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**Financial Statements**

**Gulf & Pacific Equities Corp.**

**Six Months Ended June 30, 2006**

**Unaudited**

**INDEX**

<b>Balance Sheets</b>	<b>1</b>
<b>Statements of Operations and Deficit</b>	<b>2</b>
<b>Cash Flow Statements</b>	<b>3</b>
<b>Notes to the Financial Statements</b>	<b>4 - 8</b>

**NOTICE TO READER**

The accompanying unaudited interim financial statements have been prepared by the Corporation's management and the Corporation's independent auditors have not performed a review of these financial statements.

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# Gulf & Pacific Equities Corp.

## Balance Sheets

	June 30, 2006 (unaudited)	December 31, 2005
<b>Assets</b>		
Revenue-producing properties	\$ 14,885,278	\$ 12,800,887
Cash	293,298	625,231
Deferred financing and leasing costs	267,097	244,247
Prepaid expenses	59,200	55,538
Accounts receivable	281,637	52,240
Accrued rent receivable	97,297	82,873
Capital assets	1,970	2,262
	<u>\$ 15,885,777</u>	<u>\$ 13,863,278</u>
<b>Liabilities</b>		
Mortgages payable	\$ 8,778,307	\$ 8,904,569
Convertible debentures (note 3)	2,427,870	2,286,978
Bank loans	2,249,128	-
Accounts payable and accrued liabilities	796,582	781,187
	<u>14,251,887</u>	<u>11,972,734</u>
<b>Shareholders' Equity</b>		
<b>Share Capital</b> (note 4)	2,396,560	2,265,871
<b>Paid-in Capital</b>	420,000	420,000
<b>Equity Component of Convertible Debentures</b>	1,117,552	1,122,460
<b>Contributed Surplus</b> (note 5)	139,005	100,040
<b>Warrants</b> (note 6)	202,400	202,400
<b>Deficit</b>	<u>(2,641,627)</u>	<u>(2,220,227)</u>
	<u>1,633,890</u>	<u>1,890,544</u>
	<u>\$ 15,885,777</u>	<u>\$ 13,863,278</u>

Approved on behalf of the Board

(signed) "Anthony J. Cohen" , Director

(signed) "David A. Wright" , Director

# Gulf & Pacific Equities Corp.

Statements of Operations and Deficit

Six Months Ended June 30, 2006 and 2005

Unaudited

	<u>Six Months Ended</u>		<u>Three Months Ended</u>	
	<u>June 30,</u> <u>2006</u>	<u>June 30,</u> <u>2005</u>	<u>June 30,</u> <u>2006</u>	<u>June 30,</u> <u>2005</u>
<b>Revenue</b>				
Rental	\$ 723,541	\$ 706,052	\$ 367,797	\$ 344,520
Common area and realty tax recoveries	224,006	196,617	125,031	90,816
Interest and other	13,381	18,048	3,398	9,527
	<u>960,928</u>	<u>920,717</u>	<u>496,226</u>	<u>444,863</u>
<b>Expenses</b>				
Interest	631,400	569,046	324,030	287,516
Operating costs and realty taxes	300,064	264,275	160,103	133,443
Amortization	121,648	124,068	60,824	62,034
Administration	245,851	238,350	145,246	145,865
Stock-based compensation	83,365	39,040	83,365	39,040
	<u>1,382,328</u>	<u>1,234,779</u>	<u>773,568</u>	<u>667,898</u>
<b>Net Loss for the Period</b>	(421,400)	(314,062)	(277,342)	(223,035)
<b>Deficit - Beginning of Period</b>	<u>(2,220,227)</u>	<u>(1,712,925)</u>	<u>(2,364,285)</u>	<u>(1,803,952)</u>
<b>Deficit - End of Period</b>	<u><u>\$(2,641,627)</u></u>	<u><u>\$(2,026,987)</u></u>	<u><u>\$(2,641,627)</u></u>	<u><u>\$(2,026,987)</u></u>
<b>Loss per Share - Basic and Diluted</b>	<u><u>\$ (0.06)</u></u>	<u><u>\$ (0.04)</u></u>	<u><u>\$ (0.04)</u></u>	<u><u>\$ (0.03)</u></u>
<b>Weighted Average Number of Common Shares Outstanding - Basic and Diluted</b>	<u><u>7,629,363</u></u>	<u><u>7,506,371</u></u>	<u><u>7,695,883</u></u>	<u><u>7,506,371</u></u>

