

HANDBOOK

VOLUME II:

RESEARCH



NCREIF PREA

Reporting Standards

Approved

August 2019

GROSS AND NET IRR

Adding transparency and comparability to closed-end fund performance and Investor Specific Reporting.

Findings and Recommendations from the Gross Net IRR Task Force.



NCREIF

PREA
pension real estate association

EXECUTIVE SUMMARY

A suggested approach to Internal Rate of Returns (“IRR” or “IRRs”), gross of fees and promote, net of fees and promote

IRR is perhaps the most widely accepted performance measure relied on for strategic decision making for closed-end funds, whether it is being reported for the fund’s portfolio or for the investors, (in either case over a relevant holding period(s)). Often specified in legal documents are target IRR expectations, both in terms of potential investments that are promising enough to be considered, as well as in terms of what IRR an investor might hope to achieve when the fund ends. Comparisons among targeted, projected, and actual IRRs are commonplace (though not contemplated in this paper), and it is critical to ensure that these are apples to apples comparisons.

In addition, the increasingly watchful eye of regulatory bodies has put pressure on alternative investment firms to be more transparent regarding fees and expenses paid to them; and to provide more adequate disclosures around performance results of the funds/investments they manage. Complex transactions with complicated fee structures are now subject to scrutiny. Some state regulators now require state pension plans and other state funds to provide more disclosure about fees they pay to alternative investment managers as part of their fiduciary responsibilities to their beneficiaries and taxpayers.

As regulators’ attention has turned to real estate during the past several years, it has become apparent that the private institutional real estate industry does not have a consistent and transparent approach to the presentation, calculation and disclosures of IRR, gross of fees and promote, net of fees and promote. This lack of consistency may result in flawed comparisons or incorrect conclusions. Our industry lacks consistency in its fund documentation as it relates to what can and cannot be charged to a fund, and further lacks commonality of classifications and definitions. In addition, there is a considerable degree of inconsistency in how internal rates of return are being calculated. Investors need, and now require, the ability to compare IRRs across investments and understand the underlying components of the return calculations. Although many groups are working towards improving such weaknesses (which are detailed later in the research paper), currently the information disclosed in financial and other performance reports to investors fail to provide this much needed additional transparency, consistency and comparability for investors. Clearly, detailed industry guidance is necessary in order to gain wide acceptance of a unified approach to defining, calculating, measuring and presenting IRR information.

The NCREIF PREA Reporting Standards (“Reporting Standards”) Council (“Council”) approved the formation of a project Task Force to tackle this complicated issue.

Members of the Task Force were divided into sub groups to research and communicate results to the larger group. Sub groups were organized for the following purposes:

- Research and document inconsistencies in current IRR reporting practices

- Assess stakeholder sentiment including any perceived voids in information; how, when and what type of information facilitates understanding and analysis.
- Review the related standards promulgated by the Reporting Standards Foundational Standards and understand the roles of regulators and legislatures to ensure our guidance can serve to mitigate some of their concerns surrounding transparency and disclosures.
- Review current industry initiatives and leverage key conclusions where possible.
- Develop an easy to understand hierarchy between gross IRR, net IRR, including:
 - a clear identification and definition of IRR, gross of fees and promote, net of fees and promote;
 - components included within each level; and
 - definitions of the components.
- Develop underlying calculations and disclosures and address implementation challenges.

The Task Force concluded that a hierarchal approach (levels), coupled with clear identification, definition and mapping of fees and costs would result in much needed additional transparency on since inception IRR, gross of fees and promote, net of fees and promote reporting and allow for cross comparability of closed-end funds for investors.

A summary of the recommended hierarchy and recommendations for integration into NCREIF PREA Reporting Standards are presented below¹.

Fund Level Reporting Hierarchy

- Level 1: Gross IRR before investment management fees and fund Costs². The level 1 IRR can be calculated using two methods³:
 - Level 1a – IRR reflects cash flows between a fund and its investments.
 - Level 1b – IRR reflects cash flows between investors and the fund.
- Level 2: Fund Gross IRR after deduction for fund costs but before deduction of recurring, transactional and performance-based investment management fees.
- Level 3: Level 2 less ongoing and transactional investment management fees⁴.

