

# FIRST UNION REAL ESTATE EQUITY & MORTGAGE INVESTMENTS

FORM 10-K405  
(Annual Report (Regulation S-K, item 405))

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**SECURITIES AND EXCHANGE COMMISSION**  
**WASHINGTON, D.C. 20549**  
**FORM 10-K**

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)**  
**OF THE SECURITIES EXCHANGE ACT OF 1934**

**FOR THE FISCAL YEAR ENDED 12-31-98 COMMISSION FILE NUMBER 1-6249**

**FIRST UNION REAL ESTATE EQUITY AND**  
**MORTGAGE INVESTMENTS**

(Exact name of registrant as specified in its charter)

OHIO ----- (State or other jurisdiction of incorporation or organization)	34-6513657 ----- (I.R.S. Employer Identification No.)
SUITE 1900, 55 PUBLIC SQUARE CLEVELAND, OHIO ----- (Address of principal executive offices)	44113-1937 ----- (Zip Code)
REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE:	(216) 781-4030 -----

**SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:**

TITLE OF EACH CLASS -----	NAME OF EACH EXCHANGE ON WHICH REGISTERED -----
SHARES OF BENEFICIAL INTEREST (PAR VALUE \$1 PER SHARE) -----	NEW YORK STOCK EXCHANGE -----

**SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT: NONE**

(Title of class)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Yes  No

State the aggregate market value of the voting stock held by non-affiliates of the registrant. The aggregate market value shall be computed by reference to the price at which the stock was sold, or the average bid and asked prices of such stock, as of a specified date within 60 days prior to the date of filing.

As of January 31, 1999, 26,069,303 Shares of Beneficial Interest were held by non-affiliates, and the aggregate market value of such shares was approximately \$130,346,515.

(APPLICABLE ONLY TO CORPORATE REGISTRANTS)

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date.

**31,376,105 SHARES OF BENEFICIAL INTEREST WERE OUTSTANDING AS OF JANUARY 31, 1999**

#### **DOCUMENTS INCORPORATED BY REFERENCE**

List hereunder the following documents if incorporated by reference and the Part of the Form 10-K into which the document is incorporated: (1) Any annual report to security holders; (2) Any proxy or information statement; and (3) Any prospectus filed pursuant to Rule 424(b) or (c) under the Securities Act of 1933. The listed documents should be clearly described for identification purposes.

**1999 Proxy Statement**

**FIRST UNION REAL ESTATE EQUITY AND MORTGAGE INVESTMENTS  
CROSS REFERENCE SHEET PURSUANT TO ITEM G,  
GENERAL INSTRUCTIONS TO FORM 10-K**

ITEM OF FORM 10-K

LOCATION

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## PART I

### ITEM 1. BUSINESS.

The registrant is an unincorporated association in the form of a business trust organized in Ohio under a Declaration of Trust dated August 1, 1961, as amended from time to time through July 25, 1986 (the "Declaration of Trust"), which has as its principal business activity the ownership and management of real estate investments. The registrant qualifies as a real estate investment trust ("REIT") under Sections 856 through 860 of the Internal Revenue Code (the "Code").

To encourage efficient operation and management of its property, and after receiving a ruling from the Internal Revenue Service with respect to the proposed form of organization and operation, the registrant, in 1971, caused a management company to be organized pursuant to the laws of the State of Delaware under the name First Union Management, Inc. (the "Management Company"), to lease property from the registrant and to operate such property for its own account as a separate taxable entity. At December 31, 1998, the registrant net leased 47 of its properties to the Management Company. The shares of the Management Company are held in trust, with the shareholders of the registrant, as exist from time to time, as contingent beneficiaries. The Management Company, in April 1997, acquired voting control of Imperial Parking Limited and its affiliates ("Impark") which is primarily a parking management and transit ticketing manufacturing company based in Canada. Because the Management Company owns voting control of Impark, the financial statements of Impark are consolidated with the Management Company. Additionally, for financial reporting purposes, the financial statements of the Management Company are combined with those of the registrant.

On July 22, 1998, tax legislation was enacted limiting the "grandfathering rules" applicable to stapled REITs, such as the registrant (the "Stapled REIT Legislation"). As a result, the income and activities of the Management Company with respect to any real property interests acquired by the registrant and the Management Company after March 26, 1998, for which there was no binding written agreement, public announcement or filing with the Securities and Exchange Commission on or before March 26, 1998, will be attributed to the registrant for purposes of determining whether the registrant qualifies as a REIT under the Code. The registrant terminated its management arrangements with the Management Company in March 1999, and self-manages its retail, apartment and office portfolios. The registrant entered into third-party management arrangements for the parking facilities it owns. Accordingly, the registrant no longer receives any rents from the Management Company.

The registrant owns regional enclosed shopping malls, apartment complexes, large downtown office buildings and parking facilities. The registrant's portfolio is diversified by type of property, geographical location, tenant mix and rental market. As of December 31, 1998, the registrant owned (in fee or pursuant to long-term ground leases under which the registrant is lessee) 21 shopping malls, 8 apartment complexes, 5 office properties, 7 parking garages and 2 surface parking lots in the United States and 1 parking garage and 10 surface parking lots in Canada. The registrant also owns 50% of another mall in a joint venture with an unrelated party.

All of the registrant's shopping malls compete for tenants on the basis of the rent charged and location, and encounter competition from other retail properties in their respective market areas. Some of the registrant's shopping malls compete with other shopping malls in the environs. However, the principal competition for the registrant's shopping malls may come from future shopping malls locating in their market areas. Additionally, the overall economic health of retail tenants impacts the registrant's shopping malls. Due to the overbuilding of retail space and a demand for large, open area, administrative service space in Denver, CO, in 1995, the registrant has repositioned a former retail mall into an office property and released approximately 64% of the former mall. Additionally, due to excess mall space in Abilene, TX in 1997, the registrant demolished its enclosed mall and constructed the first phase of a strip shopping center which opened in 1998. In February 1999, the registrant sold its shopping center in Buffalo Grove, IL and signed contracts to sell 8 shopping malls and 1 shopping center.

The registrant's apartment complexes compete with other apartments and residential housing in the immediate areas in which they are located and may compete with apartments and residential housing constructed in the same areas in the future.

The registrant's office properties compete for tenants principally with office buildings throughout the respective areas in which they are located. In most areas where the registrant's office buildings are located, competition for tenants has been and continues to be intense on the basis of rent, location and age of the building. The registrant sold its office building in Shreveport, LA in March 1999. The registrant currently has its Indianapolis, IN and Marysville, CA office properties under contract with closings scheduled to occur in April 1999. The registrant plans to hold and redevelop its Cleveland, OH office building.

The registrant's parking facilities compete with other parking facilities in the immediate areas in which they are located and may compete with new parking facilities constructed in the same areas in the future.

The registrant's mortgage investments are collateralized by an apartment complex and the management contract of another apartment complex. The risks inherent with the registrant's mortgage portfolio relate to the performance and the value of the apartment complexes that secure the mortgage investments. These risks may impair the realizability of the mortgage investments.

The registrant's segment data may be found in footnote 23 to the Combined Financial Statements on page 19 to Exhibit 13.

The registrant has approximately \$206 million in debt due in 1999. The registrant intends to fund the repayment by using cash available at December 31, 1998, a rights offering to shareholders, mortgage financing and the net proceeds from property sales. The registrant's credit rating, leverage, share price and liquidity limit the flexibility of the registrant to avail itself of other types of capital markets transactions at this

time.

Impark operations consist primarily of parking management in Canada. Impark also has a market presence in Buffalo, NY, Minneapolis, MN, and Milwaukee, WI. Currently, Impark derives 87%, 12% and 1% of revenue from its management of facilities in Canada, the United States and Asia, respectively. Impark's Canadian operations are not hedged against currency fluctuations. Impark faces competition from local and national parking operators in procuring management contracts from third party parking lot and garage owners. Transit ticketing products, manufactured by a wholly-owned subsidiary of Impark, are targeted to be sold to predominantly U.S. mass transit operators, and the sales of these products represent approximately 3% of Impark's gross revenues.

## **RISK FACTORS**

An investment in the registrant's securities involves various risks. The following factors should be carefully considered in addition to the other information set forth in this report.

### **NEW SENIOR MANAGEMENT LACKS PRIOR EXPERIENCE WITH THE REGISTRANT AND IN OPERATING PUBLIC COMPANIES OR REITS**

In June 1998, William A. Ackman was elected as Chairman of the Board. In October 1998, William A. Scully was appointed Vice Chairman of the Board. In November 1998, the registrant appointed Daniel P. Friedman as its President and Chief Executive Officer, and David Schonberger and Anne N. Zahner, each as Executive Vice Presidents. Until their appointments, these individuals had little, if any, previous working experience or relationships with the registrant or with the Management Company or with either of their senior management or other personnel. The failure of the new management team to work effectively with the registrant's or the Management Company's other senior management could result in the departure of key personnel or disruptions in the operations of the registrant, which in turn could have a material adverse effect on the registrant's or the Management Company's business, financial condition or results of operations.

In addition, none of the members of the new management team has ever operated or served as an executive officer, director or trustee of a public company or a REIT. The lack of experience with or knowledge of issues that confront public companies or REITs could have an adverse effect on the ability of such individuals to effectively manage the operations of the registrant and thereby could have an adverse effect on the registrant's business, financial condition or results of operations.

### **PROPOSED DEPARTURE OF SOME MEMBERS OF SENIOR MANAGEMENT**

Some members of the senior management team that was in place prior to Mr. Friedman's appointment have expressed a desire to leave the registrant and are in discussions with the registrant regarding the timing and terms of their departure. The departure of these individuals could result in the departure of additional key personnel or disruptions in the operations of the registrant, which in turn could have a material adverse effect on the registrant's business, financial condition or results of operations.

### **DIFFICULTIES IN SERVICING DEBT**

The registrant recently negotiated amendments to its principal credit facilities, including its senior credit facility (the "FUR Credit Facility"), the Cdn.\$38.8 million credit facility of Impark, an affiliate of the registrant and subsidiary of the Management Company (the "Impark Credit Facility" and, together with the FUR Credit Facility, the "Credit Facilities"), and a loan to the registrant from a syndicate of lenders led by BT Alex.Brown (the "Bridge Loan") in an original principal amount of \$90 million. Among other things, the amendments, in principle, require the registrant to make significant principal prepayments in April, May and June 1999. As of March 26, 1999, the registrant had \$167.6 million in principal outstanding under the FUR Credit Facility and the Bridge Loan and Cdn.\$35.4 million in principal outstanding under the Impark Credit Facility. The upcoming amortization payments require the registrant to reduce the principal amounts outstanding under the FUR Credit Facility and the Bridge Loan to \$158.9 million in the aggregate in April 1999, \$130.0 million in the aggregate in May 1999 and \$100.0 million in the aggregate in June 1999. All remaining principal under the FUR Credit Facility and the Bridge Loan is due on August 11, 1999. The registrant is relying on its cash reserves, cash flow from operations, net proceeds from assets sales, financing assets and net proceeds from offerings

to make these principal payments, but there can be no assurance that these sources will provide sufficient funds to enable the registrant to make these payments.

## **DEFAULT UNDER THE FUR CREDIT FACILITY, THE IMPARK CREDIT FACILITY AND THE BRIDGE LOAN**

The registrant and Impark recently negotiated amendments to, and waivers of any defaults under, the Credit Facilities and the Bridge Loan. The defaults resulted primarily from the failure to comply with various financial covenants. Although the defaults have been waived and the debt instruments have been amended, there can be no assurance that either the registrant or Impark will satisfy their respective financial covenants or their respective obligations, including principal and interest repayment obligations, under the FUR Credit Facility, the Bridge Loan or the Impark Credit Facility. If the registrant or Impark is unable to satisfy its obligations under either of these facilities or the Bridge Loan, the lenders may declare all indebtedness outstanding thereunder, together with any accrued interest thereon, due and payable immediately and by such action trigger cross-defaults under other debt instruments. There can be no assurance that the registrant or Impark will be able to refinance any of such indebtedness.

## **DEBT COVENANTS RESTRICT OPERATING FLEXIBILITY; FAILURE TO COMPLY WITH DEBT INSTRUMENTS COULD CAUSE ACCELERATION OF DEBT**

Debt instruments, including the Credit Facilities and the Bridge Loan, to which either of the registrant or the Management Company is currently a party, and to which either may become a party in the future, contain and may contain a number of significant covenants that, among other things, restrict in varying degrees either of the registrant or the Management Company from selling assets, incurring additional indebtedness, repaying other indebtedness, paying dividends, creating liens on assets, entering into leases, making investments, loans or advances, making acquisitions, engaging in mergers or consolidations, engaging in certain transactions with affiliates and certain other corporate activities. Each of the registrant's and the Management Company's ability to remain in compliance with certain such covenants will depend upon, among other things, its results of operations and may be affected by events beyond its control, including economic, financial and industry conditions. Accordingly, there can be no assurance that either of the registrant or the Management Company will remain in compliance with such agreements and covenants.

In the event of a default under such instruments or agreements relating to any indebtedness of either of the registrant or the Management Company, the holders of such indebtedness generally will be able to declare all such indebtedness, together with accrued interest thereon, to be due and payable immediately and, in the case of collateralized indebtedness, to proceed against their collateral. In addition, default under one debt instrument could in turn permit lenders under other debt instruments to declare borrowings outstanding thereunder to be due and payable pursuant to cross-default clauses. Accordingly, the occurrence of a default under any debt instrument could have a material adverse effect on the registrant or the Management Company and may cause the registrant or the Management Company to seek protection or relief under applicable bankruptcy laws.

## **CONTEMPLATED ASSET SALES WILL SHRINK PORTFOLIO AND RETURNS TO SHAREHOLDERS; REPLACEMENT ASSETS RESULTING FROM OTHER ASSET SALES MAY NOT PROVIDE GREATER SHAREHOLDER VALUE**

The registrant is in the process of selling various of its residential, retail, office and parking properties. Because the registrant intends to apply the net proceeds of these asset sales to repay outstanding indebtedness, its portfolio of properties will be smaller, less diverse and less valuable and will generate less revenue for ultimate distribution to its shareholders. In addition, the registrant may elect in the future to sell other assets. To the extent that the net proceeds of any of those asset sales are not used to acquire replacement assets or assets of at least equivalent value, the registrant's portfolio of properties will be similarly affected. There can be no assurance that the registrant will be able to sell the properties described above on advantageous terms, expeditiously or at all. Moreover, if any of these assets are sold and their net proceeds are applied towards the purchase of replacement assets, there can be no assurance that the registrant will be able to acquire replacement assets that will be as valuable as the assets they replace or provide greater returns to the registrant and its shareholders.

## **INCOME AND ACTIVITIES OF MANAGEMENT COMPANY MAY BE ATTRIBUTED TO THE REGISTRANT UNDER RECENT ANTI-STAPLING LEGISLATION AND MAY THREATEN REIT STATUS**

Under the Stapled REIT Legislation, the anti-stapling rules provided in the Code apply to real property interests acquired or substantially improved after March 26, 1998 by the registrant or the Management Company, or a subsidiary or partnership in which a 10% or greater interest is owned by either the registrant or the Management Company unless:

- the real property interests are acquired pursuant to a written agreement that was binding on March 26, 1998 and at all times thereafter or
- the acquisition of such real property interests was described in a public announcement or in a filing with the Securities and Exchange Commission on or before March 26, 1998.

Consequently, the income and activities of the Management Company with respect to any property acquired by the registrant or the Management Company after March 26, 1998, for which there was no binding written agreement, public announcement or filing with the Securities and Exchange Commission on or before March 26, 1998, will be attributed to the registrant for purposes of determining whether the registrant qualifies as a REIT under the Code. These attribution rules may make it more difficult for the registrant to qualify as a REIT and may subject the registrant to various additional taxes.

## **IMPROVED PROPERTIES MAY BECOME SUBJECT TO ANTI-STAPLING LEGISLATION UNDER CERTAIN CIRCUMSTANCES AND MAY THREATEN REIT STATUS**

The Stapled REIT Legislation also provides that a property held by a stapled REIT but not subject to the anti-stapling rules would become subject to such rules in the event of either

- an improvement placed in service after December 31, 1999 that changes the use of the property and the cost of which is greater than 200% of

(1) the undepreciated cost of the property (prior to the improvement) or

(2) in the case of property acquired where there is a substituted basis, the fair market value of the property on the date it was acquired by the stapled REIT or

- an addition or improvement that expands beyond the boundaries of the land included in such property.

The Stapled REIT Legislation contains an exception for improvements placed in service before January 1, 2004 pursuant to a binding contract in effect on December 31, 1999 and at all times thereafter.

If previously exempt property of the registrant or the Management Company becomes subject to the anti-stapling rules upon the occurrence of any of the events described above, any income generated by, and activities conducted by the registrant and the Management Company through, such properties would be attributed to the registrant for purposes of determining whether the registrant qualifies as a REIT under the Code. These attribution rules may make it more difficult for the registrant to qualify as a REIT and may subject the registrant to various additional taxes.

## **OTHER LEGISLATION COULD ADVERSELY AFFECT THE REGISTRANT'S REIT QUALIFICATION**

Other legislation (including legislation previously introduced, but not yet passed), as well as regulations, administrative interpretations or court decisions, also could change the tax law with respect to the registrant's qualification as a REIT and the federal income tax consequence of such qualification. The adoption of any such legislation, regulations or administrative interpretations or court decisions could have a material adverse effect on the results of operations, financial condition and prospects of the registrant and could restrict the registrant's ability to grow.

## **DEPENDENCE ON QUALIFICATION AS A REIT; TAX AND OTHER CONSEQUENCES IF REIT QUALIFICATION LOST**

There can be no assurance that the registrant has operated in a manner to qualify as a REIT for federal income tax purposes in the past or that it will so qualify in the future. Qualification as a REIT involves the application of highly technical and complex provisions of the Code, for which there are only limited judicial or administrative interpretations. The complexity of these provisions is greater in the case of a stapled REIT such as the registrant. Qualification as a REIT also involves the determination of various factual matters and circumstances not entirely within the registrant's control. In addition, the registrant's ability to qualify as a REIT is dependent upon its continued exemption from the anti-stapling rules of Section 269B(a)(3) of the Code, which, if they were to apply, would prevent the registrant from qualifying as a REIT. The "grandfathering" rules governing Section 269B generally provide, however, that Section 269B(a)(3) does not apply to a stapled REIT (except with respect to new real property interests as described above "--Income and Activities of Management Company May Be Attributable to the Registrant Under Recent Anti-Stapling Legislation and May Threaten REIT Status.") if the REIT and its stapled operating company were stapled on June 30, 1983. On June 30, 1983, the registrant was stapled with the Management Company. There are, however, no judicial or administrative authorities interpreting this "grandfathering" rule. Moreover, if for any reason the registrant failed to qualify as a REIT in 1983, the benefit of the "grandfathering" rule would not be available to the registrant, in which case the registrant would not qualify as a REIT for any taxable year from and after 1983. The failure of the registrant to qualify as a REIT would have a material adverse effect on the registrant's ability to make dividends to its shareholders and to pay amounts due on its indebtedness.

If it is determined that the registrant did not qualify as a REIT during any of the preceding five fiscal years, the registrant potentially could incur corporate tax with respect to a year that is still open to adjustment by the Internal Revenue Service ("IRS"). If the registrant were to fail to qualify as a REIT, it would be subject to federal income tax (including any applicable alternative minimum tax) on its taxable



income at corporate rates. In addition, unless entitled to relief under certain statutory provisions and subject to the discussion above regarding the impact if the registrant failed to qualify as a REIT in 1983, the registrant also would be disqualified from re-electing REIT status for the four taxable years following the year during which qualification is lost. Failure to qualify as a REIT would result in additional tax liability to the registrant for the year or years involved. In addition, the registrant would no longer be required by the Code to make dividends to its shareholders. To the extent that dividends to shareholders would have been made in anticipation of the registrant's qualifying as a REIT, the registrant might be required to borrow funds or to liquidate certain of its investments on disadvantageous terms to pay the applicable tax.

The failure to qualify as a REIT would also constitute a default under certain debt obligations of the registrant, which would generally allow the holders thereof to demand the immediate repayment of such indebtedness. Any acceleration of this indebtedness (including through cross-defaults) could have a material adverse effect on the registrant and its ability to make dividends to shareholders and to pay amounts due on this and other indebtedness.

### **ADVERSE EFFECTS OF REIT MINIMUM DIVIDEND REQUIREMENTS**

In order to qualify as a REIT, the registrant is generally required each year to distribute to its shareholders at least 95% of its taxable income (excluding any net capital gain). In addition, if the registrant were to dispose of assets acquired in certain acquisitions during the ten-year period following the acquisitions, the registrant would be required to distribute at least 95% of the amount of any "built-in gain" attributable to such assets that the registrant recognizes in the disposition, less the amount of any tax paid with respect to such recognized built-in gain. The registrant generally is subject to a 4% nondeductible excise tax on the amount, if any, by which certain distributions paid by it with respect to any calendar year are less than the sum of:

- 85% of its ordinary income for that year,
- 95% of its capital gain net income for that year, and
- 100% of its undistributed income from prior years.

The registrant intends to make distributions to its shareholders to comply with the 95% distribution requirement and to avoid the nondeductible excise tax. Differences in timing between the recognition of taxable income and the receipt of cash available for distribution could require the registrant to borrow funds on a short-term basis on disadvantageous terms to meet the 95% distribution requirement and to avoid the nondeductible excise tax.

Distributions to shareholders by the registrant are determined by the registrant's board of trustees ("Board of Trustees") and depend on a number of factors, including the amount of cash available for distribution, financial condition, results of operations, any decision by the Board of Trustees to reinvest funds rather than to distribute such funds, capital expenditures, the annual distribution requirements under the REIT provisions of the Code and such other factors as the Board of Trustees deems relevant. For federal income tax purposes, distributions paid to shareholders may consist of ordinary income, capital gains, return of capital, or a combination thereof. The registrant will provide shareholders with annual statements as to the taxability of distributions.

### **ABILITY TO OPERATE PROPERTIES DIRECTLY AFFECTS THE REGISTRANT'S FINANCIAL CONDITION**

The registrant's investments will be subject to the risks inherent in owning real estate. The underlying value of the registrant's real estate investments, the results of its operations and its ability to make distributions to its shareholders and to pay amounts due on its indebtedness will depend on its ability to operate the registrant's properties in a manner sufficient to maintain or increase revenues and to generate sufficient revenues in excess of its operating and other expenses.

### **ILLIQUIDITY OF REAL ESTATE**

Real estate investments are relatively illiquid. The registrant's ability to vary its portfolio in response to changes in economic and other conditions will therefore be limited. If the registrant decides to sell an investment, no assurance can be given that the registrant will be able to dispose of it in the time period it desires or that the sales price of any investment will recoup or exceed the amount of the registrant's investment.

### **INCREASES IN PROPERTY TAXES COULD AFFECT ABILITY TO MAKE EXPECTED SHAREHOLDER DISTRIBUTIONS**

The registrant's real estate investments are all subject to real property taxes. The real property taxes on properties in which the registrant invests may increase or decrease as property tax rates change and as the value of the properties are assessed or reassessed by taxing authorities. Increases in property taxes may have an adverse effect on the registrant and its ability to make distributions to shareholders and to pay amounts due on its indebtedness.

### **ENVIRONMENTAL LIABILITIES**

The obligation to pay for the cost of complying with existing environmental laws, ordinances and regulations, as well as the cost of complying

with future legislation, may affect the operating costs of the registrant. Under various federal, state and local environmental laws, ordinances and regulations, a current or previous owner or operator of real property may be liable for the costs of removal or remediation of hazardous or toxic substances on or under the property. Environmental laws often impose liability whether or not the owner or operator knew of, or was responsible for, the presence of such hazardous or toxic substances and whether or not such substances originated from the property. In addition, the presence of hazardous or toxic substances, or the failure to remediate such property properly, may adversely affect the registrant's ability to borrow by using such real property as collateral.

Certain environmental laws and common law principles could be used to impose liability for releases of hazardous materials, including asbestos-containing materials or "ACMs," into the environment. In addition, third parties may seek recovery from owners or operators of real properties for personal injury associated with exposure to released ACMs or other hazardous materials. Environmental laws may also impose restrictions on the use or transfer of property, and these restrictions may require expenditures. In connection with the ownership and operation of any of the registrant's properties, the registrant, the Management Company and the other lessees of these properties may be liable for any such costs. The cost of defending against claims of liability or remediating contaminated property and the cost of complying with environmental laws could materially adversely affect the registrant and the Management Company and their ability to pay amounts due on their indebtedness and with respect to the registrant, to make distributions to its shareholders.

Prior to undertaking major transactions, the registrant has hired independent environmental experts to review specific properties. Thirty-six properties have been reviewed and no significant environmental hazards have been uncovered. The registrant has no reason to believe that any environmental contamination or violation of any applicable law, statute, regulation or ordinance governing hazardous or toxic substances has occurred or is occurring. However, no assurance can be given that hazardous or toxic substances are not located on any of the properties. The registrant will also endeavor to protect itself from acquiring contaminated properties or properties with significant compliance problems by obtaining site assessments and property reports at the time of acquisition when it deems such investigations to be appropriate. There is no guarantee, however, that these measures will successfully insulate the registrant from all such liabilities.

### **COMPLIANCE WITH THE ADA MAY AFFECT EXPECTED DISTRIBUTIONS TO THE REGISTRANT'S SHAREHOLDERS**

Under the Americans with Disabilities Act of 1990 (the "ADA"), all public accommodations are required to meet certain federal requirements related to access and use by disabled persons. A determination that the registrant is not in compliance with the ADA could also result in the imposition of fines and/or an award of damages to private litigants. If the registrant were required to make modifications to comply with the ADA, there could be a material adverse effect on its ability to pay amounts due on its indebtedness or to make distributions to its shareholders.

### **UNINSURED AND UNDERINSURED LOSSES**

The registrant may not be able to insure its properties against losses of a catastrophic nature, such as earthquakes and floods, because such losses are uninsurable or not economically insurable. The registrant will use its discretion in determining amounts, coverage limits and deductibility provisions of insurance, with a view to maintaining appropriate insurance coverage on its investments at a reasonable cost and on suitable terms. This may result in insurance coverage that, in the event of a substantial loss, would not be sufficient to pay the full current market value or current replacement cost of the lost investment and also may result in certain losses being totally uninsured. Inflation, changes in building codes, zoning or other land use ordinances, environmental considerations, lender imposed restrictions and other factors also might make it not feasible to use insurance proceeds to replace the property after such property has been damaged or destroyed. Under such circumstances, the insurance proceeds, if any, received by the registrant might not be adequate to restore its economic position with respect to such property.

### **INABILITY TO REFINANCE**

The registrant is subject to the normal risks associated with debt and preferred stock financings, including the risk that the registrant's cash flow will be insufficient to meet required payments of principal and interest and distributions, the risk that indebtedness on its properties, or unsecured indebtedness, will not be able to be renewed, repaid or refinanced when due or that the terms of any renewal or refinancing will not be as favorable as the terms of such indebtedness. If the registrant were unable to refinance the indebtedness on acceptable terms, or at all, the registrant might be forced to dispose of one or more of its properties on disadvantageous terms, which might result in losses to the registrant, which losses could have a material adverse effect on the registrant and its ability to make distributions to shareholders and to pay amounts due on its indebtedness. Furthermore, if a property is mortgaged to secure payment of indebtedness and the registrant is unable to meet mortgage payments, the mortgagee could foreclose upon the property, appoint a receiver and receive an assignment of rents and leases or pursue other remedies, all with a consequent loss of revenues and asset value to

the registrant. Foreclosures could also create taxable income without accompanying cash proceeds, thereby hindering the registrant's ability to meet the REIT distribution requirements of the Code.

## **RISING INTEREST RATES**

The registrant has incurred and expects in the future to incur indebtedness which bears interest at variable rates. Accordingly, increases in interest rates would increase the registrant's interest costs (to the extent that the related indebtedness was not protected by interest rate protection arrangements), which could have a material adverse effect on the registrant and its ability to make distributions to shareholders and to pay amounts due on its indebtedness or cause the registrant to be in default under certain debt instruments. In addition, an increase in market interest rates may cause holders to sell their shares of beneficial interest of the registrant ("Common Shares") and reinvest the proceeds thereof in higher yielding securities, which could adversely affect the market price for the Common Shares.

## **IMPACT OF YEAR 2000 ISSUES**

In June 1998, the registrant and the Management Company implemented a multi-step Year 2000 Compliance Project (the "Project") that was intended to assess the ability of their computer systems to properly recognize dates prior to, on, or after January 1, 2000. Any failure by the registrant and the Management Company to correct a material Year 2000 issue could result in the interruption or failure of certain normal business activities or operations. The most reasonable worst case scenarios for the registrant are

- a significant number of tenants at shopping centers will not be able to record sales transactions using their automated equipment or accept credit card transactions, and
- electric utility companies will not be able to provide power to operate shopping centers, office buildings, apartment complexes or parking facilities.

The most reasonable worst case scenarios for Impark are

- its financial reporting system will not work on or after January 1, 2000, and
- parking equipment that has been identified as non-compliant will not accept credit cards from parking patrons at the facilities it manages.

The registrant and the Management Company expect the total cost of required modifications to achieve Year 2000 compliance to be between \$1.0 million and \$2.0 million, including enhancements to software programs and upgrades to hardware. If these most reasonable worst case scenarios occurred, they could have a material adverse affect on the registrant's and the Management Company's results of operations, liquidity and financial condition.

## **EXCHANGE RATE LOSSES**

At December 31, 1998, the Management Company had approximately \$157 million of revenues attributable to Impark's Canadian operations, representing approximately 48% of the registrant's and the Management Company's total revenues. The registrant does not hedge its foreign currency exposure and does not currently intend to do so in the future.

The registrant recognized a \$2.2 million charge during 1998 related to unrealized exchange rate losses on loans to affiliated Canadian companies. As of December 31, 1998, the registrant also has recorded a \$2.1 million loss from the translation of the Canadian operations as a separate component of shareholders' equity. There can be no assurance that foreign currency rate fluctuations will not have a material adverse effect on the registrant's business, financial condition or results of operations in the future.

## **RESULTS OF OPERATIONS ADVERSELY AFFECTED BY FACTORS BEYOND THE REGISTRANT'S CONTROL**

Results of operations of the registrant's properties may also be adversely affected by, among other things:

- changes in national economic conditions, changes in local market conditions due to changes in general or local economic conditions and neighborhood characteristics;
- changes in interest rates and in the availability, cost and terms of financing;
- the impact of present or future environmental legislation and compliance with environmental laws and other regulatory requirements;
- the ongoing need for capital improvements, particularly in older structures;
- changes in real estate tax rates and assessments and other operating expenses;

- adverse changes in governmental rules and fiscal policies;
- adverse changes in zoning and other land use laws; and
- earthquakes and other natural disasters (which may result in uninsured losses) and other factors which are beyond its control.

## **CAUTIONARY STATEMENTS CONCERNING FORWARD-LOOKING STATEMENTS**

Any statements in this report, including any statements in the documents that are incorporated by reference herein that are not strictly historical are forward-looking statements within the meaning of the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Any such forward-looking statements contained or incorporated by reference herein should not be relied upon as predictions of future events. Certain such forward-looking statements can be identified by the use of forward-looking terminology such as "believes," "expects," "may," "will," "should," "seeks," "approximately," "intends," "plans," "pro forma," "estimates" or "anticipates" or the negative thereof or other variations thereof or comparable terminology, or by discussions of strategy, plans, intentions or anticipated or projected events, results or conditions. Such forward-looking statements are dependent on assumptions, data or methods that may be incorrect or imprecise and they may be incapable of being realized. Such forward-looking statements include statements with respect to:

- the declaration or payment of distributions by the registrant or the Management Company,
- the ownership, management and operation of properties,
- potential acquisitions or dispositions of properties, assets or other businesses by the registrant or the Management Company,
- the policies of the registrant or the Management Company regarding investments, acquisitions, dispositions, financings and other matters,
- the qualification of the registrant as a REIT under the Code and the "grandfathering" rules under Section 269B of the Code,
- the real estate industry and real estate markets in general,
- the availability of debt and equity financing,
- interest rates,
- general economic conditions,
- supply and customer demand,
- trends affecting the registrant or the Management Company,
- the effect of acquisitions or dispositions on capitalization and financial flexibility,
- the anticipated performance of the registrant or the Management Company and of acquired properties and businesses, including, without limitation, statements regarding anticipated revenues, cash flows, funds from operations, earnings before interest, depreciation and amortization, property net operating income, operating or profit margins and sensitivity to economic downturns or anticipated growth or improvements in any of the foregoing, and
- the ability of the registrant or the Management Company and of acquired properties and businesses to grow.

Shareholders are cautioned that, while forward-looking statements reflect the respective companies' good faith beliefs, they are not guarantees of future performance and they involve known and unknown risks and uncertainties. Actual results may differ materially from those in the forward-looking statements as a result of various factors. The information contained or incorporated by reference in this prospectus and any accompanying prospectus supplement, including, without limitation, the information set forth in "Risk Factors" below or in any risk factors in documents that are incorporated by reference in this report, identifies important factors that could cause such differences. Neither the registrant nor Management Company undertakes any obligation to publicly release the results of any revisions to these forward-looking statements that may reflect any future events or circumstances.

The number of persons employed by the registrant is 43.

**ITEM 2. PROPERTIES**

The following table sets forth certain information relating to the registrant's investments at December 31, 1998:

Direct equity investments	Location	Date of acquisition	Ownership percentage	Square feet(1) (000)	Occupancy rate(2)	Year construction completed	Total cost (000)
<b>Shopping Malls:</b>							
<b>Eastern</b>							
Mountaineer	Morgantown, WV	1/29/78	100%	676(4)	87%	1975	\$ 33,513
Fingerlakes	Auburn, NY	9/28/81	100	405	60	1980	27,967
Fairgrounds Square	Reading, PA	9/30/81	100	723(5)	91	1980	42,359
Crossroads	St. Cloud, MN	1/01/72	100	738(9)	99	1966	35,201
Two Rivers	Clarksville, TN	9/26/75	100	231(10)	45	1968	8,771
Crossroads	Fort Dodge, IA	4/22/77	100	429(11)	92	1967	13,748
Kandi	Willmar, MN	3/12/79	100	448	85	1973	21,009
Woodland Commons(12)	Buffalo Grove, IL	4/03/95	100	170	100	1991	22,204
Westgate Towne Centre	Abilene, TX	4/22/77	100	163(13)	98	1962	16,900
							221,672
<b>Western</b>							
Valley North	Wenatchee, WA	8/30/73	100	267	87	1966	5,262
Mall 205	Portland, OR	3/01/75	100	432(14)	94	1970	14,371
Plaza 205	Portland, OR	4/26/78	100	167	100	1970	4,558
Valley	Yakima, WA	5/01/80	100	390(15)	89	1972	11,737
							35,928
<b>Southwestern:</b>							
Alexandria	Alexandria, LA	09/01/97	100	898	95	1973	31,681
Brazos	Lake Jackson, TX	09/01/97	100	707	92	1976	25,938
Killeen	Killeen, TX	09/01/97	100	579	93	1981	42,625
Mesilla Valley	Las Cruces, NM	09/01/97	100	593	90	1981	40,191
Park Plaza	Little Rock, AR	09/01/97	100	547	100	1988	64,145
Pecanland	Monroe, LA	09/01/97	100	923	99	1985	46,462
Shawnee	Shawnee, OK	09/01/97	100	445	95	1989	19,717
Villa Linda	Santa Fe, NM	09/01/97	100	569	92	1985	43,978
							314,737
							572,337
<b>Apartments:</b>							
<b>Midwestern</b>							
Somerset Lakes	Indianapolis, IN	11/10/88	100	360 units	93	1975	21,135
Hunter's Creek	Cincinnati, OH	12/11/96	100	146 units	98	1980	5,785
Steeplechase	Cincinnati, OH	06/30/95	100	272 units	96	1987	12,246
							39,166
<b>Southern</b>							
Briarwood	Fayetteville, NC	6/30/91	100	274 units	95	1968-70	8,425
Woodfield Gardens	Charlotte, NC	6/30/91	100	132 units	90	1974	3,933
Windgate Place	Charlotte, NC	6/30/91	100	196 units	94	1974-78	6,554
Walden Village	Atlanta, GA	6/01/92	100	372 units	96	1973	14,376
Beech Lake	Durham, NC	8/19/94	100	345 units	94	1986	20,217
							53,505
							92,671

**Mortgage Loans**

Direct Equity Investments	Original balance(s) (000)	Balance at 12/31/98 (000)	Principal repayment for 1999 (000)	Interest rate	Year of maturity
Shopping Malls:					
Eastern					
Mountaineer	\$ 4,600(3)	\$ 3,734	\$ 236	8.250%	2009

Fingerlakes	---	---	---	---	---
Fairgrounds Square	---	---(6)	---	---	---
Crossroads	49,500(3)	47,528	743	7.485	2002
Two Rivers	---	---	---	---	---
Crossroads	---	---(6)	---	---	---
Kandi	---	---(6)	---	---	---
Woodland Commons(12)	12,000(3)	11,491	256	7.750	2006
Westgate Towne Centre	---	---	---	---	---
	-----	-----	-----		
	66,100	62,753	1,235		
	-----	-----	-----		
Western					
-----					
Valley North	---	---	---	---	---
Mall 205	---	---(6)	---	---	---
Plaza 205	---	---(6)	---	---	---
Valley	---	---(6)	---	---	---
	-----	-----	-----		
	---	---	---		
	-----	-----	-----		
Southwestern:					
-----					
Alexandria	21,463	21,223(7)	199	8.430	2006
Brazos	15,749	15,573(7)	146	8.430	2006
Killeen	28,319	28,002(7)	262	8.430	2006
Mesilla Valley	24,643	24,367(7)	228	8.430	2006
Park Plaza	37,511	37,091(7)	347	8.430	2006
Pecanland	39,344	38,711(8)	543	12.250	2017
Shawnee	11,576	11,447(7)	107	8.430	2006
Villa Linda	24,692	24,416(7)	228	8.430	2006
	-----	-----	-----		
	203,297	200,830	2,060		
	-----	-----	-----		
	269,397	263,583	3,295		
	-----	-----	-----		
Apartments:					
Midwestern					
-----					
Somerset Lakes	15,000(3)	14,410	254	7.650	2006
Hunter's Creek	2,738	2,706	24	8.470	2002
Steeplechase	9,000(3)	8,632	158	7.395	2006
	-----	-----	-----		
	26,738	25,748	436		
	-----	-----	-----		
Southern					
-----					
Briarwood	---	---(6)	---	---	---
Woodfield Gardens	---	---(6)	---	---	---
Windgate Place	---	---(6)	---	---	---
Walden Village	---	---(6)	---	---	---
Beech Lake	12,500(3)	11,984	202	6.869	2005
	-----	-----	-----		
	12,500	11,984	202		
	-----	-----	-----		
	39,238	37,732	638		
	-----	-----	-----		

ITEM 2. PROPERTIES

-CONTINUED

Direct equity investments	Location	Date of acquisition	Ownership percentage	Square feet(1) (000)	Occupancy rate(2)	Year construction completed	Total cost (000)
<b>Office Buildings:</b>							
<b>Midwestern</b>							
55 Public Square	Cleveland, OH	01/15/63	100%	396	82%	1959	\$ 38,945
Circle Tower	Indianapolis, IN	10/16/74	100	102	87	1930	4,919
							-----
							43,864
							-----
<b>Southern</b>							
Henry C. Beck(16)	Shreveport, LA	08/30/74	100	185	84	1958	10,196
							-----
							10,196
							-----
<b>Western Redevelopment</b>							
North Valley Tech Center	Denver, CO	12/03/69	100	484	57(17)	1967	28,392
Sutter Buttes Center	Marysville, CA	12/19/79	100	427	54(18)	1972	13,868
							-----
							42,260
							-----
							96,320
							-----
<b>Parking Facilities:</b>							
<b>United States</b>							
Huntington Garage	Cleveland, OH	12/31/75	100	1,100 spcs	---	1969	8,127
West Third St. lot	Cleveland, OH	09/19/77	100	300 spcs	---	---	2,443
5th and Marshall Garage	Richmond, VA	02/24/98	100	793 spcs	---	1985	9,192
Long Street Garage	Columbus, OH	01/16/98	100	550 spcs	---	1978	3,928
Madison & Wells Garage	Chicago, IL	01/28/98	100	1,107 spcs	---	1998	43,184
Magic Mile Lot	Arlington, TX	03/26/98	100	1,000 spcs	---	1997	3,011
Printer's Alley Garage	Nashville, TN	07/01/98	100	275 spcs	---	1926	6,650
							-----
							76,535
							-----
<b>Canada:</b>							
10th Ave. Lot	Calgary, Alberta	05/05/97	100	55 spcs	---	---	228
1009-9th Ave. Lot	Calgary, Alberta	05/05/97	100	142 spcs	---	---	587
Parkade	Edmonton, Alberta	05/05/97	100	562 spcs	---	1958	1,241
103 St. Lot	Edmonton, Alberta	05/05/97	100	61 spcs	---	---	310
107th St.	Edmonton, Alberta	05/05/97	100	-- (18)	100	1973	196
221 9th Ave. Lot	Calgary, Alberta	05/05/97	100	148 (19)	---	---	1,370
Blanchard St.	Victoria, Br.Columbia	05/05/97	100	-- (19)	100	1982	312
Graham Ave. Lot	Winnipeg, Manitoba	05/05/97	100	175 spcs	---	---	1,124
Water Ave. Lot	Winnipeg, Manitoba	05/05/97	100	235 spcs	---	---	595
Young St. Lot	Winnipeg, Manitoba	05/05/97	100	40 spcs	---	---	98
Broadway Lot	Winnipeg, Manitoba	05/05/97	100	67 spcs	---	---	415
Donald St. Lot	Winnipeg, Manitoba	05/05/97	100	-- (20)	---	---	113
Broad St. Lot	Regina, Saskatchewan	05/05/97	100	20 spcs	---	---	35
Queens Quay	Toronto, Ontario	05/05/97	100	-- (19)	100	1950	1,206
351 Smith St.	Winnipeg, Manitoba	09/09/97	100	110 spcs	---	---	800
							-----
							8,630
							-----
							85,165
							-----
							\$846,493
							(39,634)
							-----
							\$806,859
							=====

Write-down for unrealized loss on carrying value of real estate (21)

Total equity investments

Mortgage Loans

Direct equity investments	Original balance(s) (000)	Balance at 12/31/98 (000)	Principal repayment for 1999 (000)	Interest rate	Year of maturity
Office Buildings:					
Midwestern					
55 Public Square Circle Tower	\$ ---	\$ ---(6)	\$ ---	---	---
Southern					
Henry C. Beck	---	---	---	---	---
Western Redevelopment					
North Valley Tech Center Sutter Buttes Center	---	---	---	---	---
Parking Facilities:					
United States					
Huntington Garage	9,300(3)	8,201	282	8.550%	2014
West Third St. Garage	---	---	---	---	---
5th and Marshall Garage	---	---(6)	---	---	---
Long Street Garage	1,602(3)	1,526(21)	93(21)	(21)	---(21)
Madison & Wells Garage	30,000(3)	30,000	---	LIBOR+1.75%	2001
Magic Mile Lot	---	---	---	---	---
Printer's Alley Garage	4,468(3)	4,000	---	LIBOR+1.75%	2001
	45,370	43,727	375		
Canada:					
10th Ave. Lot	---	---	---	---	---
1009-9th Ave. Lot	---	---	---	---	---
Parkade	---	---	---	---	---
103 St. Lot	---	---	---	---	---
107th St.	---	---	---	---	---
221 9th Ave. Lot	---	---	---	---	---
Blanchard St.	---	---	---	---	---
Graham Ave. Lot	---	---	---	---	---
Water Ave. Lot	---	---	---	---	---
Young St. Lot	---	---	---	---	---
Broadway Lot	---	---	---	---	---
Donald St. Lot	---	---	---	---	---
Broad St. Lot	---	---	---	---	---
Queens Quay	---	---	---	---	---
351 Smith St.	---	---	---	---	---
	45,370	43,727	375		
	\$ 354,005	\$345,042	\$ 4,308		



- (1) The square footage shown represents gross leasable area for shopping malls and net rentable area for office buildings. The apartments are shown as number of units. The parking garages and parking facilities are shown as number of parking spaces.
- (2) Occupancy rates shown are as of December 31, 1998, and are based on the total square feet at each property, except apartments which are based on the number of units and occupied at the end of the year.
- (3) The registrant obtained mortgages on the following properties subsequent to acquisition: Huntington Parking Garage in the amount of \$9,300,000 in 1993; Mountaineer Mall in the amount of \$4,600,000 in 1994; Crossroads Shopping Center (St. Cloud, MN) in the amount of \$49,500,000 in 1995; Woodland Commons in the amount of \$12,000,000 in 1996; Somerset Lakes in the amount of \$15,000,000 in 1996; Steeplechase in the amount of \$9,000,000 in 1996; Beech Lake in the amount of \$12,500,000 in 1996; Hunter's Creek in the amount of \$2.7 million; Madison & Wells Garage in the amount of \$30,000,000 in 1998. The registrant assumed \$4,468,000 and \$1,602,000 in mortgage debt upon the acquisition of the Printer's Alley Garage and the Long Street Garage, respectively.
- (4) The total mall contains 676,000 square feet; the registrant owns 618,000 square feet, the balance being ground leased to Giant Eagle Markets, Inc.
- (5) The total mall contains 723,000 square feet; the registrant owns 537,000 square feet, the balance being separately ground leased to Boscov's Department Store, Inc.
- (6) These properties are the collateral for the registrant's \$110 million revolving line of credit.
- (7) The mortgage secured by these malls requires that all rents and other tenant charges be deposited into a bank account which serves as additional security for the lender.
- (8) The mortgage loan participates in 55% of revenues, as defined, in excess of \$5,970,516.
- (9) The total mall contains 738,000 square feet; the registrant owns 626,000 square feet, the balance being separately owned by Target Stores.
- (10) The mall is currently being converted to an office complex in 1998. Approximately 58,000 square feet of office space has been leased to an office tenant opening in the second quarter of 1999.
- (11) The total mall contains 429,000 square feet; the registrant owns 332,000 square feet, the balance being separately owned by an unrelated third party with Sears, Roebuck and Co. as tenant.
- (12) This property was sold in February 1999 for \$21.6 million resulting net proceeds of \$9.3 million after repayment of debt.
- (13) The mall is currently being redeveloped as a power strip center with Winn-Dixie occupying 65,000 square feet in July 1998. Currently, 95,000 square feet is separately owned by Montgomery Ward & Co., Incorporated.
- (14) The total mall contains 432,000 square feet; the registrant owns 255,000 square feet, the balance being separately owned by Montgomery Ward Development

## Corporation.

- (15) The total mall contains 390,000 square feet; the registrant owns 272,000 square feet, the balance being separately ground leased to Sears, Roebuck and Co.
- (16) The registrant sold this building in March 1999 for \$2.1 million resulting in net proceeds of \$1.8 million.
- (17) North Valley Technical Center was repositioned from a shopping mall to an office complex during 1995. Montgomery Ward vacated the complex in 1997 allowing the registrant to continue to retenant the former mall as an office center.
- (18) The property was inundated by a flood which occurred in February 1986. The mall was subsequently rebuilt and re-opened in November 1986. A temporary tenant occupied approximately 70,000 square feet as of December 31, 1998. The Trust is pursuing a mixed use strategy for this former retail facility.
- (19) These properties are general use buildings currently being used as regional and city offices by Impark Limited.
- (20) This property is currently demolished and awaiting redevelopment.
- (21) This property has two mortgages. Interest rates are 8.25% and 8.625%. The mortgages mature in 2003 and 2009, respectively. The 8.25% mortgage, in the principal amount of \$863,000 has a principal payment for 1999 of \$50,000. The 8.625% mortgage, in the principal amount of \$663,000, has a principal payment for 1999 of \$43,000.
- (22) In December 1995, the registrant recorded a \$14 million unrealized loss on the carrying value of assets identified for disposition. Subsequent to the disposition of three office buildings and one shopping mall, this reserve was \$3,630,000 as of December 31, 1997 after restatement due to the retroactive restatement of depreciation expense. In December 1998, the registrant recorded a \$36 million unrealized loss on the carrying value of assets identified for disposition.

