in the rules applicable to Specified Investment Flow-Through (“SIFT”) trusts and partnerships in the Tax Act. We expect to allocate all of the REIT’s taxable income and to continue to qualify for the REIT Exception. As the REIT is a flow-through entity, we record current and deferred taxes on our 56.7% interest in the REIT.

n. Stock based compensation

We use the Black-Scholes option pricing model to fair value stock options granted to our employees. The estimated fair value of options on the date of grant is recognized as compensation expense on a graded vesting basis over the period in which the employee services are rendered. We estimate the number of expected forfeitures at the grant date and make adjustments for actual forfeitures as they occur.

o. Earnings per share

Basic earnings per share (“EPS”) is calculated by dividing our net income for the period by the weighted average number of common shares outstanding during the period.

Diluted EPS is calculated by adjusting the weighted average number of common shares outstanding for dilutive instruments. The number of shares included with respect to options, warrants, and similar instruments is computed using the treasury stock method. Our potentially dilutive common shares comprise stock options granted to employees.

p. Foreign currency

The consolidated financial statements are presented in Canadian dollars, which is the functional currency for our Canadian operations and our presentation currency.

Assets and liabilities of our US operations, for which the functional currency is the US dollar, are translated into our presentation currency at the exchange rates in effect at the reporting period end date and revenues and expenses are translated at average exchange rates for the period. Gains or losses on translation of foreign operations are recognized as other comprehensive income or loss.

Gains or losses on the settlement of debt or on foreign exchange cash balances are recognized in income in the period realized.

q. Financial instruments

At initial recognition, we classify our financial instruments in the following categories depending on the purpose for which the instruments were acquired:

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans to third parties and receivables are initially recognized at fair value plus transaction costs. Subsequently, loans and receivables are measured at amortized cost using the effective interest method less a provision for impairment, if necessary. Loans and receivables are comprised of accounts receivable, agreements receivable, restricted cash and cash and cash equivalents.

At each reporting date, we assess whether there is objective evidence that a financial asset is impaired, considering delinquencies in payments and financial difficulty of the debtor. The amount of the loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. The carrying amount of the asset is reduced through use of an allowance account. The amount of any losses is recognized in income.

Financial liabilities

Other liabilities are initially recognized at fair value, net of any transaction costs incurred. Other liabilities include accounts payable and accrued liabilities, and general debt. REIT Units are classified as fair value through profit or loss ("FVTPL").

We record our financial liabilities at fair value on initial recognition. Subsequently, "other liabilities" are measured at amortized cost using the effective interest rate method and financial liabilities designated as FVTPL are remeasured at fair value with changes in their fair value recorded through income.

r. Non-controlling interest in Melcor REIT

We hold an effective 56.7% interest in the REIT through ownership of all Class B LP Units. A non-controlling interest, REIT units, has been recognized on the statement of financial position to reflect the 43.3% interest held by the public through ownership of all trust units. The trust units are redeemable at the option of the holder and, therefore, are considered a puttable instrument in accordance with International Accounting Standard ("IAS") 32, Financial Instruments – Presentation ("IAS 32"). Certain conditions under IAS 32 allow the REIT to present the trust units as equity; however, on consolidation we do not meet these conditions and therefore must present the non-controlling interest as a financial liability.

As a financial liability designated as fair value through profit or loss ("FVTPL") we recorded the REIT units at fair value on initial recognition. Subsequent to initial recognition we remeasure the liability each period at fair value based upon the trust unit's closing trading price. Fair value gains and losses are recorded through income in the period they are incurred.

Distributions on trust units are recognized in the period in which they are approved and are recorded as an expense in income. For presentation purposes we aggregate the distribution expense with the fair value adjustment on the trust units under the caption 'adjustments related to REIT units'.

s. Financial derivatives

Our financial derivatives include interest rate swaps and the conversion feature on the REIT convertible debenture. Derivatives are initially recognized at fair value on the date a derivative contract is entered into and subsequently remeasured at their fair value. The host instrument financial liability is recognized initially at the fair value of a similar liability that does not have conversion feature. The conversion feature is separated from the host instrument and recognized at fair value. The fair value of the host instrument is recorded net of any related transaction costs. The method of recognizing the resulting gain or loss depends on whether the derivative is designated as a hedging instrument and, if so, the nature of the item being hedged.

Derivative instruments are recorded in the consolidated statement of financial position at their fair value. Changes in fair value of derivative instruments that are not designated as hedges for accounting purposes are recognized in the income statement.

Melcor has not designated any derivatives as hedges for accounting purposes.

t. Operating segments

Our operating segments are strategic business units that offer different products and services, and are reported in a manner consistent with the internal reporting provided to the chief operating decision maker. The accounting policies of the segments are the same as those described in the summary of significant accounting policies.

u. Statement of cash flows

Development activities is defined as the net change of land inventory and the provision for land development costs and excludes the purchase of raw land. Purchase of raw land is the cost of land net of vendor financing received (see note 9 – land inventory).

Operating assets and liabilities is defined as the net change of accounts receivable, deposits, prepaids and inventory, income taxes payable, accounts payable and accrued liabilities and deferred finance costs capitalized during the year. Excluded from operating assets and liabilities are investment property additions that are unpaid and included in accounts payable and accrued liabilities at year end.

4. ACCOUNTING STANDARD CHANGES

a. New and amended standards adopted

We have adopted the following new standard interpretation effective January 1, 2016.

i. ***IAS 1, Presentation of Financial Statements,*** was amended to clarify guidance on materiality and aggregation, the presentation of subtotals, the structure of financial statements and the disclosure of accounting policies.

   Adoption of this amended standard did not require any changes to the financial statements or disclosure of accounting policies.

ii. ***IFRS 11, Accounting for Acquisitions of Interests in Joint Operations,*** was amended to provide specific guidance on accounting for the acquisition of an interest in a joint operation that is a business.

   Adoption of this amended standard did not require any adjustment to the method of accounting for the joint operations in the financial statements.

Other standards, amendments and interpretations that were effective for the year beginning January 1, 2016 are not material to Melcor.

b. New standards not yet adopted

i. ***IAS 7, Statement of Cash Flows*** was amended to require disclosures about changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes.

   This amendment is effective for the years beginning on or after January 1, 2017.

ii. ***IAS 12, Income Taxes*** was amended to clarify (i) the requirements for recognizing deferred tax asset on unrealized losses, (ii) deferred tax where an asset is measured at fair value below the asset’s tax base and (iii) certain other aspects of accounting for deferred tax assets.

   This amendment is effective for years beginning on or after January 1, 2017.

iii. ***IFRS 2, Share-Based Payments*** was amended to address (i) certain issues related to the accounting for cash settled awards and (ii) the accounting for equity settled awards that include a “net settlement” feature in respect of employee withholding taxes.

This amendment is effective for years beginning on or after January 1, 2018.

iv. ***IFRS 15, Revenue from Contracts with Customers*** was issued in May 2014 by the IASB and supersedes IAS 18, 'Revenue', IAS 11,'Construction Contracts' and other interpretive guidance associated with revenue recognition. IFRS 15 provides a single model to determine how and when an entity should recognize revenue, as well as requiring entities to provide more informative, relevant disclosures in respect of its revenue recognition criteria.

IFRS 15 is to be applied to each prior reporting period presented retrospectively or through the recognition of the cumulative effect to opening retained earnings.

An amendment was issued in September 2015 to defer the effective date of IFRS 15 to the first interim period within years beginning on or after January 1, 2018.

An amendment to IFRS 15 was issued in April 2016 to clarify the guidance on identifying performance obligations, licenses of intellectual property and principal versus agent, and to provide additional practical expedients on transition. Amendments are effective for annual reporting periods beginning on or after January 1, 2018.

v. ***IFRS 9, Financial Instruments*** was issued in its finalized version in July 2014 to replace IAS 39. The IASB has previously published versions of IFRS 9 that introduced a new classification and measurement model with only two classification categories, ‘amortized cost’ and ‘fair value’ (in 2009 and 2010), and a new hedge accounting model in 2013.

This final version introduces a third measurement category, ‘fair value through other comprehensive income’, for financial assets, as well as an expected loss impairment model that requires more timely recognition of expected credit losses. Additional disclosures on transition from IAS 39 to IFRS 9 will be required under IFRS 7, the application of which is effective on adoption of IFRS 9.

IFRS 9 is required to be applied for accounting periods beginning on or after January 1, 2018, with earlier adoption permitted.

vi. ***IFRS 16, Leases*** was issued in January 2016 by the IASB to replace IAS 17. IFRS 16 includes several changes in the method of accounting for operating leases, including:

(i) All leases will be on the balance sheet of lessees, except those that meet the limited exception criteria;

(ii) Rent expense for leases on the balance sheet will be recorded as depreciation and finance expenses;

(iii) Timing of expenses will change as the finance lease model results in an accelerated recognition of expenses compared to a straight-line operating lease model.

