

INREIT

— REAL ESTATE INVESTMENT TRUST —

2009
Annual Report



INREIT

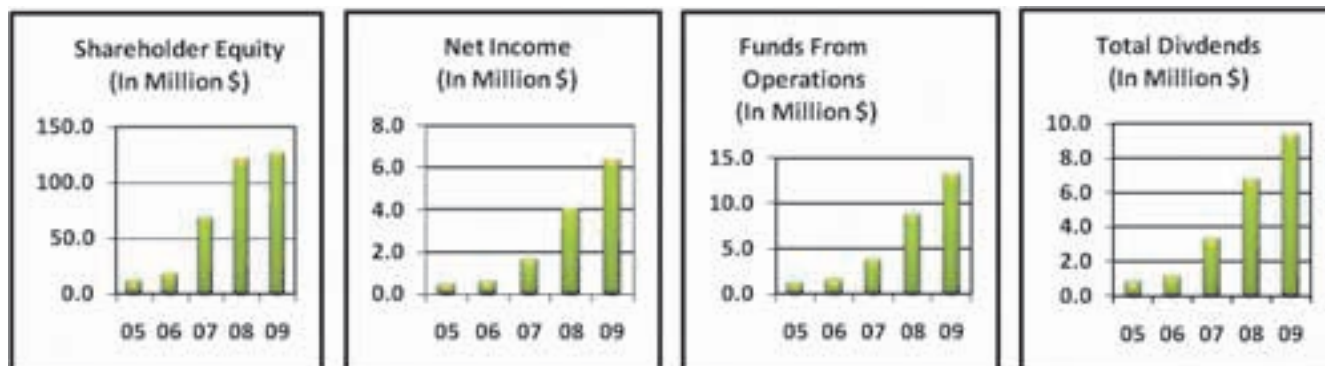
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INREIT Consolidated YTD Financial Highlights:

The following table sets forth summary financial data as of and for each of INREIT's twelve months ending December 31, 2005 through 2009.

| | 2009 | 2008 | 2007 | 2006 | 2005 |
|--------------------------------------|----------------|---------------|---------------|---------------|---------------|
| Income Statement Data | | | | | |
| Revenues | \$ 40,507,881 | \$ 27,200,963 | \$ 10,825,582 | \$ 5,209,370 | \$ 4,363,128 |
| Net Income | \$ 6,321,657 | \$ 4,042,793 | \$ 1,613,116 | \$ 565,962 | \$ 421,982 |
| Funds From Operations (FFO) | 13,184,471 | \$ 8,719,503 | \$ 3,766,233 | \$ 1,548,916 | \$ 1,180,710 |
| Balance Sheet Data | | | | | |
| Total Real Estate Investments | \$ 321,420,161 | \$263,452,787 | \$141,950,509 | \$ 54,339,110 | \$ 40,132,532 |
| Total Assets | \$ 325,662,675 | \$273,912,838 | \$149,389,237 | \$ 56,264,603 | \$ 40,795,971 |
| Shareholder Equity | \$ 125,820,046 | \$121,416,879 | \$68,288,640 | \$ 17,972,873 | \$ 11,854,911 |
| Per Share Data | | | | | |
| UPREIT Units Outstanding | 9,883,009 | 9,662,068 | 4,925,316 | 990,439 | 776,081 |
| Cash Shares Outstanding | 2,859,038 | 2,517,508 | 2,146,916 | 1,281,228 | 557,605 |
| Net Income | \$0.50 | \$0.33 | \$0.23 | \$0.25 | \$0.32 |
| Funds from Operations (FFO) | \$1.03 | \$0.72 | \$0.53 | \$0.68 | \$0.89 |
| Weighted Shares Outstanding * | | | | | |
| Net Income - Weighted Share | \$0.51 | \$0.44 | \$0.40 | \$0.35 | \$0.36 |
| FFO - Weighted Share | \$1.06 | \$0.96 | \$0.93 | \$0.96 | \$1.01 |
| Dividends Per Share | | | | | |
| | \$ 0.75 | \$ 0.74 | \$ 0.72 | \$ 0.69 | \$ 0.66 |

* Includes Cash Shares & UPREIT Operating Partnership Units (OPU's)



Above: 2005 to 2009 Comparative Graphs (For the Twelve Months Ended December 31st)





INREIT

— REAL ESTATE INVESTMENT TRUST —

Table of Contents:

| | |
|--|---------|
| INREIT Consolidated Financial Data | 1 |
| Table of Contents..... | 3 |
| Message to Shareholders..... | 4 & 5 |
| Mission Statement..... | 6 |
| Our Business..... | 7 |
| Shareholders Return..... | 8 |
| Portfolio Analysis..... | 11 |
| Properties and Locations..... | 12 & 13 |
| Acquisition Strategy..... | 15 |
| New Construction..... | 16 & 17 |
| Board of Trustees..... | 18 |
| Advisors and Staff..... | 19 |
| Our Outlook for the Future..... | 20 |
| Audited Financial Statement..... | 21 |

Front Cover: Edgewood Vista in Bismarck, ND completed in 2009.

Inside Front Cover: Gathering room located inside Edgewood Vista in Bismarck, ND.

Left: Walgreens Stores in Batesville, AR, Fayetteville, AR and Alexandria, LA.

Inside Back Cover: Best Buy Store, part of the Grand Forks Market Place, Grand Forks, ND.

Back Cover: Stony Brook Apartments located in Omaha, NE.

2009 Annual Report

Message to Shareholders:



*Earl Strinden
Chairman of the Board*

*Mr. Strinden has served as
Chairman since April 2004,
and has been an INREIT
Trustee since May of 2003.*

Dear
Shareholders,

On behalf of your Board of Trustees and Advisors, we are pleased to report another year of growth and prosperity. To you, our valued shareholders, we want to extend our gratitude for your continued investment with us.

While the economy in North Dakota continues to be resilient, we do realize that many Real Estate Investment Trusts (REITs) are struggling in the current economic climate. Much of the concern in the REIT sector is focused on refinancing debt and maintaining cash dividends. These are areas where INREIT shareholders need not be concerned. We have more financial flexibility than we've had in many years and no near-term debt maturity concerns.

INREIT has remained keenly focused on making sure our debt maturities are well-laddered. We anticipate the Treasury Department and Congress will maintain their long-standing commitment to multi-family housing by promoting policies to keep interest rates low in order to minimize any rent increases due to higher borrowing costs. Moreover, we expect Fannie Mae and Freddie Mac to remain key financial resources to the apartment industry.

As for dividends, the important metric is dividend coverage ratio. Our dividend coverage ratio, as adjusted, was 1.42 as of year-end. This ratio reflects the cushion to the extent the funds from operations (FFO) exceeds dividends and distributions paid.

It is worth noting that during this past year many REITs began paying a portion of their regular dividends in stock or reducing or even eliminating dividends altogether to preserve cash. Your Board of Trustees has voted with confidence to continue to pay cash dividends. In fact, additionally, the Trustees voted to increase the dividend for the first quarter of 2010 to 19.25¢ per share per quarter, an increase from 18.625¢. Based on our current \$14.00 share or unit price, the dividend rate equates to a 5.50% annualized return.

As discussed in last year's annual report, INREIT's first priority was to keep INREIT safe and strong throughout these difficult times. Our conservative approach has and will continue to prosper, protect, and grow INREIT.

Our portfolio performed well thanks to a solid operating platform, strong assets, and moderate leverage. This marked our fifth straight year of solid operating growth. As we close 2009, we look back at a year of change, unprecedented economic conditions and inspired hope for the future.

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Now let us discuss our accomplishments during 2009 in more detail:

- INREIT surpassed \$325 million in total assets, ending the year at \$325,662,675 an increase from \$273,912,838 as of year - end 2008, marking an 18.89% increase during 2009.
- INREIT's FFO per share surpassed 1.00 for year ending 2009. FFO per share is \$1.03, increasing from \$0.72 per share for 2008, or a 44.44% increase. Additionally, on a weighted average, FFO INREIT reached \$1.06 per share compared to \$0.96 per share in 2008.
- Total revenue in 2009 surpassed \$40 million, ending the year at \$40,507,881, a 49% increase from 2008. The primary reason for the large increase in revenue was due to the nearly \$20 million of property acquired on 12/31/2008 with no corresponding revenue being reported until 2009.
- INREIT is continually looking for ways to automate basic functions to reduce cost and improve efficiency. During 2009, INREIT automated the dividend process to allow all shareholders and limited partners to receive dividends and distributions electronically.
- During 2009, INREIT's largest real estate investment, the Edgewood Vista Senior Housing project in Bismarck, ND, was completed. Along with the completion of Edgewood Vista, INREIT purchased three (3) Walgreen's, one (1) office building and three (3) apartment complexes for a total increase in real estate investments of \$42,484,735.

With respect to the industry, we have a long-term investment horizon and therefore, seek to invest in industries with favorable long-term fundamentals. We have diversified our investments among property types and regions to reduce concentration risk and economic downturns. Unlike so many companies in

the real estate sector and elsewhere, we have not borrowed beyond our capacity to meet our repayment obligations. We resisted the temptation to overextend or to acquire properties with short-term financing. As a result, we do not need to sell properties to meet debt repayment obligations. Most importantly, we do not intend to reduce our dividend.

Once again, on behalf of the Board of Trustees and Advisors, thank you for your continued support and confidence. Know that we will manage your investment appropriately in all economic cycles, understanding that first and foremost, we are stewards of our shareholders.

Sincerely,



Kenneth P. Regan
Chief Executive Officer

Mr. Regan has served as Chief Executive Officer since January 2008, and has been an INREIT Trustee since July of 2007.

A handwritten signature in blue ink that reads "Kenneth P. Regan".

Chief Executive Officer

A handwritten signature in blue ink that reads "Earl Strindberg".

Chairman of the Board

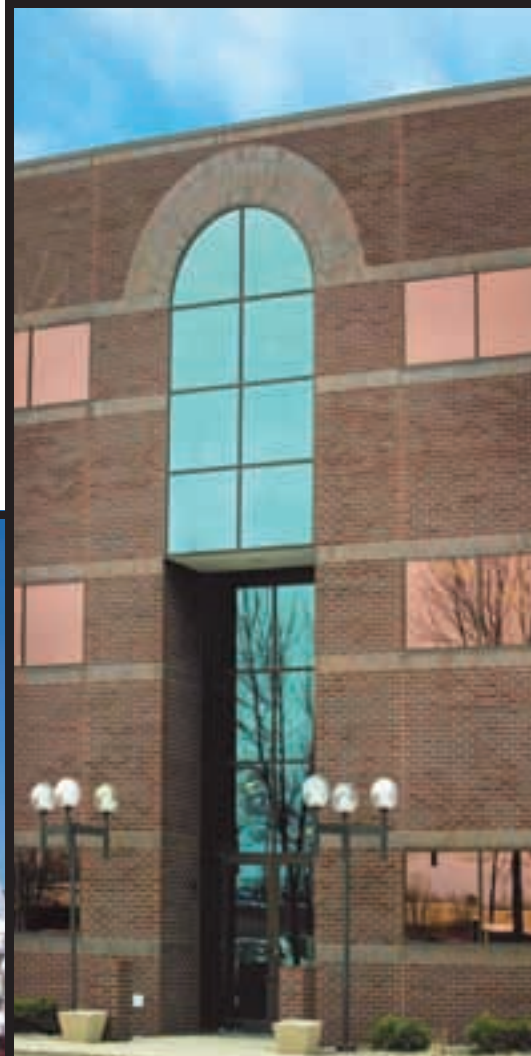


Our Mission:

The mission of INREIT is to consistently increase the value of our diversified investment portfolio through aggressive research and analysis of potential acquisitions.

INREIT will strive to make sound investment decisions while committing to the pursuit of increasing shareholder value. We will continue to focus on property in the Midwest where we currently hold the majority of our portfolio.

Our continued growth and success will be obtained through the loyal support of our shareholders, directors and advisors.