As of December 31, 1998, the registrant owned in fee its interests in Crossroads Center (St. Cloud, MN), Woodland Commons, Mall 205, Crossroads Mall (Ft. Dodge, IA), Westgate Towne Centre, Mountaineer Mall, Plaza 205, Valley Mall, Fingerlakes Mall, Fairgrounds Square Mall, 55 Public Square Building, Henry C. Beck Building, Sutter Buttes Center, Brazos Mall, Killeen Mall, Mesilla Valley Mall, Park Plaza Mall, Pecanland Mall, Shawnee Mall, Villa Linda Mall, Somerset Lakes Apartments, Briarwood Apartments, Woodfield Gardens Apartments, Windgate Place Apartments, Walden Village Apartments, Beech Lake Apartments, Steeplechase Apartments, Hunter's Creek Apartments, Parkade, West Third Lot, 10th Avenue, 1009 9th Avenue, 103 St., 107 St., 221 9th Avenue, Graham Ave., Water Ave., Young St., Broad St., Broadway, 357 Smith St., Blanchard St., Queens Quay, Donald St., St. Clair Development Property, Madison & Wells Garage, Long Street Garage, 5th & Marshall Garage, Magic Mile Lot, Printer's Alley Garage. The registrant holds a leasehold estate or estates, or a fee interest and one or more leasehold estates in Valley North Mall, Two Rivers Mall, Kandi Mall, Alexandria Mall, Circle Tower Building and North Valley Technical Center and the Huntington Garage.

## RENTALS FROM NET LEASES

The registrant leases 47 of its properties to its Management Company. The Management Company operates these properties and pays the registrant a fixed based rent and participation rent based on property revenues (Percentage Rents)

The following table sets forth the rentals paid to the registrant from the Management Company for the year ended December 31, 1998, under net leases of the properties indicated:

PROPERTY -----	ANNUAL BASE RENT -----	PERCENTAGE RENTS -----
SHOPPING MALLS:		
EASTERN		
-----		
Mountaineer (1)	\$ 755,000	\$ 712,000
Fingerlakes (1)(3)	780,000	174,000
Fairgrounds Square (1)	2,850,000	921,000
Crossroads (St. Cloud, MN.) (1)(4)	3,307,500	3,397,000
Two Rivers (1)	---	32,000
Crossroads (Ft. Dodge, IA) (1)	736,000	809,000
Westgate Towne Centre (1)	---	35,000
Kandi (1)	712,000	545,000
Woodland Commons (1)	1,600,000	416,000
WESTERN		
-----		
Valley North (1)	400,000	142,000
Mall 205 (1)	1,232,000	534,000
Plaza 205 (1)	276,000	272,000
Valley (1)	463,000	472,000
SOUTHWESTERN		
-----		
Alexandria (2)		
Brazos (2)		
Killeen (2)		
Mesilla Valley (2)		
Park Plaza (2)		
Pecanland (2)		
Shawnee (2)		
Villa Linda (2)		
APARTMENTS:		
MIDWESTERN		
-----		
Somerset Lakes (1)	971,000	1,207,000
Steeplechase (1)	800,000	595,000
Hunter's Creek (1)	500,000	36,000
SOUTHERN		
-----		
Briarwood (1)	435,000	232,000
Woodfield Gardens (1)	100,000	54,000

Windgate Place (1)	235,000	103,000
Walden Village (1)	850,000	568,000
Beech Lake (1)	955,000	722,000
OFFICE BUILDINGS:		
MIDWESTERN		
-----		
55 Public Square (1),(5)	\$1,650,000	1,260,000
Circle Tower (1)	209,000	134,000
SOUTHERN		
-----		
Henry C. Beck (1)	179,000	166,000
WESTERN		
-----		
North Valley Technical Center (1)	500,000	57,000
Sutter Buttes Center (1)	292,000	271,000
PARKING:		
UNITED STATES		
-----		
Huntington Garage (1)	825,000	154,000
West Third Lot (1)	150,000	74,000
201 West Madison Garage (1)	2,400,000	1,458,000
60 East Long Street Garage (1)	400,000	---
5th & Marshall Garage (1)	500,000	57,000
Magic Mile Lot (1)	---	92,000
Printer's Alley Garage (1)	450,000	---
CANADIAN		
-----		
10th Avenue (1)	15,600	---
1009 9th Avenue (1)	39,000	---
Parkade (1)	130,000	---
103 St.(1)	27,000	---
221 9th Ave. (1)	95,000	---
245 Graham Ave. (1)	60,000	---
168 Water Ave. (1)	65,000	---
336 Young St. (1)	7,000	---
304 Broadway (1)	8,000	---
1724 Broad St. (1)	4,000	---
351 Smith St. (1)	3,000	---

- (1) Leased to the Management Company.
- (2) The Management Company manages these shopping malls for the registrant and receives a management fee of 4% of gross receipts as a management fee, as defined, and a leasing fee of 4.5% of base rent, as defined, over the term of the lease, for new and renewal tenants, respectively.
- (3) Includes a separate lease for Fingerlakes Storage.
- (4) Includes a separate lease for the Stearns County Building.
- (5) Includes a separate lease for the Illuminating Parking Garage.

**ITEM 3. LEGAL PROCEEDINGS.**

**REGISTRANT VS. THE STATE OF CALIFORNIA**

The registrant has pursued legal action against the State of California associated with the 1986 flood of Sutter Buttes Center, formerly Peach Tree Mall. In September 1991, the court ruled in favor of the registrant on the liability portion of this inverse condemnation suit, which the State of California appealed. The registrant is proceeding with its damage claim in Superior Court of the State of California. No recognition of potential income has been made in the December 31, 1998 Combined Financial Statements.

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.**

None.

**PART II**

**ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS.**

"Market Price and Dividend Record" presented on page 1 of Exhibit 13.

**ITEM 6. SELECTED FINANCIAL DATA.**

"Selected Financial Data" presented on page 2 and 3 of Exhibit 13.

**ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.**

"Management's Discussion and Analysis of Financial Condition and Results of Operations" presented on pages 25 through 31 of Exhibit 13.

**ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES REGARDING MARKET RISK.**

Quantitative and Qualitative disclosures regarding market risk presented on page 31 of Exhibit 13.

**ITEM 8. FINANCIAL STATEMENTS.**

The "Combined Balance Sheets" as of December 31, 1998 and 1997, and the "Combined Statements of Operations, Combined Statements of Comprehensive Income, Combined Statements of Changes in Cash, Combined Statements of Shareholders' Equity" for the years ended December 31, 1998, 1997 and 1996, of the registrant, "Notes to Combined Financial Statements" and "Report of Independent Public Accountants" are presented on pages 4 through 24 of Exhibit 13.

**ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.**

None.

### **PART III**

#### **ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT.**

##### **(A) DIRECTORS.**

"Election of Trustees" presented in the registrant's 1999 Proxy Statement is incorporated herein by reference.

##### **(B) EXECUTIVE OFFICERS.**

Executive offices as presented in the registrant's 1999 Proxy Statement is incorporated by reference.

#### **ITEM 11. EXECUTIVE COMPENSATION.**

"Compensation of Trustees" and "Executive Compensation", presented in the registrant's 1999 Proxy Statement are incorporated herein by reference.

#### **ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT.**

"Security Ownership of Trustees, Officers and Others" presented in the registrant's 1999 Proxy Statement is incorporated herein by reference.

#### **ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS**

"Certain Transactions and Relationships" presented in the registrant's 1999 Proxy Statement is incorporated herein by reference.

### **PART IV**

#### **ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K.**

##### **(a) FINANCIAL STATEMENTS AND FINANCIAL STATEMENT SCHEDULES.**

###### **(1) FINANCIAL STATEMENTS:**

Combined Balance Sheets - December 31, 1998 and 1997 on page 4 of Exhibit 13.

Combined Statements of Operations - For the Years Ended December 31, 1998, 1997 and 1996 on page 5 of Exhibit 13.

Combined Statements of Comprehensive Income - For the Years Ended December 31, 1998, 1997 and 1996 on page 5 of Exhibit 13.

Combined Statements of Changes in Cash - For the Years Ended December 31, 1998, 1997 and 1996 on page 6 of Exhibit 13.

Combined Statements of Shareholders' Equity - For the Years Ended December 31, 1998, 1997 and 1996 on page 7 of Exhibit 13.

Notes to Combined Financial Statements on pages 8 to 23 of Exhibit 13.

Report of Independent Public Accountants on page 24 of Exhibit 13.

###### **(2) FINANCIAL STATEMENT SCHEDULES:**

Report of Independent Public Accountants on Financial Statement Schedules.

**Schedule III - Real Estate and Accumulated Depreciation.**

**Schedule IV - Mortgage Loans on Real Estate.**

All Schedules, other than III and IV, are omitted, as the information is not required or is otherwise furnished.

(B) EXHIBITS.

EXHIBIT NUMBER -----	DESCRIPTION -----	INCORPORATED HEREIN BY REFERENCE TO -----	PAGE -----
(3)(a)	Declaration of Trust of Registrant dated August 1, 1961, as amended through July 25, 1986	Registration Statement on Form S-3 No. 33-4493	-----
(3)(b)	By-laws of Registrant, as amended	Registration Statement on Form S-3 No. 33-4493	-----
(3)(c)	By-laws of Registrant, as amended	March 31, 1997 Form 10-Q	-----
(3)(d)	By-laws of Registrant as amended	1998 10-K	X -----
(4)(a)	Form of certificate for Shares of Beneficial Interest	Registration Statement on Form S-3 No. 33-2818	-----
(4)(b)	Form of Indenture governing Debt Securities, dated February 1, 1983 between Registrant and Ameritrust Company	Registration Statement on Form S-3 No. 2-81605	-----
(4)(c)	Form of Debt Security	Registration Statement on Form S-3 No. 33-4493	-----
(4)(d)	Form of Indenture governing Debt Securities, dated October 1, 1993 between Registrant and Society National Bank	Registration Statement on Form S-3 No. 33-68002	-----
(4)(e)	Form of Note	Registration Statement on Form S-3 No. 33-68002	-----
(4)(f)	Form of Indenture governing Debt Securities	Registration Statement on Form S-3 No. 333-00953	-----
(4)(g)	Rights Agreement between Registrant and National City Bank dated March 7, 1990	Form 8-A dated March 30, 1990 No. 0-18411	-----
(4)(h)	Certificate of Designations relating to Registrant's Series A Cumulative Redeemable Preferred Shares of Beneficial Interest	Form 8-K dated October 24, 1996	-----
(4)(i)	Standby Purchase Agreement between Registrant and Gotham Partners, L.P. dated August 11, 1998	Schedule 13D dated August 11, 1998	-----
(4)(j)	Standby Purchase Agreement between Registrant and Gotham Partners III, L.P. dated August 11, 1998	Schedule 13D dated August 11, 1998	-----
(4)(l)	Warrant to purchase 500,000 shares of beneficial interest of Registrant		X -----

EXHIBIT NUMBER -----	DESCRIPTION -----	INCORPORATED HEREIN BY REFERENCE TO -----	PAGE ----
(4)(k)	Standby Purchase Agreement between Registrant and Elliott Associates, L.P. dated August 11, 1998	Schedule 13D dated August 11, 1998	----
(10)(a)	Share Purchase Agreement dated as of December 31, 1983 between registrant and First Union Management, Inc.	Registration Statement No. 2-88719	----
(10)(b)	First Amendment to Share Purchase Agreement dated as of December 10, 1985 between registrant and First Union Management, Inc.	Registration Statement No. 33-2818	----
(10)(c)	Second Amendment to Share Purchase Agreement dated as of December 9, 1986 between registrant and First Union Management, Inc.	Registration Statement No. 33-11524	----
(10)(d)	Third Amendment to Share Purchase Agreement dated as of December 2, 1987 between registrant and First Union Management, Inc.	Registration Statement No. 33-19812	----
(10)(e)	Fourth Amendment to Share Purchase Agreement dated as of December 7, 1988 between registrant and First Union Management, Inc.	Registration Statement No. 33-26758	----
(10)(f)	Fifth Amendment to Share Purchase Agreement dated as of November 29, 1989 between registrant and First Union Management, Inc.	Registration Statement No. 33-33279	----
(10)(g)	Sixth Amendment to Share Purchase Agreement dated as of November 28, 1990 between registrant and First Union Management, Inc.	Registration Statement No. 33-38754	----
(10)(h)	Seventh Amendment to Share Purchase Agreement dated as of November 27, 1991 between registrant and First Union Management, Inc.	Registration Statement No. 33-45355	----
(10)(i)	Eighth Amendment to Share Purchase Agreement dated as of November 30, 1992 between registrant and First Union Management, Inc.	Registration Statement No. 33-57756	----
(10)(j)	Employment and Consulting Agreement with Donald S. Schofield dated September 1, 1991	1991 Form 10-K	----



EXHIBIT NUMBER -----	DESCRIPTION -----	INCORPORATED HEREIN BY REFERENCE TO -----	PAGE ----
(10)(k)	Employment Agreement with James C. Mastandrea dated July 13, 1994	June 30, 1994 Form 10-Q	----
(10)(l)	Employment Agreement with Gregory D. Bruhn dated July 13, 1994	June 30, 1994 Form 10-Q	----
(10)(m)	Credit Agreement with National City Bank dated December 5, 1994	1994 Form 10-K	----
(10)(n)	Credit Agreement with Society National Bank dated March 4, 1996	1995 Form 10-K	----
(10)(o)	1981 Employee Share Option Plan	1992 Proxy Statement	----
(10)(p)	1994 Long Term Incentive Performance Plan	1994 Proxy Statement	----
(10)(q)	Bank Credit Agreement dated September 30, 1996	September 30, 1996 Form 10-Q	----
(10)(r)	Credit agreement between Imperial Parking Limited and BT Bank of Canada	March 31, 1997 Form 10-Q	----
(10)(s)	Put agreement entered into between BT Bank of Canada, Hong Kong Bank of Canada and First Union Real Estate Equity and Mortgage Investment	March 31, 1997 Form 10-Q	----
(10)(t)	Share Purchase Agreement and amendments Impark Investments Inc. and First Union Real Estate Equity and Mortgage Investments	March 31, 1997 Form 10-Q	----
(10)(u)	Put agreement entered into between Impark E Investments Inc., the Onex Associates and First Union Real Estate Equity and Mortgage Investments	March 31, 1997 Form 10-Q	----
(10)(v)	Senior subordinated note by 3357392 Canada Inc. to 3006302 Nova Scotia Company	March 31, 1997 Form 10-Q	----
(10)(w)	Senior subordinated note by 504463 N.B. Inc. to 3006302 Nova Scotia Company	March 31, 1997 Form 10-Q	----
(10)(x)	Shareholders Agreement dated April 17, 1997 between 3357392 Canada, Inc. and 3355489 Canada, Inc. and the individuals and trusts listed on Schedule A.	March 31, 1997 Form 10-Q	----

EXHIBIT NUMBER -----	DESCRIPTION -----	INCORPORATED HEREIN BY REFERENCE TO -----	PAGE -----
(10)(y)	Shareholders Agreement dated April 17, 1997 between 504308 N.B., Inc. First Union Management, Inc. and the individuals listed on Schedule A.	March 31, 1997 Form 10-Q	-----
(10)(z)	Assignment dated March 27, 1997 between First Union Real Estate Equity and Mortgage Investments and First Union Management, Inc.	March 31, 1997 Form 10-Q	-----
(10)(aa)	Assignment dated April 16, 1997 between First Union Management, Inc. and 335489 Canada, Inc.	March 31, 1997 Form 10-Q	-----
(10)(ab)	Assignment dated April 16, 1997 between 335489 Canada, Inc. and 3357392 Canada, Inc.	March 31, 1997 Form 10-Q	-----
(10)(ac)	Amendment to assignment made May 8, 1997 between First Union Real Estate Equity and Mortgage Investments and Imperial Parking Limited.	March 31, 1997 Form 10-Q	-----
(10)(ad)	Bank credit agreement dated December 5, 1997	1997 Form 10-K	-----
(10)(ae)	First amendment to employment agreement of James C. Mastandrea	1997 Form 10-K	-----
(10)(af)	Form of charge in control agreement	1997 Form 10-K/A	-----
(10)(ag)	Fixed Rate Loan Agreement dated as of August 11, 1998 by and among the Registrant, as borrower, Bankers Trust Company, as agent, and Wellsford Capital and BankBoston, N.A., as lenders	Registration Statement on Form S-3 No. 333-63547	-----
(10)(ah)	Fixed Rate Loan Agreement dated as of August 11, 1998 by and among the Registrant, as borrower, Bankers Trust Company, as agent, and Gotham Partners, L.P., Gotham Partners III, L.P., Elliott Associates, L.P. and Blackacre Bridge Capital, L.L.C., as lenders	Registration Statement on Form S-3 No. 333-63547	-----
(10)(ai)	Employment contract for Daniel P. Friedman		X -----
(10)(aj)	Employment contract for Anne N. Zahner		X -----
(10)(ak)	Employment contract for David Schonberger		X -----

EXHIBIT NUMBER	DESCRIPTION	INCORPORATED HEREIN BY REFERENCE TO	PAGE
-----	-----	-----	-----
(10)(al)	Amendment No. 2, dated as January 8, 1999, to Amended and Restated Credit Agreement, dated as of November 1, 1997, among First Union Real Estate Equity and Mortgage Investments, and First Union Management, Inc., as borrower, and National City Bank, Bankers Trust Company, Key Bank National Associates, The Huntington National Bank, Mellon Bank, N.A. and First Merit Bank, as Lenders.	Form 8-K dated February 2, 1999.	----
	First Amendment to Fixed Rate Loan Agreement between First Union Real Estate Equity and Mortgage Investments, as Borrower; and Blackacre Bridge Capital, L.L.C., Gotham Partners, L.P., Gotham Partners III, L.P. and Elliott Associates, L.P., as Lenders, dated January 8, 1999.		
	Letter Agreement between First Union Real Estate Equity and Mortgage Investments, as Borrower; and Blackacre Bridge Capital, L.L.C. Gotham Partners, L.P., Gotham Partners III, L.P. and Elliott Associates, L.P., as Lenders, dated January 8, 1999		
	First Amendment to Fixed Rate Loan Agreement between First Union Real Estate Equity and Mortgage Investments, as Borrower; and BankBoston, N.A., Wellsford Capital and Bankers Trust Company, as Lenders, dated January 8, 1999.		
	Letter Agreement between First Union Real Estate Equity and Mortgage Investments, as Borrower; and BankBoston, N.A., Wellsford Capital and Bankers Trust Company, as Lenders, dated January 8, 1999.		

EXHIBIT NUMBER -----	DESCRIPTION -----	INCORPORATED HEREIN BY REFERENCE TO -----	PAGE -----
	Second Amendment, dated as of December 30, 1998, to the Amended and Restated Credit Agreement Dated as of April 17, 1997 between Imperial Parking Limited, as Borrower, Impark Services Limited, as Guarantor, and HongKong Bank of Canada and BT Bank of Canada, as Lenders.		
(12)	Statements of Ratios of Combined Income from Operations and Combined Net Income to Fixed Charges		X -----
(13)	1998 Annual Report		X -----
(23)	Consent of Independent Public Accountants		X -----
(24)	Powers of Attorney		X -----
(27)	Financial Data Schedule		X -----
(C)	REPORTS ON FORM 8-K. -----		
	None.		



**REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS ON**

**FINANCIAL STATEMENT SCHEDULES**

To First Union Real Estate Equity  
and Mortgage Investments:

We have audited in accordance with generally accepted auditing standards, the combined financial statements included in the registrant's 1998 Annual Report, included as Exhibit 13 of this Form 10-K, and have issued our report thereon dated March 29, 1999. Our audit was made for the purpose of forming an opinion on those combined statements taken as a whole. The schedules listed under Item 14(a)(2) on page 14 are the responsibility of management and are presented for purposes of complying with the Securities and Exchange Commission's rules and are not part of the basic combined financial statements. These schedules have been subjected to the auditing procedures applied in the audit of the basic combined financial statements and, in our opinion, fairly state in all material respects the financial data required to be set forth therein in relation to the basic combined financial statements taken as a whole.

Cleveland, Ohio, Arthur Andersen LLP March 29, 1999.

## SCHEDULE III

### REAL ESTATE AND ACCUMULATED DEPRECIATION

AS OF DECEMBER 31, 1998

(IN THOUSANDS)

Description	Encum- brances	Initial cost to Registrant		Cost capitalized subsequent to acquisition	Currency revaluation of foreign assets
		Land	Buildings and Improvements	Land and Improvements	
<b>Shopping Malls:</b>					
<b>Eastern</b>					
Mountaineer, Morgantown, WV	\$ 3,734	\$ 1,450	\$ 12,693	\$ 19,370	--
Fingerlakes, Auburn, NY	--	1,300	23,698	2,969	--
Fairgrounds Square, Reading, PA	--	2,400	22,635	17,324	--
Crossroads, St. Cloud, MN	47,528	1,680	8,303	25,218	--
Two Rivers, Clarksville, TN	--	--	3,206	5,565	--
Crossroads, Ft. Dodge, IA	--	1,151	2,792	9,805	--
Kandi, Willmar, MN	--	--	5,035	15,974	--
Woodland Commons, Buffalo Grove, IL	11,491	6,744	15,093	367	--
Westgate Towne Centre, Abilene, TX	--	1,425	3,050	12,425	--
	62,753	16,150	96,505	109,017	--
<b>Western</b>					
Valley North, Wenatchee, WA	--	405	2,916	1,941	--
Mall 205, Portland, OR	--	1,228	6,140	7,003	--
Plaza 205, Portland, OR	--	--	1,677	2,881	--
Valley, Yakima, WA	--	--	8,731	3,006	--
	--	1,633	19,464	14,831	--
<b>Southwestern</b>					
Alexandria, Alexandra, LA	21,223	8,097	23,112	472	--
Brazos, Lake Jackson, TX	15,573	4,877	19,506	1,555	--
Killeen, Killeen, TX	28,002	6,453	34,865	1,307	--
Mesilla Valley, Las Cruces, NM	24,367	9,126	30,630	435	--
Park Plaza, Little Rock, AR	37,091	5,816	58,037	292	--
Pecanland, Monroe, LA	38,711	8,874	36,891	697	--
Shawnee, Shawnee, OK	11,447	3,864	15,306	547	--
Villa Linda, Santa Fe, NM	24,416	5,652	37,799	527	--
	200,830	52,759	256,146	5,832	--
	263,583	70,542	372,115	129,680	--
<b>Apartments:</b>					
<b>Midwestern</b>					
Somerset Lakes, Indianapolis, IN	14,410	2,172	16,400	2,563	--
Hunter's Creek, Cincinnati, OH	2,706	1,098	4,395	292	--
Steeplechase, Cincinnati, OH	8,632	1,782	10,114	350	--
	25,748	5,052	30,909	3,205	--
<b>Southern</b>					
Briarwood, Fayetteville, NC	--	495	6,614	1,316	--
Woodfield Gardens, Charlotte, NC	--	171	3,087	675	--
Windgate Place, Charlotte, NC	--	353	4,818	1,383	--
Walden Village, Atlanta, GA	--	2,768	9,288	2,320	--
Beech Lake, Durham, NC	11,984	3,760	15,707	750	--
	11,984	7,547	39,514	6,444	--
	37,732	12,599	70,423	9,649	--

Description	Land	Building and Improvements	Total	Accumulated depreciation	Year construction completed	Date Acquired	Life
<b>Shopping Malls:</b>							
<b>Eastern</b>							
Mountaineer, Morgantown, WV	\$ 1,615	\$ 31,898	\$ 33,513	\$13,270	1975	01-29-78	40
Fingerlakes, Auburn, NY	1,331	26,636	27,967	11,063	1980	09-28-81	40
Fairgrounds Square, Reading, PA	2,369	39,990	42,359	12,908	1980	09-30-81	40
Crossroads, St. Cloud, MN	5,484	29,717	35,201	12,750	1966	01-01-72	40
Two Rivers, Clarksville, TN	--	8,771	8,771	4,195	1968	09-26-75	40
Crossroads, Ft. Dodge, IA	1,328	12,420	13,748	5,605	1967	04-22-77	40
Kandi, Willmar, MN	--	21,009	21,009	8,969	1973	03-12-79	40
Woodland Commons, Buffalo Grove, IL	6,807	15,397	22,204	1,544	1991	04-03-95	40
Westgate Towne Centre, Abilene, TX	1,616	15,284	16,900	4,074	1962	04-22-77	40
	20,550	201,122	221,672	74,378			
<b>Western</b>							
Valley North, Wenatchee, WA	1,026	4,236	5,262	2,407	1966	08-30-73	40
Mall 205, Portland, OR	1,228	13,143	14,371	6,912	1970	03-01-75	40
Plaza 205, Portland, OR	695	3,863	4,558	1,881	1970	04-26-78	40
Valley, Yakima, WA	623	11,114	11,737	4,804	1972	05-01-80	40
	3,572	32,356	35,928	16,004			
<b>Southwestern</b>							
Alexandria, Alexandra, LA	8,097	23,584	31,681	828	1973	09-01-97	40
Brazos, Lake Jackson, TX	4,877	21,061	25,938	737	1976	09-01-97	40
Killeen, Killeen, TX	6,453	36,172	42,625	1,309	1981	09-01-97	40
Mesilla Valley, Las Cruces, NM	9,126	31,065	40,191	1,067	1981	09-01-97	40
Park Plaza, Little Rock, AR	5,816	58,329	64,145	2,017	1988	09-01-97	40
Pecanland, Monroe, LA	8,961	37,501	46,462	1,300	1985	09-01-97	40
Shawnee, Shawnee, OK	3,864	15,853	19,717	537	1989	09-01-97	40
Villa Linda, Santa Fe, NM	5,652	38,326	43,978	1,319	1985	09-01-97	40
	52,846	261,891	314,737	9,114			
	76,968	495,369	572,337	99,496			
<b>Apartments:</b>							
<b>Midwestern</b>							
Somerset Lakes, Indianapolis, IN	2,172	18,963	21,135	5,565	1975	11-10-88	40
Hunter's Creek, Cincinnati, OH	1,098	4,687	5,785	266	1980	12-11-96	40
Steeplechase, Cincinnati, OH	1,782	10,464	12,246	980	1987	06-30-95	40
	5,052	34,114	39,166	6,811			
<b>Southern</b>							
Briarwood, Fayetteville, NC	495	7,930	8,425	1,860	1968-70	06-30-91	40
Woodfield Gardens, Charlotte, NC	171	3,762	3,933	937	1974	06-30-91	40
Windgate Place, Charlotte, NC	353	6,201	6,554	1,593	1974-78	06-30-91	40
Walden Village, Atlanta, GA	2,768	11,608	14,376	2,473	1973	06-01-92	40
Beech Lake, Durham, NC	3,760	16,457	20,217	1,976	1986	08-19-94	40
	7,547	45,958	53,505	8,839			
	12,599	80,072	92,671	15,650			



**SCHEDULE III**

Description	Encumbrances	Initial cost to Registrant		Cost capitalized subsequent to acquisition	Currency revaluation of Foreign Assets
		Land	Buildings and Improvements	Land and Improvements	
<b>Office Buildings:</b>					
Midwestern					
55 Public Square, Cleveland OH	--	2,500	19,055	17,390	--
Circle Tower, Indianapolis, IN	--	270	1,609	3,040	--
	--	2,770	20,664	20,430	--
Southern					
Henry C. Beck, Shreveport, LA	--	717	3,906	5,573	--
	--	717	3,906	5,573	--
Western					
North Valley Tech Center, Denver, CO	--	--	7,666	20,726	--
Sutter Buttes Center, Marysville, CA	--	985	3,622	9,261	--
	--	985	11,288	29,987	--
	--	4,472	35,858	55,990	--
	=====	=====	=====	=====	=====
<b>Parking Facilities:</b>					
United States					
Huntington Garage, Cleveland, OH	8,201	1,600	4,407	2,120	--
West Third St. Lot, Cleveland, OH	--	2,030	--	413	--
5th and Marshall Garage, Richmond, VA	--	1,102	8,090	--	--
Long Street Garage, Columbus, OH	1,526	1,886	2,042	--	--
Madison & Wells Garage, Chicago, IL	30,000	16,266	26,918	--	--
Magic Mile Lot, Arlington, TX	--	3,011	--	--	--
Printer's Alley Garage, Nashville, TN	4,000	1,914	4,736	--	--
	43,727	27,809	46,193	2,533	--
Canada					
10th Ave, Lot, Calgary, Alberta	--	255	--	--	(27)
1009-9th Ave. Lot, Calgary, Alberta	--	655	--	--	(68)
Parkade, Edmonton, Alberta	--	656	582	--	3
103 St. Lot, Edmonton, Alberta	--	346	--	--	(36)
107th St., Edmonton, Alberta	--	83	136	--	(23)
221 9th Ave. Lot, Calgary, Alberta	--	1,529	--	--	(159)
Blanchard St., Victoria, Br.Columbia	--	226	121	--	(35)
Graham Ave. Lot, Winnipeg, Manitoba	--	1,254	--	--	(130)
Water Ave. Lot, Winnipeg, Manitoba	--	664	--	--	(69)
Young St. Lot, Winnipeg, Manitoba	--	110	--	--	(12)
Broadway Lot, Winnipeg, Manitoba	--	464	--	--	(49)
Donald St. Lot, Winnipeg, Manitoba	--	117	--	--	(4)
Broad St. Lot, Regina, Saskatchewan	--	33	--	--	2
Queens Quay, Toronto, Ontario	--	404	942	--	(140)
351 Smith St., Winnipeg, Manitoba	--	863	--	--	(63)
	--	7,659	1,781	--	(810)
	43,727	35,468	47,974	2,533	(810)
	=====	=====	=====	=====	=====
<b>Other:</b>					
Write-down on carrying value of real estate assets	--	--	--	--	--
Real Estate net carrying value at December 31, 1998	\$345,042	\$123,081	\$526,370	\$197,852	\$ (810)
	=====	=====	=====	=====	=====

Aggregate cost for federal tax purposes is \$821,774,000.

Description	Land	Building and Improvements	Total	Accumulated depreciation	Year construction Completed	Date Acquired	Life
<b>Office Buildings:</b>							
<b>Midwestern</b>							
55 Public Square, Cleveland OH	5,822	33,123	38,945	23,716	1959	01-15-63	45
Circle Tower, Indianapolis, IN	270	4,649	4,919	2,554	1930	10-16-74	40
	6,092	37,772	43,864	26,270			
<b>Southern</b>							
Henry C. Beck, Shreveport, LA	717	9,479	10,196	4,418	1958	08-30-74	40
	717	9,479	10,196	4,418			
<b>Western</b>							
North Valley Tech Center, Denver, CO	--	28,392	28,392	9,667	1967	12-03-69	40
Sutter Buttes Center, Marysville, CA	948	12,920	13,868	5,398	1972	12-19-79	40
	948	41,312	42,260	15,065			
	7,757	88,563	96,320	45,753			
	=====	=====	=====	=====			
<b>Parking Facilities:</b>							
<b>United States</b>							
Huntington Garage, Cleveland, OH	1,600	6,527	8,127	3,027	1969	12-31-75	40
West Third St. Lot, Cleveland, OH	2,286	157	2,443	268	--	09-19-77	10
5th and Marshall Garage, Richmond, VA	1,102	8,090	9,192	202	--	02-24-98	40
Long Street Garage, Columbus, OH	1,886	2,042	3,928	68	--	01-15-98	30
Madison & Wells Garage, Chicago, IL	16,266	26,918	43,184	673	1998	01-26-98	40
Magic Mile Lot, Arlington, TX	3,011	--	3,011	54	1997	03-26-98	10
Printer's Alley Garage, Nashville, TN	1,914	4,736	6,650	94	--	07-01-98	25
	28,065	48,470	76,535	4,386			
<b>Canada</b>							
10th Ave, Lot, Calgary, Alberta	228	--	228	--	--	05-05-97	
1009-9th Ave. Lot, Calgary, Alberta	587	--	587	--	--	05-05-97	
Parkade, Edmonton, Alberta	588	653	1,241	27	1958	05-05-97	40
103 St. Lot, Edmonton, Alberta	310	--	310	--	--	05-05-97	
107th St., Edmonton, Alberta	74	122	196	5	1973	05-05-97	40
221 9th Ave. Lot, Calgary, Alberta	1,370	--	1,370	--	--	05-05-97	
Blanchard St., Victoria, Br.Columbia	202	110	312	5	1982	05-05-97	40
Graham Ave. Lot, Winnipeg, Manitoba	1,124	--	1,124	--	--	05-05-97	
Water Ave. Lot, Winnipeg, Manitoba	595	--	595	--	--	05-05-97	
Young St. Lot, Winnipeg, Manitoba	98	--	98	--	--	05-05-97	
Broadway Lot, Winnipeg, Manitoba	415	--	415	--	--	05-05-97	
Donald St. Lot, Winnipeg, Manitoba	113	--	113	--	--	05-05-97	
Broad St. Lot, Regina, Saskatchewan	35	--	35	--	--	05-05-97	
Queens Quay, Toronto, Ontario	362	844	1,206	35	1950	05-05-97	
351 Smith St., Winnipeg, Manitoba	800	--	800	--	--	05-05-97	
	6,901	1,729	8,630	72			
	34,966	50,199	85,165	4,458			
	=====	=====	=====	=====			
<b>Other:</b>							
Write-down on carrying value of real estate assets	(1,950)	(37,684)	(39,634)	--			
Real Estate net carrying value at December 31, 1998	\$130,340	\$676,519	\$806,859	\$165,357			
	=====	=====	=====	=====			

Aggregate cost for federal tax purposes is \$821,774,000.

**Schedule III**

- Continued

The following is a reconciliation of real estate assets and accumulated depreciation for the years ended December 31, 1998, 1997 and 1996:

	( IN THOUSANDS )		
	YEARS ENDED DECEMBER 31,		
	1998	Restated 1997	Restated 1996
	-----	-----	-----
Asset reconciliation:			
Balance, beginning of period	\$756,308	\$459,084	\$449,560
Additions during the period:			
Property acquisitions	69,551	318,345	5,491
Improvements	21,515	20,258	19,148
Equipment and appliances	1,588	1,396	1,116
Capital lease obligation	133	---	---
Reduction in reserve on carrying value of real estate assets	---	3,855	5,575
Deductions during the period:			
Sales of real estate	(4,878)	(45,632)	(20,385)
Reserve on carrying value of real estate assets	(36,000)	---	---
Prior period adjustment of reserve balance(1)			(479)
Currency revaluation of foreign real estate	(810)	---	---
Other - write-off of assets and certain fully depreciated tenant alterations	(548)	( 998)	( 942)
	-----	-----	-----
Balance, end of period	\$806,859 =====	\$756,308 =====	\$459,084 =====
Accumulated depreciation reconciliation:			
Balance, beginning of period	\$142,082	\$139,614	\$107,701
Prior period adjustment(1)			24,379
Additions during the period:			
Depreciation	23,761	17,301	14,808
Deductions during the period:			
Sales of real estate	---	(14,480)	(6,332)
Write-off of assets and certain fully depreciated tenant alterations	(486)	( 353)	( 942)
	-----	-----	-----
Balance, end of period	\$165,357 =====	\$142,082 =====	\$139,614 =====

(1) The registrant reduced the asset lives used to calculate depreciation expense and accumulated depreciation in 1998 and for the five years then ended and restated accumulated depreciation and reserves required for sold properties. The adjustment for the periods prior to 1996 is \$24,379,000 and adjustment to reserves for property losses prior to 1996 is \$479,000.

**SCHEDULE IV**

MORTGAGE LOANS ON REAL ESTATE

AS OF DECEMBER 31, 1998

(IN THOUSANDS, EXCEPT FOR PAYMENT TERMS AND FOOTNOTES)

Description	Current effective rate on net Investment	Final maturity Date	Periodic Payment Terms
Second Mortgage Loan: Secured by apartment complex in Dayton, OH	8.75%	12-1-02	Interest calculated at stated rate of 8.75% with installments of principal and interest payable monthly through maturity; prepayment without penalty subject to certain conditions.
Note Receivable: Secured by management contract on apartment complex in Atlanta, GA	10%	3-1-08	Interest calculated at stated rate of 10% with installments of principal and interest payable monthly through maturity; prepayment without penalty subject to certain conditions.
Note Receivable: Secured by Temple Mall Company	6%	10-19-23	Monthly interest on principal at LIBOR plus .375%, principal due at maturity, no prepayment penalty.
			Totals, December 31, 1998

Description	Face amount of Mortgage	Carrying amount of Mortgage
Second Mortgage Loan: Secured by apartment complex in Dayton, OH	\$2,600	\$2,581
Note Receivable: Secured by management contract on apartment complex in Atlanta, GA	1,800	1,727
Note Receivable: Secured by Temple Mall Company	1,200	1,200
	\$ 5,600 =====	\$ 5,508 (A) =====

(A) Aggregate cost for federal tax purposes is the carrying amount of the mortgages.

Schedule IV

- Continued

The following is a reconciliation of the carrying amounts of the mortgage loans outstanding for the years ended December 31, 1998, 1997 and 1996:

	( IN THOUSANDS )		
	YEARS ENDED DECEMBER 31,		
	1998	1997	1996
	-----	-----	-----
Balance, beginning of period	\$30,686	\$42,266	\$42,042
Additions during the period:			
-----			
Mortgage loan on mall in Fairmount, WV secured by the mall and partnership units of Crown American Properties, L.P.			
Second mortgage loan on apartment complex in Dayton, OH		2,600	
Note receivable on apartment complex in Atlanta, GA		1,800	
Note receivable on Temple Mall Company		1,200	
Deferred interest on:			
Wraparound mortgage on garden apartments in Atlanta, GA		48	332
Mortgage on mall in Fairmount, WV	6	74	68
Deductions during the period:			
-----			
Payoff of wraparound mortgage loan on garden apartments in Atlanta, GA		(17,086)	
Payoff of mortgage loan on Mall In Fairmount, WV	(6,206)		
Payoff of first mortgage loan on office building in Cleveland, OH	(18,839)		
Collection of principal	(139)	(216)	(176)
	-----	-----	-----
Balance, end of period	\$ 5,508	\$30,686	\$42,266
	=====	=====	=====

## EXHIBIT INDEX

EXHIBIT NUMBER -----	DESCRIPTION -----	INCORPORATED HEREIN BY REFERENCE TO -----	PAGE ----
(3)(a)	Declaration of Trust of Registrant dated August 1, 1961, as amended through July 25, 1986	Registration Statement on Form S-3 No. 33-4493	----
(3)(b)	By-laws of Registrant, as amended	Registration Statement on Form S-3 No. 33-4493	----
(3)(c)	By-laws of Registrant, as amended	March 31, 1997 Form 10-Q	----
(3)(d)	By-laws of Registrant as amended	1998 10-K	X ----
(4)(a)	Form of certificate for Shares of Beneficial Interest	Registration Statement on Form S-3 No. 33-2818	----
(4)(b)	Form of Indenture governing Debt Securities, dated February 1, 1983 between Registrant and Ameritrust Company	Registration Statement on Form S-3 No. 2-81605	----
(4)(c)	Form of Debt Security	Registration Statement on Form S-3 No. 33-4493	----
(4)(d)	Form of Indenture governing Debt Securities, dated October 1, 1993 between Registrant and Society National Bank	Registration Statement on Form S-3 No. 33-68002	----
(4)(e)	Form of Note	Registration Statement on Form S-3 No. 33-68002	----
(4)(f)	Form of Indenture governing Debt Securities	Registration Statement on Form S-3 No. 333-00953	----
(4)(g)	Rights Agreement between Registrant and National City Bank dated March 7, 1990	Form 8-A dated March 30, 1990 No. 0-18411	----
(4)(h)	Certificate of Designations relating to Registrant's Series A Cumulative Redeemable Preferred Shares of Beneficial Interest	Form 8-K dated October 24, 1996	
(4)(i)	Standby Purchase Agreement between Registrant and Gotham Partners, L.P. dated August 11, 1998	Schedule 13D dated August 11, 1998	
(4)(j)	Standby Purchase Agreement between Registrant and Gotham Partners III, L.P. dated August 11, 1998	Schedule 13D dated August 11, 1998	

EXHIBIT NUMBER -----	DESCRIPTION -----	INCORPORATED HEREIN BY REFERENCE TO -----	PAGE -----
(4)(k)	Standby Purchase Agreement between Registrant and Elliott Associates, L.P. dated August 11, 1998	Schedule 13D dated August 11, 1998	----
(4)(l)	Warrant to purchase 500,000 shares of Beneficial Interest of Registrant	1999 Form 10-K	X ----
(10)(a)	Share Purchase Agreement dated as of December 31, 1983 between registrant and First Union Management, Inc.	Registration Statement No. 2-88719	----
(10)(b)	First Amendment to Share Purchase Agreement dated as of December 10, 1985 between registrant and First Union Management, Inc.	Registration Statement No. 33-2818	----
(10)(c)	Second Amendment to Share Purchase Agreement dated as of December 9, 1986 between registrant and First Union Management, Inc.	Registration Statement No. 33-11524	----
(10)(d)	Third Amendment to Share Purchase Agreement dated as of December 2, 1987 between registrant and First Union Management, Inc.	Registration Statement No. 33-19812	----
(10)(e)	Fourth Amendment to Share Purchase Agreement dated as of December 7, 1988 between registrant and First Union Management, Inc.	Registration Statement No. 33-26758	----
(10)(f)	Fifth Amendment to Share Purchase Agreement dated as of November 29, 1989 between registrant and First Union Management, Inc.	Registration Statement No. 33-33279	----
(10)(g)	Sixth Amendment to Share Purchase Agreement dated as of November 28, 1990 between registrant and First Union Management, Inc.	Registration Statement No. 33-38754	----
(10)(h)	Seventh Amendment to Share Purchase Agreement dated as of November 27, 1991 between registrant and First Union Management, Inc.	Registration Statement No. 33-45355	----
(10)(i)	Eighth Amendment to Share Purchase Agreement dated as of November 30, 1992 between registrant and First Union Management, Inc.	Registration Statement No. 33-57756	----
(10)(j)	Employment and Consulting Agreement with Donald S. Schofield dated September 1, 1991	1991 Form 10-K	----



EXHIBIT NUMBER -----	DESCRIPTION -----	INCORPORATED HEREIN BY REFERENCE TO -----	PAGE -----
(10)(k)	Employment Agreement with James C. Mastandrea dated July 13, 1994	June 30, 1994 Form 10-Q	----
(10)(l)	Employment Agreement with Gregory D. Bruhn dated July 13, 1994	June 30, 1994 Form 10-Q	----
(10)(m)	Credit Agreement with National City Bank dated December 5, 1994	1994 Form 10-K	----
(10)(n)	Credit Agreement with Society National Bank dated March 4, 1996	1995 Form 10-K	----
(10)(o)	1981 Employee Share Option Plan	1992 Proxy Statement	----
(10)(p)	1994 Long Term Incentive Performance Plan	1994 Proxy Statement	----
(10)(q)	Bank Credit Agreement dated September 30, 1996	September 30, 1996 Form 10-Q	----
(10)(r)	Credit agreement between Imperial Parking Limited and BT Bank of Canada	March 31, 1997 Form 10-Q	----
(10)(s)	Put agreement entered into between BT Bank of Canada, Hong Kong Bank of Canada and First Union Real Estate Equity and Mortgage Investment	March 31, 1997 Form 10-Q	----
(10)(t)	Share Purchase Agreement and amendments Impark Investments Inc. and First Union Real Estate Equity and Mortgage Investments	March 31, 1997 Form 10-Q	----
(10)(u)	Put agreement entered into between Empark Investments Inc., the Onex Associates and First Union Real Estate Equity and Mortgage Investments	March 31, 1997 Form 10-Q	----
(10)(v)	Senior subordinated note by 3357392 Canada Inc. to 3006302 Nova Scotia Company	March 31, 1997 Form 10-Q	----
(10)(w)	Senior subordinated note by 504463 N.B. Inc. to 3006302 Nova Scotia Company	March 31, 1997 Form 10-Q	----
(10)(x)	Shareholders Agreement dated April 17, 1997 between 3357392 Canada, Inc. and 3355489 Canada, Inc. and the individuals and trusts listed on Schedule A.	March 31, 1997 Form 10-Q	----

EXHIBIT NUMBER -----	DESCRIPTION -----	INCORPORATED HEREIN BY REFERENCE TO -----	PAGE -----
(10)(y)	Shareholders Agreement dated April 17, 1997 between 504308 N.B., Inc. First Union Management, Inc. and the individuals listed on Schedule A.	March 31, 1997 Form 10-Q	-----
(10)(z)	Assignment dated March 27, 1997 between First Union Real Estate Equity and Mortgage Investments and First Union Management, Inc.	March 31, 1997 Form 10-Q	-----
(10)(aa)	Assignment dated April 16, 1997 between First Union Management, Inc. and 335489 Canada, Inc.	March 31, 1997 Form 10-Q	-----
(10)(ab)	Assignment dated April 16, 1997 between 335489 Canada, Inc. and 3357392 Canada, Inc.	March 31, 1997 Form 10-Q	-----
(10)(ac)	Amendment to assignment made May 8, 1997 between First Union Real Estate Equity and Mortgage Investments and Imperial Parking Limited.	March 31, 1997 Form 10-Q	-----
(10)(ad)	Bank credit agreement dated December 5, 1997	1997 10-K	-----
(10)(ae)	First amendment to employment agreement of James C. Mastandrea	1997 10-K	-----
(10)(af)	Form of change in control agreement	1997 10-K/A	-----
(10)(ag)	Fixed Rate Loan Agreement dated as of August 11, 1998 by and among the Registrant, as borrower, Bankers Trust Company, as agent, and Wellsford Capital and BankBoston, N.A., as lenders	Registration Statement on Form S-3 No. 333-63547	-----
(10)(ah)	Fixed Rate Loan Agreement dated as of August 11, 1998 by and among the Registrant, as borrower, Bankers Trust Company, as agent, and Gotham Partners, L.P., Gotham Partners III, L.P., Elliott Associates, L.P. and Blackacre Bridge Capital, L.L.C., as lenders	Registration Statement on Form S-3 No. 333-63547	-----
(10)(ai)	Employment contract for Daniel P. Friedman.	1998 10-K	X -----
(10)(aj)	Employment contract for Anne N. Zahner	1998 10-K	X -----
(10)(ak)	Employment contract for David Schonberger	1998 10-K	X -----

EXHIBIT  
NUMBER  
-----  
(10)(a1)

DESCRIPTION  
-----

INCORPORATED HEREIN BY  
REFERENCE TO  
-----

PAGE  
-----  
----

Amendment No. 2, dated as January 8, 1999, to Amended and Restated Credit Agreement, dated as of November 1, 1997, among First Union Real Estate Equity and Mortgage Investments, as Borrower, First Union Management, Inc., and National City Bank, Bankers Trust Company, Key Bank National Associates, The Huntington National Bank, Mellon Bank, N.A. and First Merit Bank, as Lenders.

Form 8-K dated February 2, 1999.

First Amendment to Fixed Rate Loan Agreement between First Union Real Estate Equity and Mortgage Investments, as Borrower; and Blackacre Bridge Capital, L.L.C., Gotham Partners, L.P., Gotham Partners III, L.P. and Elliott Associates, L.P., as Lenders, dated January 8, 1999.

Letter Agreement between First Union Real Estate Equity and Mortgage Investments, as Borrower; and Blackacre Bridge Capital, L.L.C. Gotham Partners, L.P., Gotham Partners III, L.P. and Elliott Associates, L.P., as Lenders, dated January 8, 1999

First Amendment to Fixed Rate Loan Agreement between First Union Real Estate Equity and Mortgage Investments, as Borrower; and BankBoston, N.A., Wellsford Capital and Bankers Trust Company, as Lenders, dated January 8, 1999.

Letter Agreement between First Union Real Estate Equity and Mortgage Investments, as Borrower; and BankBoston, N.A., Wellsford Capital and Bankers Trust Company, as Lenders, dated January 8, 1999.