# Gulf & Pacific Equities Corp.

Cash Flow Statements

Six Months Ended June 30, 2006 and 2005

Unaudited

	Six Months Ended		Three Months Ended	
	June 30, 2006	June 30, 2005	June 30, 2006	June 30, 2005
<b>Cash Provided By (Used In):</b>				
<b>Operating Activities</b>				
Net loss	\$ (421,400)	\$ (314,062)	\$ (277,342)	\$ (223,035)
Step rental revenue	(14,424)	(2,046)	8,690	(1,025)
Accretion of discount on convertible debentures	155,476	117,080	77,738	58,540
Amortization of deferred financing and leasing costs	32,823	31,134	16,411	15,567
Amortization of revenue-producing properties	121,356	123,668	60,678	61,834
Amortization of capital assets	292	400	146	200
Stock-based compensation	83,365	39,040	83,365	39,040
	(42,512)	(4,786)	(30,314)	(48,879)
Changes in non-cash balances related to operations:				
Prepaid expenses	(3,662)	(22,027)	4,888	(12,231)
Accounts receivable	(229,397)	(60,924)	(194,138)	(35,383)
Deferred financing and leasing costs	(55,673)	-	(58,715)	-
Accounts payable and accrued liabilities	15,395	107,984	(87,350)	10,789
	(315,849)	20,247	(365,629)	(85,704)
<b>Financing Activities</b>				
Cash held in trust	-	211,747	-	-
Increase in bank loans	2,249,128	-	1,234,026	-
Repayment of mortgages payable	(126,262)	(319,905)	(63,727)	(57,138)
Issuance of share capital	66,797	-	66,797	-
	2,189,663	(108,158)	1,237,096	(57,138)
<b>Investing Activities</b>				
Additions to revenue-producing properties	(2,205,747)	-	(1,060,235)	-
Additions to capital assets	-	(21,348)	-	(21,348)
	(2,205,747)	(21,348)	(1,060,235)	(21,348)
<b>Decrease in Cash</b>	(331,933)	(109,259)	(188,768)	(164,190)
<b>Cash - beginning of period</b>	625,231	1,814,430	482,066	1,869,361
<b>Cash - end of period</b>	\$ 293,298	\$ 1,705,171	\$ 293,298	\$ 1,705,171

# Gulf & Pacific Equities Corp.

Notes to the Financial Statements  
Six Months Ended June 30, 2006  
Unaudited

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## 1. Nature of Operations

The Corporation was incorporated as Gulf & Pacific Equities Corp. under the Business Corporations Act (Alberta) on April 8, 1998 and on June 17, 1998 filed Articles of Amendment to remove certain private corporation restrictions. The Corporation is listed on the TSX Venture Exchange. The Corporation commenced active operations during the 1999 fiscal year. The Corporation owns and operates commercial properties in Alberta and British Columbia.

## 2. Interim Financial Statements

The accompanying unaudited interim financial statements have been prepared by the Corporation in accordance with Canadian generally accepted accounting principles on a basis consistent with those followed in the most recent audited financial statements. These interim financial statements have not been reviewed by the Corporation's auditors.

The notes presented in these unaudited interim financial statements include only significant events and transactions and are not fully inclusive of all matters required by Canadian generally accepted accounting principles for annual audited financial statements. Accordingly, these unaudited interim financial statements should be read in conjunction with the audited financial statements and accompanying notes for the years ended December 31, 2005 and 2004.

Certain comparative figures have been reclassified to conform with the financial statement presentation adopted in the current period.

## 3. Convertible Debentures

	<u>June 30, 2006</u>		<u>December 31, 2005</u>	
	<b>Face Value</b>	<b>Carrying Amount</b>	<b>Face Value</b>	<b>Carrying Amount</b>
8% debentures	\$ 3,240,000	\$ 2,427,870	\$ 3,260,000	\$ 2,286,978

The face value of the convertible debentures consists of the following:

- (i) \$60,000 of the convertible debentures are callable by the Corporation after January 1, 2004, mature January 1, 2007 and can be converted by the holder into common shares of the Corporation at one common share for each \$0.38 principal amount of debentures.
- (ii) \$900,000 of the convertible debentures bear interest at 8%, mature September 1, 2007 and can be converted by the holder into common shares of the Corporation at one common share for each \$0.40 principal amount of debentures.

