ALFACELL CORP
Form 10-Q
March 13, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

|X| QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended: January 31, 2006

|_| TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ______________________ to ______________________

Commission File Number: 0-11088

ALFACELL CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	22-2369085
(State or other jurisdiction of organization)	(I.R.S. Employer Identification No.)

225 Belleville Avenue, Bloomfield, New Jersey 07003
(Address of principal executive offices) (Zip Code)

(973) 748-8082
(Registrant's telephone number, including area code)

NOT APPLICABLE
(Former name, former address, and former fiscal year, if changed since last report.)

Indicate by check mark whether the registrant has (1) filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes |X| No |_|

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer |_| Accelerated Filer |X| Non-accelerated Filer |_|

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes |_| No |X|

The number of shares of common stock, $.001 par value, outstanding as of March 8, 2005 was 37,390,062 shares.

ALFACELL CORPORATION
(A Development Stage Company)

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

CONDENSED BALANCE SHEETS
January 31, 2006 and July 31, 2005

	January 2006 (Unaudit
ASSETS	
Current assets:	
Cash and cash equivalents	$ 2,917
Other current assets	80
Total current assets	2,997
Property and equipment, net	75
Loan receivable, related party	166
Total assets	$ 3,238
LIABILITIES AND STOCKHOLDERS' EQUITY	
Current liabilities:	
Accounts payable	$ 833
Accrued expenses	1,553
Total liabilities	2,386
Commitments and contingencies	
Stockholders' equity:	
Preferred stock, $.001 par value; Authorized and unissued, 1,000,000 shares at January 31, 2006 and July 31, 2005	
Common stock, $.001 par value; Authorized 100,000,000 shares at January 31, 2006 and July 31, 2005; Issued and outstanding, 37,103,095 shares at January 31, 2006 and 36,534,235 shares at July 31, 2005	37
Capital in excess of par value	80,006
Deficit accumulated during development stage	(79,192
Total stockholders' equity	851
Total liabilities and stockholders' equity	$ 3,238

See accompanying notes to condensed financial statements.

ALFACELL CORPORATION
(A Development Stage Company)

CONDENSED STATEMENTS OF OPERATIONS

Three and six months ended January 31, 2006 and 2005,
and the Period from August 24, 1981
(Date of Inception) to January 31, 2006

(Unaudited)

	Three Months Ended January 31,		Six Months Ended January 31,	
	2006	2005	2006	200
Revenue:				
Sales	$ --	$ --	$ --	$
Investment income	24,053	33,704	56,048	6
Other income	--	--	--	
Total revenue	24,053	33,704	56,048	6
Costs and expenses:				
Cost of sales	--	--	--	
Research and development	1,430,041	1,554,443	2,589,431	2,47
General and administrative	879,914	422,406	1,469,724	86
Interest:				
Related parties, net	--	--	--	
Others	10	12,165	20	4
Total costs and expenses	2,309,965	1,989,014	4,059,175	3,38
Loss before state tax benefit	(2,285,912)	(1,955,310)	(4,003,127)	(3,32
State tax benefit	--	--	317,382	28
Net loss	$ (2,285,912)	$ (1,955,310)	$ (3,685,745)	$ (3,03
Loss per basic and diluted common share	$ (0.06)	$ (0.06)	$ (0.10)	$
Weighted average number of shares outstanding	36,734,042	35,211,954	36,663,531	34,93

See accompanying notes to condensed financial statements.

ALFACELL CORPORATION
(A Development Stage Company)

CONDENSED STATEMENTS OF CASH FLOWS

Six months ended January 31, 2006 and 2005,
and the Period from August 24, 1981
(Date of Inception) to January 31, 2006

(Unaudited)

	Six Months Ended January 31,		(D
	2006	2005	J
Cash flows from operating activities:			
Net loss	$ (3,685,745)	$ (3,036,160)	
Adjustments to reconcile net loss to net cash used in operating activities:			
Gain on sale of marketable securities	--	--	
Depreciation and amortization	13,892	14,220	
Loss on disposal of property and equipment	--	--	
Issuance of common stock, stock options and warrants for services rendered	644,330	13,500	
Amortization of debt discount	--	30,061	
Amortization of deferred compensation	--	--	
Amortization of organization costs	--	--	
Changes in assets and liabilities:			
Decrease (increase) in other current assets	116,900	(163,349)	
Increase in loan receivable-related party	(4,764)	(4,797)	
Increase in interest payable-related party	--	--	
Increase in accounts payable	437,239	118,148	
Increase in accrued payroll and expenses, related parties	--	--	
Increase in accrued expenses	269,361	293,544	
Net cash used in operating activities	(2,208,787)	(2,734,833)	
Cash flows from investing activities:			
Purchase of marketable equity securities	--	--	
Purchase of short-term investments	--	(1,978,189)	
Proceeds from sale of marketable equity securities	--	--	
Purchase of property and equipment	(8,503)	(41,153)	
Patent costs	--	--	
Net cash used in investing activities	(8,503)	(2,019,342)	

(continued)

See accompanying notes to condensed financial statements.

ALFACELL CORPORATION
(A Development Stage Company)

CONDENSED STATEMENTS OF CASH FLOWS, Continued

Six months ended January 31, 2006 and 2005
and the Period from August 24, 1981
(Date of Inception) to January 31, 2006

(Unaudited)

	Six Months Ended January 31,	
	2006	20
Cash flows from financing activities:		
Proceeds from short-term borrowings	$ --	$
Payment of short-term borrowings	--	
Increase in loans payable - related party, net	--	
Proceeds from bank debt and other long-term debt, net of costs	--	
Reduction of bank debt and long-term debt	--	
Proceeds from issuance of common stock, net	--	
Proceeds from exercise of stock options and warrants, net	671,485	2
Proceeds from issuance of convertible debentures, related party	--	
Proceeds from issuance of convertible debentures, unrelated party	--	
Net cash provided by financing activities	671,485	2
Net increase (decrease) in cash and cash equivalents	(1,545,805)	(4,5
Cash and cash equivalents at beginning of period	4,462,951	10,1
Cash and cash equivalents at end of period	$ 2,917,146	$ 5,6
Supplemental disclosure of cash flow information - interest paid	$ 20	$
Noncash financing activities:		
Issuance of convertible subordinated debenture for loan payable to officer	$ --	$
Issuance of common stock upon the conversion of convertible subordinated debentures, related party	$ --	$
Conversion of short-term borrowings to common stock	$ --	$
Conversion of accrued interest, payroll and expenses by related parties to stock options	$ --	$
Repurchase of stock options from related party	$ --	$
Conversion of accrued interest to stock options	$ --	$
Conversion of accounts payable to common stock	$ --	$
Conversion of notes payable, bank and accrued interest		

to long-term debt	$ --	$
Conversion of loans and interest payable, related party and accrued payroll and expenses, related parties to long-term accrued payroll and other, related party	$ --	$
Issuance of common stock upon the conversion of convertible subordinated debentures, other	$ --	$ 2
Issuance of common stock for services rendered	$ --	$
Issuance of warrants with notes payable	$ --	$

See accompanying notes to condensed financial statements.

ALFACELL CORPORATION
(A Development Stage Company)

NOTES TO CONDENSED FINANCIAL STATEMENTS

(Unaudited)

1. ORGANIZATION AND BASIS OF PRESENTATION

In the opinion of management, the accompanying unaudited condensed financial statements contain all adjustments (consisting of normal recurring adjustments) necessary to present fairly the Company's financial position as of January 31, 2006 and its results of operations and cash flows for the three and six month periods ended January 31, 2006 and 2005 and the period from August 24, 1981 (date of inception) to January 31, 2006. The results of operations for the three and six months ended January 31, 2006 are not necessarily indicative of the results to be expected for the full year. The condensed balance sheet as of July 31, 2005 presented herein has been derived from the audited financial statements included in the Form 10-K for the fiscal year ended July 31, 2005, filed with the Securities and Exchange Commission.

Certain footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been omitted in accordance with the published rules and regulations of the Securities and Exchange Commission. The condensed financial statements in this report should be read in conjunction with the financial statements and notes thereto included in the Form 10-K for the fiscal year ended July 31, 2005.

The Company is a development stage company as defined in Statement of Financial Accounting Standards No. 7. The Company is devoting substantially all of its present efforts to developing new drug products. Its planned principal operations have not commenced and, accordingly, no significant revenue has been derived therefrom.

The Company has reported net losses of approximately $6,462,000, $5,070,000 and $2,411,000 for the fiscal years ended July 31, 2005, 2004 and 2003, respectively. The loss from date of inception, August 24, 1981, to January 31, 2006 amounts to approximately $79,192,000.

The Company's long-term continued operations will depend on its ability to raise additional funds through various potential sources such as equity and debt financing, collaborative agreements, strategic alliances, sale of tax benefits, revenues from the commercial sale of ONCONASE(R), licensing of its proprietary RNase technology and its ability to realize revenues from its technology and its drug candidates via out-licensing agreements with other companies. Such additional funds may not become available as the Company may need them or may not be available on acceptable terms. Through January 31, 2006, a significant portion of the Company's financing has been through the sale of its equity securities and convertible debentures in registered offerings and private placements and the exercise of stock options and warrants. Additionally, the Company has raised capital through debt financings, the sale of tax benefits and research products, interest income and financing received from its Chief Executive Officer. Until and unless the Company's operations generate significant revenues, the Company expects to continue to fund operations from the sources of capital previously described. There can be no assurance that the Company will be able to raise the capital it needs on terms which are acceptable, if at all. As of January 31, 2006, management believes that the Company's cash

1. ORGANIZATION AND BASIS OF PRESENTATION, Continued

balance is sufficient to fund its operations through July 31, 2006, based on its expected level of expenditures in relation to activities in preparing ONCONASE(R) for marketing registrations in the U.S. and Europe and other ongoing operations of the Company. However, to assure the Company's ability to continue its operations beyond this date, the Company continues to seek additional financing through equity or debt financings and the sale of net operating loss carryforwards, but cannot be sure that it will be able to raise capital on favorable terms or at all. The Company may also obtain additional capital through the exercise of outstanding options and warrants, although it cannot provide any assurance of such exercises or estimate the amount of capital it will receive, if any. If the Company is unable to raise additional funds in the future on acceptable terms, or at all, its operations will be severely curtailed and its business and financial condition will be adversely affected.

The Company will continue to incur costs in conjunction with its U.S. and foreign registrations for marketing approval of ONCONASE(R). The Company is currently in discussions with potential strategic alliance partners to further the development and marketing of ONCONASE(R) and other related products in its pipeline. However, it cannot be sure that any such alliances will materialize.

2. EARNINGS (LOSS) PER COMMON SHARE

"Basic" earnings (loss) per common share equals net income (loss) divided by weighted average common shares outstanding during the period. "Diluted" earnings per common share equals net income divided by the sum of weighted average common shares outstanding during the period, adjusted for the effects of potentially dilutive securities. The Company's basic and diluted per share amounts are the same since the Company is in a loss position and the assumed exercise of stock options and warrants prior to January 31, 2006 would be anti-dilutive. The number of outstanding options and warrants that could dilute earnings per share in future periods was 16,199,993 and 15,208,029 at January 31, 2006 and 2005, respectively.

3. STOCK-BASED COMPENSATION

Statement of Financial Accounting Standards No. 123, Accounting for Stock-Based Compensation ("SFAS 123"), provides for the use of a fair value-based method of accounting for employee stock compensation. However, SFAS 123 also allowed an entity to continue to measure compensation cost for stock options granted to employees and directors using the intrinsic value method of accounting prescribed by Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees ("APB 25"), which only required charges to compensation expense for the excess, if any, of the fair value of the underlying stock at the date a stock option was granted (or at an appropriate subsequent measurement date) over the amount the employee had to pay to acquire the stock, if such amounts differed materially from the historical amounts. Prior to August 1, 2005, the Company had elected to continue to account for employee stock options using the intrinsic value method under APB 25. As the exercise price of all options granted under the stock option plans was equal to the market value of the underlying common stock on the grant date, no stock-based employee compensation cost had been recognized in the condensed statement of operations for the three and six months ended January 31, 2005.

3. STOCK-BASED COMPENSATION, Continued

In December 2004, the Financial Accounting Standards Board issued SFAS No. 123(R) (revised 2004), "Share-Based Payment" ("SFAS 123(R)"), which amends SFAS 123. The new standard requires all share-based payments, including stock option grants to employees, to be recognized as an operating expense in the statement of operations. The cost is recognized over the requisite service period based on fair values measured on the date of grant. The Company adopted SFAS 123(R) effective August 1, 2005 using the modified prospective method and accordingly, prior period amounts have not been restated. Under the modified prospective method, the fair value of all new stock options issued after July 31, 2005 and unvested outstanding stock options at August 1, 2005 will be recognized as expense as services are rendered. The Company recorded $305,441 or $0.01 per basic and diluted common share and $514,026 or $.01 per basic and diluted common share of stock-based compensation expense for employees under SFAS 123R for the three and six month periods ended January 31, 2006, respectively. Had the Company accounted for its stock-based awards under the fair value method for the three and six months ended January 31, 2005 the impact to its financial statements would have been as follows:

	Three Months Ended January 31,	Six Months Ended January 31,
	2005	2005

Net loss applicable to common shares		
As reported	$(1,955,310)	$(3,036,160)
Less total stock-based employee compensation expense determined under fair value method for all awards, net of related tax effects	(604,671)	(1,223,942)
Pro forma	$(2,559,981)	$(4,260,102)
Basic and diluted loss per common share		
As reported	$ (0.06)	$ (0.09)
Pro forma	(0.07)	(0.12)

For options granted during the six months ended January 31, 2006, the weighted-average fair value at the grant date was $1.27 per option and the weighted average exercise price was $1.69 per option. The fair value of the stock options was estimated using the Black-Scholes options pricing model based on the following weighted-average assumptions:

	Six Months Ended January 31, 2006	2005
Expected dividend yield	0%	0%
Risk-free interest rate	4.47%	4.25%
Expected stock price volatility	84.79%	100%
Expected term until exercise (years)	5.86	8.67
Forfeiture rate	36.61%	N/A

8

ALFACELL CORPORATION
(A Development Stage Company)

NOTES TO CONDENSED FINANCIAL STATEMENTS, Continued

(Unaudited)

3. STOCK-BASED COMPENSATION, Continued

The total intrinsic value of options exercised by employees during the six months ended January 31, 2006 was $120,894. As of January 31, 2006, there was approximately $2,319,000 of total unrecognized compensation cost related to unvested share-based compensation arrangements granted under the Company's stock option plans, which is to be recognized over a weighted average period of 1.62 years.

Shares, warrants and options issued to non-employees for services are accounted for in accordance with SFAS 123(R) and Emerging Issues Task Force ("EITF") Issue No. 96-18, Accounting for Equity Instruments that are Issued to Other Than Employees for Acquiring or In Conjunction with Selling Goods or Services. Such securities are recorded in expense and additional paid-in capital in stockholders' equity (deficiency) over the applicable service periods using variable accounting through the vesting date based on the fair value of the securities at the end of each period.

4. LOAN RECEIVABLE, RELATED PARTY

Amounts due from the Company's CEO totaling $166,106 at January 31, 2006 and $161,342 at July 31, 2005, are classified as a long-term asset in loan receivable, related party as the Company does not expect repayment of these amounts within one year. In each of the six months ended January 31, 2006 and 2005, the Company earned 8% interest in the amount of approximately $4,800 on the unpaid principal balance.

5. CAPITAL STOCK

During the quarter ended October 31, 2005, the Company issued an aggregate of 132,082 shares of common stock upon the exercise of warrants and stock options by an unrelated party, an employee and an executive officer at per share exercise prices ranging from $0.54 to $0.85. The Company realized aggregate gross proceeds of $96,738 from these exercises.

During the quarter ended January 31, 2006, the Company issued an aggregate of 436,778 shares of common stock upon the exercise of warrants and stock options by unrelated parties, employees and directors at per share exercise prices ranging from $0.26 to $1.50. The Company realized aggregate gross proceeds of $574,747 from these exercises.

During the quarter ended January 31, 2006, the Company issued 25,000 ten-year stock options to a consultant as payment for services rendered. The options vested immediately and have an exercise price of $1.32 per share. The Company recorded a total of $23,166 of non-cash expense for these options.

During the quarter ended January 31, 2006, the Company issued 50,000 five-year stock options to a consultant as payment for services to be rendered. These options vest over a one year period, 50% of which vested immediately and 12.5% will vest equally for the next four quarters following the grant date. The stock options have an exercise price of $2.04 per share. The fair value of these options

5. CAPITAL STOCK, Continued

is being expensed over the service period using the provisions of EITF 96-18. During the six months ended January 31, 2006, the Company recorded under EITF 96-18, a total of $86,006 of non-cash expense for these options.

During the six months ended January 31, 2006, the Company recorded under EITF 96-18, a total of $21,132 non-cash expense for options issued to consultants during the fiscal year ended July 31, 2005.

6. SALE OF NET OPERATING LOSS CARRYFORWARDS

New Jersey has enacted legislation permitting certain corporations located in New Jersey to sell a portion of its state tax loss carryforwards and state research and development credits in order to obtain tax benefits. For the state fiscal year 2006 (July 1, 2005 to June 30, 2006), the Company had approximately $1,903,000 of total available net operating loss carryforwards that were saleable, of which New Jersey permitted the Company to sell approximately $356,000. In December 2005, the Company received approximately $317,000 from the sale of the $356,000 of net operating loss carryforwards, which was recognized as a tax benefit for the six months ended January 31, 2006.

For the state fiscal year 2005 (July 1, 2004 to June 30, 2005), the Company had approximately $1,335,000 of total available net operating loss carryforwards that were saleable, of which New Jersey permitted the Company to sell approximately $339,000. In December 2004, the Company received approximately $288,000 from the sale of the $339,000 of net operating loss carryforwards, which was recognized as a tax benefit for the six months ended January 31, 2005.

If still available under New Jersey law, the Company will attempt to sell the remaining $1,547,000 of its net operating loss carryforwards between July 1, 2006 and June 30, 2007 (state fiscal year 2007). This amount, which is a carryover of the Company's remaining net operating loss carryforwards from state fiscal year 2006, may increase if the Company incurs additional net losses and research and development credits during state fiscal year 2007. The Company cannot estimate, however, what percentage of its saleable net operating loss carryforwards New Jersey will permit it to sell, how much money will be received in connection with the sale, if the Company will be able to find a buyer for its net operating loss carryforwards or if such funds will be available in a timely manner.

7. LITIGATION

Shogen v. Global Aggressive Growth Fund, Ltd. et al.

Kuslima Shogen, the Company's Chief Executive Officer and Chairman of the Board of Directors, filed this action on November 18, 2004, in the US District Court, District of New Jersey. The Company was not a party to this action. Several defendants, however, sought permission to name the Company and another defendant in a third-party complaint seeking payment from the Company of any sums which may be assessed against them as a result of Ms. Shogen's claims. On December 2, 2005, the Court denied that request. Accordingly, the Company continues not to be a party to this action.

7. LITIGATION, Continued

Shogen v. Pisani et al.

This action was commenced by Ms. Shogen in May 2005 in New Jersey Superior Court, Essex County. The Company was not a party to this action. Defendants filed counterclaims against Ms. Shogen, and in conjunction with those counterclaims named the Company as a third-party defendant, but they subsequently withdrew their claims against the Company. At this time, the Company continues not to be a party to this action.

8. SUBSEQUENT EVENTS

In February 2006, the Company issued an aggregate of 286,967 shares of common stock upon the exercise of warrants by unrelated parties at exercise prices ranging from $0.75 to $1.50 per share. The Company realized gross proceeds of $310,223 from these exercises.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Information herein contains, in addition to historical information, forward-looking statements that involve risks and uncertainties. All statements, other than statements of historical fact, regarding our financial position, potential, business strategy, plans and objectives for future operations are "forward-looking statements." These statements are commonly identified by the use of forward-looking terms and phrases as "anticipates," "believes," "estimates," "expects," "intends," "may," "seeks," "should," or "will' or the negative thereof or other variations thereon or comparable terminology, or by discussions of strategy. We cannot assure you that the future results covered by these forward-looking statements will be achieved. The matters set forth in Item 1A. "Risk Factors" in this quarterly report on Form 10-Q constitute cautionary statements identifying important factors with respect to these forward-looking statements, including certain risks and uncertainties, that could cause actual results to vary significantly from the future results indicated in these forward-looking statements. Other factors could also cause actual results to differ significantly from the future results indicated in these forward-looking statements.

Overview

Since our inception, we have devoted the vast majority of our resources to the research and development of ONCONASE(R) and related drug candidates. We have focused our resources towards the completion of the clinical program for unresectable, or inoperable, malignant mesothelioma.

Since ONCONASE(R) has Fast Track Designation from the Food and Drug Administration, or FDA, for the treatment of malignant mesothelioma patients, we continue to have meetings and discussions with the FDA to establish mutually agreed upon parameters for the New Drug Application, or NDA to obtain marketing approval for ONCONASE(R), assuming the Phase III clinical trial for the treatment of malignant mesothelioma yields favorable results.

We received an Orphan Medicinal Product Designation for ONCONASE(R) from the European Agency for the Evaluation of Medicinal Products, or EMEA. We continue to fulfill the EMEA requirements regarding the Marketing Authorization Application, or MAA registration requirements for ONCONASE(R) for the treatment of malignant mesothelioma.

We received Orphan Drug Designation for malignant mesothelioma in Australia from the Therapeutics Goods Administration, or TGA. This designation in Australia also entitles us to five years of marketing exclusivity, a 100% waiver of filing fees and regulatory guidance from the TGA.

Almost all of our research and development expenses since our inception of $52,627,000 have gone toward the development of ONCONASE(R) and related drug candidates. For the fiscal years 2005, 2004 and 2003 our research and development expenses were $5,082,000, $3,353,000 and $1,700,000, respectively, almost all of which were used for the development of ONCONASE(R) and related drug candidates. ONCONASE(R) is currently in an international, centrally randomized Phase III trial. The first part of the trial has been completed and the second confirmatory part of the trial is ongoing for which the full enrollment target of 316 patients has now been reached. The primary endpoint of the trial is survival, and as such, a sufficient number of deaths must occur in order to perform the required statistical analyses to determine the efficacy of ONCONASE(R) in patients with unresectable (inoperable) malignant mesothelioma. If the results of the clinical trials are positive, we expect to file for marketing registrations (NDA in the U.S. and MAA in Europe and Australia) for ONCONASE(R) within six months of completion of the statistical analyses. However, at this time, we cannot predict with certainty when a sufficient number of deaths will occur to achieve statistical significance. The timing of when we will be able to file for marketing registrations in the US, EU and Australia is data driven. Therefore, we cannot predict with

12

certainty what our total cost associated with obtaining marketing approvals will be, or when and if such approvals will be granted, or when actual sales will occur.

We fund the research and development of our products primarily from cash receipts resulting from the sale of our equity securities and convertible debentures in registered offerings and private placements and the exercise of stock options and warrants. Additionally, we have raised capital through other debt financings, the sale of our tax benefits and research products, interest income and financing received from our Chief Executive Officer. As of January 31, 2006, we believe our cash balance is sufficient to fund our operations through July 31, 2006 based on our expected level of expenditures in relation to activities in preparing ONCONASE(R) for marketing registrations and other ongoing operations of the Company. To assure our ability to continue our operations beyond this date, we continue to seek additional financing through equity or debt financings and the sale of net operating loss carryforwards, but we cannot be sure that we will be able to raise capital on favorable terms or at all. We may also obtain additional capital through the exercise of outstanding options and warrants, although we cannot provide any assurance of such exercises or estimate the amount of capital we will receive, if any. If we are unable to raise sufficient capital, our operations will be severely curtailed and our business and financial condition will be adversely affected.

Results of Operations

Three and six month periods ended January 31, 2006 and 2005

Revenues. We are a development stage company as defined in the Financial Accounting Standards Board's Statement of Financial Accounting Standards No. 7. We are devoting substantially all of our present efforts to establishing a new business and developing new drug products. Our planned principal operations of marketing and/or licensing new drugs have not commenced and, accordingly, we have not derived any significant revenue from these operations. We focus most of our productive and financial resources on the development of ONCONASE(R) and as such we have not had any sales in the three and six month periods ended January 31, 2006 and 2005. For the three and six month periods ended January 31, 2006, our investment income was $24,000 and $56,000 compared to $34,000 and $63,000 for the same period last year, a decrease of $10,000 and $7,000, respectively. These decreases were due to lower balances of cash and cash equivalents.

Research and Development. Research and development expense for the three months ended January 31, 2006 was $1,430,000 compared to $1,554,000 for the same period last year, a decrease of $124,000, or 8%. The decrease resulted from decreases in pre-clinical sponsored research and development expenses; patent expenses of approximately $91,000; near completion of key toxicology requirements and key requirements for chemistry, manufacturing and controls, including the ONCONASE(R) stability program of approximately $79,000; and costs related to clinical trials of approximately $67,000. This decrease was offset by an increase in compensation expense of approximately $160,000 which is related to share-based compensation; non-cash expense related to stock options issued to consultants of approximately $41,000; and insurance expense of approximately $12,000. The share-based compensation expense is expected to continue as a result of the adoption of SFAS 123(R), which requires us to charge compensation expense for all employee stock options.

Research and development expense for the six months ended January 31, 2006 was $2,589,000 compared to $2,476,000 for the same period last year, an increase of $113,000, or 5%. The increase was primarily due to compensation expense of approximately $291,000 of which approximately $261,000 is related to share-based compensation and non-cash expense related to stock options issued to consultants of approximately $44,000 and insurance expense of approximately $20,000. The share-based

compensation expense is expected to continue as a result of the adoption of SFAS 123(R). This increase was offset by a decreases in patent expenses of approximately $109,000; costs related to clinical trials of approximately $73,000; pre-clinical sponsored research and development expenses and expenses in connection with preparing our NDA for ONCONASE(R), including the completion of key toxicology requirements and key requirements for chemistry, manufacturing and controls, including the ONCONASE(R) stability program of approximately $21,000.