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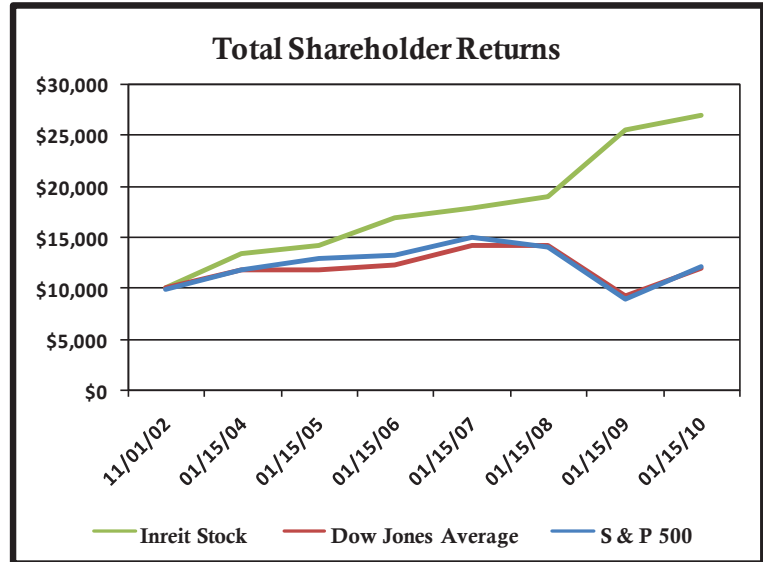
Grand Forks Market Place located in Grand Forks, ND

2009 Annual Report

Shareholder's Return

Dividend Distribution:

INREIT paid quarterly distributions to shareholders and limited partners during 2009 at a rate of 18.625 cents per quarter, for a total of \$9,275,000 in dividends/distributions to its shareholders and limited partners, an increase of \$2,562,000 from 2008. INREIT increased its annual dividend again in 2010 to 77 cents per share, an increase of 2.5 cents per share from one year ago. Since 2003, INREIT's dividend has increased from 50 cents per share, a 54% increase since inception.

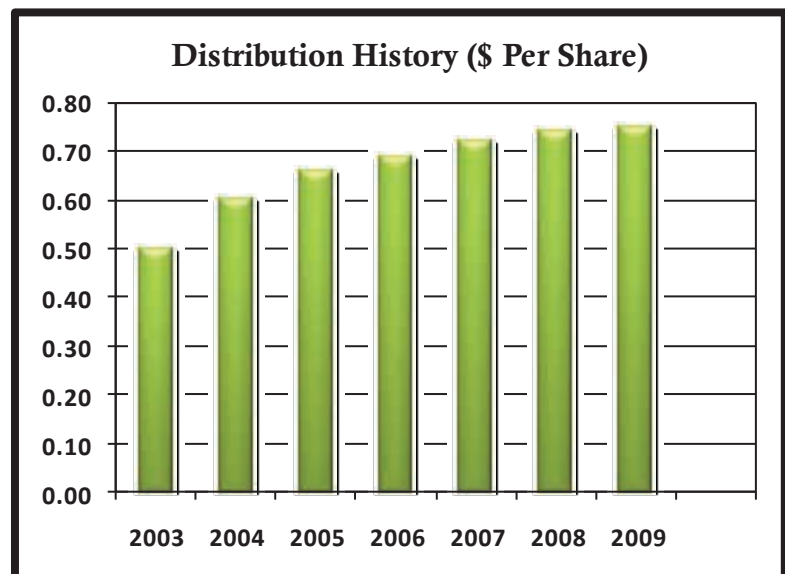


Dividend Reinvestment

INREIT offers a dividend reinvestment plan designed to make purchasing stock economical and convenient. The Plan is open to current shareholders and limited partners, as well as new investors. This Plan offers shareholders the opportunity to reinvest their cash dividends in additional shares at a 5% discount from the current asking price.

If participating in the Plan, shareholders will receive quarterly statements indicating the dividend amount paid, number of shares received through reinvestment and the price per share. Annual 1099-DIV forms will be provided to shareholders showing reportable income for tax purposes. There are no broker fees and INREIT administers the Dividend Reinvestment Plan at no charge to its shareholders.

For Illustrative purposes: \$10,000 invested in INREIT stock on November 1, 2002, with dividends reinvested, would be worth \$26,959 as of January 15, 2010. This value excludes the effect of brokerage commissions and income taxes.



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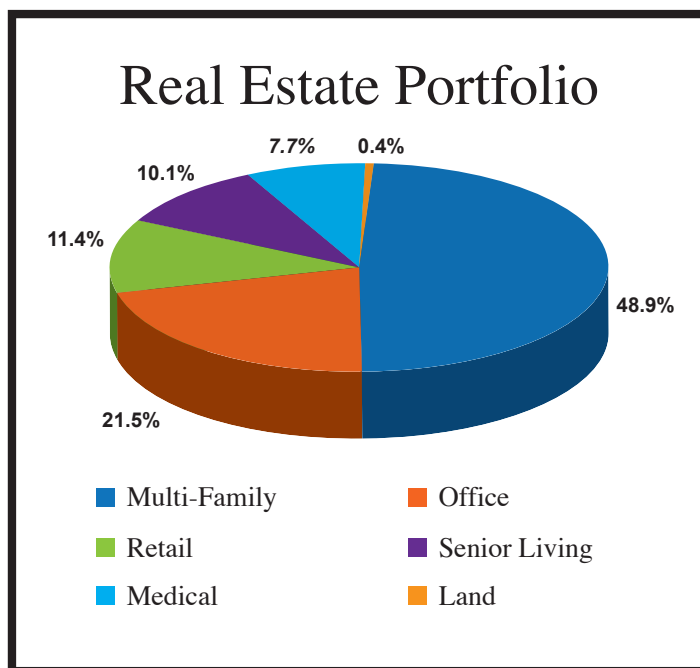


2009 Annual Report



The Regis Building (102,448 Sq. Ft.) located in Edina, MN.

Portfolio Analysis



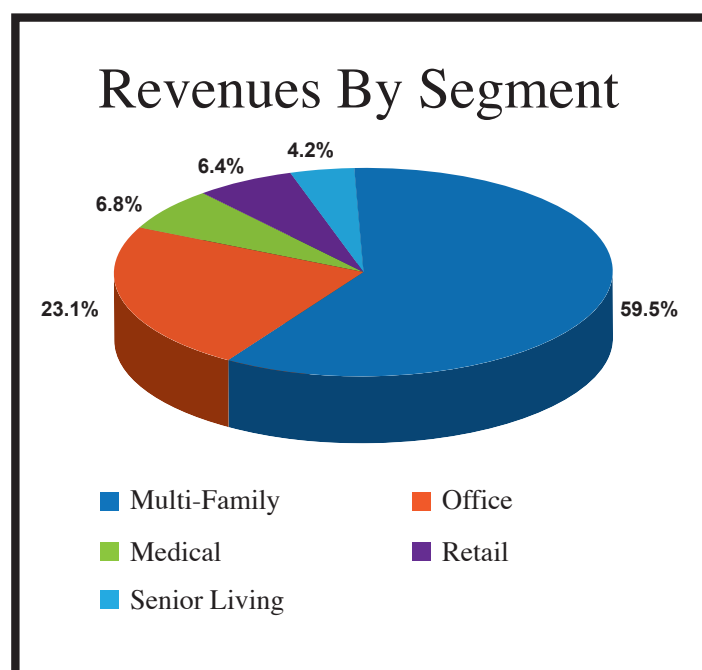
The investment in the Retail and Senior Living segments has increased to 11.4% and 10.1% respectively, while the investment in the Multi-Family segment has decreased to 48.9% from 54.1% at the end of 2008.

Diversification drives our strength, helping us to manage risk, grow cash flow and buffer against market and economic fluctuations. Our portfolio is diversified by geography, tenant-operator, asset type, operating model and payer source. This portfolio mix has enabled us to maintain our cash flow despite downturns in certain sectors, reimbursement change and challenges facing any single tenant or manager. INREIT has made well-structured investments in healthcare and senior housing assets operated by quality care providers and property managers, enabling our cash flow to grow during the turbulent economy.

INREIT's 2009 revenue breakdown reflects the effect of the relatively large amount of new investment in the Multi-Family segment in the second half of 2008. The large amount of revenue from the Multi-Family segment provides a buffer during these challenging economic conditions.

Additional revenue will be generated in retail and senior housing during 2010. The Bismarck Edgewood Vista project was not completed until October 2009 and therefore less than 20% of the annualized revenue was reported in 2009.

With the acquisition of the three Walgreen's stores and the completion of Edgewood Vista in Bismarck during 2009, INREIT's real estate portfolio mix is more balanced in comparison to 2008.



Property Locations

Multi-family Properties:

Bismarck, ND:

Fairview Apartments
Pebble Creek Apartments
Sierra Ridge Apartments
Sunset Ridge Apartments

Carrington, ND:

Ellingson Apartments

Fargo ND:

Auburn Apartments
Bayview Apartments
Brookfield Apartments
Berkshire Apartments
Betty Ann Apartments
Carlton Place
Danbury Apartments
Emerald Court
Flickertail Apartments
Hunter's Run
Maplewood Bend
Martha Alice
Maylor Manor
Oak Court
Parkwood Apartments
Prairiewood Court
Rosegate Apartments
Saddlebrook Apartments
Somerset Apartments
Southgate Apartments
Southview Village
Sunwood Estates
Twin Parks
Village Park
Village West
Westbrook Apartments
Westwood Estates
Willow Park

Grand Forks, ND:

Autumn Ridge
Carling Manor

Chandler Apartments

Colony Manor

Columbia West

Library Lane

Richfield & Harrison

Sunview Apartments

Village Apartments

**** Hawley, MN :**

Westside Apartments

Omaha, NE:

Stony Brook Apartments
Maple Ridge

Office Facilities:

Bismarck, ND:

Aetna Building

Duluth, MN:

Wells Fargo Building

Edina, MN:

Regis Building

Fargo, ND:

Bank of the West
Ear Acres Building
Echelon Building
Eide Bailly Building
Goldmark Office Park
Great American Ins. Building

Grand Forks, ND:

Gate City Building

Minot, ND:

Midtown Plaza Building

St. Cloud, MN:

Social Security Building

Retail Properties:

Alexandria, LA: Walgreens

Batesville, AR: Walgreens

Fargo, ND: West Point Center

Fayetteville, AR: Walgreens

Grand Forks, ND: GF Marketplace

**** Minneapolis, MN Area:**

Applebee's - Bloomington

Applebee's - Coon Rapids

Applebee's - Savage

Norfolk, NE: Colonial Plaza

Waite Park, MN: Becker Furniture

Medical Properties:

Biolife Plasma Centers

| | |
|-----------------|-------------------|
| Bismarck, ND | Eau Claire, WI |
| Grand Forks, ND | Janesville, WI |
| Mankato, MN | Marquette, MI |
| Onalaska, WI | Oshkosh, WI |
| Sheboygan, WI | Stevens Point, WI |

Senior Living:

Minot, ND: Edgewood Vista

Williston, ND: Golden Estates

Bismarck, ND: Edgewood Vista

Undeveloped Land

Fargo, ND: Echelon & Eide Bailly Land

Minot, ND: Four Acres in SE Minot

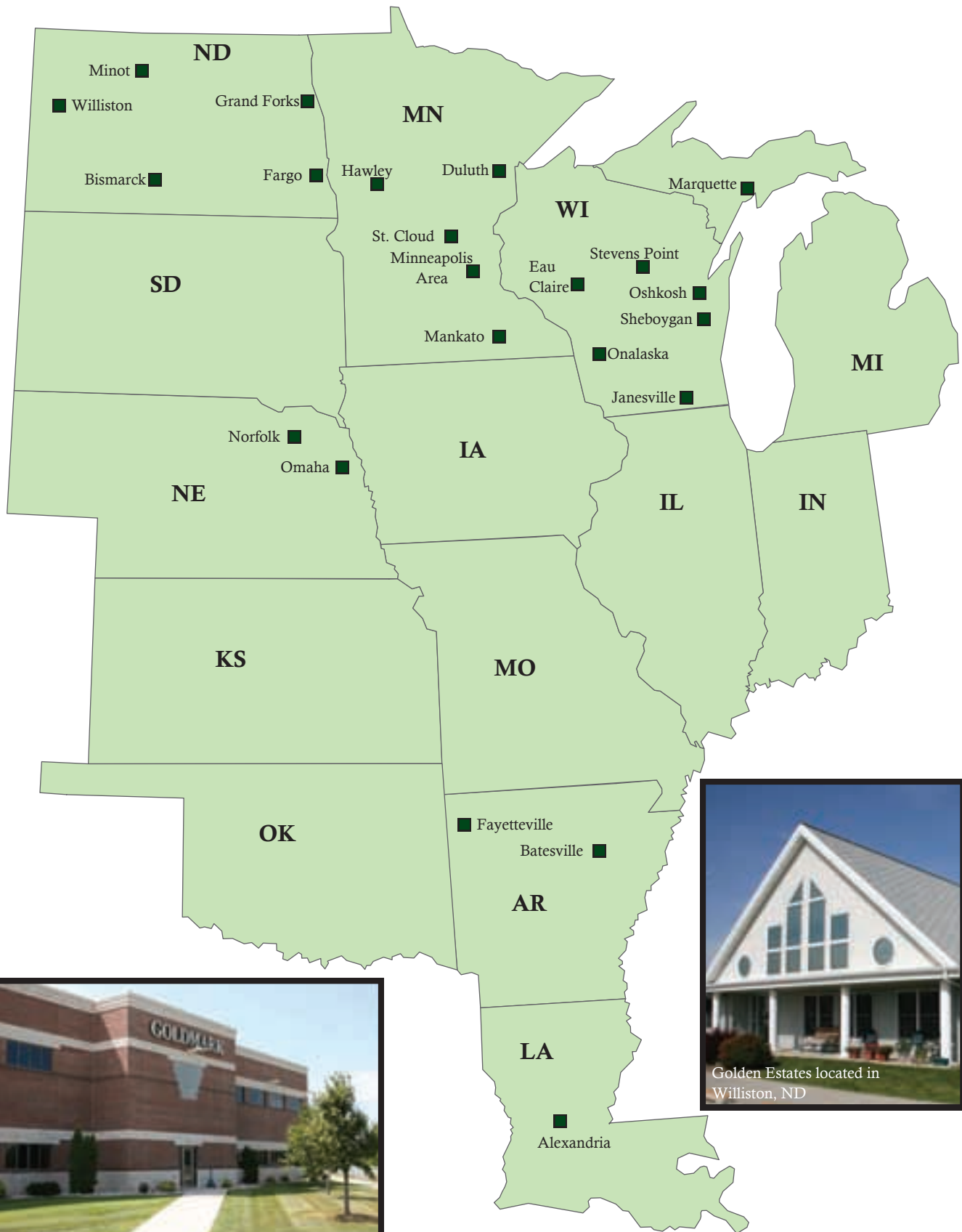
**** Property purchased in the first quarter of 2010.**



