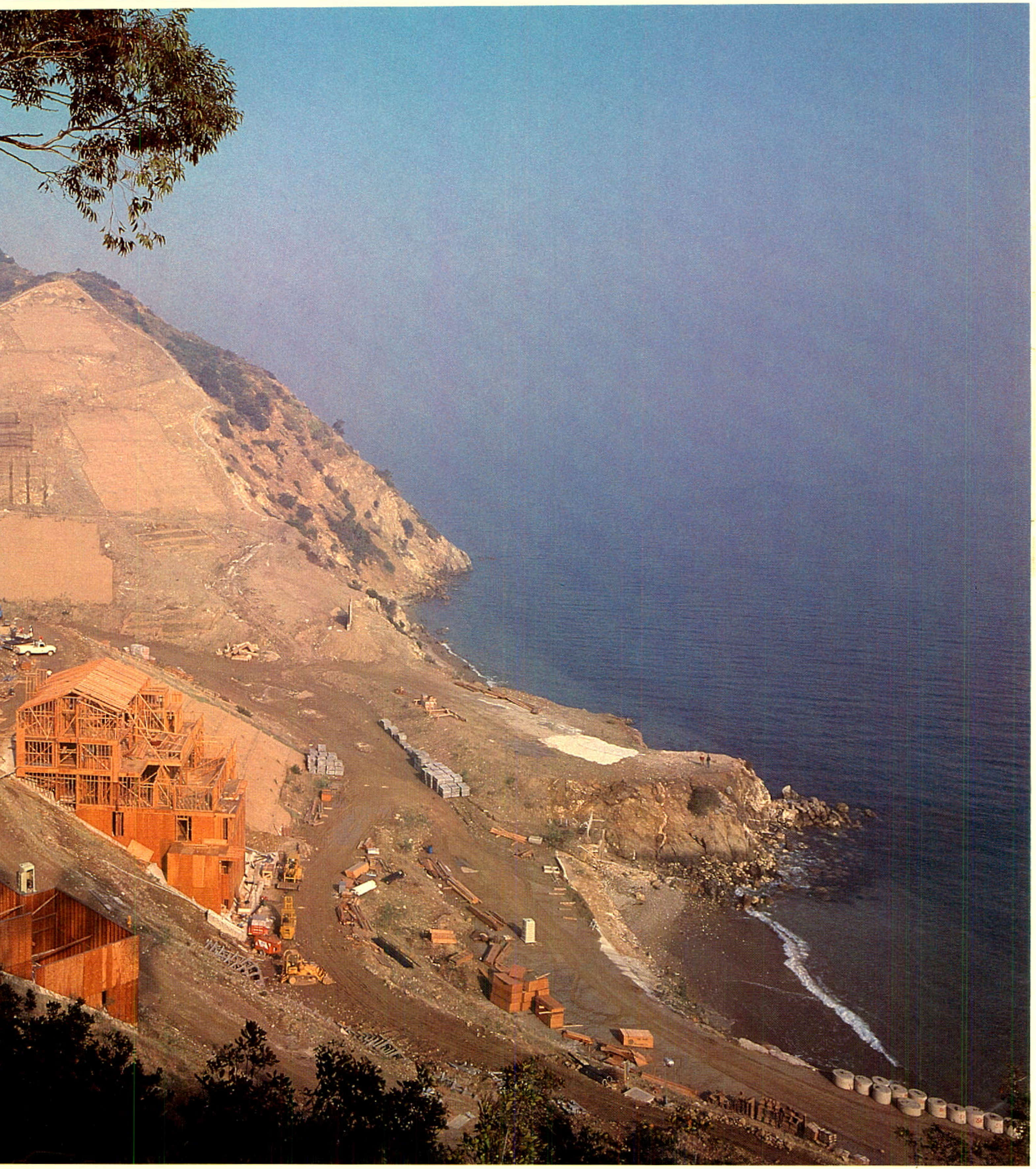
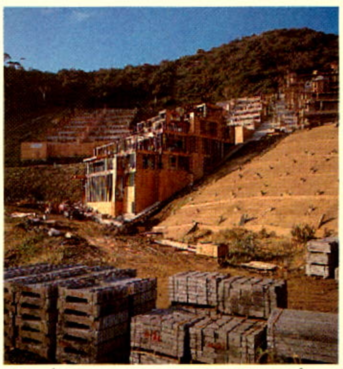
DAON DEVELOPMENT CORPORATION ANNUAL REPORT 1984



La Costa

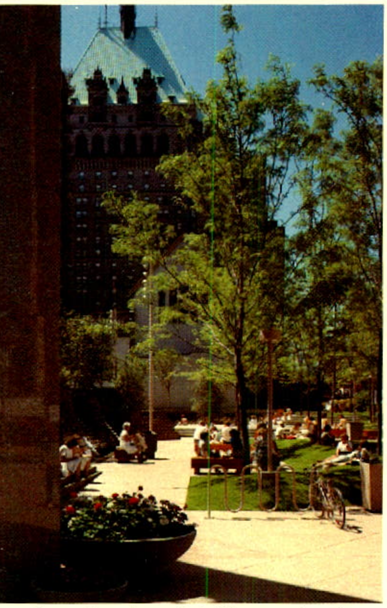
Development is continuing at La Costa, where Daon has 3,372 acres of residential land. A 15-year plan anticipates 12,000 residential units on the property, located 30 miles north of San Diego, California, and 1½ miles from the Pacific Ocean.



Hamilton Cove is Daon's most spectacular residential development project. Located on Catalina Island, 26 miles from the California mainland, the 103-acre site is currently under development. Planned are 330 luxury resort condominium units.

Hamilton Cove

PARK PLACE



Cover photo shows Park Place towering above Christ Church Cathedral, a dramatic blending of modern and historical architecture in downtown Vancouver. The one-acre plaza park and five-storey atrium (above) create an outstanding setting for the city's largest office structure.

DAON CENTRE

Daon Centre serves as the Company's corporate headquarters. Excellently located on the edge of Vancouver's harbour front, it is considered one of the city's most beautiful buildings.