General and Administrative. General and administrative expense for the three months ended January 31, 2006 was $880,000 compared to $422,000 for the same period last year, an increase of $458,000, or 109%. This increase was primarily due to an increase in compensation expense of approximately $122,000 which is related to share-based compensation. The share-based compensation expense is expected to continue as a result of the adoption of SFAS 123(R). The increase in general and administrative expense also resulted from legal fees of approximately $210,000; non-cash expense related to stock options issued to a consultant of approximately $86,000; board of directors fees of approximately $24,000 which is related to share-based compensation and Sarbanes-Oxley compliance and auditing fees of approximately $16,000.

General and administrative expense for the six months ended January 31, 2006 was $1,470,000 compared to $868,000 for the same period last year, an increase of $602,000, or 69%. This increase was primarily due to increase in compensation expense of approximately $263,000 of which approximately $229,000 is related to share-based compensation. The share-based compensation expense is expected to continue as a result of the adoption of SFAS 123(R). The increase in general and administrative expense also resulted from legal fees of approximately $221,000; non-cash expense related to stock options issued to a consultant of approximately $86,000; Sarbanes-Oxley compliance and auditing fees of approximately $68,000; board of directors fees of approximately $35,000 of which approximately $24,000 is related to share-based compensation; offset by decreases in Nasdaq membership fees of approximately $35,000; public relation related expenses of approximately $21,000 and insurance expense of approximately $15,000.

Interest. Interest expense for the three and six months ended January 31, 2006 decreased by $12,000, or 100% and $43,000, or 100%, respectively; primarily due to the maturity and conversion of convertible notes payable into common stock during the last fiscal year ended July 31, 2005.

Income Taxes. New Jersey has enacted legislation permitting certain corporations located in New Jersey to sell a portion of our state tax loss carryforwards and state research and development credits, or net operating loss carryforwards, in order to obtain tax benefits. For the state fiscal year 2006 (July 1, 2005 to June 30, 2006), we had approximately $1,903,000 of total available net operating loss carryforwards that were saleable, of which New Jersey permitted us to sell approximately $356,000. In December 2005, we received approximately $317,000 from the sale of the $356,000 of net operating loss carryforwards, which was recognized as a tax benefit for the six months ended January 31, 2006.

For the state fiscal year 2005 (July 1, 2004 to June 30, 2005), we had approximately $1,335,000 of total available net operating loss carryforwards that were saleable, of which New Jersey permitted us to sell approximately $339,000. In December 2004, we received approximately $288,000 from the sale of the $339,000 of net operating loss carryforwards, which we recognized as a tax benefit for the six months ended January 31, 2005.

If still available under New Jersey law, we will attempt to sell the remaining $1,547,000 of our net operating loss carryforwards between July 1, 2006 and June 30, 2007 (state fiscal year 2007). This amount, which is a carryover of our remaining net operating loss carryforwards from state fiscal year

2006, may increase if we incur additional net losses and research and development credits during state fiscal year 2007. We cannot estimate, however, what percentage of our saleable net operating loss carryforwards New Jersey will permit us to sell, how much money we will receive in connection with the sale, if we will be able to find a buyer for our net operating loss carryforwards or if such funds will be available in a timely manner.

Net Loss. We have incurred net losses during each year since our inception. The net loss for the three months ended January 31, 2006 was $2,286,000 as compared to $1,955,000 for the same period last year, an increase of $331,000. The net loss for the six months ended January 31, 2006 was $3,686,000 as compared to $3,036,000 for the same period last year, an increase of $650,000. The cumulative loss from the date of inception, August 24, 1981 to January 31, 2006, amounted to $79,192,000. Such losses are attributable to the fact that we are still in the development stage and, accordingly, have not derived sufficient revenues from operations to offset the development stage expenses.

Liquidity and Capital Resources

We have financed our operations since inception through the sale of our equity securities and convertible debentures in registered offerings and private placements and the exercise of stock options and warrants. Additionally, we have raised capital through debt financings, the sale of our net operating loss carryforwards and research products, interest income and financing received from our Chief Executive Officer. During the six months ended January 31, 2006, we had a net decrease in cash and cash equivalents of $1,546,000, which resulted primarily from net cash used in operating activities of $2,209,000 and net cash used in investing activities of $8,000, offset by net cash receipts of $671,000 from warrant and stock option exercises. Total cash resources as of January 31, 2006 were $2,917,000 compared to $4,463,000 at July 31, 2005.

Our current liabilities as of January 31, 2006 were $2,387,000 compared to

$1,680,000 at July 31, 2005, an increase of $707,000. The increase was primarily due an increase in accounts payable of approximately $437,000 and accrued expenses of approximately $269,000. These increases were mainly for expenses related to clinical trials of approximately $466,000; pre-clinical studies of approximately $182,000; professional fees of approximately $33,000 and payroll accruals of approximately $25,000.

Our long-term continued operations will depend on our ability to raise additional funds through various potential sources such as equity and debt financing, collaborative agreements, strategic alliances, sale of tax benefits, revenues from the commercial sale of ONCONASE(R), licensing of our proprietary RNase technology and our ability to realize revenues from our technology and our drug candidates via out-licensing agreements with other companies. Such additional funds may not become available as we need them or may not be available on acceptable terms. As of January 31, 2006, we believe our cash balance is sufficient to fund our operations through July 31, 2006, based on our expected level of expenditures in relation to activities in preparing ONCONASE(R) for marketing registrations and other ongoing operations of the Company. However, to assure our ability to continue our operations beyond this date, we continue to seek additional financing through equity or debt financings and the sale of net operating loss carryforwards, but cannot be sure that we will be able to raise capital on favorable terms or at all. We may also obtain additional capital through the exercise of outstanding options and warrants, although we cannot provide any assurance of such exercises or estimate the amount of capital we will receive, if any. If we are unable to raise sufficient capital, our operations will be severely curtailed and our business and financial condition will be adversely affected.

We will continue to incur costs in conjunction with our U.S. and foreign registrations for marketing approval of ONCONASE(R). We are currently in discussions with potential strategic alliance

partners to further the development and marketing of ONCONASE(R) and other related products in our pipeline. However, we cannot be sure that any such alliances will materialize.

The market price of our common stock is volatile, and the price of the stock could be dramatically affected one way or another depending on numerous factors. The market price of our common stock could also be materially affected by the marketing approval or lack of approval of ONCONASE(R).

Off-balance Sheet Arrangements

As part of our ongoing business, we do not participate in transactions that generate relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or variable interest entities or VIE, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. As of January 31, 2006, we are not involved in any unconsolidated VIE transactions.

Critical Accounting Policies and Estimates

Critical accounting policies are those that involve subjective or complex judgments, often as a result of the need to make estimates. The following areas all require the use of judgments and estimates: research and development expenses, accounting for stock-based compensation, accounting for warrants issued with convertible debt and deferred income taxes. Estimates in each of these areas are based on historical experience and various assumptions that we believe are appropriate. Actual results may differ from these estimates. Our accounting practices are discussed in more detail in "Management's Discussion and Analysis of Financial Condition and Results of Operations" and Note 1 of "Notes to Consolidated Financial Statements" in our Annual Report on Form 10-K for the year ended July 31, 2005.

Recently Issued Accounting Standards

In December 2004, the FASB issued SFAS No. 123(R) (revised 2004), "Share-Based Payment", which amends SFAS Statement No. 123. The new standard requires the cost of all share-based payments, including stock option grants to employees, to be recognized as an operating expense in the income statement. The cost is recognized over the requisite service period based on fair values measured on the date of grant. We adopted SFAS 123(R) effective August 1, 2005 using the modified prospective method and accordingly, prior period amounts have not been restated. Under the modified prospective method, the fair value of all new stock options issued after July 31, 2005 and unvested outstanding stock options at August 1, 2005, will be recognized as services are rendered. The impact of the adoption of SFAS 123(R) on future period earnings cannot be determined at this time because it will depend on the level of share-based payments that may be granted in the future. Prior to August 1, 2005, we accounted for stock-based awards to employees using the intrinsic value method in accordance with APB 25.

Contractual Obligations and Commercial Commitments

Our outstanding contractual obligations relate to our equipment operating lease. Since July 31, 2005, there has been no material change with respect to our contractual obligations as disclosed in "Management's Discussion and Analysis of Financial Condition and Results of Operations - Contractual Obligations and Commercial Commitments" in our annual report on Form 10-K for the fiscal year ended July 31, 2005.

16

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Not applicable.

Item 4. Controls And Procedures

(a) Evaluation of disclosure controls and procedures.

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of January 31, 2006, the end of the period covered by this report (the "evaluation date"). Based upon the evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, as of the evaluation date, our disclosure controls and procedures are effective in timely alerting them to the material information relating to us required to be included in our periodic SEC filings.

(b) Changes in internal controls.

There were no significant changes made in our internal controls over financial reporting during the three months ended January 31, 2006 or, to our knowledge, in other factors that have materially affected, or are reasonably likely to materially affect, these controls.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

Shogen v. Global Aggressive Growth Fund, Ltd. et al.

Kuslima Shogen, our Chief Executive Officer and Chairman of the Board of Directors, filed this action on November 18, 2004, in the US District Court, District of New Jersey. This case relates to shares of Alfacell common stock Ms. Shogen had posted as collateral to secure a loan she had taken from certain of the defendants in this litigation. Ms. Shogen alleges that her shares were sold unlawfully in violation of the terms of the loan. Among other things, Ms. Shogen seeks damages of $9 million plus costs and attorneys' fees. Alfacell was not a party to this action. Several defendants, however, sought permission to name Alfacell and another defendant in a third-party complaint seeking payment from Alfacell of any sums which may be assessed against them as a result of Ms. Shogen's claims. On December 2, 2005, the Court denied that request. Accordingly, Alfacell continues not to be a party to this action.

Shogen v. Pisani et al.

This action was commenced by Ms. Shogen in May 2005 in New Jersey Superior Court, Essex County. This lawsuit relates to a loan taken by Ms. Shogen from the defendants in this litigation that was secured by varying amounts of Ms. Shogen's Alfacell common stock. Ms. Shogen alleges, among other things, that the loan was usurious and therefore should be voided. Alfacell was not a party to this action. Defendants filed counterclaims against Ms. Shogen, and in conjunction with those counterclaims named Alfacell as a third-party defendant, but they subsequently withdrew their claims against Alfacell. At this time, the Company continues not to be a party to this action.

Item 1A. Risk Factors

An investment in our common stock is speculative and involves a high degree of risk. You should carefully consider the risks and uncertainties described below and the other information in this Form 10-Q and our other SEC filings before deciding whether to purchase shares of our common stock. If any of the following risks actually occur, our business and operating results could be harmed. This could cause the trading price of our common stock to decline, and you may lose all or part of your investment.

We have incurred losses since inception and anticipate that we will incur continued losses for the foreseeable future. We do not have a current source of product revenue and may never be profitable.

We are a development stage company and since our inception one of the principal sources of our working capital has been private sales of our common stock. We incurred a net loss of approximately $3,686,000 for the six months ended January 31, 2006 and net losses of approximately $6,462,000, $5,070,000 and $2,411,000 for the fiscal years ended July 31, 2005, 2004 and 2003, respectively. We have continued to incur losses since July 31, 2005. We may never achieve revenue sufficient for us to attain profitability.

Our profitability will depend on our ability to develop, obtain regulatory approvals for, and effectively market ONCONASE(R) as well as entering into strategic alliances for the development of new drug candidates from the out-licensing of our proprietary RNase technology. The commercialization of our pharmaceutical products involves a number of significant challenges. In particular our ability to commercialize ONCONASE(R) depends on the success of our clinical development programs, our efforts to obtain regulatory approval and our sales and marketing efforts or those of our marketing partners, if any, directed at physicians, patients and third-party payors. A number of factors could affect these efforts including:

- Our ability to demonstrate clinically that our products have utility and are safe;
- Delays or refusals by regulatory authorities in granting marketing approvals;
- Our limited financial resources relative to our competitors;
- Our ability to obtain an appropriate marketing partner;
- The availability and level of reimbursement for our products by third party payors;
- Incidents of adverse reactions to our products;
- Side effects or misuse of our products and unfavorable publicity that could result; and
- The occurrence of manufacturing or distribution disruptions.

We will seek to generate revenue through licensing, marketing and development arrangements prior to receiving revenue from the sale of our products. To date we have not consummated any licensing or marketing arrangements and we may not be able to successfully consummate any such arrangements. We have entered into several development arrangements, which have resulted in limited revenues for us. However, we cannot ensure that these arrangements or future arrangements, if any, will result in significant amounts of revenue for us. We, therefore, are unable to predict the extent of any future losses or the time required to achieve profitability, if at all.

We will need additional financing to continue operations, which may not be available on acceptable terms, if it is available at all.

We need additional financing in order to continue operations, including completion of our current clinical trials and filing marketing registrations for ONCONASE(R) with the FDA in the United States, with the EMEA in Europe and with the TGA in Australia. If the results from our current clinical trial do not demonstrate the efficacy and safety of ONCONASE(R) for malignant mesothelioma, our ability to raise additional capital will be adversely affected. Even if regulatory applications for marketing approvals are filed, we will need additional financing to continue operations. As of January 31, 2006, we believe that our cash balance is sufficient to fund our operations through July 31, 2006, based on our expected level of expenditures. However, to assure our ability to continue our operations beyond this date, we continue to seek additional financing through equity or debt financings and the sale of net operating loss carryforwards but we cannot be sure that we will be able to raise capital on favorable terms or at all. We may also obtain additional capital through the exercise of outstanding options and warrants, although we cannot provide any assurance of such exercises or estimate the amount of capital we will receive, if any. If we are unable to raise sufficient capital, our operations will be severely curtailed and our business and financial condition will be materially adversely affected.

We may be unable to sell certain state tax benefits in the future and if we are unable to do so, it would eliminate a source of financing that we have relied on in the past.

At July 31, 2005, we had federal net operating loss carryforwards of approximately $52,823,000 that expire from 2006 to 2025 (approximately $8,675,000 expires in the years 2006 to 2010). We also had research and experimentation tax credit carryforwards of approximately $1,955,000 that expire from 2006 to 2025 (approximately $152,000 expires in the years 2006 to 2010). New Jersey has enacted legislation permitting certain corporations located in New Jersey to sell a portion of its state tax loss carryforwards and state research and development credits in order to obtain tax benefits. The aggregate amount of tax benefits that New Jersey allows corporations to sell each state fiscal year (July 1st through June 30th) is determined annually and if New Jersey reduces such aggregate amount in any fiscal year we may be unable to sell some or all of our available tax benefits as we have in the past. In addition, there is a limited market for these types of sales and we may not be able to find someone to purchase our tax benefits for a reasonable price. Our historical results of operations and our cash flows have been improved by our sale of tax benefits and if we continue to generate a limited amount of revenue and are unable in the future to sell our tax benefits, our results of operations and our cash flows will be negatively impacted.

For the state fiscal year 2006 (July 1, 2005 to June 30, 2006), we had approximately $1,903,000 total available tax benefits that were saleable, of which New Jersey permitted us to sell approximately $356,000. In December 2005, we received approximately $317,000 from the sale of the $356,000 of tax benefits, which we recognized as tax benefits for the six months ended January 31, 2006. For the state fiscal year 2005 (July 1, 2004 to June 30, 2005), we had approximately $1,335,000 total available tax benefits that were saleable; of which New Jersey permitted us to sell approximately $339,000. In December 2004, we received approximately $288,000 from the sale of the $339,000 of tax benefits, which we recognized as a tax benefit for the six months ended January 31, 2006.

If still available under New Jersey law, we will attempt to sell the remaining $1,547,000 of our tax benefits between July 1, 2006 and June 30, 2007 (state fiscal year 2007). This amount, which is a carryover of our remaining tax benefits from state fiscal year 2006 and earlier, may increase if we incur additional tax losses during state fiscal year 2007. We cannot estimate, however, what percentage of our saleable tax benefits New Jersey will permit us to sell, how much money we will receive in connection with the sale, if we will be able to find a buyer for our tax benefits or if such funds will be available in a timely manner.

We cannot predict how long it will take us nor how much it will cost us to complete part two of our Phase III trial because it is a survival study.

We currently have ongoing a two-part Phase III trial of ONCONASE(R) as a treatment for malignant mesothelioma. The first part of the clinical trial has been completed and the second confirmatory part for which the full enrollment target of 316 patients has now been reached is still ongoing. The primary endpoint of the Phase III clinical trial is survival, which tracks the length of time patients enrolled in the study live. According to the protocol, a sufficient number of patient deaths must occur in order to perform the required statistical analyses to determine the efficacy of ONCONASE(R) in patients with unresectable (inoperable) malignant mesothelioma. Since it is impossible to predict with certainty when these patient deaths in the Phase III trial will occur, we do not have the capability of reasonably determining when a sufficient number of deaths will occur, nor when we will be able to file for marketing registrations with the FDA, EMEA and TGA.

In addition, clinical trials are very costly and time consuming. The length of time required to complete a clinical trial depends on several factors including the size of the patient population, the ability of patients to get to the site of the clinical study, and the criteria for determining which patients are eligible to join the study. Delays in patient enrollment could delay achieving a sufficient number of deaths required for statistical analyses, which therefore may delay the marketing registrations. Although we believe we could modify some of our expenditures to reduce our cash outlays in relation to our clinical trials and other NDA related expenditures, we cannot quantify which or the amount such expenditures might be modified. Hence, a delay in the commercial sale of ONCONASE(R) would increase the time frame of our cash expenditure outflows and may require us to seek additional financing. Such capital financing may not be available on favorable terms or at all.

If we fail to obtain the necessary regulatory approvals, we will not be allowed to commercialize our drugs and will not generate product revenue.

The FDA and comparable regulatory agencies in foreign countries impose substantial pre-market approval requirements on the introduction of pharmaceutical products. These requirements involve lengthy and detailed pre-clinical and clinical testing and other costly and time consuming procedures. Satisfaction of these requirements typically takes several years depending on the level of complexity and novelty of the product. We cannot apply for FDA, EMEA or TGA approval to market ONCONASE(R) until the clinical trials and all other registration requirements have been met. Drugs in late stages of clinical development may fail to show the desired safety and efficacy results despite having progressed through initial clinical testing. While limited trials with our product have produced certain favorable results, we cannot be certain that we will successfully complete Phase I, Phase II or Phase III testing of any compound within any specific time period, if at all. Furthermore, the FDA or the company may suspend clinical trials at any time on various grounds, including a finding that the subjects or patients are being exposed to an unacceptable health risk. In addition, we cannot apply for FDA, EMEA or TGA approval to market ONCONASE(R) until pre-clinical and clinical trials have been completed. Several factors could prevent the successful completion or cause significant delays of these trials including an

inability to enroll the required number of patients or failure to demonstrate the product is safe and effective in humans. Also if safety concerns develop, the FDA, EMEA and TGA could stop our trials before completion.

All statutes and regulations governing the conduct of clinical trials are subject to change by various regulatory agencies, including the FDA, in the future, which could affect the cost and duration of our clinical trials. Any unanticipated costs or delays in our clinical studies would delay our ability to generate product revenues and to raise additional capital and could cause us to be unable to fund the completion of the studies.

We may not market or sell any product for which we have not obtained regulatory approval. We cannot assure you that the FDA or other regulatory agencies will ever approve the use of our products that are under development. Even if we receive regulatory approval, such approval may involve limitations on the indicated uses for which we may market our products. Further, even after approval, discovery of previously unknown problems could result in additional restrictions, including withdrawal of our products from the market.

If we fail to obtain the necessary regulatory approvals, we cannot market or sell our products in the United States, or in other countries and our long-term viability would be threatened. If we fail to achieve regulatory approval or foreign marketing authorizations for ONCONASE(R) we will not have a saleable product or product revenues for quite some time, if at all, and may not be able to continue operations.

We are and will be dependent upon third parties for manufacturing our products. If these third parties do not devote sufficient time and resources to our products our revenues and profits may be adversely affected.

We do not have the required manufacturing facilities to manufacture our products. We presently rely on third parties to perform certain of the manufacturing processes for the production of ONCONASE(R) for use in clinical trials. Currently, we contract with Scientific Protein Laboratories, LLC for the manufacturing of ranpirnase (protein drug substance) from the oocytes, or the unfertilized eggs, of the Rana pipiens frog, which is found in the Northwest United States and is commonly called the leopard frog. We contract with Ben Venue Corporation for the manufacturing of ONCONASE(R) and with Cardinal Health and Apptuit for the labeling, storage and shipping of ONCONASE(R) for clinical trial use. We utilize the services of these third party manufacturers solely on an as needed basis with terms and prices customary for our industry.

We use FDA GMP licensed manufacturers for ranpirnase and ONCONASE(R). We have identified substantial alternative service providers for the manufacturing services for which we may contract. In order to replace an existing service provider we must amend our IND to notify the FDA of the new manufacturer. Although the FDA generally will not suspend or delay a clinical trial as a result of replacing an existing manufacturer, the FDA has the authority to suspend or delay a clinical trial if, among other grounds, human subjects are or would be exposed to an unreasonable and significant risk of illness or injury as a result of the replacement manufacturer.

We intend to rely on third parties to manufacture our products if they are approved for sale by the appropriate regulatory agencies and are commercialized. Third party manufacturers may not be able to meet our needs with respect to the timing, quantity or quality of our products or to supply products on acceptable terms.

Because we do not have marketing, sales or distribution capabilities, we expect to contract with third parties for these functions and we will therefore be dependent upon such third parties to market, sell and distribute our products in order for us to generate revenues.

We currently have no sales, marketing or distribution capabilities. In order to commercialize any product candidates for which we receive FDA or non US approval, we expect to rely on established third party strategic partners to perform these functions. For example, if we are successful in our Phase III clinical trials with ONCONASE(R), and are granted marketing approval for the commercialization of ONCONASE(R), we will be unable to introduce the product to market without establishing a marketing collaboration with a partner with marketing and distribution capabilities. To date, we have not entered into any marketing or licensing agreements for ONCONASE(R). We cannot assure you we will be able to establish or maintain relationships with one or more biopharmaceutical or other marketing companies with existing distribution systems and direct sales forces to market any or all of our product candidates, on acceptable terms, if at all. Further, it is likely that we will have limited or no control over the manner in which our product candidates are marketed or the resources devoted to such marketing efforts.

In addition, we expect to begin to incur significant expenses in determining our commercialization strategy with respect to one or more of our product candidates. The determination of our commercialization strategy with respect to a product candidate will depend on a number of factors, including:

o the extent to which we are successful in securing collaborative partners to offset some or all of the funding obligations with respect to product candidates;

o the extent to which our agreement with our collaborators permits us to exercise marketing or promotion rights with respect to the product candidate;

o how our product candidates compare to competitive products with respect to labeling, pricing, therapeutic effect, and method of delivery; and

o whether we are able to establish agreements with third party collaborators, including large biopharmaceutical or other marketing companies, with respect to any of our product candidates on terms that are acceptable

A number of these factors are outside of our control and will be difficult to determine.

Our product candidates may not be accepted by the market.

Even if approved by the FDA and other regulatory authorities, our product candidates may not achieve market acceptance, which means we would not receive significant revenues from these products. Approval by the FDA does not necessarily mean that the medical community will be convinced of the relative safety, efficacy and cost-effectiveness of our products as compared to other products. In addition, third party reimbursers such as insurance companies and HMOs may be reluctant to reimburse expenses relating to our products.

We depend upon Kuslima Shogen and our other key personnel and may not be able to retain these employees or recruit qualified replacement or additional personnel, which would have a material adverse affect on our business.

We are highly dependent upon our founder, Chairman and Chief Executive Officer, Kuslima Shogen. Kuslima Shogen's talents, efforts, personality, vision and leadership have been, and continue to be, critical to our success. The diminution or loss of the services of Kuslima Shogen, and any negative market or industry perception arising from that diminution or loss, would have a material adverse effect

on our business. While our other employees have substantial experience and have made significant contributions to our business, Kuslima Shogen is our senior executive and also our primary supporter because she represents the Company's primary means of accessing the capital markets.

Because of the specialized scientific nature of our business, our continued success also is dependent upon our ability to attract and retain qualified management and scientific personnel. There is intense competition for qualified personnel in the pharmaceutical field. As our company grows our inability to attract qualified management and scientific personnel could materially adversely affect our research and development programs, the commercialization of our products and the potential revenue from product sales.

We do not have employment contracts with Kuslima Shogen or any of our other management and scientific personnel.

Our proprietary technology and patents may offer only limited protection against infringement and the development by our competitors of competitive products.

We own two patents jointly with the United States government. These patents expire in 2016. We also own ten United States patents with expiration dates ranging from 2006 to 2019, four European patents with expiration dates ranging from 2009 to 2016, one Japanese patent that expires in 2010, and one Japanese patent that expires in 2013. We also own patent applications that are pending in the United States, Europe and Japan. The scope of protection afforded by patents for biotechnological inventions is uncertain, and such uncertainty applies to our patents as well. Therefore, our patents may not give us competitive advantages or afford us adequate protection from competing products. Furthermore, others may independently develop products that are similar to our products, and may design around the claims of our patents. Patent litigation and intellectual property litigation are expensive and our resources are limited. If we were to become involved in litigation, we might not have the funds or other resources necessary to conduct the litigation effectively. This might prevent us from protecting our patents, from defending against claims of infringement, or both. To date, we have not received any threats of litigation regarding patent issues.

Developments by competitors may render our products obsolete or non-competitive.

In February 2004, the Food and Drug Administration granted Eli Lilly & Company approval to sell its Alimta(R) medication as an orphan drug to treat patients with pleural mesothelioma. Alimta is a multi-targeted antifolate that is based upon a different mechanism of action than ONCONASE(R). To our knowledge, no other company is developing a product with the same mechanism of action as ONCONASE(R). However, there may be other companies, universities, research teams or scientists who are developing products to treat the same medical conditions our products are intended to treat. Eli Lilly is, and some of these other companies, universities, research teams or scientists may be more experienced and have greater clinical, marketing and regulatory capabilities and managerial and financial resources than we do. This may enable them to develop products to treat the same medical conditions our products are intended to treat before we are able to complete the development of our competing product.