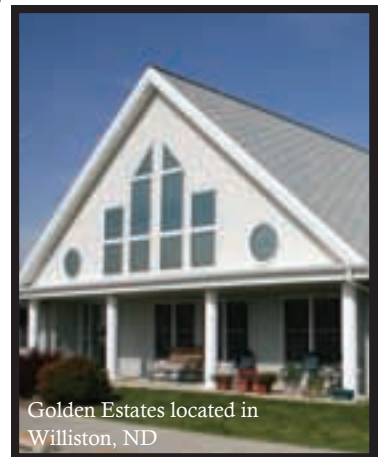
Rosegate Apartments located in Fargo, ND

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Goldmark Building located in Fargo, ND



Golden Estates located in Williston, ND



Acquisition Strategy:

Portfolio diversification is fundamental to our investment strategy as INREIT seeks to create and maintain an asset base that provides steady growth while being protected against rising property operating expenses, regional recessions, industry specific declines and fluctuations in property values and market rent levels. Regardless of capital market and economic conditions, we stay focused on improving operating results and portfolio quality, mitigating risks relating to interest rates and the real estate cycle, and applying strategies where our management skills and real estate expertise can add value.

Our Strategy to build long-term value for our shareholders remains simple:

- Pay a safe and growing dividend
- Generate steady and consistent Funds from Operations (FFO) per share growth
- Accomplish these dual objectives while assuming below average portfolio risk.

INREIT will acquire carefully underwritten investment properties to further diversify our portfolio and minimize risk.

The Advisors and Trustees will consider the following:

- Income producing capacity
- Demographic data including vacancy rates, building permits, and unemployment rates
- Property condition, if pre-owned
- Diversity as to size and location of properties
- Environmental concerns
- Availability of discount on the purchase price of an all cash purchase or on an assumption of debt transaction

Our goal is to provide shareholders with consistent growth and returns throughout any business cycle.



Stony Brook Apartments located in Omaha, NE

New Construction



Sunset Ridge Apartments:

With the completion of Edgewood Vista, our focus on construction has turned towards finishing Sunset Ridge in Bismarck, ND. This beautiful, modern Multi-family complex consists of three completed buildings with two more under construction. This five building complex is close to shopping, restaurants, and entertainment. Beautiful floor plans and modern conveniences make Sunset Ridge a renter's paradise.

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Edgewood Vista:

“Spectacular!” describes the finished product known as Edgewood Vista in Bismarck, ND. Completed in 2009, this beautiful complex has 94 independent living units, 84 assisted living units and 15 basic care. The architecture features vaulted ceilings in the dining and gathering rooms. A coffee shop and a chapel add to the charm. You’ll find that Edgewood Vista is Assisted Living at it’s finest!

2009 Annual Report

Board of Trustees

The Trustees are accountable to the Trust as fiduciaries and must exercise good faith and integrity in handling Trust affairs. The Board has the authority to approve or disapprove all investments recommended to the Trust by the Advisor. The Trustees will have ultimate control over management of the Trust and the conduct of Trust affairs; including acquisitions and dispositions of the Trust's assets.



From left: Timothy Hunt (Trustee since October 2003), James Wieland (Trustee since June 2007), Lawrence R. (Larry) O'Callaghan (Trustee since January 2003), Earl Strinden-Chairman of the Board (Trustee since May 2003), Rex Carlson (Trustee since July 2005), Peggy Becker (Trustee since January 2003), Bruce Furness (Trustee since May 2008), Clifford Fearing (Trustee since March 2005), Richard Savageau (Trustee since May 2009), Dr. Thomas I. Strinden (Trustee since January 2003), Philip Gisi (Trustee since May 2004), Kenneth P. Regan-Chief Executive Officer (Trustee since July 2007).

Our Board consists of twelve trustees, seven of whom are independent directors not affiliated with INREIT. All of our Trustees are experienced financial and real estate professionals. All of the Board committees - Audit and Executive, are composed primarily of independent trustees in order to ensure appropriate oversight by non-interested members of the board.

Audit Committee:

Phil Gisi - Chairman
Timothy Hunt
Peggy Becker
Rex Carlson - Alternate

Legal Counsel:

McGee, Hankla, Backes & Dobrovolny PC
Minot, ND

Executive Acquisition Committee:

Earl Strinden - Chairman
Phil Gisi
Rex Carlson
Bruce Furness
Cliff Fearing - Alternate

Auditors:

Eide Bailly LLP
Bismarck, ND



Advisors

The advisor for the Trust is INREIT Management, LLC, which has been specifically formed for such purpose. The Advisor will manage the affairs of the Trust, subject to the review and overall control of its Board of Trustees, who may remove the advisor without cause. The success of the Trust will depend, to a large extent, on the services and performance of the Advisor.



From Left: James Weiland, Roger Domres, Dale Lian, James D. Echtenkamp, Brad Williams, Kenneth P. Regan

INREIT Staff

Our day-to-day management and operations are the responsibility of the Advisor. The Advisors have hired a staff of qualified individuals. The staff along with the Advisors oversee our operations and provide various services to the Trust including the coordination of our offerings, investment and portfolio management, asset management and shareholder services.



From Left: Jackie Duke, Darla Iverson, Roger Domres, Anita Shipley, Laurie Schmaltz, Pete Winger

2009 Annual Report

Our Outlook for the Future

We had an extraordinary year in 2009 and remain optimistic for 2010. Like most businesses, we continue to be concerned about the weak economy and distressed credit markets. INREIT's strong balance sheet and liquidity, along with a high quality and diversified real estate portfolio, will enhance our stability in today's uncertain market. By diversifying capital in both industry and location, we are able to establish an earning platform that will bolster performance during the inevitable down cycles.

INREIT's financial flexibility coupled with our experience and skill, give us the ability to capitalize on the opportunities that today's market brings. This year we will continue to focus our efforts to:

Maintain a strong balance sheet

Maintain liquidity

Divest of non-productive and underperforming assets

Superior management of our existing assets

INREIT will also look for opportunities to:

Enhance our revenue stream

Improve NOI on under-performing assets

During 2009, a number of shareholders chose to liquidate their INREIT holdings. This was not due to a lack of confidence in INREIT but to offset other investment losses. Going into 2010, we expect fewer investors to liquidate and will be more aggressive in seeking shareholders to invest with us and share in INREIT's success. We firmly believe that over the long-term, investments in real estate are an important component of a well-diversified investment portfolio.

New Acquisitions

During the first quarter of 2010, INREIT has acquired over \$6,000,000 of income producing properties with another nearly \$4,000,000 during the second quarter.

The fourth of a five apartment building complex, (Bismarck, ND) will be completed in May 2010 with the fifth building scheduled to be completed in July 2010. Other opportunities are being scrutinized on an ongoing basis.

Dispositions

INREIT will continue to divest underperforming or non-productive assets. In addition, the Board approved of dispositions in areas where INREIT will not be acquiring additional properties.

INREIT sold its lone apartment complex in Carrington, ND and used these funds to help purchase one of the three Applebee's properties acquired in March of 2010.

Near-Term Maturities

As of year end 2009, INREIT had nearly \$10,000,000 in debt maturing this year. During the 1st quarter of 2010, INREIT has refinanced nearly \$4,000,000 with another \$2,000,000 being completed in the second quarter. Monitoring and managing short and long-term debt is always a focus.

Looking Ahead

While our view of the economy and the real estate markets is significantly more positive than a year ago, we recognize that considerable risk remains given the high level of government intervention that continues to take place. As a result, we will remain focused on our investment principals and priorities. While we look to acquire assets at a reasonable price, INREIT will maintain discipline and patient with respect to asset quality, location and price.

The recession has reinforced old lessons, and we believe the shareholders will be well served over time by our strong balance sheets and a conservative approach to managing and growing INREIT.

In closing we will use our success, experiences and strengths to continue building an excellent, sustainable enterprise that delivers reliable dividends and long-term value to our shareholders.

**CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2009 AND 2008**

**INREIT REAL ESTATE INVESTMENT TRUST
AND SUBSIDIARIES**

INREIT REAL ESTATE INVESTMENT TRUST AND SUBSIDIARIES

Table of Contents

| | <u>Page</u> |
|---|--------------------|
| INDEPENDENT AUDITOR'S REPORT | 1 |
| FINANCIAL STATEMENTS | |
| Consolidated Balance Sheets | 2 |
| Consolidated Statements of Operations | 3 |
| Consolidated Statements of Shareholders' Equity | 4 |
| Consolidated Statements of Cash Flows | 6 |
| Notes to Consolidated Financial Statements | 8 |



INDEPENDENT AUDITOR'S REPORT

Board of Trustees

INREIT Real Estate Investment Trust and subsidiaries

Minot, North Dakota

We have audited the accompanying consolidated balance sheets of **INREIT Real Estate Investment Trust and Subsidiaries** as of December 31, 2009 and 2008, and the related consolidated statements of operations, shareholders' equity, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of **INREIT Real Estate Investment Trust and Subsidiaries** as of December 31, 2009 and 2008, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Eide Bailly LLP

Bismarck, North Dakota

March 3, 2010

INREIT REAL ESTATE INVESTMENT TRUST AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
DECEMBER 31, 2009 AND 2008

| | <u>2009</u> | <u>2008</u> |
|--|------------------------------|------------------------------|
| ASSETS | | |
| PROPERTY AND EQUIPMENT, at cost, less accumulated depreciation | \$ 305,291,588 | \$ 254,577,743 |
| CASH AND CASH EQUIVALENTS | 8,702,274 | 12,202,562 |
| RESTRICTED DEPOSITS AND FUNDED RESERVES | 4,351,520 | 2,232,238 |
| DUE FROM RELATED PARTY | 879,002 | 444,359 |
| RECEIVABLES | 1,620,903 | 1,310,522 |
| PREPAID EXPENSES | 441,608 | 393,188 |
| NOTES RECEIVABLE | 1,966,396 | 424,085 |
| FINANCING COSTS, less accumulated amortization of \$299,640 in 2009 and \$175,002 in 2008 | 841,075 | 781,475 |
| SECURITIES, HELD TO MATURITY | - | 1,267,222 |
| RENT INCENTIVE, less accumulated amortization of \$16,667 in 2009 | 1,483,333 | - |
| OTHER ASSETS | 84,976 | 279,444 |
| | <u>\$ 325,662,675</u> | <u>\$ 273,912,838</u> |

See Notes to Consolidated Financial Statements

| | <u>2009</u> | <u>2008</u> |
|---|-----------------------|-----------------------|
| LIABILITIES | | |
| MORTGAGE NOTES PAYABLE | \$ 190,964,710 | \$ 141,531,558 |
| SPECIAL ASSESSMENTS PAYABLE | 1,565,683 | 1,535,100 |
| DIVIDENDS PAYABLE | 2,373,207 | 2,010,824 |
| DUE TO RELATED PARTY | 60,435 | 1,600,906 |
| TENANT SECURITY DEPOSITS PAYABLE | 1,094,283 | 874,223 |
| INVESTMENT CERTIFICATES | 468,078 | 378,037 |
| ACCOUNTS PAYABLE - TRADE | 12,772 | 41,957 |
| ACCOUNTS PAYABLE - CONSTRUCTION | 332,116 | 1,561,050 |
| FAIR VALUE OF INTEREST RATE SWAP | 168,332 | 285,850 |
| DEFERRED INSURANCE PROCEEDS | 148,880 | 291,152 |
| ACCRUED EXPENSES | 2,654,133 | 2,385,302 |
| Total liabilities | <u>199,842,629</u> | <u>152,495,959</u> |
| SHAREHOLDERS' EQUITY | | |
| NONCONTROLLING INTEREST IN OPERATING PARTNERSHIP | 100,023,106 | 99,533,435 |
| BENEFICIAL INTEREST | 25,965,272 | 22,169,294 |
| ACCUMULATED COMPREHENSIVE LOSS | (168,332) | (285,850) |
| | <u>125,820,046</u> | <u>121,416,879</u> |
| | <u>\$ 325,662,675</u> | <u>\$ 273,912,838</u> |