444 Market Street

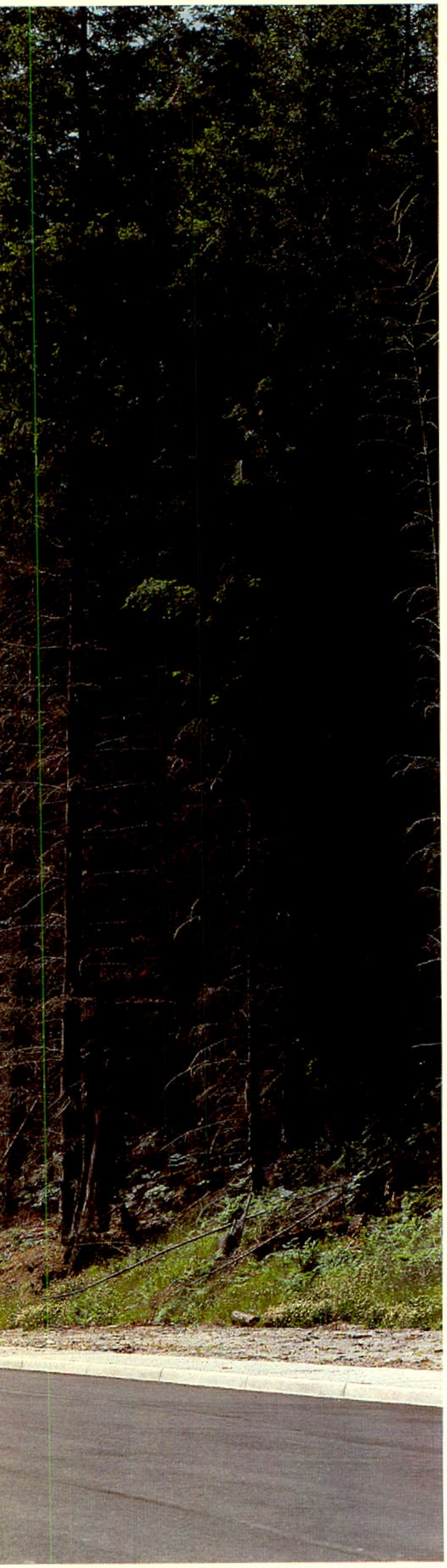
444 Market Street is one of San Francisco's largest and most impressive office buildings. The 30-storey, 605,000 square foot tower has been fully leased almost from the moment of its completion in 1981.

Five Year Financial Highlights

OPERATING RESULTS	**1984**	1983	1982	1981	1980
Total Revenue ($000)	**886,896**	483,134	821,640	696,126	697,961
Net Income (Loss) ($000)	**50,063**	(35,690)	(85,459)	17,224	51,340
Fully Diluted Earnings (Loss) per Common Share ($)	**0.82**	(0.99)	(2.44)	0.37	1.28
Cash Flow (Deficit) ($000)	**35,624**	(71,599)	(120,466)	23,075	91,224
Fully Diluted Cash Flow (Deficit) per Common Share ($)	**0.58**	(1.97)	(3.40)	0.53	2.35
FINANCIAL PERFORMANCE					
Total Assets ($000)	**1,292,806**	1,908,317	2,186,943	2,370,574	1,674,218
Income Properties ($000)	**246,380**	497,014	590,902	805,028	529,362
Shareholders' Equity: Historic Cost ($000)	**159,325**	49,887	84,388	171,881	164,362
COMMON SHARE DATA					
Price ($):					
High	**1.89**	2.95	6.20	13.62	12.50
Low	**1.25**	1.25	0.70	3.85	4.80
Trading Volume:*					
Number of Shares (000)	**10,986**	19,324	9,769	7,033	13,073
Dollar Volume ($000)	**17,254**	39,681	24,616	72,927	99,627
Dividends Paid ($)	**Nil**	Nil	0.12**	0.155	0.12
Number of Shareholders at October 31	**9,732**	4,646	4,702	4,238	4,312

*Toronto Stock Exchange only.
**Of this amount, $0.08 was by a stock dividend aggregating 1,132,293 Common Shares.

Harbour Pointe is a 1,410 acre land tract in Snohomish County, 20 miles north of Seattle. On the edge of Puget Sound, this prime property is being developed in a pleasing mix of commercial and residential.



President's Report

The year 1984 was one of recovery for Daon, marking a dramatic improvement in the Company's financial position. With the completion of the plan to restructure substantially all of the Company's debt and some of its equity, we were able to direct full attention back to the development and sale of real estate.

The results show clearly in Daon's financial report for 1984. Net income was $50.1 million on revenue of $887 million compared to a net loss of $35.7 million on revenue of $483 million for the year ended October 31, 1983.

The balance sheet has strengthened significantly. Consolidated assets now stand at $1.29 billion, a reduction of about $600 million from 1983. Consolidated liabilities have been reduced almost 40% to $1.13 billion, and shareholders' equity has increased by 219% to $159.3 million. Our debt-equity ratio is now 6.6 to 1, compared with 34.8 to 1 a year ago.

It is noteworthy that net income of $50.1 million for the year is after write-downs of $15.5 million plus $35.7 million of general reserves to provide for possible future losses on the Company's real estate holdings. If our real estate markets improve, these reserves may be unnecessary and would therefore be converted into future earnings. On the other hand, real estate markets would have to weaken substantially before earnings would be affected.

What this means is that Daon has now reduced its debt to serviceable proportions and has also reached a strong, workable asset level from which to launch future growth.

Sources of Income and Revenue

The Company's $50.1 million of net income in 1984 was derived from the profitable sale of commercial income properties and from the recovery of income taxes in the amount of $21.2 million. The sale of our interest in three regional shopping centres in Alberta allowed the Company to repay approximately $120 million of Canadian bank debt.

The relative importance of Daon's U.S. operations can be derived from the segmented information in the notes to the financial statements. More than 65% of this year's revenue was generated in the United States and more than 70% of the Company's real estate assets are there. We expect these percentages to remain relatively constant for the foreseeable future.

The year 1984 saw a continuation of the recovery of the California market for residential and commercial property. This is especially important for Daon, not just for the contribution it made to 1984 revenue, but for the future profit potential that it implies.

Valuation of Assets

In my report to you last year, I pointed out that appraisals were carried out in 1983 on all of the Company's principal properties. These appraisals assumed a fully operational company that would develop and sell its land and would complete its income properties. On that basis, appraisals established values at that time of $190 million in excess of book values. Giving consideration to these appraisals in light of our actual experience of the past year, management estimates that the excess of "market" over book value is now in the region of $140 million.

CONVERSION OF DEBT TO COMMON SHARES

Debenture holders were offered two opportunities during the past year to convert their debentures into common shares on the basis of one common share for each $5.00 of principal in the case of series debentures and one common share for each $5.75 of principal in the case of convertible debentures. In total, almost $42 million of debenture debt was converted into equity.