EXHIBIT INDEX

-----

EXHIBIT NUMBER -----	DESCRIPTION -----	INCORPORATED HEREIN BY REFERENCE TO -----	PAGE -----
	Second Amendment, dated as of December 30, 1998, to the Amended and Restated Credit Agreement Dated as of April 17, 1997 between Imperial Parking Limited, as Borrower, Impark Services Limited, as Guarantor, and HongKong Bank of Canada and BT Bank of Canada, as Lenders.		
(12)	Statements of Ratios of Combined Income from Operations and Combined Net Income to Fixed Charges		X ----
(13)	1998 Annual Report		X ----
(23)	Consent of Independent Public Accountants		X ----
(24)	Powers of Attorney		X ----
(27)	Financial Data Schedule		X ----

**Exhibit 3d.**

**FIRST UNION REAL ESTATE EQUITY AND MORTGAGE  
INVESTMENTS**

**BY-LAWS**

**AS AMENDED THROUGH  
FEBRUARY 9, 1999**

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**ARTICLE I**  
**MEETINGS OF BENEFICIARIES.**  
**SECTION 1. ANNUAL MEETING.**

The annual meeting of the Beneficiaries of the Trust for the transacting of such business as shall be specified in the notice of the meeting shall be held as provided in the Declaration of Trust.

**SECTION 2. SPECIAL MEETINGS.**

Special meetings may be called at any time as provided in the Declaration of Trust.

**SECTION 3. PLACE OF MEETING.**

All meetings of the Beneficiaries shall be held at the office of the Trust, or at such other place within or without the State of Ohio as may be designated, in the case of an annual meeting, by the Trustees, or, in the case of a special meeting, by the Trustees calling such meeting or by the person or persons requesting such meeting pursuant to the Declaration of Trust.

**SECTION 4. NOTICE OF MEETINGS.**

Written notice of each annual or special meeting of the Beneficiaries, stating the time, place and purpose thereof shall be given in accordance with the Declaration of Trust.

**SECTION 5. PROCEDURE AT MEETINGS.**

At each meeting of the Beneficiaries, the Trustees shall appoint one of their number or one of the Beneficiaries to preside thereat. The Trustees shall appoint a Secretary for each such meeting, who shall be duly sworn to the faithful discharge of his duties and to keep the minutes of such meeting, which minutes shall be signed and attested by him and filed with the records of the Trust.

**SECTION 6. QUORUM.**

A majority of the outstanding shares of the Trust present in person or by proxy shall constitute a quorum for any annual or special meeting of Beneficiaries.

**SECTION 7. NOMINATIONS AND BENEFICIARY BUSINESS.**

(a) With respect to any Annual or Special Meeting of Beneficiaries, (a "Meeting") nominations for election to the Board of Trustees and the proposal of matters to be considered by the Beneficiaries may be made only (i) by or at the direction of the Board of Trustees or (ii) by any Beneficiary who was a Beneficiary of record at the record date for the Meeting, as defined in the Declaration of Trust,

who is entitled to vote at the Meeting and who complied with the notice procedures set forth in this Section 7.

(b) For a nomination or proposal to be properly brought before a Meeting by a Beneficiary, other than a shareholder proposal included in the Trust's proxy statement pursuant to Rule 14a-8 of the Securities Exchange Act of 1934, as amended, the Beneficiary must have given timely notice thereof in writing to the Secretary of the Trust, and such Beneficiary or his representative must be present in person at the Meeting. A Beneficiary's notice shall be timely if delivered to, or mailed and received at, the principal executive offices of the Trust (i) for an Annual Meeting not less than 120 days prior to the anniversary date of the immediately preceding Annual Meeting of Beneficiaries, or Special Meeting held in lieu thereof and (ii) for a Special Meeting, not less than 120 days prior to the date requested for such meeting.

(c) A Beneficiary's notice to the Secretary shall set forth as to each nomination or proposal the Beneficiary intends to bring before the Meeting (i) as to any nomination, the name and address of any proposed nominee, the nominee's business affiliation, the information required as to nominees by Item 401 of Regulation S-K under the Securities Act of 1933 and the Securities Exchange Act of 1934, all as may be amended from time to time, a certification of the proponent that such nominee meets all the qualifications for Trustees set forth in the Declaration of Trust, including, but not limited to, Section 8.10 thereof and the written consent of such nominee to serve as Trustee if elected, (ii) as to any proposal, a brief description of the proposal desired to be brought before the Meeting, (iii) the name and address of the Beneficiary offering such nomination or proposal, (iv) the class and number of shares of the Trust's capital shares which are beneficially owned by the Beneficiary, and (v) any financial interest of the Beneficiary in such proposal. Nothing contained in this Subsection (c) shall be deemed to supersede the provisions of Section 7.2 of the Declaration of Trust relating to business that may be transacted at a Special Meeting.

## **ARTICLE II**

### **SECTION 1. REGULAR MEETINGS.**

Regular meetings of the Trustees may be held at such times and places within or without the State of Ohio as may be provided for in resolution adopted by the Trustees.

### **SECTION 2. SPECIAL MEETINGS.**

Special meetings of the Trustees may be held at any time or place within or without the State of Ohio upon call of the Chairman of the Board or any two of the Trustees at the time and place designated in the notice of meeting.

### **SECTION 3. NOTICE OF AND PARTICIPATION IN MEETINGS.**

Notice of each meeting, regular or special, shall be given by mailing or by sending to each Trustee (addressed to the address last furnished to the Trust by the Trustee) a letter at least 4 days before the



meeting, or a facsimile transmittal at least 24 hours before the meeting. Notice of any special or regular meeting, as provided in the Declaration of Trust, may be waived in writing or by facsimile transmittal by any Trustee either before or after such meeting, and such notice shall be deemed to have been waived by the Trustees attending such meeting. Except as provided in Article VI hereof, unless otherwise indicated in the notice thereof, any business may be transacted at any regular or special meeting. Meetings of the Trustees may be held through any communications equipment if all persons participating can hear each other and participation in a meeting pursuant to this sentence shall constitute presence at such meeting.

#### SECTION 4. QUORUM.

At any meeting a majority of the Trustees then in office shall constitute a quorum.

#### SECTION 5. COMPENSATION OF TRUSTEES.

The Trustees are authorized to fix a reasonable retainer for members of the Board of Trustees and the Chairman and a reasonable fee for attendance at meetings. In addition to such compensation there shall be reimbursement for expenses for traveling to and from such meetings.

#### SECTION 6. COMMITTEES OF THE BOARD OF TRUSTEES.

The Trustee may elect from their members committees of the Board and give them any or all powers of the Trustees during intervals between the meetings of the Trustees, except that such committees shall not be empowered to declare dividends or fill vacancies in the Board of Trustees or committees. All actions of such committees shall be reported to the Trustees at their next meeting.

#### SECTION 7. QUALIFICATIONS OF NOMINEES - AGE.

No nominee for Trustee shall be more than 72 years of age at the time of his election as Trustee, nor shall any Trustee nominated for a subsequent term be more than 72 years of age at the time of his election for such subsequent term, provided that any Trustee elected prior to attaining age 72 may continue to serve the remainder of his term despite attaining the age of 72 before the expiration of his term.

### **ARTICLE III OFFICERS**

#### SECTION 1. DESIGNATION OF OFFICERS.

The Trustees shall elect a Chairman of the Board, a President, a Secretary, a Treasurer, and such Vice Presidents and other officers, or assistant officers, as they shall deem advisable. Each officer and assistant officer shall have such functions and duties as the Trustees shall from time to time designate, and, in the absence of such designation, such duties as are usually associated with such office. Except as otherwise determined by the Trustees, any two or more offices may be held by the same person.

**SECTION 2. TENURE OF OFFICE.**

The officers of the Trust shall hold office at the pleasure of the Trustees, and until successors are chosen and qualified. A vacancy in any office, however created, may be filled by election by the Trustees.

**SECTION 3. DELEGATION OF DUTIES.**

The Trustees may delegate the duties of any officer to any other officer and generally may control the action of the officers and require the performance of duties in addition to those mentioned herein.

**SECTION 4. COMPENSATION.**

The Trustees are authorized to determine or to provide the method of determining the compensation of officers.

**SECTION 5. SIGNING CHECKS AND OTHER INSTRUMENTS.**

The Trustees shall determine or provide the method of determining how checks, notes, bills of exchange and similar instruments issued by or on behalf of the Trust shall be signed, countersigned, or endorsed.

**SECTION 6. CONTROL BY TRUSTEES.**

Nothing contained herein shall be interpreted to relieve the Trustees, in any manner, of their duty to control and manage the Trust property.

**ARTICLE IV  
SHARES IN TRUST**

**SECTION 1. ISSUE OF CERTIFICATE OF BENEFICIAL OWNERSHIP.**

The Chairman shall cause to be issued to each Beneficiary one or more certificates, under the seal of the Trust, signed as provided in Article III,

Section 5 hereof, certifying the number of shares owned by such Beneficiary in the Trust. Such certificates shall be countersigned by the Transfer Agent and registered by the Registrar and shall be transferable on the books of the Trust as provided in the Declaration of Trust.

**ARTICLE V  
AMENDMENTS.**

**SECTION 1. AMENDMENT OF BY-LAWS.**

The Trustees, by the affirmative vote of a majority, may at any meeting, provided the substance of the proposed amendment shall have been stated in a notice of the meeting, alter, change, or amend

in any respect, or supersede by new by-laws, in whole or in part, any of these by-laws.

**ARTICLE VI  
MISCELLANEOUS PROVISIONS.**

**SECTION 1. FISCAL YEAR.**

The fiscal year of the Trust shall be as determined from time to time by the Trustees.

**SECTION 2. NOTICE AND WAIVER OF NOTICE.**

Whenever any notice is required by these by-laws to be given, personal notice is not required unless expressly so stated; and any notice so required shall be deemed to be sufficient if given (i) by letter, by depositing the same in a post-office box in a sealed post-paid wrapper, addressed to the person entitled thereto (at his last known post-office address as shown by the register of the Trust) and such notice shall be deemed to have been given on the day of such mailing; or (ii) by facsimile transmittal if transmitted via facsimile with evidence of receipt by the sender, and such notice shall be deemed to have been given on the day of such facsimile transmittal.

**SECTION 3. CHECKS FOR MONEY.**

All checks, drafts or orders for the payment of money shall be signed by the Treasurer or Assistant Treasurer or by such other officer, officers, Trustee or Trustees as the Trustees may from time to time designate.

**SECTION 4. FORM OF CERTIFICATE OF BENEFICIAL INTEREST.**

The form of certificate of beneficial interest representing shares of \$1 par value shall be substantially as follows:

No. \_\_\_\_\_ Shares

**FIRST UNION  
Real Estate Equity and Mortgage Investments**

THIS CERTIFIES THAT \_\_\_\_\_ is the registered holder of \_\_\_\_\_ Fully Paid and Non-assessable Share of Beneficial Interest, \$1 Par Value. in

**FIRST UNION  
Real Estate Equity and Mortgage Investments**

a Trust established in business trust from under the laws of the State of Ohio under a Declaration of Trust dated as of August 1, 1961, as amended from time to time, a copy of which is on file with the Transfer Agents of the Trust by all the terms and provisions of which the holder or

transferee hereof by accepting this certificate agrees to be bound. The Trust is not a bank or trust company and does not and will not solicit, receive or accept deposits as a business. The shares represented hereby are transferable on the records of the Trust only by the registered holder hereof or by his agent duly authorized in writing on delivery to a Transfer Agent of the Trust of this certificate properly endorsed or accompanied by duly executed instrument of transfer together with such evidence of the genuineness thereof and such other matters as may reasonably be required. The transferability of the shares represented hereby is subject to such regulation, as may from time to time be adopted by the Trustees of the Trust and set forth in the By-Laws to which reference is hereby made to prevent transfers of shares which would result in disqualification of the Trust for taxation as a real estate investment trust under the Internal Revenue Code as amended.

This certificate is not valid unless countersigned by a Transfer Agent and registered by a Registrar of the Trust.

IN WITNESS WHEREOF, the Trustees of this Trust have caused this certificate to be signed by facsimile signatures.

**[ON REVERSE SIDE]**

The By-Laws of the Trust provide, among other things, that no person may acquire Trust securities (including these securities) if, thereafter, he would beneficially own more than 9.8% of the Trust's shares of beneficial interest. In applying this restriction, convertible securities of the Trust beneficially owned by such person (including convertible securities) are to be treated as if already converted into shares of beneficial interest. A copy of the By-Laws and information about the limitation on ownership may be obtained from the Secretary of the Trust.

**Section 5. Regulations on Transfer of Shares to Prevent Disqualification of the Trust Under the Internal Revenue Code**

**Notification of the Trust Under the Internal Revenue Code.**

The Chief Executive Officer of the Trust or an officer designated by him shall:

(a) From time to time cause to be prepared a list of holders of record (with their holdings) of shares of the Trust (preferred and common) and shall designate those holders which the officer acting shall have reason to believe are not also the beneficial owners of the holdings of record in their respective names;

(b) Review the list with counsel and impose such restrictions on transfer of shares as counsel shall advise should be imposed to prevent disqualification of the Trust as a Real Estate Investment Trust under Section 856 et seq. of the Internal Revenue Code.

Section 6. Restrictions on Issuance and Transfer of Securities.

(a) No person may own more than 9.8% of the outstanding Shares (the Limit), and no Securities shall be issued or transferred to any person if, following such issuance or transfer, such person's ownership of Shares would exceed the Limit. For purposes of computing the Limit, Convertible Securities owned by such person shall be treated as if the Convertible Securities owned by such person had been converted into Shares.

(b) If any Securities in excess of the Limit are issued or transferred to any person in violation of Paragraph a) hereof (the "Excess Securities"), such issuance or transfer shall be valid only with respect to such amount of Securities as does not result in a violation of Paragraph a) hereof, and such issuance or transfer shall be null and void with respect to such Excess Securities.

If the last clause of the foregoing sentence is determined to be invalid by virtue of any legal decision, statute, rule or regulation, such person shall be conclusively deemed to have acted as an agent on behalf of the Trust in acquiring the Excess Securities and to hold such Excess Securities on behalf of the Trust. As the equivalent of treasury Securities for such purposes, the Excess Securities shall not be entitled to any voting rights; shall not be considered to be outstanding for quorums or voting purposes; and shall not be entitled to receive dividends, interest or any other distribution with respect to the Securities. Any person who receives dividends, interest or any other distribution in respect to Excess Securities shall hold the same as agent for the Trust and (following a permitted transfer) for the transferee thereof.

Notwithstanding the foregoing, any holder of Excess Securities may transfer the same (together with any distributions thereon) to any person who, following such transfer, would not own Shares (within the meaning of Paragraph (a)) in excess of the Limit. Upon such permitted transfer, the Trust shall pay or distribute to the transferee any distributions on the Excess Securities not previously paid or distributed.

(c) Ownership of Securities is conditional upon the owner or prospective owner having provided to the Trust definitive written information respecting his ownership of Securities. Failure to provide such information, upon reasonable request shall result in the Securities so owned being treated as Excess Securities pursuant to Paragraph b) for so long as such failure continues.

(d) For purposes of this Section 6:

(i) Person. includes an individual, corporation, partnership, association, joint stock company, trust, unincorporated association or other entity.

(ii) Shares. means Shares of Beneficial Interest, par value \$1 per share.

(iii) Convertible Securities. means any securities of the Trust that are convertible into Shares.

(iv) Securities. means Shares and Convertible Securities.

(v) Ownership. means beneficial ownership. Beneficial ownership, for this purpose, may be determined on the basis of the beneficial ownership rules applicable under the Securities Exchange Act of 1934, as amended, or such other basis as management reasonably determines to be appropriate to effectuate the purposes hereof.

(e) Nothing herein contained shall limit the ability of the Trust to impose, or to seek judicial or other imposition of additional restrictions if deemed necessary or advisable to protect the Trust and the interests of its security holders by preservation of the Trust's status as a qualified real estate investment trust under the Code.

(f) These restrictions on issuance and transfer of Securities shall be applied only on a prospective basis. Accordingly, Paragraphs (a) and (b) hereof shall not apply to Shares in excess of the limit that were owned (within the meaning of Paragraph (a) by any person at the close of business on June 3, 1981, but Paragraph (a) and (b) shall prospectively apply to the transfer of such Shares and to further acquisitions of Securities by any such person. Similarly, Paragraphs (a) and (b) shall not apply to the conversion of Convertible Securities that were owned by any person at the close of business on such date or to the resultant Shares owned by such person, but Paragraph (a) and (b) shall prospectively apply to such Shares and to such person.

(g) Notwithstanding any other provision of this Section 6, a lower percentage (the Temporary Limit) shall operate in place of the 9.8% ownership Limit set forth in Paragraph (a) hereof for so long as there are outstanding Securities excepted from the restrictions of this Section 6 pursuant to Paragraph (f) hereof ("Exempt Securities"). The Temporary Limit shall initially be 6%, but upon the transfer of Exempt Securities the Temporary Limit shall be fixed by the Trustees from time to time but shall in no event exceed an amount equal to 25% of the difference between (i) 49% of the Shares outstanding and (ii) the number of Shares owned by any person who owns Exempt Securities. For purposes of this calculation, Convertible Securities owned by such person shall be treated as if the Convertible Securities owned by such person had been converted into Shares.

(h) If any provision of this Section 6 or any application of any such provision is determined to be invalid by any federal or state court having jurisdiction over the issue, the validity of the remaining provisions shall not be affected and other applications of such provision shall be affected only to the extent necessary to comply with the determination of such court.

**Exhibit 4(1)**

NEITHER THE WARRANTS REPRESENTED BY THIS CERTIFICATE NOR THE SHARES ISSUABLE UPON EXERCISE HEREOF HAVE BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED. THE SECURITIES HAVE BEEN ACQUIRED FOR INVESTMENT. NEITHER SUCH WARRANTS NOR SUCH SHARES MAY BE SOLD, TRANSFERRED OR OTHERWISE DISPOSED OF EXCEPT IN COMPLIANCE WITH SUCH ACT.

**WARRANT TO PURCHASE  
500,000 SHARES OF BENEFICIAL INTEREST,  
\$1 PAR VALUE PER SHARE,  
OF  
FIRST UNION REAL ESTATE EQUITY AND MORTGAGE INVESTMENTS**

NO. A-1

This certifies that Enterprise Asset Management, Inc. (the "Warrantholder"), is entitled to purchase from First Union Real Estate Equity and Mortgage Investments, a business trust organized under the laws of the State of Ohio (the "Trust"), subject to the terms and conditions hereof, at any time at or after 9:00 A.M., Cleveland, Ohio time, November 9, 1998 and before 5:00 P.M., Cleveland, Ohio time on the Expiration Date (as defined herein), the number of fully paid and non-assessable Common Shares of the Trust stated above at the Exercise Price (as defined herein).

**ARTICLE I**

**SECTION 1.01: DEFINITION OF TERMS.** As used in this Warrant, the following capitalized terms shall have the following respective meanings:

- (a) **COMMON SHARES:** Shares of beneficial interest, \$1 par value per share, of the Trust.
- (b) **EXERCISE PRICE:** \$10.00 per Warrant Share as such price may be adjusted from time to time pursuant to Article III hereof.
- (c) **EXPIRATION DATE:** The tenth anniversary of the Issuance Date.
- (d) **ISSUANCE DATE:** November 9, 1998.
- (e) **MERGER:** A consolidation or merger of the Trust with or into any other trust or corporation (other than a consolidation or merger in which the Trust is the surviving entity).
- (f) **PERSON:** An individual, partnership, joint venture, corporation, trust, limited liability company, unincorporated organization or government of any department or

agency thereof.

(g) WARRANT SHARES: Common Shares purchased or purchasable upon exercise of this Warrant.

## ARTICLE II

### DURATION AND EXERCISE OF WARRANT

SECTION 2.01: DURATION OF WARRANT. The Warrantholder may exercise this Warrant at any time and from time to time after 9:00 A.M., Cleveland, Ohio time, November 9, 1998, and before 5:00 P.M., Cleveland, Ohio time, on the Expiration Date. If this Warrant is not exercised on the Expiration Date, it shall expire, and all rights hereunder shall thereupon cease.

SECTION 2.02: EXERCISE OF WARRANT.

(a) The Warrantholder may exercise this Warrant, in whole or in part, by presentation and surrender of this Warrant to the Trust at its principal office or at the office of its stock transfer agent, if any, with the subscription form attached hereto as Exhibit A (the "Subscription Form") duly executed and accompanied by payment of the full Exercise Price for each Warrant Share to be purchased.

(b) Upon receipt of this Warrant with the Subscription Form fully executed and accompanied by payment of the aggregate Exercise Price for the Warrant Shares for which this Warrant is then being exercised, the Trust shall cause to be issued certificates for the total number of whole Common Shares for which this Warrant is being exercised in such denominations as are requested for delivery to the Warrantholder registered in the name of the Warrantholder, and the Trust shall thereupon deliver such certificates to the Warrantholder.

(c) In case the Warrantholder shall exercise this Warrant with respect to less than all of the Warrant Shares that may be purchased under this Warrant, the Trust shall execute a new warrant in the form of this Warrant for the balance of such Warrant Shares and deliver such new warrant to the Warrantholder.

(d) The Trust shall pay any and all stock transfer and similar taxes which may be payable in respect of the issue of any Warrant Shares to the Warrantholder.

SECTION 2.03: RESERVATION OF SHARES. The Trust hereby agrees that at all times there shall be reserved for issuance and delivery upon exercise of this Warrant such number of Common Shares from time to time issuable upon exercise of this Warrant. All such shares shall be duly authorized, and when issued upon such exercise, shall be validly issued, fully paid and nonassessable, and payment therefor, free and clear of all



liens, security interests, charges and other encumbrances and free and clear of all preemptive rights.

**SECTION 2.04: FRACTIONAL SHARES.** The Trust shall not be required to issue any fraction of a Common Share in connection with the exercise of this Warrant.

**SECTION 2.05: LISTING.** During such time as Common Shares are listed on a national securities exchange or automated quotation system, prior to the issuance of any Common Shares upon exercise of this Warrant, the Trust shall secure the listing of such Common Shares upon each national securities exchange or automated quotation system, if any, upon which Common Shares are then listed (subject to official notice of issuance upon exercise of this Warrant) and shall maintain, so long as any other Common Shares shall be so listed, such listing of all Common Shares from time to time issuable upon the exercise of this Warrant.

### **ARTICLE III**

#### **ADJUSTMENT OF COMMON SHARES PURCHASABLE AND OF EXERCISE PRICE**

The Exercise Price and the number and kind of Warrant Shares shall be subject to adjustment from time to time upon the happening of certain events as provided in this Article III.

#### **SECTION 3.01: MECHANICAL ADJUSTMENTS.**

(a) In case the Trust shall at any time or from time to time after the date hereof (i) pay any dividend, or make any distribution, on the outstanding Common Shares in Common Shares, (ii) subdivide the outstanding Common Shares, (iii) combine the outstanding Common Shares into a smaller number of shares or (iv) issue by reclassification of the Common Shares any shares of capital stock of the Trust (each of the events described in the foregoing clauses (i) through (iv) referred to as an "Adjustment Event"), then and in each such case, the Exercise Price in effect immediately prior to such Adjustment Event or the record date therefor, whichever is earlier, shall be adjusted so that the Warrantholder shall be entitled to receive the number and type of Common Shares which such Warrantholder would have owned or have been entitled to receive after the happening of any of the Adjustment Events described above, had such Warrant been converted into Common Shares immediately prior to the happening of such Adjustment Event or the record date therefor, whichever is earlier. An adjustment made pursuant to this Section 3.01(a) shall become effective (x) in the case of any such dividend or distribution, immediately after the close of business on the record date for the determination of holders of Common Shares entitled to receive such dividend or distribution, or (y) in the case of such subdivision, reclassification or combination, at the close of business on the day upon which such trust action becomes effective.

(b) If the Trust shall take a record of the holders of its Common Shares for the purpose of entitling them to receive a dividend or other distribution and shall thereafter, and before such dividend or distribution is paid or delivered to shareholders entitled thereto, legally abandon its plan to pay or deliver such dividend or distribution, then no adjustment in the Exercise Price then in effect shall be made by reason of the taking of such record, and any such adjustment previously made as a result of the taking of such record shall be reversed.

(c) In the case of a Merger or a proposed reorganization of the Trust or a proposed reclassification of the capital stock of the Trust (except a transaction for which provision for adjustment is otherwise made in this Section 3.01), the Warrant shall thereafter be exercisable into the number of shares of stock or other securities or property to which a holder of the number of Common Shares of the Trust deliverable upon exercise of such Warrant would have been entitled upon such Merger, reorganization or reclassification; and, in any such case, appropriate adjustment (as determined by the Board of Trustees) shall be made in the application of the provisions herein set forth with respect to the rights and interest thereafter of the holders of the Warrant, to the end that the provisions set forth herein (including provisions with respect to changes in and other adjustments of the applicable conversion price) shall thereafter be applicable, as nearly as reasonably may be, in relation to any shares of stock or other property thereafter deliverable upon the exercise of the Warrant. The Trust shall not effect any such Merger unless prior to or simultaneously with the consummation thereof the successor entity shall assume by written instrument the obligation to deliver to the Warrantholder such shares of stock, securities or assets as, in accordance with the foregoing provisions, each such holder is entitled to receive.

(d) Whenever the Exercise Price payable upon exercise of each Warrant is adjusted pursuant to paragraph (a) of this Section 3.01, the Warrant Shares shall simultaneously be adjusted by multiplying the number of Warrant Shares initially issuable upon exercise of each Warrant (as set forth on the front page of this Warrant) by \$10.00 and dividing the product so obtained by the Exercise Price, as adjusted.

(e) In the event that at any time, as a result of any adjustment made pursuant to Section 3.01(a), the Warrantholder thereafter shall become entitled to receive any shares of capital stock of the Trust other than Common Shares, thereafter the number of such other shares so receivable upon exercise of any Warrant shall be subject to adjustment from time to time in a manner and on terms as nearly equivalent as practicable to the provisions with respect to the Common Shares contained in Section 3.01.

**SECTION 3.02: NOTICES OF ADJUSTMENT.** Whenever the number of Warrant Shares or the Exercise Price is adjusted as herein provided, the Trust shall prepare and deliver forthwith to the Warrantholder a certificate signed by its Treasurer or an Assistant

Treasurer or the Secretary or an Assistant Secretary, setting forth the adjusted number of shares purchasable upon the exercise of this Warrant and the Exercise Price of such shares after such adjustment, setting forth a brief statement of the facts requiring such adjustment and setting forth the computation by which adjustment was made.

**SECTION 3.03: FORM OF WARRANT AFTER ADJUSTMENTS.** The form of this Warrant need not be changed because of any adjustments in the Exercise Price or the number or kind of the Warrant Shares, and Warrants theretofore or thereafter issued may continue to express the same price and number and kind of shares as are stated in this Warrant, as initially issued.

#### **ARTICLE IV**

##### **OTHER PROVISIONS RELATING TO RIGHTS OF WARRANTHOLDER**

**SECTION 4.01: NO RIGHTS AS SHAREHOLDERS.** Nothing contained in this Warrant shall be construed as conferring upon the Warrantholder the right to vote or to receive dividends or to consent or to receive notice as a shareholder in respect of any meeting of shareholders for the election of trustees of the Trust or of any other matter, or any rights whatsoever as shareholders of the Trust.

**SECTION 4.02: LOST, STOLEN, MUTILATED OR DESTROYED WARRANTS.** If this Warrant is lost, stolen, mutilated or destroyed, the Trust may, on such reasonable terms as to indemnity or otherwise as it may in its reasonable discretion impose (which shall, in the case of a mutilated Warrant, include the surrender thereof), issue a new Warrant of like denomination and tenor as, and in substitution for, this Warrant.

#### **ARTICLE V**

##### **TRANSFER OF WARRANTS**

**SECTION 5.01: TRANSFER.** Any sale, transfer or other disposition, in whole or in part, of this Warrant or any rights hereunder shall be made in accordance with and subject to the provisions of the Securities Act of 1933, as amended (the "Securities Act"), and the rules and regulations promulgated thereunder.

**SECTION 5.02: RESTRICTIVE LEGEND.** Each Warrant Share issued upon exercise of this Warrant shall bear a legend containing the following words:

"THE SECURITIES REPRESENTED BY THIS CERTIFICATE HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED. THE SECURITIES HAVE BEEN ACQUIRED FOR

**INVESTMENT AND MAY NOT BE SOLD, TRANSFERRED OR OTHERWISE DISPOSED OF  
EXCEPT IN COMPLIANCE WITH SUCH ACT."**

"IN MAKING AN INVESTMENT DECISION INVESTORS MUST RELY ON THEIR OWN EXAMINATION OF THE PERSON OR ENTITY CREATING THE SECURITIES AND THE TERMS OF THE OFFERING, INCLUDING THE MERITS AND RISKS INVOLVED. THESE SECURITIES HAVE NOT BEEN RECOMMENDED BY ANY FEDERAL OR STATE SECURITIES COMMISSION OR REGULATORY AUTHORITY. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE."

"THE BY-LAWS OF THE TRUST PROVIDE, AMONG OTHER THINGS, THAT NO PERSON MAY ACQUIRE TRUST SECURITIES (INCLUDING THESE SECURITIES) IF, THEREAFTER, HE WOULD BENEFICIALLY OWN MORE THAN 9.8% OF THE TRUST'S SHARES OF BENEFICIAL INTEREST. IN APPLYING THIS RESTRICTION, CONVERTIBLE SECURITIES OF THE TRUST BENEFICIALLY OWNED BY SUCH PERSON (INCLUDING CONVERTIBLE SECURITIES) ARE TO BE TREATED AS IF ALREADY CONVERTED INTO SHARES OF BENEFICIAL INTEREST. A COPY OF THE BY-LAWS AND INFORMATION ABOUT THE LIMIT ON OWNERSHIP MAY BE OBTAINED FROM THE SECRETARY OF THE TRUST."

The requirement that the above legend be placed upon certificates evidencing any such securities shall cease and terminate upon the earliest of the following events: (i) when such shares are transferred in an underwritten public offering, (ii) when such shares are transferred pursuant to Rule 144 under the Securities Act or (iii) when such shares are transferred in any other transaction if the seller delivers to the Trust an opinion of its counsel, which counsel and opinion shall be reasonably satisfactory to the Trust, or a "no-action" letter from the Staff of the Securities and Exchange Commission, in either case to the effect that such legend is no longer necessary in order to protect the Trust against a violation by it of the Securities Act upon any sale or other disposition of such shares without registration thereunder. Upon the occurrence of such event, the Trust, upon the surrender of certificates containing such legend, shall, at its own expense, deliver to the holder of any such securities as to which the requirement for such legend shall have terminated, one or more new certificates evidencing such securities not bearing such legend.

## **ARTICLE VI**

### **OTHER MATTERS**

**SECTION 6.01: SUCCESSORS AND ASSIGNS.** The terms and provisions of this Warrant shall bind and inure to the benefit of the Warrantholder and its permitted successors and assigns.

**SECTION 6.02: ENTIRE AGREEMENT.** This Warrant and the Exhibit hereto contain the entire agreement among the parties with respect to the subject matter hereof and supersede all prior and contemporaneous arrangements or understandings with respect thereto.

**SECTION 6.03: AMENDMENTS AND WAIVERS.** The terms and provisions of this Warrant, including the provisions of this sentence, may be modified or amended, or any of the provisions hereof waived, temporarily or permanently, pursuant to the written consent of the Trust and the Warrantholder.

**SECTION 6.04: COUNTERPARTS.** This Warrant may be executed in any number of counterparts, and each such counterpart hereof shall be deemed to be an original instrument, but all such counterparts together shall constitute but one agreement.

**SECTION 6.05: GOVERNING LAW.** This Warrant shall be governed by and construed in accordance with the laws of the State of Ohio without giving effect to the principles of conflicts of law. Each of the parties hereto hereby irrevocably and unconditionally consents to submit to the jurisdiction of the courts of the State of Ohio and of the United States of America, in each case located in the County of Cuyahoga, for any action, proceeding or investigation in any court or before any governmental authority ("Litigation") arising out of or relating to this Warrant and the transactions contemplated hereby (and agrees not to commence any Litigation relating thereto except in such courts), and further agrees that service of any process, summons, notice or document by U.S. registered mail to its respective address set forth in this Warrant shall be effective service of process for any Litigation brought against it in any such court. Each of the parties hereto hereby irrevocably and unconditionally waives any objection to the laying of venue of any Litigation arising out of this Warrant or the transactions contemplated hereby in the courts of the State of Ohio or the United States of America, in each case located in the County of Cuyahoga, and hereby further irrevocably and unconditionally waives and agrees not to plead or claim in any such court that any such Litigation brought in any such court has been brought in an inconvenient forum.

**SECTION 6.06: NOTICE.** All notices, requests, consents and other communications

hereunder to any party shall be deemed to be sufficient if contained in a written instrument delivered in person or sent by telecopy, nationally-recognized overnight courier or first class registered or certified mail, return receipt requested, postage prepaid, addressed to such party at the address set forth below or such other address as may hereafter be designated in writing by such party to the other parties:

(i) if to the Trust, to:

First Union Real Estate Equity and Mortgage Investments 55 Public Square, Suite 1900 Cleveland, Ohio 44113-1937 Telephone: (216) 781-4030 Attention: GENERAL COUNSEL

(ii) if to the Warrantholder, to:

Enterprise Asset Management, Inc. 11 East 44th Street New York, New York  
Telephone: (212) 824-1100 Attention: GENERAL COUNSEL

All such notices, requests, consents and other communications shall be deemed to have been given when received.

SECTION 6.07: SEVERABILITY. Whenever possible, each provision of this Warrant shall be interpreted in such manner as to be effective and valid, but if any provision of this Warrant is held to be invalid or unenforceable in any respect, such invalidity or unenforceability shall not render invalid or unenforceable any other provision of this Warrant.

IN WITNESS WHEREOF, this Warrant has been duly executed by the Trust under seal as of the \_\_\_th day of November, 1998.

**FIRST UNION REAL ESTATE EQUITY AND  
MORTGAGE INVESTMENTS**

By:

Name:  
Title:

Attest: \_\_\_\_\_  
Secretary

**EXHIBIT A TO WARRANT**

**FORM OF SUBSCRIPTION**

(To be executed only upon exercise of Warrant)

**FIRST UNION REAL ESTATE EQUITY AND MORTGAGE INVESTMENTS**

The undersigned registered holder of the within Warrant hereby irrevocably exercises such Warrant for, and purchases thereunder, \_\_\_\_\_ Common Shares covered by the within Warrant and requests that the certificates for such shares be issued in the name of, and delivered to the undersigned, whose address is set forth below. The undersigned herewith makes payment in full therefor of the Exercise Price therefor (or \$ \_\_\_\_\_ in the aggregate).

\_\_\_\_\_  
(Signature must conform in all respects to name of holder as specified on the face of Warrant)

\_\_\_\_\_  
(Street Address)

\_\_\_\_\_  
(City) (State) (Zip Code)

**Date**

**Exhibit 10(ai)**

**EMPLOYMENT AGREEMENT**

**FOR**

**DANIEL P. FRIEDMAN**



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## Schedules

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Existing Investments  
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## EMPLOYMENT AGREEMENT

THIS EMPLOYMENT AGREEMENT (the "AGREEMENT") is entered into as of November 2, 1998, by and between DANIEL P. FRIEDMAN, an individual residing in the State of New York ("EXECUTIVE"), and FIRST UNION REAL ESTATE EQUITY AND MORTGAGE INVESTMENTS, an Ohio business trust with offices at 55 Public Square, Suite 1900, Cleveland, Ohio 44113 (the "COMPANY").

### RECITALS

WHEREAS, the Company desires to employ Executive as President and Chief Executive Officer and Executive desires to be employed by the Company as President and Chief Executive Officer.

NOW, THEREFORE, in consideration of the premises and the mutual covenants and agreements set forth herein, the parties hereby agree as follows:

#### 1. EMPLOYMENT.

The Company hereby agrees to employ Executive, and Executive hereby agrees to accept such employment during the period and upon the terms and conditions set forth in this Agreement.

#### 2. EMPLOYMENT PERIOD.

(1) EMPLOYMENT PERIOD. Except as otherwise provided in this Agreement to the contrary, the terms and conditions of this Agreement shall be and remain in effect during the period of employment (the "EMPLOYMENT PERIOD") established under this Paragraph 2. The initial Employment Period shall be for a term commencing on the date of this Agreement and ending on the fourth anniversary of the date of this Agreement, unless earlier terminated as provided in this Agreement. Immediately following the execution hereof, the Executive shall resign from all positions as an employee, officer and director of his current employer and its affiliates.

(2) UNEXPIRED EMPLOYMENT PERIOD. If Executive's employment with the Company is terminated, for purposes of this Agreement the term "UNEXPIRED EMPLOYMENT PERIOD" shall mean the period commencing on the date of such termination and ending on the last day of the Employment Period.

### 3. SERVICES/PLACE OF EMPLOYMENT.

(1) SERVICES. During the Employment Period, Executive shall hold the position of President and Chief Executive Officer. Executive shall devote his best efforts and such business time, skill and attention exclusively to the business of the Company (other than absences due to vacation, illness, disability or approved leave of absence) as is necessary to perform such duties as are customarily performed by similar executive officers together with such other reasonable duties as may be more specifically enumerated from time to time by the Company's board of trustees ("BOARD OF TRUSTEES" or "BOARD") PROVIDED, HOWEVER, that the foregoing is not intended to preclude Executive from (i) owning and managing personal investments, including real estate investments, in accordance with Paragraph 8 hereof or (ii) engaging in charitable activities and community affairs, provided that (x) with respect to the activities referenced in clause (ii), Executive obtains the prior approval of the Board as to the amount of time Executive will devote to such activities and (y) the performance of the activities referred to in clauses (i) and (ii) of this Paragraph 3(a) does not prevent Executive from devoting sufficient business time to the Company to carry out Executive's duties as President and Chief Executive Officer.

(2) PLACE OF EMPLOYMENT. The principal place of employment of Executive shall be at the Company's executive offices in New York (Manhattan County), New York.

(3) MEMBERSHIP ON THE BOARD. During the Employment Period, the Company shall cause Executive to be nominated as a member of the management slate of the Board of Trustees and shall use its reasonable best efforts to cause you to be elected a trustee and a member of the Executive Committee (if such committee exists). The Company hereby confirms that Executive has been elected as a member of the Board with a term expiring in calendar year 2000.

### 4. Compensation and Benefits.

(1) SALARY. During the first twelve (12) months of the Employment Period, the Company shall pay Executive an annual base salary in the amount of \$340,000 payable in accordance with the Company's regular payroll practices. Executive's annual base salary shall be reviewed annually in accordance with the policy of the Company and shall be subject to upward adjustment based upon, among other things, Executive's performance, as determined in the sole discretion of the Board PROVIDED HOWEVER that the annual increase in base salary for each year of the Term shall be at least 5% over the annual base salary for the previous year

(the annual base salary as adjusted from time to time is hereinafter referred to as the "ANNUAL BASE SALARY"). In no event shall Executive's Annual Base Salary in effect at a particular time be reduced without his prior written consent.

(2) TAXES AND WITHHOLDING. The Company shall have the right to deduct and withhold from all compensation all social security and other federal, state and local taxes and charges which currently are or which hereafter may be required by law to be so deducted and withheld.

(3) ADDITIONAL BENEFITS. In addition to the other compensation payable pursuant to this Agreement, Executive shall be entitled to the following.

(1) BENEFITS. All fringe benefits and perquisites as are generally made available from time to time to all employees and/or to executives of the Company generally and to participate in any pension, profit-sharing or similar plan or program established from time to time by the Company for the benefit of its employees and/or executives generally, subject to the provisions of such plans. In any event, Executive's health insurance coverage shall commence on the date of this Agreement (or the Company shall reimburse Executive for COBRA payments until such coverage can commence).

(2) MEMBERSHIP FEES. Membership fees and costs for reasonable and customary memberships in professional organizations.

(3) EXPENSE REIMBURSEMENT. Reimbursement for reasonable business expenses incurred by Executive in furtherance of the interests of the Company, subject to the reasonable procedures established by the Company from time to time with respect to substantiation and approval.

(4) VACATION AND SICK LEAVE/PERSONAL DAYS. Such periods of paid vacation and sick leave/personal days allowance each year (not less than four (4) weeks vacation and seven (7) days of sick leave/personal days per full twelve (12) month period) that are consistent with the Company's vacation and sick leave/personal days policy for senior management.

(5) SHARE OPTIONS. GRANT. The grant upon execution of this Agreement of share options ("SHARE OPTIONS") to acquire 1,080,000 shares of the Company's common shares of beneficial interest ("COMMON SHARES").

The parties acknowledge that the Company's 1994 Long Term Incentive Performance Plan (the "PLAN") does not contain a sufficient number of Common Shares issuable under the Plan to cover the full amount of the Share Options as of the date of this Agreement. Notwithstanding the foregoing, the Company hereby grants Executive the full number of Share Options subject to the condition that the grant of such Share Options ("CONDITIONAL OPTIONS") shall be conditioned on the approval by the shareholders of the Company of such grant (if required) and amendments to the Plan increasing the number of Common Shares issuable thereunder and otherwise permitting the Share Options and Additional Share Options (as defined herein) to be issued in accordance with the terms of this Agreement. The Company shall use its reasonable best efforts to obtain such approval. If the Company has not obtained such shareholder approval by June 30, 1999, such failure shall permit Executive to terminate this Agreement for Good Reason in accordance with the terms of this Agreement, in which case such Conditional Options shall be forfeited.

VESTING/EXERCISE. All of the Share Options shall vest as of the date of this Agreement but may only be exercised as follows: twenty-five (25%) percent of each of the \$6.50 Options (as defined herein) and \$8.50 Options (as defined herein) shall become exercisable on each anniversary of the Employment Period whether or not the Executive is employed by the Company on such anniversary. Notwithstanding the foregoing, Share Options granted to Executive shall (I) become exercisable in full upon (a) a Change in Control (as defined herein); (b) a termination by the Company without Cause (as defined herein); (c) a termination by the Executive for Good Reason (as defined herein); or (d) the eighteen (18) month anniversary of the Company being placed into voluntary or involuntary bankruptcy if Executive has not terminated his employment prior to such eighteen (18) month anniversary; (II) become exercisable Pro Rata (as defined herein) in the event of a termination due to death or Disability (as defined herein) (the Share Options in clauses (I) and (II) being collectively defined together with any Share Options which have previously become exercisable by their terms, as the "EXERCISABLE OPTIONS"); and (III) be forfeited

in full (whether exercisable (unless previously exercised) or unexercisable) upon a termination by the Company for Cause (as defined herein). "PRO RATA" means an amount of Share Options (half of which shall be \$6.50 Options and half of which shall be \$8.50 Options) equal to (x) the percentage equal to (i) the number of days from the commencement of the Exercise Year (as defined herein) through the date of the termination event divided by (ii) 365; MULTIPLIED BY (y) the number of Share Options which would otherwise have become exercisable during the Exercise Year in which the termination event occurs. "EXERCISE YEAR" means the twelve months commencing on the last date prior to termination on which the Share Options became exercisable (or from commencement of the Employment Period if termination occurs during the first twelve months of such commencement).

The Company shall provide Executive 30 days' prior written notice of the record date for any dividends or other distributions being paid with respect to the Common Shares. If such dividend or other distribution would trigger Executive's right to terminate this Agreement due to a Change in Control (the "TRIGGER EVENT"), then, notwithstanding anything herein to the contrary, the Share Options shall become exercisable in full as of the date of such notice; PROVIDED, HOWEVER, that (i) any exercise of such Share Options by Executive shall only become effective upon the Trigger Event being consummated and (ii) if the Trigger Event is not consummated, any such Share Options which were not yet exercisable as of the date of the Trigger Event shall again become unexercisable until the date they would have otherwise become exercisable in accordance with the terms of this Agreement.

Notwithstanding anything herein to the contrary, if the exercise price adjustment (see below) results in the exercise price of a Share Option equaling zero, such Share Option shall immediately become exercisable.

**EXERCISE PRICE.** The option exercise price with regard to the Share Options granted shall be as follows: 50% at \$6.50 per Common Share (the "\$6.50 OPTIONS") and 50% at \$8.50 per Common Share (the "\$8.50 OPTIONS"). The exercise price of each Share Option will be adjusted (but

not below zero) on each anniversary of its grant by an amount equal to (i) an increase of 10% per annum (compounded annually) MINUS (ii) all dividends or other distributions (including the value of non-cash dividends, including without limitation, share dividends and spin-off distributions) declared per Common Share for the applicable year. Notwithstanding the foregoing, the adjustment to the exercise price set forth in clause (i) in the preceding sentence shall (x) not commence until the eighteen (18) month anniversary of the commencement of the Employment Period; and (y) be applied ratably at the time(s) Executive exercises the Share Options (e.g. if Share Options are exercised on the 20-month anniversary of the commencement of the Employment Term, the exercise price in effect on that date would be increased by 1.667% (2/12 of 10%) minus any dividends paid on or prior to the date of exercise (to the extent such dividends were not previously deducted)).

**OPTION EXERCISE TERM.** Subject to the terms of this Agreement, all Share Options shall be exercisable for 10 years following the date upon which they are granted unless they expire earlier in accordance with this Agreement. In the event of the non-renewal of this Agreement after the expiration of the Employment Period, a Change of Control (unless Executive does not terminate his employment under this Agreement in which event the Share Options shall remain exercisable until they would otherwise expire under the terms of this Agreement), a termination without Cause, a termination for Good Reason, death or a termination by reason of Disability, all Exercisable Options shall remain exercisable for six (6) months following such event after which they shall expire. In the event of a termination without Good Reason, (i) all Share Options which were already exercisable prior to the date of termination shall remain exercisable for thirty (30) days after such event of termination after which they shall expire, and (ii) all the Share Options which are not yet exercisable prior to the date of termination shall be exercisable for thirty (30) days after the date on which they become exercisable in accordance with the terms of this Agreement after which they shall expire (the "POST-EXERCISABLE OPTIONS").

Notwithstanding the foregoing, the option exercise term of all Share Options intended to be treated as incentive stock options shall be such shorter period of time as may be required for incentive stock option treatment pursuant to Section 422 of the Internal Revenue Code of 1986, as amended (the "CODE").

**COMPANY CALL OPTION.** With respect to the Post-Exercisable Options, the Company shall have the right (the "CALL OPTION") to require Executive to transfer the Post-Exercisable Options to the Company at any time after the date of termination by Executive of his employment Without Good Reason for a price equal to the "Exercise Spread" (as defined herein). If such Exercise Spread is zero or less, the Company may purchase the Post-Exercisable Options for no consideration. The Company shall provide written notice to Executive that it is exercising the Call Option and the date on which such notice is deemed to have been given under the terms of this Agreement shall be deemed the "VALUATION DATE". The "EXERCISE SPREAD" shall be (i) the difference between (a) the exercise price of a Post-Exercisable option and (b) the "Closing Price" of a Common Share on the Valuation Date. The "CLOSING PRICE" means (i) if the Common Shares are listed or admitted to trading on the New York Stock Exchange (the "NYSE"), the American Stock Exchange ("AMEX") any national securities exchange or the Nasdaq Stock Market ("NASDAQ"), the closing price on the Valuation Date, or if no such sale takes place on such day, the average of the closing bid and asked prices on such day; (ii) if the Common Shares are not listed or admitted to trading on the NYSE, the AMEX, any national securities exchange or the Nasdaq, the last reported sale price on the Valuation Date or, if no sale takes place on such day, the average of the closing bid and asked prices on such day, as reported by a reliable quotation source designated by the Company; or (iii) if the Common Shares are not listed or admitted to trading on the NYSE, the AMEX, any national securities exchange or the Nasdaq and no such last reported sale price or closing bid and asked prices are available, the average of the reported high bid and low asked prices on the Valuation Date, as reported by a reliable quotation source designated by the Company, or



if there shall be no bid and asked prices on the Valuation Date, the average of the high bid and low asked prices, as so reported, on the most recent day (not more than five (5) days prior to the date in question) for which prices have been so reported; PROVIDED, HOWEVER, that if there are no bid and asked prices reported during the five (5) days prior to the date in question, the Closing Price of the Common Shares shall be determined by the independent trustees of the Company acting in good faith on the basis of such quotations and other information as they consider, in their reasonable judgment, appropriate.

ISOS. Any Share Options granted hereunder shall be "INCENTIVE STOCK OPTIONS" under Section 422 of the Code to the maximum extent possible under the Code, subject to Executive satisfying applicable employment and holding period requirements under the Code.