Our business is very competitive and involves rapid changes in the technologies involved in developing new drugs. If others experience rapid technological development, our products may become obsolete before we are able to recover expenses incurred in developing our products. We will probably face new competitors as new technologies develop. Our success depends on our ability to remain competitive in the development of new drugs or we may not be able to compete successfully.

We may be sued for product liability.

Our business exposes us to potential product liability that may have a negative effect on our financial performance and our business generally. The administration of drugs to humans, whether in clinical trials or commercially, exposes us to potential product and professional liability risks which are inherent in the testing, production, marketing and sale of new drugs for humans. Product liability claims can be expensive to defend and may result in large judgments or settlements against us, which could have a negative effect on our financial performance and materially adversely affect our business. We maintain product liability insurance to protect our products and product candidates in amounts customary for companies in businesses that are similarly situated, but our insurance coverage may not be sufficient to cover claims. Furthermore, liability insurance coverage is becoming increasingly expensive and we cannot be certain that we will always be able to maintain or increase our insurance coverage at an affordable price or in sufficient amounts to protect against potential losses. A product liability claim, product recall or other claim, as well as any claim for uninsured liabilities or claim in excess of insured liabilities, may significantly harm our business and results of operations. Even if a product liability claim is not successful, adverse publicity and time and expense of defending such a claim may significantly interfere with our business.

If we are unable to obtain favorable reimbursement for our product candidates, their commercial success may be severely hindered.

Our ability to sell our future products may depend in large part on the extent to which reimbursement for the costs of our products is available from government entities, private health insurers, managed care organizations and others. Third-party payors are increasingly attempting to contain their costs. We cannot predict actions third-party payors may take, or whether they will limit the coverage and level of reimbursement for our products or refuse to provide any coverage at all. Reduced or partial reimbursement coverage could make our products less attractive to patients, suppliers and prescribing physicians and may not be adequate for us to maintain price levels sufficient to realize an appropriate return on our investment in our product candidates or compete on price.

In some cases, insurers and other healthcare payment organizations try to encourage the use of less expensive generic brands and over-the-counter, or OTC, products through their prescription benefits coverage and reimbursement policies. These organizations may make the generic alternative more attractive to the patient by providing different amounts of reimbursement so that the net cost of the generic product to the patient is less than the net cost of a prescription brand product. Aggressive pricing policies by our generic product competitors and the prescription benefits policies of insurers could have a negative effect on our product revenues and profitability.

Many managed care organizations negotiate the price of medical services and products and develop formularies for that purpose. Exclusion of a product from a formulary can lead to its sharply reduced usage in the managed care organization patient population. If our products are not included within an adequate number of formularies or adequate reimbursement levels are not provided, or if those policies increasingly favor generic or OTC products, our market share and gross margins could be negatively affected, as could our overall business and financial condition.

The competition among pharmaceutical companies to have their products approved for reimbursement may also result in downward pricing pressure in the industry or in the markets where our products will compete. We may not be successful in any efforts we take to mitigate the effect of a decline in average selling prices for our products. Any decline in our average selling prices would also reduce our gross margins.

In addition, managed care initiatives to control costs may influence primary care physicians to refer fewer patients to oncologists and other specialists. Reductions in these referrals could have a material adverse effect on the size of our potential market and increase costs to effectively promote our products.

We are subject to new legislation, regulatory proposals and managed care initiatives that may increase our costs of compliance and adversely affect our ability to market our products, obtain collaborators and raise capital.

There have been a number of legislative and regulatory proposals aimed at changing the healthcare system and pharmaceutical industry, including reductions in the cost of prescription products and changes in the levels at which consumers and healthcare providers are reimbursed for purchases of pharmaceutical products. For example, the Prescription Drug and Medicare Improvement Act of 2003 provides a new Medicare prescription drug benefit beginning in 2006 and mandates other reforms. Although we cannot predict the full effects on our business of the implementation of this new legislation, it is possible that the new benefit, which will be managed by private health insurers, pharmacy benefit managers and other managed care organizations, will result in decreased reimbursement for prescription drugs, which may further exacerbate industry-wide pressure to reduce the prices charged for prescription drugs. This could harm our ability to market our products and generate revenues. It is also possible that other proposals will be adopted. As a result of the new Medicare prescription drug benefit or any other proposals, we may determine to change our current manner of operation, provide additional benefits or change our contract arrangements, any of which could harm our ability to operate our business efficiently, obtain collaborators and raise capital.

We have only recently been relisted on the Nasdaq SmallCap Market and our stock is thinly traded and you may not be able to sell our stock when you want to do so.

From April 1999, when we were delisted from Nasdaq, until September 9, 2004, when we were relisted on the Nasdaq SmallCap Market, there was no established trading market for our common stock. During that time, our common stock was quoted on the OTC Bulletin Board and was thinly traded. There is no assurance that we will be able to comply with all of the listing requirements necessary to remain listed on the Nasdaq SmallCap Market. In addition, our stock remains thinly traded and you may be unable to sell our common stock during times when the trading market is limited.

The price of our common stock has been, and may continue to be, volatile.

The market price of our common stock, like that of the securities of many other development stage biotechnology companies, has fluctuated over a wide range and it is likely that the price of our common stock will fluctuate in the future. Over the past three years, the sale price for our common stock, as reported by Nasdaq and the OTC Bulletin Board has fluctuated from a low of $0.39 to a high of $10.07. The market price of our common stock could be impacted by a variety of factors, including:

- announcements of technological innovations or new commercial products by us or our competitors,
- disclosure of the results of pre-clinical testing and clinical trials by us or our competitors,
- disclosure of the results of regulatory proceedings,

- changes in government regulation,

- developments in the patents or other proprietary rights owned or licensed by us or our competitors,

- public concern as to the safety and efficacy of products developed by us or others,

- litigation, and

- general market conditions in our industry.

In addition, the stock market continues to experience extreme price and volume fluctuations. These fluctuations have especially affected the market price of many biotechnology companies. Such fluctuations have often been unrelated to the operating performance of these companies. Nonetheless, these broad market fluctuations may negatively affect the market price of our common stock.

Events with respect to our share capital could cause the price of our common stock to decline.

Sales of substantial amounts of our common stock in the open market, or the availability of such shares for sale, could adversely affect the price of our common stock. We had 37,103,095 shares of common stock outstanding as of January 31, 2006. The following securities that may be exercised into shares of our common stock were issued and outstanding as of January 31, 2006:

- Options. Stock options to purchase 4,073,400 shares of our common stock at a weighted average exercise price of approximately $3.13 per share.

- Warrants. Warrants to purchase 12,126,593 shares of our common stock at a weighted average exercise price of approximately $2.33 per share.

The shares of our common stock that may be issued under the options and warrants are currently registered with the SEC or are eligible for sale without any volume limitations pursuant to Rule 144(k) under the Securities Act.

Our incorporation documents may delay or prevent (i) the removal of our current management or (ii) a change of control that a stockholder may consider favorable.

We are currently authorized to issue 1,000,000 shares of preferred stock. Our Board of Directors is authorized, without any approval of the stockholders, to issue the preferred stock and determine the terms of the preferred stock. This provision allows the board of directors to affect the rights of stockholders, since the board of directors can make it more difficult for common stockholders to replace members of the board. Because the board of directors is responsible for appointing the members of our management, these provisions could in turn affect any attempt to replace current management by the common stockholders. Furthermore, the existence of authorized shares of preferred stock might have the effect of discouraging any attempt by a person, through the acquisition of a substantial number of shares of common stock, to acquire control of our company. Accordingly, the accomplishment of a tender offer may be more difficult. This may be beneficial to management in a hostile tender offer, but have an adverse impact on stockholders who may want to participate in the tender offer or inhibit a stockholder's ability to receive an acquisition premium for his or her shares.

The ability of our stockholders to recover against Armus Harrison & Co., or AHC, may be limited because we have not been able to obtain the reissued reports of AHC with respect to the financial statements included in this Form 10-K, nor have we been able to obtain AHC's consent to the use of such report herein.

Section 18 of the Securities Exchange Act of 1934 (the "Exchange Act") provides that any person acquiring or selling a security in reliance upon statements set forth in a Form 10-K may assert a claim against every accountant who has with its consent been named as having prepared or certified any part of the Form 10-K, or as having prepared or certified any report or valuation that is used in connection with

the Form 10-K, if that part of the Form 10-K at the time it is filed contains a false or misleading statement of a material fact, or omits a material fact required to be stated therein or necessary to make the statements therein not misleading (unless it is proved that at the time of such acquisition such acquiring person knew of such untruth or omission).

In June 1996, AHC dissolved and ceased all operations. Therefore, we have not been able to obtain the reissued reports of AHC with respect to the financial statements included in the Form 10-K for the fiscal year ended July 31, 2005 nor have we been able to obtain AHC's consent to the use of such report herein. As a result, in the event any persons seek to assert a claim against AHC under Section 18 of the Exchange Act for any untrue statement of a material fact contained in these financial statements or any omissions to state a material fact required to be stated therein, such persons will be barred. Accordingly, you may be unable to assert a claim against AHC under Section 18 of the Exchange Act for any purchases of the Company's Common Stock made in reliance upon statements set forth in the Form 10-K for the fiscal year ended July 31, 2005. In addition, the ability of AHC to satisfy any claims properly brought against it may be limited as a practical matter due to AHC's dissolution in 1996.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

(a) Recent Sales of Unregistered Securities

The following transactions were exempt from registrations under Section 4(2) of the Securities Act of 1933, as amended. The net proceeds from these transactions will be used for general corporate purposes.

During the quarter ended January 31, 2006, we issued an aggregate total of 337,778 shares of common stock upon the exercise of warrants at an exercise price of $1.50 per share by an unrelated party, which resulted in gross proceeds of $506,667 to us. We have previously registered the resale of these shares by the stockholders on a Form S-3 registration statement.

Item 4. Submission of Matters to a Vote of Security Holders

(a) An annual meeting of stockholders was held on January 19, 2006.

(b) All of our current directors, Kuslima Shogen, John P. Brancaccio, Stephen K. Carter, Donald R. Conklin, James J. Loughlin, David Sidransky and Paul M. Weiss, were elected at the annual meeting.

(c) The matters voted upon at the annual meeting and the results of the voting, including broker non-votes where applicable, are set forth below:

(i) For the election of directors

Director	Number of Shares of Common Stock Voted For	Number of Shares of Common Stock Withheld	Number of Non-Vot
Kuslima Shogen	30,126,920	484,709	0
John P. Brancaccio	30,443,046	168,583	0
Stephen K. Carter	30,524,266	87,363	0
Donald R. Conklin	30,437,866	173,763	0
James J. Loughlin	30,527,766	83,863	0
David Sidransky	30,498,276	113,353	0
Paul M. Weiss	30,336,516	275,113	0

(ii) Proposal to ratify the appointment of J.H. Cohn LLP as Alfacell's independent registered public accounting firm for the year ending July 31, 2006.

Number of Shares of Common Stock Voted For	Number of Shares of Common Stock Voted Against	Number of Shares of Common which Abstained from Voting
30,386,781	62,720	162,128

Item 6. Exhibits

Exhibits (numbered in accordance with Item 601 of Regulation S-K).

Exhibit No.	Item Title	Exhibit No. Incorporatio Reference
3.1	Certificate of Incorporation, dated June 12, 1981 (incorporated by reference to Registration Statement on Form S-1, File No. 333-112865, filed on February 17, 2004)	*

3.2	Amendment to Certificate of Incorporation, dated February 18, 1994 (incorporated by reference to Registration Statement on Form S-1, File No. 333-112865, filed on February 17, 2004)	*
3.3	Amendment to Certificate of Incorporation, dated December 26, 1997 (incorporated by reference to Registration Statement on Form S-1, File No. 333-112865, filed on February 17, 2004)	*
3.4	Amendment to Certificate of Incorporation, dated January 14, 2004 (incorporated by reference to Registration Statement on Form S-1, File No. 333-112865, filed on February 17, 2004)	*
3.5	Certificate of Designation for Series A Preferred Stock, dated September 2, 2003 (incorporated by reference to Registration Statement on Form S-1, File No. 333-112865, filed on February 17, 2004)	*
3.6	Certificate of Elimination of Series A Preferred Stock, dated February 3, 2004 (incorporated by reference to Registration Statement on Form S-1, File No. 333-112865, filed on February 17, 2004)	*

Exhibit No.	Item Title	Exhibit No. Incorporatio Reference
3.7	By-Laws (incorporated by reference to Exhibit 3.4 to Registration Statement on Form S-1, File No. 333-111101, filed on December 11, 2003)	*
31.1	Certification of Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	+
31.2	Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	+
32.1	Certification Principal Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	+
32.2	Certification Principal Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	+

* Previously filed; incorporated herein by reference.

\+ Filed herewith.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

ALFACELL CORPORATION
(Registrant)

March 13, 2006

/s/ Robert D. Love

Robert D. Love
Chief Financial Officer
(Principal Financial Officer and
Chief Accounting Officer)

30

our guests for various business purposes, including maintaining guest preferences to enhance our customer service and for marketing and promotion purposes. The collection and use of personal data are governed by privacy laws and regulations. Compliance with applicable privacy regulations may increase our operating costs and/or adversely impact our ability to service our guests and market our products, properties and services to our guests. In addition, non-compliance with applicable privacy regulations by us (or in some circumstances non-compliance by third parties engaged by us) could result in fines or restrictions on our use or transfer of data.

Increasing use of internet reservation channels may decrease loyalty to our brands or otherwise adversely affect us.

As is the case with many other hotel operators, a growing percentage of our hotel rooms are booked through internet travel intermediaries. If such bookings continue to increase, these intermediaries may be able to obtain higher commissions, reduced room rates or other significant contract concessions from our franchisors or us. Moreover, some of these internet travel intermediaries are attempting to commoditize hotel rooms, by increasing the importance of price and general indicators of quality at the expense of brand identification. These intermediaries hope that consumers will eventually develop brand loyalties to their reservations systems rather than to our lodging brands. If this happens our business and profitability may be significantly harmed.

Our business is seasonal in nature, and we are likely to experience fluctuations in our results of operations and financial condition.

Our business is seasonal in nature, with the first and fourth fiscal quarters generally accounting for a greater portion of annual revenues than the second and third fiscal quarters. Therefore, our results for any quarter may not be indicative of the results that may be achieved for the full fiscal year. The seasonal nature of our business increases our vulnerability to risks such as labor force shortages and cash flow problems. Further, if an adverse event such as an actual or threatened terrorist attack, international conflict, regional economic downturn or poor weather conditions should occur during the first or fourth fiscal quarters, the adverse impact to our revenues could likely be greater as a result of our southern Arizona seasonal business.

Our properties are subject to risks relating to natural disasters, terrorist activity and war and any such event could materially adversely affect our operating results.

Our financial and operating performance may be adversely affected by natural disasters particularly in locations where we own significant properties. Some types of losses, such as those from earthquake, wild fires, terrorism or environmental hazards, may be either uninsurable or too expensive to justify insuring against. Should an uninsured loss or a loss in excess of insured limits occur, we could lose all or a portion of the capital we have invested in a property, as well as the anticipated future revenue from the property. In that event, we might nevertheless remain obligated for any financial obligations related to the property. Inflation, changes in building codes and ordinances, environmental considerations and other factors also might make it impractical to rely on insurance proceeds to replace property after that property has been damaged or destroyed. Under those circumstances, the insurance proceeds received by us might not be adequate to restore our economic position with respect to such property.

Similarly, war (including the potential for war) and terrorist activity (including threats of terrorist activity), epidemics (such as SARs and bird flu), travel-related accidents, as well as geopolitical uncertainty and international conflict, which impact domestic and international travel, may cause our results to differ materially from anticipated results. Terrorism incidents such as the events of September 11, 2001 and wars such as the ongoing Iraq war significantly impact travel and tourism and consequently the demand for hotel rooms.

Hospitality companies have been the target of class actions and other lawsuits alleging violations of federal and state law.

Our operating income and profits may be reduced by legal or governmental proceedings brought by or on behalf of our employees or customers. In recent years, a number of hospitality companies have been subject to lawsuits, including class action lawsuits, alleging violations of federal and state law regarding workplace and employment matters, discrimination and similar matters. A number of these lawsuits have resulted in the payment of substantial damages by the defendants. We cannot assure you that we will not incur substantial damages and expenses resulting from lawsuits of this type, which could have a material adverse effect on our business.

Item 1B. UNRESOLVED STAFF COMMENTS

Not applicable.

Item 2. PROPERTIES

The Trust maintains its administrative offices at the InnSuites Hotels Centre in Phoenix, Arizona. On January 31, 2006, the Partnership owned four Hotels and the Trust owned one Hotel. All of the Hotels are operated as InnSuites® Hotels, while four are also marketed as Best Western® Hotels. All of the Hotels operate in the following locations:

PROPERTY	**NUMBER OF SUITES**	**YEAR OF CONSTRUCTION/ ADDITION**	**MOST RECENT RENOVATION (1)**
InnSuites Hotel and Suites Airport Albuquerque Best Western	101	1975/1985	2004
InnSuites Hotel and Suites Tucson, Catalina Foothills Best Western	159	1981/1983	2005
InnSuites Hotels and Suites Yuma Best Western	166	1982/1984	2003
InnSuites Hotel and Suites Ontario Airport Best Western	150	1990	2005
InnSuites Hotels and Suites Tucson St. Mary’s	267	1960/1971	2004
Total suites	843		

(1) The Trust defines a renovation as the remodeling of more than 10% of a property’s available suites.

See “Item 7 - Management’s Discussion and Analysis of Financial Condition and Results of Operations - General” herein for a discussion of occupancy rates at the Hotels.

See Note 5 to the Trust’s Consolidated Financial Statements - “Mortgage Notes Payable” herein for a discussion of mortgages encumbering the Hotels.

Item 3. LEGAL PROCEEDINGS

The Trust is not a party to, nor are any of its properties subject to, any material litigation or environmental regulatory proceedings.

Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The Trust held its 2005 Annual Meeting of Shareholders on August 25, 2005. The nominees listed below were elected as Trustees of the Trust to hold office for a term expiring at the 2007 Annual Meeting of Shareholders and until their successors have been duly elected and qualified. Tabulated below is the number of Shares of Beneficial Interest cast for and withheld with respect to the election of the Trustee nominees:

11

Name	For	Against
Steven Robson	8,121,714	33,551
Larry Pelegrin	8,121,714	33,551

In addition to the election of Trustees, the security holders voted on the following matters at the Annual Meeting:

• Granting the Board of Trustees the authority to implement a reverse stock split up to a maximum ratio of 1-for-4:

For	Against	Abstain
7,065,769	1,044,674	44,822

The Trust has not taken any action and currently is not planning to take any action regarding a reverse stock split, although the possibility continues to be reviewed by the Board of Trustees.

PART II

Item 5. MARKET FOR THE TRUST'S SHARES, RELATED SHAREHOLDER MATTERS AND TRUST PURCHASES OF SHARES

The Trust's Shares of Beneficial Interest are traded on the American Stock Exchange under the symbol "IHT." On April 21, 2006, the Trust had 9,271,114 shares outstanding and 519 holders of record.

The following table sets forth, for the periods indicated, the high and low sales prices of the Trust's Shares of Beneficial Interest, as quoted by the American Stock Exchange, as well as dividends declared thereon:

Fiscal Year 2006	High	Low	Dividends
First Quarter	1.52	1.11	—
Second Quarter	1.75	1.23	—
Third Quarter	1.50	1.24	—
Fourth Quarter	1.50	1.20	.01

Fiscal Year 2005	High	Low	Dividends
First Quarter	2.25	1.60	—
Second Quarter	2.25	1.48	—
Third Quarter	1.63	1.49	—
Fourth Quarter	1.95	1.12	.01

The Trust intends to maintain a conservative dividend policy to facilitate the reduction of debt and internal growth. In fiscal years 2006 and 2005, the Trust paid dividends of $0.01 per share in the fourth quarter of each year.

On January 2, 2001, the Board of Trustees approved a share repurchase program under Rule 10b-18 of the Securities Exchange Act of 1934, as amended, for the purchase of up to 250,000 limited partnership units in the Partnership and/or Shares of Beneficial Interest in open market or privately negotiated transactions. Additionally, on September 10, 2002, the Board of Trustees approved the purchase of up to 350,000 additional limited partnership units in the Partnership and/or Shares of Beneficial Interest in open market or privately negotiated transactions. On August 18, 2005, the Board of Trustees approved the purchase of up to 350,000 additional limited partnership units in the Partnership and/or Shares of Beneficial Interest in open market or privately negotiated transactions. Acquired Shares of Beneficial Interest will be held in treasury and will be available for future acquisitions and financings and/or for awards granted under the InnSuites Hospitality Trust 1997 Stock Incentive and Option Plan. During the three months ended January 31, 2006, the Trust acquired 107,184 Shares of Beneficial Interest in open market transactions at an average price of $1.32 per share. The Trust intends to continue repurchasing Shares of Beneficial Interest in compliance with applicable legal and American Stock Exchange requirements. The Trust remains authorized to repurchase an additional 214,112 limited partnership units and/or Shares of Beneficial Interest pursuant to the share repurchase program, which has no expiration date.

Issuer Purchases of Equity Securities

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans	Maximum Number of Shares that May Be Yet Purchased Under the Plans
November 1 - November 30, 2005	43,606	$ 1.33	43,606	285,322
December 1 - December 31, 2005	62,378	$ 1.31	62,378	222,944
January 1 - January 31, 2006	1,200	$ 1.43	1,200	214,112 *

*During the January 2006, the Trust repurchased 7,632 Class A Units in the Partnership under the Plans at a price of $1.40.

See Part III, Item 12 for a description of our equity compensation plans.

Item 6. SELECTED FINANCIAL DATA

The following selected financial data of the Trust as of and for the five fiscal years ended January 31, 2006, has been derived from the audited consolidated financial statements of the Trust. The consolidated financial statements of the Trust as of and for the fiscal years ended January 31, 2006 and 2005 were audited by Epstein, Weber & Conover, P.L.C., independent public accountants. The consolidated financial statements of the Trust as of and for the two fiscal years ended January 31, 2004 and 2003 were audited by McGladrey & Pullen, LLP, independent public accountants. The consolidated financial statements of the Trust as of and for the fiscal year ended January 31, 2002 were audited by KPMG, LLP, independent public accountants.

	Year Ended January 31,				
	2006	2005	2004	2003	2002
Total revenue	$ 21,248,839	$ 22,875,187	$ 24,211,328	$ 26,940,473	$ 27,656,009
Net income (loss) attributable to Shares of Beneficial Interest	$ 541,578	$ 240,442	$ (2,594,317)	$ (3,445,948)	$ (3,539,402)
Income (loss) per share - basic	$ 0.06	$ 0.10	$ (1.27)	$ (1.67)	$ (1.66)
Income (loss) per share - diluted	$ 0.02	$ 0.10	$ (1.27)	$ (1.67)	$ (1.66)
Cash dividends paid and declared per share	$ 0.01	$ 0.01	$ 0.02	$ 0.01	$ 0.01

Total assets	$	31,952,358	$	36,455,521	$	47,961,594	$	61,494,579	$	64,264,516
Notes and advances payable to banks and others	$	20,736,859	$	24,755,858	$	31,974,992	$	38,922,408	$	38,598,106
Notes and advances payable to related parties	$	514,706	$	93,512	$	6,852,241	$	9,901,153	$	8,666,360

See "Item 1 - Business" herein for a discussion of the change in the nature of the business of the Trust over the course of the years presented above. As a result, the information presented above is not comparative from year to year.

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

OVERVIEW

The Trust is engaged in the ownership and operation of hotel properties. At January 31, 2006, the InnSuites system included five moderate and full-service hotels with 843 hotel suites. Four of our Hotels are branded through franchise agreements with Best Western. All five Hotels are trademarked as InnSuites Hotels. We are also involved in various operations incidental to the operation of hotels, such as the operation of restaurants and meeting/banquet room rentals.

13

Our operations consist of one reportable segment, hotel ownership, which derives its revenue from the operation of the Hotels. In addition, we receive management fees, trademark license fees and reservation fees.

Our results are significantly affected by occupancy and room rates at the Hotels, our ability to manage costs, and changes in the number of available suites caused by acquisition and disposition activities. Results are also significantly impacted by overall economic conditions and conditions in the travel industry. Unfavorable changes in these factors could negatively impact hotel room demand and pricing which would reduce our profit margins on rented suites. Additionally, our ability to manage costs could be adversely impacted by significant increases in operating expenses, resulting in lower operating margins.

We anticipate that improved economic conditions, both generally and specifically in the travel industry, will positively impact the operations of the Trust in fiscal year 2007. Better overall economic conditions are expected to result in increased business and leisure travel and support higher room rates, and therefore higher operating margins. We expect the major challenge for fiscal year 2007 to be strong competition for group business in the markets in which we operate that may affect the Trust’s ability to increase room rates while maintaining market share. We believe that we have positioned the hotels to remain competitive through selective refurbishment and carrying a relatively large number of two-room suites at each location.

Effective February 1, 2004, the Trust relinquished its REIT status. As of that date, any distributions to its shareholders are not deductible for purposes of computing the Trust’s taxable income and the Trust will be subject to income tax, including any applicable alternative minimum tax, on its taxable income at regular corporate rates, without offset for distributions of such income to its shareholders. As of January 31, 2006, the Trust has $14.0 million in federal net loss carryforward available to offset future federal tax liability.

GENERAL

The following discussion should be read in conjunction with the Trust’s consolidated financial statements and notes thereto.

The accounting policies that we believe are most critical and involve the most subjective judgments include our estimates and assumptions of future revenue and expenditures used to project hotel cash flows. Future cash flows are used in the valuation calculation of our hotel properties to determine the recoverability (or impairment) of the carrying amounts in the event management is required to test the asset for recoverability of its carrying value under Statement of Financial Accounting Standards No. 144. If the carrying amount of an asset exceeds the estimated future cash flows over its estimated remaining life, the Trust recognizes an impairment expense to reduce the asset’s carrying value to its fair value. Fair value is determined by either the most current third-party property appraisal, if available, or the present value of future undiscounted cash flows over the remaining life of the asset. Our evaluation of future cash flows is based on our historical experience and other factors, including certain economic conditions and committed future bookings. See “- Critical Accounting Policies and Estimates” below.