CONSOLIDATION OF OPERATIONS

The most descriptive word for the new Daon is "streamlined." Overhead is down significantly from prior years and the number of employees has stabilized at 144, half in the United States and half in Canada, including head office corporate personnel. New hiring in anticipation of increased U.S. activity will probably take the total over 150 in the coming year. We are now the size of company we wish to be, lean in all divisions but able to respond vigorously to opportunities as they are presented.

BUSINESS STRATEGY

We have many outstanding properties to develop and market, and we have begun to seek out purchase opportunities. The one major change in this respect is that we will not place the company at full risk on a specific project. Debt recourse will be to the project only. We will risk only the cash equity that is required to acquire and develop each property.

Daon has substantial interests in several income producing office structures in Vancouver, most notably Daon Centre, its headquarters building, and Park Place, the city's largest office tower, as well as buildings in Montreal, San Francisco and Riverside, California.

Current emphasis, however, is on the marketing of land in southern California, where the demand has been so strong that the Company has been hard pressed to deliver land to builders. Daon sold more than $120 million (U.S.) of land in the U.S. during fiscal 1984, most of it unserviced land for residential development, and this demand shows no signs of diminishing.

We have some equally outstanding land tracts in Alberta, where the economy is in a slow recovery stage. Except for some sales of serviced commercial land in Calgary, patience can best describe our position in Alberta.

The Company has been engaged for several years in planning and feasibility studies on the 22 acre Metrotown site in Burnaby that would become the central core of the City of Burnaby. We hold an option to purchase the property.

The key ingredient to proceeding with development is commitment from major department stores that would anchor the first phase of retail development. Department stores in Canada are experiencing rather poor operating results and it appears unlikely that such commitments will be obtained in the next few months. This means a delay in the time schedule, a necessary review of the entire feasibility and probably means that we must renegotiate the terms of the land acquisition.

In view of this uncertainty the Company has written off its entire investment to date in this property (approximately $3 million).

We are anxious to develop this exciting project subject to an improvement in the retail business that will allow department stores to enter into firm commitments to lease.

RANCHO CUCAMONGA

OUTLOOK

Lower interest rates during fiscal 1984 and a strong possibility of even lower rates in 1985 prompt greater optimism for the real estate

development industry than at any time during the past three years.

The Company is now in a position to withstand all but the most severe economic downcycle. Assuming stable interest rates and continuing strength in California, 1985 presents a bright picture for Daon. Over the longer term, we will continue to rely on our California operations, looking to better performance in the western provinces, especially Alberta, to provide the impetus for sustained profitability.

On Behalf of the Board,

J. W. Poole,
President and Chief Executive Officer.

December 18, 1984.

Rancho Cucamonga Business Park is a mixed-use business park located in San Bernardino County, approximately 40 miles from Los Angeles. The Company acquired the 292-acre property in 1980 and expects to complete development and sale by 1988.

Consolidated Statement of Operations

FOR THE YEAR ENDED OCTOBER 31, 1984

	Note Reference	1984	1983
		(in thousands of dollars)	
REVENUE			
Real estate sales	18	**$777,370**	$358,833
Rental		**67,501**	88,573
Other	19	**42,025**	35,728
Total revenue		**886,896**	483,134
EXPENSES			
Cost of real estate sales		**729,632**	392,613
Rental operating costs		**35,777**	45,028
Interest	20	**65,081**	72,475
General and administrative		**13,027**	16,245
Depreciation and amortization		**4,388**	5,025
Other	21	**10,078**	28,804
Total expenses		**857,983**	560,190
INCOME (LOSS) BEFORE RECOVERY OF INCOME TAXES		**28,913**	(77,056)
Recovery of income taxes	13	**21,150**	41,366
NET INCOME (LOSS)		**$ 50,063**	$ (35,690)
FULLY DILUTED EARNINGS (LOSS) PER COMMON SHARE	15	**$ 0.82**	$ (0.99)

DAON
DEVELOPMENT
CORPORATION

Consolidated Statement of Retained Earnings

FOR THE YEAR ENDED OCTOBER 31, 1984

	1984	1983
	(in thousands of dollars)	
Retained earnings, beginning of year	**$ 2,271**	$ 37,961
Net income (loss)	**50,063**	(35,690)
	52,334	2,271
Dividends		
Preference Shares	**667**	–
75¢ Class A Shares	**94**	–
Share issue expenses (net of tax)	**5,047**	–
	5,808	–
RETAINED EARNINGS, END OF YEAR	**$ 46,526**	$ 2,271

CONSOLIDATED BALANCE SHEET

OCTOBER 31, 1984

	Note Reference	**1984**	1983
		(in thousands of dollars)	
ASSETS			
Properties:			
Commercial	2	**$ 241,471**	$ 623,494
Land	3	**556,248**	776,724
Residential	4	**139,131**	168,071
Total properties		**936,850**	1,568,289
Cash and term deposits	5	**61,276**	54,758
Amounts receivable	6	**287,394**	265,651
First mortgage receivable	7	**73,510**	–
Term preferred shares	7	**(73,510)**	–
Other assets	8	**7,286**	19,619
		$1,292,806	$1,908,317
LIABILITIES			
Debt on properties:	9		
Commercial		**$ 236,453**	$ 564,265
Land		**364,397**	583,535
Residential		**51,392**	77,498
Total debt on properties		**652,242**	1,225,298
Bank indebtedness	10	**148,236**	223,975
Debentures payable	11	**103,154**	149,988
Other secured liabilities	9	**151,783**	137,972
Accounts payable and accruals	12	**56,524**	82,265
Deferred income taxes	13	**21,542**	38,932
		1,133,481	1,858,430
CONTINGENT LIABILITIES AND COMMITMENTS	17		
SHAREHOLDERS' EQUITY			
Capital stock	14	**98,618**	46,473
Retained earnings		**46,526**	2,271
Deferred gain on foreign exchange		**27,085**	14,027
		172,229	62,771
Shares held by subsidiary	16	**12,904**	12,884
		159,325	49,887
		$1,292,806	$1,908,317

Approved by the Directors:

G. R. Dawson, *Director*

J. W. Poole, *Director*

Consolidated Statement of Cash Flow (Deficit) from Operations

FOR THE YEAR ENDED OCTOBER 31, 1984

	Note Reference	1984	1983
		(in thousands of dollars)	
Net income (loss)		**$ 50,063**	$ (35,690)
Items not involving a current outlay (receipt) of cash:			
Deferred income taxes		**(21,150)**	(41,366)
Depreciation and amortization		**4,388**	5,025
Other		**2,323**	432
CASH FLOW (DEFICIT) FROM OPERATIONS		**$ 35,624**	$ (71,599)
FULLY DILUTED CASH FLOW (DEFICIT) PER COMMON SHARE	15	**$ 0.58**	$ (1.97)