TRANSFERABILITY. Executive shall not be entitled to assign, hypothecate, alienate, pledge or otherwise transfer the Share Options except to a member of Executive's Immediate Family or an entity controlled by Executive or Executive's Immediate Family (other than Share Options intended to be incentive stock options within the meaning of Section 422 of the Code which shall not be transferable). "IMMEDIATE FAMILY" shall mean a spouse, child, parent, sibling or in-law. Any such transferee shall be bound by the terms of this Agreement and the Plan with respect to such Share Options.

(6) ADDITIONAL SHARE OPTIONS. The grant of additional share options ("ADDITIONAL SHARE OPTIONS") in an amount equal to 3% of the first \$120 million of equity (common or convertible preferred securities) ("NEW EQUITY") raised by the Company subsequent to October 15, 1998. The Additional Share Options shall be considered "Share Options" for purposes of this Agreement except that (i) such options shall be granted and shall vest as of the date of issuance of the New Equity; (ii) the per share exercise price of such options shall be equal to the per share issue price of the New Equity; and (iii) such options shall become and remain exercisable (or be immediately exercisable) in the same proportion and same manner and duration that the previously granted Share Options are already

exercisable or become exercisable (E.G. if 25% of the previously granted Share Options have already become exercisable at the time the Additional Share Options are granted, 25% of all the Additional Share Options shall be immediately exercisable upon grant, with the balance of the Additional Share Options proportionally becoming exercisable on the same timetable as the previously granted Share Options). In addition, Executive shall be entitled to receive such other share options as may be granted by the Board in its sole discretion.

(vii) LEGAL FEES AND COSTS. Payment of the Executive's reasonable legal fees incurred in connection with the preparation and negotiation of this Agreement, up to an aggregate maximum of \$35,000 for Executive, David Schonberger and Anne N. Zahner.

## 5. TERMINATION OF EMPLOYMENT AND CHANGE IN CONTROL.

(1) REASON FOR TERMINATION. Executive's employment hereunder may be terminated during the Employment Period under the following circumstances:

(1) CAUSE. The Company shall have the right to terminate Executive's employment for Cause upon Executive's: (A) conviction of, or plea of guilty or no contest to, an illegal act with respect to the Company; (B) conviction of, or plea of guilty or no contest to, a felony involving moral turpitude; or (C) Executive's willful and continued failure to use best efforts to substantially perform his duties hereunder (other than any such failure resulting from Executive's (x) incapacity due to Disability or (y) inability due to the unreasonableness of the duties requested to be performed) or willful misconduct or gross negligence in the performance of his duties hereunder for a period of thirty (30) days after written demand for substantial performance is delivered by the Company specifically identifying the manner in which the Company believes Executive has not substantially performed his duties or engaged in actions which constitute willful misconduct or gross negligence, PROVIDED, HOWEVER, that no termination for Cause shall occur unless a majority of the Board has voted to terminate Executive for Cause after Executive has received notice and an opportunity to cure the alleged Cause in accordance with this Paragraph 5(a)(i) and has failed to do so. If the Executive is terminated for Cause, the date of termination shall be the date

such written demand is delivered. Additionally, no act, or failure to act, on Executive's part shall be considered "WILLFUL" unless done, or omitted to be done, by him (I) not in good faith and (II) without reasonable belief that his action or omission was in furtherance of the interests of the Company.

(2) DEATH. Executive's employment hereunder shall terminate upon his death.

(3) DISABILITY. The Company shall have the right to terminate Executive's employment due to "Disability" in the event that there is a determination by the Company, upon the advice of an independent qualified physician mutually selected by Executive and the Company, that Executive has become physically or mentally incapable of performing his duties under this Agreement and such disability has disabled Executive for a period of one hundred eighty (180) days out of three hundred and sixty (360) days. (1)

(4) GOOD REASON. Executive shall have the right to terminate his employment for "Good Reason": (A) upon the occurrence of any material breach of this Agreement by the Company which shall include but not be limited to: (1) an assignment to Executive of duties materially inconsistent with Executive's status as President and Chief Executive Officer or a material and adverse alteration in the nature of, or material diminution in, Executive's duties and/or responsibilities, reporting obligations, titles or authority; (2) upon a reduction in Executive's Annual Base Salary or a material reduction in other benefits (not affecting the Company's executives generally) or a failure to pay such amounts when due; and (3) upon the relocation of the Company's principal executive offices or Executive's own office location to a location outside of Manhattan, it being acknowledged that the Company shall establish an office in Manhattan although as of the date hereof the Company does not yet have such an office; (B) upon the Company's failure to nominate Executive for election to the Board of Trustees or the Company's failure to use its reasonable best efforts to elect Executive to the Board; (C) upon Executive being forced to resign from the Board without Cause; (D) upon the Company being placed into voluntary or involuntary bankruptcy; or (E) the Company's failure to obtain shareholder approval pursuant to Paragraph 4(c)(v); PROVIDED, HOWEVER, that no termination for Good Reason shall occur unless the Company has received notice from

Executive of termination for Good Reason and the Company has failed to cure such alleged action which may have given rise to Executive's right to terminate for Good Reason within thirty (30) days after written notice of such alleged actions is delivered to the Company specifically identifying such alleged actions. Any dispute between the parties as to an alleged breach by the Company as set forth in clause (A)(1) above shall be resolved by arbitration pursuant to Paragraph 11.

(5) WITHOUT CAUSE. The Company shall have the right to terminate the Executive's employment hereunder without Cause subject to the terms and conditions of this Agreement.

(6) WITHOUT GOOD REASON. The Executive shall have the right to terminate his employment hereunder without Good Reason subject to the terms and conditions of this Agreement.

(7) CHANGE IN CONTROL. Executive shall have the right to terminate his employment hereunder following a Change in Control. For purposes of this Agreement "Change in Control" shall mean that any of the following events has occurred:

(A) An acquisition (other than directly from the Company) of any voting securities of the Company (treating all classes of outstanding voting securities or other securities convertible into voting securities as if they were converted into voting securities) (the "VOTING SECURITIES") by any "person", "entity" or "group of affiliated persons" (as such terms are used for purposes of Section 13(d) or 14(d) (collectively, "PERSONS") of the Securities Exchange Act of 1934, as amended (the "1934 Act") (other than Gotham Partners, L.P. ("GOTHAM"), Apollo Real Estate Advisors, L.P. ("APOLLO") or any affiliate of Gotham or Apollo or entity in which Gotham or Apollo own at least a 50% interest (collectively, the "GOTHAM/APOLLO ENTITIES")) immediately after which such Person has "Beneficial Ownership" (within the meaning of Rule 13d-3 promulgated under the 1934 Act and irrespective of any vesting or waiting periods) of thirty (30%) percent or more of the combined voting power of the Company's then outstanding Voting Securities; provided, however, that in determining whether a Change in Control has occurred, Voting Securities which are acquired

in a "Non-Control Acquisition" (as hereinafter defined) shall not constitute an acquisition which would cause a Change in Control. A "NON-CONTROL ACQUISITION" shall mean an acquisition by (1) an employee benefit plan (or a trust forming a part thereof) maintained by (x) the Company or (y) any corporation or other Person of which a majority of its voting power or its equity securities or equity interest is owned directly or indirectly by the Company (a "Subsidiary"), (2) the Company or any Subsidiary, or (3) any Person in connection with a "Non-Control Transaction."

(B) Six (6) of the ten (10) individuals who were appointed to the Board after April 1, 1998 (the "INCUMBENT BOARD") cease for any reason to be members of the Board; PROVIDED, HOWEVER, that if the election, or nomination for election by the Company's shareholders, of any new trustee was approved by Friedman, such new trustee shall, for purposes of this Agreement, be considered as a member of the Incumbent Board.

(C) A merger, consolidation or reorganization involving the Company, unless

(1) the shareholders of the Company, immediately before such merger, consolidation or reorganization, own, directly or indirectly, immediately following such merger, consolidation or reorganization, more than seventy (70%) percent of the combined voting power of the outstanding Voting Securities of the entity resulting from such merger or consolidation or reorganization (the "SURVIVING ENTITY") in substantially the same proportion as their ownership of the Voting Securities immediately before such merger, consolidation or reorganization, and

(2) the individuals who were members of the Incumbent Board immediately prior to the execution of the agreement providing for such merger, consolidation or reorganization constitute at least two-thirds of the members of the board of directors of the Surviving Entity or an entity beneficially owning, directly or indirectly, a majority of the Voting Securities of the Surviving Entity, and

(3) no Person (other than the Company, any Subsidiary, any employee benefit plan (or any trust forming a part thereof) maintained by the Company, the Surviving Entity or any Subsidiary, or any Person who, immediately prior to such merger, consolidation or reorganization had Beneficial Ownership of thirty (30%) percent or more of the then outstanding Voting Securities) owns, directly or indirectly, thirty percent or more of the combined voting power of the Surviving Entity's then outstanding voting securities.

A transaction described in clauses (1) through (3) shall herein be referred to as a "NON-CONTROL TRANSACTION".

(D) A complete liquidation or dissolution of the Company.

(E) the Company makes aggregate cash or non-cash distributions to its shareholders of the proceeds from the sales of assets equal to or greater than \$4.00 per Common Share and immediately following such distribution the "Net Asset Value" of the Company is less than \$150 million. "NET ASSET VALUE" shall be the fair market value of all of the Company's assets (as determined by mutual agreement of Executive and the Company or, if the parties cannot agree, by an arbitrator in accordance with Paragraph 11) less all Company liabilities.

Notwithstanding the foregoing, a Change in Control shall not be deemed to occur solely because any Person (the "SUBJECT PERSON") acquired Beneficial Ownership of more than the permitted amount of the outstanding Voting Securities as a result of the acquisition of Voting Securities by the Company which, by reducing the number of Voting Securities outstanding, increases the proportional number of shares Beneficially Owned by the Subject Person, provided that if a Change in Control would occur (but for the operation of this sentence) as a result of the acquisition of Voting Securities by the Company, and after such share acquisition by the Company, the Subject Person becomes the Beneficial Owner of any additional Voting Securities which increases the percentage of the then outstanding Voting Securities Beneficially Owned by the Subject Person, then a Change in Control shall occur.

(2) NOTICE OF TERMINATION. Any termination of Executive's employment by the Company or any such termination by Executive (other than on account of death) shall be communicated

by written Notice of Termination to the other party hereto. For purposes of this Agreement, a "NOTICE OF TERMINATION" shall mean a notice which shall indicate the specific termination provision in this Agreement relied upon and shall set forth in reasonable detail the facts and circumstances claimed to provide a basis for termination of Executive's employment under the provision so indicated. In the event of the termination of Executive's employment on account of death, written Notice of Termination shall be deemed to have been provided on the date of death.

#### 6. COMPENSATION UPON TERMINATION OF EMPLOYMENT.

(1) **BY THE COMPANY FOR CAUSE OR BY EXECUTIVE WITHOUT GOOD REASON.** In the event the Company terminates Executive's employment for Cause or Executive terminates his employment without Good Reason, the Company shall pay Executive and Executive shall be entitled to receive any (i) unpaid Annual Base Salary at the rate then in effect accrued through and including the date of termination and (ii) reimbursement of expenses incurred prior to the date of termination ("EXPENSE REIMBURSEMENT").

Except for any rights which Executive may have to unpaid salary amounts, the LTC Payment (as defined herein) and Expense Reimbursement through and including the date of termination and Exercisable Options (and, with respect to a termination by Executive without Good Reason, any Share Options which have not yet become exercisable on the date of termination), the Company shall have no further obligations hereunder following such termination other than pursuant to Paragraphs 6(d), 10 and 12. The aforesaid amounts shall be payable in full immediately upon such termination.

(2) **UPON DEATH OR DISABILITY.** In the event of termination of Executive's employment as a result of either Executive's death or Disability, the Company shall pay to Executive, his estate or his personal representative (i) the accrued but unpaid Annual Base Salary at the rate then in effect; (ii) earned but unpaid incentive compensation or bonuses for completed performance periods; (iii) an amount equal to 12 months of the Annual Base Salary at the rate then in effect (the "SALARY PAYMENT"); and (iv) Expense Reimbursement. The aforesaid amounts shall be payable in cash without discount for early payment, at the option of Executive, his estate or his personal representative, either in full immediately upon such termination or monthly over the Unexpired Employment Period (the "PAYMENT ELECTION"). In the event of termination of employment due to Disability, Executive shall also receive continuation of health coverage through the end of the Unexpired Employment Period on the same basis as health coverage is provided by the Company for active employees and as may be amended from time to time ("MEDICAL CONTINUATION").

Except for any rights which Executive may have hereunder including the accrued Annual Base Salary, the Salary Payment, Exercisable Options, the LTC Payment, Expense Reimbursement and in the event of a termination of employment due to Disability, Medical Continuation, the Company shall have no further obligations hereunder following such termination other than pursuant to Paragraphs 6(d), 10 and 12. The foregoing payments shall be in addition to any benefits to which Executive may be entitled under any insurance maintained by the Company.

(3) BY THE COMPANY WITHOUT CAUSE OR BY EXECUTIVE FOR GOOD REASON OR IN THE EVENT OF A CHANGE IN CONTROL.

(i) NO BANKRUPTCY. In the event the Company terminates Executive's employment for any reason other than Cause, death or Disability or Executive terminates his employment for Good Reason (other than as set forth in Paragraph 6(c)(ii)), or in the event of a Change of Control, the Company shall pay to Executive and Executive shall be entitled to receive the sum total of:

(A) the accrued but unpaid Annual Base Salary at the rate then in effect; (B) earned but unpaid incentive compensation and/or bonuses for completed performance periods; (C)(1) if the effective date of termination is on or prior to the eighteen (18) month anniversary of the commencement of the Employment Term, an amount equal to three (3) times the Annual Base Salary at the rate then in effect or (2) if the effective date of termination is after the eighteen (18) month anniversary of the commencement of the Employment Term, an amount equal to two and one-half (2.5) times the Annual Base Salary at the rate then in effect (as applicable, the "TERMINATION PAYMENT"); and (D) continuation of Executive's participation in all benefit plans, programs or arrangements of the Company (except tax-qualified plans), including, without limitation, Medical Continuation, for a period of two years following such termination. The aforesaid amount shall be payable in cash without discount for early payment, at the option of Executive, in accordance with the Payment Election.

(ii) BANKRUPTCY. Executive may not terminate employment for Good Reason due to the Company being placed in bankruptcy until the eighteen (18) month anniversary thereof. If Executive thereafter terminates this Agreement, the Company shall pay to Executive and Executive shall be entitled to receive the same payments and benefits set forth in Paragraph 6(c)(i); PROVIDED, HOWEVER, that if the date of being placed in bankruptcy is (x) on or prior to the eighteen (18) month anniversary of the commencement of the Employment Term, Executive shall receive the Termination Payment set forth in Paragraph 6(c)(i)(C)(1) and (y) after the eighteen (18) month anniversary of the commencement of the Employment Term, Executive shall receive the Termination Payment set forth in Paragraph 6(c)(i)(C)(2).



(iii) SECTION 280G. Notwithstanding anything contained in this Agreement to the contrary, to the extent that any payment or distribution of any type to or for Executive by the Company, any affiliate of the Company, any person who acquires ownership or effective control of the Company or ownership of a substantial portion of the Company's assets (within the meaning of Section 280G of the Code and the regulations thereunder), or any affiliate of such person, whether paid or payable or distributed or distributable pursuant to the terms of this Agreement or otherwise (the "TOTAL PAYMENTS") is or will be subject to the excise tax imposed under Section 4999 of the Code (the "EXCISE TAX"), then the Total Payments shall be reduced (but not below zero) if and to the extent that a reduction in the Total Payments would result in the Executive retaining a larger amount, on an after-tax basis (taking into account federal, state and local income taxes and the Excise Tax), than if the Executive received the entire amount of such Total Payments. Executive shall have the right to specify the order in which the Company shall reduce or eliminate the Total Payments in order to effectuate the foregoing.

Except for any rights which Executive may have hereunder including the accrued Annual Base Salary, the Termination Payment, Exercisable Options, the LTC Payment, Expense Reimbursement and Medical Continuation, the Company shall have no further obligations hereunder following such termination other than pursuant to Paragraphs 6(d), 10 and 12.

(4) GENERAL. The parties agree to cooperate to structure all termination payments made pursuant to this Agreement in a manner so that such payments are not subject to the Excise Tax.

## 7. MITIGATION; PAYMENTS PENDING RESOLUTION OF DISPUTES.

Executive shall not be required to mitigate amounts payable under this Agreement by seeking other employment or otherwise, and there shall be no offset against amounts due Executive under this Agreement on account of subsequent employment. Amounts owed to Executive under this Agreement shall not be offset by any claims the Company may have against Executive and such payment shall not be affected by any other circumstances, including, without limitation, any counterclaim, recoupment, defense, or other right which the Company may have against Executive or others. During the pendency of any dispute between the Company and Executive with respect to the termination of this Agreement, the Company shall establish and maintain an escrow account ("ESCROW ACCOUNT") with Battle Fowler LLP ("ESCROW AGENT") pursuant to an agreement reasonably acceptable to Executive and the Escrow Agent. The Company shall pay into the Escrow Account from time to time the compensation and cash-value of the benefits which would otherwise be payable to Executive if there were no dispute. Upon resolution of the dispute, the Escrow Agent shall pay the funds in the Escrow Account as required by the court or arbitrator with jurisdiction over the dispute or in accordance with the joint instructions of the parties.

## 8. NON-COMPETE.

(1) NON-COMPETITION. Executive agrees that, without the prior written consent of a majority of the Board and in accordance with applicable law, and except as provided in subparagraph 8(b), during the Employment Period, Executive shall not invest, manage or otherwise be engaged in commercial real estate.

(2) EXCLUDED ACTIVITIES. Nothing contained in this Paragraph 8 shall preclude Executive from:

(1) Continuing to own, manage in accordance with past practices or make additional capital contributions to Executive's existing investments listed on SCHEDULE A attached hereto.

(2) making passive investments of 5% or less in publicly listed or traded real estate companies.

## 9. NO SOLICITATION; CONFIDENTIALITY.

(1) NO SOLICITATION. During the Restricted Period (as defined herein), Executive shall not, nor cause any other person to, without the prior written consent of the Board, directly or indirectly, solicit for employment, employ in any capacity or make an unsolicited recommendation to any other person that it employ or solicit for employment any person who is or was, at any

time during the Employment Period or the Restricted Period, an officer, executive or key employee of the Company or of any of its affiliates (other than David Schonberger and Anne N. Zahner, whose solicitation, employment or recommendation by Executive shall not be prohibited by the terms of this Agreement). As used in this Agreement, "RESTRICTED PERIOD" shall mean the six (6) months following Executive's termination of employment for any reason.

(2) CONFIDENTIALITY. Executive acknowledges that, through his status as Chief Executive Officer and President of the Company, he has, and will have, possession of Confidential Information (as defined herein) as to the business of the Company. Executive agrees that all such Confidential Information constitutes a vital part of the business of the Company and its affiliates and is by its nature trade secrets and confidential information proprietary to the Company and its affiliates. Executive agrees that he shall not divulge, communicate, furnish or make accessible (whether orally or in writing or in books, articles or any other medium) to any individual, firm, partnership, corporation or other entity or person, any knowledge or information with respect to Confidential Information directly or indirectly relating to the business of the Company or any of its affiliates. The term "CONFIDENTIAL INFORMATION" shall mean any information not generally known in the relevant trade or industry or otherwise not generally available to the public, which was obtained from the Company or which was learned, discovered, developed, conceived, originated or prepared during or as a result of the performance of any services by Executive on behalf of the Company.

(3) RETURN OF COMPANY DOCUMENTS. All memoranda, notes, lists, notebooks, records and other documents or papers (and all copies thereof), including such items stored in computer memories, portable computers and the like, on microfiche, disk or by any other means, made or compiled by or on behalf of Executive or made available to Executive relating to the Company are and shall be the Company's property and shall be delivered to the Company promptly upon the termination of Executive's employment with the Company or at any other time after such termination on request.

(4) UNENFORCEABILITY. The provisions contained in Paragraphs 8 and 9 as to the time periods and scope of activities, persons or entities affected shall be deemed divisible so that, if any provision contained in Paragraphs 8 or 9 is determined to be invalid or unenforceable, such provision shall be deemed modified so as to be valid and enforceable to the full extent lawfully permitted.

(5) REMEDIES. Executive agrees that (i) the provisions of Paragraphs 8 and 9 are reasonable and necessary for the

protection of the Company; (ii) the Company would not have entered into this Agreement unless the Executive agreed to the inclusion of such provisions; (iii) such provisions may not be adequately enforced by an action for damages and (iv) in the event of a breach thereof by Executive, the Company shall be entitled to apply for and obtain injunctive relief in any court of competent jurisdiction to restrain the breach or threatened breach of such violation or otherwise to enforce specifically such provisions against such violation, without the necessity of the posting of any bond by the Company. The forgoing remedies are in addition to any rights the Company may have against Executive for damages in the event Executive breaches any of the provisions of Paragraphs 8 and 9.

#### 10. PREVIOUS EMPLOYER.

(1) COMMITMENT TO PAY/FUND. The Company agrees to take the following actions with respect to the following commitments with respect to Executive's immediately prior employer, Enterprise Asset Management, Inc. ("EAM") and Executive:

(i) LONG-TERM COMPENSATION ("LTC"). The Company shall pay the LTC to Executive as follows: (x) 1/3 on commencement of the Employment Period and 1/3 on each of the second and fourth anniversaries of the commencement of the Employment Period and (y) if this Agreement is terminated for any reason, Company shall make a lump sum payment equal to the present value (discounted at 10% per annum) of any unpaid LTC (the "LTC PAYMENT"). Executive shall reimburse Company to the extent Executive receives payment from EAM of LTC paid by the Company.

(ii) LOAN GUARANTEES. If EAM fails to continue to guarantee existing loans owed by Executive, the Company shall provide replacement loans on the same or better terms and conditions as the existing loans ("REPLACEMENT LOANS").

(iii) LOAN REPAYMENT. If EAM demands repayment prior to maturity of existing loans to Executive from EAM, the Company shall provide replacement loans on the same or better terms and conditions as the existing loans ("NEW LOANS").

Executive's LTC, guarantees and loans are listed in SCHEDULE B attached hereto.

In the event this Agreement is terminated for any reason, Executive shall repay all Replacement Loans and New Loans within ninety (90) days of such date of termination. The Replacement

Loans and New Loans shall be nonrecourse to Executive and the Company's sole recourse for the repayment of any Replacement Loans or New Loans shall be any payments due to Executive from the Company under this Agreement, the Share Options and the assets which were purchased with the proceeds from the loans which have been replaced by the Replacement Loan or the New Loan.

(2) INDEMNITY. In the event the Executive is made party or threatened to be made a party to any action, suit or proceeding, whether civil, criminal, administrative or investigative (a "PROCEEDING"), by EAM, its officers, directors, equity owners or Affiliates, by reason of Executive's having negotiated or entered into this Agreement or otherwise having become an employee of the Company, the Company shall indemnify, hold harmless and defend Executive against any and all claims, demands, suits, judgments, assessments and settlements including all expenses incurred or suffered by Executive in connection therewith (including, without limitation, all legal fees incurred using counsel reasonably acceptable to Executive) (collectively, "DAMAGES"). Expenses incurred by Executive in connection with any Proceeding shall be paid by the Company in advance upon request of Executive that the Company pay such expenses.

(3) REPRESENTATIONS. Executive hereby represents and warrants to the Company that Executive has not entered into any written or oral agreement for employment with EAM or any other person or entity other than the letter agreement dated May 3, 1993; regarding the payment of LTC.

(4) SURVIVAL. The provisions of this Paragraph shall remain in effect after this Agreement is terminated irrespective of the reasons for termination.

#### 11. ARBITRATION.

The parties hereto will endeavor to resolve in good faith any controversy, disagreement or claim arising between them with respect to the interpretation, performance or operation of Paragraphs 5(a)(iv)(A)(1) and 5(a)(vii)(E) of this Agreement. If they are unable to do so, any such controversy, disagreement or claim will be submitted to binding arbitration, for final resolution without appeal, by either party giving written notice to the other of the existence of a dispute with respect to such Paragraph which it desires to have arbitrated. The arbitration will be conducted in New York, New York by a panel of three (3) arbitrators and will be held in accordance with the rules of the American Arbitration Association. Of the three arbitrators, one will be selected by the Company, one will be selected by Executive and the third will be selected by the two arbitrators so selected. Each party will notify the other party of the arbitrator selected by [him] [her] or it within fifteen (15) days after the giving of the written notice referred to in this

Paragraph 11. The decision and award of the arbitrators must be in writing and will be final and binding upon the parties hereto. Judgment upon the award may be entered in any court having jurisdiction thereof, or application may be made to such court for a judicial acceptance of the award and an order of enforcement, as the case may be. Subject to the provisions of Paragraph 12(b), the expenses of arbitration will be borne in accordance with the determination of the arbitrators.

## 12. INDEMNIFICATION/LEGAL FEES/"KEY MAN" INSURANCE.

(1) INDEMNIFICATION. In the event the Executive is made party or threatened to be made a party to any Proceeding, by reason of Executive's employment with or serving as an officer or director of the Company, the Company shall indemnify, hold harmless and defend Executive to the fullest extent authorized by Ohio law, as the same exists and may hereafter be amended, against any and all Damages and such indemnification shall continue as to Executive even after Executive is no longer employed by the Company and shall inure to the benefit of his heirs, executors, and administrators. Notwithstanding the foregoing, Executive shall not be entitled to indemnification pursuant to this Paragraph 12(a) if a court or other tribunal conclusively determines that Executive engaged in actions in connection with Executive's employment with the Company which were committed in bad faith, were the result of active and deliberate dishonesty, or constitute willful misconduct, fraud or gross negligence.

Expenses incurred by Executive in connection with any Proceeding referred to in this Paragraph 12 shall be paid by the Company in advance upon request of Executive that the Company pay such expenses; but only in the event that Executive shall have delivered in writing to the Company an undertaking to reimburse the Company for expenses with respect to which Executive is not entitled to indemnification.

The provisions of this Paragraph shall remain in effect after this Agreement is terminated irrespective of the reasons for termination. The indemnification provisions of this Paragraph shall not supersede or reduce any indemnification provided to Executive under any separate agreement, or the by-laws of the Company since it is intended that this Agreement shall expand and extend the Executive's rights to receive indemnity.

The Company shall maintain in effect during the Employment Period a directors' and officers' liability insurance policy, with a policy limit of at least \$10,000,000, subject to customary exclusions, with respect to claims made against officers and directors of the Company.

(2) LEGAL FEES. Except as set forth below, if any contest or dispute shall arise between the Company and Executive regarding or as a result of any provision of this Agreement, the Company shall pay, or reimburse Executive for, all legal fees and expenses reasonably incurred by Executive in connection with such contest or dispute; PROVIDED, HOWEVER, that if Executive is not successful in respect of substantially all of Executive's claims pursued or defended in connection with such contest or dispute, Executive shall pay or reimburse the Company for all such fees and expenses advanced by the Company. Executive shall pay the first \$50,000 of his fees or expenses as they are incurred and the Company shall pay all such fees and expenses over \$50,000 as they are incurred. If Executive is successful in respect of substantially all of such claims, the Company shall reimburse Executive for any amounts paid by Executive as soon as practicable following the final resolution of such contest or dispute.

(3) KEY MAN INSURANCE. Executive shall cooperate with, and take such actions as may be reasonably requested by, the Company in the event the Company determines to obtain "key man" insurance with respect to Executive.

### 13. SUCCESSORS AND ASSIGNS.

(1) COMPANY. Unless Executive elects to terminate this Agreement as a result of a Change in Control, the Company shall require any successor (whether direct or indirect, by purchase, merger, consolidation or otherwise) to all or substantially all of the business and/or assets of the Company, to expressly assume and agree to perform this Agreement in the same manner and to the same extent that the Company would be required to perform it if no such succession had taken place.

(2) EXECUTIVE. This Agreement and all rights of Executive hereunder may be transferred only by will or the laws of descent and distribution. Upon Executive's death, this Agreement and all rights of Executive hereunder shall inure to the benefit of and be enforceable by Executive's beneficiary or beneficiaries, personal or legal representatives, or estate, to the extent any such person succeeds to Executive's interests under this Agreement. Executive shall be entitled to select and change a beneficiary or beneficiaries to receive any benefit or compensation payable hereunder following Executive's death by giving Company written notice thereof. If Executive should die following the date of termination while any amounts would still be payable to him hereunder if he had continued to live, all such amounts, unless otherwise provided herein, shall be paid in accordance with the terms of this Agreement to such person or persons so appointed in writing by Executive, including, without limitation, under any applicable plan, or otherwise to his legal representatives or estate.

#### 14. MODIFICATION OR WAIVER.

No amendment, modification, waiver, termination or cancellation of this Agreement shall be binding or effective for any purpose unless it is made in a writing signed by the party against whom enforcement of such amendment, modification, waiver, termination or cancellation is sought. No course of dealing between or among the parties to this Agreement shall be deemed to affect or to modify, amend or discharge any provision or term of this Agreement. No delay on the part of the Company or Executive in the exercise of any of their respective rights or remedies shall operate as a waiver thereof, and no single or partial exercise by the Company or Executive of any such right or remedy shall preclude other or further exercise thereof. A waiver of right or remedy on any one occasion shall not be construed as a bar to or waiver of any such right or remedy on any other occasion.

The respective rights and obligations of the parties hereunder shall survive the Executive's termination of employment and termination of this Agreement to the extent necessary for the intended preservation of such rights and obligations.

#### 15. NOTICES.

All notices or other communications required or permitted hereunder shall be made in writing and shall be deemed to have been duly given if delivered by hand or delivered by a recognized delivery service or mailed, postage prepaid, by express, certified or registered mail, return receipt requested, and addressed to the Company at the address set forth above or Executive at his address as set forth in the Company records (or to such other address as shall have been previously provided in accordance with this Paragraph 15).

#### 16. GOVERNING LAW.

This agreement will be governed by and construed in accordance with the laws of the State of New York without regard to principles of conflicts of laws thereunder.

#### 17. SEVERABILITY.

Whenever possible, each provision and term of this Agreement shall be interpreted in such manner as to be effective and valid under applicable law, but if any provision or term of this Agreement shall be held to be prohibited by or invalid under such applicable law, then, such provision or term shall be ineffective only to the extent of such prohibition or invalidity, without invalidating or affecting in any manner whatsoever the remainder of such provisions or term or the remaining provisions or terms of this Agreement.



18. COUNTERPARTS.

This Agreement may be executed in separate counterparts, each of which is deemed to be an original and both of which taken together shall constitute one and the same agreement.

19. HEADINGS.

The headings of the Paragraphs of this Agreement are inserted for convenience only and shall not be deemed to constitute a part hereof and shall not affect the construction or interpretation of this Agreement.

20. ENTIRE AGREEMENT.

This Agreement constitutes the entire agreement of the parties with respect to the subject matter hereof and supersedes all other prior agreements and undertakings, both written and oral, among the parties with respect to the subject matter hereof.

21. EXCULPATION.

Notwithstanding anything contained herein to the contrary, this Agreement is made and executed on behalf of the Company by its officer(s) on behalf of the trustees thereof, and none of the trustees or any additional or successor trustee hereafter appointed, or any beneficiary, officer, employee or agent of the Company shall have any liability in his personal or individual capacity, but instead, Executive shall look solely to the property and assets of the Company for satisfaction of claims of any nature arising from or in connection with this Agreement.

**[SIGNATURE PAGE FOLLOWS]**

IN WITNESS WHEREOF, the undersigned have executed this Agreement as of the date first above written.

**COMPANY:**

**FIRST UNION REAL ESTATE EQUITY AND  
MORTGAGE INVESTMENTS**

By:

Name:

Title:

**EXECUTIVE:**

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**Schedule A**

**Existing Investments**

**Dan Friedman**

**Investments Owned**

1. Greenburgh, NY
2. Mt. Kisco, NY (T.J. Maxx)
3. 150 Bay Street
4. 299 Broadway
5. 349 East 149th Street
6. 379 West Broadway
7. NYC Holdings
8. Angelene
9. Cheshire Properties
10. Chester Apartments
11. Emax Securities (various entities)
12. Manor Building
13. Peripheral Land
14. Peru Mall
15. Sigma LLC
16. Dancor Investments (various)

**Investments Managed**

None

**Schedule B**

**Long Term Compensation \$379,241.89**

Loans from EAM \$336,000.00

**Loans Guaranteed by EAM \$115,000.00**

B-1

**Exhibit 10(a)**

**EMPLOYMENT AGREEMENT**

**FOR**

**ANNE NELSON ZAHNER**

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## Schedules

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Schedule A  
Schedule B

Existing Investments  
Prior Employer Agreements

## EMPLOYMENT AGREEMENT

THIS EMPLOYMENT AGREEMENT (the "AGREEMENT") is entered into as of November 2, 1998, by and between ANNE NELSON ZAHNER, an individual residing in the State of New York ("EXECUTIVE"), and FIRST UNION REAL ESTATE EQUITY AND MORTGAGE INVESTMENTS, an Ohio business trust with offices at 55 Public Square, Suite 1900, Cleveland, Ohio 44113 (the "COMPANY").

### **RECITALS**

WHEREAS, the Company desires to employ Executive as Executive Vice President and Executive desires to be employed by the Company as Executive Vice President.

NOW, THEREFORE, in consideration of the premises and the mutual covenants and agreements set forth herein, the parties hereby agree as follows:

#### 1. EMPLOYMENT.

The Company hereby agrees to employ Executive, and Executive hereby agrees to accept such employment during the period and upon the terms and conditions set forth in this Agreement.

#### 2. EMPLOYMENT PERIOD.

(1) EMPLOYMENT PERIOD. Except as otherwise provided in this Agreement to the contrary, the terms and conditions of this Agreement shall be and remain in effect during the period of employment (the "EMPLOYMENT PERIOD") established under this Paragraph 2. The initial Employment Period shall be for a term commencing on the date of this Agreement and ending on the fourth anniversary of the date of this Agreement, unless earlier terminated as provided in this Agreement. Immediately following the execution hereof, the Executive shall resign from all positions as an employee, officer and director of her current employer and its affiliates.

(2) UNEXPIRED EMPLOYMENT PERIOD. If Executive's employment with the Company is terminated, for purposes of this Agreement the term "UNEXPIRED EMPLOYMENT PERIOD" shall mean the period commencing on the date of such termination and ending on the last day of the Employment Period.

### 3. SERVICES/PLACE OF EMPLOYMENT.

(1) SERVICES. During the Employment Period, Executive shall hold the position of Executive Vice President. Executive shall devote her best efforts and such business time, skill and attention exclusively to the business of the Company (other than absences due to vacation, illness, disability or approved leave of absence) as is necessary to perform such duties as are customarily performed by similar executive officers together with such other reasonable duties as may be more specifically enumerated from time to time by the Company's board of trustees ("BOARD OF TRUSTEES" or "BOARD") PROVIDED, HOWEVER, that the foregoing is not intended to preclude Executive from (i) owning and managing personal investments, including real estate investments, in accordance with Paragraph 8 hereof or (ii) engaging in charitable activities and community affairs, provided that (x) with respect to the activities referenced in clause (ii), Executive obtains the prior approval of the Board as to the amount of time Executive will devote to such activities and (y) the performance of the activities referred to in clauses (i) and (ii) of this Paragraph 3(a) does not prevent Executive from devoting sufficient business time to the Company to carry out Executive's duties as Executive Vice President.

(2) PLACE OF EMPLOYMENT. The principal place of employment of Executive shall be at the Company's executive offices in New York (Manhattan County), New York.

### 4. Compensation and Benefits.

(1) SALARY. During the first twelve (12) months of the Employment Period, the Company shall pay Executive an annual base salary in the amount of \$200,000 payable in accordance with the Company's regular payroll practices. Executive's annual base salary shall be reviewed annually in accordance with the policy of the Company and shall be subject to upward adjustment based upon, among other things, Executive's performance, as determined in the sole discretion of the Board PROVIDED HOWEVER that the annual increase in base salary for each year of the Term shall be at least 5% over the annual base salary for the previous year (the annual base salary as adjusted from time to time is hereinafter referred to as the "ANNUAL BASE SALARY"). In no event shall Executive's Annual Base Salary in effect at a particular time be reduced without her prior written consent.

(2) TAXES AND WITHHOLDING. The Company shall have the right to deduct and withhold from all compensation all social security and other federal, state and local taxes and charges which currently are or which hereafter may be required by law to be so deducted and withheld.

(1)



(3) **ADDITIONAL BENEFITS.** In addition to the other compensation payable pursuant to this Agreement, Executive shall be entitled to the following.

(1) **BENEFITS.** All fringe benefits and perquisites as are generally made available from time to time to all employees and/or to executives of the Company generally and to participate in any pension, profit-sharing or similar plan or program established from time to time by the Company for the benefit of its employees and/or executives generally, subject to the provisions of such plans. In any event, Executive's health insurance coverage shall commence on the date of this Agreement (or the Company shall reimburse Executive for COBRA payments until such coverage can commence).

(2) **MEMBERSHIP FEES.** Membership fees and costs for reasonable and customary memberships in professional organizations.

(3) **EXPENSE REIMBURSEMENT.** Reimbursement for reasonable business expenses incurred by Executive in furtherance of the interests of the Company, subject to the reasonable procedures established by the Company from time to time with respect to substantiation and approval.

(4) **VACATION AND SICK LEAVE/PERSONAL DAYS.** Such periods of paid vacation and sick leave/personal days allowance each year (not less than four (4) weeks vacation and seven (7) days of sick leave/personal days per full twelve (12) month period) that are consistent with the Company's vacation and sick leave/personal days policy for senior management.

(5) **SHARE OPTIONS. GRANT.** The grant upon execution of this Agreement of share options ("SHARE OPTIONS") to acquire 360,000 shares of the Company's common shares of beneficial interest ("COMMON SHARES").

The parties acknowledge that the Company's 1994 Long Term Incentive Performance Plan (the "PLAN") does not contain a sufficient number of Common Shares issuable under the Plan to cover the full amount of the Share Options as of the date of this Agreement. Notwithstanding the foregoing, the Company hereby grants Executive the full number of Share Options subject to the condition that the grant of such Share Options ("CONDITIONAL OPTIONS") shall be conditioned on

the approval by the shareholders of the Company of such grant (if required) and amendments to the Plan increasing the number of Common Shares issuable thereunder and otherwise permitting the Share Options and Additional Share Options (as defined herein) to be issued in accordance with the terms of this Agreement. The Company shall use its reasonable best efforts to obtain such approval. If the Company has not obtained such shareholder approval by June 30, 1999, such failure shall permit Executive to terminate this Agreement for Good Reason in accordance with the terms of this Agreement, in which case such Conditional Options shall be forfeited.

VESTING/EXERCISE. All of the Share Options shall vest as of the date of this Agreement but may only be exercised as follows: twenty-five (25%) percent of each of the \$6.50 Options (as defined herein) and \$8.50 Options (as defined herein) shall become exercisable on each anniversary of the Employment Period whether or not the Executive is employed by the Company on such anniversary. Notwithstanding the foregoing, Share Options granted to Executive shall (I) become exercisable in full upon (a) a Change in Control (as defined herein); (b) a termination by the Company without Cause (as defined herein); (c) a termination by the Executive for Good Reason (as defined herein); or (d) the eighteen (18) month anniversary of the Company being placed into voluntary or involuntary bankruptcy if Executive has not terminated her employment prior to such eighteen (18) month anniversary; (II) become exercisable Pro Rata (as defined herein) in the event of a termination due to death or Disability (as defined herein) (the Share Options in clauses (I) and (II) being collectively defined together with any Share Options which have previously become exercisable by their terms, as the "EXERCISABLE OPTIONS"); and (III) be forfeited in full (whether exercisable (unless previously exercised) or unexercisable) upon a termination by the Company for Cause (as defined herein). "PRO RATA" means an amount of Share Options (half of which shall be \$6.50 Options and half of which shall be \$8.50 Options) equal to (x) the percentage equal to (i) the number of days from the commencement of the Exercise Year (as defined herein) through the date of the termination event divided by (ii) 365;

MULTIPLIED BY (y) the number of Share Options which would otherwise have become exercisable during the Exercise Year in which the termination event occurs. "EXERCISE YEAR" means the twelve months commencing on the last date prior to termination on which the Share Options became exercisable (or from commencement of the Employment Period if termination occurs during the first twelve months of such commencement).

The Company shall provide Executive 30 days' prior written notice of the record date for any dividends or other distributions being paid with respect to the Common Shares. If such dividend or other distribution would trigger Executive's right to terminate this Agreement due to a Change in Control (the "TRIGGER EVENT"), then, notwithstanding anything herein to the contrary, the Share Options shall become exercisable in full as of the date of such notice; PROVIDED, HOWEVER, that (i) any exercise of such Share Options by Executive shall only become effective upon the Trigger Event being consummated and (ii) if the Trigger Event is not consummated, any such Share Options which were not yet exercisable as of the date of the Trigger Event shall again become unexercisable until the date they would have otherwise become exercisable in accordance with the terms of this Agreement.

Notwithstanding anything herein to the contrary, if the exercise price adjustment (see below) results in the exercise price of a Share Option equaling zero, such Share Option shall immediately become exercisable.

EXERCISE PRICE. The option exercise price with regard to the Share Options granted shall be as follows: 50% at \$6.50 per Common Share (the "\$6.50 OPTIONS") and 50% at \$8.50 per Common Share (the "\$8.50 OPTIONS"). The exercise price of each Share Option will be adjusted (but not below zero) on each anniversary of its grant by an amount equal to  
(i) an increase of 10% per annum (compounded annually) MINUS  
(ii) all dividends or other distributions (including the value of non-cash dividends, including without limitation, share dividends and spin-off distributions) declared per Common Share for the applicable year. Notwithstanding the foregoing, the adjustment to the exercise price set forth in clause (i) in the preceding sentence shall

(x) not commence until the eighteen (18) month anniversary of the commencement of the Employment Period; and (y) be applied ratably at the time(s) Executive exercises the Share Options (e.g. if Share Options are exercised on the 20-month anniversary of the commencement of the Employment Term, the exercise price in effect on that date would be increased by 1.667% (2/12 of 10%) minus any dividends paid on or prior to the date of exercise (to the extent such dividends were not previously deducted)).

**OPTION EXERCISE TERM.** Subject to the terms of this Agreement, all Share Options shall be exercisable for 10 years following the date upon which they are granted unless they expire earlier in accordance with this Agreement. In the event of the non-renewal of this Agreement after the expiration of the Employment Period, a Change of Control (unless Executive does not terminate her employment under this Agreement in which event the Share Options shall remain exercisable until they would otherwise expire under the terms of this Agreement), a termination without Cause, a termination for Good Reason, death or a termination by reason of Disability, all Exercisable Options shall remain exercisable for six (6) months following such event after which they shall expire. In the event of a termination without Good Reason, (i) all Share Options which were already exercisable prior to the date of termination shall remain exercisable for thirty (30) days after such event of termination after which they shall expire, and (ii) all the Share Options which are not yet exercisable prior to the date of termination shall be exercisable for thirty (30) days after the date on which they become exercisable in accordance with the terms of this Agreement after which they shall expire (the "POST-EXERCISABLE Options").

Notwithstanding the foregoing, the option exercise term of all Share Options intended to be treated as incentive stock options shall be such shorter period of time as may be required for incentive stock option treatment pursuant to Section 422 of the Internal Revenue Code of 1986, as amended (the "CODE").

**COMPANY CALL OPTION.** With respect to the Post-Exercisable Options, the Company shall have

the right (the "CALL OPTION") to require Executive to transfer the Post-Exercisable Options to the Company at any time after the date of termination by Executive of her employment Without Good Reason for a price equal to the "Exercise Spread" (as defined herein). If such Exercise Spread is zero or less, the Company may purchase the Post-Exercisable Options for no consideration. The Company shall provide written notice to Executive that it is exercising the Call Option and the date on which such notice is deemed to have been given under the terms of this Agreement shall be deemed the "VALUATION DATE". The "EXERCISE SPREAD" shall be (i) the difference between (a) the exercise price of a Post-Exercisable option and (b) the "Closing Price" of a Common Share on the Valuation Date. The "CLOSING PRICE" means (i) if the Common Shares are listed or admitted to trading on the New York Stock Exchange (the "NYSE"), the American Stock Exchange ("AMEX") any national securities exchange or the Nasdaq Stock Market ("NASDAQ"), the closing price on the Valuation Date, or if no such sale takes place on such day, the average of the closing bid and asked prices on such day; (ii) if the Common Shares are not listed or admitted to trading on the NYSE, the AMEX, any national securities exchange or the Nasdaq, the last reported sale price on the Valuation Date or, if no sale takes place on such day, the average of the closing bid and asked prices on such day, as reported by a reliable quotation source designated by the Company; or (iii) if the Common Shares are not listed or admitted to trading on the NYSE, the AMEX, any national securities exchange or the Nasdaq and no such last reported sale price or closing bid and asked prices are available, the average of the reported high bid and low asked prices on the Valuation Date, as reported by a reliable quotation source designated by the Company, or if there shall be no bid and asked prices on the Valuation Date, the average of the high bid and low asked prices, as so reported, on the most recent day (not more than five (5) days prior to the date in question) for which prices have been so reported; PROVIDED, HOWEVER, that if there are no bid and asked prices reported during the five (5) days prior to the date in question, the Closing Price of the Common Shares shall be determined by the independent trustees of the

Company acting in good faith on the basis of such quotations and other information as they consider, in their reasonable judgment, appropriate.

ISOS. Any Share Options granted hereunder shall be "INCENTIVE STOCK OPTIONS" under Section 422 of the Code to the maximum extent possible under the Code, subject to Executive satisfying applicable employment and holding period requirements under the Code.

TRANSFERABILITY. Executive shall not be entitled to assign, hypothecate, alienate, pledge or otherwise transfer the Share Options except to a member of Executive's Immediate Family or an entity controlled by Executive or Executive's Immediate Family (other than Share Options intended to be incentive stock options within the meaning of Section 422 of the Code which shall not be transferable). "IMMEDIATE FAMILY" shall mean a spouse, child, parent, sibling or in-law. Any such transferee shall be bound by the terms of this Agreement and the Plan with respect to such Share Options.

(6) ADDITIONAL SHARE OPTIONS. The grant of additional share options ("ADDITIONAL SHARE OPTIONS") in an amount equal to 1% of the first \$120 million of equity (common or convertible preferred securities) ("NEW EQUITY") raised by the Company subsequent to October 15, 1998. The Additional Share Options shall be considered "Share Options" for purposes of this Agreement except that (i) such options shall be granted and shall vest as of the date of issuance of the New Equity; (ii) the per share exercise price of such options shall be equal to the per share issue price of the New Equity; and (iii) such options shall become and remain exercisable (or be immediately exercisable) in the same proportion and same manner and duration that the previously granted Share Options are already exercisable or become exercisable (E.G. if 25% of the previously granted Share Options have already become exercisable at the time the Additional Share Options are granted, 25% of all the Additional Share Options shall be immediately exercisable upon grant, with the balance of the Additional Share Options proportionally becoming exercisable on the same timetable as the previously granted Share Options). In addition, Executive shall be entitled to receive

such other share options as may be granted by the Board in its sole discretion.

(vii) LEGAL FEES AND COSTS. Payment of the Executive's reasonable legal fees incurred in connection with the preparation and negotiation of this Agreement, up to an aggregate maximum of \$35,000 for Executive, Daniel P. Friedman and David Schonberger.

#### 5. TERMINATION OF EMPLOYMENT AND CHANGE IN CONTROL.

(1) REASON FOR TERMINATION. Executive's employment hereunder may be terminated during the Employment Period under the following circumstances:

(1) CAUSE. The Company shall have the right to terminate Executive's employment for Cause upon Executive's: (A) conviction of, or plea of guilty or no contest to, an illegal act with respect to the Company; (B) conviction of, or plea of guilty or no contest to, a felony involving moral turpitude; or (C) Executive's willful and continued failure to use best efforts to substantially perform her duties hereunder (other than any such failure resulting from Executive's (x) incapacity due to Disability or (y) inability due to the unreasonableness of the duties requested to be performed) or willful misconduct or gross negligence in the performance of her duties hereunder for a period of thirty (30) days after written demand for substantial performance is delivered by the Company specifically identifying the manner in which the Company believes Executive has not substantially performed her duties or engaged in actions which constitute willful misconduct or gross negligence, PROVIDED, HOWEVER, that no termination for Cause shall occur unless a majority of the Board has voted to terminate Executive for Cause after Executive has received notice and an opportunity to cure the alleged Cause in accordance with this Paragraph 5(a)(i) and has failed to do so. If the Executive is terminated for Cause, the date of termination shall be the date such written demand is delivered. Additionally, no act, or failure to act, on Executive's part shall be considered "WILLFUL" unless done, or omitted to be done, by her (I) not in good faith and (II) without reasonable belief that her action or omission was in furtherance of the interests of the Company.