At January 31, 2006 and 2005, the Trust owned a 69.14% and 65.75%, respectively, interest in four of the Hotels through its sole general partner’s interest in the Partnership and owned a 99.9% interest in one Hotel. The Trust purchased 51,300, 532,077 and 57,509 Partnership units during the years ended January 31, 2006, 2005 and 2004, respectively.

Prior to May 1, 2004, the Partnership leased its hotel properties to InnSuites Hotels. The corresponding rent expense for InnSuites Hotels and rent revenue for the Partnership, as well as the resulting rent receivable and payable, eliminate in consolidation. On May 1, 2004, the percentage lease agreements between the Partnership and InnSuites Hotels were terminated. During the fourth quarter of fiscal year 2004, the Partnership agreed to waive InnSuites Hotels accrued but unpaid rent in exchange for InnSuites Hotels extending its lease agreements one year. The total amount waived was $3,134,130. This transaction had a net effect of increasing the Trust's stockholders equity by $1,518,834.

The expenses of the Trust consist primarily of property taxes, insurance, corporate overhead, interest on mortgage debt, professional fees, depreciation of the Hotels and hotel operating expenses. Under the terms of its Partnership Agreement, the Partnership is required to reimburse the Trust for all such expenses. Accordingly, management believes that a review of the historical performance of the operations of the Hotels, particularly with respect to occupancy, which is calculated as rooms sold divided by total rooms available, average daily rate ("ADR"), calculated as total room revenue divided by number of rooms sold, and revenue per available room ("REVPAR"), calculated as total room revenue divided by number of rooms available, is appropriate for understanding revenue from the Hotels. Occupancy increased 1.17% to 69.72% from 68.55% in the prior year. ADR decreased by $0.28 to $70.55 in fiscal year 2006 from $70.83 in fiscal year 2005. The increase in occupancy resulted in an increase in REVPAR of $0.64 to $49.19 in fiscal year 2006 from $48.55 in fiscal year 2005.

The following table shows certain historical financial and other information for the periods indicated:

	For the Year Ended January 31,		
	2006	2005	2004
Occupancy	69.72%	68.55%	62.79%
Average Daily Rate (ADR)	$ 70.55	$ 70.83	$ 66.27
Revenue Per Available Room (REVPAR)	$ 49.19	$ 48.55	$ 41.61

No assurance can be given that the trends reflected in this data will continue or that occupancy, ADR and REVPAR will not decrease as a result of changes in national or local economic or hospitality industry conditions.

The Trust enters into transactions with certain related parties from time to time. For information relating to such related party transactions see the following:

• For a discussion of management and licensing agreements with certain related parties, see "Item 1 - Business - Management and Licensing Contracts."

• For a discussion of acquisitions involving certain related parties, see "Item 1 - Business - Acquisition of InnSuites Hotels by the Trust."

• For a discussion of the sales of the Trust's Phoenix and Tempe, Arizona hotels to a related party during fiscal years 2005 and 2006, see "Item 1 - Business - Sale of Hotel Properties" and Note 19 to the Trust's Consolidated Financial Statements - "Sale of Hotel Properties."

• For a discussion of guarantees of the Trust's mortgage notes payable by certain related parties, see Note 5 to the Trust's Consolidated Financial Statements - "Mortgage Notes Payable."

• For a discussion of notes and advances payable by the Trust to certain related parties, see Note 7 to the Trust's Consolidated Financial Statements - "Notes and Advances Payable to Related Parties."

• For a discussion of the Trust's employment agreement with Mr. Wirth, see Note 12 to the Trust's Consolidated Financial Statements - "Advisory Agreement/Employment Agreements."

Results of Operations of the Trust for the year ended January 31, 2006 compared to the year ended January 31, 2005.

Overview

A summary of operating results for the fiscal years ended January 31, 2006 and 2005 is:

	2006	2005	Change	% Change
Revenue	$ 21,248,839	$ 22,875,187	$ (1,626,348)	(7.1)%
Operating Income (Loss)	$ 349,349	$ (221,647)	$ 570,996	>100.0%
Net Income	$ 541,578	$ 240,442	$ 301,136	>100.0%
Income Per Share - Basic	$ 0.06	$ 0.10	$ (0.04)	(40.0)%
Income Per Share - Diluted	$ 0.02	$ 0.10	$ (0.08)	(80.0)%

The Trust’s overall results in 2006 were positively affected by the disposition of certain of its underperforming properties in the prior two fiscal years and the improved operating results of the remaining hotel properties due to the continued strengthening of the travel industry.

For the twelve months ended January 31, 2006, the Trust had total revenue of $21.2 million compared to $22.9 million for the twelve months ended January 31, 2005, a decrease of approximately $1.6 million. This decrease in total revenue is primarily due to the sale of the Tempe and Phoenix, Arizona and San Diego, California properties during the last two fiscal years and decreased occupancy at the Ontario, California location due to a conversion of the property to a new brand affiliation. The negative effects of this brand conversion are not expected to continue in fiscal year 2007. Total expenses of $22.8 million for the twelve months ended January 31, 2006 reflect a decrease of approximately $2.5 million compared to total expenses of $25.3 million for the twelve months ended January 31, 2005. The decrease is primarily due to the sales of the Tempe and Phoenix, Arizona and San Diego, California properties during the last two fiscal years, reduced depreciation due to a large portion of Trust assets reaching the end of their estimated lives, and expenses in the prior year related to the purchase of the management and licensing contracts.

For the twelve months ended January 31, 2006, the Trust had a net gain on disposition of hotels of $1.8 million, a decrease of $3.3 million, or 63.9%, from $5.1 million in fiscal year 2005. The fiscal year 2006 gain is primarily a result of the sale of the Phoenix, Arizona property during the second quarter. The fiscal year 2005 gain is primarily a result of the sale of the San Diego, California property during the first quarter.

General and administrative expenses include overhead charges for management, accounting, shareholder and legal services for the Trust. In comparing general and administrative expenses for the twelve months ended January 31, 2006 and 2005, these expenses decreased $497,000, or 11.2%, to $3.9 million in fiscal year 2006, from $4.4 million in fiscal year 2005. This decrease was primarily due to expenses of approximately $274,000 in fiscal year 2005 related to the purchase of the management and licensing contracts and the disposition of certain Trust properties, which resulted in a $340,000 decrease in expenses.

Total operating expenses for the twelve months ended January 31, 2006 were $20.9 million, a decrease of approximately $2.2 million, or 9.5%, from $23.1 million in the twelve months ended January 31, 2005. The decrease was primarily due to the sales of the Tempe and Phoenix, Arizona and San Diego, California properties during the last two fiscal years, reduced depreciation due to a large portion of Trust assets reaching the end of their estimated lives, and expenses in the prior year related to the purchase of the management and licensing contracts.

Total interest expense for the twelve months ended January 31, 2006 was $1.9 million, a decrease of $350,000, or 15.5%, from $2.3 million in the twelve months ended January 31, 2005. Interest on mortgage notes payable for the twelve months ended January 31, 2006 was $1.8 million, a decrease of $243,000, or 11.6%, from $2.1 million in the twelve months ended January 31, 2005. The decrease is primarily due to the satisfaction of the mortgage note payable secured by the Phoenix, Arizona property in connection with the disposition of that property. Interest on notes payable to related parties decreased 86.6%, or $109,000, to $17,000 from $125,000 during the years ended January 31, 2006 and 2005, respectively. The decrease is primarily due to interest incurred on notes totaling $6.2 million due to affiliates of Mr. Wirth which were outstanding during the first quarter of fiscal year 2005. These notes were paid off at the end of the first quarter of fiscal year 2005 in connection with the sales of the Tempe, Arizona and San Diego, California properties.

Real estate and personal property taxes, insurance and ground rent was $1.3 million for the twelve months ended January 31, 2006 and 2005. The decrease of $71,000, or 5.3%, was primarily due to the sale of the Phoenix, Arizona property during the second quarter of fiscal year 2006, which resulted in a decrease of $64,000.

Hotel property depreciation for the twelve months ended January 31, 2006 compared to 2005 decreased approximately $637,000, or 23.1%, to $2.1 million from $2.8 million, respectively. The decrease was primarily due to the sale of the Phoenix, Arizona property, which accounted for a $239,000 decrease, and a large portion of the Trust’s furniture and equipment reaching the end of its useful life at the beginning of fiscal year 2006.

The Trust had other income of $60,000 for the twelve months ended January 31, 2006 relating to insurance proceeds received by the Ontario, California hotel. There was no such income during the twelve months ended January 31, 2005.

The Trust had income before minority interest, income taxes and cumulative effect of adoption of accounting principle of $349,000 for the twelve months ended January 31, 2006, compared to $2.6 million in the prior year. After deducting the loss allocated to the minority interest of $267,000 and taxes of $75,000, the Trust had net income attributable to Shares of Beneficial Interest of approximately $541,000 for fiscal year 2006. This represented an increase of approximately $301,000 in net income attributable to Shares of Beneficial Interest comparing the twelve months ended January 31, 2006 and 2005. Basic net income per share was $0.06 for the twelve months ended January 31, 2006, compared to $0.10 for 2005.

Results of Operations of the Trust for the year ended January 31, 2005 compared to the year ended January 31, 2004.

Overview

A summary of operating results for the fiscal years ended January 31, 2005 and 2004 is:

		2005		2004		Change	% Change
Revenue	$	22,875,187	$	24,211,328	$	(1,336,141)	(5.5)%
Operating Loss	$	(221,647)	$	(272,479)	$	50,832	18.7%
Net Income (Loss)	$	240,442	$	(2,594,317)	$	2,834,759	>100.0%
Income (Loss) Per Share - Basic and Diluted	$	0.10	$	(1.27)	$	1.37	>100.0%

The Trust's overall results in 2005 were positively affected by the disposition of certain of its underperforming properties, the impact of which was partially offset by expenses related to its acquisition of the management and licensing contracts from the Management Company, which will eliminate those expenses in future years.

For the twelve months ended January 31, 2005, the Trust had total revenue of $22.9 million compared to $24.2 million for the twelve months ended January 31, 2004, a decrease of approximately $1.3 million. This decrease in total revenue is primarily due to the sale of the Tempe, Arizona and San Diego, California properties in the first quarter of fiscal year 2005. Total expenses of $25.3 million for the twelve months ended January 31, 2005 reflect a decrease of approximately $2.5 million compared to total expenses of $27.9 million for the twelve months ended January 31, 2004. The decrease is primarily due to the sales of the Tempe, Arizona and San Diego, California properties in the first quarter of fiscal year 2005 and an impairment charge of $458,000 related to the Buena Park, California and Tempe, Arizona properties in fiscal year 2004.

Loss on impairment of hotel property was approximately $458,000 for the twelve months ended January 31, 2004. This loss resulted from write-downs for impairments of the Buena Park, California and Tempe, Arizona hotel properties. During fiscal year 2004, the Trust entered into purchase agreements related to both properties at amounts below their carrying values. The Buena Park, California property was written down by $329,000 to its fair value of $6.5 million, which was its subsequent sales price. The Tempe, Arizona property was written down by $129,000 to its fair value of $6.8 million, which was its subsequent sales price. See Note 19 to the Trust's Consolidated Financial Statements - "Hotels Held for Sale and Sale of Hotel Properties." No such loss was recorded for the twelve months ended January 31, 2005.

For the twelve months ended January 31, 2005, the Trust had a net gain on disposition of hotels of $5.1 million. The Trust had no gains reported in fiscal year 2004. The fiscal year 2005 gain is primarily a result of the sale of the San Diego, California property during the first quarter.

General and administrative expenses include overhead charges for management, accounting, shareholder and legal services for the Trust. In comparing general and administrative expenses for the twelve months ended January 31, 2005 and 2004, these expenses decreased $258,000, or 5.5%, to $4.4 million in fiscal year 2005, from $4.7 million in fiscal year 2004. This decrease was primarily due to elimination of management and franchise fees paid by the Trust due to the consolidation of the Management Company and Licensing Corp. and subsequent purchase of those contracts, offset by the increased expenses to effect those transactions.

Total operating expenses for the twelve months ended January 31, 2005 were $23.1 million, a decrease of approximately $1.4 million, or 5.7%, from $24.5 million in the twelve months ended January 31, 2004. The decrease was primarily due to the sales of the Tempe, Arizona and San Diego, California properties during the first quarter of fiscal year 2005 and impairment charges of $458,000 recognized during fiscal year 2004.

Total interest expense for the twelve months ended January 31, 2005 was $2.3 million, a decrease of $1.1 million, or 33.0%, from $3.4 million in the twelve months ended January 31, 2004. Interest on mortgage notes payable for the twelve months ended January 31, 2005 was $2.1 million, a decrease of $675,000, or 24.4%, from $2.8 million in the twelve months ended January 31, 2004. The decrease is primarily due to the satisfaction of the mortgage notes payable secured by the Tempe, Arizona and San Diego, California properties in connection with the disposition of those properties. Interest on notes payable to banks for the twelve months ended January 31, 2005 was $24,000, a decrease of $30,000, or 56.2%, from $54,000 in the prior fiscal year, due to the Trust satisfying its term loan in full in March 2003 and its line of credit in full in August 2003. Interest on notes payable to related parties decreased 77.0%, or $419,000, to $125,000 from $544,000 during the years ended January 31, 2005 and 2004, respectively. The decrease is primarily due to payments totaling $6.2 million on notes due to affiliates of Mr. Wirth in connection with the sales of the Tempe, Arizona and San Diego, California properties during the first quarter of fiscal year 2005.

Real estate and personal property taxes, insurance and ground rent decreased $340,000, or 20.4%, to $1.3 million from $1.7 million in comparing the twelve months ended January 31, 2005 and 2004, respectively. Real estate and personal property taxes and property insurance decreased due to the sales of the Tempe, Arizona and San Diego, California properties during the first quarter of fiscal year 2005 and the sale of the Buena Park, California property during the third quarter of fiscal year 2004.

Hotel property depreciation for the twelve months ended January 31, 2005 compared to 2004 decreased approximately $222,000, or 7.5%, to $2.8 million from $3.0 million, respectively. The decrease was primarily due to the sale of certain hotel properties.

The Trust had income before minority interest, income taxes and cumulative effect of adoption of accounting principle of $2.6 million for the twelve months ended January 31, 2005, compared to a loss before minority interest of $3.6 million in the prior year. After deducting the income allocated to the minority interest of $1.4 million, taxes of $160,000 and the cumulative effect of adoption of accounting principle of $854,000, the Trust had net income attributable to Shares of Beneficial Interest of approximately $240,000. This represented an increase of approximately $2.7 million in net income attributable to Shares of Beneficial Interest comparing the twelve months ended January 31, 2005 and 2004. Basic and diluted net income per share was $0.10 for the twelve months ended January 31, 2005, compared to a loss of $1.27 for 2004.

LIQUIDITY AND CAPITAL RESOURCES

Overview

The Trust’s principal source of cash to meet its cash requirements, including distributions to its shareholders, is its share of the Partnership’s cash flow and its direct ownership of the Yuma, Arizona property. The Partnership’s principal source of revenue is hotel operations for the four hotel properties it owns. The Trust’s liquidity, including its ability to make distributions to its shareholders, will depend upon the ability of itself and the Partnership to generate sufficient cash flow from hotel operations.

Hotel operations are significantly affected by occupancy and room rates at the Hotels, which have improved over the prior three fiscal years, our ability to manage costs, and changes in the number of available suites caused by acquisition and disposition activities. Results are also significantly impacted by overall economic conditions and conditions in the travel industry. Unfavorable changes in these factors could negatively impact hotel room demand and pricing which would reduce our profit margins on rented suites.

We anticipate that better overall economic conditions will result in increased business and leisure travel and support higher room rates, and therefore higher operating margins. Challenges in fiscal year 2007 are expected to include continued competition for group business in the markets in which we operate and the Trust’s ability to increase room rates while maintaining market share.

Net cash provided by operating activities totaled $878,000, $660,000, and $88,000 for the years ended January 31, 2006, 2005 and 2004, respectively. The increase in 2006 as compared to 2005 was primarily due to increased operating income due to better hotel performance. The increase in 2005 as compared to 2004 was primarily due to the disposition of underperforming properties resulting in improved operating results.

Net cash (used in) provided by investing activities totaled $(65,000), $8.0 million, and $10.2 million for the years ended January 31, 2006, 2005 and 2004, respectively. The decrease in 2006 as compared to 2005 and 2004 was due to fewer dispositions during fiscal year 2006.

18

Net cash used in financing activities totaled $(780,000), $(8.6) million, and $(10.4) million for the years ended January 31, 2006, 2005 and 2004, respectively. The increase in 2006 as compared to 2005 was primarily due to the San Diego mortgage payoff in fiscal year 2005. The increase in 2005 as compared to 2004 was primarily due to reduced net payments on notes payable to Mr. Wirth and his affiliates during fiscal year 2005.

The Trust received $1.2 million in proceeds from the sales of hotel properties in fiscal year 2006. The Trust used these proceeds to fund operations and capital improvements.

The Trust received $9.4 million in proceeds for the sales of hotel properties in fiscal year 2005. The Trust used $4.8 million of these proceeds to satisfy a mortgage note payable, $1.4 million to satisfy related party notes and interest payable, and retained the remaining proceeds to reduce trade payables and to fund future operations and capital improvements.

The Trust received $12.2 million in proceeds for the sales of hotel properties in fiscal year 2004. The Trust used $3.0 million of these proceeds to satisfy a mortgage note payable, $4.4 million to satisfy related party notes payable, $3.0 million to satisfy bank notes payable and the remaining proceeds to fund operations.

As of January 31, 2006, the Trust has no commitments for capital expenditures beyond a 4% reserve for refurbishment and replacements that is set aside annually, as described below.

The Trust is obligated under loan agreements relating to four of its hotels to deposit 4% of the individual hotel’s room revenue into an escrow account to be used for capital expenditures. These accounts are restricted by the mortgage lenders. As of January 31, 2006, $226,294 was held in these accounts and is reported on the Trust’s Consolidated Balance Sheet as “Restricted Cash.” The accounts are required to be used for capital improvements to the Hotels and refurbishment and replacement of furniture, fixtures and equipment. During the twelve months ended January 31, 2006 and 2005, the Hotels spent approximately $1.2 million and $1.3 million, respectively, for capital expenditures. The Trust considers the majority of these improvements to be revenue producing. Therefore, these amounts have been capitalized and are being depreciated over their estimated useful lives. The Trust plans to spend approximately $710,000 for capital expenditures in fiscal year 2007. The Hotels also spent approximately $1.4 million during both fiscal years 2006 and 2005 on repairs and maintenance and these amounts have been charged to expense as incurred.

The Trust has minimum debt payments of $1.9 million and $1.1 million due during fiscal years 2007 and 2008, respectively. The Trust plans to renew its bank line of credit when it matures during fiscal year 2007. The Trust believes it can satisfy its remaining obligations during fiscal years 2007 and 2008 using revenue generated by the Hotels’ operations.

Management believes that cash on hand, future cash receipts from operations, proceeds from condo-hotel conversions and borrowings from affiliates in fiscal year 2007 will be sufficient to meet the Trust’s obligations as they become due for the next twelve months.

The Trust may seek to negotiate additional credit facilities or issue debt instruments. Any debt incurred or issued by the Trust may be secured or unsecured, long-term, medium-term or short-term, bear interest at a fixed or variable rate and be subject to such other terms as the Trust considers prudent.

The Trust will acquire or develop additional hotels only as suitable opportunities arise, and the Trust will not undertake acquisition or redevelopment of properties unless adequate sources of financing are available. Funds for future acquisitions or development of hotels are expected to be derived, in whole or in part, from borrowings or from the proceeds of additional issuances of Shares of Beneficial Interest or other securities. However, there can be no assurance that the Trust will successfully acquire or develop additional hotels or that proceeds from borrowings or issuances of Shares of Beneficial Interest will be available or in amounts and on terms sufficient to allow such transactions.

FUTURE POSITIONING

The Trust’s management has identified condo-hotel conversions and sales as an opportunity for the Trust. The condo-hotel concept has become increasingly popular throughout the country, and may have the potential to eclipse time-share or fractional ownership as the preferred vacation, second or third home ownership vehicle. The Trust, through its wholly-owned subsidiary, InnSuites Hotels, is currently pursuing condo-hotel ownership primarily for its Arizona locations. In the event this concept proves to be feasible for its current hotel properties, the Trust may realize condominium sales revenue and revenue from long-term management and trademark agreements with potential homeowners’ associations and/or future condominium owners.

CONTINUED LISTING WITH THE AMERICAN STOCK EXCHANGE

On June 13, 2003, the Trust received notice from the American Stock Exchange (“Amex”) indicating that the Trust failed to meet certain of Amex’s continued listing standards as set forth under Section 1003(a) of the Amex Company Guide. On December 10, 2004, the shareholders of the Trust approved several proposals relating to the Trust’s plan to return to compliance with Amex’s continued listing standards. On January 4, 2005, the Board of Trustees approved the implementation of the proposals. The proposals were consummated on January 31, 2005.

In total, on January 31, 2005, the Trust issued 13,005,089 Shares of Beneficial Interest in the Trust of which 6,602,695 returned to the Trust as treasury shares and 6,402,394 remained outstanding following implementation of the proposals. Mr. Wirth and his affiliates, through these transactions, received 5,182,186 Shares of Beneficial Interest in the Trust.

As of January 31, 2006, the Trust has total shareholders’ equity of $6.7 million and is compliant with Amex’s continued listing standards.

SHARE REPURCHASE PROGRAM

On January 2, 2001, the Board of Trustees approved a share repurchase program under Rule 10b-18 of the Securities Exchange Act of 1934, as amended, for the purchase of up to 250,000 limited partnership units in the Partnership and/or Shares of Beneficial Interest in open market or privately negotiated transactions. Additionally, on September 10, 2002, the Board of Trustees approved the purchase of up to 350,000 additional limited partnership units in the Partnership and/or Shares of Beneficial Interest in open market or privately negotiated transactions. On August 18, 2005, the Board of Trustees approved the purchase of up to 350,000 additional limited partnership units in the Partnership and/or Shares of Beneficial Interest in open market or privately negotiated transactions. Acquired Shares of Beneficial Interest will be held in treasury and will be available for future acquisitions and financings and/or for awards granted under the InnSuites Hospitality Trust 1997 Stock Incentive and Option Plan. During fiscal year 2006, the Trust acquired 20,100 Shares of Beneficial Interest in open market transactions at an average price of $1.34 per share and 112,253 Shares of Beneficial Interest in privately-negotiated transactions at an average price of $1.32. The Trust intends to continue repurchasing Shares of Beneficial Interest in compliance with applicable legal and American Stock Exchange requirements.

OFF-BALANCE SHEET FINANCINGS AND LIABILITIES

Other than lease commitments, legal contingencies incurred in the normal course of business and employment contracts for key employees, the Trust does not have any off-balance sheet financing arrangements or liabilities. The Trust does not have any majority-owned subsidiaries that are not included in the consolidated financial statements. See “Item 7 - Management’s Discussion and Analysis of Financial Condition and Results of Operations - Accounting Matters” below for a discussion of new accounting interpretations with respect to variable interest entities and the impact of such interpretations on the Trust.

CONTRACTUAL OBLIGATIONS

The following summarizes our contractual obligations at January 31, 2006, and the effect such obligations are expected to have on our liquidity and cash flow in future periods:

CONTRACTUAL OBLIGATIONS	PAYMENTS DUE BY PERIOD TOTAL	LESS THAN 1 YEAR	1-3 YEARS	3-5 YEARS	THEREAFTER
Mortgage notes payable, notes payable to banks, other notes payable and notes and advances payable to related parties	$ 21,251,565	$ 1,923,896	$ 2,243,933	$ 6,016,982	$ 11,066,754
Operating leases	7,031,830	193,018	386,036	386,036	6,066,740
TOTAL	$ 28,283,395	$ 2,116,914	$ 2,629,969	$ 6,403,018	$ 17,133,494

The Trust expects to incur interest expense in relation to the notes included in the above table as summarized below:

	TOTAL	LESS THAN 1 YEAR	1-3 YEARS	3-5 YEARS	THEREAFTER
	$ 7,973,947	$ 1,707,938	$ 3,086,963	$ 2,213,515	$ 965,531

InnSuites Hotels has entered into franchise arrangements with Best Western International, a third party, for four of the hotel properties. These agreements provide for fees to be paid by InnSuites Hotels based on revenues and reservations received, and contain no minimum payment provisions.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The Trust believes that the policies it follows for the valuation of its hotel properties, which constitute the majority of Trust assets, are its most critical policies. The Trust applies SFAS No. 144 “Accounting for the Impairment or Disposal of Long-Lived Assets,” to determine when it is necessary to test an asset for recoverability. On an events and circumstances basis, the Trust reviews the carrying value of its hotel properties both held for use and held for sale. The Trust will record an impairment loss and reduce the carrying value of a property when anticipated undiscounted future cash flows and/or a current appraisal of the property do not support its carrying value. In cases where the Trust does not expect to recover the carrying cost of hotel properties held for use, it will reduce the carrying value to the fair value of the hotel, as determined by a current appraisal. In cases where the Trust does not expect to recover the carrying cost of hotel properties held for sale, it will reduce the carrying value to the sales price less costs to sell. The Trust did not recognize impairment expense in fiscal year 2006 or 2005. For the twelve months ended January 31, 2004, the Trust recorded impairment losses of $458,000. As of January 31, 2006, the Trust management does not believe that the carrying values of any of its hotel properties are impaired.

ACCOUNTING MATTERS

In December 2004, Statement of Financial Accounting Standards No. 123 (revised 2004) was issued. This Statement is a revision of FASB Statement No. 123, Accounting for Stock Based Compensation, and supercedes APB Opinion No. 25, Accounting for Stock Issued to Employees. This Statement establishes standards for accounting for transactions in which an entity exchanges its equity securities for goods and services. The Trust adopted this Statement during fiscal year 2006. The adoption of this Statement did not affect the Trust's financial results.