INREIT REAL ESTATE INVESTMENT TRUST AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
YEARS ENDED DECEMBER 31, 2009 AND 2008

| | <u>2009</u> | <u>2008</u> |
|---|---------------------|---------------------|
| INCOME | | |
| Income from rental operations | \$ 38,194,670 | \$ 25,740,651 |
| Interest income | 609,202 | 416,065 |
| Gain on disposal of property and equipment | 319,237 | 344,646 |
| Insurance proceeds | 199,546 | - |
| Other income | 1,185,226 | 699,601 |
| | <u>40,507,881</u> | <u>27,200,963</u> |
| EXPENSES | | |
| Expenses from rental operations | | |
| Interest | 10,353,901 | 7,255,723 |
| Depreciation and amortization | 7,381,597 | 5,021,384 |
| Real estate taxes | 4,399,957 | 3,102,639 |
| Property management fees | 3,235,665 | 1,879,146 |
| Utilities | 2,831,072 | 1,895,546 |
| Repairs and maintenance | 3,970,801 | 2,661,428 |
| Insurance | 670,863 | 368,705 |
| Salary and wages | 36,173 | 34,486 |
| Food costs for residents | 22,759 | 26,156 |
| Administrative | 70,115 | 63,207 |
| | <u>32,972,903</u> | <u>22,308,420</u> |
| Administration of REIT | | |
| Administrative expenses | 50,529 | 57,192 |
| Advisory fees | 649,824 | 610,686 |
| Director fees | 38,300 | 37,650 |
| Rent | 300 | 1,800 |
| Legal and accounting | 162,561 | 142,422 |
| | <u>901,514</u> | <u>849,750</u> |
| Total expenses | <u>33,874,417</u> | <u>23,158,170</u> |
| INCOME BEFORE LOSS ON IMPAIRMENT OF PROPERTY | 6,633,464 | 4,042,793 |
| LOSS ON IMPAIRMENT OF PROPERTY | <u>311,807</u> | <u>-</u> |
| NET INCOME | 6,321,657 | 4,042,793 |
| NET INCOME ATTRIBUTABLE TO THE NONCONTROLLING INTEREST | <u>4,969,645</u> | <u>2,991,080</u> |
| NET INCOME ATTRIBUTABLE TO INREIT REAL ESTATE INVESTMENT TRUST | <u>\$ 1,352,012</u> | <u>\$ 1,051,713</u> |

INREIT REAL ESTATE INVESTMENT TRUST AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
YEARS ENDED DECEMBER 31, 2009 AND 2008

| | Common Shares | Common Shares Amount | Accumulated Earnings (Deficit) | Total Beneficial Interest | Noncontrolling Interest | Accumulated Comprehensive Loss | Total |
|---|------------------|----------------------------|--------------------------------------|---------------------------------|----------------------------|--------------------------------------|----------------|
| BALANCE, DECEMBER 31, 2007 | 2,146,916 | \$22,373,666 | \$ (4,138,304) | \$ 18,235,362 | \$ 50,053,278 | \$ - | \$ 68,288,640 |
| Issuance of common shares | 315,799 | 4,163,459 | | 4,163,459 | | | 4,163,459 |
| Contribution of assets in exchange for the issuance of minority interest shares | | | | | 54,925,817 | | 54,925,817 |
| Repurchase of shares | (80,969) | (1,002,228) | | (1,002,228) | | | (1,002,228) |
| Dividends | | | (1,278,596) | (1,278,596) | (3,424,199) | | (4,702,795) |
| Dividends declared | | | (462,593) | (462,593) | (1,548,231) | | (2,010,824) |
| Dividends reinvested | 87,787 | 1,183,543 | | 1,183,543 | | | 1,183,543 |
| UPREIT units converted to REIT common shares | 47,978 | 580,499 | | 580,499 | (580,499) | | - |
| Syndication costs | | | (301,865) | (301,865) | (2,883,811) | | (3,185,676) |
| Decrease in fair value of interest rate swap | | | | | | (285,850) | (285,850) |
| Net income | | | 1,051,713 | 1,051,713 | 2,991,080 | | 4,042,793 |
| BALANCE, DECEMBER 31, 2008 | 2,517,511 | \$27,298,939 | \$ (5,129,645) | \$ 22,169,294 | \$ 99,533,435 | \$ (285,850) | \$ 121,416,879 |

(continued on next page)

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY – page 2

| | Common Shares | Common Shares Amount | Accumulated Earnings (Deficit) | Total Beneficial Interest | Noncontrolling Interest | Accumulated Comprehensive Loss | Total |
|---|------------------|----------------------------|--------------------------------------|---------------------------------|----------------------------|--------------------------------------|----------------|
| BALANCE, DECEMBER 31, 2008 | 2,517,511 | \$27,298,939 | \$ (5,129,645) | \$ 22,169,294 | \$ 99,533,435 | \$ (285,850) | \$ 121,416,879 |
| Issuance of common shares | 275,220 | 3,906,520 | | 3,906,520 | | | 3,906,520 |
| Contribution of assets in exchange for the issuance of minority interest shares | | | | | 5,522,930 | | 5,522,930 |
| Repurchase of shares | (243,891) | (2,928,404) | (1,477,139) | (2,928,404) | (5,425,130) | | (2,928,404) |
| Dividends | | | (532,496) | (532,496) | (1,840,711) | | (6,902,269) |
| Dividends declared | | | | | | | (2,373,207) |
| Dividends reinvested | 97,733 | 1,300,741 | | 1,300,741 | | | 1,300,741 |
| UPREIT units converted to REIT common shares | 212,466 | 2,461,120 | | 2,461,120 | (2,461,120) | | - |
| Syndication costs | | | (286,376) | (286,376) | (275,943) | | (562,319) |
| Increase in fair value of interest rate swap | | | | | | 117,518 | 117,518 |
| Net income | | | 1,352,012 | 1,352,012 | 4,969,645 | | 6,321,657 |
| BALANCE, DECEMBER 31, 2009 | 2,859,039 | \$32,038,916 | \$ (6,073,644) | \$ 25,965,272 | \$100,023,106 | \$ (168,332) | \$ 125,820,046 |

INREIT REAL ESTATE INVESTMENT TRUST AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2009 AND 2008

| | <u>2009</u> | <u>2008</u> |
|--|----------------------------|----------------------------|
| OPERATING ACTIVITIES | | |
| Net income | \$ 1,352,012 | \$ 1,051,713 |
| Adjustments to reconcile net income to net cash from operating activities | | |
| Gain on sale of property and equipment | (319,237) | (344,646) |
| Loss on impairment of property | 311,807 | - |
| Depreciation | 7,256,706 | 4,918,909 |
| Amortization | 124,891 | 102,475 |
| Minority interest | 4,969,645 | 2,991,080 |
| Effects on operating cash flows due to changes in | | |
| Tenant security deposits | (243,621) | (851,490) |
| Due from related party | (434,643) | 240,353 |
| Receivables | (310,381) | (1,064,374) |
| Prepaid expenses | (48,420) | (278,941) |
| Rent incentive | (1,483,333) | - |
| Other assets | 194,468 | (52,444) |
| Due to related party for accrued management fees | (10,963) | (36,291) |
| Tenant security deposits payable | 220,060 | 540,324 |
| Accounts payable | (29,185) | 29,551 |
| Accrued expenses | 268,831 | 1,407,048 |
| NET CASH FROM OPERATING ACTIVITIES | <u>11,818,637</u> | <u>8,653,267</u> |
| INVESTING ACTIVITIES | | |
| Purchase of property and equipment | (29,782,599) | (27,601,867) |
| Due to related party for acquisition fees | (528,300) | 528,300 |
| Cash received during purchase of property | - | 3,615,812 |
| Proceeds from sale of property and equipment | 278,270 | 4,604,530 |
| Insurance proceeds received | 549,551 | - |
| Real estate tax and insurance escrows | (697,797) | 1,095,149 |
| Purchase of securities | - | (400,000) |
| Notes receivable issued | - | (430,028) |
| Notes receivable payments received | 47,803 | 5,943 |
| Proceeds from sale of securities | 1,267,222 | 912,528 |
| Deferred insurance proceeds | (142,272) | 291,152 |
| Net deposits to replacement reserve | (524,821) | (115,795) |
| Net deposits to exchange escrow | (653,043) | - |
| NET CASH USED FOR INVESTING ACTIVITIES | <u>(30,185,986)</u> | <u>(17,494,276)</u> |

(continued on next page)

CONSOLIDATED STATEMENTS OF CASH FLOWS – page 2

| | <u>2009</u> | <u>2008</u> |
|---|-------------------------|--------------------------|
| FINANCING ACTIVITIES | | |
| Payments for financing costs | (184,491) | (222,455) |
| Proceeds from investment certificates issued | 333,240 | 190,798 |
| Payments on investment certificates | (243,199) | (43,188) |
| Principal payments on special assessments payable | (216,108) | (177,826) |
| Proceeds from issuance of mortgage notes payable | 28,696,777 | 22,568,698 |
| Principal payments on mortgage notes payable | (3,760,345) | (2,482,731) |
| Net change in notes payable | - | (200,309) |
| Payments on construction payable | (1,561,050) | - |
| Proceeds from issuance of shares | 3,906,520 | 4,163,459 |
| Repurchase of shares | (2,928,404) | (1,002,228) |
| Distributions paid to shareholders | (638,991) | (478,814) |
| Distributions paid to minority partners | (6,973,361) | (4,171,835) |
| Payment of syndication costs | (562,319) | (3,185,676) |
| Due to related party for syndication costs | (1,001,208) | 559,756 |
| NET CASH FLOWS FROM FINANCING ACTIVITIES | <u>14,867,061</u> | <u>15,517,649</u> |
| NET CHANGE IN CASH AND CASH EQUIVALENTS | (3,500,288) | 6,676,640 |
| CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR | <u>12,202,562</u> | <u>5,525,922</u> |
| CASH AND CASH EQUIVALENTS AT END OF YEAR | <u>\$ 8,702,274</u> | <u>\$ 12,202,562</u> |
| SCHEDULE OF CASH FLOW INFORMATION | | |
| Cash paid during the year for interest, net of capitalized interest of \$423,207 and \$2,662 in 2009 and 2008 | <u>\$ 10,121,642</u> | <u>\$ 6,980,373</u> |
| SUPPLEMENTARY SCHEDULE OF NONCASH INVESTING AND FINANCING ACTIVITIES | | |
| Distributions reinvested | <u>\$ 1,300,741</u> | <u>\$ 1,183,543</u> |
| Distributions declared and not paid | <u>\$ 532,496</u> | <u>\$ 462,593</u> |
| UPREIT distributions declared and not paid | <u>\$ 1,840,711</u> | <u>\$ 1,548,231</u> |
| UPREIT units converted to REIT common shares | <u>\$ 2,461,120</u> | <u>\$ 580,499</u> |
| Acquisition of assets in exchange for the issuance of minority interest shares in UPREIT | <u>\$ 5,522,930</u> | <u>\$ 54,925,817</u> |
| Acquisition of assets through assumption of debt and property purchased with financing | <u>\$ 24,496,720</u> | <u>\$ 44,630,407</u> |
| Acquisition of assets included in payables | <u>\$ 332,116</u> | <u>\$ 1,561,050</u> |
| Increase in land improvements due to increase in special assessments payable | <u>\$ 246,691</u> | <u>\$ 863,345</u> |
| Issuance of note receivable for sale of land | <u>\$ 1,590,114</u> | <u>\$ -</u> |
| Unrealized (gain) loss on interest rate swap | <u>\$ (117,518)</u> | <u>\$ 285,850</u> |

INREIT REAL ESTATE INVESTMENT TRUST AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2009 AND 2008

NOTE 1 - ORGANIZATION

The INREIT Real Estate Investment Trust ("INREIT") is a registered, but unincorporated business trust organized in North Dakota in November 2002. INREIT has elected to be taxed as a Real Estate Investment Trust ("REIT") under Sections 856-860 of the Internal Revenue Code, which requires that 75 percent of the assets of a REIT must consist of real estate assets and that 75 percent of its gross income must be derived from real estate. The net income of the REIT is allocated in accordance with the stock ownership in the same fashion as a regular corporation.