IFRS 16 is required to be applied for annual periods beginning on or after January 1, 2019

We are currently assessing the impact of adopting these standards on our consolidated financial statements.

5. CRITICAL ACCOUNTING ESTIMATES

We make estimates and assumptions that affect the carrying amounts of assets and liabilities, disclosure of contingent liabilities and the reported amount of income for the period. Actual results could differ from estimates previously reported. The estimates and assumptions that are critical to the determination of the amounts reported in the financial statements relate to the following:

a. Valuation of agreements receivable

We review our agreements receivable on a regular basis to estimate the risk of default on outstanding balances. Factors such as the related builder’s reputation and financial status, the geographic location of the lot, and length of time the agreement receivable has been outstanding are all considered when estimating any impairment on agreements receivable. Refer to note 27 (a) for further information related to credit risk associated with agreements receivable.

b. Valuation of investment properties

The fair value of investment property is dependent on stabilized net operating income or forecasted future cash flows and property specific capitalization or discount rates. The stabilized net operating income or forecasted future cash flows involve assumptions of future rental income, including estimated market rental rates and vacancy rates, estimated direct operating costs and estimated capital expenditures. Capitalization and discount rates take into account the location, size and quality of the property, as well as market data at the valuation date.

Refer to note 28 for further information about methods and assumptions used in determining fair value.

c. Determination of the provision for land development costs

We estimate the future costs of completing the development of land by preparing internal budgets of costs and reviewing these estimates regularly to determine if adjustments to increase or decrease the provision for land development costs are required. This estimate impacts the measurement of cost of sales reported given that land inventory is sold prior to all costs being committed or known as the nature of land development considers a long-term time frame to complete all municipal requirements.

d. Income taxes

Significant estimates are required in determining our provision for income taxes. We recognize liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the current tax and deferred tax provision.

The deferred tax assets recognized at December 31, 2016 are supported by future profitability assumptions over a five-year horizon. In the event of changes in these profitability assumptions the tax assets recognized may be adjusted.

6. SIGNIFICANT JUDGMENTS

In the process of applying our accounting policies, we make various judgments, apart from those involving estimations, that can significantly impact the amounts recognized in the financial statements. These include:

a. Capitalization of borrowing costs

IAS 23, Borrowing Costs, requires the capitalization of borrowing costs to qualifying assets. IAS 23 also requires the determination of whether the borrowings are specific to a project or general in calculating the capitalized borrowing costs. Judgment is involved in identifying directly attributable borrowing costs to be included in the carrying value of qualifying assets and in determining if funds borrowed are for general purposes or specifically for the construction of qualifying assets. We consider our centrally managed treasury function with assessment of the circumstances surrounding individual borrowings in making this judgment. Capitalization to land inventory occurs when the land is classified to land under development and ceases when the land is considered developed and ready for sale. Borrowing costs are capitalized to investment properties when under active development. We have determined that all of our borrowings are general, except project specific financing (note 15c), as the decision on how to deploy operating and acquisition funds is a centrally managed corporate decision.

b. Transfer of land to investment property

We typically acquire raw land with the intent of developing it in our Community Development division. When development plans are formulated, we may decide that specific land holdings will be developed into investment properties. Once appropriate evidence of a change in use is established, typically in the form of an operating lease for the investment property, the land is transferred to investment properties. At that time, the land is recognized at fair value in accordance with our accounting policy for investment properties, and any gain or loss is reflected in earnings in the period the transfer occurs.

c. Classification of tenant incentives

Payments are often made to tenants of our commercial properties when new leases are signed. When the payments add future value to the space independent of the lease in place, such costs are capitalized to the investment property. If the costs incurred are specific to the lessee, and do not have stand-alone value, these costs are treated as tenant incentives and amortized on a straight-line basis to revenue over the lease term in accordance with SIC 15, Operating leases – incentives.

d. Investment properties

Our accounting policies related to investment properties are described in note 3f. In applying this policy, judgment is required in determining whether certain costs are additions to the carrying amount of an investment property and, for properties under development, identifying the point at which substantial completion of the property occurs.

In determining the fair value of our investment property, judgment is required in assessing the 'highest and best use' as required under IFRS 13, Fair value measurement. We have determined that the current use of our investment properties is its 'highest and best use'.

e. Compliance with REIT legislation

Under current tax legislation, a real estate investment trust is not liable for Canadian income taxes provided that its taxable income is fully allocated to unitholders during the year. In order for the Trust to continue to be taxed as a mutual fund trust, we need to maintain its REIT status. At inception, the Trust qualifies as a REIT under the specified investment flow-through ("SIFT") rules in the Canadian Income Tax Act. The Trust's current and continuing qualification as a REIT depends on the Trust's ability to meet the various requirements imposed under the SIFT rules, which relate to matters such as its organizational structure and the nature of its assets and revenues. We apply judgment in determining whether it continues to qualify as a REIT under the SIFT rules. Should the Trust cease to qualify, it would be subject to income tax on its earnings.

7. INTEREST IN MELCOR REIT

On November 12, 2015, we sold to the REIT a multi-tenant retail property (held within a 50% joint venture) and a single-tenant industrial property for a purchase price of $15,250. The purchase price was paid with the REIT's line of credit and available cash.

As at December 31, 2016 we hold a 56.7% (2015 - 56.7%) ownership interest in the REIT through ownership of all 14,615,878 Class B LP Units of the Partnership.

The publicly held interest in the REIT is presented as a liability in our consolidated financial statements. Refer to note 25 for summary financial information of the REIT at December 31, 2016.

8. AGREEMENTS RECEIVABLE

Agreements receivable are due in 2017, except for $28,526 due in 2018, $9,294 due in 2019 and $1,482 due in 2020 (2015 - balance due 2016, except $25,295 due in 2017 and $1,472 due in 2018). Subsequent to the interest adjustment date, which provides an interest relief period to qualifying registered builders, these receivables earn interest at prime plus two percent (4.70% at December 31, 2016) and are collateralized by the specific real estate sold.

Management monitors agreements receivables for indications of impairment on an ongoing basis. Balances are reduced to their estimated net realizable values when there is doubt regarding collection of the full amount of principal and interest. At December 31, 2016, a provision for impairment of $810 was recorded (2015 - $1,500). This provision reflects management's best estimate and is subject to measurement uncertainty introduced by the impact of the uncertain economic environment. As a result, material revisions to this estimate may be required in future periods. Refer to note 27 for further discussion surrounding credit risk.

9. LAND INVENTORY

As at December 31	**2016**	**2015**
Raw land held	**333,854**	353,809
Land under development	**142,350**	134,200
Developed land	**204,056**	208,793
	680,260	696,802

A breakdown of our land purchases are as follows:

	2016	2015
Land purchases	**159 acres**	147 acres
Land cost	**14,098**	14,000
Vendor financing	**2,134**	11,500
Settlement of receivable	**2,210**	—
Net cash to close	**9,754**	2,500

Land purchased in the year includes 144 acres of raw land (2015 - 156 acres) and 15 acres of lot inventory (2015 - nil).

During the year, certain land inventories were reclassified to investment properties, and fair value gains of $1,789 (2015 - $1,817) were recognized in the consolidated financial statements. For the purposes of segment reporting, this is disclosed as revenue of $13,929 (2015 - $5,680) and cost of sales of $12,140 (2015 - $3,863) for the Community Development division.

The weighted average interest rate used for capitalization of borrowing costs to land under development is 4.03% for the year ended December 31, 2016 (2015 – 4.09%). Borrowing costs capitalized to land inventory during the year were $3,878 (2015 - $4,503).

Land inventory expensed to cost of sales during the year was $89,980 (2015 - $99,523).

The net realizable value exceeds the carrying cost of all land inventories at December 31, 2016 and 2015, such that no provision for impairment is required.