In December 2004, the FASB issued Statement of Financial Accounting Standards No. 153, "Exchanges of Nonmonetary Assets, an amendment of APB Opinion No. 29," ("SFAS No. 153"), which is effective for fiscal years beginning after June 15, 2005. SFAS No. 153 replaces APB Opinion No. 29's exceptions to recording these transfers at fair value. SFAS No. 153 is not expected to have a material impact on the Trust's financial statements or results of operations.

In February 2004, the Trust adopted FIN 46R, which amended FIN 46, "Consolidation of Variable Interest Entities," an interpretation of Accounting Research Bulletin No. 51, "Consolidated Financial Statements." FIN 46R requires an existing unconsolidated variable interest entity to be consolidated by its primary beneficiary if the entity does not effectively disperse risk among all parties involved or if other parties do not have significant capital to finance activities without subordinated financial support from the primary beneficiary. The primary beneficiary is the party that absorbs a majority of the entity's expected losses, receives a majority of its expected residual returns, or both, as a result of holding variable interests, which are the ownership, contractual or other pecuniary interests in an entity.

As of February 1, 2004, the Trust recorded a charge for the cumulative effect of a change in accounting principle resulting from its recognition of the $854,000 net stockholder's deficit of the Management Company, which was the Trust's variable interest entity under FIN 46R. The $854,000 charge represented the net effect of the Trust reporting $160,000 in net assets (consisting primarily of receivables) and $1,014,000 in net liabilities (consisting primarily of debt) upon consolidating the financial results of the Management Company.

All revenue and expense items for the Management Company and Licensing Corp. relating to services provided to the Hotels were eliminated when their financial results were consolidated with the Trust's results. Revenues and expenses relating to services provided by the Management Company and Licensing Corp. to hotels not owned by the Trust, however, were not eliminated. Payroll reimbursements shown in the current period represent amounts received from hotels not owned by the Trust.

The effect of consolidating the financial results of the Management Company and Licensing Corp. was accounted for as a cumulative effect of a change in accounting principle. As a result of consolidating the financial results of the Management Company with its results, as of February 1, 2004, the Trust's financial results include a $854,402 charge for the cumulative effect of a change in accounting principle on the Statements of Operations resulting in a reduction in its Stockholders' Equity which represents the aggregate stockholders' deficit reported by the Management Company as of February 1, 2004.

After June 8, 2004, consolidation of the financial results of the Management Company and Licensing Corp. is no longer required by FIN 46R since InnSuites Hotels acquired the management contracts and licensing agreements from the Management Company on that date. See Note 20 to the Trust's Consolidated Financial Statements - "Purchase of Management and Licensing Contracts."

In May 2005, the FASB issued SFAS No. 154, "Accounting Changes and Error Corrections," which replaces APB Opinion No. 20, "Accounting Changes," and SFAS No. 3, "Reporting Accounting Changes in Interim Financial Statements — An Amendment of APB Opinion No. 28." SFAS No. 154 provides guidance on the accounting for and reporting of accounting changes and error corrections. It establishes retrospective application, or the latest practicable date, as the required method for reporting a change in accounting principle (unless a different method is prescribed by the new standard) and the reporting of a correction of an error. SFAS No. 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. The adoption of SFAS No. 154 is not expected to have a material impact on Trust's financial position or results of operations.

INFLATION

The Trust's revenue is based on the underlying Hotel revenue. Therefore, the Trust relies entirely on the performance of the Hotels and InnSuites Hotels' ability to increase revenue to keep pace with inflation. Operators of hotels in general, and InnSuites Hotels in particular, can change room rates quickly, but competitive pressures may limit InnSuites Hotels' ability to raise rates faster than inflation.

FORWARD-LOOKING STATEMENTS

Certain statements in this Form 10-K, including statements containing the phrases “believes,” “intends,” “expects,” “anticipates,” “predicted,” “will be,” “should be,” “looking ahead” or similar words, constitute “forward-looking statements” w the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. The Trust intends that such forward-looking statements be subject to the safe harbors created by such Acts. These forward-looking statements include statements regarding the intent, belief or current expectations of the Trust, its Trustees or its officers in respect of (i) the declaration or payment of dividends; (ii) the leasing, management or operation of the Hotels; (iii) the adequacy of reserves for renovation and refurbishment; (iv) the Trust’s financing plans; (v) the Trust’s position regarding investments, acquisitions, developments, financings, conflicts of interest and other matters; (vi) the Trust’s plans and expectations regarding condo-hotel conversions; and (vii) trends affecting the Trust’s or any Hotel’s financial condition or results of operations.

These forward-looking statements reflect the Trust's current views in respect of future events and financial performance, but are subject to many risks and factors relating to the operations and business environment of the Hotels which may cause the actual results of the Trust to differ materially from any future results expressed or implied by such forward-looking statements. Examples of such risks include, but are not limited to:

- fluctuations in hotel occupancy rates;
- changes in room rental rates which may be charged by InnSuites Hotels in response to market rental rate changes or otherwise;
- seasonality of our business;
- interest rate fluctuations;
- changes in governmental regulations, including federal income tax laws and regulations;
- competition;
- any changes in the Trust's financial condition or operating results due to acquisitions or dispositions of hotel properties;
- insufficient resources to pursue our current growth strategy;
- concentration of our investments in the InnSuites Hotels® brand;
- loss of franchise contracts;
- real estate and hospitality market conditions;
- hospitality industry factors;
- our ability to meet present and future debt service obligations;
- terrorist attacks or other acts of war;
- outbreaks of communicable diseases;
- natural disasters;
- loss of key personnel;
- local or national economic and business conditions, including, without limitation, conditions which may affect public securities markets generally, the hospitality industry or the markets in which the Trust operates or will operate; and
- uncertainties the Trust might encounter in changing from a REIT to a tax-paying entity.

The Trust does not undertake any obligation to update publicly or revise any forward-looking statements whether as a result of new information, future events or otherwise. Pursuant to Section 21E(b)(2)(E) of the Securities Exchange Act of 1934, the qualifications set forth hereinabove are inapplicable to any forward-looking statements in this Form 10-K relating to the operations of the Partnership.

Item 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Trust is exposed to interest rate risk primarily as a result of its mortgage notes payable, notes payable to banks, other notes payable and notes and advances payable to related parties. The proceeds from these loans were used to maintain liquidity, fund capital expenditures and expand the Trust's real estate investment portfolio and operations. The Trust's interest rate risk management objective is to limit the impact of interest rate changes on earnings and cash flow and to lower its overall borrowing costs. To achieve its objectives, the Trust borrows using fixed rate debt, when possible. The Trust could enter into derivative financial instruments such as interest rate swaps, caps and treasury locks in order to mitigate its interest rate risk on a related financial instrument. To date, the Trust has not entered into any such derivative transactions.

The Trust's interest rate risk is monitored using a variety of techniques. The table below presents the principal amounts, weighted average interest rates, fair value and other terms required, by year of expected maturity, in order to evaluate the expected cash flow and sensitivity to interest rate changes.

	Fiscal							
Debt Type	**2007**	**2008**	**2009**	**2010**	**2011**	**Thereafter**	**Total**	**Fair Value**
Fixed rate debt (1)	$ 1,313,116	984,505	1,008,190	1,061,041	1,125,978	11,066,754	16,559,584	17,437,083
Average interest rate	8.30%	7.95%	7.97%	7.98%	8.00%	8.02%	8.04%	7.50%
Variable rate debt (1)	$ 610,780	120,713	130,525	3,829,963	—	—	4,691,981	4,769,691
Interest rate available on January 31, 2006	8.53%	8.50%	8.50%	8.50%	8.50%	8.50%	8.50%	8.53%

(1) The fair value of fixed rate debt and variable rate debt were determined based on current rates offered for fixed rate debt and variable rate LIBOR debt with similar risks and maturities.

The table incorporates only those exposures that exist as of January 31, 2006 and does not consider those exposures or positions that could arise after that date. Moreover, because firm commitments are not represented in the table above, the information presented therein has limited predictive value. As a result, the Trust's interest rate fluctuations will depend on the exposures that arise during any particular period and future interest rates.

Item 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

INNSUITES HOSPITALITY TRUST
LIST OF CONSOLIDATED FINANCIAL STATEMENTS AND SCHEDULES

The following consolidated financial statements of InnSuites Hospitality Trust are included in Item 8:

The following financial statement schedules of InnSuites Hospitality Trust are included in Item 8:

All other schedules are omitted, as the information is not required or is otherwise furnished.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and Board of Trustees of
InnSuites Hospitality Trust
Phoenix, Arizona:

We have audited the accompanying consolidated balance sheets of InnSuites Hospitality Trust and subsidiaries as of January 31, 2006 and 2005, and the related consolidated statements of operations, shareholders' equity (deficit) and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion of these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). 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 examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of InnSuites Hospitality Trust and subsidiaries as of January 31, 2006 and 2005, 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.

/s/EPSTEIN, WEBER & CONOVER, PLC

Scottsdale, Arizona
April 24, 2006

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and Board of Trustees of
InnSuites Hospitality Trust
Phoenix, Arizona:

Our audits on the 2006 and 2005 statements were conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States) and were made for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The related consolidated supplemental schedules III and IV are presented for purposes of complying with the Securities and Exchange Commission's rules and are not a part of the basic consolidated financial statements. These schedules have been subjected to the auditing procedures applied in our audits of the basic consolidated financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic consolidated financial statements taken as a whole.

/s/EPSTEIN, WEBER & CONOVER, PLC

Scottsdale, Arizona
April 24, 2006

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and Board of Trustees
InnSuites Hospitality Trust and Subsidiaries
Phoenix, Arizona

We have audited the accompanying consolidated balance sheet of InnSuites Hospitality Trust (the "Trust") and Subsidiaries as of January 31, 2004 and the related consolidated statements of operations, shareholders' (deficit) equity and cash flows for the year ended January 31, 2004. These financial statements are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). 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 examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of InnSuites Hospitality Trust and Subsidiaries as of January 31, 2004 and the results of their operations and their cash flows for each of the two years in the period ended January 31, 2004 in conformity with U.S. generally accepted accounting principles.

/s/ McGladrey & Pullen, LLP

Phoenix, Arizona
March 12, 2004

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and Board of Trustees
InnSuites Hospitality Trust and Subsidiaries
Phoenix, Arizona

Our audits on the 2004 financial statements were conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States) and were made for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The related consolidated supplemental schedules III and IV are presented for purposes of complying with the Securities and Exchange Commission's rules and are not a part of the basic consolidated financial statements. The schedules have been subjected to the auditing procedures applied in our audits of the basic consolidated financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic consolidated financial statements taken as a whole.

/s/ McGladrey & Pullen, LLP

Phoenix, Arizona
March 12, 2004

INNSUITES HOSPITALITY TRUST AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

		JANUARY 31	
		2006	**2005**
ASSETS			
Current Assets:			
Cash and Cash Equivalents	$	34,251	1,343
Restricted Cash		226,294	250,642
Accounts Receivable, including $14,828 and $144,928 from related parties, net of Allowance for Doubtful Accounts of $112,000 and $278,000, respectively		531,961	969,751
Prepaid Expenses and Other Current Assets		494,829	510,864
Total Current Assets		1,287,335	1,732,600
Hotel Properties, net		30,215,391	31,190,139
Hotel Properties Held for Sale, net		—	3,121,235
Deferred Finance Costs, Long-Term Portion		175,645	226,560
Deposits, Long-Term		14,987	14,987
Deferred Income Tax Benefit		259,000	170,000
TOTAL ASSETS	$	31,952,358	36,455,521
LIABILITIES AND SHAREHOLDERS' EQUITY			
LIABILITIES			
Current Liabilities :			
Accounts Payable and Accrued Expenses, including $95,418 and $153,811 accrued interest and payables to related parties as of January 31, 2006 and 2005, respectively	$	2,594,733	2,762,693
Purchase Deposit from Related Party		—	700,000
Notes Payable to Banks		500,000	500,000
Current Portion of Mortgage Notes Payable		879,265	1,060,827
Current Portion of Other Notes Payable		121,558	78,975
Current Portion of Notes Payable to Related Parties		428,989	33,735
Total Current Liabilities		4,524,545	5,136,230
Mortgage Notes Payable		19,029,612	22,946,618
Notes Payable to Related Parties		85,717	59,777
Other Notes Payable		206,424	169,438
TOTAL LIABILITIES		23,846,298	28,312,063
MINORITY INTEREST IN PARTNERSHIP		1,388,132	1,878,824
SHAREHOLDERS' EQUITY			
Shares of Beneficial Interest, without par value; unlimited authorization; 9,145,365 and 8,719,649 shares issued and outstanding at January 31, 2006 and 2005, respectively		17,155,106	16,568,246
Treasury Stock, 7,494,578 and 7,391,825 shares held at January 31, 2006 and 2005, respectively		(10,437,178)	(10,303,612)

TOTAL SHAREHOLDERS' EQUITY		6,717,928	6,264,634
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$	31,952,358	36,455,521

See accompanying notes to unaudited
consolidated financial statements

INNSUITES HOSPITALITY TRUST AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS

	YEARS ENDED JANUARY 31,		
	2006	**2005**	**2004**
REVENUE			
Room	$ 16,029,694	$ 17,729,550	$ 22,026,498
Food and Beverage	1,122,191	1,238,808	1,363,216
Telecommunications	56,804	99,894	154,231
Other	462,462	736,873	667,383
Management and Trademark Fees, including $209,862, $115,105 and $0 from related parties for 2006, 2005 and 2004, respectively	382,260	278,888	—
Payroll Reimbursements, including $2,471,324, $2,191,474 and $0 from related parties for 2006, 2005 and 2004, respectively	3,195,428	2,791,174	—
TOTAL REVENUE	21,248,839	22,875,187	24,211,328
OPERATING EXPENSES			
Room	4,222,369	5,010,738	6,019,634
Food and Beverage	1,168,246	1,226,074	1,323,480
Telecommunications	153,313	226,559	311,408
General and Administrative (includes $0, $0 and $741,537 of management and licensing fees to related parties for 2006, 2005 and 2004, respectively)	3,948,539	4,445,613	4,703,160
Sales and Marketing	1,362,805	1,642,232	2,109,528
Repairs and Maintenance	1,427,470	1,387,407	1,797,719
Hospitality	697,625	827,166	1,066,854
Utilities	1,166,233	1,232,940	1,686,040
Hotel Property Depreciation	2,118,492	2,755,499	2,977,583
Real Estate and Personal Property Taxes, Insurance and Ground Rent	1,258,380	1,329,463	1,669,510
Other	180,590	221,969	360,490
Payroll Costs Related to Management Contracts	3,195,428	2,791,174	—
Loss on Impairment of Hotel Property	—	—	458,401
TOTAL OPERATING EXPENSES (includes $0, $0 and $7,389,988 in contract labor expense to related party for 2006, 2005 and 2004, respectively)	20,899,490	23,096,834	24,483,307
OPERATING INCOME (LOSS)	349,349	(221,647)	(272,479)
Interest Income	2,134	7,517	981
Other Income	59,677	—	—
Gain on Disposition of Hotels	1,847,425	5,113,540	—
TOTAL OTHER INCOME	1,909,236	5,121,057	981
Interest on Mortgage Notes Payable	1,846,801	2,089,708	2,764,876
Interest on Notes Payable to Banks	28,322	23,659	53,984
Interest on Notes Payable and Advances Payable to Related Parties	16,769	125,336	544,069
Interest on Other Notes Payable	17,205	20,878	10,290
TOTAL INTEREST EXPENSE	1,909,097	2,259,581	3,373,219
	349,488	2,639,829	(3,644,717)

INCOME (LOSS) BEFORE MINORITY INTEREST, INCOME TAXES AND CUMULATIVE EFFECT OF ADOPTION OF ACCOUNTING PRINCIPLE						
LESS MINORITY INTEREST		(267,265)		1,384,985		(1,050,400)
Income Tax Provision		(75,175)		(160,000)		—
INCOME (LOSS) ATTRIBUTABLE TO SHARES OF BENEFICIAL INTEREST BEFORE CUMULATIVE EFFECT OF ADOPTION OF ACCOUNTING PRINCIPLE		541,578		1,094,844		(2,594,317)
CUMULATIVE EFFECT OF ADOPTION OF ACCOUNTING PRINCIPLE		—		(854,402)		—
INCOME (LOSS) ATTRIBUTABLE TO SHARES OF BENEFICIAL INTEREST	$	541,578	$	240,442	$	(2,594,317)
INCOME (LOSS) PER SHARE BEFORE CUMULATIVE EFFECT OF ADOPTION OF ACCOUNTING PRINCIPLE- Basic	$	0.06	$	0.45	$	(1.27)
NET LOSS FROM CUMULATIVE EFFECT OF ADOPTION OF ACCOUNTING PRINCIPLE - Basic		—		(0.35)		—
NET INCOME (LOSS) PER SHARE - Basic	$	0.06	$	0.10	$	(1.27)
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING - Basic		9,096,338		2,424,837		2,035,200
INCOME (LOSS) PER SHARE BEFORE CUMULATIVE EFFECT OF ADOPTION OF ACCOUNTING PRINCIPLE- Diluted	$	0.02	$	0.45	$	(1.27)
NET LOSS FROM CUMULATIVE EFFECT OF ADOPTION OF ACCOUNTING PRINCIPLE - Diluted		—		(0.35)		—
NET INCOME (LOSS) PER SHARE - Diluted	$	0.02	$	0.10	$	(1.27)
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING - Diluted		13,341,783		2,424,837		2,035,200
CASH DIVIDENDS PER SHARE	$	.01	$	.01	$	.02

See accompanying notes to
consolidated financial statements

INNSUITES HOSPITALITY TRUST AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (DEFICIT)
FOR THE YEARS ENDED JANUARY 31, 2006, 2005 AND 2004

BALANCE, JANUARY 31, 2003	$	(1,250,182)
Net Loss Attributable to Shares of Beneficial Interest		(2,594,317)
Dividends		(40,986)
Purchase of Treasury Stock		(29,095)
Issuance of Shares of Beneficial Interest for Compensation		99,680
Related Party Fees Forgiven		530,721
Accrued Rent Forgiven by the Partnership		1,518,834
Proceeds from Sale of Hotel Property to Related Party in Excess of Carrying Value		192,910
Distribution to Minority Interest Holders		(128,049)
Reallocation of Minority Interest		126,885
BALANCE, JANUARY 31, 2004		(1,573,599)
Net Income Attributable to Shares of Beneficial Interest		240,442
Dividends		(23,220)
Purchase of Treasury Stock		(225,917)
Shares of Beneficial Interest issued for Services Received		49,280
Shares of Beneficial Interest issued to Satisfy Notes Payable to Related Parties		690,820
Shares of Beneficial Interest issued to Purchase Management and Licensing Contracts		155,000
Shares of Beneficial Interest issued to Satisfy Advances Payable to the Partnership		3,661,659
Shares of Beneficial Interest issued to Purchase Yuma Hospitality Minority Interest		2,766,515
Purchase of Yuma Hospitality Minority Interest Above Carrying Value		1,177,425
Purchase of Partnership Units Above Carrying Value		98,684
Reallocation of Minority Interest		(752,455)
BALANCE, JANUARY 31, 2005		6,264,634
Net Income Attributable to Shares of Beneficial Interest		541,578
Dividends		(91,450)
Purchase of Treasury Stock		(175,442)
Shares of Beneficial Interest issued for Services Received		37,888
Partnership Interest Acquired with Shares of Beneficial Interest		213,202
Reallocation of Minority Interest		(72,482)
BALANCE, JANUARY 31, 2006	$	6,717,928

See accompanying notes to
consolidated financial statements

INNSUITES HOSPITALITY TRUST AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOW

	YEARS ENDED JANUARY 31, 2006	2005	2004
CASH FLOW FROM OPERATING ACTIVITIES			
Net Income (Loss) Attributable to Shares of Beneficial Interest	$ 541,578	$ 240,442	$ (2,594,317)
Adjustments to Reconcile Net Income (Loss) Attributable to Shares of Beneficial Interest to Net Cash Provided by Operating Activities:			
Cumulative Effect of Adoption of Accounting Principle	—	854,402	—
Net Income from Variable Interest Entities	—	352,882	—
Issuance of Shares for Management and Licensing Contracts	—	155,000	—
Impairment of Hotel Property	—	—	458,401
Provision for Uncollectible Receivables	354,165	377,465	198,448
Minority Interest	(267,265)	1,032,103	(1,050,400)
Hotel Property Depreciation	2,118,492	2,755,499	2,977,583
Deferred Income Taxes	(89,000)	(170,000)	—
(Gain) Loss on Disposal Sale of Hotel Property	(1,834,080)	(4,999,797)	124,310
Amortization of Deferred Loan Fees	36,373	38,312	49,036
Capital Contribution from Waived Management and Licensing Fee Expense	—	—	530,721
Changes in Assets and Liabilities:			
(Increase) Decrease in Prepaid Expenses and Other Assets	(57,734)	311,781	126,318
Decrease (Increase) in Accounts Receivable	134,808	(439,814)	(507,907)
Increase in Purchase Deposit from Related Party	—	700,000	—
(Decrease) in Accounts Payable and Accrued Expenses	(59,451)	(547,850)	(224,509)
NET CASH PROVIDED BY OPERATING ACTIVITIES	877,886	660,425	87,684
CASH FLOW FROM INVESTING ACTIVITIES			
Sale of Hotel Properties	1,190,192	9,377,138	12,150,503
Improvements and Additions to Hotel Properties	(1,272,259)	(1,308,008)	(1,863,893)
Change in Restricted Cash	17,311	(113,852)	(91,003)
NET CASH (USED IN) PROVIDED BY INVESTING ACTIVITIES	(64,756)	7,955,278	10,195,607
CASH FLOW FROM FINANCING ACTIVITIES			
Principal Payments on Mortgage Notes Payable	(931,386)	(6,087,771)	(4,306,890)
Payments on Notes Payable to Banks	(2,217,000)	(720,000)	(3,087,250)
Borrowings on Notes Payable to Banks	2,217,000	500,000	440,000
Repurchase of Partnership Units	(774)	(453,223)	(337)
Repurchase of Treasury Stock	(30,191)	(113,517)	(29,095)
Payment of Dividends	(91,450)	(23,220)	(40,986)
Distributions to Minority Interest Holders	—	(85,683)	—
Payments on Notes and Advances Payable to Related Parties	(35,806)	(1,740,299)	(4,773,927)

Borrowings on Notes and Advances Payable to Related Parties	400,000	198,000	1,507,750
Payments on Other Notes Payable	(90,615)	(88,647)	(81,075)
NET CASH USED IN FINANCING ACTIVITIES	(780,222)	(8,614,360)	(10,371,810)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	32,908	1,343	(88,519)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	1,343	—	88,519
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 34,251	$ 1,343	$ —

See accompanying notes to
consolidated financial statements

33

INNSUITES HOSPITALITY TRUST AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
AS OF AND FOR THE YEARS ENDED JANUARY 31, 2006, 2005 AND 2004

1. NATURE OF OPERATIONS AND BASIS OF PRESENTATION

InnSuites Hospitality Trust (the "Trust") owns, as of January 31, 2006, directly and through a partnership interest, five hotels with an aggregate of 843 suites in Arizona, southern California and New Mexico (the "Hotels"). The Hotels operate as InnSuites Hotels.

Prior to February 1, 2004, the Trust operated as a self-managed and self-administered "umbrella partnership real estate investment trust ("REIT")," with operations through an operating partnership, RRF Limited Partnership, a Delaware limited partnership (the "Partnership"). Effective February 1, 2004, the Trust terminated its election to be taxed as a REIT. The Trust is the sole general partner of the Partnership and owned 69.14% and 64.75% of the Partnership as of January 31, 2006 and 2005, respectively. The Trust's weighted average ownership for the years ended January 31, 2006, 2005, and 2004 was 67.87%, 57.00% and 51.12%, respectively. The Partnership owns four of the hotel properties and incurs the related expenses. The Trust owns and operates the Yuma, Arizona hotel property directly, which it acquired from the Partnership on January 31, 2005. See Note 21 -"Compliance with the American Stock Exchange Continued Listing Standards." Prior to May 1, 2004, the Hotels were leased to InnSuites Hotels, Inc. ("InnSuites Hotels"), a wholly-owned subsidiary of the Trust. Subsequent to May 1, 2004, the Trust and the Partnership operate the Hotels owned by each of them. Prior to June 8, 2004, InnSuites Hotels held the franchise agreement for each Hotel and contracted with Suite Hospitality Management, Inc. (the "Management Company") for certain property management services and employment services. Until July 2, 2003, the Management Company was owned 9.8% by the James F. Wirth ("Mr. Wirth"), Chairman, President and Chief Executive Officer of the Trust. On June 8, 2004, the Trust purchased the "InnSuites" trademarks and tradenames and related licensing agreements and acquired the management agreements with the Management Company. See Note 20 - "Purchase of Management and Licensing Contracts."

After June 8, 2004, InnSuites Hotels provides hotel management services to the Hotels, as well as four hotels featuring 544 suites owned by affiliates of Mr. Wirth and one unrelated hotel property featuring 131 suites. Under the management agreements, InnSuites Hotels provides the personnel at the hotels, the expenses of which are reimbursed at cost, and manages the hotels' daily operations. All such expenses and reimbursements between InnSuites Hotels and the Partnership have been eliminated in consolidation. InnSuites Hotels received 2.5% of total revenue from the Hotels owned by the Partnership and the Trust in exchange for management services during fiscal year 2006 and 2.0% of room revenue during fiscal year 2005. During the second half of fiscal year 2006, InnSuites Hotels also received an accounting fee between $1,000 and $2,000 per month under these agreements. These agreements expire on January 31, 2008. InnSuites Hotels received between 1% and 2% of room revenue from the Hotels owned by affiliates of Mr. Wirth in exchange for management services during fiscal years 2006 and 2005 and between $1,000 and $2,000 per month for accounting services during fiscal year 2006. These agreements require that these hotels pay 2% of room revenue, unless these hotels fail to reach 80% of their budgeted profit, at which point the fees are reduced to 1% of room revenue. Effective February 1, 2006, these agreements are fixed at 2.0% of room revenue plus $2,000 per month for accounting services. These agreements expire on February 1, 2007 and may be cancelled by either party with 90-days notice or 30-days notice in the event the property changes ownership. InnSuites Hotels received 5% of total revenue from the unrelated hotel in San Diego, California in exchange for management services during fiscal year 2006. This agreement expires on March 31, 2007, and may be cancelled by either party with 90-days notice or 30-days notice in the event the property changes ownership.