INREIT previously established an operating partnership (INREIT Properties, LLLP) and transferred all of its assets and liabilities to the operating partnership in exchange for general partnership units. The general partner has management responsibility for all activities of the operating partnership. As of December 31, 2009 and 2008, INREIT had an ownership percentage of approximately 21 percent. INREIT Properties, LLLP is the 100% owner of Grand Forks Inreit, LLC, Minot Vista Properties, LLC, Autumn Ridge Inreit, LLC, Bismarck Interstate INREIT, LLC, 32nd Avenue Inreit, LLC, INREIT BL Mankato, LLC, INREIT BL Janesville, LLC, INREIT BL Eau Claire, LLC, INREIT BL Stevens Point, LLC, INREIT BL Sheboygan, LLC, INREIT BL Oshkosh, LLC, INREIT BL Onalaska, LLC, INREIT BL Grand Forks, LLC, INREIT BL Marquette, LLC, INREIT BL Bismarck, LLC, INREIT Stonybrook, LLC, INREIT Alexandria, LLC, INREIT Batesville, LLC, INREIT Fayetteville, LLC, and a 50% owner of Marketplace Investors, LLC,

NOTE 2 - PRINCIPAL ACTIVITY AND SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The consolidated financial statements include the accounts of INREIT; INREIT Properties, LLLP; Grand Forks Inreit, LLC; Minot Vista Properties, LLC; Autumn Ridge Inreit, LLC; Bismarck Interstate INREIT, LLC; 32nd Avenue Inreit, LLC; INREIT BL Mankato, LLC; INREIT BL Janesville, LLC; INREIT BL Eau Claire, LLC; INREIT BL Stevens Point, LLC; INREIT BL Sheboygan, LLC; INREIT BL Oshkosh, LLC; INREIT BL Onalaska, LLC; INREIT BL Grand Forks, LLC; INREIT BL Marquette, LLC; INREIT BL Bismarck, LLC; INREIT Stonybrook, LLC; INREIT Alexandria, LLC; INREIT Batesville, LLC; INREIT Fayetteville, LLC; and Marketplace Investors, LLC. All significant intercompany transactions and balances have been eliminated in consolidation.

Principal Business Activity

INREIT has a general partner interest in INREIT Properties, LLLP, which owns and operates the following property:

Residential Property

- 2,160 units in Fargo, North Dakota.
- 533 units in Grand Forks, North Dakota.
- 262 units in Bismarck, North Dakota.
- 20 units in Carrington, North Dakota.
- 316 units in Omaha, Nebraska.
- 16 unit assisted living facility in Williston, North Dakota.
- 398 unit assisted living facility in Bismarck, North Dakota.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Commercial Property

- 31,000 square foot office building in Fargo, North Dakota.
- 20,000 square foot office building in Minot, North Dakota.
- 45,000 square foot retail complex in Norfolk, Nebraska.
- 15,000 square foot office and retail complex in Fargo, North Dakota.
- 28,500 square foot office and retail complex in Fargo, North Dakota.
- 30,200 square foot retail facility in Waite Park, Minnesota.
- 17,000 square foot office building in Fargo, North Dakota.
- 128,385 square foot office complex in Fargo, North Dakota.
- 10,810 square foot office building in St. Cloud, Minnesota.
- 100,810 square foot office building in Duluth, MN.
- 11,973 square foot office building in Fargo, North Dakota.
- 21,492 square foot office building and 1,625 square foot storage area in Grand Forks, North Dakota.
- 102,448 square foot office building in Edina, Minnesota.

INREIT Properties, LLLP is the 100% owner of Grand Forks Inreit, LLC, which owns a 1/3 interest as a tenant in common of Grand Forks Marketplace Retail Center. INREIT Properties, LLLP is also the 50% owner of Marketplace Investors, LLC, which owns a 1/3 interest as a tenant in common of Grand Forks Marketplace Retail Center. Grand Forks Marketplace Retail Center has approximately 183,000 square feet of commercial space in Grand Forks, North Dakota.

INREIT Properties, LLLP owns a 1/3 interest as a tenant in common of a 136 unit apartment complex located in Bismarck, North Dakota.

INREIT Properties, LLLP owns a 2/3 interest as a tenant in common of a commercial building with approximately 75,000 square feet of rental space in Fargo, North Dakota.

INREIT Properties, LLLP is the owner of Minot Vista Properties, LLC, which owns and leases a 174 unit assisted living facility in Minot, North Dakota.

INREIT Properties, LLLP is the owner of Bismarck Interstate INREIT, LLC, which owns and leases two commercial buildings with approximately 75,000 square feet of rental space in Bismarck, North Dakota.

INREIT Properties, LLLP is the owner of INREIT Alexandria, LLC, INREIT Batesville, LLC, and INREIT Fayetteville, LLC, which own a total of three separate commercial properties totaling 43,930 square feet. These properties are located in Alexandria, Louisiana, Batesville, Arkansas, and Fayetteville, Arkansas.

INREIT Properties, LLLP is the owner of INREIT BL Mankato, LLC, INREIT BL Janesville, LLC, INREIT BL Eau Claire, LLC, INREIT BL Stevens Point, LLC, INREIT BL Sheboygan, LLC, INREIT BL Oshkosh, LLC, INREIT BL Onalaska, LLC, INREIT BL Grand Forks, LLC, INREIT BL Marquette, LLC, and INREIT BL Bismarck, LLC, which own a total of ten separate commercial properties totaling 124,686 square feet. These properties are located in Mankato, Minnesota; Janesville, Wisconsin; Eau Claire, Wisconsin; Stevens Point, Wisconsin; Sheboygan, Wisconsin; Oshkosh, Wisconsin; Onalaska, Wisconsin; Grand Forks, North Dakota; Marquette, Michigan; and Bismarck, North Dakota.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Concentration of Credit Risk

INREIT's cash balances are maintained in various bank deposit accounts. The bank deposit accounts may exceed federally insured limits at various times throughout the year.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Property and Equipment

Property and equipment is stated at cost. All costs associated with the development and construction of real estate investments, including acquisition fees and interest, are capitalized as a cost of the property. Expenditures for renewals and improvements that significantly add to the productive capacity or extend the useful life of an asset are capitalized. Expenditures for routine maintenance and repairs, which do not add to the value or extend useful lives, are charged to expense as incurred.

Depreciation is provided for over the estimated useful lives of the individual assets using the straight-line method over the following estimated useful lives:

| | |
|----------------------------|----------|
| Buildings and improvements | 40 years |
| Furniture and fixtures | 9 years |

Depreciation expense for the year ended December 31, 2009 and 2008, totaled \$7,256,706 and \$4,918,909, respectively.

Annually, INREIT evaluates its real estate investments for significant changes in the operations to assess whether any impairment indications are present, including recurring operating losses and significant adverse changes in legal factors or business climate that affect the recovery of the recorded value. If any real estate investment is considered impaired, a loss is provided to reduce the carrying value of the property to its estimated fair value.

Cash and Cash Equivalents

Highly liquid investments with a maturity of three months or less when purchased are classified as cash equivalents.

Receivables

Receivables consist primarily of amounts due for rent and real estate taxes. The receivables are non-interest bearing. The carrying amount of receivables is reduced by an amount that reflects management's best estimates of the amounts that will not be collected. As of December 31, 2009 and 2008, management determined that no allowance was necessary for uncollectible receivables.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Securities

INREIT's securities are all classified and accounted for as held to maturity. Securities classified as held to maturity are those securities that INREIT has the ability and intent to hold to maturity. Securities held to maturity are recorded at amortized cost.

Purchase premiums and discounts are recognized in interest income using the effective interest method over the terms of the securities. Declines in the fair value of securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, management considers the length of time and the extent to which the fair value has been less than cost, the financial condition and near-term prospects of the issuer, and the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

Rental Incentives

Rental incentives consist of up-front cash payments to lessees to sign the lease. Rental incentives are amortized against rental income over the term of the lease.

Noncontrolling Interest

Interests in the operating partnership held by limited partners are represented by operating partnership units. The operating partnerships' income is allocated to holders of units based upon the ratio of their holdings to the total units outstanding during the period. Capital contributions, distributions, syndication costs, and profits and losses are allocated to noncontrolling interests in accordance with the terms of the operating partnership agreement.

Financing Costs

Financing costs incurred in connection with financing have been capitalized and are being amortized over the life of the financing using the straight-line method.

Syndication Costs

Syndication costs consist of costs paid to attorneys, accountants, and selling agents, related to the raising of capital. Included in syndication costs are acquisition fees and commissions. These fees are paid based on management's discretion. Syndication costs are recorded as a reduction to equity and minority interest.

Federal Income Taxes

INREIT has elected to be taxed as a real estate investment trust ("REIT") under the Internal Revenue Code. A REIT calculates taxable income similar to other domestic corporations, with the major difference being that a REIT is entitled to a deduction for dividends paid. A REIT is generally required to distribute each year at least 90 percent of its taxable income. If it chooses to retain the remaining 10 percent of taxable income, it may do so, but it will be subject to a corporate tax on such income. REIT shareholders are taxed on REIT distributions of ordinary income in the same manner as they are taxed on other corporate distributions.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

INREIT intends to continue to qualify as a real estate investment trust as defined by the Internal Revenue Code and, as such, will not be taxed on the portion of the income that is distributed to the shareholders. In addition, INREIT intends to distribute all of its taxable income, therefore, no provision or liability for income taxes have been recorded in the financial statements.

INREIT Properties, LLLP is organized as a limited partnership. Income or loss is allocated to the partners in accordance with the provisions of the Internal Revenue Code 704(b) and 704(c). UPREIT status allows non-recognition of gain by an owner of appreciated real estate if that owner contributes the real estate to a partnership in exchange for partnership interest. The conversion of partnership interest to shares of beneficial interest in the REIT will be a taxable event to the limited partner.

INREIT has adopted the provisions of FASB Accounting Standards Codification Topic ASC 740-10, on January 1, 2009. The implementation of this standard had no impact on the financial statements. As of both the date of adoption, and as of December 31, 2009, the unrecognized tax benefit accrual was zero.

Recent Accounting Pronouncements

In December 2007, the FASB issued Accounting Standards Codification Topic ASC 810-10. ASC 810-10 changes the accounting and reporting for minority interests. Minority interests will be re-characterized as noncontrolling interests and will be reported as a component of equity separate from the parent's equity, and purchases or sales of equity interests that do not result in a change in control will be accounted for as equity transactions. In addition, net income attributable to the noncontrolling interest will be included in consolidated net income on the face of the income statement and upon a loss of control, the interest sold, as well as any interest retained, will be recorded at fair value with any gain or loss recognized in earnings. Effective January 1, 2009, INREIT adopted ASC 810-10.

Revenue Recognition

Housing units are rented under short-term lease agreements. Commercial space is rented under long-term lease agreements.

INREIT derives over 95% of its revenues from tenant rents and other tenant-related activities. Tenant rents include base rents, expense reimbursements (such as common area maintenance, real estate taxes and utilities), and straight-line rents. INREIT records base rents on a straight-line basis, which means that the monthly base rent income according to the terms of INREIT's leases with its tenants is adjusted so that an average monthly rent is recorded for each tenant over the term of its lease. The straight-line rent adjustment increased revenue by \$411,304 and \$489,060 in 2009 and 2008. The straight-line receivable balance included in receivables on the consolidated balance sheet as of December 31, 2009 and 2008 was \$900,364 and \$489,060, respectively. INREIT receives payments for these reimbursements from substantially all its multi-tenant commercial tenants throughout the year based on estimates. Differences between estimated recoveries and the final billed amounts, which are immaterial, are recognized in the subsequent year.

Advertising and Marketing

Costs incurred for advertising and marketing are expensed as incurred. Advertising and marketing expense for the years ended December 31, 2009 and 2008 was \$31,800 and \$17,333, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Capitalized Interest

Interest of \$423,207 and \$2,662 has been capitalized to property and equipment for the years ended December 31, 2009 and 2008, respectively.