Initially, the \$900,000 was in the form of a 14% convertible debenture with a five year term and was unsecured. During the second quarter of 2004, the Corporation obtained the consent of the holders of 14% convertible debentures to change the terms of the debentures. Effective April 15, 2004, the debentures bear interest at 8% and the term of the debentures was extended to September 1, 2007.

# Gulf & Pacific Equities Corp.

Notes to the Financial Statements

Six Months Ended June 30, 2006

Unaudited

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### 3. Convertible Debentures (continued)

The face value of the re-issued convertible debentures was allocated as follows:

Debenture	\$ 372,000
Conversion feature	<u>528,000</u>
	<u>\$ 900,000</u>

(iii) \$2,280,000 of convertible debentures bear interest at 8%, mature November 18, 2009 and are unsecured. The debentures can be converted by the holder into common shares of the Corporation at the following rates: one common share for each \$0.315 principal amount of debentures converted during the first two years from the closing date; one common share for each \$0.350 principal amount of debentures converted during the third year from the closing date; \$0.385 principal amount of debentures converted during the fourth year from the closing date; and \$0.425 principal amount of debentures converted during the fifth year from the closing date. The Corporation has the option to redeem the debentures at any time prior to maturity for the aggregate of the face value of the debentures plus earned interest. The Corporation has the right to force early conversion of the debentures in the event that the common shares of Corporation trade for a period of five consecutive days (a "Trading Period") at a price equal to or above the following prices and the cumulative trading volume of the common shares of the Corporation during this Trading Period represents not less than 5% of Corporation's issued and outstanding common shares: \$0.60 per common share at any time during the two year period from the closing date; and \$1.00 per common share at any time during the third, fourth and fifth years from closing date.

These convertible debentures were issued on November 18, 2004 in connection with a private placement. The Corporation issued 2,300 units at \$1,000 per unit. Each unit consisted of an unsecured convertible debenture in the amount of \$1,000 and 1,500 common share purchase warrants.

In 2004, the Corporation used the following assumptions to measure the fair value of the debenture and common share purchase warrants: discount rate of 18%; dividend yield of 0%; and a volatility factor of the expected market price of the Corporation's shares of 40%. The cash proceeds received per unit less the fair value of the debenture and common share purchase warrants was allocated the conversion feature. The unit price was allocated as follows:

	<u>Per Unit</u>	<u>Allocation of Proceeds</u>
Debenture	\$ 679	\$ 1,561,930
Conversion feature	245	564,420
Warrants	<u>76</u>	<u>173,650</u>
	<u>\$ 1,000</u>	<u>\$ 2,300,000</u>

# Gulf & Pacific Equities Corp.

Notes to the Financial Statements

Six Months Ended June 30, 2006

Unaudited

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### 3. Convertible Debentures (continued)

Aggregate proceeds from the private placement were \$2,300,000 before deducting agent's cash commission of \$184,000 and the offering expenses of \$157,904. The Corporation also granted 575,000 common share purchase warrants to the agent.

Private placement costs of \$370,654 include \$341,904 cash settled amounts and \$28,750 fair value of common share purchase warrants granted. The private placement costs were allocated as follows: \$251,711 deferred financing costs and \$118,943 issue costs.

During the six months ended June 30, 2006, \$20,000 of the debentures were converted to 63,492 common shares.

### 4. Share Capital

#### (a) Authorized:

Unlimited preference shares

Unlimited common shares

#### (b) Common Shares Issued and Outstanding:

	<u>Number</u>	<u>Amount</u>
Balance - December 31, 2005	7,506,371	\$ 2,265,871
Issued for: conversion of debentures	63,492	19,492
exercise of options	<u>301,650</u>	<u>111,197</u>
Balance - June 30, 2006	<u>7,871,513</u>	<u>\$ 2,396,560</u>

During the six months ended June 30, 2006, the Corporation:

- i) Issued 63,492 common shares pursuant to the conversion of \$20,000 debentures. The Corporation has allocated the carrying values of the liability component and equity component of the debentures of \$14,584 and \$4,908 respectively to the common share.
- ii) Issued 301,650 common shares to directors and officers pursuant to the exercise of an equivalent number of stock options for cash proceeds of \$66,797. The Corporation has allocated the \$44,400 recorded value of these options to the common shares.