DAON
DEVELOPMENT
CORPORATION

Consolidated Statement of Changes in Financial Position

FOR THE YEAR ENDED OCTOBER 31, 1984

	1984	1983
	(in thousands of dollars)	
OPERATIONAL ACTIVITIES		
Cash flow (deficit) from operations	**$ 35,624**	$ (71,599)
Cash recovered through sales of properties:		
recovery of real estate costs	**729,632**	392,613
less debt discharged on properties sold	**564,900**	242,098
	164,732	150,515
Gross cash flow from operations	**200,356**	78,916
Cash applied to properties:		
commercial	**51,891**	122,742
land	**92,128**	111,893
residential	**34,644**	37,208
	178,663	271,843
less net proceeds from property debt	**88,145**	186,392
	90,518	85,451
NET CASH PROVIDED FROM (APPLIED TO) OPERATIONAL ACTIVITIES	**109,838**	(6,535)
NET CASH PROVIDED FROM OTHER ACTIVITIES	**7,081**	6,258
CORPORATE FINANCING ACTIVITIES		
Net (increase) decrease in amounts receivable	**(81,916)**	97,017
Net decrease in bank debentures of Daon Development Corporation	**(70,179)**	(426)
Net decrease in bank debt of Daon Corporation	**(14,993)**	(4,040)
Net decrease in debentures payable	**(47,752)**	(50,146)
Net increase (decrease) in other secured liabilities	**6,022**	(90,054)
Net decrease in accounts payable and accruals	**(28,517)**	(10,213)
Term preferred shares issued	**72,827**	–
Common Shares issued	**51,384**	–
Translation adjustment	**2,723**	342
NET CASH APPLIED TO CORPORATE FINANCING	**(110,401)**	(57,520)
INCREASE (DECREASE) IN CASH AND TERM DEPOSITS	**$ 6,518**	$ (57,797)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

OCTOBER 31, 1984

1. Summary of Significant Accounting Policies

A. General

The Company is a member of the Canadian Institute of Public Real Estate Companies. The Company's accounting policies and its standards of financial disclosure are in accordance with the recommendations of that Institute.

B. Consolidation

The consolidated financial statements of the Company include:

(i) The accounts of Daon Development Corporation and its subsidiaries.

(ii) The accounts of incorporated and unincorporated joint ventures and partnerships, to the extent of the Company's interest in their respective assets, liabilities, revenues and expenses.

C. Income recognition

The Company recognizes income as follows:

(i) Sales of land and income producing properties
When the Company has fulfilled all material conditions and has received a down payment that is appropriate in the circumstances having regard to the financial resources of the purchaser.

(ii) Sales of residential properties
When the sale has been completed and the purchaser is entitled to occupancy.

(iii) Rental
Rental income from each income producing property is recognized in the consolidated statement of operations when breakeven cash flow after debt service is achieved. Prior to achieving this level of cash flow the Company capitalizes rental losses as a part of the normal development cost of an income property, subject to not capitalizing costs beyond fair market value of the property and subject to a reasonable maximum lease-up period.

D. Properties

(i) Income producing properties are carried at cost less accumulated depreciation. Depreciation on buildings is provided on the sinking fund basis over a 50-year life for office buildings and shopping centres and a 40-year life for residential and industrial buildings. The sinking fund method provides for a depreciation charge of a fixed annual amount increasing at the rate of 5% per annum, which will result in the cost of the properties being fully depreciated over their estimated useful lives.

(ii) Properties under development for retention as income producing properties are carried at cost. Each property under development for sale is carried at the lower of its cost and net realizable value.

(iii) Each property held for future development is carried at the lower of its cost and net realizable value.

(iv) The Company capitalizes all direct costs relating to properties under development and properties held for future development. In addition, certain indirect costs including specific interest, property taxes and interest on the portion of total costs financed by general corporate borrowings are capitalized. Where overhead costs, including salaries, can be clearly identified with the development of a property, the Company allocates these costs to that property.

E. Investments

Each investment is carried at cost. Sales transactions are recorded on settlement dates.

F. Deferred charge for interest

The Company records interest expense on bank indebtedness and debentures payable at contract rates. Under the terms of the Financial Restructuring completed on April 30, 1984, the Company may satisfy its interest liability in Common Shares (see Notes 10 and 11). Accordingly, interest expense is adjusted by a deferred charge to reflect the difference between the agreed upon value of the Common Shares to be issued in satisfaction of the interest liability and the market value of the Common Shares on November 3, 1983, the date the Financial Restructuring was approved. The amount will be adjusted to market at the earlier of the creditors' election to accept Common Shares or October 31, 1986.

Notes to Consolidated Financial Statements (continued)

OCTOBER 31, 1984

1. Summary of Significant Accounting Policies (continued)

G. Depreciation and amortization of other assets

Equipment is depreciated using either the diminishing balance or straight-line method over the estimated useful lives of the assets concerned. Debenture financing costs are amortized over the term of the financing after giving effect to any payments applied.

H. Foreign exchange

Asset and liability accounts in foreign currencies are translated into Canadian dollars at the rates of exchange in effect at the balance sheet dates. Revenue and expenses are translated at weighted average rates prevailing during the year. Gains or losses from exchange translations, other than on the Company's investments in foreign operations and long-term monetary items are included in the consolidated statement of operations. The gains and losses from exchange translations on the Company's investments in foreign operations are deferred and included as part of Shareholders' Equity. Gains or losses from exchange translations on long-term monetary items are deferred and amortized until repayment becomes imminent, at which time they are included in the consolidated statement of operations.

2. Commercial

	1984	1983
	(in thousands of dollars)	
Income producing properties	**$177,147**	$388,843
Accumulated depreciation	**7,582**	6,653
	169,565	382,190
Properties under development	**71,906**	205,204
Properties held for future development	–	36,100
	$241,471	$623,494

The Company's commercial properties consist of office buildings, shopping centres and industrial buildings, which are completed or under construction, and sites held for future development.

3. Land

	1984	1983
	(in thousands of dollars)	
Properties under development	**$ 37,055**	$130,086
Properties held for future development	**519,193**	646,638
	$556,248	$776,724

The Company's land properties consist of completed lots, land subdivisions for sale and large parcels of undeveloped land held for future development.