10. INVESTMENT PROPERTIES

Investment properties consists of the following:

As at December 31	2016	2015
Investment properties	**929,299**	847,387
Properties under development	**41,394**	56,961
Total	**970,693**	904,348

The following table summarizes the change in investment properties during the year:

			2016
	Investment properties	**Properties under development**	**Total**
Balance - beginning of year	**847,387**	**56,961**	**904,348**
Additions			
Direct acquisition	**64,186**	**—**	**64,186**
Transfer from land inventory	**—**	**12,140**	**12,140**
Direct leasing costs	**1,006**	**289**	**1,295**
Property improvements	**3,777**	**—**	**3,777**
Property development	**1,939**	**8,949**	**10,888**
Capitalized borrowing costs	**—**	**103**	**103**
Disposals	**(38,961)**	**—**	**(38,961)**
Transfers	**44,967**	**(44,967)**	**—**
Net fair value adjustment on investment properties	**7,876**	**7,919**	**15,795**
Foreign currency translation (included in OCI)	**(2,878)**	**—**	**(2,878)**
Balance - end of year	**929,299**	**41,394**	**970,693**

			2015
	Investment properties	Properties under development	Total
Balance - beginning of year	863,966	37,138	901,104
Additions			
Direct acquisition	983	3,018	4,001
Acquisition through business combination	14,619	—	14,619
Transfer from land inventory	—	4,211	4,211
Direct leasing costs	587	424	1,011
Property improvements	5,024	—	5,024
Property development	439	25,533	25,972
Capitalized borrowing costs	—	258	258
Disposals	(81,153)	(3,088)	(84,241)
Transfers	20,067	(20,067)	—
Net fair value adjustment on investment properties	40	9,534	9,574
Foreign currency translation (included in OCI)	22,815	—	22,815
Balance - end of year	847,387	56,961	904,348

Acquisitions:

During the year, we completed the acquisition of three suburban office properties in the greater Denver area:

- On February 26 - the Offices at Promenade for $23,073 (US$17,032) (including transaction costs). As part of the purchase Melcor also assumed a mortgage on the property with a carrying value of $15,618 (US$11,529). We recorded the assumed mortgage at its fair value on initial recognition. The fair value of the mortgage was calculated using a market interest rate for an equivalent mortgage;
- On March 3 - the Offices at Inverness for $13,067 (US$9,746) (including transaction costs); and
- On March 31 - Syracuse Hill One for $13,216 (US$10,188) (including transaction costs).

We also acquired a multi-family residential property, Northridge Apartments, in St. Albert, Alberta on October 24, 2016 for $14,830 (including transaction costs). As part of the purchase Melcor also assumed a mortgage on the property with a carrying value of $9,848. The mortgage was re-financed on closing with the lender for additional proceeds of $652. We recorded the assumed mortgage at its fair value on initial recognition.

These acquisitions were funded through available cash and were accounted for as asset acquisitions.

Disposals:

On December 9, 2016, we disposed of a US residential rental property in the Greater Houston Area, resulting in proceeds (net of transaction costs) of $38,418 (US $29,186).

During the year we also disposed of three US single tenant residential units in the Greater Phoenix Area, resulting in proceeds (net of transaction costs) of $543 (US $502).

Acquisitions and disposals in the comparative year:

During 2015 we completed the following acquisitions in our US portfolio:

- On April 13, 2015 we acquired Centennial Airport Plaza in Denver, Colorado for cash consideration of $6,145 (US $4,880).
- On September 1, 2015 we acquired Evans Business Center (47,358 sf), located in the Greater Phoenix area for cash consideration of $8,474 (US $6,430).

These acquisitions were accounted for as business combinations with all the consideration allocated to Investment Properties.

In 2015 we completed the following dispositions from our portfolio:

- On August 27, 2015, we disposed of a US residential rental property in the Greater Houston Area, resulting in proceeds (net of transaction costs) of $42,729 (US $32,378).
- On September 3, 2015, we disposed of a commercial development site in Alberta, resulting in proceeds of $3,088 (net of transaction costs).
- On October 14, 2015, we disposed of a US single tenant residential rental property in the Greater Phoenix Area, resulting in proceeds (net of transaction costs) of $899 (US $697).
- On December 17, 2015 we disposed of a US residential rental property in the Greater Houston Area, resulting in proceeds (net of transaction costs) of $37,525 (US $26,861).

In accordance with our policy, as detailed in note 3f, we record our investment properties at fair value. Fair value adjustments on investment properties are primarily driven by changes in capitalization rates and stabilized NOI, while development activity on properties under development and leasing activity drive fair value adjustments on properties under development. Supplemental information on fair value measurement, including valuation techniques and key inputs, is included in note 28.

Properties transferred from property under development to commercial properties during the year totaled $44,967 (2015 - $20,067).

Presented separately from investment properties is $36,546 (2015 - $37,823) in tenant incentives and $8,226 (2015 -$5,924) in straight-line rent adjustments (included in note 12). The fair value of investment properties has been reduced by these amounts.

The weighted average interest rate used for capitalization of borrowing costs to investment properties under development is 3.91% for the year ended December 31, 2016 (2015 – 4.27%).

Our investment properties are leased to tenants primarily under long term operating leases. Rentals are receivable from tenants monthly. Minimum lease payments under non-cancellable operating leases of investment properties are receivable as follows:

	2016	**2015**
Within one year	**57,127**	49,641
Later than one year but not later than 5 years	**171,053**	153,060
Later than 5 years	**125,713**	128,839
Total	**353,893**	331,540

11. PROPERTY AND EQUIPMENT

	Golf course assets					
	Land	**Buildings**	**Equipment**	**Greens and tees**	**Corporate**	**Total**
January 1, 2016						
Cost	**1,293**	**8,031**	**8,021**	**6,476**	**6,469**	**30,290**
Accumulated depreciation	**—**	**(2,415)**	**(5,564)**	**(2,715)**	**(3,327)**	**(14,021)**
Opening net book value	**1,293**	**5,616**	**2,457**	**3,761**	**3,142**	**16,269**
Additions	**—**	**22**	**579**	**22**	**206**	**829**
Disposals	**—**	**—**	**(20)**	**—**	**—**	**(20)**
Depreciation	**—**	**(221)**	**(605)**	**(233)**	**(512)**	**(1,571)**
Net Book Value - December 31, 2016	**1,293**	**5,417**	**2,411**	**3,550**	**2,836**	**15,507**

	Golf course assets					
	Land	**Buildings**	**Equipment**	**Greens and tees**	**Corporate**	**Total**
January 1, 2015						
Cost	1,293	7,968	7,835	6,444	5,855	29,395
Accumulated depreciation	—	(2,186)	(5,173)	(2,468)	(2,720)	(12,547)
Opening net book value	1,293	5,782	2,662	3,976	3,135	16,848
Additions	—	62	434	31	612	1,139
Disposals	—	—	(13)	—	—	(13)
Depreciation	—	(228)	(626)	(246)	(605)	(1,705)
Net Book Value - December 31, 2015	1,293	5,616	2,457	3,761	3,142	16,269

12. OTHER ASSETS

	2016	**2015**
Tenant incentives	**36,546**	37,823
Deposits and prepaids	**5,266**	5,899
Straight-line rent adjustments	**8,226**	5,924
Inventory	**527**	560
	50,565	50,206

During the year we provided tenant incentives of $5,067 (2015 - $5,786) and recorded $6,344 (2015 - $6,045) of amortization expense. In accordance with SIC 15, Operating leases - incentives, amortization of tenant incentives are recorded on a straight-line basis over the term of the lease against rental revenue.

13. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	2016	**2015**
Trade accounts payable	**16,402**	20,151
Distribution payable	**627**	627
Other payables	**16,770**	18,348
Provision for decommissioning obligation	**1,475**	1,408
	35,274	40,534

As described in note 3r distributions on trust units are recognized in the period in which they are approved and are recorded as an expense. As at December 31, 2016, distribution payable pertains to the December 2016 monthly distribution which was subsequently paid on January 16, 2017 (2015 - December 2015 monthly distribution paid on January 15, 2016).

Decommissioning obligation relates to one of our commercial properties held by the REIT. The total decommissioning obligation is estimated based on the future obligation and timing of these expenditures to be incurred. We estimate the net present value of the obligation based on an undiscounted total future provision of $2,014 (December 31, 2015 - $2,014). At December 31, 2016, a discount rate of 4.00% (December 31, 2015 - 4.00%) and an inflation rate of 2.00% (December 31, 2015 - 2.00%) were used to calculate the net present value of the obligation. Due to uncertainty surrounding the nature and timing of this obligation, amounts are subject to change.

14. PROVISION FOR LAND DEVELOPMENT

	2016	2015
Balance - beginning of year	**93,839**	108,268
New development projects	**98,737**	119,873
Changes to estimates	**(3,123)**	(5,556)
Costs incurred	**(97,869)**	(128,746)
Balance - end of year	**91,584**	93,839

15. GENERAL DEBT

General debt consists of the following:

		2016	2015
Melcor - revolving credit facilities	a	**32,728**	84,813
REIT - revolving credit facility	b	**17,324**	19,258
Project specific financing	c	**5,213**	25,280
Secured vendor take back debt on land inventory	d	**65,408**	76,092
Debt on investment properties and golf course assets	e	**455,189**	393,319
REIT - convertible debenture	f	**32,749**	32,246
		608,611	631,008

a. Melcor - revolving credit facilities

We have available credit facilities with approved loan limits of $205,649 (2015 - $213,949) with a syndicate of major chartered banks. The portion of these loan limits that pertain solely to Melcor is $120,000 (2015 - $120,000) with the remaining balance pertaining to specific joint arrangements.

The amount of the total credit facilities currently used is $32,728 (2015 - $84,813). We have pledged agreements receivable, specific lot inventory, undeveloped land inventory and a general security agreement as collateral for our credit facilities. The carrying value of assets pledged as collateral is $338,678 (2015 - $381,680).