After June 8, 2004, InnSuites Hotels owns the "InnSuites" trademark and holds trademark agreements with the Hotels, as well as four hotels featuring 544 suites owned by affiliates of Mr. Wirth and two unrelated hotel properties featuring 307 suites. InnSuites Hotels received 1.25% (2.5% for the hotel which does not carry a third-party franchise) of total revenue from the Hotels owned by the Partnership and the Trust in exchange for use of the “InnSuites” trademark during fiscal year 2006 and 1.0% (2.0% for the hotel without a third-party franchise) during fiscal year 2005. The revenue and expenses related to these contracts have been eliminated in consolidation. These agreements expire on January 31, 2007. InnSuites Hotels received between 1% and 2% of room revenue from the Hotels owned by affiliates of Mr. Wirth in exchange for use of the “InnSuites” trademark during fiscal years 2006 and 2005. These agreements require that these hotels pay 2% of room revenue, unless these hotels fail to reach 80% of their budgeted profit, at which point the fees are reduced to 1% of room revenue. Effective February 1, 2006, these fees are fixed at 1.25% of room revenue. These agreements have no expiration date and may be cancelled by either party with 12-months notice or 90-days notice in the event the property changes ownership. InnSuites Hotels received 2% of total revenue from the unrelated hotel in San Diego, California in exchange for trademark licensing services during fiscal years 2006 and 2005. This agreement may be cancelled by either party with 90-days notice. InnSuites Hotels received 0.5% of room revenue from the unrelated hotel in Buena Park, California in exchange for trademark licensing services during fiscal years 2006 and 2005. This agreement has no expiration date and may be cancelled by either party with 30-days notice.

As a REIT, through January 31, 2004, the Trust was prohibited from operating its properties other than through an independent management company or a taxable REIT subsidiary. On June 8, 2004, the management agreements of the Management Company were purchased by the Trust and the Trust began managing the Hotels, certain hotels owned by Mr. Wirth and an unrelated hotel. See Note 20 - “Purchase of Management and Licensing Contracts.”

PARTNERSHIP AGREEMENT

The Partnership Agreement of the Partnership provides for the issuance of two classes of limited partnership units, Class A and Class B. Class A and Class B limited partnership units are identical in all respects, except that each Class A limited partnership unit shall be convertible into one newly-issued Share of Beneficial Interest of the Trust, at any time at the option of the particular limited partner. The Class B limited partnership units may only become convertible with the approval of the Board of Trustees, in its sole discretion. As of January 31, 2006 and 2005, 669,617 and 1,189,386, respectively, Class A limited partnership units were issued and outstanding representing 5.1% and 9.0%, respectively, of the total partnership units. Additionally, as of January 31, 2006 and 2005, 3,407,938 and 3,467,938, respectively, Class B limited partnership units were outstanding to Mr. Wirth and his affiliates, in lieu of the issuance of Class A limited partnership units representing 25.8% and 26.2%, respectively, of the total partnership units. If all of the Class A and B limited partnership units outstanding at January 31, 2006 were converted, the limited partners in the Partnership would receive 4,077,555 Shares of Beneficial Interest of the Trust. As of January 31, 2006 and 2005, the Trust owns 9,133,962 and 8,554,193, respectively, general partner units in the Partnership, representing 69.14% and 64.75%, respectively, of the total partnership units.

BASIS OF PRESENTATION

As sole general partner of the Partnership, the Trust exercises unilateral control over the Partnership, and the Trust owns all of the issued and outstanding classes of shares of InnSuites Hotels. Therefore, the financial statements of the Partnership and InnSuites Hotels are consolidated with the Trust, and all significant intercompany transactions and balances have been eliminated.

RECLASSIFICATIONS

The Trust has reclassified certain balances on the January 31, 2005 balance sheet to conform to the January 31, 2006 presentation of a classified balance sheet. The reclassifications had no effect on net income or total shareholders' equity.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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, the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The Trust’s operations are affected by numerous factors, including the economy, competition in the hotel industry and the effect of the economy on the travel and hospitality industries. The Trust cannot predict if any of the above items will have a significant impact in the future, nor can it predict what impact, if any, the occurrence of these or other events might have on the Trust’s operations and cash flows. Significant estimates and assumptions made by management are used for, but not limited to, the estimated useful lives of long-lived assets and estimates of future cash flows used to test a long-lived asset for recoverability, the fair values of the long-lived assets and the realization of net operating losses.

HOTEL PROPERTIES

Hotel properties are stated at cost and are depreciated using the straight-line method over estimated lives ranging from 5 to 40 years for buildings and improvements and 3 to 10 years for furniture and equipment.

The Trust adopted SFAS No. 144, “Accounting for the Impairment or Disposal of Long-Lived Assets,” in accounting for its hotel properties effective the beginning of fiscal year 2003 and previously applied SFAS No. 121 “Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of”in accounting for its hotel properties in fiscal year 2002. Properties held for sale at the beginning of fiscal year 2003 continued to be accounted for under SFAS No. 121. The adoption of SFAS No. 144 had no significant effect on the financial statements.

Management applies SFAS No. 144 to determine when it is required to test an asset for recoverability of its carrying value. If the carrying amount of an asset exceeds the estimated undiscounted future cash flows over its estimated remaining life, the Trust recognizes an impairment expense to reduce the asset’s carrying value to its fair value. The estimated future cash flows are based upon, among other things, assumptions about expected future operating performance, and may differ from actual cash flows. Long-lived assets evaluated for impairment are analyzed on a property-specific basis independent of the cash flows of other groups of assets. If the sum of the projected undiscounted cash flows (excluding interest) is less than the carrying value of the assets, the assets will be written down to the estimated fair value in the period in which the determination is made. The Trust determines the estimated useful lives of its assets based on the expected future economic benefit of the asset and its ability to hold such assets. Fair value is determined by the most current third-party property appraisal obtained in 2005, if available. Evaluation of future cash flows is based on historical experience and other factors, including certain economic conditions and committed future bookings. Management has determined that no additional impairment of long-lived assets exists during fiscal years 2006 and 2005.

During fiscal year 2004, the Trust recorded impairment charges of $458,000 relating to its Buena Park, California and Tempe, Arizona properties. These charges were recorded to reduce the carrying value of the properties to the sales amount. The Trust recognized the impairment charges at the time it entered in to the sales contracts.

During fiscal years 2006 and 2005, events and circumstances indicated that one of the Trust’s properties held in use should be evaluated for impairment. However, the Trust’s estimated future undiscounted cash flows and the third-party appraisal obtained in fiscal year 2005 of the property both indicated that the value of the property exceeded its carrying value. However, it is possible that future changes in the economic climate or real estate markets may adversely impact the fair values of the hotel properties, resulting in the need for the Trust to recognize an impairment expense to adjust the carrying value of those properties to their fair values.

Gains and losses on sales of properties are recognized at the time of sale or deferred to the extent required by generally accepted accounting principles.

The Trust will classify a hotel property as “held for sale” in the period (generally not to exceed one year) in which (1) it has made the decision to actively seek a buyer of the property and/or (2) a binding agreement to purchase the property has been signed under which the buyer has committed a significant amount of refundable cash and no significant financing contingencies exist which could cause the transaction not to be completed in a timely manner. If these criteria are met, the Trust will record an impairment loss if the fair value less the costs to sell is lower than the carrying amount of the hotel and will cease recording depreciation.

CASH AND CASH EQUIVALENTS

The Trust considers all highly liquid short-term investments with original maturities of three months or less to be cash equivalents.

REVENUE RECOGNITION

Room, food and beverage, telecommunications, management and licensing fees, and other revenue are recognized as earned as services are provided and items are sold. Payroll reimbursements are recorded as personnel services are provided and are not netted with the corresponding payroll expense.

36

RECEIVABLES

Accounts receivable are carried at original amounts less an estimate made for doubtful accounts based on a review of outstanding amounts on a quarterly basis. Management records an allowance for doubtful accounts for 50% of the balances over 90 days and 100% of the balances over 120 days. Accounts receivables are written off when deemed uncollectible. Recoveries, if any, of receivables previously written off are recorded when received. The Trust does not charge interest on accounts receivable balances.

STOCK-BASED COMPENSATION

The Trust applies the provisions of Accounting Principles Board (“APB”) Opinion No. 25, Accounting for Stock Issued to Employees, and provides pro forma net income (loss) disclosures for employee stock based compensation grants as if the fair-value-based method defined in Statement of Financial Accounting Standards (“SFAS”) No. 123R, Accounting for Stock-Based Compensation, had been applied. In accordance with APB Opinion No. 25, stock-based compensation expense is recorded in the statement of operations over the vesting period only if the current estimated market price on the underlying stock on the date an option is granted exceeds the exercise price. The Trust adopted SFAS No. 123 during fiscal year 2006.

No stock-based compensation cost has been recognized for options granted to employees for the years ended January 31, 2006, 2005 and 2004. The following pro forma information presents pro forma net loss information as if compensation expense had been recognized for stock-based compensation as determined under the fair-value-based method prescribed by SFAS No. 123 using the Black-Scholes options pricing model:

	2005	2004
Net income (loss):		
	$ 240,442	$ (2,594,317)
Plus:		
Stock compensation recorded in the statements of operations	$ 49,280	$ —
Minus:		
Total stock-based compensation expense as defined under the fair value method	$ (49,280)	$ —
Pro forma stock compensation expense	$ —	(175)
Pro forma	$ 240,442	$ (2,594,492)
Net income (loss) per share - basic		
As reported	$ 0.10	$ (1.27)
Pro forma	$ 0.10	$ (1.27)

No stock options were issued during the fiscal years ended January 31, 2006, 2005 and 2004. During the second quarter of fiscal year 2006, the Trust accepted the voluntary surrender of all outstanding stock options. The options were surrendered in order to reduce costs and simplify the Trust’s reporting and compliance obligations to the Securities and Exchange Commission and the American Stock Exchange. The Trust made no payments to the holders of the options for their surrender. The Trust has no obligation, explicit or implied, for the surrender of the options, including but not limited to the reissuance of options at some time in the future. As of January 31, 2006, the Trust has no stock options outstanding.

INCOME TAXES

Prior to February 1, 2004, the Trust elected to be taxed as a REIT under Sections 856 through 860 of the U.S. Internal Revenue Code (the "Code"). To qualify as a REIT, the Trust was required to meet a number of organizational and operational requirements, including a requirement that it currently distribute at least 90% of its adjusted taxable income to its shareholders. As a REIT, the Trust was not subject to federal corporate income tax on that portion of its net income that was distributed to shareholders.

Effective February 1, 2004, the Trust relinquished its REIT status. As of that date, any distributions to its shareholders are not deductible for purposes of computing the Trust's taxable income and the Trust will be subject to income tax, including any applicable alternative minimum tax, on its taxable income at regular corporate rates, without offset for distributions of such income to its shareholders.

Susequent to February 1, 2004, the Trust became subject to federal and state corporate income tax and accounts for deferred taxes utilizing a liability method whereby deferred tax assets are recognized for deductible temporary differences and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance when it was determined to be more likely than not that some portion or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities were adjusted for the effects of changes in tax laws and rates on the date of enactment.

DIVIDENDS AND DISTRIBUTIONS

In fiscal years 2006, 2005 and 2004, the Trust paid dividends of $0.01, $0.01 and $0.02, respectively, per share in the fourth quarter. The Trust's ability to pay dividends is largely dependent upon the operations of the hotels.

MINORITY INTEREST

The Trust accounts for minority interest in accordance with EITF Issue No. 94-2 "Treatment of Minority Interests in Certain Real Estate Investments" and EITF Issue No. 95-7 "Implementation Issues Related to the Treatment of Minority Interest in Certain Real Estate Investment Trusts."

Minority interest in the Partnership represents the limited partners' proportionate share of the capital and earnings of the Partnership. Income or loss is allocated to the minority interest based on its weighted average ownership percentage in the Partnership throughout the period, and capital is allocated based on its ownership percentage at year-end. Any difference is recorded as a reallocation of minority interest as a component of shareholders' equity.

INCOME (LOSS) PER SHARE

Basic and diluted income (loss) per Share of Beneficial Interest have been computed based on the weighted-average number of Shares of Beneficial Interest and potentially dilutive securities outstanding during the periods.

For the twelve months ended January 31, 2006, 2005 and 2004, there were Class A and Class B limited partnership units outstanding, which are convertible into Shares of Beneficial Interest of the Trust. Assuming conversion at the beginning of each period, the aggregate weighted-average of these Shares of Beneficial Interest would have been 4,245,445, 5,680,962 and 6,457,165 in addition to the basic shares outstanding for fiscal year 2006, 2005 and 2004, respectively. These Shares of Beneficial Interest issuable upon conversion of the Class A and Class B limited partnership units are anti-dilutive during fiscal years 2005 and 2004 due to the fact that the conversion of these units would result in increased earnings per share. Therefore, they have not been included in the number of issued and outstanding Shares of Beneficial Interest used in the calculation of diluted earnings per share for those years.

For the twelve months ended January 31, 2005 and 2004, 232,600 and 246,000 stock options, respectively, were not included in the computation of diluted earnings per share as their inclusion would have had an antidilutive effect because of the fact that the option exercise prices are greater than the average market price of the Trust's Shares of Beneficial Interest. As of January 31, 2006, there are no stock options outstanding.

FAIR VALUE OF FINANCIAL INSTRUMENTS

For disclosure purposes, fair value is determined by using available market information and appropriate valuation methodologies. Due to their short maturities, cash and cash equivalents are carried at cost, which reasonably approximates fair value.

The fair value of mortgage notes payable, notes payable to banks and notes and advances payable to related parties is estimated by using the current rates which would be available for similar loans having the same remaining maturities.

The carrying value of accounts payable and accrued expenses and other notes payable approximates fair value, due to their short-term nature. See Note 14 - “Fair Value of Financial Instruments.”

NEW ACCOUNTING PRONOUNCEMENTS

In December 2004, Statement of Financial Accounting Standards No. 123 (revised 2004) was issued. This Statement is a revision of FASB Statement No. 123, Accounting for Stock Based Compensation, and supercedes APB Opinion No. 25, Accounting for Stock Issued to Employees. This Statement establishes standards for accounting for transactions in which an entity exchanges its equity securities for goods and services. The Trust adopted this Statement during fiscal year 2006. The adoption of this Statement did not affect the Trust's financial results. The Trust adopted SFAS No. 123R subsequent to the surrender of all outstanding stock options. The Trust applied the modified prospective application.

In May 2005, the FASB issued SFAS No. 154, "Accounting Changes and Error Corrections," which replaces APB Opinion No. 20, "Accounting Changes," and SFAS No. 3, "Reporting Accounting Changes in Interim Financial Statements — An Amendment of APB Opinion No. 28." SFAS No. 154 provides guidance on the accounting for and reporting of accounting changes and error corrections. It establishes retrospective application, or the latest practicable date, as the required method for reporting a change in accounting principle (unless a different method is prescribed by the new standard) and the reporting of a correction of an error. SFAS No. 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. The adoption of SFAS No. 154 is not expected to have a material impact on Trust's financial position or results of operations.

SEGMENT REPORTING

The Trust views its operations as one operating business segment, a hospitality company that owns five hotel properties with an aggregate of 843 suites in Arizona, southern California and New Mexico.

ADVERTISING COSTS

Amounts incurred for advertising costs with third parties are expensed as incurred. Advertising expense totaled approximately $755,000, $785,000 and $2,110,000 for the years ended January 31, 2006, 2005, and 2004, respectively.

3. HOTEL PROPERTIES

As of January 31 of the respective years, hotel properties, and hotel properties held for sale, consisted of the following:

		2006		**2005**
Land	$	2,824,520	$	2,824,520
Building and improvements		33,520,145		32,958,443
Furniture, fixtures and equipment		7,213,866		6,913,030
Total hotel properties		43,558,531		42,695,993
Less accumulated depreciation		(13,343,140)		(11,505,854)
Hotel properties, net	$	30,215,391	$	31,190,139
Hotel properties, held for sale	$	--	$	3,121,235

4. ACQUISITIONS

During the second quarter of fiscal year 2005, the Trust acquired the management and licensing agreements. See Note 20 - "Purchase of Management and Licensing Contracts."

5. MORTGAGE NOTES PAYABLE

At January 31, 2006, the Trust had mortgage notes payable outstanding with respect to each of the Hotels. The mortgage notes payable have various repayment terms and have scheduled maturity dates ranging from July 29, 2009 to May 1, 2016. Weighted average interest rates on the mortgage notes payable for the years ended January 31, 2006, 2005 and 2004 were 8.21%, 8.03% and 7.72%, respectively.

The following table summarized the Trust's mortgage notes payable as of January 31:

	2006	2005
Mortgage note payable, due in variable monthly installments ($38,970 as of January 31, 2006), including interest at prime rate plus 1.0% per year (8.5% as of January 31, 2006), through July 29, 2009, secured by the Tucson St. Mary's property with a carrying value of $9.3 million at January 31, 2006.	$ 4,191,981	$ 4,285,505
Mortgage note payable, due in monthly installments of $48,738, including interest at 8% per year, through May 1, 2016, secured by the Tucson Oracle property with a carrying value of $5.2 million at January 31, 2006.	4,103,465	4,349,266
Mortgage note payable, due in monthly installments of $71,141, including interest at 8.28% per year, through May 11, 2011, secured by the Ontario property with a carrying value of $7.0 million at January 31, 2006.	8,448,212	8,586,467
Mortgage note payable, due in monthly installments of $15,858, including interest at 8.875% per year, through September 1, 2015, secured by the Albuquerque property with a carrying value of $1.8 million at January 31, 2006.	1,232,062	1,309,249
Mortgage note payable, due in monthly installments of $41,168, including interest at 9.25% per year, through August 1, 2011, secured by the Yuma property with a carrying value of $6.6 million at January 31, 2006.	1,933,157	2,186,099
Mortgage note payable, paid in full during fiscal year 2006 in connection with the sale of the Phoenix property.	—	3,290,859
Totals	$ 19,908,877	$ 24,007,445

Mr. Wirth and certain of his affiliates have guaranteed $1,966,579 and $3,738,479 of the mortgage notes payable as of January 31, 2006 and 2005, respectively. The net book value of the properties securing these mortgage notes payable at January 31, 2006 and 2005 was $15,862,000 and $19,441,000, respectively. See Note 9 - "Minimum Debt Payments" for scheduled minimum payments.

6. NOTES PAYABLE TO BANKS

On July 21, 2004, the Trust obtained a bank line of credit secured by a security agreement, business loan agreement and commercial guaranty of the Partnership all dated July 21, 2004. The line of credit is secured by the assets of the Trust alone, which is comprised mainly of its investment in the subsidiaries. Under the terms of the line of credit, the Trust can draw up to $500,000, bearing interest at prime plus 1.5% (8.75% as of January 31, 2006) per annum, and is required to make monthly interest-only payments. The line of credit matured on July 20, 2005. The Trust renewed the line of credit through May 31, 2006. As of January 31, 2006 and 2005, the Trust had drawn the entire $500,000 available under the line of credit.

7. NOTES AND ADVANCES PAYABLE TO RELATED PARTIES

Notes and advances payable to related parties consist of funds provided by Mr. Wirth, certain of his affiliates and other related parties to permit the Trust to repurchase additional general partnership units in the Partnership and to fund working capital and capital improvement needs. The aggregate amounts outstanding to related parties were approximately $515,000 and $94,000 as of January 31, 2006 and 2005, respectively. The notes and advances payable to related parties are as follows as of January 31 of the respective years:

	2006	2005
Note payable to Rare Earth Financial, L.L.C., an affiliate of Mr. Wirth, unsecured and bearing interest at 7% per annum. Due in one installment of accrued interest and unpaid principal on April 15, 2006.	$ 400,000	$ —
Note payable to The Anderson Charitable Remainder Unitrust, an affiliate of Mason Anderson, former Trustee of the Trust, bearing interest at 7% per annum, and secured by Shares of Beneficial Interest in the Trust. Due in monthly principal and interest payments of $1,365 through November 2009.	54,929	—
Note payable to Wayne Anderson, son of Mason Anderson, former Trustee of the Trust, bearing interest at 7% per annum, and secured by Shares of Beneficial Interest in the Trust. Due in monthly principal and interest payments of $574 through June 2009.	20,886	26,114
Note payable to Karen Anderson, daughter of Mason Anderson, former Trustee of the Trust, bearing interest at 7% per annum, and secured by Shares of Beneficial Interest in the Trust. Due in monthly principal and interest payments of $574 through June 2009.	20,886	26,115
Note payable to Kathy Anderson, daughter of Mason Anderson, former Trustee of the Trust, bearing interest at 7% per annum, and secured by Shares of Beneficial Interest in the Trust. Due in monthly principal and interest payments of $495 through June 2009.	18,005	22,512
Note payable to The Anderson Charitable Remainder Unitrust, an affiliate of Mason Anderson, former Trustee of the Trust. Paid in full during fiscal year 2006.	—	18,771
Totals	$ 514,706	$ 93,512

During the second and third quarters of fiscal year 2004, the Trust issued five promissory notes in the amount of $208,000, $75,000, $200,000, $110,000 and $60,000 to Rare Earth Development Company, an affiliate of Mr. Wirth, all of which were paid in full in the third quarter of fiscal year 2004 utilizing a portion of the cash proceeds from the sale of the Buena Park property.

During the second quarter of fiscal year 2004, the Trust issued a promissory note in the amount of $225,000 to Rare Earth Financial, L.L.C., an affiliate of Mr. Wirth, which was paid in full in the third quarter of fiscal year 2004 utilizing a portion of the cash proceeds from the sale of the Buena Park property.

During the first quarter of fiscal year 2005, the Trust repurchased 433,036 Class B limited partnership units in the Partnership from affiliates of Mr. Wirth, issuing promissory notes in the aggregate amount of $974,331. During the first quarter of fiscal year 2005, the Trust repaid $449,500 of these notes. During the fourth quarter of fiscal year 2005, the Trust repaid the remaining balance of these notes with Shares of Beneficial Interest with an aggregate value of $467,552. Additionally, Mr. Wirth converted 100,000 Class B limited partnership units in the Partnership into 100,000 Shares of Beneficial Interest.

As of February 2, 2004, J. R. Chase, the sole stockholder of the Management Company, agreed to transfer 32,363 Shares of Beneficial Interest in the Trust to the Management Company in order to facilitate the Management Company's acquisition of Licensing Corp. from Mr. Wirth. In consideration of the transfer of those Shares, the Management Company agreed to pay Mr. Chase $72,817. The Management Company fully satisfied this obligation during June 2004. See Note 20, "Purchase of Management and Licensing Contracts."

During the second quarter of fiscal year 2005, the Trust issued promissory notes totaling $83,000 to affiliates of Mason Anderson, who was Trustee of the Trust from January through August 2005, in exchange for 47,084 Shares of Beneficial Interest in the Trust.

During the second quarter of fiscal year 2005, the Trust issued 55,423 Shares of Beneficial Interest to satisfy unpaid principal and interest totaling $95,882 to Mr. Robson, a Trustee of the Trust.

During the fourth quarter of fiscal year 2005, the Partnership reclassified $700,000 of advances payable to Rare Earth Financial, L.L.C., an affiliate of Mr. Wirth, to a deposit for the purchase of the Phoenix, Arizona hotel property by another affiliate of Mr. Wirth.

During the third quarter of fiscal year 2006, the Partnership issued a promissory note in the amount of $400,000 to Rare Earth Financial, L.L.C., an affiliate of Mr. Wirth. The full unpaid principal and accrued interest are due in one installment on April 15, 2006. Subsequent to year-end, this note was paid off using a new line of credit with Rare Earth Financial, L.L.C. (See Note 22 - “Subsequent Events”).

The Trust paid interest on related party notes to Mr. Wirth and his affiliates in the amounts of $8,905, $443,959 and $205,101 for the twelve months ended January 31, 2006, 2005 and 2004, respectively. The Trust incurred interest expense on related party notes to Mr. Wirth and his affiliates in the amounts of $10,856, $122,314 and $515,214 for the twelve months ended January 31, 2006, 2005 and 2004, respectively.

8. OTHER NOTES PAYABLE

As of January 31, 2006, the Trust had $327,982 in secured promissory notes outstanding to unrelated third parties arising from the repurchase of 207,850 Class A limited partnership units in the Partnership and the repurchase of 84,312 Shares of Beneficial Interest in privately negotiated transactions. The promissory notes bear interest at 7% per year and are due in varying monthly payments through March 2011. The repurchased Class A limited partnership units and Shares of Beneficial Interest secure the notes. As of January 31, 2005, the Trust had outstanding $248,413 in secured promissory notes to unrelated third parties arising from the repurchase of certain limited partnership units and Shares of Beneficial Interest.

9. MINIMUM DEBT PAYMENTS

Scheduled minimum payments of debt as of January 31, 2006 are as follows in the respective fiscal years indicated:

FISCAL YEAR ENDED		**AMOUNT**
2007	$	1,923,896
2008		1,105,218
2009		1,138,715
2010		4,891,004
2011		1,125,978
Thereafter		11,066,754
	$	21,251,565

10. DESCRIPTION OF CAPITAL STOCK

Holders of the Trust’s Shares of Beneficial Interest are entitled to receive dividends when and if declared by the Board of Trustees of the Trust out of funds legally available therefor. The holders of Shares of Beneficial Interest, upon any liquidation, dissolution or winding-down of the Trust, are entitled to share ratably in any assets remaining after payment in full of all liabilities of the Trust. The Shares of Beneficial Interest possess ordinary voting rights, each share entitling the holder thereof to one vote. Holders of Shares of Beneficial Interest do not have cumulative voting rights in the election of Trustees and do not have preemptive rights.