4. Residential

	1984	1983
	(in thousands of dollars)	
Income producing properties	**$ 80,775**	$117,288
Accumulated depreciation	**3,960**	2,464
	76,815	114,824
Properties under development	**62,316**	53,247
	$139,131	$168,071

The Company's residential properties consist of apartment buildings for rent, and condominiums and single family houses, completed or under construction.

5. Cash and Term Deposits

Included in cash and term deposits are $11,299,000 (1983 – $28,375,000) of restricted amounts, which can only be applied to specific liabilities or which will become available to the Company in future periods.

6. Amounts Receivable

	1984	1983
	(in thousands of dollars)	
Mortgages and agreements for sale	**$272,021**	$245,877
Rents and other tenant charges	**2,163**	4,654
Secured advances due from joint venture partners	**2,716**	9,424
Sundry	**10,494**	5,696
	$287,394	$265,651

The mortgages and agreements for sale yield a weighted averaged interest rate of 12.1% per annum (1983 – 11.8%).

The due dates of the amounts receivable are as follows:

	(in thousands of dollars)
Years ending October 31, 1985	$ 75,679
1986	47,571
1987	63,246
1988	12,807
1989	26,237
Subsequent to 1989	61,854
	$287,394

7. First Mortgage Receivable/Term Preferred Shares

Prior to the sale of certain properties, the project debt secured by these properties was repaid from the proceeds of the issue of term preferred shares by a subsidiary. The first mortgage receivable arising from the sale of such properties has been pledged to secure the redemption of the term preferred shares. Both the first mortgage receivable and the term preferred shares have an outstanding principal of $111,220,000, but have been discounted in these consolidated financial statements. The proceeds from the first mortgage receivable are sufficient to satisfy all dividend and principal payments on the term preferred shares.

8. Other Assets

	1984	1983
	(in thousands of dollars)	
Marketable securities	**$ –**	$ 4,150
Prepaid expenses	**3,962**	6,352
Equipment and sundry assets, at cost less accumulated depreciation of $3,220,000 (1983 – $6,233,000)	**1,234**	4,938
Debenture financing and issue expenses, net of accumulated amortization of $1,997,000 (1983 – $2,286,000)	**2,090**	4,179
	$ 7,286	$ 19,619

9. Project Debt

	1984 (in thousands of dollars)					1983
		Recourse				
	Limited and Non-Recourse	Debt Serviced By Subordinated Project Lender	Debt Serviced By Anticipated Project Cash Flow	Other	**Total**	Total
Commercial	$189,389	$ 15,067	$ 30,440	$ 1,557	**$236,453**	$ 564,265
Land	216,850	25,649	95,343	26,555	**364,397**	583,535
Residential	7,801	–	5,441	38,150	**51,392**	77,498
Total debt on properties	414,040	40,716	131,224	66,262	**652,242**	1,225,298
Amounts receivable	66,404	–	81,789	3,590	**151,783**	135,149
Other assets	–	–	–	–	**–**	2,823
	$480,444	$ 40,716	$213,013	$ 69,852	**$804,025**	$1,363,270

9. Project Debt (continued)

The limited and non-recourse project debt is secured by individual properties or mortgages and agreements for sale and has the following terms:

(a) The debt is serviced only from cash generated by the individual asset securing the debt.

(b) The term of the debt recognizes the time frame required for the property to be developed and/or sold in the normal course of business.

(c) Recourse to the Company is limited in one of the following ways: (i) in return for the project lender agreeing to make the debt non-recourse, the Company has granted the project lender a profit participation in the asset to a maximum of 30%; (ii) any principal or interest outstanding on October 31, 1986 that is not satisfied by the asset securing the project debt, will be satisfied by the issuance of a maximum 4,700,000 Common Shares. These shares will be issued after October 31, 1986 and before February 28, 1987.

(d) Additional future financing will be provided by the project lender to service any prior ranking debt, and where the Company and the project lender deem appropriate, to fund the planning, development and marketing costs required to complete the development and/or sale of the asset.

Other recourse project debt represents secured project debt that did not require modification under the Financial Restructuring.

10. Bank Indebtedness

	1984	1983
	(in thousands of dollars)	
Daon Development Corporation		
Bank Debentures	**$ 1,034**	$ 72,547
Daon Corporation		
Bank Debt (1984 – U.S. $103,136,000; 1983 – U.S. $117,113,000)	**135,489**	144,307
Total principal	**136,523**	216,854
Accrued interest	**57,321**	34,192
Deferred charge	**(45,608)**	(27,071)
	$148,236	$223,975

The terms of this bank indebtedness are as follows:

(a) The bank indebtedness will continue to bear interest at contract rates. However, accrued interest to October 31, 1986 will be satisfied by the issuance of Common Shares on the basis of one Common Share for $8.00 of accrued interest. Interest resulting from the applicable rate exceeding 10½% per annum will be satisfied by Warrants on the same basis as amounts are satisfied by Common Shares. Each Warrant entitles the holder to purchase one Common Share at $8.00 until March 31, 1992.

(b) The principal amount of the bank debentures and bank debt will be repaid as follows:

	Daon Development Corporation	Daon Corporation
	(in thousands of dollars)	
Years ending October 31, 1985	$ –	$ 30,091
1986	–	36,170
1987	207	13,232
1988	207	13,232
1989	207	13,232
Subsequent to 1989	413	29,532
	$ 1,034	$135,489

(c) The bank debentures of Daon Development Corporation are secured by fixed charges against certain properties and by a floating charge against all other properties other than shares and indebtedness of subsidiaries. The bank debt of Daon Corporation is secured by a fixed charge on substantially all of the real and personal property of Daon Corporation.

(d) The terms of the bank indebtedness contain covenants, which restrict expenditures, borrowings and sales of assets of the Company.

11. Debentures Payable

	1984	1983
	(in thousands of dollars)	
Daon Development Corporation		
Series Debentures		
9¾% Debentures, Series C	**$ 4,275**	$ 6,974
11½% Debentures, Series E	**9,438**	14,301
11¼% Debentures, Series F	**11,754**	17,154
11% Debentures, Series G	**10,865**	14,218
11¼% Debentures, Series H	**9,692**	13,842
Floating Rate Debenture, Series I	**8,475**	8,875
Floating Rate Debenture, Series K	**7,480**	7,833
Payments held by The National Victoria and Grey Trust Company on behalf of the Series Debentureholders	**–**	(366)
	61,979	82,831
10¾% Convertible Subordinated Debentures	**26,282**	50,000
Daon Corporation		
Floating Rate Subordinated Debenture, Series A (1984 – U.S. $10,000,000; 1983 – U.S. $11,357,000)	**13,137**	13,994
Total principal	**101,398**	146,825
Accrued interest	**11,595**	22,774
Deferred charge	**(9,839)**	(19,611)
	$103,154	$149,988

The terms of the Debentures are as follows:

(a) The Debentures bear interest at contract rates. However, accrued interest will be satisfied by the issuance of Common Shares on the basis of one Common Share for the following:

(i) $12.00 of accrued interest on the Series Debentures and the Floating Rate Subordinated Debenture to October 31, 1986.