The facilities mature on July 31, 2018, renewable one year in advance of expiry.

Depending on the form under which the credit facilities are accessed, rates of interest will vary between prime plus 0.75% to prime plus 2.25% or banker’s acceptance rate plus a 3.00% stamping fee resulting in interest rates ranging from 3.45% to 4.95% at December 31, 2016 (2015 - 3.85% to 4.95%). The agreements also bear a standby fee of 0.50% for the unused portions of the facilities. The weighted average effective interest rate on borrowings, based on year end balances, is 4.04% (December 31, 2015 - 4.19%).

b. REIT - revolving credit facility

The REIT has an available credit limit based upon the carrying values of specific investment properties up to a maximum of $35,000 for general purposes, including a $5,000 swingline sub-facility. The agreement also provides the REIT with $5,000 in available letters of credit which bear interest at 2.25%. The new facility matures on May 1, 2018, with an extension option of up to three years at the discretion of the lenders. Depending on the form under which the new facility is accessed, rates of interest will vary between prime plus 1.15% or bankers' acceptance plus 2.25% stamping fee. Interest payments are due and payable based upon the form of the facility drawn upon, and principal is due and payable upon maturity. The agreement also bears a standby fee of 0.45% for the unused portion of the facility. The lenders hold demand debentures, a first priority general security and a general assignment of leases and rents over specific investment properties as security for the new facility.

As at December 31, 2016, the carrying value of pledged properties was $55,647 (December 31, 2015 - $56,900). We initially capitalized $341 in transaction costs associated with the facility, of which $114 was unamortized at December 31, 2016 and is presented net of the outstanding balance (December 31, 2015 - $232). The unamortized discount on bankers acceptance of $42 (2015 - $13) and restricted cash of $nil (2015 - $202) is also included in the December 31, 2016 outstanding balance.

As at December 31, 2016 we had $17,480 (December 31, 2015 - $19,301) drawn from the facility; and posted letters of credit of $nil (December 31, 2015 - $nil). The weighted average effective interest rate on borrowings, based on year end balances, is 3.48% (December 31, 2015 - 3.24%).

c. Project specific financing

	2016	2015
Project specific debt on land, with interest rates between 3.20% and 4.08% (2015 - 3.20% to 4.20%)	5,213	13,430
Project specific debt on investment properties under development, with interest rates at nil (2015 - 3.20%)	—	11,850
	5,213	25,280

Land inventory and agreements receivable with a December 31, 2016 carrying value of $18,255 (2015 - $39,500) have been pledged as collateral on project specific debt on land. The debts are due on demand by the lenders. The weighted average interest rate on the above debts, based on year end balances, is 3.63% (2015 - 3.24%). Specific investment properties under development with a December 31, 2016 carrying value of $nil (2015 - $25,205), have been pledged as collateral on project specific debt on investment properties under development.

d. Secured vendor take back debt on land inventory

	2016	2015
Agreements payable with interest at the following contractual rates:		
Fixed rates of 3.00% - 6.00% (2015 - 3.85% to 6.00%)	65,408	76,092
	65,408	76,092

As at December 31, 2016 $13,495 (2015 - $15,640) of debt was payable in US dollars (2016 - US$10,051 and 2015 - US$11,301). The debts mature from 2017 to 2019.

Land inventory with a December 31, 2016 carrying value of $126,973 (2015 - $203,393), has been pledged as collateral for the above debt. The weighted average effective interest rate for the above debts, based on year end balances, is 4.56% (2015 – 4.68%).

The minimum contractual principal payments due within each of the next five years are as follows:

2017	15,627
2018	15,024
2019	16,903
2020	7,700
2021	10,154
	65,408

e. Debt on investment properties and golf course assets

Debt on investment properties and golf course assets	2016	2015
Variable rate mortgages amortized over 10 to 30 years at variable interest rates	60,693	71,514
Mortgages amortized over 15 to 25 years at fixed interest rates	396,784	323,383
	457,477	394,897
Fair value adjustment for interest rate swaps	88	427
Unamortized deferred financing fees	(2,376)	(2,010)
	455,189	393,314
Interest rate ranges	(2.48% -6.16%)	(2.48% -6.16%)

As at December 31, 2016 $56,733 (2015 - $47,102) of debt was payable in US dollars (2016 - US $42,253 and 2015 - US $34,033). The debts mature from 2017 to 2026.

Specific investment properties and golf courses with a carrying value of $870,857 (2015 - $615,206) and assignment of applicable rents and insurance proceeds have been pledged as collateral for the above debt. The weighted average effective interest rate for the above debts, based on year end balances, is 3.54% (2015 – 3.76%).

The minimum contractual principal payments due within each of the next five years and thereafter are as follows:

2017	29,729
2018	79,935
2019	89,908
2020	64,266
2021	63,375
Thereafter	130,264
	457,477

f. REIT - convertible debenture

On December 3, 2014, the REIT issued a 5.50% extendible convertible unsecured subordinated debenture ("REIT debenture") to the public for gross proceeds of $34,500, including $4,500 issued pursuant to the exercise of an over-allotment option. The REIT debenture bears interest at an annual rate of 5.50% payable semi-annually in arrears on June 30 and December 31 in each year commencing June 30, 2015. The maturity date of the REIT debenture is December 31, 2019. The REIT debenture can be converted into trust units at the holders' option at any point prior to the maturity date at a conversion price of $12.65 per unit (the "Conversion Price"). On and from December 31, 2017, and prior to December 31, 2018, the REIT debenture may be redeemed by the REIT, in whole at any time, or in part from time to time, at a price equal to the principal amount thereof plus accrued and unpaid interest, provided that the volume weighted-average trading price of the trust units for a specified period (the "Current Market Price") preceding the date on which notice of redemption is given is not less than 125% of the Conversion Price. On and from December 31, 2018, and prior to the maturity date, the REIT debenture may be redeemed by the REIT, in whole at any time or in part from time to time, at a price equal to the principal amount thereof plus accrued and unpaid interest. Subject to regulatory approval and other conditions, the REIT may, at its option, elect to satisfy its obligation to pay the principal amount of the REIT debenture on redemption or at maturity, in whole or in part, by delivering that number of freely tradeable trust units obtained by dividing the principal amount of the REIT debenture being repaid by 95% of the Current Market Price on the date of redemption or maturity. The issuance was qualified under a short form prospectus dated November 25, 2014.

The fair value of the host instrument component was calculated using a market interest rate for an equivalent non-convertible, non-extendible bond. The conversion feature component is separated and recognized at its fair value and presented as a liability.

A reconciliation of the convertible debenture is as follows:

($000s)	Host Instrument	Conversion Feature	Total
Balance at December 31, 2014	**31,780**	**185**	**31,965**
Amortization of discount and transaction costs	466	—	**466**
Fair value adjustment on conversion feature	—	(180)	**(180)**
Balance at December 31, 2015	**32,246**	**5**	**32,251**
Amortization of discount and transaction costs	503	—	**503**
Fair value adjustment on conversion feature	—	56	**56**
Balance at December 31, 2016	**32,749**	**61**	**32,810**

During the year ended December 31, 2016, we recognized $1,898 of interest expense which is included in finance costs (note 20) (2015 - $1,898).

At December 31, 2016 we remeasured the conversion feature to fair value resulting in a fair value loss of $56 for the year (2015 - fair value gain of $180). Supplemental information on fair value measurement, including valuation techniques and key inputs, is included in note 28.

16. SHARE CAPITAL

a. Common Shares

		2016
(# of shares)	**Number of Shares Issued**	**Amount ($000s)**
Common shares, beginning of the year	**33,233,712**	**70,061**
Share options exercised	**129,417**	**2,102**
Shares purchased for cancellation	**(12,231)**	**(26)**
Common shares, end of the year	**33,350,898**	**72,137**

		2015
(# of shares)	**Number of Shares Issued**	**Amount ($000s)**
Common shares, beginning of the year	33,115,691	67,767
Share options exercised	134,449	2,328
Shares purchased for cancellation	(16,428)	(34)
Common shares, end of the year	33,233,712	70,061

Authorized:

- Unlimited common shares
- Unlimited common shares, non-voting
- Unlimited first preferred shares
- Unlimited first preferred shares, non-voting

We announced a Normal Course Issuer Bid on March 27, 2015 which expired March 30, 2016. Under this bid, we were allowed to purchase up to 1,653,451 common shares (5% of issued and outstanding) with a daily repurchase restriction of 3,057 common shares.

On March 29, 2016 we announced a new Normal Course Issuer bid commencing March 31, 2016 and ending March 30, 2017. Under the bid, we may acquire up to 1,661,810 common shares in total (approximately 5% of our issued and outstanding common shares) with a daily repurchase restriction of 1,433 common shares.