NOTE 3 - PROPERTY AND EQUIPMENT

Property and equipment as of December 31, 2009 is as follows:

| | Residential | Commercial | Total |
|------------------------------------|------------------------------|------------------------------|------------------------------|
| Land and land improvements | \$ 17,616,191 | \$ 19,136,229 | \$ 36,752,420 |
| Building and improvements | 161,441,426 | 109,753,763 | 271,195,189 |
| Furniture and fixtures | 10,367,282 | 1,466,420 | 11,833,702 |
| Construction in progress (Note 17) | 1,638,850 | - | 1,638,850 |
| | <u>191,063,749</u> | <u>130,356,412</u> | <u>321,420,161</u> |
| Less accumulated depreciation | <u>(9,089,235)</u> | <u>(7,039,338)</u> | <u>(16,128,573)</u> |
| | <u>\$ 181,974,514</u> | <u>\$ 123,317,074</u> | <u>\$ 305,291,588</u> |

Property and equipment as of December 31, 2008 is as follows:

| | Residential | Commercial | Total |
|-------------------------------|------------------------------|-----------------------------|------------------------------|
| Land and land improvements | \$ 17,167,546 | \$ 13,513,499 | \$ 30,681,045 |
| Building and improvements | 130,267,183 | 84,141,257 | 214,408,440 |
| Furniture and fixtures | 8,249,731 | 1,466,420 | 9,716,151 |
| Construction in progress | 8,647,151 | - | 8,647,151 |
| | <u>164,331,611</u> | <u>99,121,176</u> | <u>263,452,787</u> |
| Less accumulated depreciation | <u>(5,094,088)</u> | <u>(3,780,956)</u> | <u>(8,875,044)</u> |
| | <u>\$ 159,237,523</u> | <u>\$ 95,340,220</u> | <u>\$ 254,577,743</u> |

During 2009, INREIT recorded an impairment loss of \$311,807 on one property due to the net book value of the property and equipment exceeding its fair market value. The impairment of the property and equipment was as a result of incurring recurring losses, vacancies, and negative cash flows. INREIT used the appraised value from an independent appraisal, in measuring the impairment loss.

During 2009, INREIT received insurance proceeds in the amount of \$749,098 for damages caused by a storm on two properties. INREIT reduced the book value of the property and equipment by \$549,552 and recorded income in the amount of \$199,546.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 4 - RESTRICTED DEPOSITS AND FUNDED RESERVES

| | 2009 | 2008 |
|---------------------------------------|---------------------|---------------------|
| Tenant security deposits | \$ 1,118,972 | \$ 875,351 |
| Real estate tax and insurance escrows | 1,575,427 | 877,630 |
| Replacement reserves | 1,004,078 | 479,257 |
| Exchange escrow | 653,043 | - |
| | <u>\$ 4,351,520</u> | <u>\$ 2,232,238</u> |

Tenant Security Deposits

Pursuant to management policy, INREIT has set aside funds to repay tenant security deposits upon tenant move-out.

Real Estate Tax and Insurance Escrows

Pursuant to the terms of certain mortgages and management policy, INREIT established and maintains real estate tax escrows and insurance escrows to pay real estate taxes and insurance. INREIT is to contribute to the account monthly an amount equal to 1/12 of the estimated real estate taxes and insurance premiums.

Replacement Reserves

Pursuant to the terms of certain mortgages and management policy, INREIT established and maintains several replacement reserve accounts. INREIT makes monthly deposits into the replacement reserve accounts to be used for repairs and replacements on the property. Certain replacement reserve accounts require authorization from the mortgage company for withdrawals.

Exchange Escrow

INREIT established an exchange escrow account in order to facilitate a Section 1031 exchange upon the sale of their Minot Land. The cash proceeds from the Minot Land sale are held in escrow until qualifying properties are purchased at which time, the cash necessary to purchase the replacement property is transferred to the seller. As of December 31, 2009, INREIT has used a portion of the proceeds to purchase a Walgreens property in Alexandria, LA. The remaining balance in the escrow will be used in 2010 to purchase another qualifying like-kind property.

NOTE 5 - NOTES RECEIVABLE

Notes receivable at December 31, 2009 and 2008 consisted of the following:

| | 2009 | 2008 |
|--------------------------|---------------------|-------------------|
| Tenant improvement notes | \$ 376,282 | \$ 424,085 |
| Minot land sale | 1,590,114 | - |
| | <u>\$ 1,966,396</u> | <u>\$ 424,085</u> |

The tenant improvement notes are for repairs which were financed by INREIT and made on commercial buildings which the tenants are responsible for paying.

(continued on next page)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The note receivable for the Minot land sale is a 7% note due in monthly installments of principal and interest amortized over a twenty-five year period and accruing interest at the rate of 7% payable on a quarterly basis. Installments of principal and interest are due once the premise achieves stabilization which is defined as having a certificate of occupancy issued and having a vacancy rate not in excess of 5%.

NOTE 6 - SECURITIES

Debt securities have been classified in the balance sheet according to management's intent. INREIT did not have any debt securities at December 31, 2009. The amortized cost and fair value of securities at December 31, 2008 were as follows:

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|---------------------------------------|---------------------|------------------------------|-------------------------------|---------------------|
| Securities held to maturity: | | | | |
| December 31, 2008 | | | | |
| U.S. Government and federal agency | \$ 866,352 | \$ - | \$ - | \$ 866,352 |
| State and municipal bonds | 400,870 | - | - | 400,870 |
| | <u>\$ 1,267,222</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ 1,267,222</u> |

The scheduled maturities of the above securities as of December 31, 2008 were as follows:

| | Amortized Cost | Fair Value |
|---------------------|---------------------|---------------------|
| Due within one year | <u>\$ 1,267,222</u> | <u>\$ 1,267,222</u> |

Proceeds from the sales of securities during the years ended December 31, 2009 and 2008 were approximately \$1,293,000 and \$913,000, respectively, resulting in no gross realized or unrealized gains or losses.

NOTE 7 - HEDGING ACTIVITIES

As part of INREIT's interest rate risk management strategy, INREIT uses a derivative instrument to minimize significant unanticipated earnings fluctuations that may arise from rising variable interest rate costs associated with existing borrowings. To meet these objectives the Company entered into an interest rate swap in the amount of \$1,293,900 to provide a fixed rate of 7.25%, which matures on April 15, 2020. The swap was issued at approximate market terms and thus no fair value adjustment was recorded at its inception. The carrying amount of the swap has been adjusted to its fair value at the end of the year, which because of changes in forecasted levels of LIBOR resulted in reporting a liability for the fair value of the future net payments forecasted under the swap. This interest rate swap is accounted for as an effective hedge in accordance with ASC 815-20 whereby it is recorded at fair value and changes in fair value are recorded to comprehensive income. As of December 31, 2009 and 2008, INREIT has recorded a liability and other comprehensive loss of \$168,332 and \$285,850, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 8 - MORTGAGE NOTES PAYABLE

Mortgage notes payable consist of:

| | 2009 | 2008 |
|---|--------------|--------------|
| 5.26% mortgage note payable, due in monthly installments of \$25,522, including interest until July 2013, secured by a mortgage on property, security agreement, and an assignment of rents (Note 17) | \$ 6,241,156 | \$ 6,364,141 |
| 6.55% mortgage note payable, due in monthly installments of \$3,869, including interest until February 2014, secured by a mortgage on property and equipment | 301,932 | 327,383 |
| 8.3% mortgage note payable, due in monthly installments of \$19,058, unpaid principal and interest due November 2010, secured by a mortgage on property and equipment | 2,305,858 | 2,338,995 |
| 7.15% mortgage note payable, due in monthly installments of \$5,439, including interest, unpaid principal and interest due March 2011, secured by a mortgage on property and a security interest in cash or investment accounts with the lender | 737,947 | 752,221 |
| 7.25% mortgage note payable, due in varying monthly installments of approximately \$9,500, including interest, unpaid principal and interest due April 2020, secured by a mortgage on property and a security interest in cash or investment accounts held with the lender (Note 8) | 1,191,772 | 1,216,608 |
| 6.35% mortgage note payable, due in monthly installments of \$7,586, including interest, unpaid principal and interest due June 2010, secured by a mortgage on property and a security interest in cash or investment accounts with the lender | 928,387 | 958,585 |
| Variable rate mortgage note payable, interest fixed at 6.25% through June 2010, thereafter adjusted every 5 years, due in monthly installments of \$15,356 until July 2025, secured by a mortgage on property and an assignment of rents | 1,836,178 | 1,903,388 |
| 5.74% mortgage note payable, due in monthly installments of \$18,945, including interest, until January 2016, secured by a mortgage on property, security agreement, and an assignment of rents | 3,082,535 | 3,129,016 |
| 6.66% mortgage note payable, due in monthly installments of \$41,114, including interest, until December 2021, secured by a mortgage on property | 5,708,690 | 5,812,757 |

(continued on next page)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

| | 2009 | 2008 |
|--|-----------|-----------|
| 5.92% mortgage note payable, due in monthly installments of \$22,291, including interest, until November 2019, secured by a mortgage on property and guaranty of owners (Note 17) | 1,201,857 | 1,219,306 |
| 5.46% mortgage note payable, due in monthly installments of \$5,842, including interest, until August 2019, secured by a mortgage on property (Note 17) | 966,647 | 983,463 |
| 7% mortgage note payable, due in monthly installments of \$35,628, including interest, until May 2022, secured by a mortgage on property (Note 17) | 5,186,346 | 5,246,425 |
| 5.93% mortgage note payable, due in monthly installments of \$45,224, including interest, until August 2017, secured by a mortgage on property and assignment of rents and leases | 7,387,593 | 7,483,000 |
| 6.65% mortgage note payable, due in monthly installments of \$9,798, including interest, until May 2014, remainder due at that time, secured by a mortgage on property | 1,357,124 | 1,382,262 |
| 5.33% mortgage note payable, due in monthly installments of \$68,688, including interest, until September 2020, secured by a mortgage on property | 6,733,795 | 7,185,975 |
| 5.96% mortgage note payable, due in monthly installments of \$20,297, including interest, until July 2021, secured by a mortgage on property, security agreement, and an assignment of rents | 3,245,330 | 3,293,895 |
| 6.67% mortgage note payable, due in monthly installments of \$21,872, including interest, until December 2013, secured by a mortgage on property, security agreement, and an assignment of rents | 2,823,017 | 2,894,572 |
| 7.18% mortgage note payable, due in monthly installments of \$16,258, including interest, until January 2013, secured by a mortgage on property, security agreement, and an assignment of rents | 1,972,666 | 2,024,107 |
| 6.3% mortgage note payable, due in monthly installments of \$4,224, including interest, until October 2017, remainder due at that time, secured by a mortgage on property and business assets | 664,466 | 672,672 |
| 6.3% mortgage note payable, due in monthly installments of \$2,032, including interest, until October 2017, remainder due at that time, secured by a mortgage on property and business assets | 319,576 | 322,992 |

(continued on next page)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

| | 2009 | 2008 |
|---|------------|------------|
| 6.1% mortgage note payable, due in monthly installments of \$13,862, including interest, until December 2017, remainder due at that time, secured by a mortgage on property and business assets | 2,230,629 | 2,259,930 |
| 6.1% mortgage note payable, due in monthly installments of \$12,680, including interest, until December 2017, remainder due at that time, secured by a mortgage on property and business assets | 2,040,477 | 2,067,280 |
| 6.59% mortgage note payable, due in monthly installments of \$2,574, including interest, until December 2012, remainder due at that time, secured by a mortgage on property | 942,865 | 959,824 |
| 6.23% mortgage note payable, due in monthly installments of \$13,642, including interest, until January 2013, remainder due at that time, secured by mortgage on property | 1,982,545 | 2,019,744 |
| 6.73% mortgage note payable, due in monthly installments of \$17,314, including interest, until December 2013, remainder due at that time, secured by mortgage on property, security agreement, and an assignment of rents | 2,224,703 | 2,280,692 |
| 5.03% mortgage note payable, due in monthly installments of \$19,122, including interest, until September 2019, remainder due at that time, secured by mortgage on property, security agreement, and an assignment of rents | 3,314,589 | 3,375,656 |
| 6.01% mortgage note payable, due in monthly payments \$8,716, including interest, unpaid principal and interest due January 2010, secured by a mortgage on property and an assignment of leases | 5,784,216 | 5,895,408 |
| 7.06% - 7.65% mortgage notes payable, due in various monthly installments of principals and interest, until March 2016, remainder due at that time, secured by mortgage on property and assignment of rents | 14,397,577 | 15,160,882 |
| 5.72% mortgage note payable, due in monthly installments of \$17,683, including interest, until January 2013, remainder due at that time, secured by mortgage on property, deed to secure debt or deed of trust | 2,715,931 | 2,771,050 |
| 5.50% mortgage note payable, due in monthly installments of \$3,735, including interest, until June 2013, remainder due at that time, secured by mortgage on property | 590,300 | 602,289 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

| | 2009 | 2008 |
|---|-----------|-----------|
| 5.98% mortgage note payable, due in monthly installments of \$11,965, including interest, until September 2017, remainder due at that time, secured by mortgage on property, deed to secure debt or deed of trust | 1,970,994 | 1,994,308 |
| 5.93% mortgage note payable, due in monthly installments of \$15,174, including interest, until September 2017, remainder due at that time, secured by mortgage on property, deed to secure debt or deed of trust | 2,512,627 | 2,542,665 |
| 6.15% mortgage note payable, due in monthly installments of \$6,862, including interest, until July 2016, remainder due at that time, secured by mortgage on property | 982,642 | 1,003,837 |
| 6.15% mortgage note payable, due in monthly installments of \$35,057, including interest, until June 2015, remainder due at that time, secured by mortgage on property and an assignment of rents | 5,601,233 | 5,670,418 |
| 6.00% mortgage note payable, due in monthly installments of \$13,084, including interest, until May 2015, remainder due at that time, secured by mortgage on property and an assignment of rents | 2,120,727 | 2,148,182 |
| 6.83% mortgage note payable, due in monthly installments of \$2,800, including interest, until June 2018, remainder due at that time, secured by mortgage on property and an assignment of rents | 398,677 | 404,451 |
| 6.83% mortgage note payable, due in monthly installments of \$12,500, including interest, until June 2018, remainder due at that time, secured by mortgage on property and an assignment of rents | 1,738,377 | 1,766,918 |
| Variable rate mortgage note payable (5.95% at December 31, 2009 and 2008), adjusted every three years, due in monthly installments of \$7,700, including interest, until April 2018, remainder due at that time, secured by mortgage on property and an assignment of rents | 1,162,062 | 1,183,648 |
| 6.83% mortgage note payable, due in monthly installments of \$5,100, including interest, until June 2018, remainder due at that time, secured by mortgage on property and an assignment of rents | 718,100 | 729,156 |
| 6.83% mortgage note payable, due in monthly installments of \$2,500, including interest, until June 2018, remainder due at that time, secured by mortgage on property and an assignment of rents | 351,218 | 356,689 |