(ii) $14.00 of accrued interest on the Convertible Subordinated Debentures to October 31, 1988.

Interest on the Floating Rate Debentures resulting from the applicable rate exceeding 10½% per annum will be satisfied by Warrants on the same basis as amounts are satisfied by Common Shares. Each Warrant entitles the holder to purchase one Common Share at $8.00 until March 31, 1992.

(b) The principal amount of the Debentures will be repaid as follows:

	(in thousands of dollars)
Years ending October 31, 1985	$ 2,420
1986	2,911
1987	1,060
1988	1,060
1989	10,727
Subsequent to 1989	83,220
	$101,398

(c) The Series Debentures are secured by a fixed charge against certain properties and by the shares and indebtedness of substantially all subsidiaries of Daon Development Corporation and a floating charge against the remaining properties. The Convertible Subordinated Debentures are secured by a fixed charge against certain properties of Daon Development Corporation. The Floating Rate Subordinated Debenture, Series A is secured by a fixed charge, which is subordinated to bank indebtedness, on substantially all the real and personal property of Daon Corporation.

(d) Each 10¾% Convertible Subordinated Debenture is convertible into Common Shares at the option of the holder at any time on or before January 31, 1991, at a conversion price of $15.00 per Common Share adjusted for stock dividends declared.

(e) The terms of the Debentures contain covenants, which restrict expenditures, borrowings and sales of assets of the Company.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

11. Debentures Payable (continued)

(f) The PUT Transactions

On March 29, 1984, Mr. Justice Meredith, of the Supreme Court of British Columbia, decided in legal proceedings brought by The National Victoria and Grey Trust Company, that the security given by the Company for its obligation to purchase the Floating Rate Subordinated Debenture, Series A of Daon Corporation, was in breach of the trust indenture under which the Series Debentures, Series C to K, were issued. The decision did not determine whether the money paid by the Company on account of its obligation to purchase the Debenture of Daon Corporation would be repayable by Bank of Montreal to which it was paid and if so, to whom. The bank has appealed the decision. Until the matter is resolved, the Company will continue to treat the payment of approximately $46,400,000 (U.S. $38,000,000) as a payment on account of its obligation to purchase the Debenture of Daon Corporation.

On November 1, 1984, in a majority decision, the Court of Appeal of British Columbia dismissed the appeal by the bank. The bank has applied for leave to appeal to the Supreme Court of Canada.

The final resolution of the legal proceedings does not materially affect the consolidated balance sheet. If the bank's appeal is unsuccessful, the only effect on the Company is to reduce the principal amount of outstanding Series Debentures by approximately $46,400,000 and to increase the principal amount of the Floating Rate Subordinated Debenture, Series A by U.S. $38,000,000.

12. Accounts Payable and Accruals

	1984	1983
	(in thousands of dollars)	
Accounts payable	**$ 8,113**	$ 23,918
Accrued liabilities	**23,926**	25,175
Deferred income and deposits	**2,279**	3,270
Costs to complete properties sold	**22,206**	29,902
	$ 56,524	$ 82,265

13. Income Taxes

The Company follows the tax allocation method of accounting for income taxes. Deferred income taxes arise primarily from:

(a) The capitalization of certain development and carrying costs for book purposes, which are deducted currently for tax purposes.

(b) Income from partnerships recorded currently for book purposes which are taxable in later periods.

(c) Income recorded currently for book purposes which are reported for tax purposes as the sale proceeds are collected.

(d) The difference between depreciation rates employed for book purposes and those allowed for tax purposes.

Daon Corporation has accumulated operating losses of $125,717,000 which may be applied against future income, the benefit of which has not been recorded in these consolidated financial statements. A reconciliation of income tax rates is contained in the following table:

	1984	1983
Expected Canadian income tax (recovery) rate	**50.0 %**	(50.0)%
Less adjustment to the expected income tax (recovery) rate due to:		
(a) Capital gains	**(97.0)**	–
(b) Additional expenses deducted for tax purposes	**(25.4)**	(16.4)
(c) Tax loss benefits carry-forward not recognized	–	8.8
(d) Other	**(.8)**	3.9
Actual income tax (recovery) rate	**(73.2)%**	(53.7)%

14. Capital Stock

Authorized –

Daon Development Corporation

500,000,000 Common Shares without par value (1983 – 80,000,000)

10,000,000 Preference Shares with a par value of $10 each issuable in series, of which 2,500,000 are designated as 8⅝% Cumulative Redeemable Preference Shares, Senior Series A and 1,500,000 are designated as 9½% Cumulative Redeemable Preference Shares, Senior Series B. These shares are non-voting.

2,000,000 75¢ Class A Shares, non-voting, without par value

	1984	1983
Issued and Outstanding –	(in thousands of dollars)	
Daon Development Corporation		
57,465,051 Common Shares (1983 – 40,846,988)	**$ 80,372**	$ 9,755
1,003,047 8⅝% Cumulative Redeemable Preference Shares, Senior Series A (1983 – 2,202,800)	**10,030**	22,028
682,859 9½% Cumulative Redeemable Preference Shares, Senior Series B (1983 – 1,364,600)	**6,829**	13,646
355,598 75¢ Class A Shares (1983 – 641,076)	**579**	1,044
Daon Corporation		
517,985 Series A Preferred Shares (1983 – nil) may be exchanged for Daon Development Corporation Common Shares, at the rate of one Common Share for each Series A Preferred Share	**808**	–
	$ 98,618	$ 46,473

The following is a summary of the activity in the Company's Common Share Capital account during the year:

	Common Shares	Amount
Balance at beginning of year	40,846,988	$ 9,755,000
Converted from:		
Series Debentures	3,622,762	18,116,000
10¾% Convertible Subordinated Debentures	4,124,796	23,718,000
8⅝% Cumulative Redeemable Preference Shares, Senior Series A	1,847,616	11,998,000
9½% Cumulative Redeemable Preference Shares, Senior Series B	1,049,882	6,817,000
75¢ Class A Shares	245,507	465,000
Issued in satisfaction of interest and dividends	2,352,200	3,619,000
Issued in satisfaction of other transactions	3,375,300	5,884,000
Balance at end of year	57,465,051	$80,372,000

The dividends on the Preference Shares, Series A and B and the 75¢ Class A Shares will be paid in the form of stock dividends of Common Shares on the basis of one Common Share for the following:

(a) $14.50 of dividends (based on the stated rate) on the Preference Shares, Series A and B from September 30, 1984, the date dividends were last paid, to October 31, 1991.