(2) DEATH. Executive's employment hereunder shall terminate upon her death.

(3) **DISABILITY.** The Company shall have the right to terminate Executive's employment due to "Disability" in the event that there is a determination by the Company, upon the advice of an independent qualified physician mutually selected by Executive and the Company, that Executive has become physically or mentally incapable of performing her duties under this Agreement and such disability has disabled Executive for a period of one hundred eighty (180) days out of three hundred and sixty (360) days. (1)

(4) **GOOD REASON.** Executive shall have the right to terminate her employment for "Good Reason": (A) upon the occurrence of any material breach of this Agreement by the Company which shall include but not be limited to: (1) an assignment to Executive of duties materially inconsistent with Executive's status as Executive Vice President or a material and adverse alteration in the nature of, or material diminution in, Executive's duties and/or responsibilities, reporting obligations, titles or authority; (2) upon a reduction in Executive's Annual Base Salary or a material reduction in other benefits (not affecting the Company's executives generally) or a failure to pay such amounts when due; and (3) upon the relocation of the Company's principal executive offices or Executive's own office location to a location outside of Manhattan, it being acknowledged that the Company shall establish an office in Manhattan although as of the date hereof the Company does not yet have such an office; (B) upon the Company's failure to nominate Daniel P. Friedman ("FRIEDMAN") for election to the Board of Trustees or the Company's failure to use its reasonable best efforts to elect Friedman to the Board; (C) upon Friedman being forced to resign from the Board without Cause; (D) upon Friedman's termination of his Employment Agreement for Good Reason; (E) upon the Company being placed into voluntary or involuntary bankruptcy; or (F) the Company's failure to obtain shareholder approval pursuant to Paragraph 4(c)(v); **PROVIDED, HOWEVER,** that no termination for Good Reason shall occur unless the Company has received notice from Executive of termination for Good Reason and the Company has failed to cure such alleged action which may have given rise to Executive's right to terminate for Good Reason within thirty (30) days after written notice of such alleged actions is delivered to the Company specifically identifying such alleged actions.



Any dispute between the parties as to an alleged breach by the Company as set forth in clause (A)(1) above shall be resolved by arbitration pursuant to Paragraph 11.

(5) WITHOUT CAUSE. The Company shall have the right to terminate the Executive's employment hereunder without Cause subject to the terms and conditions of this Agreement.

(6) WITHOUT GOOD REASON. The Executive shall have the right to terminate her employment hereunder without Good Reason subject to the terms and conditions of this Agreement.

(7) CHANGE IN CONTROL. Executive shall have the right to terminate her employment hereunder following a Change in Control. For purposes of this Agreement "Change in Control" shall mean that any of the following events has occurred: (1)

(A) An acquisition (other than directly from the Company) of any voting securities of the Company (treating all classes of outstanding voting securities or other securities convertible into voting securities as if they were converted into voting securities) (the "VOTING SECURITIES") by any "person", "entity" or "group of affiliated persons" (as such terms are used for purposes of Section 13(d) or 14(d) (collectively, "PERSONS") of the Securities Exchange Act of 1934, as amended (the "1934 Act") (other than Gotham Partners, L.P. ("GOTHAM"), Apollo Real Estate Advisors, L.P. ("APOLLO") or any affiliate of Gotham or Apollo or entity in which Gotham or Apollo own at least a 50% interest (collectively, the "GOTHAM/APOLLO ENTITIES")) immediately after which such Person has "Beneficial Ownership" (within the meaning of Rule 13d-3 promulgated under the 1934 Act and irrespective of any vesting or waiting periods) of thirty (30%) percent or more of the combined voting power of the Company's then outstanding Voting Securities; provided, however, that in determining whether a Change in Control has occurred, Voting Securities which are acquired in a "Non-Control Acquisition" (as hereinafter defined) shall not constitute an acquisition which would cause a Change in Control. A "NON-CONTROL ACQUISITION" shall mean an acquisition by (1) an employee benefit plan (or a trust forming a part thereof) maintained by (x) the

Company or (y) any corporation or other Person of which a majority of its voting power or its equity securities or equity interest is owned directly or indirectly by the Company (a "Subsidiary"), (2) the Company or any Subsidiary, or (3) any Person in connection with a "Non-Control Transaction."

(B) Six (6) of the ten (10) individuals who were appointed to the Board after April 1, 1998 (the "INCUMBENT BOARD") cease for any reason to be members of the Board; PROVIDED, HOWEVER, that if the election, or nomination for election by the Company's shareholders, of any new trustee was approved by Friedman, such new trustee shall, for purposes of this Agreement, be considered as a member of the Incumbent Board.

(C) A merger, consolidation or reorganization involving the Company, unless

(1) the shareholders of the Company, immediately before such merger, consolidation or reorganization, own, directly or indirectly, immediately following such merger, consolidation or reorganization, more than seventy (70%) percent of the combined voting power of the outstanding Voting Securities of the entity resulting from such merger or consolidation or reorganization (the "SURVIVING ENTITY") in substantially the same proportion as their ownership of the Voting Securities immediately before such merger, consolidation or reorganization, and

(2) the individuals who were members of the Incumbent Board immediately prior to the execution of the agreement providing for such merger, consolidation or reorganization constitute at least two-thirds of the members of the board of directors of the Surviving Entity or an entity beneficially owning, directly or indirectly, a majority of the Voting Securities of the Surviving Entity, and

(3) no Person (other than the Company, any Subsidiary, any employee benefit plan (or any trust forming a part thereof) maintained by the Company, the Surviving Entity or any Subsidiary, or any Person who, immediately prior to such merger, consolidation or reorganization had Beneficial Ownership of thirty (30%) percent or

more of the then outstanding Voting Securities) owns, directly or indirectly, thirty percent or more of the combined voting power of the Surviving Entity's then outstanding voting securities.

A transaction described in clauses (1) through (3) shall herein be referred to as a "Non-Control Transaction".

(D) A complete liquidation or dissolution of the Company.

(E) the Company makes aggregate cash or non-cash distributions to its shareholders of the proceeds from the sales of assets equal to or greater than \$4.00 per Common Share and, immediately following such distribution the "Net Asset Value" of the Company is less than \$150 million. "NET ASSET VALUE" shall be the fair market value of all of the Company's assets (as determined by mutual agreement of Executive and the Company or, if the parties cannot agree, by an arbitrator in accordance with Paragraph 11) less all Company liabilities.

Notwithstanding the foregoing, a Change in Control shall not be deemed to occur solely because any Person (the "SUBJECT PERSON") acquired Beneficial Ownership of more than the permitted amount of the outstanding Voting Securities as a result of the acquisition of Voting Securities by the Company which, by reducing the number of Voting Securities outstanding, increases the proportional number of shares Beneficially Owned by the Subject Person, provided that if a Change in Control would occur (but for the operation of this sentence) as a result of the acquisition of Voting Securities by the Company, and after such share acquisition by the Company, the Subject Person becomes the Beneficial Owner of any additional Voting Securities which increases the percentage of the then outstanding Voting Securities Beneficially Owned by the Subject Person, then a Change in Control shall occur.

(2) NOTICE OF TERMINATION. Any termination of Executive's employment by the Company or any such termination by Executive (other than on account of death) shall be communicated by written Notice of Termination to the other party hereto. For purposes of this Agreement, a "NOTICE OF TERMINATION" shall mean a notice which shall indicate the specific termination provision in this Agreement relied upon and shall set forth in reasonable detail the facts and circumstances claimed to provide a basis for termination of Executive's

employment under the provision so indicated. In the event of the termination of Executive's employment on account of death, written Notice of Termination shall be deemed to have been provided on the date of death.

## 6. COMPENSATION UPON TERMINATION OF EMPLOYMENT.

(1) **BY THE COMPANY FOR CAUSE OR BY EXECUTIVE WITHOUT GOOD REASON.** In the event the Company terminates Executive's employment for Cause or Executive terminates her employment without Good Reason, the Company shall pay Executive and Executive shall be entitled to receive any (i) unpaid Annual Base Salary at the rate then in effect accrued through and including the date of termination and (ii) reimbursement of expenses incurred prior to the date of termination ("EXPENSE REIMBURSEMENT").

Except for any rights which Executive may have to unpaid salary amounts, the LTC Payment (as defined herein) and Expense Reimbursement through and including the date of termination and Exercisable Options (and, with respect to a termination by Executive without Good Reason, any Share Options which have not yet become exercisable on the date of termination), the Company shall have no further obligations hereunder following such termination other than pursuant to Paragraphs 6(d), 10 and 12. The aforesaid amounts shall be payable in full immediately upon such termination.

(2) **UPON DEATH OR DISABILITY.** In the event of termination of Executive's employment as a result of either Executive's death or Disability, the Company shall pay to Executive, her estate or her personal representative (i) the accrued but unpaid Annual Base Salary at the rate then in effect; (ii) earned but unpaid incentive compensation or bonuses for completed performance periods; (iii) an amount equal to 12 months of the Annual Base Salary at the rate then in effect (the "SALARY PAYMENT"); and (iv) Expense Reimbursement. The aforesaid amounts shall be payable in cash without discount for early payment, at the option of Executive, her estate or her personal representative, either in full immediately upon such termination or monthly over the Unexpired Employment Period (the "PAYMENT ELECTION"). In the event of termination of employment due to Disability, Executive shall also receive continuation of health coverage through the end of the Unexpired Employment Period on the same basis as health coverage is provided by the Company for active employees and as may be amended from time to time ("MEDICAL CONTINUATION").

Except for any rights which Executive may have hereunder including the accrued Annual Base Salary, the Salary Payment, Exercisable Options, the LTC Payment, Expense Reimbursement and in the event of a termination of employment due to Disability, Medical Continuation, the Company shall have no further obligations hereunder following such termination other than

pursuant to Paragraphs 6(d), 10 and 12. The foregoing payments shall be in addition to any benefits to which Executive may be entitled under any insurance maintained by the Company.

(3) BY THE COMPANY WITHOUT CAUSE OR BY EXECUTIVE FOR GOOD REASON OR IN THE EVENT OF A CHANGE IN CONTROL.

(i) NO BANKRUPTCY. In the event the Company terminates Executive's employment for any reason other than Cause, death or Disability or Executive terminates her employment for Good Reason (other than as set forth in Paragraph 6(c)(ii)), or in the event of a Change of Control, the Company shall pay to Executive and Executive shall be entitled to receive the sum total of: (A) the accrued but unpaid Annual Base Salary at the rate then in effect; (B) earned but unpaid incentive compensation and/or bonuses for completed performance periods; (C)(1) if the effective date of termination is on or prior to the eighteen (18) month anniversary of the commencement of the Employment Term, an amount equal to three (3) times the Annual Base Salary at the rate then in effect or (2) if the effective date of termination is after the eighteen (18) month anniversary of the commencement of the Employment Term, an amount equal to two and one-half (2.5) times the Annual Base Salary at the rate then in effect (as applicable, the "TERMINATION PAYMENT"); and (D) continuation of Executive's participation in all benefit plans, programs or arrangements of the Company (except tax-qualified plans), including, without limitation, Medical Continuation, for a period of two years following such termination. The aforesaid amount shall be payable in cash without discount for early payment, at the option of Executive, in accordance with the Payment Election.

(ii) BANKRUPTCY. Executive may not terminate employment for Good Reason due to the Company being placed in bankruptcy until the eighteen (18) month anniversary thereof. If Executive thereafter terminates this Agreement, the Company shall pay to Executive and Executive shall be entitled to receive the same payments and benefits set forth in Paragraph 6(c)(i); PROVIDED, HOWEVER, that if the date of being placed in bankruptcy is (x) on or prior to the eighteen (18) month anniversary of the commencement of the Employment Term, Executive shall receive the Termination Payment set forth in Paragraph 6(c)(i)(C)(1) and (y) after the eighteen (18) month anniversary of the commencement of the Employment Term, Executive shall receive the Termination Payment set forth in Paragraph 6(c)(i)(C)(2).

(iii) SECTION 280G. Notwithstanding anything contained in this Agreement to the contrary, to the extent that any payment or distribution of any type to or for Executive by the Company, any affiliate of the Company, any person who acquires ownership or effective control of the Company or ownership of a substantial portion of the Company's assets (within the meaning of Section 280G of the Code and the

regulations thereunder), or any affiliate of such person, whether paid or payable or distributed or distributable pursuant to the terms of this Agreement or otherwise (the "TOTAL PAYMENTS") is or will be subject to the excise tax imposed under Section 4999 of the Code (the "EXCISE TAX"), then the Total Payments shall be reduced (but not below zero) if and to the extent that a reduction in the Total Payments would result in the Executive retaining a larger amount, on an after-tax basis (taking into account federal, state and local income taxes and the Excise Tax), than if the Executive received the entire amount of such Total Payments. Executive shall have the right to specify the order in which the Company shall reduce or eliminate the Total Payments in order to effectuate the foregoing.

Except for any rights which Executive may have hereunder including the accrued Annual Base Salary, the Termination Payment, Exercisable Options, the LTC Payment, Expense Reimbursement and Medical Continuation, the Company shall have no further obligations hereunder following such termination other than pursuant to Paragraphs 6(d), 10 and 12.

(4) GENERAL. The parties agree to cooperate to structure all termination payments made pursuant to this Agreement in a manner so that such payments are not subject to the Excise Tax.

#### 7. MITIGATION; PAYMENTS PENDING RESOLUTION OF DISPUTES.

Executive shall not be required to mitigate amounts payable under this Agreement by seeking other employment or otherwise, and there shall be no offset against amounts due Executive under this Agreement on account of subsequent employment. Amounts owed to Executive under this Agreement shall not be offset by any claims the Company may have against Executive and such payment shall not be affected by any other circumstances, including, without limitation, any counterclaim, recoupment, defense, or other right which the Company may have against Executive or others. During the pendency of any dispute between the Company and Executive with respect to the termination of this Agreement, the Company shall establish and maintain an escrow account ("ESCROW ACCOUNT") with Battle Fowler LLP ("ESCROW AGENT") pursuant to an agreement reasonably acceptable to Executive and the Escrow Agent. The Company shall pay into the Escrow Account from time to time the compensation and cash-value of the benefits which would otherwise be payable to Executive if there were no dispute. Upon resolution of the dispute, the Escrow Agent shall pay the funds in the Escrow Account as required by the court or arbitrator with jurisdiction over the dispute or in accordance with the joint instructions of the parties.

#### 8. NON-COMPETE.

(1) NON-COMPETITION. Executive agrees that, without the prior written consent of a majority of the Board and in accordance with applicable law, and except as provided in subparagraph 8(b), during the Employment Period, Executive shall not invest, manage or otherwise be engaged in commercial real estate.

(2) EXCLUDED ACTIVITIES. Nothing contained in this Paragraph 8 shall preclude Executive from:

(1) Continuing to own, manage in accordance with past practices or make additional capital contributions to Executive's existing investments listed on SCHEDULE A attached hereto.

(2) making passive investments of 5% or less in publicly listed or traded real estate companies.

#### 9. NO SOLICITATION; CONFIDENTIALITY.

(1) NO SOLICITATION. During the Restricted Period (as defined herein), Executive shall not, nor cause any other person to, without the prior written consent of the Board, directly or indirectly, solicit for employment, employ in any capacity or make an unsolicited recommendation to any other person that it employ or solicit for employment any person who is or was, at any time during the Employment Period or the Restricted Period, an officer, executive or key employee of the Company or of any of its affiliates (other than Friedman and David Schonberger, whose solicitation, employment or recommendation by Executive shall not be prohibited by the terms of this Agreement). As used in this Agreement, "RESTRICTED PERIOD" shall mean the six (6) months following Executive's termination of employment for any reason.

(2) CONFIDENTIALITY. Executive acknowledges that, through her status as Executive Vice President of the Company, she has, and will have, possession of Confidential Information (as defined herein) as to the business of the Company. Executive agrees that all such Confidential Information constitutes a vital part of the business of the Company and its affiliates and is by its nature trade secrets and confidential information proprietary to the Company and its affiliates. Executive agrees that she shall not divulge, communicate, furnish or make accessible (whether orally or in writing or in books, articles or any other medium) to any individual, firm, partnership, corporation or other entity or person, any knowledge or information with respect to Confidential Information directly or indirectly relating to the business of the Company or any of its affiliates. The term "CONFIDENTIAL INFORMATION" shall mean any information not generally known in the relevant trade or industry or otherwise not generally available to the public, which was obtained from the Company or which was learned, discovered, developed,

conceived, originated or prepared during or as a result of the performance of any services by Executive on behalf of the Company. (1)

(3) RETURN OF COMPANY DOCUMENTS. All memoranda, notes, lists, notebooks, records and other documents or papers (and all copies thereof), including such items stored in computer memories, portable computers and the like, on microfiche, disk or by any other means, made or compiled by or on behalf of Executive or made available to Executive relating to the Company are and shall be the Company's property and shall be delivered to the Company promptly upon the termination of Executive's employment with the Company or at any other time after such termination on request.

(4) UNENFORCEABILITY. The provisions contained in Paragraphs 8 and 9 as to the time periods and scope of activities, persons or entities affected shall be deemed divisible so that, if any provision contained in Paragraphs 8 or 9 is determined to be invalid or unenforceable, such provision shall be deemed modified so as to be valid and enforceable to the full extent lawfully permitted.

(5) REMEDIES. Executive agrees that (i) the provisions of Paragraphs 8 and 9 are reasonable and necessary for the protection of the Company; (ii) the Company would not have entered into this Agreement unless the Executive agreed to the inclusion of such provisions; (iii) such provisions may not be adequately enforced by an action for damages and (iv) in the event of a breach thereof by Executive, the Company shall be entitled to apply for and obtain injunctive relief in any court of competent jurisdiction to restrain the breach or threatened breach of such violation or otherwise to enforce specifically such provisions against such violation, without the necessity of the posting of any bond by the Company. The forgoing remedies are in addition to any rights the Company may have against Executive for damages in the event Executive breaches any of the provisions of Paragraphs 8 and 9.

#### 10. PREVIOUS EMPLOYER.

(1) COMMITMENT TO PAY/FUND. The Company agrees to take the following actions with respect to the following commitments with respect to Executive's immediately prior employer, Enterprise Asset Management, Inc. ("EAM") and Executive:

(i) LONG-TERM COMPENSATION ("LTC"). The Company shall pay the LTC to Executive as follows: (x) 1/3 on commencement of the Employment Period and 1/3 on each of the second and fourth anniversaries of the commencement of the Employment Period and (y) if this Agreement is terminated for any reason,



Company shall make a lump sum payment equal to the present value (discounted at 10% per annum) of any unpaid LTC (the "LTC PAYMENT"). Executive shall reimburse Company to the extent Executive receives payment from EAM of LTC paid by the Company.

(ii) LOAN GUARANTEES. If EAM fails to continue to guarantee existing loans owed by Executive, the Company shall provide replacement loans on the same or better terms and conditions as the existing loans ("REPLACEMENT LOANS").

(iii) LOAN REPAYMENT. If EAM demands repayment prior to maturity of existing loans to Executive from EAM, the Company shall provide replacement loans on the same or better terms and conditions as the existing loans ("NEW LOANS").

Executive's LTC, guarantees and loans are listed in SCHEDULE B attached hereto.

Notwithstanding the foregoing, the Replacement Loans and New Loans shall have a term of no less than three (3) years with principal payable from time to time from the net after-tax proceeds received by Executive (the "NET PROCEEDS") from (i) the LTC Payment; (ii) the exercise of Share Options; (iii) payments due to Executive from the Company upon termination of Executive's employment under this Agreement; and (iv) the assets which were purchased with the proceeds from the loans which have been replaced by the Replacement Loan or the New Loan (collectively, the "COLLATERAL"). The Company may offset Net Proceeds payable by it to Executive against the Replacement Loan or the New Loan and any such offset shall reduce the then outstanding principal amount of such loan. The Replacement Loans and New Loans shall be nonrecourse to Executive and the Company's sole recourse for the repayment of any Replacement Loans or New Loans shall be to the Collateral.

(2) INDEMNITY. In the event the Executive is made party or threatened to be made a party to any action, suit or proceeding, whether civil, criminal, administrative or investigative (a "PROCEEDING"), by EAM, its officers, directors, equity owners or Affiliates, by reason of Executive's having negotiated or entered into this Agreement or otherwise having become an employee of the Company, the Company shall indemnify, hold harmless and defend Executive against any and all claims, demands, suits, judgments, assessments and settlements including all expenses incurred or suffered by Executive in connection therewith (including, without limitation, all legal fees incurred using counsel reasonably acceptable to Executive) (collectively, "DAMAGES"). Expenses incurred by Executive in connection with

any Proceeding shall be paid by the Company in advance upon request of Executive that the Company pay such expenses.

(3) REPRESENTATIONS. Executive hereby represents and warrants to the Company that Executive has not entered into any written or oral agreement for employment with EAM or any other person or entity other than the letter agreement dated February 1, 1998 regarding the payment of LTC.

(4) SURVIVAL. The provisions of this Paragraph shall remain in effect after this Agreement is terminated irrespective of the reasons for termination.

#### 11. ARBITRATION.

The parties hereto will endeavor to resolve in good faith any controversy, disagreement or claim arising between them with respect to the interpretation, performance or operation of Paragraphs 5(a)(iv)(A)(1) and 5(a)(vii)(E) of this Agreement. If they are unable to do so, any such controversy, disagreement or claim will be submitted to binding arbitration, for final resolution without appeal, by either party giving written notice to the other of the existence of a dispute with respect to such Paragraph which it desires to have arbitrated. The arbitration will be conducted in New York, New York by a panel of three (3) arbitrators and will be held in accordance with the rules of the American Arbitration Association. Of the three arbitrators, one will be selected by the Company, one will be selected by Executive and the third will be selected by the two arbitrators so selected. Each party will notify the other party of the arbitrator selected by her or it within fifteen (15) days after the giving of the written notice referred to in this Paragraph 11. The decision and award of the arbitrators must be in writing and will be final and binding upon the parties hereto. Judgment upon the award may be entered in any court having jurisdiction thereof, or application may be made to such court for a judicial acceptance of the award and an order of enforcement, as the case may be. Subject to the provisions of Paragraph 12 (b), the expenses of arbitration will be borne in accordance with the determination of the arbitrators.

#### 12. INDEMNIFICATION/LEGAL FEES/"KEY MAN" INSURANCE.

(1) INDEMNIFICATION. In the event the Executive is made party or threatened to be made a party to any Proceeding, by reason of Executive's employment with or serving as an officer or director of the Company, the Company shall indemnify, hold harmless and defend Executive to the fullest extent authorized by Ohio law, as the same exists and may hereafter be amended, against any and all Damages and such indemnification shall continue as to Executive even after Executive is no longer employed by the Company and shall inure to the benefit of her

heirs, executors, and administrators. Notwithstanding the foregoing, Executive shall not be entitled to indemnification pursuant to this Paragraph 12(a) if a court or other tribunal conclusively determines that Executive engaged in actions in connection with Executive's employment with the Company which were committed in bad faith, were the result of active and deliberate dishonesty, or constitute willful misconduct, fraud or gross negligence.

Expenses incurred by Executive in connection with any Proceeding referred to in this Paragraph 12 shall be paid by the Company in advance upon request of Executive that the Company pay such expenses; but only in the event that Executive shall have delivered in writing to the Company an undertaking to reimburse the Company for expenses with respect to which Executive is not entitled to indemnification.

The provisions of this Paragraph shall remain in effect after this Agreement is terminated irrespective of the reasons for termination. The indemnification provisions of this Paragraph shall not supersede or reduce any indemnification provided to Executive under any separate agreement, or the by-laws of the Company since it is intended that this Agreement shall expand and extend the Executive's rights to receive indemnity.

The Company shall maintain in effect during the Employment Period a directors' and officers' liability insurance policy, with a policy limit of at least \$10,000,000, subject to customary exclusions, with respect to claims made against officers and directors of the Company.

(2) **LEGAL FEES.** Except as set forth below, if any contest or dispute shall arise between the Company and Executive regarding or as a result of any provision of this Agreement, the Company shall pay, or reimburse Executive for, all legal fees and expenses reasonably incurred by Executive in connection with such contest or dispute; **PROVIDED, HOWEVER,** that if Executive is not successful in respect of substantially all of Executive's claims pursued or defended in connection with such contest or dispute, Executive shall pay or reimburse the Company for all such fees and expenses advanced by the Company. Executive shall pay the first \$25,000 of her fees or expenses as they are incurred and the Company shall pay all such fees and expenses over \$25,000 as they are incurred. If Executive is successful in respect of substantially all of such claims, the Company shall reimburse Executive for any amounts paid by Executive as soon as practicable following the final resolution of such contest or dispute.

(3) **KEY MAN INSURANCE.** Executive shall cooperate with, and take such actions as may be reasonably requested by,

the Company in the event the Company determines to obtain "key man" insurance with respect to Executive.

### 13. SUCCESSORS AND ASSIGNS.

(1) COMPANY. Unless Executive elects to terminate this Agreement as a result of a Change in Control, the Company shall require any successor (whether direct or indirect, by purchase, merger, consolidation or otherwise) to all or substantially all of the business and/or assets of the Company, to expressly assume and agree to perform this Agreement in the same manner and to the same extent that the Company would be required to perform it if no such succession had taken place.

(2) EXECUTIVE. This Agreement and all rights of Executive hereunder may be transferred only by will or the laws of descent and distribution. Upon Executive's death, this Agreement and all rights of Executive hereunder shall inure to the benefit of and be enforceable by Executive's beneficiary or beneficiaries, personal or legal representatives, or estate, to the extent any such person succeeds to Executive's interests under this Agreement. Executive shall be entitled to select and change a beneficiary or beneficiaries to receive any benefit or compensation payable hereunder following Executive's death by giving Company written notice thereof. If Executive should die following the date of termination while any amounts would still be payable to him hereunder if he had continued to live, all such amounts, unless otherwise provided herein, shall be paid in accordance with the terms of this Agreement to such person or persons so appointed in writing by Executive, including, without limitation, under any applicable plan, or otherwise to her legal representatives or estate.

### 14. MODIFICATION OR WAIVER.

No amendment, modification, waiver, termination or cancellation of this Agreement shall be binding or effective for any purpose unless it is made in a writing signed by the party against whom enforcement of such amendment, modification, waiver, termination or cancellation is sought. No course of dealing between or among the parties to this Agreement shall be deemed to affect or to modify, amend or discharge any provision or term of this Agreement. No delay on the part of the Company or Executive in the exercise of any of their respective rights or remedies shall operate as a waiver thereof, and no single or partial exercise by the Company or Executive of any such right or remedy shall preclude other or further exercise thereof. A waiver of right or remedy on any one occasion shall not be construed as a bar to or waiver of any such right or remedy on any other occasion.

The respective rights and obligations of the parties hereunder shall survive the Executive's termination of employment and termination of this Agreement to the extent necessary for the intended preservation of such rights and obligations.

#### 15. NOTICES.

All notices or other communications required or permitted hereunder shall be made in writing and shall be deemed to have been duly given if delivered by hand or delivered by a recognized delivery service or mailed, postage prepaid, by express, certified or registered mail, return receipt requested, and addressed to the Company at the address set forth above or Executive at her address as set forth in the Company records (or to such other address as shall have been previously provided in accordance with this Paragraph 15).

#### 16. GOVERNING LAW.

This agreement will be governed by and construed in accordance with the laws of the State of New York without regard to principles of conflicts of laws thereunder.

#### 17. SEVERABILITY.

Whenever possible, each provision and term of this Agreement shall be interpreted in such manner as to be effective and valid under applicable law, but if any provision or term of this Agreement shall be held to be prohibited by or invalid under such applicable law, then, such provision or term shall be ineffective only to the extent of such prohibition or invalidity, without invalidating or affecting in any manner whatsoever the remainder of such provisions or term or the remaining provisions or terms of this Agreement.

#### 18. COUNTERPARTS.

This Agreement may be executed in separate counterparts, each of which is deemed to be an original and both of which taken together shall constitute one and the same agreement.

#### 19. HEADINGS.

The headings of the Paragraphs of this Agreement are inserted for convenience only and shall not be deemed to constitute a part hereof and shall not affect the construction or interpretation of this Agreement.

#### 20. ENTIRE AGREEMENT.

This Agreement constitutes the entire agreement of the parties with respect to the subject matter hereof and supersedes

all other prior agreements and undertakings, both written and oral, among the parties with respect to the subject matter hereof.

## 21. EXCULPATION.

Notwithstanding anything contained herein to the contrary, this Agreement is made and executed on behalf of the Company by its officer(s) on behalf of the trustees thereof, and none of the trustees or any additional or successor trustee hereafter appointed, or any beneficiary, officer, employee or agent of the Company shall have any liability in her personal or individual capacity, but instead, Executive shall look solely to the property and assets of the Company for satisfaction of claims of any nature arising from or in connection with this Agreement.

**[SIGNATURE PAGE FOLLOWS]**

IN WITNESS WHEREOF, the undersigned have executed this Agreement as of the date first above written.

**COMPANY:**

**FIRST UNION REAL ESTATE EQUITY AND  
MORTGAGE INVESTMENTS**

By:

Name:

Title:

**EXECUTIVE:**

---

**Schedule A**

**Existing Investments**

**Anne Zahner**

**Investments Owned**

22. Greenburgh, NY

23. NYC Holdings

24. Angelene

25. Chester Apartments

26. Emax Securities (various entities)

27. Peru Mall

**Investments Managed**

None



**Schedule B**

**Anne Zahner**

Long Term Compensation	\$ 27,184.56
Loans from EAM	None
Loans Guaranteed by EAM	\$139,000.00

**Exhibit 10(ak)**

**EMPLOYMENT AGREEMENT**

**FOR**

**DAVID SCHONBERGER**

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**SCHEDULES**

Schedule A  
Schedule B

Existing Investments  
Prior Employer Agreements

## EMPLOYMENT AGREEMENT

THIS EMPLOYMENT AGREEMENT (the "AGREEMENT") is entered into as of November 2, 1998, by and between DAVID SCHONBERGER, an individual residing in the State of New York ("EXECUTIVE"), and FIRST UNION REAL ESTATE EQUITY AND MORTGAGE INVESTMENTS, an Ohio business trust with offices at 55 Public Square, Suite 1900, Cleveland, Ohio 44113 (the "COMPANY").

### RECITALS

WHEREAS, the Company desires to employ Executive as Executive Vice President and Executive desires to be employed by the Company as Executive Vice President.

NOW, THEREFORE, in consideration of the premises and the mutual covenants and agreements set forth herein, the parties hereby agree as follows:

#### 1. EMPLOYMENT

The Company hereby agrees to employ Executive, and Executive hereby agrees to accept such employment during the period and upon the terms and conditions set forth in this Agreement.

#### 2. EMPLOYMENT PERIOD

(1) EMPLOYMENT PERIOD. Except as otherwise provided in this Agreement to the contrary, the terms and conditions of this Agreement shall be and remain in effect during the period of employment (the "EMPLOYMENT PERIOD") established under this Paragraph 2. The initial Employment Period shall be for a term commencing on the date of this Agreement and ending on the fourth anniversary of the date of this Agreement, unless earlier terminated as provided in this Agreement. Immediately following the execution hereof, the Executive shall resign from all positions as an employee, officer and director of his current employer and its affiliates.

(2) UNEXPIRED EMPLOYMENT PERIOD. If Executive's employment with the Company is terminated, for purposes of this Agreement the term "UNEXPIRED EMPLOYMENT PERIOD" shall mean the period commencing on the date of such termination and ending on the last day of the Employment Period.

### 3. SERVICES/PLACE OF EMPLOYMENT

(1) SERVICES. During the Employment Period, Executive shall hold the position of Executive Vice President. Executive shall devote his best efforts and such business time, skill and attention exclusively to the business of the Company (other than absences due to vacation, illness, disability or approved leave of absence) as is necessary to perform such duties as are customarily performed by similar executive officers together with such other reasonable duties as may be more specifically enumerated from time to time by the Company's board of trustees ("BOARD OF TRUSTEES" or "BOARD") PROVIDED, HOWEVER, that the foregoing is not intended to preclude Executive from (i) owning and managing personal investments, including real estate investments, in accordance with Paragraph 8 hereof or (ii) engaging in charitable activities and community affairs, provided that (x) with respect to the activities referenced in clause (ii), Executive obtains the prior approval of the Board as to the amount of time Executive will devote to such activities and (y) the performance of the activities referred to in clauses (i) and (ii) of this Paragraph 3(a) does not prevent Executive from devoting sufficient business time to the Company to carry out Executive's duties as Executive Vice President.

(2) PLACE OF EMPLOYMENT. The principal place of employment of Executive shall be at the Company's executive offices in New York (Manhattan County), New York.

### 4. Compensation and Benefits

(1) SALARY. During the first twelve (12) months of the Employment Period, the Company shall pay Executive an annual base salary in the amount of \$200,000 payable in accordance with the Company's regular payroll practices. Executive's annual base salary shall be reviewed annually in accordance with the policy of the Company and shall be subject to upward adjustment based upon, among other things, Executive's performance, as determined in the sole discretion of the Board PROVIDED HOWEVER that the annual increase in base salary for each year of the Term shall be at least 5% over the annual base salary for the previous year (the annual base salary as adjusted from time to time is hereinafter referred to as the "ANNUAL BASE SALARY"). In no event shall Executive's Annual Base Salary in effect at a particular time be reduced without his prior written consent.

(2) TAXES AND WITHHOLDING. The Company shall have the right to deduct and withhold from all compensation all social security and other federal, state and local taxes and charges which currently are or which hereafter may be required by law to be so deducted and withheld.

(3) **ADDITIONAL BENEFITS.** In addition to the other compensation payable pursuant to this Agreement, Executive shall be entitled to the following.

(1) **BENEFITS.** All fringe benefits and perquisites as are generally made available from time to time to all employees and/or to executives of the Company generally and to participate in any pension, profit-sharing or similar plan or program established from time to time by the Company for the benefit of its employees and/or executives generally, subject to the provisions of such plans. In any event, Executive's health insurance coverage shall commence on the date of this Agreement (or the Company shall reimburse Executive for COBRA payments until such coverage can commence).

(2) **MEMBERSHIP FEES.** Membership fees and costs for reasonable and customary memberships in professional organizations.

(3) **EXPENSE REIMBURSEMENT.** Reimbursement for reasonable business expenses incurred by Executive in furtherance of the interests of the Company, subject to the reasonable procedures established by the Company from time to time with respect to substantiation and approval.

(4) **VACATION AND SICK LEAVE/PERSONAL DAYS.** Such periods of paid vacation and sick leave/personal days allowance each year (not less than four (4) weeks vacation and seven (7) days of sick leave/personal days per full twelve (12) month period) that are consistent with the Company's vacation and sick leave/personal days policy for senior management.

(5) **SHARE OPTIONS. GRANT.** The grant upon execution of this Agreement of share options ("SHARE OPTIONS") to acquire 360,000 shares of the Company's common shares of beneficial interest ("COMMON SHARES").

The parties acknowledge that the Company's 1994 Long Term Incentive Performance Plan (the "PLAN") does not contain a sufficient number of Common Shares issuable under the Plan to cover the full amount of the Share Options as of the date of this Agreement. Notwithstanding the foregoing, the Company hereby grants Executive the full number of Share Options subject to the condition that the grant of such Share Options ("CONDITIONAL OPTIONS") shall be conditioned on

the approval by the shareholders of the Company of such grant (if required) and amendments to the Plan increasing the number of Common Shares issuable thereunder and otherwise permitting the Share Options and Additional Share Options (as defined herein) to be issued in accordance with the terms of this Agreement. The Company shall use its reasonable best efforts to obtain such approval. If the Company has not obtained such shareholder approval by June 30, 1999, such failure shall permit Executive to terminate this Agreement for Good Reason in accordance with the terms of this Agreement, in which case such Conditional Options shall be forfeited.

**VESTING/EXERCISE.** All of the Share Options shall vest as of the date of this Agreement but may only be exercised as follows: twenty-five (25%) percent of each of the \$6.50 Options (as defined herein) and \$8.50 Options (as defined herein) shall become exercisable on each anniversary of the Employment Period whether or not the Executive is employed by the Company on such anniversary. Notwithstanding the foregoing, Share Options granted to Executive shall (I) become exercisable in full upon (a) a Change in Control (as defined herein); (b) a termination by the Company without Cause (as defined herein); (c) a termination by the Executive for Good Reason (as defined herein); or (d) the eighteen (18) month anniversary of the Company being placed into voluntary or involuntary bankruptcy if Executive has not terminated his employment prior to such eighteen (18) month anniversary; (II) become exercisable Pro Rata (as defined herein) in the event of a termination due to death or Disability (as defined herein) (the Share Options in clauses (I) and (II) being collectively defined together with any Share Options which have previously become exercisable by their terms, as the "EXERCISABLE OPTIONS"); and (III) be forfeited in full (whether exercisable (unless previously exercised) or unexercisable) upon a termination by the Company for Cause (as defined herein). "PRO RATA" means an amount of Share Options (half of which shall be \$6.50 Options and half of which shall be \$8.50 Options) equal to (x) the percentage equal to (i) the number of days from the commencement of the Exercise Year (as defined herein) through the date of the termination event divided by (ii) 365;

MULTIPLIED BY (y) the number of Share Options which would otherwise have become exercisable during the Exercise Year in which the termination event occurs. "EXERCISE YEAR" means the twelve months commencing on the last date prior to termination on which the Share Options became exercisable (or from commencement of the Employment Period if termination occurs during the first twelve months of such commencement).

The Company shall provide Executive 30 days' prior written notice of the record date for any dividends or other distributions being paid with respect to the Common Shares. If such dividend or other distribution would trigger Executive's right to terminate this Agreement due to a Change in Control (the "TRIGGER EVENT"), then, notwithstanding anything herein to the contrary, the Share Options shall become exercisable in full as of the date of such notice; PROVIDED, HOWEVER, that (i) any exercise of such Share Options by Executive shall only become effective upon the Trigger Event being consummated and (ii) if the Trigger Event is not consummated, any such Share Options which were not yet exercisable as of the date of the Trigger Event shall again become unexercisable until the date they would have otherwise become exercisable in accordance with the terms of this Agreement.

Notwithstanding anything herein to the contrary, if the exercise price adjustment (see below) results in the exercise price of a Share Option equaling zero, such Share Option shall immediately become exercisable.

EXERCISE PRICE. The option exercise price with regard to the Share Options granted shall be as follows: 50% at \$6.50 per Common Share (the "\$6.50 OPTIONS") and 50% at \$8.50 per Common Share (the "\$8.50 OPTIONS"). The exercise price of each Share Option will be adjusted (but not below zero) on each anniversary of its grant by an amount equal to (i) an increase of 10% per annum (compounded annually) MINUS (ii) all dividends or other distributions (including the value of non-cash dividends, including without limitation, share dividends and spin-off distributions) declared per Common Share for the applicable year. Notwithstanding the foregoing, the adjustment to the exercise price set forth in clause (i) in the preceding sentence shall



(x) not commence until the eighteen (18) month anniversary of the commencement of the Employment Period; and (y) be applied ratably at the time(s) Executive exercises the Share Options (e.g. if Share Options are exercised on the 20-month anniversary of the commencement of the Employment Term, the exercise price in effect on that date would be increased by 1.667% (2/12 of 10%) minus any dividends paid on or prior to the date of exercise (to the extent such dividends were not previously deducted)).

**OPTION EXERCISE TERM.** Subject to the terms of this Agreement, all Share Options shall be exercisable for 10 years following the date upon which they are granted unless they expire earlier in accordance with this Agreement. In the event of the non-renewal of this Agreement after the expiration of the Employment Period, a Change of Control (unless Executive does not terminate his employment under this Agreement in which event the Share Options shall remain exercisable until they would otherwise expire under the terms of this Agreement), a termination without Cause, a termination for Good Reason, death or a termination by reason of Disability, all Exercisable Options shall remain exercisable for six (6) months following such event after which they shall expire. In the event of a termination without Good Reason, (i) all Share Options which were already exercisable prior to the date of termination shall remain exercisable for thirty (30) days after such event of termination after which they shall expire, and (ii) all the Share Options which are not yet exercisable prior to the date of termination shall be exercisable for thirty (30) days after the date on which they become exercisable in accordance with the terms of this Agreement after which they shall expire (the "POST-EXERCISABLE Options").

Notwithstanding the foregoing, the option exercise term of all Share Options intended to be treated as incentive stock options shall be such shorter period of time as may be required for incentive stock option treatment pursuant to Section 422 of the Internal Revenue Code of 1986, as amended (the "CODE").

**COMPANY CALL OPTION.** With respect to the Post-Exercisable

Options, the Company shall have

the right (the "CALL OPTION") to require Executive to transfer the Post-Exercisable Options to the Company at any time after the date of termination by Executive of his employment Without Good Reason for a price equal to the "Exercise Spread" (as defined herein). If such Exercise Spread is zero or less, the Company may purchase the Post-Exercisable Options for no consideration. The Company shall provide written notice to Executive that it is exercising the Call Option and the date on which such notice is deemed to have been given under the terms of this Agreement shall be deemed the "VALUATION DATE". The "EXERCISE SPREAD" shall be (i) the difference between (a) the exercise price of a Post-Exercisable option and (b) the "Closing Price" of a Common Share on the Valuation Date. The "CLOSING PRICE" means (i) if the Common Shares are listed or admitted to trading on the New York Stock Exchange (the "NYSE"), the American Stock Exchange ("AMEX") any national securities exchange or the Nasdaq Stock Market ("NASDAQ"), the closing price on the Valuation Date, or if no such sale takes place on such day, the average of the closing bid and asked prices on such day; (ii) if the Common Shares are not listed or admitted to trading on the NYSE, the AMEX, any national securities exchange or the Nasdaq, the last reported sale price on the Valuation Date or, if no sale takes place on such day, the average of the closing bid and asked prices on such day, as reported by a reliable quotation source designated by the Company; or (iii) if the Common Shares are not listed or admitted to trading on the NYSE, the AMEX, any national securities exchange or the Nasdaq and no such last reported sale price or closing bid and asked prices are available, the average of the reported high bid and low asked prices on the Valuation Date, as reported by a reliable quotation source designated by the Company, or if there shall be no bid and asked prices on the Valuation Date, the average of the high bid and low asked prices, as so reported, on the most recent day (not more than five (5) days prior to the date in question) for which prices have been so reported; PROVIDED, HOWEVER, that if there are no bid and asked prices reported during the five (5) days prior to the date in question, the Closing Price of the Common Shares shall be determined by the independent trustees of the

Company acting in good faith on the basis of such quotations and other information as they consider, in their reasonable judgment, appropriate.

ISOS. Any Share Options granted hereunder shall be "INCENTIVE STOCK OPTIONS" under Section 422 of the Code to the maximum extent possible under the Code, subject to Executive satisfying applicable employment and holding period requirements under the Code.

TRANSFERABILITY. Executive shall not be entitled to assign, hypothecate, alienate, pledge or otherwise transfer the Share Options except to a member of Executive's Immediate Family or an entity controlled by Executive or Executive's Immediate Family (other than Share Options intended to be incentive stock options within the meaning of Section 422 of the Code which shall not be transferable). "IMMEDIATE FAMILY" shall mean a spouse, child, parent, sibling or in-law. Any such transferee shall be bound by the terms of this Agreement and the Plan with respect to such Share Options.

(6) ADDITIONAL SHARE OPTIONS. The grant of additional share options ("ADDITIONAL SHARE OPTIONS") in an amount equal to 1% of the first \$120 million of equity (common or convertible preferred securities)("NEW EQUITY") raised by the Company subsequent to October 15, 1998. The Additional Share Options shall be considered "Share Options" for purposes of this Agreement except that (i) such options shall be granted and shall vest as of the date of issuance of the New Equity; (ii) the per share exercise price of such options shall be equal to the per share issue price of the New Equity; and (iii) such options shall become and remain exercisable (or be immediately exercisable) in the same proportion and same manner and duration that the previously granted Share Options are already exercisable or become exercisable (E.G. if 25% of the previously granted Share Options have already become exercisable at the time the Additional Share Options are granted, 25% of all the Additional Share Options shall be immediately exercisable upon grant, with the balance of the Additional Share Options proportionally becoming exercisable on the same timetable as the previously granted Share Options). In addition, Executive shall be entitled to receive

such other share options as may be granted by the Board in its sole discretion.

(vii)LEGAL FEES AND COSTS. Payment of the Executive's reasonable legal fees incurred in connection with the preparation and negotiation of this Agreement, up to an aggregate maximum of \$35,000 for Executive, Daniel P. Friedman and Anne N.

**Zahner.**

**5. TERMINATION OF EMPLOYMENT AND CHANGE IN CONTROL**

(1) REASON FOR TERMINATION. Executive's employment hereunder may be terminated during the Employment Period under the following circumstances:

(1) CAUSE. The Company shall have the right to terminate Executive's employment for Cause upon Executive's: (A) conviction of, or plea of guilty or no contest to, an illegal act with respect to the Company; (B) conviction of, or plea of guilty or no contest to, a felony involving moral turpitude; or (C) Executive's willful and continued failure to use best efforts to substantially perform his duties hereunder (other than any such failure resulting from Executive's (x) incapacity due to Disability or (y) inability due to the unreasonableness of the duties requested to be performed) or willful misconduct or gross negligence in the performance of his duties hereunder for a period of thirty (30) days after written demand for substantial performance is delivered by the Company specifically identifying the manner in which the Company believes Executive has not substantially performed his duties or engaged in actions which constitute willful misconduct or gross negligence, PROVIDED, HOWEVER, that no termination for Cause shall occur unless a majority of the Board has voted to terminate Executive for Cause after Executive has received notice and an opportunity to cure the alleged Cause in accordance with this Paragraph 5(a)(i) and has failed to do so. If the Executive is terminated for Cause, the date of termination shall be the date such written demand is delivered. Additionally, no act, or failure to act, on Executive's part shall be considered "WILLFUL" unless done, or omitted to be done, by him (I) not in good faith and (II) without reasonable belief that his action or omission was in furtherance of the interests of the Company.

(2) DEATH. Executive's employment hereunder shall terminate upon his death.

(3) **DISABILITY.** The Company shall have the right to terminate Executive's employment due to "Disability" in the event that there is a determination by the Company, upon the advice of an independent qualified physician mutually selected by Executive and the Company, that Executive has become physically or mentally incapable of performing his duties under this Agreement and such disability has disabled Executive for a period of one hundred eighty (180) days out of three hundred and sixty (360) days. (1)

(4) **GOOD REASON.** Executive shall have the right to terminate his employment for "Good Reason": (A) upon the occurrence of any material breach of this Agreement by the Company which shall include but not be limited to: (1) an assignment to Executive of duties materially inconsistent with Executive's status as Executive Vice President or a material and adverse alteration in the nature of, or material diminution in, Executive's duties and/or responsibilities, reporting obligations, titles or authority; (2) upon a reduction in Executive's Annual Base Salary or a material reduction in other benefits (not affecting the Company's executives generally) or a failure to pay such amounts when due; and (3) upon the relocation of the Company's principal executive offices or Executive's own office location to a location outside of Manhattan, it being acknowledged that the Company shall establish an office in Manhattan although as of the date hereof the Company does not yet have such an office; (B) upon the Company's failure to nominate Daniel P. Friedman ("FRIEDMAN") for election to the Board of Trustees or the Company's failure to use its reasonable best efforts to elect Friedman to the Board; (C) upon Friedman being forced to resign from the Board without Cause; (D) upon Friedman's termination of his Employment Agreement for Good Reason; (E) upon the Company being placed into voluntary or involuntary bankruptcy; or (F) the Company's failure to obtain shareholder approval pursuant to Paragraph 4(c)(v); provided, **HOWEVER**, that no termination for Good Reason shall occur unless the Company has received notice from Executive of termination for Good Reason and the Company has failed to cure such alleged action which may have given rise to Executive's right to terminate for Good Reason within thirty (30) days after written notice of such alleged actions is delivered to the Company specifically identifying such alleged actions.