On January 2, 2001, the Board of Trustees approved a share repurchase program under Rule 10b-18 of the Securities Exchange Act of 1934, as amended, for the purchase of up to 250,000 limited partnership units in the Partnership and/or Shares of Beneficial Interest in open market or privately negotiated transactions. Additionally, on September 10, 2002, the Board of Trustees approved the purchase of up to 350,000 additional limited partnership units in the Partnership and/or Shares of Beneficial Interest in open market or privately negotiated transactions. On August 18, 2005, the Board of Trustees approved the purchase of up to 350,000 additional limited partnership units in the Partnership and/or Shares of Beneficial Interest in open market or privately negotiated transactions. Acquired Shares of Beneficial Interest will be held in treasury and will be available for future acquisitions

42

and financings and/or for awards granted under the InnSuites Hospitality Trust 1997 Stock Incentive and Option Plan. During fiscal year 2006, the Trust acquired 20,100 Shares of Beneficial Interest in open market transactions at an average price of $1.34 per share and 112,253 Shares of Beneficial Interest in privately-negotiated transactions at an average price of $1.32. The Trust intends to continue repurchasing Shares of Beneficial Interest in compliance with applicable legal and American Stock Exchange requirements. The Trust is authorized to repurchase an additional 214,112 limited partnership units and/or Shares of Beneficial Interest pursuant to the share repurchase program.

For the years ended January 31, 2006, 2005 and 2004, the Trust repurchased 132,353, 130,717 and 22,500 Shares of Beneficial Interest at an average price of $1.33, $1.73 and $1.29 per share, respectively. Repurchased Shares of Beneficial Interest are accounted for as treasury stock in the Trust's Consolidated Statements of Shareholders' (Deficit) Equity.

11. FEDERAL INCOME TAXES

The Trust and subsidiaries had income tax net operating loss carryforwards of approximately $14.0 million and $15.2 million at January 31, 2006 and 2005, respectively. The quarterly allocation of cash dividends paid per Share of Beneficial Interest and the characterization of dividends as either ordinary income or return of capital for an individual shareholder's income tax purposes were as follows:

	CALENDAR 2005			**CALENDAR 2004**			**CALENDAR 2003**		
Month Paid	**Ordinary Income**	**Return of Capital**	**Total Paid**	**Ordinary Income**	**Return of Capital**	**Total Paid**	**Ordinary Income**	**Return of Capital**	**Total Paid**
January	$ .01	—	$ .01	—	$ .02	$ .02	—	$ .01	$ .01
May	—	—	—	—	—	—	—	—	—
July	—	—	—	—	—	—	—	—	—
October	—	—	—	—	—	—	—	—	—
Total	$ .01	—	$ .01	—	$ .02	$ .02	—	$ .01	$ .01

The tax status of distributions to shareholders in calendar 2006 will be dependent on the level of the Trust's earnings in that year. If certain changes in the Trust's ownership should occur, there could be an annual limitation on the amount of carryforwards that can be utilized, which could potentially impair the ability to utilize the full amount of the carryforwards.

The total dividends per Share of Beneficial Interest applicable to operating results for the years ended January 31, 2006, 2005 and 2004, amounted to $0.01 per share, $0.01 per share and $0.02 per share, respectively.
The Trust and subsidiaries have federal and state net operating loss carryforwards which are estimated to expire as follows:

	Amount	
Year	**Federal**	**State**
2008	$ —	$ —
2009	—	—
2017	1,167,598	—
2018	3,883,556	—
2019	1,163,799	—
2020	1,979,025	—
2021	250,847	—
2022	1,580,590	—

2023		1,671,294		—
2024		2,302,410		—
	$	13,999,119	$	—

43

Total and net deferred income tax assets at January 31,		2006		2005
Net operating loss carryforwards	$	5,600,000	$	6,722,000
Book/Tax differences in operating assets		50,000		94,000
Total deferred income tax assets		5,650,000		6,816,000
Deferred income tax liability associated with book/tax differences in hotel properties		(2,900,000)		(3,425,000)
Net deferred income tax asset		2,750,000		3,391,000
Valuation allowance		(2,491,000)		(3,221,000)
Net deferred income tax asset	$	259,000	$	170,000

Income taxes for the year ended January 31,		2006		2005
Current income tax provision	$	164,000	$	330,000
Deferred income tax benefit		(89,000)		(170,000)
Net income tax provision	$	75,000	$	160,000

The differences between the statutory and effective tax rates is as follows for the year ended January 31, 2006:

Federal statutory rates	$	210,000	34%
State income taxes		37,000	6%
Utilization of federal net operating loss carrfyforward and related recognition of tax benefit		(214,000)	(35)%
Alternative minimum tax		42,000	7%
Effective rate	$	75,000	12%

The valuation allowance decreased by approximately $730,000 in the year ended January 31, 2006, primarily due to the utilization of approximately $2,607,185 of federal and state net operating loss carryforwards.

The Trust had income taxes payable of $241,000 and $330,000 recorded as of January 31, 2006 and 2005, respectively.

In addition to the net operating losses carryforward, there are other deferred tax assets which are fully allowed for at January 31, 2004 and January 31, 2003. Effective February 1, 2004, the Trust relinquished its REIT status. As of that date, any distributions to its shareholders are not deductible for purposes of computing the Trust's taxable income and the Trust will be subject to income tax, including any applicable alternative minimum tax, on its taxable income at regular corporate rates, without offset for distributions of such income to its shareholders.

12. ADVISORY AGREEMENT/EMPLOYMENT AGREEMENTS

Mr. Wirth has an employment agreement with the Trust that expires in December 2007. The employment agreement provides that Mr. Wirth received no compensation from the Trust as long as a previously enforceable advisory agreement was in effect. However, pursuant to the terms of the employment agreement, since the Advisor (as defined in the advisory agreement) no longer provides services to the Partnership or the Trust, Mr. Wirth is to be compensated at an amount up to the same annual basis as the Advisor would have been compensated under the terms of the advisory agreement had it remained in effect. Mr. Wirth is currently being compensated, however, at a lesser rate of $141,000 a year.

13. OTHER RELATED PARTY TRANSACTIONS

The Partnership is responsible for all operating expenses incurred by the Trust in accordance with the Partnership Agreement.

As of January 31, 2006 and 2005, Mr. Wirth and his affiliates held 3,407,938 and 3,467,938 Class B limited partnership units, respectively, which represented 25.8% and 26.3% of the total outstanding partnership units. As of January 31, 2006 and 2005, Mr. Wirth and his affiliates held 5,569,624 and 5,817,869 Shares of Beneficial Interest in the Trust, respectively, which represented 60.9% and 66.8% of the total issued and outstanding Shares of Beneficial Interest.

At January 31, 2006 and 2005, the Trust owned a 69.14% interest and 64.75% interest, respectively, in the Hotels through its sole general partner's interest in the Partnership.

44

14. FAIR VALUE OF FINANCIAL INSTRUMENTS

The carrying amounts and fair values of the Trust's significant financial instruments at January 31, 2006 and 2005 are as follows:

	2006		2005	
	CARRYING AMOUNT	FAIR VALUE	CARRYING AMOUNT	FAIR VALUE
Mortgage notes payable	$ 19,908,877	$ 20,867,605	$ 24,007,445	$ 25,675,971
Notes payable to banks	500,000	500,000	500,000	500,000
Notes and advances payable to related parties	514,706	513,500	93,512	94,713
Other notes payable	327,982	325,669	248,413	252,911

15. SUPPLEMENTAL CASH FLOW DISCLOSURES

	2006	2005	2004
Cash paid for interest	$ 1,894,693	$ 2,514,975	$ 3,030,616
Promissory notes issued by the Trust to acquire Class A limited partnership units	81,933	179,500	87,800
Promissory notes issued by the Trust to acquire Shares of Beneficial Interest	145,251	112,400	—
Promissory notes issued by the Trust to acquire Class B limited partnership units	—	971,831	—
Shares issued to Trustees and Officers in exchange for services	37,888	49,280	43,680
Shares issued to affiliates to satisfy notes payable	—	690,821	—
Accrued interest reclassified to principal due on notes payable to related parties	—	—	417,264
Promissory notes assigned to satisfy notes payable to related parties	—	—	200,000

During the first quarter of fiscal year 2005, the Trust reduced the principal balance of its note payable to Hulsey Hotels Corporation, an affiliate of Mr. Wirth, by $119,427 to offset receivables in the same amount that were owed to the Trust by other entities affiliated with Mr. Wirth.

During the first quarter of fiscal year 2005, J. R. Chase, the sole stockholder of the Management Company, agreed to transfer 32,363 Shares of Beneficial Interest in the Trust to the Management Company in order to facilitate the Management Company's acquisition of Licensing Corp. from Mr. Wirth. In consideration of the transfer of those

Shares, the Management Company agreed to pay Mr. Chase $72,817. The Management Company fully satisfied this obligation during June 2004.

During the second quarter of fiscal year 2005, Rare Earth Financial, an affiliate of Mr. Wirth, assumed from the Management Company a note payable with a principal balance of $23,303.

The Trust issued 528,469, 113,048 and 40,000 Shares of Beneficial Interest during the years ended January 31, 2006, 2005 and 2004, respectively, in exchange for Class A limited partnership units. The issued Shares of Beneficial Interest were valued at $693,173, $205,747 and $56,000, respectively.

16. COMMITMENTS AND CONTINGENCIES

Two of the Hotels are subject to non-cancelable ground leases expiring in 2050 and 2033. Total expense associated with the non-cancelable ground leases for the fiscal years ended January 31, 2006, 2005 and 2004 was $193,000, $190,000 and $188,000, respectively, plus a variable component based on gross revenues of each property that totaled approximately $90,000, $80,000 and $74,000, respectively.

Future minimum lease payments under these non-cancelable ground leases are as follows:

Fiscal Year Ending January 31,		
2007	$	193,018
2008		193,018
2009		193,018
2010		193,018
2010		193,018
Thereafter		6,066,740
Total	$	7,031,830

The Trust is obligated under loan agreements relating to four of its hotels to deposit 4% of the individual hotel's room revenue into an escrow account to be used for capital expenditures. The escrow funds applicable to the four hotel properties for which a mortgage lender escrow exists are reported on the Trust's Consolidated Balance Sheet as "Restricted Cash."

InnSuites Hotels has entered into franchise arrangements with Best Western International for four of the hotel properties. These agreements provide for fees to be paid by the Hotels based on revenue and reservations received, and contain no minimum payment provisions.

The nature of the operations of the Hotels exposes them to risks of claims and litigation in the normal course of their business. Although the outcome of these matters cannot be determined, management does not expect that the ultimate resolution of these matters will have a material adverse effect on the consolidated financial position, results of operations or liquidity of the Trust.

The Trust is involved from time to time in various other claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Trust's consolidated financial position, results of operations or liquidity.

17. STOCK OPTION PLAN

During fiscal year 1999, the shareholders of the Trust adopted the 1997 Stock Incentive and Option Plan (the "Plan"). Pursuant to the Plan, the Compensation Committee may grant options to the Trustees, officers, other key employees, consultants, advisors and similar employees of the Trust and certain of its subsidiaries and affiliates. The number of options that may be granted in a year is limited to 10% of the total Shares of Beneficial Interest and limited partnership units in the Partnership (Class A and Class B) outstanding as of the first day of such year.

Generally, granted options expire 10 years from the date of grant, are exercisable during the optionee's lifetime only by the recipient and are non-transferable. Unexercised options held by employees of the Trust generally terminate on the date the individual ceases to be an employee of the Trust.

There were no options granted in fiscal year 2006, 2005 or 2004, and no options outstanding as of January 31, 2006. The Plan currently has 1,000,000 options available to grant.

The Plan also permits the Trust to award stock appreciation rights, none of which, as of January 31, 2006, have been issued.

The following table summarizes the stock option activity during fiscal years 2006, 2005 and 2004, and provides information about the stock options outstanding at January 31, 2006:

Stock Option Activity	**Number of Options**	**Weighted-Average Exercise Price**
Outstanding, January 31, 2003	253,200	$ 2.50
Granted	—	—
Forfeited	(7,200)	2.50
Exercised	—	—
Outstanding, January 31, 2004	246,000	$ 2.50
Granted	—	—
Forfeited	(13,400)	2.50
Exercised	—	—
Outstanding, January 31, 2005	232,600	$ 2.50
Granted	—	—
Forfeited	(232,600)	2.50
Exercised	—	—
Outstanding, January 31, 2006	—	$ —

Stock Option Information	**January 31, 2006**
Options exercisable	—
Weighted Average Exercise Price	—
Weighted Average Remaining Contractual Life	—

For stock options granted to non-employees of the Trust, compensation was recognized over the respective vesting period based upon the fair value of the options as calculated using the Black-Scholes pricing model. The Trust did not grant any stock options to non-employees during fiscal years 2006, 2005, and 2004. The Trust had equity related compensation expense of $37,888, $49,280 and $43,680 for the years ended January 31, 2006, 2005, and 2004 respectively.

18. QUARTERLY RESULTS (UNAUDITED)

The following is a summary of the results of operations, by quarter, for the fiscal years ended January 31, 2006 and 2005. Management believes that all adjustments (consisting of normal recurring accruals) necessary for a fair presentation of such interim results have been included. The results of operations for any interim period are not necessarily indicative of those for the entire fiscal year.

FISCAL 2006	**APRIL 30**	**JULY 31**	**OCTOBER 31**	**JANUARY 31**	**FISCAL 2006**

Total revenue	$	6,573,433	$	4,852,780	$	4,698,158	$	5,124,468	$	21,248,839
Total revenue less interest expense on mortgage loans and operating expenses	$	419,576		(869,643)		(628,114)		(419,271)	$	(1,497,452)
Net income (loss)	$	404,301		658,129		(371,668)		(162,321)	$	541,578
Income (loss) per share - basic	$	.05		.07		(.04)		(.02)	$	0.06
Income (loss) per share - diluted	$	.03		.07		(.04)		(.02)	$	0.02
Dividends declared per share	$	—		—		—		.01	$	.01
FISCAL 2005		**APRIL 30**		**JULY 31**		**OCTOBER 31**		**JANUARY 31**		**FISCAL 2005**
Total revenue	$	7,358,640	$	4,922,554	$	5,062,591	$	5,531,402	$	22,875,187
Total revenue less interest expense on mortgage loans and operating expenses	$	421,304		(1,230,942)		(780,262)		(721,455)	$	(2,311,355)
Net income (loss)	$	2,028,243		(934,548)		(340,502)		(475,916)	$	240,442
Income (loss) per share - basic	$	.94		(.40)		(.14)		(.17)	$	0.10
Income (loss) per share - diluted	$	.56		(.40)		(.14)		(.17)	$	0.10
Dividends declared per share	$	—		—		—		.01	$	.01

19. SALE OF HOTEL PROPERTIES

On March 25, 2004, the Trust sold its Tempe, Arizona hotel to Tempe/Phoenix Airport Resort LLC (“Tempe Resort”), an affiliate of Mr. Wirth, for its appraised value of $6.8 million, which was also its carrying value. The purchase price was satisfied by Tempe Resort assuming the Trust’s mortgage note payable on the property of $1.7 million and assuming notes payable to Mr. Wirth and affiliates of $5.1 million.

On April 1, 2004, the Trust sold its San Diego, California hotel to an unrelated third party for $9.7 million, which the Trust received in cash. The Trust used $4.8 million of the proceeds to satisfy its mortgage note payable on the property, $1.4 million to satisfy notes and interest payable to related parties, and retained the remaining proceeds to reduce trade payables and to fund future operations and capital improvements.

The net gain realized on both sales was $5,113,540, of which approximately $2,217,000 was applicable to the minority interest.

On July 27, 2005, the Trust sold its Phoenix, Arizona hotel to Phoenix Northern Resort LLC, an affiliate of Mr. Wirth, for its appraised value of $5.1 million. The buyer satisfied the purchase price by assuming the Trust’s $3.2 million mortgage note payable secured by the property, paying $1.7 million in cash prior to the closing, and paying $192,000 in cash at the closing. The total gain on the sale was $1.8 million, with $1.3 million of the gain attributable to holders of Shares of Beneficial Interest.

None of the above-listed properties have been reported as discontinued operations in the Trust’s financial statements. Based on the criteria of EITF Abstract Issue No. 03-13, “Applying the Conditions in Paragraph 42 of FASB Statement No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, in Determining Whether to Report Discontinued Operations,” the Trust concluded it was not necessary to report hotels “held for sale” or “disposed of” when the Trust maintains significant continuing involvement. The Trust provides management, trademark, reservation and advertising services to all of the hotel properties listed above, which management believes provides the Trust the ability to significantly influence the operating and financial policies of these hotels.

20. PURCHASE OF MANAGEMENT AND LICENSING CONTRACTS

In February 2004, the Trust adopted FIN 46R, which amended FIN 46, “Consolidation of Variable Interest Entities,” an interpretation of Accounting Research Bulletin No. 51, “Consolidated Financial Statements.” FIN 46R requires an existing unconsolidated variable interest entity to be consolidated by its primary beneficiary if the entity does not effectively disperse risk among all parties involved or if other parties do not have significant capital to finance activities without subordinated financial support from the primary beneficiary. The primary beneficiary is the party that absorbs a majority of the entity’s expected losses, receives a majority of its expected residual returns, or both, as a result of holding variable interests, which are the ownership, contractual or other pecuniary interests in an entity.

As of February 1, 2004, the Trust recorded a charge for the cumulative effect of a change in accounting principle resulting from its recognition of the $854,000 net stockholder’s deficit of the Management Company, which was the Trust’s variable interest entity under FIN 46R. The $854,000 charge represented the net effect of the Trust reporting $160,000 in net assets (consisting primarily of receivables) and $1,014,000 in net liabilities (consisting primarily of debt) upon consolidating the financial results of the Management Company.

The effect of consolidating the financial results of the Management Company and Licensing Corp. was accounted for as a cumulative effect of a change in accounting principle. As a result of consolidating the financial results of the Management Company with its results, as of February 1, 2004, the Trust’s financial results include a $854,402 charge for the cumulative effect of a change in accounting principle on the Statements of Operations resulting in a reduction in its stockholders’ equity which represents the aggregate stockholders’ deficit reported by the Management Company as of February 1, 2004.

In connection with the Trust's relinquishment of its REIT status, the Trust no longer required the services of a separate management company. The Trust determined it was in its best interest to buy out the management contracts and licensing agreements and directly manage the Hotels through the Trust's wholly owned subsidiary, InnSuites Hotels. As a result of this buy out, the Management Company (which was the Trust's variable interest entity under FIN 46R) was no longer consolidated in the second quarter. As of June 8, 2004, all of the Trust's obligations were satisfied, and the Management Company is in the process of being liquidated.

Effective June 8, 2004, InnSuites Hotels acquired the management agreements under which the Management Company provided management services to the Hotels. In consideration of the acquisition, the stockholder of the Management Company received $20,000 and 90,000 Shares of Beneficial Interest of the Trust, reflecting a transaction value of approximately $159,500 in the aggregate. Following the acquisition, InnSuites Hotels will self-manage the Hotels. The Trust also manages one unrelated hotel in San Diego, California and four hotels owned by Mr. Wirth.

Effective June 8, 2004, InnSuites Hotels acquired the license agreements under which Licensing Corp. provided licensing services to the Hotels, and the related registered and unregistered InnSuites trademarks and tradenames. In consideration of the acquisitions, the Management Company (as the sole stockholder of Licensing Corp.) received $60,000 and 10,000 Shares of Beneficial Interest of the Trust and InnSuites Hotels satisfied Licensing Corp.'s line of credit in the amount of $459,000, reflecting a transaction value of approximately $534,500 in the aggregate. The Trust also provides licensing services to two unrelated hotels in San Diego and Buena Park, California and four hotels owned by Mr. Wirth. The Trust paid $459,000 in cash to satisfy the Management Company's line of credit. An additional $80,000 was paid to the Management Company to satisfy the Trust's obligation for net liabilities of approximately the same amount. The Shares of Beneficial Interest issued by the Trust for both the management contracts and licensing agreements were valued at $155,000, which amount was recorded as an expense.

21. COMPLIANCE WITH THE AMERICAN STOCK EXCHANGE CONTINUED LISTING STANDARDS

On December 10, 2004, the shareholders of the Trust approved several proposals relating to the Trust's plan to return to compliance with the American Stock Exchange ("Amex") continued listing standards. On January 4, 2005, the Board of Trustees approved the implementation of the proposals. The proposals were consummated on January 31, 2005, and resulted in:

A) The Trust issuing 6,577,732 Shares of Beneficial Interest in the Trust to the Partnership to satisfy advances and interest payable to the Partnership totaling approximately $8.6 million. The Partnership concurrently distributed the Shares to its unit holders. Of the 6,577,732 Shares of Beneficial Interest distributed by the Partnership, 3,761,071 were returned to the Trust and became treasury stock. The remaining 2,816,661 Shares of Beneficial Interest remain outstanding.

B) The Trust issuing 4,969,712 Shares of Beneficial Interest in the Trust, with a fair value of approximately $6.5 million, to the Partnership to acquire its ownership interest in Yuma Hospitality Properties, Ltd., which owns and operates the Yuma, Arizona hotel property. The Partnership concurrently distributed the Shares to its unit holders. Of the 4,969,712 Shares of Beneficial Interest distributed by the Partnership, 2,841,624 were returned to the Trust and became treasury stock. The remaining 2,128,088 Shares of Beneficial Interest remain outstanding. The fair value was determined using the carrying values of assets and liabilities, except for fixed assets, which were valued using appraised value. The portion of the excess of fair value over book value that relates to the minority interest partnership totals $1.2 million, and has been recorded as an increase in the basis of those fixed assets.

C) The Trust issuing 457,645 Shares of Beneficial Interest in the Trust to satisfy $594,938 of notes and interest payable to affiliates of Mr. Wirth. The entire balance of Shares issued remains outstanding.

D) The Trust issuing 1,000,000 Shares of Beneficial Interest in the Trust to Mr. Wirth and his affiliates in exchange for 1,000,000 Class B limited partnership units in the Partnership, which increased the Trust's ownership interest in the Partnership 7.6%. The entire balance of Shares issued remains outstanding.

In total, on January 31, 2005, the Trust issued 13,005,089 Shares of Beneficial Interest in the Trust, of which 6,602,695 returned to the Trust as treasury stock and 6,402,394 remain outstanding. The transactions were valued at the closing price of a Trust Share of Beneficial Interest on January 24, 2005, which was $1.30. The Trust did not record a gain or loss, and did not increase the basis of consolidated assets as a result of the transactions, except for the acquisition of the minority interest ownership in Yuma Hospitality Properties. Mr. Wirth and his affiliates, through these transactions, received 5,182,186 Shares of Beneficial Interest in the Trust.

As of January 31, 2006, the Trust has total shareholders' equity of $6.7 million and is compliant with Amex continued listing standards.

22. SUBSEQUENT EVENTS

On March 1, 2006, the Partnership established a $700,000 subordinated line of credit with Rare Earth Financial, L.L.C., an affiliate of Mr. Wirth. The line of credit will be available for borrowings from time to time, will expire on March 1, 2008, is secured by 49% of the Partnership's interest in its Tucson St. Mary's hotel property, and is subordinated to the Trust's commercial bank line of credit. Outstanding borrowings under the line of credit will bear interest at 7.0% per year. The Trust borrowed $400,000 under the line of credit on March 1, 2006 in order to refinance an outstanding promissory note payable to Rare Earth Financial which was due on April 15, 2006.

On March 1, 2006, the Trust issued 21,600 Shares of Beneficial Interest, with a total value of $28,944, to the Trustees in exchange for their services during fiscal year 2006. The Trust also issued 36,000 Shares of Beneficial Interest, with a total value of $48,240, to the Trustees as prepayment for their services during fiscal year 2007.

On March 1, 2006, the Trust issued 41,700 Shares of Benefical Interest, with a total value of $55,878, as bonuses to its executive officers and other key employees.

SCHEDULE III

INNSUITES HOSPITALITY TRUST AND SUBSIDIARY
REAL ESTATE AND ACCUMULATED DEPRECIATION
AS OF JANUARY 31, 2006

		Initial Cost to Tenant		Cost Capitalized Subsequent to Acquisition		Gross Amounts at Which Carried at Close of Period	
	Encumbrances	**Land**	**Building and Improvements**	**Land**	**Building and Improvements**	**Land**	**Building and Improvements**
InnSuites Hotel and Suites Tucson, Catalina Foothills Best Western							
Tucson, Arizona	$ 4,103,465	$ —	$ 4,220,820	$ —	$ 2,210,442	$ —	$ 6,431,262
InnSuites Hotels and Suites							
Yuma							
Yuma, Arizona	1,933,157	251,649	4,983,292	53,366	2,476,435	305,015	7,459,727
Best Western							
Airport Ontario Hotel and Suites							
Ontario, California	8,448,212	1,633,064	5,450,872	—	1,694,576	1,633,064	7,145,448
InnSuites Hotels and Suites							
Tucson St. Mary's							
Tucson, Arizona	4,191,981	900,000	9,166,549	(20,564)	975,673	879,436	10,152,222
InnSuites Hotels and Suites							
Albuquerque Airport Best							

Western							
Albuquerque, New Mexico	1,232,062	—	1,903,970	—	351,854	—	2,255,824
InnSuites Hospitality Trust							
Phoenix, Arizona	—	7,005	75,662	—	—	7,005	75,662
	$ 19,908,877	$ 2,791,718	$ 25,801,165	$ 32,802	$ 7,718,980	$ 2,824,520	$ 33,520,145

50

	Gross Land and Building	Accumulated Depreciation	Net Book Value Land and Buildings and Improvements	Date of Construction	Date of Acquisition	Depreciation in Income Statement is Computed
InnSuites Hotel and Suites Tucson, Catalina Foothills Best Western Tucson, Arizona	$ 6,431,262	$ 1,432,164	$ 4,999,098	1981	1998	5-40 years
InnSuites Hotels and Suites Yuma Yuma, Arizona	7,764,742	1,560,406	6,204,336	1982	1998	5-40 years
Best Western Airport Ontario Hotel and Suites Ontario, California	8,778,512	2,028,429	6,750,083	1990	1998	5-40 years
InnSuites Hotels and Suites Tucson St. Mary's Tucson, Arizona	11,031,658	2,149,692	8,881,966	1960	1998	5-40 years
InnSuites Hotels and Suites Albuquerque Airport Best Western Albuquerque, New Mexico	2,255,824	608,060	1,647,764	1975	2000	5-40 years
InnSuites Hospitality Trust Phoenix, Arizona	82,667	4,012	78,655	2004	2004	33 years
	$ 36,344,665	$ 7,782,763	$ 28,561,902			

(See accompanying independent auditors report.)