(b) $15.00 of dividends (based on the stated rate) on the 75¢ Class A Shares from September 30, 1984, the date dividends were last paid, to October 31, 1992.

Terms of the bank indebtedness and debentures payable prohibit the declaration or payment of dividends on Common Shares until the later of October 31, 1986 or the date the bank indebtedness and debentures are paid.

In addition to the Common Shares issued and outstanding at October 31, 1984, the Company is obligated to issue 6,828,659 Common Shares in satisfaction of unpaid interest and dividends accrued to October 31, 1984.

The Company has a stock option plan, under which options are outstanding to directors, officers and employees to purchase 346,667 Common Shares at a price of $1.2495 per Common Share and 368,333 Common Shares at a price of $1.47 per Common Share.

Notes to Consolidated Financial Statements (continued)

15. Per Share Calculations

	For the Year Ended October 31, 1984	1983
Earnings (loss) per Common Share		
Basic	**$1.19**	$(0.99)
Adjusted basic	**1.01**	(0.99)
Fully diluted	**0.82**	(0.99)
Cash flow (deficit) per Common Share		
Basic	**$0.84**	$(1.97)
Adjusted basic	**0.72**	(1.97)
Fully diluted	**0.58**	(1.97)

Basic earnings (loss) and cash flow (deficit) per Common Share have been calculated using the weighted average number of Common Shares outstanding during the year (net of shares held by subsidiary) after providing for dividends on the outstanding Preference Shares and 75¢ Class A shares.

Adjusted basic earnings (loss) and cash flow (deficit) per Common Share have been calculated using an average number of Common Shares outstanding during the year that assumes that Common Shares issued on conversion of the Company's various securities and in satisfaction of dividends have been outstanding for the entire year (net of shares held by subsidiary).

The number of Common Shares used in determining the October 31, 1984 fully diluted earnings and cash flow per Common Share is as follows:

	Common Shares
(a) Common Shares issued and outstanding, net of shares held by subsidiary	53,099,768
(b) Series A Preferred Shares of Daon Corporation issued and outstanding	517,985
(c) Common Shares to be issued in satisfaction of unpaid interest and dividends as of October 31, 1984, pursuant to the Financial Restructuring	6,828,659
(d) Employee stock options	715,000
	61,161,412

16. Shares Held by Subsidiary

The subsidiary now holds 4,365,283 (1983 – 4,362,379) Common Shares of the Company at a cost of $12,904,000 (1983 – $12,884,000).

17. Contingent Liabilities and Commitments

(a) As part of the Company's Financial Restructuring completed in 1984, the terms of certain project debt were modified to such an extent that the benefits of owning the assets were in substance transferred to the lender. Accordingly assets totalling $124,804,000 together with the associated debt of a similar amount have been eliminated from the Company's consolidated financial statements. The Company has provided in these consolidated financial statements for its obligation to issue Common Shares for any principal and interest not satisfied by the asset (see Note 9 (c)(ii)).

(b) The Company is contingently liable for obligations of certain joint ventures and partnerships amounting to $89,808,000 (1983 – $140,674,000). However, the assets of each joint venture or partnership are available, and in management's opinion adequate, to satisfy the individual obligations of the joint venture or partnership.

(c) The Company has entered into lease agreements for terms of up to 68 years (1983 – 88 years). The maximum annual rental payments required are $3,265,000 (1983 – $3,927,000). The Company has also guaranteed annual payments to a maximum of $1,777,000 (1983 – $15,663,000) in connection with the sale of certain assets. The Company has entered into leases or subleases which largely offset the maximum annual rental payments required.

(d) The Company has contracted costs to complete income properties under development amounting to $26,453,000 (1983 – $62,729,000). The Company has finance commitments for $24,842,000 (1983 – $61,552,000) of these costs.

17. Contingent Liabilities and Commitments (continued)

(e) The estimated cost to complete residential properties under development and land under development amounts to \$53,372,000 (1983 – \$86,965,000). The major part of these costs is interest on debt secured by these properties. Under the terms of the agreements with project lenders covering the majority of the project debt, this interest will only be paid out of proceeds from the sale of these properties (see Note 9).

(f) The Company has been named as a defendant in numerous lawsuits alleging actual and punitive damages, the total of which are substantial. However, after reviewing the merits of these lawsuits with counsel, it is management's opinion that the ultimate costs of settlement will not materially affect the Company's financial position.

(g) The Company has no unfunded pension liabilities.

18. Real Estate Sales

Real estate sales for the year ended October 31, 1984 includes \$281,748,000 (1983 – \$92,945,000) of sales made to lenders in settlement of obligations to those lenders.

19. Other Revenue

	1984	1983
	(in thousands of dollars)	
Interest and other income	**$ 39,198**	$ 35,191
Management fee income	**565**	537
Investment income	**2,262**	–
	$ 42,025	$ 35,728

20. Interest

	1984	1983
	(in thousands of dollars)	
Interest charges were incurred from:		
Project debt and other secured liabilities	**$130,174**	$163,767
Bank indebtedness	**24,928**	25,913
Debentures payable	**12,853**	17,051
Other interest	**4,281**	3,518
	172,236	210,249
less interest directly capitalized or allocated to properties		
under development and held for future development	**76,613**	91,095
deferred charge	**30,542**	46,679
	$ 65,081	$ 72,475

21. Other Expense

	1984	1983
	(in thousands of dollars)	
Financial Restructuring costs	**$ 4,440**	$ 14,898
Reserves for litigation settlements	**1,433**	2,921
Leasehold improvements written off	**1,500**	6,044
Other expenses	**2,705**	4,941
	$ 10,078	$ 28,804

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

OCTOBER 31, 1984

22. Capitalized Costs

During the year the Company capitalized the following indirect costs:

	1984	1983
	(in thousands of dollars)	
Interest	**$ 76,613**	$ 91,095
Property taxes	**6,960**	7,930
Other indirect costs	**5,062**	5,193
	$ 88,635	$104,218
These costs were capitalized to properties as follows:		
Commercial	**$ 16,999**	$ 26,387
Land	**68,819**	71,708
Residential	**2,817**	6,123
	$ 88,635	$104,218