Any dispute between the parties as to an alleged breach by the Company as set forth in clause (A)(1) above shall be resolved by arbitration pursuant to Paragraph 11.

(5) WITHOUT CAUSE. The Company shall have the right to terminate the Executive's employment hereunder without Cause subject to the terms and conditions of this Agreement.

(6) WITHOUT GOOD REASON. The Executive shall have the right to terminate his employment hereunder without Good Reason subject to the terms and conditions of this Agreement.

(7) CHANGE IN CONTROL. Executive shall have the right to terminate his employment hereunder following a Change in Control. For purposes of this Agreement "Change in Control" shall mean that any of the following events has occurred: (1)

(A) An acquisition (other than directly from the Company)

of any voting securities of the Company (treating all classes of outstanding voting securities or other securities convertible into voting securities as if they were converted into voting securities) (the "VOTING SECURITIES") by any "person", "entity" or "group of affiliated persons" (as such terms are used for purposes of Section 13(d) or 14(d) (collectively, "PERSONS") of the Securities Exchange Act of 1934, as amended (the "1934 Act") (other than Gotham Partners, L.P. ("GOTHAM"), Apollo Real Estate Advisors, L.P. ("APOLLO") or any affiliate of Gotham or Apollo or entity in which Gotham or Apollo own at least a 50% interest (collectively, the "GOTHAM/APOLLO ENTITIES")) immediately after which such Person has "Beneficial Ownership" (within the meaning of Rule 13d-3 promulgated under the 1934 Act and irrespective of any vesting or waiting periods) of thirty (30%) percent or more of the combined voting power of the Company's then outstanding Voting Securities; provided, however, that in determining whether a Change in Control has occurred, Voting Securities which are acquired in a "Non-Control Acquisition" (as hereinafter defined) shall not constitute an acquisition which would cause a Change in Control. A "NON-CONTROL ACQUISITION" shall mean an acquisition by (1) an employee benefit plan (or a trust forming a part thereof) maintained by (x) the

Company or (y) any corporation or other Person of which a majority of its voting power or its equity securities or equity interest is owned directly or indirectly by the Company (a "Subsidiary"), (2) the Company or any Subsidiary, or (3) any Person in connection with a "Non-Control Transaction."

(B) Six (6) of the ten (10) individuals who were appointed to the Board after April 1, 1998 (the "INCUMBENT BOARD") cease for any reason to be members of the Board; PROVIDED, HOWEVER, that if the election, or nomination for election by the Company's shareholders, of any new trustee was approved by Friedman, such new trustee shall, for purposes of this Agreement, be considered as a member of the Incumbent Board.

(C) A merger, consolidation or reorganization involving the Company, unless

(1) the shareholders of the Company, immediately before such merger, consolidation or reorganization, own, directly or indirectly, immediately following such merger, consolidation or reorganization, more than seventy (70%) percent of the combined voting power of the outstanding Voting Securities of the entity resulting from such merger or consolidation or reorganization (the "SURVIVING ENTITY") in substantially the same proportion as their ownership of the Voting Securities immediately before such merger, consolidation or reorganization, and

(2) the individuals who were members of the Incumbent Board immediately prior to the execution of the agreement providing for such merger, consolidation or reorganization constitute at least two-thirds of the members of the board of directors of the Surviving Entity or an entity beneficially owning, directly or indirectly, a majority of the Voting Securities of the Surviving Entity, and

(3) no Person (other than the Company, any Subsidiary, any employee benefit plan (or any trust forming a part thereof) maintained by the Company, the Surviving Entity or any Subsidiary, or any Person who, immediately prior to such merger, consolidation or reorganization had Beneficial Ownership of thirty (30%) percent or

more of the then outstanding Voting Securities) owns, directly or indirectly, thirty percent or more of the combined voting power of the Surviving Entity's then outstanding voting securities.

A transaction described in clauses (1) through (3) shall herein be referred to as a "Non-Control Transaction".

(D) A complete liquidation or dissolution of the Company.

(E) the Company makes aggregate cash or non-cash distributions to its shareholders of the proceeds from the sales of assets equal to or greater than \$4.00 per Common Share and immediately following such distribution the "Net Asset Value" of the Company is less than \$150 million. "NET ASSET VALUE" shall be the fair market value of all of the Company's assets (as determined by mutual agreement of Executive and the Company or, if the parties cannot agree, by an arbitrator in accordance with Paragraph 11) less all Company liabilities.

Notwithstanding the foregoing, a Change in Control shall not be deemed to occur solely because any Person (the "SUBJECT PERSON") acquired Beneficial Ownership of more than the permitted amount of the outstanding Voting Securities as a result of the acquisition of Voting Securities by the Company which, by reducing the number of Voting Securities outstanding, increases the proportional number of shares Beneficially Owned by the Subject Person, provided that if a Change in Control would occur (but for the operation of this sentence) as a result of the acquisition of Voting Securities by the Company, and after such share acquisition by the Company, the Subject Person becomes the Beneficial Owner of any additional Voting Securities which increases the percentage of the then outstanding Voting Securities Beneficially Owned by the Subject Person, then a Change in Control shall occur.

(2) NOTICE OF TERMINATION. Any termination of Executive's employment by the Company or any such termination by Executive (other than on account of death) shall be communicated by written Notice of Termination to the other party hereto. For purposes of this Agreement, a "NOTICE OF TERMINATION" shall mean a notice which shall indicate the specific termination provision in this Agreement relied upon and shall set forth in reasonable detail the facts and circumstances claimed to provide a basis for termination of Executive's



employment under the provision so indicated. In the event of the termination of Executive's employment on account of death, written Notice of Termination shall be deemed to have been provided on the date of death.

## 6. COMPENSATION UPON TERMINATION OF EMPLOYMENT

(1) **BY THE COMPANY FOR CAUSE OR BY EXECUTIVE WITHOUT GOOD REASON.** In the event the Company terminates Executive's employment for Cause or Executive terminates his employment without Good Reason, the Company shall pay Executive and Executive shall be entitled to receive any (i) unpaid Annual Base Salary at the rate then in effect accrued through and including the date of termination and (ii) reimbursement of expenses incurred prior to the date of termination ("EXPENSE REIMBURSEMENT").

Except for any rights which Executive may have to unpaid salary amounts, the LTC Payment (as defined herein) and Expense Reimbursement through and including the date of termination and Exercisable Options (and, with respect to a termination by Executive without Good Reason, any Share Options which have not yet become exercisable on the date of termination), the Company shall have no further obligations hereunder following such termination other than pursuant to Paragraphs 6(d), 10 and 12. The aforesaid amounts shall be payable in full immediately upon such termination.

(2) **UPON DEATH OR DISABILITY.** In the event of termination of Executive's employment as a result of either Executive's death or Disability, the Company shall pay to Executive, his estate or his personal representative (i) the accrued but unpaid Annual Base Salary at the rate then in effect; (ii) earned but unpaid incentive compensation or bonuses for completed performance periods; (iii) an amount equal to 12 months of the Annual Base Salary at the rate then in effect (the "SALARY PAYMENT"); and (iv) Expense Reimbursement. The aforesaid amounts shall be payable in cash without discount for early payment, at the option of Executive, his estate or his personal representative, either in full immediately upon such termination or monthly over the Unexpired Employment Period (the "PAYMENT ELECTION"). In the event of termination of employment due to Disability, Executive shall also receive continuation of health coverage through the end of the Unexpired Employment Period on the same basis as health coverage is provided by the Company for active employees and as may be amended from time to time ("MEDICAL CONTINUATION").

Except for any rights which Executive may have hereunder including the accrued Annual Base Salary, the Salary Payment, Exercisable Options, the LTC Payment, Expense Reimbursement and in the event of a termination of employment due to Disability, Medical Continuation, the Company shall have no further obligations hereunder following such termination other than

pursuant to Paragraphs 6(d), 10 and 12. The foregoing payments shall be in addition to any benefits to which Executive may be entitled under any insurance maintained by the Company.

**(3) BY THE COMPANY WITHOUT CAUSE OR BY EXECUTIVE FOR GOOD REASON OR IN THE EVENT OF A CHANGE IN CONTROL.**

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(i) **NO BANKRUPTCY.** In the event the Company terminates Executive's employment for any reason other than Cause, death or Disability or Executive terminates his employment for Good Reason (other than as set forth in Paragraph 6(c)(ii)), or in the event of a Change of Control, the Company shall pay to Executive and Executive shall be entitled to receive the sum total of: (A) the accrued but unpaid Annual Base Salary at the rate then in effect; (B) earned but unpaid incentive compensation and/or bonuses for completed performance periods; (C)(1) if the effective date of termination is on or prior to the eighteen (18) month anniversary of the commencement of the Employment Term, an amount equal to three (3) times the Annual Base Salary at the rate then in effect or (2) if the effective date of termination is after the eighteen (18) month anniversary of the commencement of the Employment Term, an amount equal to two and one-half (2.5) times the Annual Base Salary at the rate then in effect (as applicable, the "TERMINATION PAYMENT"); and (D) continuation of Executive's participation in all benefit plans, programs or arrangements of the Company (except tax-qualified plans), including, without limitation, Medical Continuation, for a period of two years following such termination. The aforesaid amount shall be payable in cash without discount for early payment, at the option of Executive, in accordance with the Payment Election.

(ii) **BANKRUPTCY.** Executive may not terminate employment for Good Reason due to the Company being placed in bankruptcy until the eighteen (18) month anniversary thereof. If Executive thereafter terminates this Agreement, the Company shall pay to Executive and Executive shall be entitled to receive the same payments and benefits set forth in Paragraph 6(c)(i); PROVIDED, HOWEVER, that if the date of being placed in bankruptcy is (x) on or prior to the eighteen (18) month anniversary of the commencement of the Employment Term, Executive shall receive the Termination Payment set forth in Paragraph 6(c)(i)(C)(1) and (y) after the eighteen (18) month anniversary of the commencement of the Employment Term, Executive shall receive the Termination Payment set forth in Paragraph 6(c)(i)(C)(2).

(iii) **SECTION 280G.** Notwithstanding anything contained in this Agreement to the contrary, to the extent that any payment or distribution of any type to or for Executive by the Company, any affiliate of the Company, any person who acquires ownership or effective control of the Company or ownership of a substantial portion of the Company's assets (within the meaning of Section 280G of the Code and the

regulations thereunder), or any affiliate of such person, whether paid or payable or distributed or distributable pursuant to the terms of this Agreement or otherwise (the "TOTAL PAYMENTS") is or will be subject to the excise tax imposed under Section 4999 of the Code (the "EXCISE TAX"), then the Total Payments shall be reduced (but not below zero) if and to the extent that a reduction in the Total Payments would result in the Executive retaining a larger amount, on an after-tax basis (taking into account federal, state and local income taxes and the Excise Tax), than if the Executive received the entire amount of such Total Payments. Executive shall have the right to specify the order in which the Company shall reduce or eliminate the Total Payments in order to effectuate the foregoing.

Except for any rights which Executive may have hereunder including the accrued Annual Base Salary, the Termination Payment, Exercisable Options, the LTC Payment, Expense Reimbursement and Medical Continuation, the Company shall have no further obligations hereunder following such termination other than pursuant to Paragraphs 6(d), 10 and 12.

(4) GENERAL. The parties agree to cooperate to structure all termination payments made pursuant to this Agreement in a manner so that such payments are not subject to the Excise Tax.

#### 7. MITIGATION; PAYMENTS PENDING RESOLUTION OF DISPUTES

Executive shall not be required to mitigate amounts payable under this Agreement by seeking other employment or otherwise, and there shall be no offset against amounts due Executive under this Agreement on account of subsequent employment. Amounts owed to Executive under this Agreement shall not be offset by any claims the Company may have against Executive and such payment shall not be affected by any other circumstances, including, without limitation, any counterclaim, recoupment, defense, or other right which the Company may have against Executive or others. During the pendency of any dispute between the Company and Executive with respect to the termination of this Agreement, the Company shall establish and maintain an escrow account ("ESCROW ACCOUNT") with Battle Fowler LLP ("ESCROW AGENT") pursuant to an agreement reasonably acceptable to Executive and the Escrow Agent. The Company shall pay into the Escrow Account from time to time the compensation and cash-value of the benefits which would otherwise be payable to Executive if there were no dispute. Upon resolution of the dispute, the Escrow Agent shall pay the funds in the Escrow Account as required by the court or arbitrator with jurisdiction over the dispute or in accordance with the joint instructions of the parties.

#### 8. NON-COMPETE

(1) NON-COMPETITION. Executive agrees that, without the prior written consent of a majority of the Board and in accordance with applicable law, and except as provided in subparagraph 8(b), during the Employment Period, Executive shall not invest, manage or otherwise be engaged in commercial real estate.

(2) EXCLUDED ACTIVITIES. Nothing contained in this Paragraph 8 shall preclude Executive from:

(1) Continuing to own, manage in accordance with past practices or make additional capital contributions to Executive's existing investments listed on SCHEDULE A attached hereto.

(2) making passive investments of 5% or less in publicly listed or traded real estate companies.

#### 9. NO SOLICITATION; CONFIDENTIALITY.

(1) NO SOLICITATION. During the Restricted Period (as defined herein), Executive shall not, nor cause any other person to, without the prior written consent of the Board, directly or indirectly, solicit for employment, employ in any capacity or make an unsolicited recommendation to any other person that it employ or solicit for employment any person who is or was, at any time during the Employment Period or the Restricted Period, an officer, executive or key employee of the Company or of any of its affiliates (other than Friedman and Anne N. Zahner, whose solicitation, employment or recommendation by Executive shall not be prohibited by the terms of this Agreement). As used in this Agreement, "RESTRICTED PERIOD" shall mean the six (6) months following Executive's termination of employment for any reason.

(2) CONFIDENTIALITY. Executive acknowledges that, through his status as Executive Vice President of the Company, he has, and will have, possession of Confidential Information (as defined herein) as to the business of the Company. Executive agrees that all such Confidential Information constitutes a vital part of the business of the Company and its affiliates and is by its nature trade secrets and confidential information proprietary to the Company and its affiliates. Executive agrees that he shall not divulge, communicate, furnish or make accessible (whether orally or in writing or in books, articles or any other medium) to any individual, firm, partnership, corporation or other entity or person, any knowledge or information with respect to Confidential Information directly or indirectly relating to the business of the Company or any of its affiliates. The term "CONFIDENTIAL INFORMATION" shall mean any information not generally known in the relevant trade or industry or otherwise not generally available to the public, which was obtained from the Company or which was learned, discovered, developed,

conceived, originated or prepared during or as a result of the performance of any services by Executive on behalf of the Company.

(3) RETURN OF COMPANY DOCUMENTS. All memoranda, notes, lists, notebooks, records and other documents or papers (and all copies thereof), including such items stored in computer memories, portable computers and the like, on microfiche, disk or by any other means, made or compiled by or on behalf of Executive or made available to Executive relating to the Company are and shall be the Company's property and shall be delivered to the Company promptly upon the termination of Executive's employment with the Company or at any other time after such termination on request.

(4) UNENFORCEABILITY. The provisions contained in Paragraphs 8 and 9 as to the time periods and scope of activities, persons or entities affected shall be deemed divisible so that, if any provision contained in Paragraphs 8 or 9 is determined to be invalid or unenforceable, such provision shall be deemed modified so as to be valid and enforceable to the full extent lawfully permitted.

(5) 20

(6) Remedies. Executive agrees that (i) the provisions of Paragraphs 8 and 9 are reasonable and necessary for the protection of the Company; (ii) the Company would not have entered into this Agreement unless the Executive agreed to the inclusion of such provisions; (iii) such provisions may not be adequately enforced by an action for damages and (iv) in the event of a breach thereof by Executive, the Company shall be entitled to apply for and obtain injunctive relief in any court of competent jurisdiction to restrain the breach or threatened breach of such violation or otherwise to enforce specifically such provisions against such violation, without the necessity of the posting of any bond by the Company. The forgoing remedies are in addition to any rights the Company may have against Executive for damages in the event Executive breaches any of the provisions of Paragraphs 8 and 9.

## 10. PREVIOUS EMPLOYER

(1) COMMITMENT TO PAY/FUND. The Company agrees to take the following actions with respect to the following commitments with respect to Executive's immediately prior employer, Enterprise Asset Management, Inc. ("EAM") and Executive:

(i) LONG-TERM COMPENSATION ("LTC"). The Company shall pay the LTC to Executive as follows: (x) 1/3 on commencement of the Employment Period and 1/3 on each of the second and fourth anniversaries of the

commencement of the Employment Period and (y) if this Agreement is terminated for any reason, Company shall make a lump sum payment equal to the present value (discounted at 10% per annum) of any unpaid LTC (the "LTC PAYMENT"). Executive shall reimburse Company to the extent Executive receives payment from EAM of LTC paid by the Company.

(ii) LOAN GUARANTEES. If EAM fails to continue to guarantee existing loans owed by Executive, the Company shall provide replacement loans on the same or better terms and conditions as the existing loans ("REPLACEMENT LOANS").

(iii) LOAN REPAYMENT. If EAM demands repayment prior to maturity of existing loans to Executive from EAM, the Company shall provide replacement loans on the same or better terms and conditions as the existing loans ("NEW LOANS").

Executive's LTC, guarantees and loans are listed in SCHEDULE B attached hereto.

In the event this Agreement is terminated for any reason, Executive shall repay all Replacement Loans and New Loans within ninety (90) days of such date of termination. The Replacement Loans and New Loans shall be nonrecourse to Executive and the Company's sole recourse for the repayment of any Replacement Loans or New Loans shall be any payments due to Executive from the Company under this Agreement, the Share Options and the assets which were purchased with the proceeds from the loans which have been replaced by the Replacement Loan or the New Loan.

(2) INDEMNITY. In the event the Executive is made party or threatened to be made a party to any action, suit or proceeding, whether civil, criminal, administrative or investigative (a "PROCEEDING"), by EAM, its officers, directors, equity owners or Affiliates, by reason of Executive's having negotiated or entered into this Agreement or otherwise having become an employee of the Company, the Company shall indemnify, hold harmless and defend Executive against any and all claims, demands, suits, judgments, assessments and settlements including all expenses incurred or suffered by Executive in connection therewith (including, without limitation, all legal fees incurred using counsel reasonably acceptable to Executive) (collectively, "DAMAGES"). Expenses incurred by Executive in connection with any Proceeding shall be paid by the Company in advance upon request of Executive that the Company pay such expenses.

(3) REPRESENTATIONS. Executive hereby represents and warrants to the Company that Executive has not entered into any

written or oral agreement for employment with EAM or any other person or entity.

(4) SURVIVAL. The provisions of this Paragraph shall remain in effect after this Agreement is terminated irrespective of the reasons for termination.

## 11. ARBITRATION

The parties hereto will endeavor to resolve in good faith any controversy, disagreement or claim arising between them with respect to the interpretation, performance or operation of Paragraphs 5(a)(iv)(A)(1) and 5(a)(vii)(E) of this Agreement. If they are unable to do so, any such controversy, disagreement or claim will be submitted to binding arbitration, for final resolution without appeal, by either party giving written notice to the other of the existence of a dispute with respect to such Paragraph which it desires to have arbitrated. The arbitration will be conducted in New York, New York by a panel of three (3) arbitrators and will be held in accordance with the rules of the American Arbitration Association. Of the three arbitrators, one will be selected by the Company, one will be selected by Executive and the third will be selected by the two arbitrators so selected. Each party will notify the other party of the arbitrator selected by him or it within fifteen (15) days after the giving of the written notice referred to in this Paragraph 11. The decision and award of the arbitrators must be in writing and will be final and binding upon the parties hereto. Judgment upon the award may be entered in any court having jurisdiction thereof, or application may be made to such court for a judicial acceptance of the award and an order of enforcement, as the case may be. Subject to the provisions of Paragraph 12 (b), the expenses of arbitration will be borne in accordance with the determination of the arbitrators.

## 12. INDEMNIFICATION/LEGAL FEES/"KEY MAN" INSURANCE.

(1) INDEMNIFICATION. In the event the Executive is made party or threatened to be made a party to any Proceeding, by reason of Executive's employment with or serving as an officer or director of the Company, the Company shall indemnify, hold harmless and defend Executive to the fullest extent authorized by Ohio law, as the same exists and may hereafter be amended, against any and all Damages and such indemnification shall continue as to Executive even after Executive is no longer employed by the Company and shall inure to the benefit of his heirs, executors, and administrators. Notwithstanding the foregoing, Executive shall not be entitled to indemnification pursuant to this Paragraph 12(a) if a court or other tribunal conclusively determines that Executive engaged in actions in connection with Executive's employment with the Company which were committed in bad faith, were the result of active and

deliberate dishonesty, or constitute willful misconduct, fraud or gross negligence.

Expenses incurred by Executive in connection with any Proceeding referred to in this Paragraph 12 shall be paid by the Company in advance upon request of Executive that the Company pay such expenses; but only in the event that Executive shall have delivered in writing to the Company an undertaking to reimburse the Company for expenses with respect to which Executive is not entitled to indemnification.

The provisions of this Paragraph shall remain in effect after this Agreement is terminated irrespective of the reasons for termination. The indemnification provisions of this Paragraph shall not supersede or reduce any indemnification provided to Executive under any separate agreement, or the by-laws of the Company since it is intended that this Agreement shall expand and extend the Executive's rights to receive indemnity.

The Company shall maintain in effect during the Employment Period a directors' and officers' liability insurance policy, with a policy limit of at least \$10,000,000, subject to customary exclusions, with respect to claims made against officers and directors of the Company.

(2) LEGAL FEES. Except as set forth below, if any contest or dispute shall arise between the Company and Executive regarding or as a result of any provision of this Agreement, the Company shall pay, or reimburse Executive for, all legal fees and expenses reasonably incurred by Executive in connection with such contest or dispute; PROVIDED, HOWEVER, that if Executive is not successful in respect of substantially all of Executive's claims pursued or defended in connection with such contest or dispute, Executive shall pay or reimburse the Company for all such fees and expenses advanced by the Company. Executive shall pay the first \$25,000 of his fees or expenses as they are incurred and the Company shall pay all such fees and expenses over \$25,000 as they are incurred. If Executive is successful in respect of substantially all of such claims, the Company shall reimburse Executive for any amounts paid by Executive as soon as practicable following the final resolution of such contest or dispute.

(3) KEY MAN INSURANCE. Executive shall cooperate with, and take such actions as may be reasonably requested by, the Company in the event the Company determines to obtain "key man" insurance with respect to Executive.

### 13. SUCCESSORS AND ASSIGNS.



(1) COMPANY. Unless Executive elects to terminate this Agreement as a result of a Change in Control, the Company shall require any successor (whether direct or indirect, by purchase, merger, consolidation or otherwise) to all or substantially all of the business and/or assets of the Company, to expressly assume and agree to perform this Agreement in the same manner and to the same extent that the Company would be required to perform it if no such succession had taken place.

(2) EXECUTIVE. This Agreement and all rights of Executive hereunder may be transferred only by will or the laws of descent and distribution. Upon Executive's death, this Agreement and all rights of Executive hereunder shall inure to the benefit of and be enforceable by Executive's beneficiary or beneficiaries, personal or legal representatives, or estate, to the extent any such person succeeds to Executive's interests under this Agreement. Executive shall be entitled to select and change a beneficiary or beneficiaries to receive any benefit or compensation payable hereunder following Executive's death by giving Company written notice thereof. If Executive should die following the date of termination while any amounts would still be payable to him hereunder if he had continued to live, all such amounts, unless otherwise provided herein, shall be paid in accordance with the terms of this Agreement to such person or persons so appointed in writing by Executive, including, without limitation, under any applicable plan, or otherwise to his legal representatives or estate.

#### 14. MODIFICATION OR WAIVER

No amendment, modification, waiver, termination or cancellation of this Agreement shall be binding or effective for any purpose unless it is made in a writing signed by the party against whom enforcement of such amendment, modification, waiver, termination or cancellation is sought. No course of dealing between or among the parties to this Agreement shall be deemed to affect or to modify, amend or discharge any provision or term of this Agreement. No delay on the part of the Company or Executive in the exercise of any of their respective rights or remedies shall operate as a waiver thereof, and no single or partial exercise by the Company or Executive of any such right or remedy shall preclude other or further exercise thereof. A waiver of right or remedy on any one occasion shall not be construed as a bar to or waiver of any such right or remedy on any other occasion.

The respective rights and obligations of the parties hereunder shall survive the Executive's termination of employment and termination of this Agreement to the extent necessary for the intended preservation of such rights and obligations.

#### 15. NOTICES

All notices or other communications required or permitted hereunder shall be made in writing and shall be deemed to have been duly given if delivered by hand or delivered by a recognized delivery service or mailed, postage prepaid, by express, certified or registered mail, return receipt requested, and addressed to the Company at the address set forth above or Executive at his address as set forth in the Company records (or to such other address as shall have been previously provided in accordance with this Paragraph 15).

#### 16. GOVERNING LAW

This agreement will be governed by and construed in accordance with the laws of the State of New York without regard to principles of conflicts of laws thereunder.

#### 17. SEVERABILITY

Whenever possible, each provision and term of this Agreement shall be interpreted in such manner as to be effective and valid under applicable law, but if any provision or term of this Agreement shall be held to be prohibited by or invalid under such applicable law, then, such provision or term shall be ineffective only to the extent of such prohibition or invalidity, without invalidating or affecting in any manner whatsoever the remainder of such provisions or term or the remaining provisions or terms of this Agreement.

#### 18. COUNTERPARTS

This Agreement may be executed in separate counterparts, each of which is deemed to be an original and both of which taken together shall constitute one and the same agreement.

#### 19. HEADINGS

The headings of the Paragraphs of this Agreement are inserted for convenience only and shall not be deemed to constitute a part hereof and shall not affect the construction or interpretation of this Agreement.

#### 20. ENTIRE AGREEMENT

This Agreement constitutes the entire agreement of the parties with respect to the subject matter hereof and supersedes all other prior agreements and undertakings, both written and oral, among the parties with respect to the subject matter hereof.

#### 21. EXCULPATION

Notwithstanding anything contained herein to the contrary, this Agreement is made and executed on behalf of the Company by its officer(s) on behalf of the trustees thereof, and none of the trustees or any additional or successor trustee hereafter appointed, or any beneficiary, officer, employee or agent of the Company shall have any liability in his personal or individual capacity, but instead, Executive shall look solely to the property and assets of the Company for satisfaction of claims of any nature arising from or in connection with this Agreement.

**[SIGNATURE PAGE FOLLOWS]**

IN WITNESS WHEREOF, the undersigned have executed this Agreement as of the date first above written.

**COMPANY: FIRST UNION REAL ESTATE EQUITY AND  
MORTGAGE INVESTMENTS**

By:

---

Name:

Title:

**EXECUTIVE:**

---

**David Schonberger**

**SCHEDULE A**  
**EXISTING INVESTMENTS**

**DAVID SCHONBERGER**

**INVESTMENTS OWNED AND MANAGED**

22. Greenburgh, NY

23. Mt. Kisco, NY (T.J. Maxx)

24. Hopewell Junction - Land Contract

25. GP - Ridgefield, CT - 24,000 Sq. ft. Mixed Use

**INVESTMENTS OWNED**

26. Emax Securities (various entities)

27. Peru Mall

**SCHEDULE B**

**DAVID SCHONBERGER**

Long Term Compensation	None
Loans from EAM	None
Loans Guaranteed by EAM	None

**SCHEDULE A**

**EXISTING INVESTMENTS**

**DAN FRIEDMAN**

None

**SCHEDULE A**

**EXISTING INVESTMENTS**

**DAVID SCHONBERGER**

1. Greenburgh, NY
2. Mt. Kisco, NY (T.J. Maxx)
3. Hopewell Junction - Land Contract
4. GP - Ridgefield, CT - 24,000 Sq. ft. Mixed Use



**SCHEDULE A**

**EXISTING INVESTMENTS**

**ANNE ZAHNER**

None

**Schedule B**

**Dan Friedman**

Long Term Compensation	\$379,241.89
Loan from EAM	\$336,000.0
Loans Guaranteed by EAM	\$115,000.00

Schedule B

-----  
David Schonberger  
-----

Long Term Compensation	None
Loans from EAM	None
Loans Guaranteed by EAM	None

**Schedule B**

**Anne Zahner**

Long Term Compensation		\$27,184.56
Loans from EAM	None	
Loans Guaranteed by EAM		\$139,000.00

**EXHIBIT 12**

**FIRST UNION REAL ESTATE EQUITY AND MORTGAGE INVESTMENTS AND  
FIRST UNION MANAGEMENT, INC.  
STATEMENTS OF RATIOS OF COMBINED INCOME FROM OPERATIONS  
AND COMBINED NET INCOME TO FIXED CHARGES  
(IN THOUSANDS, EXCEPT RATIOS)**

	YEARS ENDED DECEMBER 31,				
	1998	Restated(2) 1997	Restated(2) 1996	Restated(2) 1995	Restated (2) 1994
	----	----	----	----	----
Income (loss) before capital gain or loss, extraordinary loss, cumulative effect of accounting change and after loss allocated to minority interest	\$(91,465)	\$ 4,434	\$ 1,681	\$ 881	\$ 4,261
Add fixed charges, exclusive of construction interest capitalized	51,437	30,479	24,018	22,987	21,865
Income (loss) from operations, as defined	(40,028)	34,913	25,699	23,868	26,126
Capital gains	10,346	1,468	---	31,577	---
Reduction for unrealized loss on carrying value of assets identified for disposition	---	---	---	(14,000)	---
Net income (loss), as defined	\$(29,682)	\$36,381	\$25,699	\$41,445	\$26,126
Fixed charges:					
Interest					
- Mortgage loans	\$ 29,032	\$15,437	\$ 8,877	\$ 7,670	\$ 7,335
- Senior notes	5,856	8,875	9,090	9,305	9,305
- Notes payable	3,757	---	---	---	---
- Bank loans and other	12,214	5,552	5,459	5,422	4,640
- Capitalized interest	---	---	121	169	---
Amortization of debt issue costs	150	215	196	184	168
Rents (1)	428	400	396	406	417
Fixed charges, as defined	\$ 51,437	\$30,479	\$24,139	\$23,156	\$21,865
Preferred dividend accrued	\$ 2,999	\$ 4,831	\$ 845	\$ ---	\$ ---
Ratio of income (loss) from operations, as defined, to fixed charges	--	1.15	1.06	1.03	1.19
Ratio of net income (loss), as defined, to fixed charges	--	1.19	1.06	1.79	1.19
Ratio of net income (loss) as defined, to fixed charges and preferred dividend	--	1.03	1.03	1.79	1.19

(1) The interest portion of rentals is assumed to be one-third of all ground rental and net lease payments.

(2) The Trust has restated its Combined Financial Statements for each of the five years ended December 31, 1998 as a result of changing the lives of assets used to calculate depreciation expense.

**Exhibit 13**

**FIRST UNION REAL ESTATE INVESTMENTS**

**FINANCIAL HIGHLIGHTS**

**YEARS ENDED DECEMBER 31, (IN THOUSANDS, EXCEPT PER SHARE DATA AND FOOTNOTE)**

	1998 ----	RESTATED 1997 ----
Revenues	\$ 324,526	\$ 235,544
Income (loss) before capital gain, extraordinary loss and after minority interest	(91,465)	4,434
Net income (loss) before preferred dividend	(83,518)	5,676
Net income (loss) applicable to shares of beneficial interest	(86,517)	845
Dividends declared	3,478	11,651
Per share		
Loss applicable to shares of beneficial interest before capital gain, extraordinary loss and after minority interest	\$ (3.07)	\$ (.02)
Net income (loss) applicable to shares of beneficial interest, basic and diluted	(2.81)	.03
Dividends declared per share of beneficial interest	.11	.44

**MARKET PRICE AND DIVIDEND RECORD**

1998 QUARTERS ENDED	HIGH ----	LOW ---	DIVIDENDS DECLARED -----
December 31	\$ 6 1/8	\$ 3 7/16	\$
September 30	9 9/16	5 3/16	
June 30	11 7/8	8 3/4	
March 31	16 7/8	11	.11
			----- \$ .11 =====
1997 QUARTERS ENDED			
December 31	\$ 16 5/16	\$ 13 5/16	\$ .11
September 30	14 1/8	12 5/8	.11
June 30	14 1/4	12 3/4	.11
March 31	14 1/2	11 5/8	.11
			----- \$ .44 =====

The Trust's shares are traded on the New York Stock Exchange (Ticker Symbol: FUR). As of December 31, 1998, there were 3,500 recordholders of the Trust's shares of beneficial interest. The Trust estimates the total number of beneficial owners at approximately 11,000.

**SELECTED FINANCIAL DATA**
**FOR THE YEARS ENDED DECEMBER 31, (IN THOUSANDS, EXCEPT PER SHARE DATA AND FOOTNOTES)**

	RESTATED(1) 1994	RESTATED(1) 1995	RESTATED(1) 1996	RESTATED(1) 1997	1998
<b>OPERATING RESULTS</b>					
Revenues(2)	\$ 76,339	\$ 79,205	\$ 81,867	\$ 235,544	\$ 324,526
Income (loss) before capital gain, extraordinary loss, cumulative effect of accounting change and before minority interest(2),(3),(4)	4,261	881	1,681	3,490	(91,465)
Unrealized loss on carrying value of assets identified for disposition		(14,000)			
Capital gains, net		31,577		1,468	10,346
Income (loss) before extraordinary loss, cumulative effect of accounting change and before minority interest(2),(3),(4)	4,261	18,458	1,681	4,958	(81,119)
Extraordinary loss from early extinguishment of debt(5)		(910)	(286)	(226)	(2,399)
Cumulative effect of change in accounting method(6)		(4,325)			
Loss allocated to minority interest(2)				944	
Net income (loss) before preferred dividend	4,261	13,223	1,395	5,676	(83,518)
Net income (loss) applicable to shares of beneficial interest	4,261	13,223	550	845	(86,517)
Dividends declared for shares of beneficial interest	7,273	7,542	7,684	11,651	3,478
<b>Per share of beneficial interest</b>					
Income (loss) before capital gain, extraordinary loss, cumulative effect of accounting change and after minority interest(2),(3),(4)	\$ .24	\$ .05	\$ .05	\$ (.02)	\$ (3.07)
Income (loss) before extraordinary loss, cumulative effect of accounting change and after minority interest(2),(3),(4)	.24	1.02	.05	.04	(2.73)
Extraordinary loss from early extinguishment of debt(5)		(.05)	(.02)	(.01)	(.08)
Cumulative effect of change in accounting method(6)		(.24)			
Net income (loss) applicable to shares of beneficial interest, basic and diluted	.24	.73	.03	.03	(2.81)
Dividends declared per share of beneficial interest	.40	.41	.44	.44	.11
<b>FINANCIAL POSITION AT YEAR END</b>					
Total assets	\$ 352,005	\$ 376,144	\$ 413,054	\$ 790,226	\$ 786,684
Current portion of debt(7)					205,910
Long-term obligations(8)	238,296	258,454	254,868	483,459	383,089
Total equity	78,756	77,500	124,957	235,310	150,696
<b>OTHER DATA</b>					
Net cash provided by or (used for)					
Operations	\$ 19,053	\$ 12,989	\$ 11,085	\$ 15,740	\$ 6,413
Investing	(26,507)	(28,345)	(47,002)	(112,233)	(52,429)
Financing	(28,094)	15,783	35,466	110,406	74,327

This selected financial data should be read in conjunction with the Combined Financial statements and notes thereto.

(1) As a result of the Trust's review of lives assigned to real estate assets for calculation of depreciation expense during the fourth quarter of 1998, reduced asset lives have been assigned. Consequently, the Trust has restated its Combined Financial Statements for the years 1994 through 1998. Shareholders' equity at December 31, 1993 was restated from \$103,766,000 to \$81,806,000.

(2) In September 1997, First Union acquired the interests of its joint venture partners in eight shopping malls and 50% of another mall for \$88 million in cash and the assumption of \$203 million of mortgage debt. In April 1997, First Union's affiliated management company acquired voting control of Impark for \$37 million in cash, the assumption of \$26 million in debt and the issuance of \$12 million of stock in Impark to Impark employees and to its former owner.

(3) In 1998, loss before capital gain, and extraordinary loss, effect of accounting change included the following expenses related to the proxy contest and the resulting change in the composition of the Trust's Board of Trustees:

Litigation and proxy expenses	\$ 4.8 million
Other professional fees to avoid change in composition of Board	1.5 million
Severance expenses for employee change in control agreements and employment contract termination	6.1 million
Expenses related to termination of First Union's former chairman, president and chief executive officer	3.4 million
Vesting of restricted stock upon change in composition of Board	4.7 million
	-----
	\$20.5 million
	=====

In 1995, income before capital gain, extraordinary loss, cumulative effect of accounting change and minority interest included \$1.6 million of litigation and proxy expenses.

(4) In 1998, the Trust recognized \$36 million in unrealized losses on the carrying value of properties identified for disposition and Impark recognized a \$15 million reduction of goodwill.

(5) In 1998, the Trust repaid approximately \$87.5 million of its 8 7/8% Senior Notes resulting in \$1.6 million in unamortized issue costs and solicitation fees being expensed. Also, in the fourth quarter of 1998, the Trust renegotiated its bank agreement and \$90 million note payable resulting in \$.8 million of deferred costs being expensed. In 1997 and 1996, the Trust renegotiated its bank credit agreements, resulting in a \$226,000 and \$286,000 charge, respectively, related to the write-off of unamortized costs. In November 1995, the Trust repaid approximately \$36 million of mortgage debt resulting in a \$910,000 charge for the write-off of unamortized costs and prepayment premiums.

(6) In December 1995, the Trust changed its accounting method to directly expense internal leasing costs and recorded a \$4.3 million noncash charge for the cumulative effect of the accounting change as of the beginning of 1995. Funds from operations for previous years have been restated for the change in accounting method on a basis comparable to 1995.

(7) Included in the current portion of debt for 1998 is the \$90 million note payable due August 11, 1999, the \$101 million bank credit facility due August 1999, the \$10.6 million deferred obligation, and 1999 mortgage principal payments.

(8) Included in long-term obligations are senior notes and mortgage loans. Bank loans are classified as long term for 1994 through 1997. Impark's bank loans are classified as long term for 1997 and 1998.



# COMBINED BALANCE SHEETS

AS OF DECEMBER 31, (IN THOUSANDS)

	1998 ----	RESTATED 1997 -----
ASSETS		
INVESTMENTS IN REAL ESTATE		
Land	\$130,340	\$109,308
Buildings and improvements	676,519	647,000
	-----	-----
	806,859	756,308
Less - Accumulated depreciation	(165,357)	(142,082)
	-----	-----
Total investments in real estate	641,502	614,226
INVESTMENT IN JOINT VENTURE		
	1,722	1,575
MORTGAGE LOANS AND NOTES RECEIVABLE, including current portion of \$58 and \$6,469, respectively		
	5,508	30,686
OTHER ASSETS		
Cash and cash equivalents - unrestricted	28,649	2,582
- restricted	16,526	14,282
Accounts receivable and prepayments, net of allowances of \$1,395 and \$1,462, respectively	21,809	20,070
Investments	5	13,103
Inventory	2,798	3,374
Goodwill, net	45,379	66,560
Management and lease agreements, net	1,852	4,113
Deferred charges and other, net	6,864	6,300
Unamortized debt issue costs, net	7,758	7,445
Other	6,312	5,910
	-----	-----
Total assets	\$786,684	\$790,226
	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY		
LIABILITIES		
Mortgage loans, including current portion of \$4,308 and \$3,877, respectively	\$345,042	\$313,537
Notes payable	94,996	
Senior notes	12,538	100,000
Bank loans	125,821	69,922
Accounts payable and accrued liabilities	42,659	38,000
Deferred obligations	10,602	10,807
Deferred capital gains and other deferred income	3,283	10,646
Liability to former owner of Impark		10,957
	-----	-----
Total liabilities	634,941	553,869
	-----	-----
MINORITY INTEREST		
	1,047	1,047
SHAREHOLDERS' EQUITY		
Preferred shares of beneficial interest, \$25 liquidation preference, 2,300,000 shares authorized 1,349,000 shares and 2,300,000 shares outstanding in 1998 and 1997, respectively	31,737	54,109
Shares of beneficial interest, \$1 par, unlimited authorization, outstanding	31,416	28,179
Additional paid-in capital	190,679	170,567
Undistributed loss from operations	(115,968)	(25,973)
Undistributed capital gains	14,949	14,949
Deferred compensation		(5,643)
Accumulated other comprehensive income		
Available for sale securities		(66)
Foreign currency translation adjustment	(2,117)	(812)
	-----	-----
Total shareholders' equity	150,696	235,310
	-----	-----
	\$786,684	\$790,226
	=====	=====

The accompanying notes are an integral part of these statements.

# COMBINED STATEMENTS OF OPERATIONS

## FOR THE YEARS ENDED DECEMBER 31, (IN THOUSANDS, EXCEPT PER SHARE DATA)

	1998	RESTATED 1997	RESTATED 1996
	-----	-----	-----
<b>REVENUES</b>			
Rents	\$ 320,592	\$ 225,388	\$ 75,555
Interest - Mortgage loans	1,211	2,907	4,732
- Short-term investments	1,337	1,525	80
- Investments	302	494	
Equity in income from joint venture	148	488	528
Management fees	353	2,808	617
Other income	583	1,934	355
	-----	-----	-----
	324,526	235,544	81,867
	-----	-----	-----
<b>EXPENSES</b>			
Property operating	223,667	157,215	25,786
Real estate taxes	12,453	9,948	8,297
Depreciation and amortization	33,389	22,892	15,890
Interest - Mortgage loans	29,032	15,437	8,877
- Notes payable	3,757		
- Senior notes	5,856	8,875	9,090
- Bank loans and other	12,214	5,552	5,459
General and administrative	37,577	12,135	6,787
Litigation and proxy	4,848		
Foreign currency loss	2,198		
Unrealized loss on carrying value of assets identified for disposition and impaired assets	51,000		
	-----	-----	-----
	415,991	232,054	80,186
	-----	-----	-----
INCOME (LOSS) BEFORE CAPITAL GAIN, EXTRAORDINARY LOSS AND MINORITY INTEREST	(91,465)	3,490	1,681
Capital gains, net	10,346	1,468	
	-----	-----	-----
INCOME (LOSS) BEFORE EXTRAORDINARY LOSS AND MINORITY INTEREST	(81,119)	4,958	1,681
Extraordinary loss from early extinguishment of debt	(2,399)	(226)	(286)
Loss allocated to minority interest		944	
	-----	-----	-----
NET INCOME (LOSS) BEFORE PREFERRED DIVIDEND	(83,518)	5,676	1,395
Preferred dividend	(2,999)	(4,831)	(845)
	-----	-----	-----
NET INCOME (LOSS) APPLICABLE TO SHARES OF BENEFICIAL INTEREST	\$ (86,517)	\$ 845	\$ 550
	=====	=====	=====
<b>PER SHARE DATA</b>			
Income (loss) applicable to shares of beneficial interest before capital gain, extraordinary loss, and after minority interest	\$ (3.07)	\$ (.02)	\$ .05
Income (loss) before extraordinary loss and after minority interest	(2.73)	.04	.05
Extraordinary loss from early extinguishment of debt	(.08)	(.01)	(.02)
	-----	-----	-----
NET INCOME (LOSS) APPLICABLE TO SHARES OF BENEFICIAL INTEREST, BASIC AND DILUTED	\$ (2.81)	\$ .03	\$ .03
	=====	=====	=====
ADJUSTED SHARES OF BENEFICIAL INTEREST, BASIC	30,772	24,537	17,172
ADJUSTED SHARES OF BENEFICIAL INTEREST, DILUTED	31,015	25,415	17,706

### COMBINED STATEMENTS OF COMPREHENSIVE INCOME

For the years ended December 31, (In thousands)

Net income (loss)	\$ (86,517)	\$ 845	\$ 550
Other comprehensive income			
Available for sale securities	66	(66)	
Foreign currency translation adjustment	(1,305)	(812)	
	-----	-----	-----
Comprehensive income (loss)	\$ (87,756)	\$ (33)	\$ 550
	=====	=====	=====

The accompanying notes are an integral part of these statements.

**COMBINED STATEMENTS OF CHANGES IN CASH**

**FOR THE YEARS ENDED DECEMBER 31, (IN THOUSANDS)**

	1998	RESTATED 1997	RESTATED 1996
	-----	-----	-----
<b>CASH PROVIDED BY (USED FOR) OPERATIONS</b>			
Net income (loss) before preferred dividend	\$ (83,518)	\$ 5,676	\$ 1,395
Adjustments to reconcile net income (loss) before preferred dividend to net cash provided by operations			
Depreciation and amortization	33,389	22,892	15,890
Extraordinary loss from early extinguishment of debt	2,399	226	286
Capital gains, net	(10,346)	(1,468)	
Unrealized loss on carrying value of assets identified for disposition and impaired assets	51,000		
Vesting of restricted shares	4,706		
Foreign currency loss	2,198		
Increase in deferred charges and other, net	(1,316)	(4,998)	(963)
Increase in deferred income	355	2,073	
Increase in deferred interest on mortgage investments	(6)	(122)	(400)
(Decrease) increase in deferred obligations	(20)	(18)	155
Net changes in other assets and liabilities	7,572	(8,521)	(5,278)
	-----	-----	-----
Net cash provided by operations	6,413	15,740	11,085
	-----	-----	-----
<b>CASH PROVIDED BY (USED FOR) INVESTING</b>			
Repayment of mortgage investment and note payable	25,045	16,200	
Principal received from mortgage investments	139	216	176
Proceeds from sales of properties	6,507	18,374	8,825
Purchase of investments	(1,771)	(12,746)	
Sale of investments	15,141		
Investments in properties	(63,022)	(834)	(5,491)
Acquisition of joint venture interests, net of cash acquired		(72,900)	
Investment in joint venture			(30,248)
Deposit for property acquisitions	(170)	(2,315)	
Investment in Impark, net of cash acquired	(11,195)	(36,574)	
Investments in capital and tenant improvements	(23,103)	(21,654)	(20,264)
	-----	-----	-----
Net cash used for investing	(52,429)	(112,233)	(47,002)
	-----	-----	-----
<b>CASH PROVIDED BY (USED FOR) FINANCING</b>			
Increase (decrease) in bank loans	57,446	19,582	(43,800)
Issuance of preferred shares of beneficial interest, net of costs			54,109
Increase in notes payable	90,000		
Increase in mortgage loans	30,000	2,737	48,500
Repayment of mortgage loans - Normal payments	(3,951)	(2,765)	(3,286)
- Balloon payments	(468)	(13,835)	
Repayment of senior notes	(87,462)		
Repayment of medium term notes			(5,000)
Proceeds from sale of interest rate cap			1,025
Purchase of First Union shares	(1,830)		(7,125)
Sale of First Union shares	2,996	121,291	252
Sale of hedge agreement	825		
Debt issue costs paid	(3,320)	(1,261)	(1,414)
Dividends paid to shares of beneficial interest	(6,577)	(10,473)	(7,789)
Dividends paid to preferred shares of beneficial interest	(3,332)	(4,870)	
Other			(6)
	-----	-----	-----
Net cash provided by financing	74,327	110,406	35,466
	-----	-----	-----
Increase (decrease) in cash and cash equivalents	28,311	13,913	(451)
Cash and cash equivalents at beginning of year	16,864	2,951	3,402
	-----	-----	-----
Cash and cash equivalents at end of year	\$ 45,175	\$ 16,864	\$ 2,951
	=====	=====	=====

The accompanying notes are an integral part of these statements.