(continued on next page)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

| | 2009 | 2008 |
|--|-----------|-----------|
| 5.6% mortgage note payable, due in monthly installments of \$12,658, including interest, until December 2012, remainder due at that time, secured by mortgage on property and an assignment of rents | 1,973,363 | 2,012,027 |
| 6.25% mortgage note payable, due in monthly installments of \$25,200, including interest, until August 2015, remainder due at that time, secured by mortgage on property and an assignment of rents | 3,707,627 | 3,771,747 |
| 5.96% mortgage note payable, due in monthly installments of \$6,727, including interest, until October 2015, remainder due at that time, secured by mortgage on property | 1,018,639 | 1,037,213 |
| 5.96% mortgage note payable, due in monthly installments of \$11,488, including interest, until October 2015, remainder due at that time, secured by mortgage on property | 1,739,517 | 1,771,240 |
| 5.96% mortgage note payable, due in monthly installments of \$5,045, including interest, until October 2015, remainder due at that time, secured by mortgage on property | 763,983 | 777,910 |
| 6.96% mortgage note payable, due in monthly installments of \$16,897, including interest, until June 2013, remainder due at that time, secured by mortgage on property, deed to secure debt or deed of trust | 2,106,383 | 2,160,479 |
| 7.8% mortgage note payable, due in monthly installments of \$12,914, including interest, until September 2014, remainder due at that time, secured by mortgage on property, deed to secure debt or deed of trust | 1,558,986 | 1,590,990 |
| Variable rate mortgage note payable (4.0% at December 31, 2009 and 2008), adjusted every three years, due in monthly installments of \$31,300, including interest, until December 2013, remainder due at that time, secured by mortgage on property and an assignment of rents | 5,754,992 | 5,900,000 |
| 5.5% mortgage note payable, due in monthly installments of \$16,024, including interest, until December 2013, remainder due at that time, secured by mortgage on property and an assignment of rents | 2,540,063 | 2,590,000 |
| 5.6% mortgage note payable, due in monthly installments of \$14,905, including interest, until December 2013, remainder due at that time, secured by mortgage on property and an assignment of rents | 2,340,404 | 2,385,000 |
| 6.96% mortgage note payable, due in monthly installments of \$24,848, including interest, until June 2013, remainder due at that time, secured by mortgage on property and an assignment of rents | 3,097,625 | 3,177,178 |

(continued on next page)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

| | 2009 | 2008 |
|---|------------|-----------|
| 6.96% mortgage note payable, due in monthly installments of \$22,198, including interest, until July 2013, remainder due at that time, secured by mortgage on property and an assignment of rents | 2,773,324 | 2,843,981 |
| 5.64% construction note payable, due in monthly installments of \$116,225, including interest, until June 2015, remainder due at that time, secured by mortgage on property and an assignment of the executed lease | 15,993,433 | 809,003 |
| 5.96% mortgage note payable, due in monthly installments of \$5,955, including interest, until January 2016, remainder due at that time, secured by mortgage on property and an assignment of rents | 904,823 | - |
| 5.5% mortgage note payable, due in monthly installments of \$7,492, including interest, until July 2014, remainder due at that time, secured by mortgage on property and an assignment of rents | 1,210,605 | - |
| 5.4% mortgage note payable, due in monthly installments of \$34,815, including interest, until April 2015, remainder due at that time, secured by mortgage on property and an assignment of rents | 5,977,338 | - |
| 5.75% mortgage note payable, due in monthly installments of \$8,551, including interest, until May 2019, remainder due at that time, secured by mortgage on property and an assignment of rents | 1,344,250 | - |
| 5.75% mortgage note payable, due in monthly installments of \$12,742, including interest, until March 2014, remainder due at that time, secured by mortgage on property and corporate guaranty | 1,766,080 | - |
| 5.75% mortgage note payable, due in monthly installments of \$7,545, including interest, until May 2019, remainder due at that time, secured by mortgage on property and an assignment of rents | 1,186,103 | - |
| 5.68% mortgage note payable, due in monthly installments of \$63,989, including interest, until October 2015, remainder due at that time, secured by mortgage on property, security agreement, and assignment of rents and leases | 10,307,428 | - |
| 5.69% mortgage note payable, due in monthly installments of \$20,960, including interest, until April 2025 remainder due at that time, secured by mortgage on property, security agreement and assignment of rents and leases | 2,569,193 | - |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

| | <u>2009</u> | <u>2008</u> |
|---|------------------------------|------------------------------|
| 6.85% mortgage note payable, due in monthly installments of \$49,216, including interest, until March 2034 remainder due at that time, secured by mortgage on property, security agreement and assignment of rents and leases | 6,976,561 | - |
| 6.85% mortgage note payable, due in monthly installments of \$38,325, including interest, until August 2033, remainder due at that time, secured by mortgage on property, security agreement and assignment of rents and leases | 5,380,629 | - |
| | <u>\$ 190,964,710</u> | <u>\$ 141,531,558</u> |

The mortgage notes agreements include covenants that, in part, impose maintenance of certain debt service coverage and debt to worth ratios.

Long-term debt maturities are as follows:

| <u>Years ending December 31,</u> | <u>Amount</u> |
|----------------------------------|------------------------------|
| 2010 | \$ 13,654,960 |
| 2011 | 5,644,821 |
| 2012 | 9,862,364 |
| 2013 | 36,975,400 |
| 2014 | 10,210,464 |
| Thereafter | <u>114,616,701</u> |
| | <u>\$ 190,964,710</u> |

NOTE 9 - INVESTMENT CERTIFICATES

INREIT periodically issues investment certificates bearing various interest rates in exchange for cash. The interest rate depends upon the maturity of the investment certificate. During 2009, INREIT issued investment certificates ranging from 4 to 5.75 percent totaling \$333,240. During 2008, INREIT issued investment certificates ranging from 4.5 to 7 percent totaling \$190,798. At December 31, 2009 and 2008, INREIT had outstanding investment certificates totaling \$468,078 and \$378,037, respectively.

Maturities of investment certificates are as follows: 2010 - \$252,195; 2011 - \$81,837; 2012 - \$85,600; 2013 - \$0; 2014 - \$48,446.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 10 - FAIR VALUE MEASUREMENT

In September 2006 the FASB issued ASC 820-10 and in February 2007 issued ASC 825-10. Both standards address the aspects of the expanding application of fair value accounting. Effective January 1, 2008, INREIT adopted ASC 820-10 and ASC 825-10. There were no adjustments to accumulated deficit as a result of the adoption of ASC 820-10. ASC 825-10 permits a company to measure certain financial assets and financial liabilities at fair value that were not previously required to be measured at fair value. INREIT has elected not to measure any financial assets or financial liabilities at fair value which were not previously required to be measured at fair value.

ASC 820-10 established a three-level valuation hierarchy for fair value measurement. Management uses these valuation techniques to establish the fair value of the assets at the measurement date. These valuation techniques are based upon observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect management's assumptions. These two types of inputs create the following fair value hierarchy:

- Level 1 – Quoted prices for identical instruments in active markets;
- Level 2 – Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose significant inputs are observable;
- Level 3 – Instruments whose significant inputs are unobservable.

Assets measured at fair value on a recurring basis in accordance with ASC 820-10:

| Liabilities | Total 12/31/09 | Quoted Prices: Level 1 | Significant Other Inputs: Level 2 | Significant Nonobservable Inputs: Level 3 |
|----------------------------------|---------------------------|---------------------------------------|--|--|
| Fair value of interest rate swap | \$ 168,332 | \$ - | \$ 168,332 | \$ - |
| Assets | Total 12/31/08 | Quoted Prices: Level 1 | Significant Other Inputs: Level 2 | Significant Nonobservable Inputs: Level 3 |
| Fair value of interest rate swap | \$ 285,850 | \$ - | \$ 285,850 | \$ - |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 11 - SPECIAL ASSEMENTS PAYABLE

At December 31, 2009 and 2008, special assessments payable totaled \$1,565,683 and \$1,535,100, respectively. Future principal payments related to special assessments payable over the next five years are as follows:

| <u>Years ending December 31,</u> | <u>Amount</u> |
|----------------------------------|---------------------|
| 2010 | \$ 201,683 |
| 2011 | 197,611 |
| 2012 | 180,379 |
| 2013 | 147,428 |
| 2014 | 118,036 |
| Thereafter | 720,546 |
| | <u>\$ 1,565,683</u> |

NOTE 12 - ACCRUED EXPENSES

| | <u>2009</u> | <u>2008</u> |
|-------------------|---------------------|---------------------|
| Real estate taxes | \$ 1,743,802 | \$ 1,724,018 |
| Interest | 816,230 | 583,971 |
| Unearned rent | 91,991 | 74,906 |
| Other | 2,110 | 2,407 |
| | <u>\$ 2,654,133</u> | <u>\$ 2,385,302</u> |

NOTE 13 - MINORITY INTEREST OF UNITHOLDERS IN OPERATING PARTNERSHIPS

As of December 31, 2009 and 2008, minority shareholders partnership units totaled 9,883,009 and 9,662,068, respectively. During 2009 and 2008, INREIT paid distributions of \$6,973,361 and \$4,171,835, respectively, to minority interest shareholders. As of December 31, 2009 and 2008, INREIT had declared distributions of \$1,840,711 and \$1,548,231, respectively, to minority shareholders to be paid the following year.

During 2009 and 2008, minority shareholders converted 212,466 and 47,978 partnership units to INREIT shares, totaling \$2,461,120 and \$580,499, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 14 - RELATED PARTY TRANSACTIONS

Due from related party as of December 31, 2009 and 2008 is as follows:

| | <u>2009</u> | <u>2008</u> |
|------------------------------------|-------------------|-------------------|
| Goldmark Property Management | \$ 127,914 | \$ 151,557 |
| Edgewood Vista Senior Living, Inc. | <u>751,088</u> | <u>292,802</u> |
| | <u>\$ 879,002</u> | <u>\$ 444,359</u> |

Due to related party as of December 31, 2009 and 2008 is as follows:

| | <u>2009</u> | <u>2008</u> |
|------------------------|------------------|---------------------|
| DL/JKJD, LLC | \$ - | \$ 656,245 |
| INREIT Management, LLC | 54,859 | 594,122 |
| HSC Partner, LLC | <u>5,576</u> | <u>350,539</u> |
| | <u>\$ 60,435</u> | <u>\$ 1,600,906</u> |

Property Management Fees

During 2009 and 2008, INREIT paid property management fees of 5 percent of rents to INREIT Management, LLC. The management team of INREIT Management, LLC consists of Board of Trustee members Kenneth Regan and James Wieland. For the years ended December 31, 2009 and 2008, INREIT paid management fees of \$18,540 and \$18,022, respectively, to INREIT Management, LLC.

During 2009 and 2008, INREIT paid property management fees of 5 percent of rents to Goldmark Property Management. The management team of Goldmark Property Management consists of Board of Trustee members Kenneth Regan and James Wieland. For the years ended December 31, 2009 and 2008, INREIT incurred management fees of \$3,048,048 and \$1,690,001, respectively, to Goldmark Property Management.

Director Fees

INREIT paid director fees of \$38,300 and \$37,650 in 2009 and 2008, respectively.

Advisory Management Fees

During 2009 and 2008, INREIT incurred \$649,824 and \$610,686 to INREIT Management, LLC for advisory management fees. As of December 31, 2009 and 2008, the Company owed INREIT Management, LLC \$54,859 and \$65,822, respectively, for unpaid advisory management fees. These fees cover the office facilities, equipment, supplies, and staff required to manage the day-to-day operations of INREIT, and is paid based on .50% of net invested assets during 2009 and .75% of net invested assets during 2008 from these facilities (Note 19).