(A) Aggregate cost for federal income tax purposes at January 31, 2006 and 2005 are as follows:

		2006	2005
Land	$	1,856,788	2,275,007
Buildings and improvements		20,740,754	21,750,426
	$	22,597,542	24,025,433

Reconciliation of Real Estate:

Balance at January 31, 2004	$	48,825,009
Sale of Hotel Properties		(11,368,505)
Write-up of Assets		1,192,230
Improvement to Hotel Properties		546,762
Balance at January 31, 2005	$	39,195,496
Sale of Hotel Properties		(3,456,490)
Improvement to Hotel Properties		605,659
Balance at January 31, 2006	$	36,344,665

SCHEDULE IV

MORTGAGES LOANS ON REAL ESTATE

Description	**Interest Rate**	**Maturity Date**	**Periodic Payment Term**	**Face Amount of Mortgages**	**1/31/05 Carrying Amount**
Mortgage Note Secured by Albuquerque, NM property	8.875%	9/1/2015	180 monthly installments	$ 1,575,000	$ 1,232,062
Mortgage Note Secured by Ontario, CA property	8.280%	5/11/2011	120 monthly installments, with balloon payment of $7,498,458 due at maturity	9,000,000	8,448,212
Mortgage Note Secured by Yuma, AZ property	9.250%	8/1/2011	180 monthly installments	4,000,000	1,933,157
Mortgage Note Secured by Tucson St. Mary's, AZ property	Prime rate plus 1% (8.5% as of 1/31/06)	7/29/2009	83 monthly installments, with balloon payment of $3,800,488 due at maturity	4,500,000	4,191,981
Mortgage Note Secured by Tucson Oracle, AZ property	8.000%	5/1/2016	180 monthly installments	5,100,000	4,103,465
				$ 24,175,000	$ 19,908,877

Mortgage Note Reconciliation

Balance at January 31, 2004		$ 31,805,715
Deductions during period:		
	Assumed by buyer of Tempe, AZ hotel	(1,710,499)
	Principal payments	(6,087,771)
Balance at January 31, 2005		24,007,445
Deductions during period:		
	Assumed by buyer of Phoenix, AZ hotel	(3,167,182)
	Principal payments	(931,386)
Balance at January 31, 2006		$ 19,908,877

53

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

On January 20, 2005, the Trust received written notice, dated January 17, 2005, from McGladrey & Pullen, LLP ("McGladrey") that McGladrey had resigned as the Trust's principal independent accountant to audit the Trust's financial statements. Anthony Waters, the Trust's Chief Financial Officer, spoke with representatives of McGladrey on January 17, 2005 regarding the Trust's relationship with McGladrey, however, Mr. Waters did not believe that McGladrey had resigned on that date.

The reports of McGladrey on the Trust's financial statements for the fiscal years ended January 31, 2004 and 2003 did not contain an adverse opinion or a disclaimer of opinion and were not qualified or modified as to uncertainty, audit scope or accounting principles. In connection with the audits of the Trust's financial statements for the fiscal years ended January 31, 2004 and 2003, and in the subsequent interim periods through January 20, 2005, there were no disagreements with McGladrey on any matter of accounting principles or practices, financial statement disclosure or auditing scope and procedure which, if not resolved to the satisfaction of McGladrey, would have caused McGladrey to make reference to the matter in its report.

In connection with the audits of the Trust's financial statements for the fiscal years ended January 31, 2004 and 2003, and in the subsequent interim periods through January 20, 2005, there were no "reportable events" as that term is described in Item 304(a)(l)(v) of Regulation S-K, except that, on January 7, 2005, McGladrey provided a letter to the Audit Committee and management of the Trust noting two reportable conditions under standards established by the American Institute of Certified Public Accountants that McGladrey believed to be material weaknesses. McGladrey has advised the Trust that it believes that these two reportable conditions constitute "reportable events."

The first reportable condition involved the lack of sufficient segregation of duties and responsibilities with respect to the recording and approval of financial information that occurred due to the departure of the Trust's Controller. Effective January 31, 2005, the Trust rehired its former Controller who will oversee the recording of financial information while the Trust's Chief Financial Officer will continue in his prior role of approving financial information. The second reportable condition involved the need for "numerous adjusting journal entries" and "significant financial statement presentation changes," which resulted in McGladrey concluding that the Trust's "monthly internal financial statements may not be reliable." The Trust has hired additional accounting staff and implemented additional measures that will better ensure the reliability of the Trust's internal financial statements.

On December 10, 2004, the Audit Committee discussed the conditions described above with McGladrey, but did not receive the letter identifying those conditions as reportable conditions and material weaknesses until January 7, 2005. Management of the Trust subsequently discussed the letter received on January 7, 2005 with McGladrey. The Trust has authorized McGladrey to respond fully to the inquiries of any successor accountant concerning the subject matter of the reportable conditions described above.

On April 4, 2005, the Trust engaged Epstein, Weber & Conover, P.L.C. ("EWC") to act as the Trust's principal independent accountant to audit the Trust's financial statements. The decision to engage the new accountants was recommended and approved by the Audit Committee of the Board of Trustees of the Trust.

During the fiscal years ended January 31, 2005 and 2004, and during all subsequent interim periods through April 4, 2005, the Trust did not consult with EWC regarding the application of accounting principles to a specified transaction, either completed or proposed, the type of audit opinion that might be rendered on the Trust's financial statements or any of the matters described in the preceding paragraphs of this Item 9.

Item 9A. CONTROLS AND PROCEDURES

As of the end of the period covered by this report, the Trust conducted an evaluation, under the supervision and with the participation of the principal executive officer and principal financial officer, of the Trust's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934). Based on this evaluation, the principal executive officer and principal financial officer concluded that the Trust's disclosure controls and procedures are effective to ensure that information required to be disclosed by the Trust in reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the Commission's rules and forms. There was no change in the Trust's internal control over financial reporting during the Trust's most recently completed fiscal year that has materially affected, or is reasonably likely to materially affect, the Trust's internal control over financial reporting.

ITEM 9B. OTHER INFORMATION

None.

PART III

ITEM 10. TRUSTEES AND EXECUTIVE OFFICERS OF THE TRUST

Nominees, Trustees and Executive Officers

The information concerning the Trustees and executive officers of the Trust set forth in the following table is based in part on information received from the respective Trustees and executive officers and in part on the Trust's records. The following table sets forth the name, age, term of office and principal business experience for each Trustee, nominee for Trustee and executive officer of the Trust, as applicable.

Name	**Principal Occupations During Past Five Years, Age as of April 21, 2006 And Directorships Held**	**Trustee Since**
Nominee Whose Term Expires in 2009		
Marc E. Berg(1)	Executive Vice President, Secretary and Treasurer of the Trust since February 10, 1999. Vice President - Acquisitions of the Trust from December 16, 1998 to February 10, 1999. Consultant to InnSuites Hotels since 1989. Self-employed as a Registered Investment Advisor since 1985. Age: 53.	January 30, 1998
Trustees Whose Terms Expire in 2007		
James F. Wirth(1)	Chairman, President and Chief Executive Officer of the Trust since January 30, 1998. President and owner (together with his affiliates) of Suite Hotels LLC, Rare Earth Financial L.L.C. and affiliated entities, owners	January 30, 1998

	and operators of hotels, since 1980. President of Rare Earth Development Company, a real estate investment company owned by Mr. Wirth and his affiliates, since 1973. Age: 60.	
Peter A. Thoma(2),(3),(4)	Owner and operator of A&T Verleih, Hamburg, Germany, a hospitality service and rental company, since 1997. Age: 39.	April 13, 1999

Trustees For Terms Expiring in 2008

Larry Pelegrin(2),(3),(4)	Retired marketing executive with an extensive background in travel industry automation systems and call center sales. Director of Sales and Marketing of ARINC, a provider of transportation communications services, from 1994 to 2001. Previous employment included senior marketing positions with Best Western International and Ramada Inns. Age: 68.	August 25, 2005
Steven S. Robson(2),(3),(4)	President of Robson Communities, Inc. and Scott Homes and Scott Multifamily, Inc., residential real estate developers, since 1979. Age: 50.	June 16, 1998

---

(1) Member of the Executive Committee.
(2) Member of the Audit Committee.
(3) Member of the Compensation Committee.
(4) Member of the Governance and Nominating Committee.

Other Executive Officers

Anthony B. Waters	Chief Financial Officer of the Trust since February 29, 2000. Controller of the Trust from June 17, 1999 to February 29, 2000. Accountant and auditor with Michael Maastricht, CPA from June 16, 1998 to June 15, 1999, performing audits for InnSuites Hotels, Inc. Self-employed, concentrating in computerized accounting and information systems, from 1990 to June 1998. Age: 59.

The Board of Trustees of the Trust has determined that Mr. Pelegrin, a member of the Trust's Audit Committee, qualifies as a "financial expert" under applicable Commission rules, and that Messrs. Thoma, Robson and Pelegrin are "independent," as such term is defined by Commission rules and Amex listing standards.

Section 16(a) Beneficial Ownership Reporting Compliance

Based on Trust records and information, and upon representations from the reporting persons, the Trust believes that all Commission filing requirements applicable to Trustees, executive officers and beneficial owners of more than 10% of a registered class of equity securities of the Trust under Section 16(a) of the Securities Exchange Act of 1934, as amended, for the fiscal year ended January 31, 2006, were complied with, except that Mr. Pelegrin's Form 3 was not timely filed on his behalf.

Code of Ethics for Senior Financial Officers

The Trust has adopted a Code of Ethics that applies to its Chief Executive Officer, Chief Financial Officer and principal accounting officer and persons performing similar functions. The Trust has posted its Code of Ethics on its website at www.innsuitestrust.com. The Trust intends to satisfy all Commission and Amex disclosure requirements regarding any amendment to, or waiver of, the Code of Ethics relating to its Chief Executive Officer, Chief Financial Officer and principal accounting officer, and persons performing similar functions, by posting such information on its website and making any necessary filings with the Commission. In addition, the Trust has adopted a Code of Conduct and Ethics that applies to all of its employees, officers and Trustees. It is also available on the Trust’s website at www.innsuitestrust.com.

ITEM 11. EXECUTIVE COMPENSATION

On March 1, 2006, the Trust issued 7,200 unrestricted Shares of Beneficial Interest ("Shares") to Messrs. Robson and Thoma, 4,000 unrestricted Shares to Mr. Pelegrin, and 3,200 unrestricted Shares to Mr. Anderson as compensation for services rendered as a Trustee of the Trust during fiscal year 2006. The Trust has issued 12,000 restricted Shares to each Trustee, other than Messrs. Wirth and Berg, as compensation for services to be rendered during fiscal year 2007. The restricted Shares were issued on March 1, 2006 and will vest in 10% increments over a ten month period.

Summary Compensation Table

The table below shows individual compensation information for the Trust's Chief Executive Officer and any other executive officer whose total annual salary and bonus for the fiscal year ended January 31, 2006 exceeded $100,000.

Name and Principal Position	Fiscal Year	Annual Salary	Restricted Stock Awards
James F. Wirth	2006	$141,000	—
President and Chief	2005	$130,000	—
Executive Officer (1)	2004	$ 95,231(2)	—
Anthony B. Waters	2006	$141,000	$ 2,048(3)
Chief Financial Officer	2005	$126,400	$ 3,200(4)
	2004	$126,000	$ 6,240(5)

(1) The terms of Mr. Wirth's Employment Agreement are summarized below. See "Item 13 - Certain Relationships and Related Transactions - Employment Agreement with Mr. Wirth."
(2) Although Mr. Wirth's annual salary for fiscal year 2004 was set at $130,000, Mr. Wirth agreed to a salary reduction that resulted in an annual salary of $95,231 for fiscal year 2004.
(3) Represents the fair market value on the date of grant of 1,600 Shares issued to Mr. Waters as a bonus on April 6, 2005.
(4) Represents the fair market value on the date of grant of 2,000 Shares issued to Mr. Waters as a bonus on March 26, 2004.
(5) Represents the fair market value on the date of grant of 4,800 Shares issued to Mr. Waters as a bonus on June 30, 2003.

During the second quarter of fiscal year 2006, the Trust accepted the voluntary surrender of all outstanding stock options. As a result, none of the Trust's executive officers hold any stock options.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following table provides information about the Trust's equity compensation plans (other than qualified employee benefits plans and plans available to shareholders on a pro rata basis) as of January 31, 2006:

Equity Compensation Plan Information

Plan Category	**Number of Securities to be Issued Upon Exercise of Outstanding Options, Warrants and Rights**	**Weighted - Average Exercise Price of Outstanding Options, Warrants and Rights**	**Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column (a))**
Equity compensation plans approved by security holders	0	$ N/A	477,200
Equity compensation plans not approved by security holders	None	None	None

The following table sets forth information as of April 21, 2006 in respect of any persons known to the Trust to be the beneficial owner of more than 5% of the Shares (of which there were none, other than Mr. Wirth) and the number of Shares owned beneficially by each Trustee, nominee and executive officer, and the Trustees, nominees and executive officers as a group.

Five Percent Beneficial Owners and
Beneficial Ownership of Trustees, Nominees and Executive Officers

Name	**Shares Beneficially Owned**	**Percentage of Outstanding Shares**
Trustees, Nominees and Executive Officers		
James F. Wirth (1)	5,573,624	60.1%
Marc E. Berg	60,225	*
Steven S. Robson	212,723	2.3%
Peter A. Thoma	57,900	*
Larry Pelegrin	19,870	*
Anthony B. Waters	23,000	*
	5,947,342	64.2%

Trustees, Nominees and Executive Officers as a group (six persons)

---

(1) All Shares are owned jointly by Mr. Wirth and his spouse, except for 150,000 Shares that are held individually by Mr. Wirth. Mr. Wirth and his spouse also own all 3,407,938 issued and outstanding Class B limited partnership units in the Partnership, the conversion of which is restricted and permitted only at the discretion of the Board of Trustees of the Trust. Mr. Wirth's business address is 1615 E. Northern Avenue, Suite 102, Phoenix, Arizona 85020.

* Less than one percent (1.0%).

58

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

Employment Agreement with Mr. Wirth

James F. Wirth, Chairman, President and Chief Executive Officer of the Trust, has an Employment Agreement with the Trust expiring in December 2007. Pursuant to the terms of the Employment Agreement, upon the termination of the Advisory Agreement with Mid-America ReaFund Advisors, Inc. ("MARA"), a company owned by Mr. Wirth and his spouse, which termination occurred effective January 1, 1999, Mr. Wirth is to receive, each year through 2007, up to the amount MARA would have received for advisory and management services under the Advisory Agreement, but in no event will his compensation exceed $160,000 per year. Based upon a review of the performance of the Trust and upon the recommendation of the Compensation Committee, during fiscal year 2006, Mr. Wirth was paid an annual salary equal to $141,000, which is less than he is entitled to receive under the terms of his Employment Agreement. Mr. Wirth's annual salary for fiscal year 2007 has been set at $141,000. The Compensation Committee does not rely on any particular set of financial or non-financial factors, measures or criteria when determining the compensation offered to Mr. Wirth.

Sale of Phoenix, Arizona Property

On July 27, 2005, the Trust sold its Phoenix, Arizona hotel to Phoenix Northern Resort LLC, an affiliate of Mr. Wirth, for its appraised value of $5.1 million. The buyer satisfied the purchase price by assuming the Trust's $3.2 million mortgage note payable secured by the property, paying $1.7 million in cash prior to the closing, and paying $192,000 in cash at the closing. The total gain on the sale was $1.8 million, with $1.3 million of the gain attributable to holders of Shares of Beneficial Interest.

Related Party Loans and Advances to the Trust

Notes and advances payable to related parties consist of funds provided by Mr. Wirth, certain of his affiliates and other related parties to permit the Trust to repurchase additional general partnership units in the Partnership and to fund working capital and capital improvement needs. The aggregate amounts outstanding to related parties were approximately $515,000 and $94,000 as of January 31, 2006 and 2005, respectively.

The notes and advances payable to related parties are as follows as of January 31 of the respective years:

		2006		**2005**
Note payable to Rare Earth Financial, LLC, an affiliate of Mr. Wirth, unsecured and bearing interest at 7% per annum. Due in one installment of accrued interest and unpaid principal on April 15, 2006.	$	400,000	$	—
Note payable to the Anderson Charitable Remainder Unitrust, an affiliate of Mason Anderson, former Trustee of the Trust, bearing interest at 7% per annum, and secured by Shares of Beneficial Interest in the Trust. Due in monthly principal and interest payments of $1,365 through November 2009.		54,929		—
Note payable to Wayne Anderson, son of Mason Anderson, former Trustee of the Trust, bearing interest at 7% per annum, and secured by Shares of Beneficial Interest in the Trust. Due in monthly principal and interest		20,886		26,114

payments of $574 through June 2009.				
Note payable to Karen Anderson, daughter of Mason Anderson, former Trustee of the Trust, bearing interest at 7% per annum, and secured by Shares of Beneficial Interest in the Trust. Due in monthly principal and interest payments of $574 through June 2009.		20,886		26,115
Note payable to Kathy Anderson, daughter of Mason Anderson, former Trustee of the Trust, bearing interest at 7% per annum, and secured by Shares of Beneficial Interest in the Trust. Due in monthly principal and interest payments of $495 through June 2009.		18,005		22,512
Note payable to The Anderson Charitable Remainder Unitrust, an affiliate of Mason Anderson, former Trustee of the Trust. Paid in full during fiscal year 2006.		—		18,771
Totals	$	514,706	$	93,512

59

During the second quarter of fiscal year 2005, the Trust issued promissory notes totaling $83,000 to affiliates of Mason Anderson, who was Trustee of the Trust between January and August 2005, in exchange for 47,084 Shares of Beneficial Interest in the Trust.

During the third quarter of fiscal year 2006, the Partnership issued a promissory note in the amount of $400,000 to Rare Earth Financial, L.L.C., an affiliate of Mr. Wirth. The full unpaid principal and accrued interest are due in one installment on April 15, 2006. Subsequent to year-end, this note was paid off using a new line of credit with Rare Earth Financial, L.L.C.

The Trust paid interest on related party notes to Mr. Wirth and his affiliates in the amounts of $8,905, $443,959 and $205,101 for the twelve months ended January 31, 2006, 2005 and 2004, respectively. The Trust incurred interest expense on related party notes to Mr. Wirth and his affiliates in the amounts of $10,856, $122,314 and $515,214 for the twelve months ended January 31, 2006, 2005 and 2004, respectively.

On March 1, 2006, the Partnership established a $700,000 subordinated line of credit with Rare Earth Financial, L.L.C., an affiliate of Mr. Wirth. The line of credit will be available for borrowings from time to time, will expire on March 1, 2008, is secured by 49% of the Partnership's interest in its Tucson St. Mary's hotel property, and is subordinated to the Trust's commercial bank line of credit. Outstanding borrowings under the line of credit will bear interest at 7.0% per year. The Trust borrowed $400,000 under the line of credit on March 1, 2006 in order to refinance an outstanding promissory note payable to Rare Earth Financial which had been due on April 15, 2006.

Sales and Project Coordination Agreement

On March 1, 2006, the Trust entered into a Sales and Project Coordination Agreement (the "Project Agreement") with Rare Earth Development Company, an affiliate of Mr. Wirth. The Project Agreement requires Rare Earth Development Company to coordinate the conversion of hotel properties, to be designated by the Trust, into condo-hotel units, including coordination of the construction, marketing and sales of such condo-hotel units. Rare Earth Development Company will receive a brokerage fee of 6% of the sales price of each condo-hotel unit (subject to the potential splitting of such brokerage fee with unaffiliated brokers) payable contingent upon the sale and closing of a condo-hotel unit. In the event that the sale of a unit is financed by the Trust, Rare Earth Development Company has agreed to defer the payment of its brokerage fee over a two-year period (with 1/3 payable at closing, 1/3 payable on the first anniversary of closing, and 1/3 payable on the second anniversary of closing, so long as the buyer is not in default of its obligations to the Trust).

All related party transactions are subject to appropriate review and oversight by the Audit Committee of the Board of Trustees.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

Audit Fees

The aggregate fees for professional services rendered by EWC for the audit of the Trust's annual financial statements for the fiscal years ended January 31, 2006 and January 31, 2005 were $63,500 and $61,000, respectively. The aggregate fees for professional services rendered by McGladrey for the audit of the Trust's annual financial statements for the fiscal year ended January 31, 2005 were $78,130. The aggregate fees for professional services rendered by EWC for reviewing the interim financial statements included in the Trust's quarterly reports on Form 10-Q filed during the fiscal year ended January 31, 2006 was $29,240. The aggregate fees for professional services rendered by McGladrey for reviewing the interim financial statements included in the Trust's quarterly reports on Form 10-Q filed during the fiscal year ended January 31, 2005 was $60,220.

Audit-Related Fees

The Trust incurred no fees for audit-related services, such as comfort letters, consents and assistance with and review of documents filed with the Commission, for the fiscal years ended January 31, 2006 and January 31, 2005.

Tax Fees

The aggregate fees for EWC tax compliance, tax advice and tax planning for the fiscal years ended January 31, 2006 and January 31, 2005 were $25,000 in each year. The aggregate fees for McGladrey tax compliance, tax advice and tax planning for the fiscal year ended January 31, 2005 were $2,935. The Audit Committee pre-approved all tax fees billed for the fiscal year ended January 31, 2006.

All Other Fees

The Trust incurred no fees for other services rendered during the fiscal years ended January 31, 2006 and January 31, 2005.

The Audit Committee of the Trust has considered whether the provision of these services, other than the audit of the Trust's annual financial statements, is compatible with EWC and McGladrey maintaining their respective independence from the Trust.

The Audit Committee pre-approves all fees for services performed by EWC, including audit and non-audit services. Unless a type of service EWC provided received general pre-approval, it will require specific pre-approval by the Audit Committee. Any proposed services exceeding pre-approved cost levels will require specific pre-approval by the Audit Committee. The term of any pre-approval is 12 months from the date of pre-approval, unless the Audit Committee specifically provides for a different period.

Since May 6, 2003, the effective date of Commission rules requiring Audit Committee pre-approval of audit and non-audit services performed by the Trust's independent auditors, all of the services provided by EWC and McGladrey were approved in accordance with the policies and procedures described above.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a)(1) and (2) Financial Statements and Schedules

Financial Statements/Schedules of InnSuites Hospitality Trust

(a)(3) Exhibit List

Exhibit No.	Exhibit
3.1	Second Amended and Restated Declaration of Trust of InnSuites Hospitality Trust dated June 16, 1998, as further amended on July 12, 1999 (incorporated by reference to Exhibit 3.1 of the Registrant's Annual Report on Form 10-K for the fiscal year ended January 31, 2005 filed with the Securities and Exchange Commission on May 16, 2005).
10.1	First Amended and Restated Agreement of Limited Partnership of RRF Limited Partnership dated January 31, 1998 (incorporated by reference to Exhibit 10.1 of the Registrant's Registration Statement on Form S-2, filed with the Securities and Exchange Commission on September 8, 1998).
10.2*	Employment Agreement dated as of January 31, 1998, between InnSuites Hospitality Trust and James F. Wirth (incorporated by reference to Exhibit 10.2 of the Registrant's Annual Report on Form 10-K for the fiscal year ended January 31, 2005 filed with the Securities and Exchange Commission on May 16, 2005).
10.3*	Form of Indemnification Agreement between InnSuites Hospitality Trust and each Trustee and executive officer.
10.4	Promissory Note dated October 14, 2005 by RRF Limited Partnership in favor of Rare Earth Financial, L.L.C. (incorporated by reference to Exhibit 10.1 of the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended October 31, 2005 filed with the Securities and Exchange Commission on

December 6, 2005).

10.5	Promissory Note dated March 1, 2006 by RRF Limited Partnership in favor of Rare Earth Financial, L.L.C.
10.6	Sales and Project Coordination Agreement dated March 1, 2006 between Rare Earth Development Company and InnSuites Hospitality Trust.

14	Code of Ethics for Senior Financial Officers (incorporated by reference to Exhibit 14 of the Registrant's Annual Report on Form 10-K for the fiscal year ended January 31, 2004, filed with the Securities and Exchange Commission on April 30, 2004).
21	Subsidiaries of the Registrant.
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer required by Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Financial Officer required by Section 906 of the Sarbanes-Oxley Act of 2002.

* Management contract or compensatory plan or arrangement.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of Securities Exchange Act of 1934, the Trust has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

INNSUITES HOSPITALITY TRUST

Dated: May 1, 2006	By:	/s/ James F. Wirth James F. Wirth, Chairman, President and Chief Executive Officer (Principal Executive Officer)
Dated: May 1, 2006	By:	/s/ Anthony B. Waters Anthony B. Waters, Chief Financial Officer (Principal Financial Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Trust and in the capacities and on the dates indicated.

Dated: May 1, 2006	By: /s/ James F. Wirth James F. Wirth, Chairman President and Chief Executive Officer (Principal Executive Officer)
Dated: May 1, 2006	By: /s/ Anthony B. Waters Anthony B. Waters, Chief Financial Officer (Principal Financial Officer)
Dated: May 1, 2006	By: /s/ Marc E. Berg Marc E. Berg, Trustee
Dated: May 1, 2006	By: /s/ Steven S. Robson Steven S. Robson, Trustee
Dated: May 1, 2006	By: /s/ Peter A. Thoma Peter A. Thoma, Trustee
Dated: May 1, 2006	By: /s/ Larry Pelegrin

Larry Pelegrin, Trustee

64