# COMBINED STATEMENTS OF SHAREHOLDERS' EQUITY

(IN THOUSANDS, EXCEPT FOOTNOTES)

	PREFERRED SHARES OF BENEFICIAL INTEREST	SHARES OF BENEFICIAL INTEREST	ADDITIONAL PAID-IN CAPITAL	RESTATED UNDISTRIBUTED INCOME (LOSS) FROM OPERATIONS (1) (2)	UNDISTRIBUTED CAPITAL GAINS	DEFERRED COMPEN- SATION	FOREIGN CURRENCY TRANSLATION ADJUSTMENT	AVAILABLE FOR SALE SECURITIES
BALANCE DECEMBER 31, 1995		\$17,485	\$55,081	\$ 16,823	\$14,949	\$ (1,983)		
Prior period adjustment(1)				(24,856)				
Balance December 31, 1995 as restated		17,485	55,081	(8,033)	14,949	(1,983)		
Net income before preferred dividend (restated)				1,395				
Dividends paid or accrued on shares of beneficial interest (\$.44/share)				(7,684)				
Dividends accrued on preferred shares (\$.3674/share)				(845)				
Sale of 2,300,000 preferred shares of beneficial interest, \$25 per share, net	\$54,109							
Shares sold under long-term incentive ownership plan and share option agreements		31	221					
Restricted shares issued		142	1,603			(1,745)		
Restricted shares forfeited		(36)	(226)					
Deferred compensation related to restricted shares						499		
Other				(7)				
BALANCE DECEMBER 31, 1996 (RESTATED)	54,109	17,622	56,672	(15,167)	14,949	(3,229)	--	--
Net income before preferred dividend (restated)				5,676				
Dividends paid or accrued on shares of beneficial interest (\$.44/share)				(11,651)				
Dividends accrued on preferred shares (\$2.10/share)				(4,831)				
Sale of 3,910,000 shares of beneficial interest, net		3,910	42,211					
Sale of 6,325,000 shares of beneficial interest, net		6,325	68,139					
Shares sold under long-term incentive ownership plan and share option agreements		96	611					
Restricted shares issued		226	2,934			(3,160)		
Deferred compensation related to restricted shares						746		
Foreign currency translation adjustment							\$ (812)	
Available for sale securities								\$ (66)
BALANCE DECEMBER 31, 1997 (RESTATED)	54,109	28,179	170,567	(25,973)	14,949	(5,643)	(812)	(66)
Net loss before preferred dividend				(83,518)				
Dividends paid on shares of beneficial interest (\$.11/share)				(3,478)				
Dividends paid or accrued on preferred shares (\$2.10/share)				(2,999)				
Conversion of preferred shares	(22,372)	3,144	19,228					
Shares sold under long-term incentive ownership plan and share option agreements		373	2,623					
Restricted shares issued		343	4,632			(4,975)		
Restricted shares forfeited		(453)	(5,147)			5,600		
Shares purchased		(170)	(1,660)					
Issuance of 500,000 stock warrants			436					
Deferred compensation related to restricted shares						312		
Vesting of restricted shares						4,706		
Foreign currency translation adjustment							(1,305)	
Available for sale securities								66
BALANCE DECEMBER 31, 1998	\$31,737	\$31,416	\$190,679 (2)	\$(115,968) (3)	\$14,949	\$ --	\$(2,117)	\$ --

(1) The Trust changed its useful lives for the calculation of depreciation expense in 1998 and restated its Combined Financial Statements for the five years ended December 31, 1998. The cumulative effect of changing the asset lives prior to December 31, 1994 is \$24,856,000.

(2) Includes the balance of cumulative undistributed net loss of First Union Management, Inc. of \$5,825,000, \$6,621,000, \$5,497,000 and \$36,346,000 as of December 31, 1995, 1996, 1997 and 1998, respectively.

(3) Cumulative distributions in excess of the Trust's net income from inception are \$11,330,000.

The accompanying notes are an integral part of these statements.

## NOTES TO COMBINED FINANCIAL STATEMENTS

### 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

First Union Real Estate Investments ("Trust") and First Union Management Inc. ("Company") are in the real estate, parking management and parking and transit ticketing equipment manufacturing industries with properties and operations primarily in the United States and Canada. The accounting policies of the Trust and Company conform to generally accepted accounting principles and give recognition, as appropriate, to common practices within the real estate, parking and manufacturing industries.

Under a trust agreement, the shares of the Company are held for the benefit of the shareholders of the Trust. Accordingly, the financial statements of the Company and the Trust have been combined. Additionally, as the Company owns voting control of Imperial Parking Limited ("Impark"), the financial statements of Impark are consolidated with those of the Company.

The preparation of the financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses during the reporting periods. Actual results could differ from these estimates.

The Trust's properties are leased to the Company through February 28, 1999. Thereafter, the Trust became self-managed.

At December 31, 1998 and 1997, buildings and improvements included equipment and appliances of \$8.1 million and \$7.2 million, respectively.

Tenant leases generally provide for billings of certain operating costs and retail tenant leases generally provide for percentage rentals, in addition to fixed minimum rentals. The Trust and Company accrue the recovery of operating costs based on actual costs incurred and accrue percentage rentals based on current estimates of each retail tenant's sales. In July 1998, the Trust adopted the Financial Accounting Standards Board's Emerging Issues Task Force Bulletin 98-9 (EITF-98-9), "Accounting for Contingent Rent in Interim Financial Periods" on a prospective basis. EITF-98-9 requires that contingent rental income, such as percentage rent which is dependent on sales of retail tenants, be recognized in the period that a tenant exceeds its specified sales breakpoint. Consequently, the Trust will accrue the majority of percentage rent income in the fourth quarter of each year in accordance with EITF-98-9. For the years ended December 31, 1998, 1997 and 1996, the accrued recovery of operating costs and percentage rent income approximated \$36.2 million, \$21.9 million and \$15.7 million, respectively. Impark recognizes gross revenue collected or due from parking lots which it manages. Deferred revenue is derived primarily from revenue received in advance of its due date.

Depreciation for financial reporting purposes is computed using the straight-line method. Buildings are depreciated over their estimated useful lives of 10 to 40 years, based on the property's age, overall physical condition, type of construction materials and intended use. Improvements to the buildings are depreciated over the remaining useful life of the building at the time the improvement is completed. Tenant alterations are depreciated over the life of the lease of the tenant. The Trust annually reviews its portfolio of properties for any impairment as required by Statement of Financial Accounting Standards (SFAS) 121 (Accounting for Long-Lived Assets and Long-Lived Assets to be Disposed of).

The Trust's buildings are depreciated as follows:

LIFE (IN YEARS)	BUILDINGS (IN THOUSANDS)
40	\$669,583
30	2,042
25	4,736
10	158
	-----
	\$676,519

The Trust's useful lives for the calculation of depreciation:

Shopping malls	40
Apartments	40
Office buildings	40
Parking garages	25 - 40
Parking facilities	10

Equipment and appliances are depreciated over useful lives of five to ten years. Parking equipment is depreciated using the declining balance method resulting in approximately 20 - 30% of the equipment balance being depreciated per year. Parking leasehold improvements are depreciated over five years. Routine maintenance and repairs, including replacements, are charged to expense; while replacements which improve or extend the lives of existing properties are capitalized.

Goodwill represents the excess of cost over the value assigned to the net assets from the purchase of Impark. Goodwill is amortized on a straight-line basis over 40 years. Accumulated amortization at December 31, 1998 and 1997, was \$2.3 million and \$.8 million, respectively. Impark recorded a U.S. \$15 million reduction of goodwill in December 1998, in accordance with SFAS 121.

Lease and management agreements are recorded at cost and represent Impark's investment in parking lot agreements acquired from other parking lot management companies. The underlying value of this asset is calculated by discounting future cash flows of each agreement over its length of term. Management and lease agreements terminated before the life of the agreements are expensed. Amortization is provided on a straight-line basis over their useful lives of approximately three years as of the acquisition in April 1997. Accumulated amortization at December 31, 1998 and 1997 was \$3.6 million and \$1.3 million, respectively.

Impark's inventory consists of equipment parts and supplies and is recorded at the lower of cost determined on a first-in, first-out basis, or replacement cost.

The Trust accounts for its investment in a joint venture which it does not control using the equity method of accounting. This investment, which represents a 50% non-controlling ownership interest in a shopping mall, was recorded initially at the Trust's cost and subsequently adjusted for the Trust's equity in income and cash distributions.

At December 31, 1998 and 1997, \$12.6 million and \$14.3 million of cash was restricted based on terms of a mortgage. Additionally, \$3.9 million of cash as of December 31, 1998 was classified as restricted as it secures benefits under change of control agreements with employees of the Trust and Company.

Investments as of December 31, 1997, consisted of shares of beneficial interest of other real estate investment trusts and a U.S. Treasury Bill. The shares of beneficial interest were classified as securities available for sale and were reported at their fair value in the balance sheet. The U.S. Treasury Bill was classified as a held-to-maturity security and was recorded at cost plus accrued interest. The U.S. Treasury Bill was collateral to secure an obligation due to the former owners of Impark. The shares of beneficial interest of other real estate investment trusts and the U.S. Treasury Bill were sold in 1998.

The Trust has calculated earnings per share for 1998 and 1997 in accordance with SFAS 128 (Earnings Per Share) and restated 1996. SFAS 128 requires that common share equivalents be excluded from the weighted average shares outstanding for the calculation of basic earnings per share. The reconciliation of shares outstanding for the basic and fully diluted earnings per share calculation is as follows (in thousands):

	1998 -----	1997 -----	1996 -----
Basic weighted average shares	30,772	24,537	17,172
Stock options, treasury method	243	571	367
Restricted shares, treasury method		307	167
	-----	-----	-----
Diluted weighted average shares	31,015	25,415	17,706
	=====	=====	=====

The preferred shares and warrants to purchase shares of beneficial interest are anti-dilutive and are not included in the weighted average shares outstanding for the diluted earnings per share.

The assets and liabilities of the Canadian operations are translated into U.S. dollars at the exchange rates in effect at the balance sheet date. Income statement accounts are translated at the weighted average exchange rates for the year. The gains or losses resulting from these translations are recorded in a separate component of shareholders' equity. Gains or losses resulting from realized foreign currency and intercompany transactions are included in net income.

Financial instruments held by the Trust and the Company include cash and cash equivalents, accounts receivable, mortgage loans receivable, accounts payable, revolving credit agreements, long-term debt, interest rate caps and a currency swap contract. The Trust and the Company do not hold or issue financial instruments or derivative financial instruments for trading purposes.

During 1998, the Financial Accounting Standards Board ("FASB") issued SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities." The statement requires companies to recognize all derivatives on the balance sheet as assets or liabilities, measured at fair value. Gains or losses resulting from changes in the values of those derivatives would be accounted for depending on the use of the derivative and whether it qualifies for hedge accounting. This statement is effective for fiscal years beginning after June 15, 1999. The Trust will adopt this Statement on January 1, 2000, and is in the process of determining the effect that adoption will have on its financial statements.

In March 1998, the American Institute of Certified Public Accountants ("AICPA") issued Statement of Position ("SOP") 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use," which is effective for the Trust and Company as of January 1, 1999. This SOP requires capitalization of certain development costs of software to be used internally.

In April 1998, the AICPA issued SOP 98-5, "Reporting on the Costs of Start-Up Activities," which is effective for the Trust as of January 1, 1999. This SOP requires start-up and organization costs to be expensed as incurred and also requires previously deferred start-up costs to be recognized as a cumulative effect adjustment in the statement of income upon adoption.

These SOPs, which the Trust and Company plan to adopt as of January 1, 1999, are not expected to have a material effect on the Trust's and Company's financial statements.

Certain reclassifications have been made to prior year balances so that they are comparable to 1998.

## 2. RESTATEMENT OF COMBINED FINANCIAL STATEMENTS

The Trust has restated its Combined Financial Statements for each of the five years ended December 31, 1998 as a result of changing the lives of assets used to calculate depreciation expense. The cumulative effect of changing the lives of the assets for years prior to 1994 results in a charge to undistributed income as included in shareholders equity of approximately \$22 million.

Net income and net income per share both basic and diluted prior to and after the restatement for the change in depreciation lives are disclosed in the following table (amounts in thousands except per share):

YEAR	NET INCOME AS PREVIOUSLY REPORTED	CHANGE IN DEPRECIATION EXPENSE	CHANGE IN CAPITAL GAINS FOR SOLD PROPERTIES BASED ON RESTATED DEPRECIATION	RESTATED NET INCOME
----	-----	-----	-----	-----
1997	\$ 3,043	\$(3,441)	\$1,243	\$ 845
1996	3,291	(2,741)	---	550
1995	13,891	(2,375)	1,707	13,223
1994	6,485	(2,224)	---	4,261

YEAR	NET INCOME PER SHARE AS PREVIOUSLY REPORTED	CHANGE IN DEPRECIATION EXPENSE PER SHARE	CHANGE IN CAPITAL GAIN PER SHARE	RESTATED NET INCOME (LOSS) PER SHARE
----	-----	-----	-----	-----
1997	\$.12	\$(.14)	\$.05	\$.03
1996	.19	(.16)	---	.03
1995	.77	(.13)	.09	.73
1994	.36	(.12)	---	.24

## 3. LIQUIDITY

The Trust has a \$90 million note payable due on August 11, 1999 and the reduction of the availability of its bank loan facility commitment during 1999 with the facility to be terminated on August 11, 1999.

As of December 31, 1998, the Trust has \$90 million outstanding under the notes payable and \$101 million outstanding under the bank credit facility. The Trust plans to repay the debt in 1999 with a combination of property sales, a \$50 million rights offering, mortgage financing, and cash available.

The Trust sold a shopping center and an office building in the first quarter of 1999 generating \$11.1 million of net proceeds which was used to repay a portion of the note payable. Additionally, the Trust has entered into contracts to sell six properties to generate \$45.6 million in net proceeds and obtain \$66.4 million in mortgage financing on seven properties. The sale of the properties and mortgage financing is to be completed throughout the second quarter of 1999. The Trust also expects to complete a rights offering of approximately \$50 million in April 1999 pending an effective registration statement. The cash generated from these transactions is expected to approximate \$162 million. Additionally, the Trust had \$28.6 million of cash at December 31, 1998.

As a contingency to the aforementioned sales transactions, the Trust has contracted to sell an additional five shopping malls which is anticipated to generate \$56.8 million in net proceeds.

Although the Trust believes that the transactions listed above will occur as planned, there can be no assurance that each transaction will be completed or they will occur in the time frame or at the anticipated amounts.



#### 4. COMPREHENSIVE INCOME

Effective January 1, 1998, the Trust adopted SFAS 130 (Reporting Comprehensive Income) which requires disclosure of comprehensive income and its components in a full set of general-purpose financial statements. Comprehensive income is defined as changes in shareholders' equity such as foreign currency translation adjustments and reserves for the valuation of securities held for sale. The adoption of this statement had no impact on the Trust's net income or shareholders' equity. Prior year financial statements have been reclassified to conform to the requirements of this statement.

#### 5. WARRANTS TO PURCHASE SHARES OF BENEFICIAL INTEREST

The Trust in November 1998 issued 500,000 warrants which allow a third party to purchase 500,000 shares of beneficial interest at \$10 per share. The warrants expire in November 2008. The Trust issued the warrants to the third party as part of the consideration for various services provided to the Trust and recorded \$.4 million in expense as a measurement of this consideration. The fair value of the consideration was determined using the Black-Scholes model with the warrants' term of 10 years, a 4% dividend yield, a 4% risk free interest rate and a volatility factor of 32%.

#### 6. FINANCIAL INSTRUMENT

In 1997, the Trust entered into a foreign currency swap agreement maturing in 2009 to reduce the impact of foreign exchange rates on intercompany debt. The contract was tied to a \$36 million Canadian principal, 4% per annum interest obligation with respect to a \$26 million U.S. principal, 4.065% per annum interest, intercompany transaction. Both notional amounts increased by approximately 8% per annum. The interest differential paid or received on the swap contract was recognized as an adjustment to interest expense. The Trust was required to collateralize its position in the swap contract with a \$2 million U.S. interest bearing deposit as of December 31, 1997. The collateral amount was not impaired as of December 31, 1997. In June 1998, the Trust sold the swap agreement for \$825,000 in cash and was returned its full collateral securing this agreement.

#### 7. COMBINED STATEMENTS OF CHANGES IN CASH

The Trust and the Company consider all highly liquid short-term investments with original maturities of three months or less to be cash equivalents. The Trust and Company paid interest of \$51.4 million, \$29.9 million and \$24.1 million in 1998, 1997 and 1996, respectively. During 1996, \$121,000 of interest related to construction projects was capitalized.

#### 8. UNREALIZED LOSS ON CARRYING VALUE OF ASSETS IDENTIFIED FOR DISPOSITION AND IMPAIRED ASSET

Management reviews the net realizable value of the Trust's portfolio periodically to determine whether an allowance for possible losses is necessary. The carrying value of the Trust's investments in real estate is evaluated on an individual property basis in accordance with SFAS 121. In December 1998, the Trust recorded \$36 million in unrealized losses on the carrying value of three shopping centers, two office properties and a parking facility which were identified for disposition. The Trust determined that these assets, which are actively being marketed for sale, were impaired based on the bids received for these assets as compared to their net book value. The bids received for these assets best represent the cash flow to be realized in accordance with SFAS 121. Assets identified for disposition as of December 31, 1998, had a net book value of \$44.2 million, net of the \$39.6 million balance of the asset reserve as of December 31, 1998.

Impark recorded a \$15 million U.S. reduction of goodwill in December 1998, in accordance with SFAS 121. Management annually evaluates the amortization life for goodwill by reviewing the recoverability of Impark's assets, including goodwill related to the acquisition of Impark. Measurement of the recoverability of the net book value of Impark is based on estimated undiscounted future cash flows of Impark over a holding period and applying a multiple of earnings of similar companies to value the entire operations, including goodwill. When the recoverability of Impark's assets, including goodwill, is less than its net book value, a discount factor is applied to the estimated future cash flows and the resulting amount is then compared to the net book value. The difference is recognized as an impairment under SFAS 121 by reducing goodwill. The estimates used for future cash flows may differ from actual performance due to the number of variables having an effect on daily operations and markets in which these operations are located.

In January 1997, the Trust sold a shopping center for \$9 million in cash. The sale resulted in a capital loss of \$4 million which was provided for as part of a \$14 million noncash, unrealized loss on the carrying value of certain assets that was recorded in December 1995.

In February 1996, the Trust sold two office buildings and an attached parking garage in Cleveland, OH for \$1.8 million in cash and a \$7 million, 8% note secured by the properties. The note was repaid in June 1996. This sale resulted in a capital loss of \$5.5 million which was provided for as part of a \$14 million noncash, unrealized loss on the carrying value of certain assets that was recorded in December 1995.

The amount of assets identified for sale, the reserve for loss and the losses deducted from the reserve are summarized for the years ended December 31 in the following table (amounts in thousands):

	1998 -----	RESTATED 1997 -----	RESTATED 1996 -----
Assets identified for sale			
Net book value of assets identified for sale (At historical cost less accumulated depreciation)	\$ 5,163	\$ 27,451	\$ 41,527
Additions	79,034	808	1,362
Depreciation	(360)	(387)	(1,312)
Sales of assets		(22,709)	(14,126)
	-----	-----	-----
Net book value of assets identified for sale at year end	\$ 83,837 =====	\$ 5,163 =====	\$ 27,451 =====
Reserve for loss	\$ 3,630	\$ 7,605	\$ 13,060
Additions to reserve	36,000		
Losses realized on sale of assets		(3,975)	(5,455)
	-----	-----	-----
Reserve at year end	\$ 39,630 =====	\$ 3,630 =====	\$ 7,605 =====

Property net operating income which is rents less operating expenses for assets identified for disposition are summarized for the years ended December 31 in the following table (amounts in thousands):

	1998 -----	1997 -----	1996 -----
Revenues	\$15,217	\$17,145	\$20,842
Operating expenses	7,756	8,456	9,895
	-----	-----	-----
Property net operating income	\$ 7,461 =====	\$ 8,689 =====	\$10,947 =====

## 9. CAPITAL GAINS AND LOSSES

In May 1998, the Trust sold its investment in the land beneath the Huntington Building in Cleveland, OH for \$6.1 million resulting in a capital gain of \$1.7 million. Additionally, an \$18.8 million mortgage investment secured by the Huntington Building was repaid in 1998 resulting in the recognition of a \$7.7 million capital gain which was deferred when the building was sold in 1982 since the Trust received the mortgage note as consideration. In June 1998, the Trust sold a forward exchange agreement resulting in a gain of \$.8 million. The forward exchange contract was purchased to protect the Trust from foreign currency fluctuations resulting from notes issued in conjunction with the acquisition of Impark. In December 1998, the Trust sold a land parcel in Monroe, LA resulting in a gain of \$.1 million.

In November 1997, the Trust sold an apartment complex in Dayton, OH, for \$.7 million in cash, a \$2.6 million, 8.75% second mortgage, secured by the property, and the assumption by the purchaser, of a \$7.6 million existing mortgage loan. The capital gain recognized was \$2.7 million. In December 1997, the Trust sold an office complex in Oklahoma City, OK, for \$4.7 million in cash resulting in a capital loss of \$1.2 million.

## 10. EXTRAORDINARY LOSS FROM EARLY EXTINGUISHMENT OF DEBT

In 1998, the Trust repaid \$87.5 million of its 8 7/8% senior notes resulting in \$1.6 million of unamortized issue costs and solicitation fees being expensed. Additionally, the Trust renegotiated its bank credit agreement and the terms of the \$90 million note payable in 1998 resulting in \$.8 million of deferred costs related to the bank credit agreement and note payable being expensed.

In 1997 and 1996, the Trust renegotiated its bank credit agreements resulting in \$226,000 and \$286,000, respectively, of deferred costs relating to its prior bank credit agreements being expensed.

## 11. ACQUISITIONS

On April 17, 1997, the Company acquired voting control of Impark for \$36.6 million in cash, assuming \$26 million in debt and issuing to its former owners \$10.5 million in non-voting stock in Impark and issuing to Impark employees \$.7 million of non-voting stock, \$.2 million in voting stock and \$1 million in preferred stock of Impark. The transaction was recorded using purchase accounting.

On September 1, 1997, the Trust purchased the interests of its joint venture partners in eight shopping malls and 50% of another mall for \$88 million in cash and the assumption of \$203 million of mortgage debt. The transaction was recorded using purchase accounting.

The following unaudited pro forma information presents a summary of consolidated results of the Trust, the Company and Impark and the former joint venture properties as if the acquisitions occurred at the beginning of 1996 with pro forma adjustments to give effect to the amortization of goodwill, management and lease agreements, depreciation of property and interest expense (in thousands, except per share data):

(UNAUDITED)	RESTATED 1997	RESTATED 1996
Revenue	\$323,104	\$313,303
Net income (loss) applicable to shares of beneficial interest	(71)	47
Net income (loss) applicable to shares of beneficial interest per share	--	--

## 12. LIABILITY TO FORMER OWNERS OF IMPARK

The Company issued \$10.5 million in non-voting common stock in Impark to its former owners in connection with the acquisition of Impark. The purchase price payable under the non-voting common stock increased from the aggregate issue price as of April 17, 1997 at an 8% per annum rate on the outstanding amount for the first six months and compounded by an additional one percentage point per annum each six month period thereafter up to a maximum rate of 17% per annum. To secure the Trust's obligations under this agreement, the Trust placed United States Treasury securities on deposit with a trustee and classified these securities as Investments in the December 31, 1997 Combined Balance Sheets. The non-voting common stock was recorded as an Other Liability in the Combined Balance Sheets as of December 31, 1997 and was being accreted to its final put price as a charge to expense. On June 1, 1998 the Company purchased the remaining non-voting common stock of Impark that it did not own for \$11.2 million and the Trust subsequently sold the United States Treasury securities that served as collateral.

## 13. INVESTMENTS IN MORTGAGE LOANS AND NOTES RECEIVABLE

As of December 31, the Trust had the following investments in mortgage loans and notes receivable (amounts in thousands):

	CURRENT RATE ON INVESTMENT	1998	1997
First mortgage loan secured by an office building in Cleveland, OH, maturing in 2011	9.65%		\$18,908
Mortgage loan secured by a mall in Fairmont, WV, maturing in 1998 and partnership units of Crown American Properties, L.P.	9%		6,199
Second mortgage loan secured by an apartment complex in Dayton, OH, maturing in 2002	8.75%	\$2,581	2,600
Note receivable secured by management contract on an apartment complex in Atlanta, GA, maturing in 2008	10%	1,727	1,779
Note receivable secured by Temple Mall Company, maturing in 2023	6%	1,200	1,200
		\$5,508	\$30,686

The Cleveland, OH and Fairmont, WV mortgages were paid in full in 1998. The book value of mortgage investments approximates fair market value as of December 31, 1998 based on current market conditions and market interest rates.

## 14. BANK LOANS

### TRUST

As of December 31, 1998, the Trust has \$101 million outstanding under a fully secured \$110 million credit agreement at a weighted interest rate of 8.37% and 8.02% for December 31, 1997. In accordance with an agreement in principle subject to final documentation; the credit available under this agreement is reduced to \$80 million on April 30, 1999 and \$50 million on June 30, 1999. The pending agreement will amend the present commitment reduction dates of March 17, 1999 and May 17, 1999, respectively. The Trust expects to pay a fee of \$.3 million to obtain the additional time period. The agreement in principle also provides for a reduction in the total credit facility commitment from \$110 million. It also requires that \$9 million of proceeds from an anticipated rights offering be used to repay exiting borrowings. This credit agreement matures in August 1999. Interest under this agreement is calculated, at the option of the Trust, based on an Eurodollar rate plus 300 basis points or the prime rate of the lender plus 50 basis points. The Trust may not use borrowings under this credit agreement to repay any other existing debt of the Trust, the Company or Impark. Additionally, the Trust has posted an \$8 million letter of credit as collateral for Impark's credit facility, reducing the Trust's available borrowing by this amount. As the bank loans are at market interest rates, the fair value is the carrying amount of the loans. The weighted average interest rate for 1998 and 1997 for the credit agreement was 7.9% and 8%, respectively.

Commitment fees not greater than 3/8% per annum are payable on the unused portion of the revolving credit

agreement. The agreement contains certain requirements including maintaining minimum funds from operations (income from operations plus depreciation and amortization), net worth, leverage, debt service and interest coverage. The Trust obtained a waiver at September 30, 1998 for violation of its financial covenants and also obtained modification to the debt service, interest coverage and net worth requirements and the methodology for calculating net income by excluding certain non-recurring or extraordinary charges or expenses through the termination of the credit facility. Also, the Trust has received a waiver with respect to the change in the majority of the Trust's Board of Trustees until June 30, 1999. The waiver and modification of the calculation of net income was obtained for an \$8 million fee. The Trust is in compliance with the required covenants as of December 31, 1998.

The Trust has a rate guarantee contract in the notional amount of \$73.5 million which is tied to LIBOR increasing to a maximum rate of 7%. This rate contract is used by the Trust to reduce the impact of changes for interest rates on its floating rate bank loans. The contract expires in October 2000 and the cost is being amortized over the life of the contract.

## **IMPARK**

As of December 31, 1998, Impark has \$33.8 million Canadian outstanding under a secured credit agreement at an weighted average interest rate of 7% and 6% for December 31, 1997. The credit agreement consists of revolving, acquisition, and term bank commitments of \$6.5 million, \$9 million and \$31.4 million Canadian, respectively. The revolving, acquisition and term bank facilities have \$1.5 million, \$9 million, and \$31.4 million Canadian outstanding, respectively, at December 31, 1998. The credit agreement matures in April 2000. The weighted average interest rate for the credit agreement was 7% for 1998 and 5.6% for 1997. As the bank loans are at market interest rates, the fair value is the carrying amount of the loans.

The Trust for a fee to the bank facility lenders, provided a letter of credit for \$8 million U.S. to secure a portion of the balance outstanding under the bank facility, and has agreed to collateralize, on August 11, 1999, the bank facility with \$5 million U.S. in securities and to allow the bank facility to be put to the Trust in November 1999.

The revolving and acquisition credit facilities bear interest at the lender's prime rate plus 50 basis points and the term facility bears interest at the Canadian Bankers Acceptance rate plus 150 basis points. Both interest rates increase by 25 basis points after June 30, 1999. Additionally, Impark will pay a fee of 55 basis points retroactive to the bank credit facilities inception date to the lenders upon maturity of the credit facility. In exchange for a fee of \$4 million Canadian, Impark has obtained reduced requirements under its interest coverage and leverage financial covenants through September 30, 1999 and may deduct certain non-recurring or extraordinary charges for determining earnings before interest, taxes, depreciation and amortization for covenant purposes. The fee also waived Impark's non-compliance with its financial covenants at September 30, 1998. Impark also received a waiver for the change in the majority of the Trust's Board of Trustees through June 30, 1999. Impark was in compliance with its bank covenants at December 31, 1998.

## **15. MORTGAGE LOANS PAYABLE AND DEFERRED OBLIGATION**

As of December 31, 1998, the Trust had outstanding \$345 million of mortgage loans due in installments extending to the year 2018. Interest rates on fixed rate mortgages range from 6.869% to 12.25% with \$34 million of mortgage loans bearing interest based on LIBOR. The weighted average interest rate of these mortgages is 7.32% at December 31, 1998. Principal payments due during the five years following December 31, 1998 are \$4.3 million, \$4.7 million, \$39.1 million, \$52.3 million and \$5.6 million, respectively. A \$38.7 million mortgage at 12.25% requires participation in the cash flow of the secured property over predefined levels. An \$162.1 million mortgage note at 8.43% requires all rents and other tenant charges from the seven properties that are security for the mortgage to be directly deposited into a bank account which is pledged as additional security for the mortgage note and is restricted in use by the lender. The Trust also has outstanding a \$10.6 million deferred obligation at an interest rate of 14.88%, which is due upon demand. The fair value of the mortgage loans payable and deferred obligation at December 31, 1998 is approximately book value based on current market interest rates and market conditions.

## **16. SENIOR NOTES**

In July 1998, the Trust commenced a tender offer to purchase for cash all \$100 million principal amount of its 8 7/8% Senior Notes due 2003 at \$970 per \$1,000 principal amount of Senior Notes, plus accrued and unpaid interest. Concurrent with the tender offer, the Trust conducted a consent solicitation and offered a consent payment of \$30 per \$1,000 principal amount of Senior Notes to amend the indenture governing the Senior Notes and to terminate listing of the Senior Notes on the New York Stock Exchange. In August 1998, pursuant to the tender offer and consent solicitation, holders of approximately 88% of the outstanding Senior Notes consented to the indenture amendments and delisting and the Trust purchased approximately \$87.5 million principal amount of Senior Notes. The Trust has approximately \$12.5 million of 8 7/8% Senior Notes outstanding at December 31, 1998. The fair value of the Senior Notes is approximately \$12.4 million based on current market quotations.

## **17. PREFERRED SHARES OF BENEFICIAL INTEREST**

In October 1996, the Trust issued \$57.5 million of Series A cumulative convertible redeemable preferred shares of beneficial interest ("Series A Preferred Shares"). The 2,300,000 Series A Preferred Shares were issued at a par value of \$25 per share and are each convertible into 3.31 shares of beneficial interest. The distributions on the

Series A Preferred Shares are cumulative and equal to the greater of \$2.10 per share (equivalent to 8.4% of the liquidation preference per annum) or the cash distributions on the shares of beneficial interest into which the Series A Preferred Shares are convertible (determined on each of the quarterly distribution payment dates for the Series A Preferred Shares). The Series A Preferred Shares are not redeemable prior to October 29, 2001, and at no time will they be redeemable for cash. On and after October 29, 2001, the Series A Preferred Shares are redeemable at the option of the Trust at the conversion rate of one Series A Preferred Share for 3.31 shares of beneficial interest. The Trust may exercise its option only if for 20 trading days within any period of 30 consecutive trading days, the closing price of the shares of beneficial interest on the New York Stock Exchange equals or exceeds the conversion price of \$7.5625 per share of beneficial interest.

In February 1998, 951,000 preferred shares of beneficial interest were converted to 3,144,000 shares of beneficial interest.

## 18. NOTES PAYABLE

The Trust as of December 31, 1998 has notes payable of \$90 million and \$4.9 million outstanding.

The \$90 million note payable bears interest at 12% and has a final maturity of August 11, 1999. The Trust has an agreement in principle with the lenders, subject to final documentation, whereby the Trust will be required to reduce the outstanding principal balance to less than \$70 million by May 15, 1999 and to less than \$50 million by May 31, 1999. Additionally, a fee of 1% of the outstanding balance as of February 11, 1999, a fee of 50 basis points of the outstanding principal amount of the note on March 31, 1999 if the balance exceeds \$60 million, and a fee of 50 to 100 basis points of the outstanding note balance on May 31, 1999 depending on the balance outstanding is required to be paid under the terms of the note. The Trust agreed, in principle, to pay a fee of \$2.0 million to obtain a stand-by purchase commitment for two noteholders, who are also shareholders, to purchase up to \$50 million from a contemplated rights offering. The note payable lenders have agreed, in principle, to allow \$9.0 million of the net proceeds from the rights offering, that would otherwise be used to repay a portion of the note payable, to be used to repay the bank loans. This \$9.0 million portion of the note payable will bear interest at 15% annually and matures on August 11, 1999. Of the \$2.0 million stand-by commitment fee, Gotham entities are collectively entitled to receive \$1.6 million but agreed to accept only \$1.4 million. The other stand-by purchaser will receive \$4 million. The standby commitment fee is payable whether or not the offering is consummated and is payable upon the earlier of the closing of the offering or March 31, 1999. Additionally, if a second rights offering is conducted by the Trust, the standby purchasers are entitled to another fee of up to 4% of their standby commitment unless the Trust cancels or decreases the standby commitment. The standby purchasers possess certain rights to terminate their obligation as standby purchasers under both the first and second offerings. The standby purchase arrangements with respect to the first offering expire on April 15, 1999 and with respect to the second offering expire on August 11, 1999. The note payable requires that the Trust and Impark be in compliance with all financial covenants under its bank facilities. The note payable lenders granted the Trust a waiver under this requirement as of September 30, 1998, in exchange for a fee of \$300,000. The Trust is in compliance with the note payable covenants as of December 31, 1998. The fair value of the note payable is book value based on current market conditions.

The Trust has a \$4.9 million note payable to the trustee of an escrow account which secures the change in control agreements entered into by the Trust and the Company with their employees. The note is payable upon demand by the trustee. The fair value of the note payable is book value based on current market conditions.

## 19. SHARE OPTIONS

The Trust has the following share option plans for key personnel.

### 1981 STOCK OPTION PLAN

This plan provides that option prices be at the fair market value of the shares at the date of grant and that option rights granted expire 10 years after the date granted. Adopted in 1981, the plan originally reserved 624,000 shares for the granting of incentive and nonstatutory share options. Subsequently, the shareholders approved amendments to the plan reserving an additional 200,000 shares, for a total of 824,000 shares, for the granting of options and extending the expiration date to December 31, 1996. The amendments did not affect previously issued options. In June 1998, a change in the majority of the Trust's Board of Trustees resulted in all share options not previously vested to become fully vested as of that date.

The activity of the plan is summarized for the years ended December 31 in the following table:

	1998	WEIGHTED	1997	WEIGHTED	1996	WEIGHTED
	SHARES	AVERAGE	SHARES	AVERAGE	SHARES	AVERAGE
	-----	-----	-----	-----	-----	-----
Granted	---		---		409,500	\$7.37
Exercised	186,155	\$8.51	39,809	\$7.64	9,455	9.42
Canceled	317,281	8.22	13,590	13.14	96,450	15.84
Expired	16,120	17.43	22,880	17.55	21,640	24.76
Available	---		---		23,427	

As of December 31, 1998, the following options were outstanding under the 1981 plan:

Year Options Granted	Options Outstanding				Options Exercisable	
	Number Outstanding	Range of Exercise Prices	Weighted Average Remaining Years of Options	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
1989	31,720	\$17.07-18.87	.70	\$17.51	31,720	\$17.51
1990	3,120	11.06	1.80	11.06	3,120	11.06
1992	2,000	10.00	3.80	10.00	2,000	10.00
1994	6,250	7.375	5.30	7.375	6,250	7.375
1996	69,240	7.375	7.20	7.375	69,240	7.375
	112,330			\$10.386	112,330	\$10.386
	=====			=====	=====	=====

The weighted average of 631,886 options outstanding on January 1, 1998 was \$ 8.93 per share.

Included in the above table are 9,360 shares that the Company may purchase from the Trust at prices ranging from \$11.06 to \$17.07 per share to satisfy the Company's obligations to deliver shares to certain of its key employees pursuant to options previously granted. The option agreements with the Company's employees provide that option prices be at the fair market value of the Trust shares at the date of grant and that option rights granted expire 10 years after the date granted.

#### 1994 LONG-TERM INCENTIVE OWNERSHIP PLAN

This plan, adopted in 1994, reserved 1,629,785 shares for the granting of incentive and nonstatutory share options and restricted shares. In accordance with the plan, 9% of the shares of beneficial interest resulting from the conversion of preferred shares in February 1998 and the January and June 1997 shares of beneficial interest offerings have been reserved and added to the plan for grant. The share options expire eight to ten years after being granted. The price of the options is the fair market value of the shares at the date of grant with the exception of the option grants in 1998. The stock options granted in 1998 were granted at exercise prices exceeding market. Additionally, these options have a cost of capital feature whereby the exercise price of the options will increase by 10%, compounded annually and prorated monthly, beginning in May 2000 and in each November thereafter, less the amount of per share dividends or other distributions to shareholders. As the 1998 option grants are deemed to be variable, compensation expense will be recorded when the market price of shares of beneficial interest exceeds the option price for these shares at the date of grant for these options. As of December 31, 1998, the option price of shares of beneficial interest did not exceed the market price of shares of beneficial interest, consequently no compensation expense was recorded for 1998. In June 1998, a change in the majority of the Trust's Board of Trustees occurred resulting in all stock options vesting that had been previously granted.

Since the inception of this plan and prior to the June 1998 change in the composition of the Board of Trustees, restricted shares were issued to key employees. The restricted shares received dividends and had voting rights but could not be sold or transferred until the restriction period lapsed after eight years from the date of grant, or earlier if the Trust's share price equaled or exceeded \$21 for 20 consecutive days, or upon a change in control as defined in the plan. Restricted shares were granted when defined levels of funds from operations and net capital gains were achieved during any four consecutive calendar quarters. Additionally, restricted shares were granted in place of share options. These restricted shares received dividends and had voting rights but could not be sold or transferred for four years or upon a change in control as defined in the plan. Beginning in 1998, other restricted shares were granted to plan participants based on defined improvements to funds from operations and shareholder return. These restricted shares were to vest when funds from operations for four consecutive quarters doubled as compared to the funds from operations in the quarter the restricted shares were granted, or the share price of shares of beneficial interest was 50% greater than the share price on the five trading days of the quarter immediately preceding the grant date of the shares, or upon a change of control as defined in the plan. The restricted shares received dividends and were eligible to vote. In June 1998, a change in the majority of the Trust's Board of Trustees occurred resulting in all restrictions being removed from the restricted shares that had been previously granted and a \$4.7 million expense was recorded for the remaining deferred compensation which had not been expensed as of that date. Deferred compensation of \$5 million in 1998, \$3.2 million in 1997 and \$1.7 million in 1996 was recorded. Amortization of the deferred compensation of \$312,000, \$746,000 and \$499,000, respectively, was recognized in 1998, 1997 and 1996.



The activity of this plan is summarized for the years ended December 31 in the following table:

	1998 SHARES	WEIGHTED AVERAGE	1997 SHARES	WEIGHTED AVERAGE	1996 SHARES	WEIGHTED AVERAGE
Share options granted	1,800,000	\$ 7.50	327,000	\$14.19	79,000	\$7.38
Share options canceled	501,468	10.83	7,102	7.38	18,400	7.37
Share options exercised	168,382	7.10	52,754	7.31	10,700	6.84
Restricted shares granted	343,964		226,867		142,500	
Restricted shares canceled	606,852		3,521		37,007	
Shares purchased by employees	18,499		9,005		11,094	
Additional shares reserved	282,941		921,150			
Available share options and restricted shares	270,485		1,041,687		672,786	

As of December 31, 1998, the 1994 plan had the following options outstanding:

Year Options Granted	Outstanding Options			Options Exercisable		
	Number Outstanding	Range of Exercise Prices	Weighted Average Remaining Years of Options	Number Exercisable	Weighted Average Exercise Price	Weighted Average Exercise Price
1995	11,003	\$ 7.50-7.75	4.40	11,003	\$ 7.6629	\$ 7.6629
1996	21,171	7.375	5.20	21,171	7.375	7.375
1997	60,000	14.125-14.25	6.30	60,000	14.1875	14.1875
1998	1,800,000	6.50-8.50	9.83		7.50	
	1,892,174			92,174	\$7.7116	\$11.8439
	=====			=====	=====	=====

The weighted average price of the 762,024 options outstanding as of January 1, 1998 is \$10.13 per share.

The Trust accounts for stock option awards in accordance with APB 25 and has adopted the disclosure-only provisions of SFAS 123 (Accounting for Stock-Based Compensation). Consequently, no compensation cost has been recognized for the share option plans. If compensation expense for the Trust's two share option plans had been recorded based on the fair value at the grant date for awards in 1998, 1997 and 1996, consistent with SFAS 123, the Trust's net income would be adjusted as follows (amounts in thousands, except per share data):

	1998	Restated 1997	Restated 1996
Net income (loss) applicable to shares of beneficial interest	\$(86,517)	\$845	\$550
Effect of stock options as calculated	(557)	(569)	(430)
Net income (loss) as adjusted	\$(87,074)	\$ 276	\$120
	=====	=====	=====
Per share			
Basic and diluted:			
Net income (loss)	\$(2.81)	\$.02	\$.03
Effect of stock options as calculated	(.02)	(.02)	(.02)
Net income (loss), as adjusted	\$(2.83)	\$ --	\$.01
	=====	=====	=====

The fair value of each option grant is estimated on the date of the grant using the Black-Scholes option pricing model, with the following weighted average assumptions used for grants in 1998, 1997 and 1996.

	1998	1997	1996
Risk-free interest rate	5%	5.7%	6.35%
Expected option life	10	4	10
Expected volatility	32%	23%	30%
Expected dividend yield	4%	3.5%	3.5%

## 20. SHAREHOLDER RIGHTS PLAN

In March 1990, the Board of Trustees declared a dividend consisting of one right to purchase one share of beneficial interest of the Trust with

respect to each share of beneficial interest. The rights may be exercised only if a person or group acquires 15% or more of the outstanding shares of beneficial interest, makes a tender offer for at least

15% of the outstanding shares of beneficial interest or is declared to be an "adverse person." The exercise price of each right is \$50. If a person or group acquires 15% or more of the outstanding shares of beneficial interest (except in a tender offer approved by the Board of Trustees), is declared to be an "adverse person" or engages in certain self-dealing transactions with the Trust ("flip-in events"), each right (other than rights owned by a 15% owner or an "adverse person") entitles the holder to purchase one share of beneficial interest of the Trust for par value (now \$1 per share). The Board of Trustees has agreed to increase the 15% threshold for shares of beneficial interest acquired through a contemplated rights offering so that a "flip-in" event will not occur due to the rights offering. If the Trust is acquired in a merger or other business combination ("flip-over events"), each right entitles the holder to purchase, for \$1, shares of the acquiring company having a market value equal to the market value of one share of beneficial interest of the Trust. The rights may be redeemed by the Trust at a price of \$0.01 per right at any time prior to the earlier of a "flip-in" or "flip-over" event or the expiration of the rights on March 30, 2000.

## 21. FEDERAL INCOME TAXES

The Trust has made no provision for current or deferred income taxes on the basis that it qualified under Sections 856-860 of the Internal Revenue Code as a real estate investment trust and has distributed all of its taxable income to shareholders. The Trust and Company have accrued \$.6 million and \$1.2 million in taxes relating to Canadian operations for 1998 and 1997, respectively.

The Trust and Company treat certain items of income and expense differently in determining net income reported for financial reporting and tax purposes. Such items resulted in a net increase in income for tax reporting purposes of approximately \$69 million in 1998, \$8 million for 1997, and a net increase of \$1.6 million for 1996.

As of December 31, 1998, net investments after accumulated depreciation in real estate for tax purposes was approximately \$655 million.

The 1998 quarterly allocation of cash dividends per share of beneficial interest for individual shareholders' income tax purposes was as follows:

DATE PAID -----	LONG-TERM CAPITAL GAINS	ORDINARY INCOME	TOTAL PAID
February 2, 1998	\$.1066	\$.0034	\$.11
April 30, 1998	.1066	.0034	.11
	-----	-----	-----
	\$.2132	\$.0068	\$.22
	=====	=====	=====

For the year ended December 31, 1997, the cash dividends paid of \$.44 consisted of \$.3174 per share of ordinary income and \$.1226 per share of capital gains, and for the year ended December 31, 1996, \$.422 per share of ordinary income and \$.018 per share of capital gains.

The 1998 quarterly allocation of cash dividends per share for the preferred shares of beneficial interest for individual shareholders' income tax purposes was as follows:

DATE PAID -----	LONG-TERM CAPITAL GAINS	ORDINARY INCOME	TOTAL PAID
February 2, 1998	\$.5086	\$.0164	\$.525
April 30, 1998	.5086	.0164	.525
July 31, 1998	.5086	.0164	.525
October 30, 1998	.5086	.0164	.525
	-----	-----	-----
	\$2.0344	\$.0656	\$2.10
	=====	=====	=====

For the year ended December 31, 1997, the cash dividends paid of \$2.1172 per share for the preferred shares of beneficial interest consisted of \$1.5272 per share of ordinary income and \$.59 of capital gain.

## 22. LEGAL CONTINGENCY

The Trust has pursued legal action against the State of California associated with the 1986 flood of Sutter Buttes Center, formerly Peach Tree Center. In September 1991, the court ruled in favor of the Trust on the liability portion of this inverse condemnation suit, which the State of California appealed. The Trust is proceeding with its damage claim. No recognition of potential income has been made in the accompanying Combined Financial Statements.

### 23. BUSINESS SEGMENTS

In 1998, the Trust and Company adopted SFAS No. 131 (Disclosures about Segments of an Enterprise and Related Information). This statement requires companies to identify segments consistent with the manner in which management makes decisions about allocating resources to segments and measuring their performance.

The Trust's and the Company's business segments include ownership of shopping centers, apartment complexes, office buildings, parking facilities, mortgage investments and parking management (Impark). Corporate rent and operating expense consist primarily of ground lease income from a property leased to a third party. Rent, property operating expense and real estate taxes, interest expense, depreciation, capital improvements and identifiable assets for real estate assets and for Impark have been identified for each of the business segments for the last three years. Impark derives 87% and 88% of its rent from Canadian operations for 1998 and 1997, respectively. Property net operating income is property rent less property operating expense and real estate taxes. Corporate interest expense consists of the Trust's non-recourse notes payable, senior note, and bank loan interest expense. Corporate depreciation and amortization consist primarily of the amortization of deferred issue costs on non-recourse debt and the leasehold improvements for its corporate office. Corporate assets consist primarily of cash and cash equivalents, leasehold improvements for the corporate offices and deferred issue costs for non-recourse debt and senior notes. All intercompany transactions between segments have been eliminated. (See table of business segments on next page.)