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Acquisition Fees

During 2009 and 2008, INREIT incurred \$1,355,848 and \$3,283,900, respectively, to INREIT Management, LLC for acquisition fees. These fees are for performing due diligence on properties acquired in an I.R.C Section 721 exchange, and are paid on 3% of the purchase price up to a maximum of \$300,000 per individual property in 2009 and \$150,000 per individual property in 2008 (Note 19). As of December 31, 2008, INREIT owed \$528,300 to INREIT Management, LLC for acquisition fees.

Commissions

During 2009 and 2008, INREIT incurred brokerage fees of \$114,378 and \$455,203, respectively, to Roger Domres, or entities owned by Roger Domres, stockholder of INREIT and a shareholder of INREIT Management, LLC. Brokerage fees are paid based on 4% of UPREIT units and 8% of INREIT units sold. During 2009 and 2008, INREIT incurred marketing fees of \$67,648 and \$591,090, respectively, to HSC Partner, LLC, an entity owned by Roger Domres. As of December 31, 2009 and 2008, INREIT owed \$5,576 and \$350,539, respectively, to HSC Partner, LLC for brokerage and marketing fees.

During 2009 and 2008, INREIT incurred brokerage fees of \$283,240 and \$1,788,081 to Dale Lian, or entities owned by Dale Lian, stockholder of INREIT and a shareholder of INREIT Management, LLC. Brokerage fees are paid based on 4% of UPREIT units and 8% of INREIT units sold. As of December 31, 2009, INREIT did not owe any brokerage fees to Dale Lian, or entities owned by Dale Lian. As of December 31, 2008, INREIT owed \$656,245 to Dale Lian, or entities owned by Dale Lian, for brokerage fees.

During 2009, INREIT incurred commission fees of \$272,641 to Goldmark Schlossman Commercial Real Estate Services Inc., which consists of Board of Trustee members Kenneth Regan and James Wieland.

Rental Income

During 2009 and 2008, INREIT received rental income of \$1,123,946 and \$706,893, respectively, under various lease agreements with Edgewood Vista Senior Living, Inc., an entity affiliated with Philip Gisi, a member of the Board of Trustees. As of December 31, 2009, INREIT was owed \$419,192 from Edgewood Vista Senior Living, Inc. for rental income. As of December 31, 2009 and 2008, INREIT was owed \$284,673 and \$157,806, respectively, from Edgewood Vista Senior Living, Inc. for real estate taxes related to the properties.

During 2009 and 2008, INREIT received rental income of \$158,489 and \$155,885, respectively, under an operating lease agreement with Goldmark Property Management.

As of December 31, 2008, INREIT was owed \$54,794 from Goldmark Property Management for rent collected during 2008 which was not paid to INREIT.

Rent Incentive

During 2009, INREIT provided a rent incentive of \$1,500,000 to a property owned by Edgewood Development Group, an entity affiliated with Philip Gisi. The rent incentive is being amortized against rental income over the term of the lease. During 2009, INREIT amortized \$16,667 against income.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

CAM Income Receivable

As of December 31, 2009, INREIT was owed \$47,222 from Edgewood Vista Senior Living, Inc. for insurance payments made by INREIT.

Interest Receivable

As of December 31, 2008, INREIT was owed \$134,996 from Edgewood Vista Senior Living, Inc. for rental interest related to the construction of the Edgewood Vista Senior Living Center. The rental interest is based on INREIT's equity in the construction of the complex.

Insurance Proceeds

As of December 31, 2008, INREIT was owed \$138,480 from Goldmark Property Management for insurance proceeds related to damages sustained to a residential complex.

Restricted Deposits

As of December 31, 2009 and 2008, INREIT owed \$47,939 and \$41,717, respectively, to Goldmark Property Management for security deposits maintained by INREIT, which were owed to Goldmark Property Management.

Investment Certificates

During 2008, Dale Lian purchased an investment certificate from INREIT totaling \$100,000. The certificate was outstanding as of December 31, 2008. The certificate accrued interest at 4.5% and matured in April 2009.

Construction Costs / Development Fees

During 2009 and 2008, INREIT incurred construction costs and development fees of \$2,194,519 and \$1,536,838, respectively, to Edgewood Development Group. As of December 31, 2008, INREIT owed \$201,543 to Edgewood Development Group for developer fees.

During 2009, INREIT incurred construction costs of \$1,638,850 to Goldmark Property Management.

Purchases

During 2009, INREIT purchased a 102,448 square foot commercial office building in Edina, Minnesota, from an entity affiliated with James Echtenkamp, a related party. The approximate purchase price of the building was \$13,100,000.

During 2009, INREIT purchased a 24 unit apartment building in Fargo, North Dakota, from an entity affiliated with James Wieland, a related party. The approximate purchase price of the building was \$750,000.

During 2008, INREIT purchased an 80 unit apartment complex in Fargo, North Dakota, from an entity affiliated with James Wieland, a related party. The approximate purchase price of the complex was \$2,723,000.

During 2008, INREIT purchased a 12 unit apartment building in Grand Forks, North Dakota, from an entity affiliated with Dale Lian. The approximate purchase price of the building was \$741,000.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

During 2008, INREIT purchased a 12 unit apartment building in Fargo, North Dakota, from an entity affiliated with Kenneth Regan and Dale Lian; related parties. The approximate purchase price of the building was \$450,000.

During 2008, INREIT purchased 15 apartment complexes from various entities affiliated with Kenneth Regan and James Wieland. The approximate purchase price of the complexes was \$43,179,000.

During 2008, INREIT purchased two apartment complexes from various entities affiliated with Kenneth Regan, James Wieland, and Dale Lian. The approximate purchase price of the complexes was \$8,995,000.

During 2008, INREIT purchased six apartment complexes from various entities affiliated with Kenneth Regan, James Wieland, Dale Lian, and James Echtenkamp; related parties. The approximate purchase price of the complexes was \$16,217,000.

Sales

During 2008, INREIT sold four, 12 unit assisted living facilities in Grand Island, Nebraska; Norfolk, Nebraska; Columbus, Nebraska; and Belgrade, Montana. The facilities were sold to an entity affiliated with Philip Gisi. The sales price of the facilities totaled approximately \$4,610,000.

NOTE 15 - RENTALS UNDER OPERATING LEASES / RENTAL INCOME

Commercial space is rented under long-term lease agreements. Minimum future rentals on noncancelable operating leases as of December 31 are as follows:

| <u>Years ending December 31,</u> | <u>Amount</u> |
|----------------------------------|-----------------------|
| 2009 | \$ 13,268,893 |
| 2010 | 12,584,463 |
| 2011 | 11,548,513 |
| 2012 | 11,219,410 |
| 2013 | 10,869,718 |
| Thereafter | <u>59,538,042</u> |
| | <u>\$ 119,029,039</u> |

Residential apartment units are rented to individual tenants with lease terms up to one year. Gross revenues from residential rentals totaled \$23,956,098 and \$13,578,743 for the years ended December 31, 2009 and 2008, respectively.

For the years ended December 31, 2009 and 2008, gross revenues from commercial property rentals, including CAM (common area maintenance) income of \$3,728,311 and \$3,368,908, respectively, totaled \$14,238,572 and \$12,161,908. Commercial properties are leased to tenants under terms expiring at various dates through 2023. Lease terms often include renewal options.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 16 - PROPERTY MANAGEMENT FEES

INREIT has entered into various management agreements with unrelated management companies. The agreements provide for INREIT to pay management fees based on a percentage of rental income (5%). During 2009 and 2008, INREIT incurred property management fees of \$187,617 and \$189,145, respectively, to unrelated management companies.

During 2009 and 2008, INREIT incurred management fees of 5% of rents to INREIT Management, LLC; and Goldmark Property Management, a related party (Note 14).

NOTE 17 - COMMITMENTS AND CONTINGENCIES

Environmental Matters

Federal law (and the laws of some states in which INREIT may acquire properties) imposes liability on a landowner for the presence on the premises of hazardous substances or wastes (as defined by present and future federal and state laws and regulations). This liability is without regard to fault or knowledge of the presence of such substances and may be imposed jointly and severally upon all succeeding landowners. If such hazardous substance is discovered on a property acquired by INREIT, INREIT could incur liability for the removal of the substances and the cleanup of the property. There can be no assurance that INREIT would have effective remedies against prior owners of the property. In addition, INREIT may be liable to tenants and may find it difficult or impossible to sell the property either prior to or following such a cleanup.

Risk of Uninsured Property Losses

INREIT maintains property damage, fire loss, and liability insurance. However, there are certain types of losses (generally of a catastrophic nature), which may be either uninsurable or not economically insurable. Such excluded risks may include war, earthquakes, tornados, certain environmental hazards, and floods. Should such events occur, (i) the INREIT might suffer a loss of capital invested, (ii) tenants may suffer losses and may be unable to pay rent for the spaces, and (iii) the trust may suffer a loss of profits which might be anticipated from one or more properties.

Construction in Progress

As of December 31, 2009, construction was in progress on Sunset Ridge, residential real estate in Bismarck, North Dakota. As of December 31, 2009, INREIT had incurred costs of \$1,638,850 relating to the construction of the project. The project is expected to be completed in 2010 at a cost of approximately \$4,725,000. As of December 31, 2009, INREIT owed \$332,116 for construction costs.

Tenant in Common Ownership

As a tenant in common, INREIT owns their respective share of the assets of the properties as well as being liable for their respective share of the debts. INREIT owned the following properties as a tenant in common.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

INREIT Properties, LLLP is the 100% owner of Grand Forks Inreit, LLC, which owns a 1/3 interest as a tenant in common of Grand Forks Marketplace Retail Center. INREIT Properties, LLLP is also the 50% owner of Marketplace Investors, LLC, which owns a 1/3 interest as a tenant in common of Grand Forks Marketplace Retail Center. Grand Forks Marketplace Retail Center has approximately 183,000 square feet of commercial space in Grand Forks, North Dakota. The property is encumbered by a non-recourse first mortgage with Key Bank Real Estate Capital with a balance at December 31, 2009 of \$12,482,312. As of December 31, 2009, INREIT owed \$6,241,156 for their respective share of the balance.

INREIT Properties, LLLP owns a 2/3 interest as a tenant in common of a commercial building with approximately 75,000 square feet of rental space in Fargo, North Dakota. The property is encumbered by a first mortgage with GE Commercial Finance Business Property Corporation with a balance at December 31, 2009 in the amount of \$7,779,519. As of December 31, 2009, INREIT owed \$5,186,346 for its respective share of the balance. INREIT along with the other tenant in common is jointly liable for the entire balance.

INREIT Properties, LLLP owns a 1/3 interest as a tenant in common of a 136 unit apartment complex located in Bismarck, North Dakota. The property is encumbered by Phase I and Phase II first mortgages with NorthMarq Capital with a balance at December 31, 2009 in the amount of \$2,899,941 and \$3,605,571, respectively. As of December 31, 2009, INREIT owed \$966,647 and \$1,201,857, respectively, for its share of the balances. INREIT along with the other tenant in common is jointly liable for the entire balance.

NOTE 18 - OTHER COMPREHENSIVE LOSS

The details related to other comprehensive loss are as follows:

| | <u>2009</u> | <u>2008</u> |
|---|----------------------------|--------------------------|
| Net income | <u>\$ 6,633,464</u> | <u>\$ 4,042,793</u> |
| Other comprehensive loss | | |
| Increase (decrease) in fair value of interest rate swap | <u>117,518</u> | <u>(285,850)</u> |
| Total other comprehensive loss | <u>117,518</u> | <u>(285,850)</u> |
| Comprehensive income | <u>6,750,982</u> | <u>3,756,943</u> |
| Comprehensive income attributable to the noncontrolling interest | <u>5,062,285</u> | <u>2,779,592</u> |
| Comprehensive income attributable to INREIT Real Estate Investment Trust | <u><u>\$ 1,688,697</u></u> | <u><u>\$ 977,351</u></u> |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 19 - SUBSEQUENT EVENTS

Subsequent to year-end, INREIT declared a dividend of \$0.1925 per share to shareholders of record as of March 31, 2010, to be payable in April 2010.

Subsequent to year-end, INREIT entered into a purchase agreement to acquire three commercial properties in Minnesota for \$6,145,000.

Subsequent to year-end, INREIT entered into a purchase agreement to acquire a commercial property in Laurel, Mississippi for \$3,901,500.

Subsequent to year-end, INREIT purchased an apartment complex in Hawley, Minnesota through a 721 exchange. The acquisition price of the complex was \$425,000.

Subsequent to year-end, INREIT, sold an apartment complex in Carrington, ND at a price of \$710,000.

INREIT has evaluated subsequent events through March 3, 2010, the date which the financial statements were issued.





Stony Brook

APARTMENTS & TOWNHOMES

INREIT

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