#### (c) Stock-based Compensation

- i) During the six months ended June 30, 2006, the Corporation:
  - a) Granted 50,000 fully vested stock options to a director. Each option entitles the holder to purchase one share of the Corporation's common stock at a price of \$0.305 per share until April 26, 2011. The estimated fair value of \$14,665 has been recorded as stock-based compensation.

# Gulf & Pacific Equities Corp.

Notes to the Financial Statements

Six Months Ended June 30, 2006

Unaudited

## 4. Share Capital (continued)

- b) Granted 300,000 fully vested stock options to directors and officers. Each option entitles the holder to purchase one share of the Corporation's common stock at a price of \$0.305 per share until June 9, 2011. The estimated fair value of \$68,700 has been recorded as stock-based compensation.

The fair value of stock options to directors, officers and employees was estimated at the grant date based on the Black-Scholes pricing model, using the following weighted average assumptions:

Expected dividend yield	Nil
Risk-free interest rate	4.29%
Expected life	5.0 years
Expected volatility	88%

Option pricing models require the input of highly subjective assumptions including the expected price volatility. Changes in the subjective input assumptions can materially affect the fair value estimate, and therefore, the existing models do not necessarily provide a reliable measure of the fair value of the Corporation's stock options.

- ii) Stock options were granted, exercised and expired/cancelled as follows:

	<u>Number</u>	<u>Weighted Average Exercise Price</u>
Balance - December 31, 2005	701,650	\$ 0.237
Granted	350,000	0.305
Exercised	<u>(301,650)</u>	<u>0.221</u>
Balance - June 30, 2006	<u>750,000</u>	<u>\$ 0.275</u>

- iii) At June 30, 2006, 750,000 options which had been granted to certain directors, officers, employees and consultants to purchase common shares of the Corporation subject to various requirements were outstanding as follows:

<u>Outstanding</u>	<u>Exercisable</u>	<u>Year of Grant</u>	<u>Exercise Price per Option</u>	<u>Expiry Date</u>
180,000	180,000	2003	\$ 0.180	August 26, 2008
220,000	220,000	2005	\$ 0.305	June 1, 2010
50,000	50,000	2006	\$0.305	April 26, 2011
<u>300,000</u>	<u>300,000</u>	<u>2006</u>	<u>\$0.305</u>	<u>June 9, 2011</u>
<u>750,000</u>	<u>750,000</u>			



# Gulf & Pacific Equities Corp.

Notes to the Financial Statements  
Six Months Ended June 30, 2006  
Unaudited

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## 5. Contributed Surplus

Contributed surplus consists of the recorded value of options granted to directors, officers, employees and consultants. The changes during the period ended June 30, 2006 is as follows:

Balance - December 31, 2005	\$ 100,040
Options granted	83,365
Options exercised	<u>(44,400)</u>
Balance - June 30, 2006	<u>\$ 139,005</u>

## 6. Warrants

The Corporation issued 4,025,000 warrants in 2004 in connection with a private placement. Each warrant entitles the holder to acquire a common share of the Corporation for \$0.40 until November 18, 2006. The Corporation has the right to accelerate the exercise period of the warrants to 30 days from the end of the Trading Period if the common shares of the Corporation trade at a price of \$0.60 or more per common share for a Trading Period and the cumulative trading volume of the common shares of the Corporation during this Trading Period represents not less than 5% of Corporation's issued and outstanding common shares.

## 7. Related Party Transactions

During the six months ended June 30, 2006, the Corporation:

- a) charged a related party rent totalling approximately \$11,215 (2005 - \$7,643). The companies are related by virtue of the fact that they have the same President and Chief Financial Officer.
- b) charged a related party rent totalling approximately \$6,000 (2005 - \$6,000). The companies are related by virtue of the fact that they have the same President and Chief Executive Officer.
- c) was charged management fees of \$12,000 (2005 - \$12,000) by a shareholder. In addition, an amount of approximately \$80,000 was paid to this shareholder during the six months ended June 30, 2006 relating to a service fee. This amount has been capitalized to the construction-in-progress.
- d) was charged consulting fees of \$18,000 (2005 - \$Nil) by an officer.

These transactions are in the normal course of operations and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.