During the year, there were 12,231 common shares purchased for cancellation by Melcor pursuant to the NCIB at a cost of $153 (2015 - 16,428 common shares purchased for cancellation at a cost of $215). Share capital was reduced by $26 and retained earnings decreased by $127 (2015 - share capital reduced by $34 and retained earnings decreased by $181). As at December 31, 2016, 1,649,579 additional common shares may be repurchase by Melcor under the current NCIB (2015 - 1,637,023) .

b. Stock-Based Compensation Plans

On September 28, 2000, Melcor's Board of Directors approved a stock-based compensation plan (the "2000 Plan"). Under the 2000 Plan, Melcor may grant options to full-time, salaried employees and designated contractors after one year of service. The 2000 Plan requires that the option price shall not be less than the weighted average trading price for the 20 consecutive days during which shares traded on the TSX immediately prior to the granting of the stock option. The options vest at 20% per year and expire seven (7) years from the date of issuance. The 2000 Plan was approved by Melcor's shareholders at the Shareholders Annual Meeting in May 2001. Melcor has 90,400 shares reserved for issuance under the 2000 Plan (2015 – 90,400).

On February 23, 2007 Melcor's Board of Directors approved a stock-based compensation plan (the "2007 Plan"). Under the 2007 Plan, Melcor may grant options to full-time, salaried employees and designated contractors after one year of service. The 2007 Plan requires that the option price shall not be less than the weighted average trading price for the 20 consecutive days during which shares traded on the TSX immediately prior to the granting of the stock option. At the discretion of the board, the options vest over a period of three years and expire no longer than seven (7) years from the date of issuance. The 2007 Plan was approved by Melcor's shareholders at the Shareholders Annual Meeting in April 2007. Melcor has 1,654,566 shares reserved for issuance under the 2007 Plan (2015 – 1,783,983).

c. Stock Options Available for Granting

2000 Plan	2016	2015
Stock options available, beginning and end of the year	90,400	90,400

2007 Plan	2016	2015
Stock options available, beginning of the year	877,199	969,466
Stock options granted	(263,400)	(235,500)
Stock options expired / canceled	245,067	143,233
Stock options available, end of the year	858,866	877,199

d. Stock Options Outstanding Under the 2000 & 2007 Plans

2016	Number of Options	Weighted Average Exercise Price
Stock options outstanding, beginning of the year	906,784	16.86
Stock options granted to employees	263,400	13.21
Stock options exercised	(129,417)	12.76
Stock options expired / canceled	(245,067)	16.40
Stock options outstanding, end of the year	795,700	16.46

2015	Number of Options	Weighted Average Exercise Price
Stock options outstanding, beginning of the year	948,966	16.75
Stock options granted to employees	235,500	14.05
Stock options exercised	(134,449)	13.29
Stock options expired / canceled	(143,233)	14.50
Stock options outstanding, end of the year	906,784	16.86

The weighted average share price at the date of exercise was $13.78 (2015 - $16.47).

e. Stock Options Outstanding and Exercisable Under the 2000 & 2007 Plans

			2016
Stock option expiry date	**Outstanding Stock Options (#)**	**Exercise Price Per Share ($)**	**Stock Options Exercisable**
December 12, 2018	157,900	19.26	157,900
December 19, 2019	179,900	21.35	121,600
December 21, 2020	194,500	14.05	66,500
December 13, 2021	263,400	13.21	—
	795,700		346,000

f. Stock Based Compensation Expense

The following assumptions were used in the Black-Scholes option pricing model for options granted. Expected volatility was based on historical volatility.

	2016	**2015**
Expected volatility	**23%**	24%
Risk-free interest rate	**0.95%**	0.59%
Annual dividend rate	**3.30%**	4.20%
Expected life of options in years	**3.86**	3.80

The weighted average grant date fair value of stock options granted during the year was $1.63 (2015 - $1.61) per stock option. Current year vesting of options resulted in a $302 (2015 - $339) charge to stock-based compensation expense and corresponding credit to contributed surplus.

17. PER SHARE AMOUNTS

(# of shares)	**2016**	**2015**
Basic weighted average common shares outstanding during the year	**33,248,925**	33,115,691
Dilutive effect of options	**3,615**	54,488
Diluted weighted average common shares	**33,252,540**	33,170,179

For the year ended December 31, 2016, there were 795,700 stock options excluded from the calculation of diluted earnings per share (2015 - 725,700).

Diluted earnings per share was calculated based on the following:

	2016	**2015**
Profit attributable to shareholders	**34,433**	75,958
Profit for computation of diluted earnings per share	**34,433**	75,958

18. ACCUMULATED OTHER COMPREHENSIVE INCOME

	2016	**2015**
Balance, beginning of the year	**28,705**	10,023
Other comprehensive gain (loss)	**(3,515)**	18,682
Balance, end of the year	**25,190**	28,705

The other comprehensive gain represents the net unrealized foreign currency translation gain on our net investment in our foreign operations.

19. COMMITMENTS AND CONTINGENCIES

In the normal course of operations, we issue letters of credit as collateral for the completion of obligations pursuant to development agreements signed with municipalities. As at December 31, 2016 we had $39,425 (December 31, 2015 - $47,347) in letters of credit outstanding and recorded a net liability of $91,584 (December 31, 2015 - $93,839) in provision for land development costs in respect of these development agreements.

Normally, obligations collateralized by the letters of credit diminish as the developments proceed, through a series of staged reductions over a period of years (average of three to four years) and are ultimately extinguished when the municipality has issued final completion certificates.

We enter into joint arrangements and, in doing so, may take on risk beyond our proportionate interest in the joint arrangement. These situations generally arise where preferred financing terms can be arranged on the condition that the strength of our company's covenant will backstop that of the other joint arrangement participant(s) who also provide similar guarantees. We will have to perform on our guarantee only if a joint arrangement participant was in default of their guarantee. At December 31, 2016 we had guaranteed $12,458 (December 31, 2015 - $24,843) in credit facilities in excess of the amount recognized as a liability. We also guaranteed $12,477 (December 31, 2015 - $14,052) in excess of our share of letters of credit posted with the municipalities.

The loan guarantees include those which are ongoing, as they relate to the relevant lines of credit, and those which have staged reductions as they relate to the financing of specific assets or projects such as infrastructure loans, short-term land loans or mortgages.

To mitigate the possibility of financial loss, we are diligent in our selection of joint arrangement participants. As well, we have remedies available within the joint arrangement agreement, to address the application of the guarantees. In certain instances there are reciprocal guarantees amongst joint arrangement participants.

We also enter into lease agreements with tenants which specify tenant incentive payments upon completion of the related tenant improvements. Incentive payments of approximately $1,111 may be required from lease agreements entered during the year.

20. FINANCE COSTS

	2016	**2015**
Interest on Melcor - revolving credit facilities	**3,222**	5,428
Interest on REIT - revolving credit facility	**749**	369
Interest on REIT convertible debenture	**1,898**	1,884
Interest on general debt	**19,919**	19,184
Financing costs and bank charges	**1,247**	2,269
Loss on debt settlement	**2,760**	2,805
	29,795	31,939
Less: capitalized interest	**(3,981)**	(4,761)
	25,814	27,178

Cumulative interest capitalized on land inventory at the end of the year is $39,792 (2015 - $37,405). Finance costs paid during the year was $28,611 (2015 - $30,312).

21. REVENUE AND EXPENSE BY NATURE

a. Revenue:

The components of revenue are as follows:

	2016	2015
Sale of land	138,074	161,059
Rental income	92,847	86,787
Management fees	3,282	6,813
Golf course revenue	8,258	8,650
Total revenue	242,461	263,309

b. Cost of sales:

The components of cost of sales are as follows:

	2016	2015
Cost of land sold	89,980	99,523
Investment property direct operating expenses	37,375	36,134
Direct golf course expenses	5,121	5,300
Depreciation expense	1,571	1,705
Total cost of sales	134,047	142,662

c. General and administrative expenses:

The components of general and administrative expenses are as follows:

	2016	2015
Employee salary and benefits		
Salaries and wages	10,215	11,461
Employee benefits	802	865
Stock based compensation	302	339
Marketing	2,121	2,580
Other	7,317	8,446
Total	20,757	23,691

Included in employee salary and benefits is the compensation of key management. Key management includes our directors and members of the executive management team. Compensation awarded to key management includes:

	2016	2015
Salaries and wages	2,774	3,268
Employee benefits	42	80
Stock based compensation	142	97
Total	2,958	3,445

d. Fair value adjustment on investment properties

The components of the fair value adjustment are as follows:

	2016	2015
Land transferred to investment properties	1,789	1,817
Property under development	6,130	7,717
Commercial and residential properties	7,876	40
Total	15,795	9,574

22. INCOME TAX

Components of tax expense:

	2016	2015
Current tax expense		
Current year	21,480	21,564
Adjustment to prior years	434	(488)
	21,914	21,076
Deferred tax expense		
Origination and reversal of temporary differences	628	(1,693)
Change in tax rates	—	5,183
	628	3,490
Total tax expense	22,542	24,566

Reconciliation of effective tax rate:

	2016	2015
Income before taxes	56,975	100,524
Statutory rate	27%	26%
	15,383	26,136.24
Non-taxable portion of capital gains and fair value adjustment	2,105	64
Non-taxable portion of REIT income	(1,982)	(2,039)
Impact of higher tax rates in US subsidiary	1,846	1,240
Non-deductible expenses	1,427	550
Non-taxable fair value adjustments on REIT units	3,763	(6,568)
Change in tax rates	—	5,183
Total tax expense	22,542	24,566

Movement in deferred tax balances during the year:

	December 31, 2016			
	Opening	Recognized in profit or loss	Recognized in OCI	**Closing**
Investment property and capital assets	54,408	5,067	(45)	**59,430**
Reserves for tax purposes	15,756	(4,400)	—	**11,356**
Interest deducted for tax purposes	(2,922)	(293)	—	**(3,215)**
Provision for decommissioning obligation	(213)	(10)	—	**(223)**
Convertible debenture	117	(7)	—	**110**
Tax loss carry-forwards	(271)	271	—	**—**
Deferred tax liability	66,875	628	(45)	**67,458**

	December 31, 2015			
	Opening	Recognized in profit or loss	Recognized in OCI	Closing
Investment property and capital assets	55,278	(759)	(111)	54,408
Reserves for tax purposes	16,533	(777)	—	15,756
Interest deducted for tax purposes	(1,798)	(1,124)	—	(2,922)
Provision for decommissioning obligation	(199)	(14)	—	(213)
Convertible debenture	161	(44)	—	117
Tax loss carry-forwards	(5,618)	6,208	(861)	(271)
Deferred tax liability	64,357	3,490	(972)	66,875

No deferred tax liability has been recognized in respect of the net unrealized foreign currency exchange gain in accumulated other comprehensive income. Income tax paid during the year was $22,567 (2015 - $27,503).

23. JOINT ARRANGEMENTS

The table below discloses our proportionate share of the assets, liabilities, revenue, and earnings of 28 arrangements (2015 – 29) that are recorded in these financial statements as follows:

Joint Venture	Interest	Principle activity	Country of incorporation
Anders East Developments	33%	Active land development with investment property	Canada
Anders East Two Communities	50%	Non-active land development	Canada
Blackmud Communities	39%	Active land development	Canada
Black Knight Communities	50%	Active land development	Canada
Capilano Investments	50%	Investment property	Canada
Chestermere Communities	50%	Active land development with investment property	Canada
Highview Communities	60%	Active land development	Canada
HV Nine	7%	Active land development	Canada
Jagare Ridge Communities	50%	Active land development and recreational property	Canada
Jesperdale Communities	50%	Active land development	Canada
Kinwood Communities	50%	Active land development	Canada
Lakeside Communities	50%	Non-active land development	Canada
Larix Communities	50%	Active land development	Canada
Lewis Estates Communities	60%	Active land development and recreational property	Canada
MMY Properties	33%	Investment property	Canada
Rosenthal Communities	50%	Active land development	Canada
South Shepard Communities	50%	Non-active land development	Canada
Stonecreek Shopping Centre	30%	Investment property	Canada
Sunset Properties	60%	Active land development	Canada
Terwillegar Pointe Communities	50%	Non-active land development	Canada
Watergrove Developments	50%	Manufactured home community	Canada
West 33 Developments	50%	Non-active land development	Canada
Westmere Properties	50%	Investment property	Canada
Whitecap Communities	50%	Active land development	Canada
Windermere	50%	Active land development	Canada
Windermere at Glenridding	35%	Active land development	Canada
Winterburn Developments	50%	Active land development	Canada
Villeneuve Communities	60%	Active land development	Canada

The following summarizes financial information about our share of assets, liabilities, revenue and earnings of our interest in joint arrangements that are recorded in our accounts for the year ended December 31, 2016.

	2016	2015
Assets	**401,410**	437,059
Liabilities	**140,399**	169,731
Revenue	**62,224**	103,466
Net Earnings	**18,881**	17,478

Contingent liabilities arising for liabilities of other joint arrangement participants are disclosed in note 19.

24. SEGMENTED INFORMATION

In the following schedules, segment earnings has been calculated for each segment by deducting from revenues of the segment all direct costs and administrative expenses which can be specifically attributed to the segment, as this is the basis for measurement of segment performance. Common costs, which have not been allocated, include finance costs, foreign exchange gains, adjustments to REIT units and income tax expense.

The allocation of these costs on an arbitrary basis to the segments would not assist in the evaluation of the segments' contributions. Inter-segment transactions are entered into under terms and conditions similar to those with unrelated third parties.

Community Development

This division is responsible for purchasing and developing land to be sold as residential, industrial and commercial lots.

Property Development

This division develops high-quality retail, office and industrial revenue-producing properties on serviced commercial sites developed primarily from our community development division. Once substantial completion of construction and leasing are complete, these properties are transferred to our investment property division at fair value (refer to note 10).

Investment Property

This division owns 21 leasable commercial, retail and residential properties (2015 – 16 properties) and other rental income producing assets such as parking lots and land leases.

REIT

This division owns 38 leasable commercial and retail properties (2015 – 38 properties) and other rental income producing assets such as residential property, parking lots and land leases.

Recreation Property

This division owns and manages three 18-hole golf course operations (one of which is 60% owned), and has a 50% ownership interest in one 18-hole golf course.

US Operations

Melcor has a wholly owned subsidiary with operations in the US, which includes a Community Development division and an Investment Property division. The subsidiary's related balances are below.

A reconciliation of our revenues and assets by geographic location is as follows:

External Revenue:

(in Canadian dollars)	2016	2015
United States	**25,362**	20,146
Canada	**217,099**	243,163
Total	**242,461**	263,309

Total Assets:

As at December 31 (in Canadian dollars)	2016	2015
United States	**203,415**	184,908
Canada	**1,688,573**	1,707,061
Total	**1,891,988**	1,891,969

Our divisions reported the following results:

2016	Community Development	Property Development	Investment Properties	REIT	Recreational Properties	Corporate	Subtotal	Intersegment Elimination	Total
Revenue (note 21)	154,201	45,729	35,774	66,042	9,176	—	310,922	(68,461)	**242,461**
Cost of sales (note 21)	(102,508)	(45,650)	(13,994)	(25,770)	(6,180)	(512)	(194,614)	60,567	**(134,047)**
Gross profit	51,693	79	21,780	40,272	2,996	(512)	116,308	(7,894)	**108,414**
General and administrative expense (note 21)	(8,537)	(1,858)	(2,620)	(2,653)	(2,275)	(5,946)	(23,889)	3,132	**(20,757)**
Fair value adjustment on investment properties (note 10, 21 and 28)	—	6,130	11,449	(6,546)	—	—	11,033	4,762	**15,795**
Gain on sale of assets	—	—	—	—	37	—	37	—	**37**
Interest income	1,119	4	6	35	—	14	1,178	—	**1,178**
Segment Earnings	*44,275*	*4,355*	*30,615*	*31,108*	*758*	*(6,444)*	*104,667*	—	***104,667***
Foreign exchange loss									**(412)**
Finance costs (note 20)									**(25,814)**
Adjustments related to REIT units (note 25)									**(21,466)**
Income before income taxes									**56,975**
Income tax expense (note 22)									**(22,542)**
Net income for the year									**34,433**

2015	Community Development	Property Development	Investment Properties	REIT	Recreational Properties	Corporate	Subtotal	Intersegment Elimination	Total
Revenue (note 21)	167,281	30,068	32,103	65,482	9,665	—	304,599	(41,290)	263,309
Cost of sales (note 21)	(100,193)	(29,743)	(12,678)	(25,613)	(6,400)	(608)	(175,235)	32,573	(142,662)
Gross profit	67,088	325	19,425	39,869	3,265	(608)	129,364	(8,717)	120,647
General and administrative expense (note 21)	(9,649)	(1,621)	(3,636)	(2,529)	(2,294)	(7,526)	(27,255)	3,564	(23,691)
Fair value adjustment on investment properties (note 10, 21 and 28)	—	7,717	2,122	(5,418)	—	—	4,421	5,153	9,574
Gain on sale of assets	—	—	—	—	58	—	58	—	58
Interest income	2,356	—	14	56	—	1	2,427	—	2,427
Segment Earnings	*59,795*	*6,421*	*17,925*	*31,978*	*1,029*	*(8,133)*	*109,015*	—	*109,015*
Foreign exchange gains									1,008
Finance costs (note 20)									(27,178)
Adjustments related to REIT units (note 25)									17,679
Income before income taxes									100,524
Income tax expense (note 22)									(24,566)
Net income for the year									75,958

25. NON-CONTROLLING INTEREST IN MELCOR REIT

In accordance with our policy, as detailed in notes 3(r) and 28, we account for the 43.3% publicly held interest in the REIT as a financial liability measured at fair value through profit or loss (“FVTPL”). As at December 31, 2016 the REIT units had a fair value of $94,340 (2015 - $80,401). We recorded adjustments related to REIT units for the year of $21,466 (2015 - $17,679).