	1998	RESTATED 1997	RESTATED 1996
	----	----	----
Rents			
Shopping Centers	\$ 97,584	\$ 58,284	\$ 42,570
Apartments	17,056	17,835	16,306
Office Buildings	13,275	13,989	11,794
Parking Facilities	10,805	4,206	3,722
Impark	180,760	129,918	---
Corporate	1,112	1,156	1,163
	-----	-----	-----
	\$ 320,592	\$ 225,388	\$ 75,555
Less - Operating Expenses			
Shopping Centers	\$ 32,433	\$ 17,182	\$ 11,911
Apartments	6,182	6,729	6,105
Office Buildings	6,069	6,753	6,701
Parking Facilities	2,444	1,017	200
Impark	175,625	124,624	---
Corporate	914	910	869
	-----	-----	-----
	\$ 223,667	\$ 157,215	\$ 25,786
Less - Real Estate Taxes			
Shopping Centers	\$ 8,918	\$ 6,857	\$ 5,736
Apartments	975	1,382	1,234
Office Buildings	992	1,085	885
Parking Facilities	1,568	624	442
	-----	-----	-----
	\$ 12,453	\$ 9,948	\$ 8,297
Property Net Operating Income			
Shopping Centers	\$ 56,233	\$ 34,245	\$ 24,923
Apartments	9,899	9,724	8,967
Office Buildings	6,214	6,151	4,208
Parking Facilities	6,793	2,565	3,080
Impark	5,135	5,294	---
Corporate	198	246	294
	-----	-----	-----
	\$ 84,472	\$ 58,225	\$ 41,472
Less - Depreciation and Amortization			
Shopping Centers	\$ 15,880	\$ 10,414	\$ 8,574
Apartments	2,751	2,952	2,796
Office Buildings	4,282	3,963	3,410
Parking Facilities	1,604	281	214
Impark	5,789	4,105	---
Corporate	3,083	1,177	896
	-----	-----	-----
	\$ 33,389	\$ 22,892	\$ 15,890
Less - Interest Expense			
Shopping Centers	\$ 23,832	\$ 11,224	\$ 4,693
Apartments	2,819	3,406	2,951
Office Buildings	---	15	143
Parking Facilities	2,381	784	753
Impark	2,682	2,082	---
Corporate	19,145	12,353	14,886
	-----	-----	-----
	\$ 50,859	\$ 29,864	\$ 23,426
Mortgage Investment Income	\$ 1,211	\$ 2,907	\$ 4,732
Corporate Income (Expense)			
Short-term investment income	\$ 1,337	\$ 1,525	\$ 80
Other income	1,386	5,724	1,500
General and administrative	(37,577)	(12,135)	(6,787)
Foreign currency loss	(2,198)	---	---
Litigation and proxy costs	(4,848)	---	---
Unrealized loss on carrying value of real estate and impaired assets	(51,000)	---	---
	-----	-----	-----
Income (loss) before capital gain, extraordinary loss and minority interest	\$ (91,465)	\$ 3,490	\$ 1,681
	=====	=====	=====
Capital expenditures			
Shopping Centers	\$ 12,585	\$ 9,381	\$ 10,083
Apartments	2,081	1,497	1,606
Office Buildings	8,045	9,741	8,444
Parking Facilities	392	1,035	131
	-----	-----	-----
	\$ 23,103	\$ 21,654	\$ 20,264
	=====	=====	=====

Identifiable assets			
Shopping Centers	\$ 471,996	\$ 498,238	\$ 179,899
Apartments	79,011	79,386	89,090
Office Buildings	45,404	45,412	49,343
Parking Facilities	81,554	17,353	7,238
Impark	66,169	88,529	---
Mortgages	5,508	30,686	42,466
Corporate	37,042	30,622	45,018
	-----	-----	-----
Total Assets	\$ 786,684	\$ 790,226	\$ 413,054
	=====	=====	=====

## 24 SUBSEQUENT EVENT

The Trust in February 1999 sold a shopping center for \$21.6 million, resulting in net proceeds of \$9.3 million after repayment of mortgage debt. The Trust in March 1999 sold an office building resulting in net proceeds of \$1.8 million.

## 25. MINORITY INTEREST IN IMPARK

The Company owns 76% of the voting common stock of Impark with the remainder owned by employees of Impark. Consequently, for financial reporting purposes the financial statements of Impark and the Company are consolidated with the minority interest's share of the loss resulting from Impark being allocated to the employee shareholders. As the equity of the minority shareholders was depleted as of December 31, 1997, no further losses have been allocated to the minority shareholders subsequent to 1997.

## 26. MINIMUM RENTS

The future minimum lease payments that are scheduled to be received under noncancellable operating leases are as follows (amounts in thousands):

1999	\$ 67,856
2000	60,308
2001	52,710
2002	46,936
2003	41,309
Thereafter	154,058
	-----
	\$423,177
	=====

## 27. RELATED PARTY TRANSACTIONS

In connection with the \$90 million note payable, the Trust paid fees of \$1.4 million to the lenders. One of the lenders is Gotham Partners, L.P. and another is Gotham Partners III, L.P. ("Gotham") which received fees of \$.2 million through December 31, 1998. The Trust paid interest of \$3.7 million to the lenders, of which Gotham received \$.6 million through December 31, 1998. The fees and interest were allocated among the lenders based on the amounts they loaned to the Trust. Gotham and one of the other lenders agreed to provide a stand-by commitment to purchase up to \$45 million from a contemplated rights offering in exchange for a fee of \$1.8 million. Gotham agreed to acquire 7/9ths of the shares of beneficial interest required under the stand-by commitment and, accordingly, it will receive a proportionate share of the fee amounting to \$1.4 million. Gotham and the other lender also agreed to provide a stand-by commitment for a second rights offering of up to \$50 million in exchange for a fee of up to \$1.8 million, of which Gotham would receive up to \$1.4 million depending on the amount of the rights offering. Gotham owns 9.70% of the shares of beneficial interest as of December 31, 1998.

The Trust in 1998 reimbursed Gotham for \$3.1 million in proxy expenses.

The Company has engaged a law firm, that has a partner who is a Trustee, to advise it on strategic matters regarding Impark. As of December 31, 1998, no payments have been made to this firm.

The Company leases four of its parking facilities to a third party which is partially owned by an affiliate of a Trust shareholder, Apollo Real Estate Investment Fund II, L.P. and Apollo Real Estate Advisors. In 1998, the Trust received \$.9 million in rent from this third party.

The Trust in December 1998 engaged a company, a shareholder of which is a relative of a principal of Gotham, to provide mortgage brokerage services. No fees have been paid to this party through December 31, 1998

## 28. SEVERANCE ACCRUAL

During 1998, the Trust recorded severance expense of \$6.1 million for change in control agreements, other compensation arrangements for continuation of employment, and termination of an employment contract. At December 31, 1998, the Trust had paid \$1.0 million of these benefits and has a balance of \$5.1 million remaining to be paid. The Trust recognizes these expenses over the periods that employees are required to remain in the employment of the Trust. If an employee is terminated without any period of required continuing employment, these benefits are expensed if and when paid.

The Trust also paid \$3.4 million related to the termination of employment of its former chairman, president and chief executive officer. As a result of the proxy contest in 1998 and the change in the composition of the Trust's board of Trustees, restricted stock became unrestricted and the Trust recognized \$4.7 million of deferred compensation as an expense.

## 29. CONTINGENCIES

The Trust, in exchange for a fee from Impark, has provided performance guarantees for the manufacturing and installation of transit ticket vending equipment. The guarantees of \$5.3 million and \$6.2 million expire in February 2001



and 2002, respectively. As of December 31, 1998, no amounts have been drawn against these guarantees.

### 30. QUARTERLY RESULTS OF OPERATIONS (UNAUDITED)

The following is an unaudited condensed summary of the combined results of operations by quarter for the years ended December 31, 1998 and 1997. In the opinion of the Trust and Company, all adjustments (consisting of normal recurring accruals) necessary to present fairly such interim combined results in conformity with generally accepted accounting principles have been included. The first three quarters of 1998 and four quarters of 1997 have been restated to reflect the change in the lives of assets used to calculate depreciation. Additionally, the third quarter of 1998 has been restated for the reduction of a severance accrual made in the fourth quarter of 1998.

	QUARTERS ENDED			
	RESTATED MARCH 31	RESTATED JUNE 30	RESTATED SEPTEMBER 30	DECEMBER 31
(IN THOUSANDS, EXCEPT PER SHARE DATA AND FOOTNOTES)				
1998				
Revenues	\$ 80,354	\$ 81,847	\$ 78,670	\$ 83,655
Loss before preferred dividend and extraordinary loss from early extinguishment of debt	(3,579)	(11,076)	(8,598)	(57,866)
Extraordinary loss from early extinguishment of debt			(1,633)	(766)
Net loss before preferred dividend	(3,579) (1)	(11,076) (2)	(10,231) (3)	(58,632) (4)
Net loss applicable to shares of beneficial interest	\$ (4,454)	\$ (11,784)	\$ (10,939)	\$ (59,340)
Comprehensive net loss	\$ (4,450)	\$ (12,073)	\$ (11,276)	\$ (59,957)
Per share				
Loss applicable to shares of beneficial interest before extraordinary loss	\$ (.15)	\$ (.38)	\$ (.30)	\$ (1.87)
Extraordinary loss from early extinguishment of debt			(.05)	(.02)
Net loss applicable to shares of beneficial interest, basic and diluted	\$ (.15)	\$ (.38)	\$ (.35)	\$ (1.89)
As previously reported:				
Net loss previously disclosed	\$ (3,272)	\$ (10,602)	\$ (11,657)	
Change in depreciation expense	(1,182)	(1,182)	(1,182)	
Change in severance accrual			1,900	
Net loss as restated	\$ (4,454)	\$ (11,784)	\$ (10,939)	
Net loss per share as previously disclosed, basic and diluted	\$ (0.11)	\$ (0.34)	\$ (0.37)	
Net loss per share as restated, basic and diluted	(0.15)	(0.38)	(0.35)	

(1) Included \$.9 million loss U.S. from Impark's manufacturing subsidiary and \$.9 million in proxy and litigation expenses.

(2) Included \$3.4 million expense for the termination of the former Chairman, President and Chief Executive Officer, \$3.9 million in proxy and litigation expenses, \$4.7 million expense for the vesting of restricted shares, \$2.3 million reserve on a property acquisition deposit due to the Trust terminating the deal, \$1.5 million in professional fees regarding the Trust's restructuring, \$1 million in bank loan waiver fees and a \$.4 million reserve for the termination of a systems project and \$1.5 million in foreign currency translation loss.

(3) Included \$1.7 million severance accrual, \$.8 million in expense for terminations of former employees, \$1.6 million in legal fees for possible corporate and financial transactions of the Trust, \$1.1 million in foreign currency translation loss for marking an intercompany receivable to the spot rate, the reduction in the accrual of percentage rent of \$1.5 million due to the adoption of EITF 98-9 and a \$1.6 million extraordinary loss from the repayment of \$87.5 of Senior Notes prior to their maturity.

(4) Included \$1.1 million in expense for various services provided to the Trust by a third party and warrants issued in connection therewith, \$.8 million in legal fees for possible corporate and financial transactions, \$.5 million in professional fees resulting from an unsuccessful effort to refinance the Trust's bridge and bank loans, \$.8 extraordinary loss resulting from amendments to the Trust's bank credit facility and \$90 million note payable, \$4.4 million severance accrual offset by \$1.5 million in additional percentage rent accrued due to the prospective adoption of EITF 98-9. Also includes \$51 million unrealized loss on carrying value of assets identified for disposition and impaired.

(5) Included a noncash recognition of income from the repayment of a wraparound mortgage investment.

(6) Included recognition of income of \$.5 million from a casualty loss.

1997  
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	QUARTERS ENDED			
	RESTATED MARCH 31	RESTATED JUNE 30	RESTATED SEPTEMBER 30	RESTATED DECEMBER 31
Revenues	\$ 22,122	\$ 58,946	\$ 73,135	\$ 81,341
Income before preferred dividend, extraordinary loss from early extinguishment of debt and after minority interest	1,318	1,074	1,086	2,424
Extraordinary loss from early extinguishment of debt				(226)
Net income before preferred dividend	1,318	1,074	1,086	2,198
Net income applicable to shares of beneficial interest	\$ 110(5)	\$ (135)(6)	\$ (123)	\$ 993
Comprehensive net income (loss)	\$ 114	\$ (150)	\$ (209)	\$ 212
Per share				
Loss applicable to shares of beneficial interest before extraordinary loss and after minority interest	\$ .01	\$ (.01)	\$ (.01)	\$ .05
Extraordinary loss from early extinguishment of debt				(.01)
Loss applicable to shares of beneficial interest - basic and diluted	\$ .01	\$ (.01)	\$ (.01)	\$ .04
As previously reported:				
Net income previously disclosed	\$ 970	\$ 727	\$ 738	\$ 608
Change in depreciation expense	(860)	(862)	(861)	(860)
Change in loss on sale of property				1,245
Net income (loss) as restated	\$ 110	\$ (135)	\$ (123)	\$ 993
Net loss per share as previously disclosed, basic and diluted	\$ 0.05	\$ 0.03	\$ 0.03	\$ 0.04
Net loss per share as restated, basic and diluted	0.01	(0.01)	(0.01)	0.04

## **REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS**

### **TO THE SECURITYHOLDERS AND TRUSTEES OF FIRST UNION REAL ESTATE EQUITY AND MORTGAGE INVESTMENTS:**

We have audited the accompanying combined balance sheets of First Union Real Estate Equity and Mortgage Investments (an unincorporated Ohio business trust, also known as First Union Real Estate Investments) and First Union Management Inc. (a Delaware corporation) and its subsidiaries as of December 31, 1998 and 1997, and the related combined statements of operations, combined statements of comprehensive income, shareholders' equity and changes in cash for each of the three years in the period ended December 31, 1998 (1997 and prior as restated - see note 2). These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the combined financial position of First Union Real Estate Equity and Mortgage Investments and First Union Management Inc. and its subsidiaries as of December 31, 1998 and 1997, and the results of their operations and their changes in cash for each of the three years in the period ended December 31, 1998, in conformity with generally accepted accounting principles.

Cleveland, Ohio,  
**March 29, 1999. ARTHUR ANDERSEN LLP**

## **MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

### **RESTATEMENT OF COMBINED FINANCIAL STATEMENTS**

The Trust has restated its Combined Financial Statements for each of the five years ended December 31, 1998 as a result of changing the lives of assets to calculate depreciation expense.

### **FINANCIAL CONDITION**

In January 1998, the Trust acquired two parking garages for \$44.8 million in cash, the assumption of \$.7 million in mortgage debt and the issuance of a \$.9 million mortgage note payable. The parking garages are located in Chicago, IL, and Columbus, OH. Additionally, in February 1998, the Trust acquired a parking garage in Richmond, VA for \$9.1 million in cash and a development site in Cleveland, OH for \$3.3 million in cash. The development site is leased on a short-term basis to the former owner until construction of a parking garage commences. In March 1998, the Trust acquired a surface parking lot adjacent to the Ballpark at Arlington in Arlington, TX for \$3 million in cash. In July 1998, the Trust acquired a parking garage in Nashville, TN for \$2.1 million in cash and the assumption of a \$4.5 million mortgage. During 1998, the Trust acquired three parcels of land adjacent to two shopping centers that it owns for \$.7 million. The cash required for these acquisitions was funded with proceeds from the Trust's bank credit facilities.

The Trust in January 1998 received \$6.2 million in cash as full repayment of a mortgage investment secured by a property in Fairmont, WV. In May 1998, the Trust received \$18.8 million in cash as full repayment of a mortgage investment secured by an office building in Cleveland, OH. The proceeds were used to repay bank loans under the Trust's bank credit facilities.

In February 1998, 951,000 preferred shares of beneficial interest were converted into approximately 3,144,000 shares of beneficial interest.

The Trust in May 1998, sold its investment in the land beneath an office building in Cleveland for \$6.1 million resulting in a capital gain of \$1.7 million. The proceeds were used to reduce short-term borrowings.

In May 1998, the Trust obtained a \$30 million non-recourse mortgage secured by its parking garage in Chicago, IL. The mortgage is for three years at an interest rate of LIBOR plus 175 basis points and is interest only.

On June 1, 1998, the Trust's affiliated management company purchased the remaining non-voting common shares of Impark for \$11.2 million from Impark's former owner. The non-voting common stock was recorded as an Other Liability in the Combined Financial Statements. The Trust, for a fee from the former owner of Impark, had provided a financial guarantee that the shares would be redeemed. Upon completion of the redemption, the Trust sold \$11.5 million of U.S. Treasury bills which had collateralized the financial guarantee.

In July 1998, the Trust commenced a tender offer to purchase for cash all \$100 million principal amount of its 8 7/8% Senior Notes due 2003 at \$970 per \$1,000 principal amount of Senior Notes, plus accrued and unpaid interest. Concurrent with the tender offer, the Trust conducted a consent solicitation and offered a consent payment of \$30 per \$1,000 principal amount of Senior Notes to amend the indenture governing the Senior Notes and to terminate listing of the Senior Notes on the New York Stock Exchange. The purpose of the tender offer and consent solicitation was (i) to prevent the possibility that the Trust would be required to purchase the Senior Notes at 101% of their principal amount, an obligation which the Trust did not have the financial resources to satisfy, and (ii) to provide the Trust with additional financial and operating flexibility. Prior to its amendment, the Senior Note indenture required the Trust to offer to purchase the Senior Notes at 101% of their principal amount if within 90 days following the date of a "change of control," the rating of the Senior Notes by both Standard & Poor's Corporation ("S&P") and Moody's Investors Services, Inc. declined by one or more rating levels. In April 1998, S&P placed the Trust on Credit Watch and in November 1998, downgraded the Trust's debt rating. In June 1998, Moody's placed the Senior Notes under review for possible downgrade and in October 1998, downgraded its rating for the Senior Notes.

In August 1998, pursuant to the tender offer and consent solicitation, holders of approximately 88% of the outstanding Senior Notes consented to the indenture amendments and the Senior Notes were delisted from the New York Stock Exchange. The Trust purchased approximately \$87.5 million principal amount of Senior Notes. The purchase of the Senior Notes was financed with the proceeds of a \$90 million loan (the "Bridge Loan") that matures in August 1999. The lenders under the Bridge Loan are Bankers Trust, as agent, and BankBoston, N.A., Blackacre Bridge Capital, Elliott Associates, Gotham Partners, L.P. and Gotham Partners III, L.P., and Wellsford Capital, each as an equal participant.

As a result of legal fees for several matters, accrued severance expenses for employee terminations, a new accounting pronouncement requiring the deferral of percentage rent from tenants, and foreign currency mark-to-market

losses, the Trust was not in compliance with the debt service coverage, interest coverage, leverage ratio and funds from operations covenants under its bank credit facility for the third quarter of 1998. Additionally, Impark was not in compliance with covenants relating to the leverage ratio and interest coverage under its bank credit agreement for the third quarter of 1998. Further, the lenders under the facilities determined that a change in the majority of the Trust's Board of Trustees occurred in June 1998. This change in the Board would have breached covenants under both credit facilities, but the lenders waived these breaches.

The lenders under the Trust credit facility agreed to modify the debt service and interest coverage requirements and the methodology for calculating net income by excluding certain non-recurring or extraordinary charges or expenses, including percentage rent on a pro forma basis, and eliminating any expense or adjustment in any fiscal quarter relating to any non-cash foreign currency mark-to-market expense or adjustment. In addition, the lenders under the Trust's credit facility extended the waiver with respect to the Board of Trustees' change of control until June 30, 1999. In consideration for these modifications, the Trust paid the lenders an \$825,000 fee. Concomitant with the covenant modifications and the waiver extension, the lenders reduced their maximum commitment under the Trust credit facility from \$125 million to \$110 million and will reduce such commitment further to \$80 million on March 17, 1999 and to \$50 million on May 17, 1999. The lenders have agreed in principle in March 1999 in exchange for a payment fee of \$300,000, extended by 45 days the reduction of the commitment to April 30, 1999 and June 30, 1999, respectively. As part of the Amendment to extend the dates of the commitment reduction in March 1999, the lenders reduced the credit facility commitment by \$5 million to \$105 million. Additionally, upon the completion of the rights offering, \$9 million of the proceeds will be used to repay the credit facility and the commitment will be reduced by \$9 million to \$96 million. The lenders also increased the interest rate under the facility from the Eurodollar rate plus 200 basis points or the prime rate to the Eurodollar rate plus 300 basis points or the prime rate plus 50 basis points.

The lenders under the Impark credit facility agreed to (i) modify the interest coverage and leverage requirements and the methodology for determining earnings before interest, taxes, depreciation and amortization by adjusting for certain non-recurring or extraordinary charges or expenses for each of the quarters ended September 30, 1998 through September 30, 1999 and (ii) decrease the margin added to the Canadian Bankers Acceptance interest rate from 175 basis points to 150 basis points. In addition, the lenders extended the waiver with respect to the default caused by the change in the majority of the Trust's Board of Trustees until June 30, 1999. In consideration for these amendments and the waiver extension, the principal balance under the Impark credit facility was reduced from Cdn. \$50 million to Cdn. \$38.8 million, Impark paid the lenders a fee of Cdn. \$388,400, and the Trust issued an \$8 million U.S. letter of credit under the Trust's credit facility as collateral for Impark's obligations and agreed to provide an additional \$5 million U.S. in collateral for such obligations on August 11, 1999.

The lenders under the Bridge Loan agreed to extend the maturity of the loan to August 11, 1999 and incorporate the revised covenants in the Trust's credit facility. In consideration for these amendments, the Trust paid the Bridge Loan lenders a fee of \$300,000 and agreed, in principle, to (i) reduce the outstanding principal balance under the Bridge Loan to less than \$70 million by May 15, 1999 (previous reduction date was March 31, 1999) and to less than \$50 million by May 31, 1999, (ii) increase the lenders' interest rate on the loan from 9.875% to 12% per annum and (iii) pay (A) on February 11, 1999 a fee of 1% of the outstanding principal amount of the loan on such date, (B) a fee in an amount equal to 50 basis points of the outstanding principal amount of the loan on March 31, 1999, if the balance outstanding is greater than \$60 million and (C) a fee in an amount equal to 50 or 100 basis points of the outstanding principal amount of the loan on May 31, 1999, depending on the loan balance outstanding at May 31, 1999. The Trust further amended the Bridge Loan, in principle, to have \$9.0 million of proceeds from an anticipated rights offering, that would otherwise be used to repay a portion of the Bridge Loan, to be used to repay the Trust's credit facility. This \$9.0 million portion of the Bridge Loan will bear interest at 15% annually.

In November 1998, in consideration for various services that it had previously provided to the Trust, a third party was issued ten-year warrants exercisable for 500,000 shares of beneficial interest at a price of \$10 per share and was paid \$750,000. The Trust recorded \$436,000 in expense as a measurement of the consideration represented by the stock warrants based on the Black-Scholes option pricing model.

In December 1998, the Trust, and Impark recorded a non-cash charge of approximately \$51 million in accordance with SFAS 121, "Impairment of Long Lived Assets". The Trust determined that certain real estate assets held for sale are impaired based on the bids received from purchasers compared to the net book value of these assets held for sale and recorded a \$36 million charge. As the Trust intends to sell these assets, the bids received best represent the cash flow to be realized in accordance with SFAS 121. Additionally, Impark recorded a \$15 million U.S. reduction of goodwill. A review for impairment was triggered based on Impark's operating results being less than the proforma projection used to purchase Impark. The impairment was indicated by projected undiscounted future cash flows of Impark being less than the net book value of Impark's assets, including goodwill related to the acquisition. The impairment amount was calculated based on discounting projected cash flows of Impark, which showed the net book value of Impark's assets, including goodwill, would not be realized by \$15 million U.S.

#### **YEAR 2000**

In June 1998, the Trust implemented a multi-step Year 2000 Compliance Project (the "Project"). The Project is addressing the issue of computer systems and embedded computer chips that may not be able to properly recognize dates prior to, on, or after January 1, 2000.

The general phases of the Project are as follows: (1) inventorying systems and equipment that may be affected by the Year 2000 issue; (2) assigning priorities to the items identified; (3) evaluating the Year 2000 compliance of items deemed

to be critical to the Trust's operations; (4) testing critical items; (5) repairing or replacing critical items that are determined not to be Year 2000 compliant and (6) developing and implementing contingency plans for each location.

As of December 31, 1998, the inventory and priority assessment phases of the Project were completed. Critical items are those believed by the Trust to involve a risk to the safety of individuals, or that may cause damage to property, or affect revenues. Testing of critical items is being performed and is expected to be completed in the first quarter of 1999.

The Project addresses three main sections: (a) Information Technology Systems; (b) Process Control and Instrumentation; and (c) Third Party Tenants, Suppliers and Customers.

The Information Technology Systems section consists of all computer hardware and software. These systems are primarily used for accounting and financial reporting as well as property management purposes throughout the Trust's operations. Impark uses other systems mainly for revenue control purposes at the parking facility level. The testing phase is ongoing as hardware and software are remediated, upgraded or replaced. Currently, Impark's accounting and financial reporting systems are not Year 2000 compliant; these systems will be replaced by a new general-purpose financial reporting and general ledger package by October 31, 1999. Additionally, new hardware and software are being installed at various properties and subsidiaries, which is anticipated to be completed by June 30, 1999.

The Process Control and Instrumentation section includes the hardware, software and associated embedded computer chips that are used in the operations of certain facilities owned by the Trust. Testing and repair of this equipment is in process. The Trust's evaluation of these items and communications with manufacturers and suppliers revealed that the majority of this equipment is mechanical in nature and is not date-sensitive, and accordingly will not require remediation or replacement to function properly in the Year 2000. Contingency planning is in process, and all repair and testing is expected to be completed by June 30, 1999.

The Third Party Tenants, Suppliers and Customers section includes the process of identifying critical suppliers and customers and obtaining information from them regarding their plans and progress in addressing the Year 2000 problem. A written notice regarding the Year 2000 problem was sent to all tenants occupying space at properties owned by the Trust and to landlords of parking facilities operated by Impark. Additionally, inquiries have been forwarded to critical third parties (primarily financial institutions and utility service providers), and responses are currently being obtained and evaluated. These evaluations will be followed by the development of contingency plans. All activities for this section are expected to be completed by June 30, 1999.

The total cost of required modifications to achieve Year 2000 compliance is not expected to be material to the Trust's financial position. Estimated total costs are expected to be between \$1.0 million and \$2.0 million, including enhancements to software programs and upgrades to hardware, some portion of which would have been done irrespective of the Year 2000 problem.

The failure to correct a material Year 2000 issue could result in the interruption or failure of certain normal business activities or operations. The most reasonable worst case scenarios for the Trust are

- A significant number of tenants at shopping centers will not be able to record sales transactions using their automated equipment or accept credit card transactions, and
- Electric utility companies will not be able to provide power to operate shopping centers, office buildings, apartment complexes or parking facilities.

The most reasonable worst case scenarios for Impark are

- Its financial reporting system will not work on or after January 1, 2000, and
- Parking equipment that has been identified as non-compliant will not accept credit cards from parking patrons at the facilities it manages.

## **FEDERAL TAX LEGISLATION**

On July 22, 1998, the President of the United States signed legislation that limits the "grandfathering rules" applicable to Real Estate Investment Trusts (REITS) which have a paired management company. (The shares of the affiliated management company are considered to be "paired" with the Trust.) As a result of this legislation, the Trust and the affiliated management company will be treated as one entity with respect to properties acquired on or after March 26, 1998 and activities or services relating to such properties that are undertaken or performed by one of the paired entities on or after this date. This legislation limits the benefits of the Trust's paired structure with the affiliated management company. The Trust is currently evaluating the potential value of its paired structure.

## LIQUIDITY AND CAPITAL RESOURCES

Net cash provided by operations was \$6.4 million as compared to cash provided by operations of \$15.7 million when comparing 1998 to 1997. The decrease in cash provided from operations is primarily the result of a net loss before the preferred dividend of \$83.5 million. The net loss was primarily caused by several charges relating to the proxy contest and change in the Board of Trustees' composition as detailed in the following section "Results of Operations" and the non cash charge of \$51 million for the unrealized loss on the carrying value of assets held for sale and impaired. The net loss of \$83.5 million is offset by the non cash charges of \$33.4 million for depreciation and amortization and the \$51 million charge to recognize the unrealized loss on the carrying value of assets held for sale and impaired. Dividends to shares of beneficial interest paid in 1998 of \$6.6 million represented 103% of net cash from operations.

The Trust received \$25 million in full repayment of two mortgage investments secured by a mall in Fairmont, WV and an office building in Cleveland, OH during 1998. The proceeds were used to repay borrowings under the Trust's bank credit facilities. Additionally, the Trust in May 1998 sold land in Cleveland, OH for \$6.1 million which was also used to repay bank credit facilities.

As noted previously, the Trust acquired five parking facilities and a development site for \$62.3 million in cash. The properties were acquired by borrowing under the bank credit facilities, assumption of two mortgages totaling \$5.2 million and the issuance of a \$.9 million second mortgage.

The Trust invested \$23.1 million in its existing portfolio primarily to construct the first phase of a shopping center in Abilene, TX and continue to tenant the former retail center in Denver, CO, which has been converted into an office technology center.

As noted previously, the Trust's affiliated management company purchased the remaining non-voting common stock of Impark in June 1998 for \$11.2 million.

During the second quarter of 1998, the Trust sold \$2.1 million of stock of another REIT and \$11.5 in U.S. Treasury bills. The U.S. Treasury bills were collateral for a financial guarantee that the Trust had made in conjunction with the Trust's affiliated management company's acquisition of Impark.

In May 1998, the Trust obtained a \$30 million mortgage loan on its Chicago, IL parking garage. The proceeds were used to repay bank lines of credit.

In June 1998, the Trust suspended its quarterly dividend to shareholders of beneficial interest and adopted a policy of making only the minimum required distributions to maintain its tax status as a REIT. Additionally, the Trust has adopted a policy of making dividend distributions on an annual basis. The Trust, for 1998, has made all distributions required to maintain its tax status as a REIT.

As noted previously, the Trust obtained a \$90 million Bridge Loan which was used to repurchase approximately \$87.5 million in Senior Notes.

The Trust in 1999 has the following debt maturities (in thousands of dollars):

Bank loans	\$101,000
Bridge loan	90,000
Mortgage principal payments	4,308
Other obligations	10,602
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	\$205,910
	=====

The bank loans require paydowns to \$80 million and \$50 million by April 30, 1999 and June 30, 1999, respectively. The remaining \$50 million must be repaid by August 11, 1999. The Bridge Loan must be paid down to \$70 million by May 15, 1999 and to \$50 million on May 31, 1999. The remaining \$50 million must be paid by August 11, 1999. The \$10.6 million obligation may be called during 1999 at the option of the creditor.

To fund the repayment of these obligations, the Trust intends to sell certain assets, conduct a rights offering, use cash available of \$28.6 million as of December 31, 1998, refinance certain assets, and use cash from operations. To facilitate the rights offering, the Trust, in September 1998, filed a registration statement on Form S-3 with the Securities and Exchange Commission.

If the Trust is not able to meet the deadlines for debt repayment, it may be forced to seek bankruptcy protection.

## **RESULTS OF OPERATIONS - 1998 VERSUS 1997**

Net loss applicable to shares of beneficial interest for 1998 was \$86.5 million as compared to net income of \$.8 million for 1997. The net loss for 1998 included a \$2.25 million loss on a property acquisition deposit that was approved prior to the change in the majority of the Board of Trustees in June 1998, and which was offset by \$200,000 later in 1998 by assigning the contract to a third party, a \$3.4 million payment to the Trust's former chairman and chief executive officer, a \$4.7 million expense due to lifting of restrictions on restricted shares which followed the change in the majority of the Trust's Board of Trustees, \$1.5 million in other professional fees to avoid a change in the composition of the Trust's Board, \$4.8 million in proxy and litigation expenses and a \$51 million noncash charge to recognize the loss on carrying value of assets held for sale and impaired assets. Additionally, the Trust incurred \$2.2 million in foreign currency mark-to-market losses, \$6.1 million in accrued severance expenses for change in control agreements and for employee terminations and \$2.6 million in legal fees.

In February 1998, 951,000 preferred shares of beneficial interest were converted into common shares of beneficial interest resulting in a decreased preferred dividend when comparing 1998 to 1997.

Net loss for 1998 included \$10.3 million of capital gains. The Trust sold its land beneath a building in Cleveland, OH resulting in a capital gain of \$1.7 million. An additional capital gain of \$7.7 million was recognized when a mortgage investment was repaid. This capital gain had been deferred from a property sale in 1982 since the Trust received the mortgage note as purchase consideration. The Trust also realized a capital gain from the sale of a forward exchange contract of \$.8 million in the second quarter of 1998. In December 1998, the Trust sold a land parcel in Monroe, LA resulting in a \$.1 million capital gain. Additionally, the net loss for 1998 included \$1.6 million of unamortized Senior Note issue costs and professional fees which were expensed in the third quarter of 1998 when the Trust repaid approximately \$87.5 million of the Senior Notes prior to their maturity and \$.8 million of deferred costs which were expensed when the Trust renegotiated its bank agreement and \$90 million Bridge Loan.

Mortgage loan interest income declined by \$1.7 million, when comparing 1998 to 1997. The decline in interest income when comparing 1998 to 1997 was caused by the repayment of a mortgage investment secured by a shopping mall in Fairmont, WV in January 1998 and the repayment of a mortgage investment secured by an office building in Cleveland, OH in May 1998.

The Trust had approximately \$11.5 million invested in U.S. Treasury bills and approximately \$2.1 million invested in the stock of another REIT for the first five months of 1998. The U.S. Treasury bills were purchased in April 1997 to secure the Trust's obligation under an agreement with the former owners of Impark to collateralize the \$10.5 million in non-voting stock and accrued interest which the former owners of Impark received when the Trust's affiliated management company purchased voting control of Impark in April 1997. The REIT stock was acquired in the third and fourth quarters of 1997 as a long-term investment. As noted previously, the non-voting common stock of Impark was purchased in June 1998 allowing the Trust to sell the U.S. Treasury bills. The Trust also sold its holdings in the REIT stock as a result of its change in investment strategy.

In September 1996, the Trust invested in a joint venture that owned eight shopping malls and 50% of another mall. The Trust in September 1997 purchased the interests of its joint venture partners. Consequently, the Trust's investment income and management fees for the Trust's affiliated management company declined when comparing 1998 to 1997.

Property net operating income for 1998 increased \$26.2 million when comparing 1998 to 1997 on a non-comparable basis. The acquisition of the former joint venture properties in September 1997 and the five parking facilities in the first three months of 1998 produced \$21.8 million and \$3.7 million, respectively, of increased property net operating income when comparing 1998 to the same period of 1997. These increases were offset by the decrease in property net operating income of \$1.5 million resulting from the sale of an office building and an apartment complex in the last four months of 1997. Property net operating income increased by \$2.2 million for the comparable portfolio when comparing 1998 to the same period of 1997. The increase was attributable to the continued lease-up of the North Valley Tech Center and increased rental rates in the apartment portfolio.

Mortgage interest expense increased when comparing 1998 to that of 1997 primarily due to the \$203 million in mortgage debt assumed in September 1997 in conjunction with the purchase of the remaining interest in the Trust's joint venture and the \$30 million mortgage obtained in May 1998.

Bank loan interest expense increased when comparing 1998 to the prior year due to increased borrowing, exclusive of the bank debt assumed in the April 1997 acquisition of Impark. The average balance for 1998 outstanding, exclusive of Impark's bank debt, was \$90 million. The average balance outstanding for 1997 was approximately \$19 million. The bank loans increased when comparing 1998 to 1997 primarily due to borrowings to fund the parking garage acquisitions and development site, partially fund the Trust's purchase of its partners' interest in the joint venture and to fund tenant and capital improvements during 1998 and 1997. Additionally, the bank covenant waiver fees of \$.6 million for the second quarter covenant waivers were recorded as bank loan interest expense in 1998. Offsetting the increase in the bank credit facilities were the proceeds from property sales during the last four months of 1997 and in May 1998, the repayment of mortgage investments in the first and third quarters of 1998 and



the \$30 million mortgage obtained in May 1998. Additionally, the inclusion of Impark for all of 1998, as compared to eight and a half months in 1997, in the results of the affiliated management company, resulted in bank interest expense increasing by \$.8 million when comparing 1998 to 1997.

Depreciation and amortization expense for 1998 increased over 1997 primarily due to the amortization of goodwill and management contracts associated with the acquisition of Impark in April 1997, the depreciation from the eight shopping malls acquired in September 1997 when the Trust acquired its joint venture partners' interest in the malls and the depreciation from the four parking facilities which were acquired in the first quarter of 1998.

General and administrative expenses increased when comparing 1998 to 1997 primarily related to several charges as a result of the proxy contest and the change in the majority of the Board of Trustees. The charges in the second quarter of 1998 included \$4.8 million in proxy and litigation expenses of which \$3.1 million was a reimbursement for Gotham's proxy expenses, \$3.4 million resulting from the termination of the former chairman, president and chief executive officer, \$4.7 million for the vesting of restricted shares which occurred upon the change in the majority of the Board of Trustees, and \$1.5 million in additional professional fees to avoid a change in the composition of the Trust's Board. Additionally, in the third and fourth quarters of 1998, the Trust accrued \$6.1 million of severance expense for employee termination, change in control and continuation of employment agreements. During the last six months of 1998, the Trust incurred approximately \$2.6 million in legal fees for negotiation of the \$90 million note payable and credit facilities, potential sales of properties and corporate acquisitions and corporate due diligence and preparation of a rights offering. The Trust expensed \$.5 million in fees for an unsuccessful effort to refinance its current debt in December 1998. Impark's general and administrative expenses increased over 1997 due to its inclusion in results for a full year in 1998 versus eight and a half months in 1997, and approximately \$2.5 million in expansion costs into U.S. markets incurred in 1998 and a \$.4 million expense for the termination of a contract to replace its computer system. The Trust also recorded a \$2.25 million expense when it did not close on the purchase of a parking facility because the Board of Trustees believed that the contract, which was approved prior to the change in the majority of the Board in June 1998, was on disadvantageous terms. First Union partially offset this loss by assigning the contract to a third party for \$200,000.

## **RESULTS OF OPERATIONS - 1997 VERSUS 1996**

Net income applicable to shares of beneficial interest for 1997 was \$.8 million. The net income applicable to shares of beneficial interest for 1997 included a noncash recognition of \$700,000 of income from the repayment of a wraparound mortgage investment, as the proceeds of \$18 million exceeded the Trust's basis in the wraparound investment and the recognition of \$500,000 in income from a casualty loss at one of the Trust's shopping centers. Net income applicable to shares of beneficial interest for 1997 was after the \$4.8 million preferred dividend for the preferred shares which were issued in October 1996. In November 1997, the Trust sold an apartment complex in Dayton, OH, resulting in a capital gain of \$2.7 million; while in December 1997, the Trust sold an office complex in Oklahoma City, OK, resulting in a loss of \$1.2 million. The net capital gain resulting from these transactions was \$1.5 million.

Mortgage investment income declined when comparing 1997 to 1996 due primarily to the repayment of a wraparound mortgage investment in February 1997, as noted previously.

Short-term investment income increased in 1997 as compared to 1996 due to the Trust having an average of \$31 million invested in short-term securities in 1997 versus minimal short-term investments in 1996.

Property net operating income was \$16.8 million greater when comparing 1997 and 1996. The comparable office property portfolio produced \$1.2 million in increased property net operating income when comparing 1997 and 1996 primarily due to increased occupancy at a former retail center in Denver, CO, and at office buildings in Cleveland, OH, and Indianapolis, IN, and a real estate tax refund in Cleveland, OH. The comparable parking portfolio had a decline of \$500,000 in property net operating income primarily due to increased real estate tax expense and the expiration of a fixed minimum rent management contract. The comparable retail portfolio had decreased net operating income of \$1.2 million when comparing 1997 and 1996 due primarily to the recognition of a \$1.1 million termination fee in 1996. The comparable apartment portfolio had increased property net operating income of \$600,000 when comparing 1997 and 1996 primarily due to the increased occupancy at an apartment complex in Durham, NC, and rent increases at the Trust's other apartment complexes. The acquisition of Impark in April 1997 and the Trust's purchase of its partners' interest in the joint venture in September 1997 produced \$17.2 million in property operating income on a non-comparable basis. The acquisition of an apartment complex in December 1996 and parking facilities in May 1997 partially offset the decline in property net operating income from the shopping mall, office buildings and apartment complex sold in January 1997 and last four months of 1997, resulting in a decline of \$400,000 in property net operating income.

Mortgage interest expense increased when comparing 1997 to 1996 due to the \$203 million in mortgage debt assumed in September 1997 in conjunction with the Trust's purchase of the remaining interest of the joint venture.

Interest on bank loans decreased when comparing 1997 to the same period of 1996. In 1997, the Trust had an average of \$19 million in bank borrowings versus \$51 million in 1996. The net proceeds from the sale of preferred shares of beneficial interest in October 1996, the proceeds from a sale of a shopping mall in January 1997 and a portion of the net proceeds from the sale of shares of beneficial interest in January 1997 and June 1997 were used to repay short-term bank loans. However, partially offsetting the decrease in bank loan interest and other expense is the addition, in April 1997, of approximately \$26 million in bank loans assumed in the acquisition of Impark and the accrual of the liability associated with a put-right which was attached to the Impark common shares issued to the former owners of Impark as part of the acquisition consideration.

Depreciation and amortization expense increased when comparing 1997 to 1996. This increase in depreciation and amortization expense was primarily attributed to the amortization of goodwill and management contracts related to the acquisition of Impark, the depreciation of the malls acquired in September 1997, and the Trust's capital improvement program. These increases are partially offset by the non-recurring, non-cash \$680,000 write-off of a tenant allowance which occurred in the first quarter of 1996 when the Trust replaced an anchor tenant at one of its malls.

General and administrative expenses for 1997 increased when compared to 1996. The increase is mainly attributed to the general and administrative expenses from the management of the nine properties acquired in a joint venture for 1997 and the acquisition of Impark in the second quarter of 1997. The increase in general and administrative expenses for 1997 was partially offset by a non-recurring, noncash charge of \$650,000 in 1996 for the termination of an employment contract of a former executive.

### **EFFECTS OF FOREIGN CURRENCY ON THE TRUST AND COMPANY**

Impark operates internationally and enters into transactions denominated in a foreign currency. As a result, the Trust and its affiliated management company are subject to the variability that arises from exchange rate movements. The effects of foreign currency on operating results are discussed above. The Trust and its affiliated management company do not hedge the risks in foreign currency exchange rate movements. Impark derives 87% of its revenues in Canada.

### **INTEREST RATE RISK**

The Trust and Impark have entered into certain financing arrangements that require interest payments based on floating interest rates. As such, the Trust's and Impark's financial results are subject to changes in the market rate of interest. To reduce the exposure to changes in the market rate of interest, the Trust has entered into a rate guarantee contract for a portion of its floating rate financing arrangements. The Trust does not enter into rate guarantee contracts for trading purposes.

Certain statements contained in the annual report that are forward-looking are based on current expectations that are subject to a number of uncertainties and risks, and actual results may differ materially. The uncertainties and risks include, but are not limited to, changes in market activity, changes in local real estate conditions and markets, actions by competitors, interest rate movements and general economic conditions. Further information about these matters can be found in the Trust's Annual Report filed with the SEC on Form 10K.

**EXHIBIT 23**

**CONSENT OF INDEPENDENT PUBLIC ACCOUNTANTS**

As independent public accountants, we hereby consent to the incorporation of our reports included in this Form 10-K, into the registrant's previously filed Registration Statements on Form S-3 (Registration Nos. 2-88719, 33-2818, 33-11524, 33-19812, 33-26758, 33-33279, 33-38754, 33-45355, 33-57756 and 333-953).

Cleveland, Ohio, Arthur Andersen LLP March 29, 1999.

**Exhibit 24**

**FIRST UNION REAL ESTATE EQUITY AND MORTGAGE INVESTMENTS**

**ANNUAL REPORT ON FORM 10-K  
FOR THE YEAR ENDED DECEMBER 31, 1998**

**Power of Attorney of Officers and Trustees**

The undersigned, an Officer or Trustee or both an Officer and Trustee of First Union Real Estate Equity and Mortgage Investments, an Ohio business trust (the "Trust") which anticipates filing with the Securities and Exchange Commission, Washington, D.C., under the provisions of the Securities Exchange Act of 1934, an Annual Report on Form 10-K for the year ended December 31, 1998 (hereinafter called the "Form 10-K"), does hereby constitute and appoint Daniel P. Friedman and Paul F. Levin, and either of them, with full power of substitution and resubstitution, as attorneys or attorney to sign for him and in his name the Form 10-K and any and all amendments and exhibits thereto, and any and all other documents to be filed with the Securities and Exchange Commission pertaining to the Form 10-K, with full power and authority to do and perform any and all acts and things whatsoever required or necessary to be done in the premises, as fully to all intents and purposes as he could do if personally present, hereby ratifying and approving the acts of said attorneys and any of them and any such substitute.

IN WITNESS WHEREOF, the undersigned has hereunto set his hand this 29th day of March, 1999.

*/s/ WILLIAM A. ACKMAN*  
-----

*/s/ DANIEL J. ALTOBELLO*  
-----

*/s/ DAVID P. BERKOWITZ*  
-----

*/s/ WILLIAM E. CONWAY*  
-----

*/s/ ALLEN H. FORD*  
-----

*/s/ DANIEL P. FRIEDMAN*  
-----

*/s/ STEPHEN J. GARCHIK*  
-----

*/s/ RUSSELL R. GIFFORD*  
-----

*/s/ DAVID S. KLAFTER*  
-----

*/s/ WILLIAM SCULLY*  
-----

*/s/ DANIEL SHUCHMAN*  
-----

*/s/ STEPHEN S. SNIDER*  
-----

*/s/ MARY ANN TIGHE*  
-----

*/s/ JAMES A. WILLIAMS*  
-----

**Exhibit 24**

**FIRST UNION REAL ESTATE EQUITY AND MORTGAGE INVESTMENTS**

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**FOR THE YEAR ENDED DECEMBER 31, 1998**

**Power of Attorney of Officers and Trustees**

The undersigned, an Officer or Trustee or both an Officer and Trustee of First Union Real Estate Equity and Mortgage Investments, an Ohio business trust (the "Trust") which anticipates filing with the Securities and Exchange Commission, Washington, D.C., under the provisions of the Securities Exchange Act of 1934, as amended, an Annual Report on Form 10-K for the year ended December 31, 1998 (hereinafter called the "Form 10-K"), does hereby constitute and appoint Daniel P. Friedman and Paul F. Levin, and either of them, with full power of substitution and resubstitution, as attorneys or attorney to sign for him and in his name the Form 10-K and any and all amendments and exhibits thereto, and any and all other documents to be filed with the Securities and Exchange Commission pertaining to the Form 10-K, with full power and authority to do and perform any and all acts and things whatsoever required or necessary to be done in the premises, as fully to all intents and purposes as he could do if personally present, hereby ratifying and approving the acts of said attorneys and any of them and any such substitute.

IN WITNESS WHEREOF, the undersigned has hereunto set his hand this \_\_\_ day of \_\_\_\_\_, 1999.

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**ARTICLE 5**

CIK: 0000037008

NAME: FIRST UNION REAL ESTATE EQUITY AND MORTGAGE INVESTMENTS

MULTIPLIER: 1

PERIOD TYPE	YEAR
FISCAL YEAR END	DEC 31 1998
PERIOD START	JAN 01 1998
PERIOD END	DEC 31 1998
CASH	45,175,000
SECURITIES	5,000
RECEIVABLES	21,809,000
ALLOWANCES	0
INVENTORY	2,798,000
CURRENT ASSETS	69,787,000
PP&E	806,859,000
DEPRECIATION	(165,357,000)
TOTAL ASSETS	786,684,000
CURRENT LIABILITIES	42,659,000
BONDS	578,397,000
PREFERRED MANDATORY	0
PREFERRED	31,737,000
COMMON	121,076,000
OTHER SE	(2,117,000)
TOTAL LIABILITY AND EQUITY	786,684,000
SALES	320,592,000
TOTAL REVENUES	324,526,000
CGS	0
TOTAL COSTS	415,991,000
OTHER EXPENSES	365,132,000
LOSS PROVISION	0
INTEREST EXPENSE	50,859,000
INCOME PRETAX	(91,465,000)
INCOME TAX	0
INCOME CONTINUING	(91,465,000)
DISCONTINUED	0
EXTRAORDINARY	0
CHANGES	0
NET INCOME	(86,517,000)
EPS PRIMARY	(2.81)
EPS DILUTED	(2.81)

**ARTICLE 5**

RESTATED:

CIK: 0000037008

NAME: FIRST UNION REAL ESTATE EQUITY AND MORTGAGE INVESTMENTS

MULTIPLIER: 1

PERIOD TYPE	YEAR
FISCAL YEAR END	DEC 31 1997
PERIOD START	JAN 01 1997
PERIOD END	DEC 31 1997
CASH	16,864,000
SECURITIES	13,103,000
RECEIVABLES	20,070,000
ALLOWANCES	0
INVENTORY	3,374,000
CURRENT ASSETS	53,411,000
PP&E	756,308,000
DEPRECIATION	(142,082,000)
TOTAL ASSETS	790,226,000
CURRENT LIABILITIES	38,000,000
BONDS	483,459,000
PREFERRED MANDATORY	182,079,000
PREFERRED	54,109,000
COMMON	182,079,000
OTHER SE	(878,000)
TOTAL LIABILITY AND EQUITY	790,226,000
SALES	225,388,000
TOTAL REVENUES	235,544,000
CGS	0
TOTAL COSTS	232,054,000
OTHER EXPENSES	202,190,000
LOSS PROVISION	0
INTEREST EXPENSE	29,864,000
INCOME PRETAX	3,490,000
INCOME TAX	0
INCOME CONTINUING	3,490,000
DISCONTINUED	0
EXTRAORDINARY	0
CHANGES	0
NET INCOME	845,000
EPS PRIMARY	(.03)
EPS DILUTED	(.03)

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