23. Joint Ventures and Partnerships

The following amounts included within the consolidated financial statements represent the Company's proportionate share of its interest in joint venture and partnership developments:

	1984	1983
	(in thousands of dollars)	
Assets	**$204,086**	$284,209
Liabilities	**200,191**	228,820
Revenue	**166,858**	74,150
Expenses	**129,575**	77,827

24. Segmented Information

	1984	1983
	(in thousands of dollars)	
SEGMENTED REVENUE BY DIVISION:		
Commercial		
Real estate sales	**$499,002**	$ 83,537
Rental revenue	**58,178**	74,144
	557,180	157,681
Land		
Real estate sales	**207,798**	108,344
Residential		
Real estate sales	**70,570**	166,952
Rental revenue	**9,323**	14,429
	79,893	181,381
Total real estate sales and rental revenue	**$844,871**	$447,406
SEGMENTED OPERATING INCOME (LOSS) BY DIVISION:		
Commercial		
Real estate sales	**$ 68,987**	$ (11,284)
Rental revenue	**28,646**	38,068
	97,633	26,784
Land		
Real estate sales	**(18,303)**	(24,422)
Residential		
Real estate sales	**(2,946)**	1,926
Rental revenue	**3,078**	5,477
	132	7,403
Operating income	**79,462**	9,765
Unallocated corporate items (net)	**(29,399)**	(45,455)
Net income (loss)	**$ 50,063**	$ (35,690)

24. Segmented Information (continued)

REVENUE BY GEOGRAPHIC SEGMENTS:	1984	1983
	(in thousands of dollars)	
Canada		
Real estate sales	$ 245,995	$ 37,881
Rental revenue	27,002	39,963
	272,997	77,844
United States		
Real estate sales	531,375	320,952
Rental revenue	40,499	48,610
	571,874	369,562
Total real estate sales and rental revenue	$ 844,871	$ 447,406
OPERATING INCOME (LOSS) BY GEOGRAPHIC SEGMENTS:		
Canada		
Real estate sales	$ 19,256	$ (14,160)
Rental revenue	16,732	24,205
	35,988	10,045
United States		
Real estate sales	28,482	(19,620)
Rental revenue	14,992	19,340
	43,474	(280)
Operating income	79,462	9,765
Unallocated corporate items (net)	(29,399)	(45,455)
Net income (loss)	$ 50,063	$ (35,690)
ASSETS BY GEOGRAPHIC SEGMENTS:		
Real estate properties		
Canada	$ 264,330	$ 561,214
United States	672,520	1,007,075
	936,850	1,568,289
Corporate assets	355,956	340,028
Consolidated assets	$1,292,806	$1,908,317

DAON
DEVELOPMENT
CORPORATION

Auditors' Report

To the Shareholders,
Daon Development Corporation:

We have examined the consolidated balance sheet of DAON DEVELOPMENT CORPORATION (a British Columbia company) and subsidiaries as of October 31, 1984 and 1983, and the related consolidated statements of operations, retained earnings, cash flow (deficit) from operations and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, the accompanying consolidated financial statements present fairly the financial position of Daon Development Corporation and subsidiaries as of October 31, 1984 and 1983, and the results of their operations and changes in their financial position for the years then ended, in accordance with generally accepted accounting principles consistently applied during the periods.

December 11, 1984.
Vancouver, British Columbia.

Arthur Andersen & Co.
Chartered Accountants

Corporate Directory

Directors and Officers

Directors

Graham R. Dawson,
Chairman and
Chief Executive Officer
Dawson Construction
Limited, Vancouver

Edgar F. Kaiser, Jr.,
Chairman and
Chief Executive Officer
Bank of British Columbia,
Vancouver

William B. Laurie,
Vice-Chairman,
Chief Financial Officer
and Secretary
Dawson Construction
Limited, Vancouver

William H. Levine,
Executive Vice-President
Daon Development
Corporation, Vancouver

George B. McKeen,
Chairman
McKeen & Wilson Ltd.,
Vancouver

John W. Poole,
President and
Chief Executive Officer
Daon Development
Corporation, Vancouver

Officers

Graham R, Dawson,
Chairman of the Board

James H. Findlay,
Senior Vice-President and Secretary

William H. Levine,
Executive Vice-President and
Chief Financial Officer

John W. Poole,
President and
Chief Executive Officer

Jonathan H. B. Rees,
Vice-President and Treasurer

George C. Reifel,
Vice-President, Finance

June E. Vassos,
Assistant Secretary

Operating Management

Canada

Daon Development Corporation

James H. Findlay,
Senior Vice-President

Percy A. Ford,
Vice-President, Land
(Northern Alberta)

H. Gordon MacKenzie,
Vice-President

Donald R. Milliken,
Vice-President, Shopping Centres

United States

Daon Corporation

Thomas J. Reilly,
Executive Vice-President

Warren A. Colton, III,
Vice-President, Land

Jack H. Corrigan,
Vice-President,
Commercial/Industrial

R. Chad Dreier,
Vice-President and Controller

Jonathan J. Feucht,
Vice-President,
Residential Marketing

Daniel J. Liddiard,
Vice-President, Construction

William B. Seith,
Vice-President

Corporate Offices

Daon Development Corporation

999 West Hastings Street
Vancouver, B.C. V6C 2W7

Branch offices in Calgary
and Edmonton

Daon Corporation

#100–4350 Von Karman
Newport Beach
California 92660

Branch offices in Seattle
and Carlsbad

Daon (Netherlands) B.V.

530–534 Keizersgracht
Amsterdam
The Netherlands

Auditors

Arthur Andersen & Co.

Transfer Agents and Registrars

Common Shares and
75¢ Class A Shares
The National Victoria and
Grey Trust Company

8⅝% Preference Shares,
Senior Series A and
9½% Preference Shares,
Senior Series B
The Canada Trust Company

Trustees for Debentures

The National Victoria and
Grey Trust Company
Central Trust Company

Stock Exchange Listings

Vancouver Stock Exchange
The Toronto Stock Exchange
Montreal Stock Exchange
Alberta Stock Exchange
The London Stock Exchange

Horizon/Sunridg

The Horizon/Sunridge commercial and industrial properties currently being developed by Daon, are located in the fastest growing sector of Calgary.

DAON

PRINTED IN CANADA BY LAWSON CREATIVE COLOR GROUP