In 2015, there were 123,703 trust units purchased for cancellation by the REIT pursuant to the normal course issuer bid ("NCIB") at a cost of $1,000, which is recorded as a reduction in the balance of REIT units on the consolidated statement of financial position. The NCIB ended one year from commencement, on June 29, 2016.

As illustrated in the table below, the adjustment is comprised of:

	2016	**2015**
Fair value adjustment on REIT units	(13,939)	25,261
Distributions to REIT unitholders	(7,527)	(7,582)
Adjustments related to REIT units	(21,466)	17,679

The following tables summarize the financial information relating to Melcor's subsidiary, the REIT, that has material non-controlling interest (NCI), before intra-group eliminations (presented at 100%).

	2016	2015
Assets	663,724	666,458
Liabilities	359,828	362,129
Net assets	303,896	304,329
Cost of NCI	103,959	103,959
Fair value of NCI	94,340	80,401

	2016	2015
Revenue	66,042	65,482
Net income (loss) and comprehensive income (loss)	(11,176)	41,070
Cash flows from operating activities	12,312	10,563
Cash flows used in investing activities	(2,828)	(18,113)
Cash flows (used) from financing activities, before distributions to REIT unitholders	(327)	8,420
Cash flows used in financing activities - cash distributions to REIT unitholders	(7,527)	(7,582)
Net increase (decrease) in cash and cash equivalents	1,630	(6,712)

26. MANAGEMENT OF CAPITAL RESOURCES

We define capital as share capital, contributed surplus, accumulated other comprehensive income, retained earnings and general debt. Our objective when managing capital is to utilize debt to improve our performance, support the growth of our assets, and finance capital requirements arising from the cyclical nature of our business. Specifically, we plan to utilize shorter term debt for financing infrastructure, land inventory, receivables and development activities and to utilize longer term debt and equity for the purchase of property and land assets.

We manage the capital structure through adjusting the amount of long-term debt, credit facilities, the amount of dividends paid, and through normal course issuer bids.

There were no changes to the way we define capital, our objectives, and our policies and processes for managing capital from the prior fiscal period.

We are subject to financial covenants on our $120,000 (2015 - $120,000) Melcor revolving credit facility. The covenants include a maximum debt to total capital ratio of 1.25, a minimum interest coverage ratio of 3.00, and a minimum net book value of shareholders' equity of $300,000. As at December 31, 2016, and throughout the period, we were in compliance with our financial covenants.

In addition, we are subject to financial covenants on our $35,000 REIT revolving credit facility. The covenants include a maximum debt to total capital ratio of 60% (excluding convertible debentures), a minimum debt service coverage ratio of 1.50, and a minimum adjusted unitholders' equity of $140,000. As at December 31, 2016, and throughout the period, the REIT was in compliance with its financial covenants.

We also have financial covenants on certain mortgages for investment properties. At December 31, 2016, and throughout the period, we were in compliance with our financial covenants on our mortgages. We prepare financial forecasts to monitor the changes in our debt and capital levels and our ability to meet our financial covenants.

27. RISK MANAGEMENT

We are exposed to the following risks as a result of holding financial instruments:

a. Credit Risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. Our financial assets that are exposed to credit risk consist of cash and cash equivalents, restricted cash, accounts receivable, and agreements receivable. Our maximum exposure to credit risk is the carrying amount of cash and cash equivalents, restricted cash, accounts receivable and agreements receivable.

We invest our cash in bank accounts and short-term deposits with a major Canadian chartered bank. Accounts receivable balances include amounts due from other joint arrangement participants for their portion of management fees due to us as well as other various smaller balances due from municipal governments, other developers and tenants. There have been no impairment adjustments made to these accounts.

We manage our credit risk in the Investment Property and REIT Divisions through careful selection of tenants and look to obtain national tenants or tenants in businesses with a long standing history, or perform financial background checks including business plan review for smaller tenants. We manage our concentration risk in the Investment Property Division by renting to an expansive tenant base, with no dependency on rents from any one specific tenant. Management has reviewed outstanding receivable balances at December 31, 2016 and has provided for $289 of outstanding receivables related to accounts where collectibility is doubtful (2015 - $191). We expect full payment of remaining balances outstanding, and accordingly, no additional allowance for doubtful accounts has been recorded.

Agreements receivable are collateralized by specific real estate sold. Agreements receivable relate primarily to land sales in Alberta and, accordingly, collection risk is related to the economic conditions of that region. We manage credit risk by selling to certain qualified registered builders. Concentration risk is low as we sell to a large builder base, and no receivables are concentrated to one specific builder.

Management has reviewed all agreements receivable balances as at December 31, 2016 and considered the following in assessing credit risk:

i. The credit quality of agreements receivable that are neither past due nor impaired is determined based on whether balances are due from builders on our approved builder list, and based on geographic location. The approved builder list contains those builders which have a long standing track record, good volumes, positive perception in the industry, and a strong history of repayment. At December 31, 2016, 97% of agreements receivable are due from approved builders (2015 – 96%).

ii. At December 31, 2016, we have identified $3,947 (2015 - $1,942) in agreements receivable which are in arrears and have indications of possible impairment. Agreements receivable which were past due are as follows:

	2016	2015
0 - 6 months past due	3,602	1,722
Greater than 6 months past due	345	220

iii. Total loans included in agreements receivable that would have otherwise been past due or impaired at December 31, 2016, but whose terms have been renegotiated is $28,543 (2015 - $38,046).

In light of economic conditions, we have recorded a provision for impairment of $810 (2015 - $1,500) in relation to agreements receivables. The factors considered in determining that these assets were impaired were primarily the geographic location and related product type. Agreements receivable balances were reviewed on a project by project basis and the loans identified as impaired relate to multiple product types in various regions throughout Alberta.

b. Liquidity Risk

Liquidity risk is the risk that we will not be able to meet our financial obligations as they fall due. We manage liquidity risk to ensure that we have sufficient liquid financial resources to finance operations and meet long-term debt repayments. We monitor rolling forecasts of our liquidity, which includes cash and cash equivalents and the undrawn portion of the operating loan, on the basis of expected cash flows. In addition, we monitor balance sheet liquidity ratios against loan covenant

requirements and maintain ongoing debt financing plans. We believe that we have access to sufficient capital through internally generated cash flows, external sources and undrawn committed borrowing facilities to meet current spending forecasts.

Refer to note 15 for the maturity analysis of general debt and details on the bank indebtedness. Accounts payable and accrued liabilities are expected to be repaid in the next twelve months.

c. Market Risk

We are subject to interest rate cash flow risk as our operating credit facilities and certain of our general debt bear interest at rates that vary in accordance with prime borrowing rates in Canada. For each 1% change in the rate of interest on loans subject to floating rates, the change in annual interest expense is approximately $1,160 (2015 - $2,009) based upon applicable year end debt balances. We are not subject to other significant market risks pertaining to our financial instruments.

28. FAIR VALUE MEASUREMENT

Fair value is the price that market participants would be willing to pay for an asset or liability in an orderly transaction under current market conditions at the measurement date.

The fair value of Melcor's financial instruments were determined as follows:

- the carrying amounts of cash and cash equivalents, restricted cash, accounts receivable, agreements receivable and accounts payable and accrued liabilities approximate their fair values based on the short term maturities of these financial instruments.
- fair values of general debt and derivative financial liabilities - interest rate swaps are estimated by discounting the future cash flows associated with the debt at market interest rates (Level 2).
- fair value of derivative financial liabilities - conversion feature on the REIT's convertible debenture is estimated based upon unobservable inputs, including volatility and credit spread (Level 3).
- fair value of REIT units are estimated based on the closing trading price of the REIT’s trust units (Level 1).

In addition, Melcor carries its investment properties at fair value, as detailed in note 3f, which is determined based on the accepted valuation methods of direct income capitalization or discounted future cash flows (Level 3).

The following table summarizes Melcor's assets and liabilities carried at fair value and its financial assets and liabilities where carrying value does not approximate fair value.

	December 31, 2016					December 31, 2015	
($000s)	**Fair Value hierarchy**	**Fair Value**	**Amortized Cost**	**Total Carrying Value**	**Total Fair Value**	Total Carrying Value	Total Fair Value
Non-financial assets							
Investment properties	**Level 3**	**970,693**	**—**	**970,693**	**970,693**	904,348	904,348
Financial liabilities							
General debt, excluding derivative financial liability	**Level 3**	**—**	**608,550**	**608,550**	**618,506**	631,003	638,297
Derivative financial liability							
Interest rate swaps	**Level 3**	**27**	**—**	**27**	**27**	318	318
Conversion feature on convertible debenture	**Level 3**	**61**	**—**	**61**	**61**	5	5
REIT units	**Level 1**	**94,340**	**—**	**94,340**	**94,340**	80,401	80,401

The table below analyzes assets and liabilities carried at fair value in the consolidated statement of financial position, by the levels in the fair value hierarchy. The fair hierarchy categorizes fair value measurement into three levels based upon the inputs to valuation technique, which are defined as follows:

- Level 1: quote prices (unadjusted) in active markets for identical assets or liabilities that are accessible at the measurement date.
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.
- Level 3: unobservable inputs for the asset or liability.

There were no transfers between the levels of the fair value hierarchy during the year.

Investment properties

Investment properties are remeasured to fair value on a recurring basis, determined based on the accepted valuation methods of direct income capitalization or discounted future cash flows. The application of these valuation methods results in these measurements being classified as Level 3 in the fair value hierarchy.

Under the discounted future cash flows method, fair values are determined by discounting the forecasted future cash flows over ten years plus a terminal value determined by applying a terminal capitalization rate to forecasted year eleven cash flows.

Under the direct income capitalization method, fair values are determined by dividing the stabilized net operating income of the property by a property specific capitalization rate.

The significant unobservable inputs in the Level 3 valuations are as follows:

- Capitalization rate - based on actual location, size and quality of the property and taking into consideration available market data as at the valuation date;
- Stabilized net operating income - revenue less direct operating expenses adjusted for items such as average lease up costs, vacancies, non-recoverable capital expenditures, management fees, straight-line rents and other non-recurring items;
- Discount rate - reflecting current market assessments of the uncertainty in the amount and timing of cash flows;
- Terminal capitalization rate - taking into account assumptions regarding vacancy rates and market rents; and
- Cash flows - based on the physical location, type and quality of the property and supported by the terms of existing leases, other contracts or external evidence such as current market rents for similar properties.

An increase in the cash flows or stabilized net operating income results in an increase in fair value of investment property whereas an increase in the capitalization rate, discount rate or terminal capitalization rate decreases the fair value of the investment property.

In determining the fair value of our investment properties judgment is required in assessing the ‘highest and best use’ as required under IFRS 13, *Fair value measurement*. We have determined that the current uses of our investment properties are their ‘highest and best use’.

Melcor’s executive management team is responsible for determining fair value measurements on a quarterly basis, including verifying all major inputs included in the valuation and reviewing the results. Melcor’s management, along with the Audit Committee, discuss the valuation process and key inputs on a quarterly basis. At least once every three years, the valuations are performed by qualified external valuators who hold recognized and relevant professional qualifications and have recent experience in the location and category of the investment property being valued.

Investment properties were valued by Melcor's internal valuation team as at December 31, 2016 of which 45 investment properties (of 82 legal phases valued) with a fair value of $430,312 were valued by qualified independent external valuation professionals during the year which resulted in fair value gains of $15,795 recorded as fair value adjustment on investment properties in the statements of income and comprehensive income (2015 - investment properties were valued by Melcor Development Ltd.'s internal valuation team of which 37 investment properties (of 76 legal phases valued) with a fair value of $586,298 were valued by qualified independent external valuation professionals during the year which resulted in fair value gains of $9,574).

The following table summarizes the valuation approach, significant unobservable inputs, and the relationship between the inputs and the fair value:

Asset	Valuation approach	Significant unobservable inputs	Relationship between inputs and fair value
Investment properties	Direct capitalization or discounted cash flows	- Capitalization rate - Discount rate - Terminal rate - Stabilized NOI - Cash flows	Inverse relationship between capitalization, discount and terminal rates and fair value (higher rates result in decreased fair value); whereas higher stabilized NOI or cash flows results in increased fair value.
Properties under development	Direct capitalization less cost to complete	- Capitalization rate - Stabilized NOI - Costs to complete	Inverse relationship between capitalization rate and fair value (higher capitalization rate results in lower fair value); whereas higher stabilized NOI results in increased fair value.
Properties under development - undeveloped land	Direct comparison	- Comparison to market transactions for similar assets	Land value reflects market value.

Weighted average stabilized net operating income for investment properties is $1,477 (2015 - $1,488). Other significant valuation metrics and unobservable inputs are set out in the following table. Fair values are most sensitive to changes in capitalization rates.

	Investment Properties			**Properties under Development**		
December 31, 2016	**Min**	**Max**	**Weighted Average**	**Min**	**Max**	**Weighted Average**
Capitalization rate	**5.50%**	**8.75%**	**6.58%**	**6.00%**	**6.00%**	**6.00%**
Terminal capitalization rate	**5.75%**	**9.00%**	**6.81%**	**6.25%**	**6.25%**	**6.25%**
Discount rate	**6.00%**	**9.75%**	**7.65%**	**7.00%**	**7.50%**	**7.07%**

	Investment Properties			Properties under Development		
December 31, 2015	Min	Max	Weighted Average	Min	Max	Weighted Average
Capitalization rate	5.50%	9.00%	6.54%	5.75%	6.75%	6.58%
Terminal capitalization rate	5.75%	9.25%	6.80%	6.00%	7.25%	7.03%
Discount rate	6.50%	10.00%	7.68%	7.00%	7.75%	7.47%

An increase in the capitalization rates by 50 basis points would decrease the carrying amount of investment properties by $57,485 (2015 - $55,483). A decrease in the capitalization rates by 50 basis points would increase the carrying amount of investment properties by $66,944 (2015 - $64,662).

General Debt, excluding derivative financial liabilities

The fair value of revolving credit facilities approximates the carrying value excluding unamortized financing costs. The facilities bear interest, at our option, at a rate per annum equal to either the bank's prime lending rate plus 0.75% to 2.25% or at the bank's then prevailing banker's acceptance rate plus a stamping fee of 2.25% to 3%.

The fair value of project specific financing, secured vendor take back debt on land inventory and debt on investment properties and golf course assets have been calculated by discounting the expected cash flows of each loan using a discount rate specific to each individual loan. The discount rate is determined using the bond yield for similar instruments of similar maturity adjusted for each individual project's specific credit risk. In determining the adjustment for credit risk, we consider current market conditions and other indicators of credit worthiness.

REIT units

REIT units are remeasured to fair value on a recurring basis and categorized as Level 1 in the fair value hierarchy. The units are fair valued based on the trading price of the REIT units at the period end date. At December 31, 2016 the fair value of the REIT units was $94,340 (2015 - $80,401). During the year a fair value loss of $13,939 (2015 - gain of $25,261) was recognized in the statement of income and comprehensive income. In 2015 the fair value of REIT units was also impacted by the $1,000 repurchase of trust units during the year (note 25).

Derivative financial liabilities

Our derivative financial liabilities are comprised of floating for fixed interest rate swaps on mortgages (level 2) and the conversion feature on our convertible debenture (level 3).

The fair value of the interest rate swaps are calculated as the net present value of the future cash flows expected to arise on the variable and fixed portion, determined using applicable yield curves at the measurement date. As at December 31, 2016 the fair value of interest rate swap contracts was $27.

The derivative financial liability was valued by qualified independent external valuation professionals at December 31, 2016. This resulted in a fair value loss of $54 being recognized in income. The significant unobservable inputs used in the fair value measurement of the conversion feature on the REIT convertible debenture as at December 31, 2016 are as follows:

- Volatility - expected volatility as at December 31, 2016 was derived from the historical prices of the REIT's trust units. As the REIT was formed on May 1, 2013, we have used the entire historical data up until December 31, 2016. Volatility was 16.73% (2015 - 15.86%).
- Credit spread - the credit spread of the convertible debenture was imputed from the traded price of the convertible debenture as at December 31, 2016. The credit spread used was 3.71% (2015 - 4.60%).

29. SUBSEQUENT EVENTS

Distributions on REIT trust units:

On January 16, 2017 we declared a distribution of $0.05625 per unit for the months of January, February and March 2017. The distributions will be payable as follows:

Month	Record Date	Distribution Date	Distribution Amount
January 2017	January 31, 2017	February 15, 2017	$0.05625 per unit
February 2017	February 28, 2017	March 15, 2017	$0.05625 per unit
March 2017	March 31, 2017	April 17, 2017	$0.05625 per unit

Dividend declared:

On March 15, 2017, our board of directors declared a quarterly dividend of $0.13 per share payable on April 5, 2017 to shareholders of record on March 27, 2017.

30. COMPARATIVE FIGURES

The 2015 comparative balance of the purchase of land inventory of $2,500 has been reclassified from investing activities to operating activities in the consolidated statement of cash flows to reflect better presentation of the underlying nature of cash flows.