¹ While the hierarchy was created to specifically address closed-end fund issues, we believe that many of the recommendations can be tailored for applicability to separate accounts and open-end funds at a later point in time.

² Level 1 should be presented net of transaction related costs (other than transaction costs deemed to be transaction fees) and deal level expenses.

³ Optionality is provided in Level 1a and 1b to allow for a cash flow starting point of property cash flows or fund level cash flows. This was necessary due to divergence of opinions as to the appropriate starting point of level 1. The remaining levels reflect cash flows between investors and the fund.

⁴ Determination of whether a transaction related charge is a transaction cost (included in level 1) or a transaction fee (included in level 3) should be treated consistently with the framework provided in the Total Global Expense Ratio (TGER).

- Level 4: Level 3 less performance-based investment management fees (e.g., incentive fees, carried interest and promotes).

Investor Specific Reporting Hierarchy

- Level 5: Individual Limited Partner specific reporting which captures the experience of a single investor, including all investor specific timing, fees and costs.

The Task Force makes the following implementation recommendation to the NCREIF PREA Reporting Standards:

Comparison of Quarterly IRR Requirements for Closed-end Funds			
Required or Recommended per Vol 1	Description	Proposed change	Proposed required or recommended in RS 2020
Required	Since inception IRR gross of fees	Change from requirement	Recommended
Required	Since inception IRR net of fees	None	Required
<i>Disclosures</i>			
Required	Gross of fees: types of fees deducted from gross return to arrive at net	Move: types of fees deducted from gross return to arrive at net to "net of fees" disclosures below	N/A
		Add: type/level of gross IRR reporting	Required
		Add: Levels 1a, 1b or 2 as preferred gross of fee reporting	Recommended
	Where a subscription line is used, disclose:	Year of first investment of the fund	Required
		Length of time between the first investment and the first capital call	Required
Required	Net of fees: Presented for all investor classes	Add: type/level of net IRR reporting	Required
		Add: Level 4 as preferred net of fee reporting	Recommended
		Add: types of fees deducted from gross return to arrive at net	Required
		Add: When Level 1 IRR is presented, stipulate that the spread between gross	Required

		and net includes fund load/fund costs	
Required	Time period and frequency of cash flows: time period for calculation and frequency of cash flows-quarterly minimum prior to January 1, 2020 and monthly minimum thereafter.	none	Required
	(New*) Realized IRR end date: Must disclose ending date of realized IRR calculation. If final net asset of fund/property haven't be distributed as of the IRR end date, the method used in determining the final distribution and IRR end date must be disclosed.	none	Required
*Approved by Council in connection with changes to TWR in fall of 2018.			

- PR.06 – Gross and Net IRR requirement
 - Require that the Gross and Net IRR include a reference to the reporting hierarchy.
 - Recommend that the Gross IRR reflect a Level 1a, 1b or Level 2 Fund level IRR. Disclosure of level used for Gross IRR would be required in PR.06.1 for consistency and comparability across closed-end funds.
 - Recommend that the Net IRR reflect a Level 4 Fund level IRR for IRR for consistency across closed-end funds.
- PR.06.1 – Gross IRR disclosures
 - Move the existing language “The Account Report must clearly disclose what types of fees are deducted from the gross return to arrive at the net return.” to PR.06.2.
 - Require disclosure of level 1 or 2. If using level 1, user should specify the cash flow starting point (Level 1a or Level 1b).
- PR.06.2 – Net IRR disclosures
 - Move the existing language from PR.06.1 to PR.06.2 “The Account Report must clearly disclose what types of fees are deducted from the gross return to arrive at the net return.”
 - If a level 1 IRR is provided to satisfy the Gross IRR requirement, the manager must note that the difference between Gross and Net includes vehicle related costs (aka “fund load” or “Fund costs”).
- PR.06.3
 - No changes recommended.

Qualifications and Limitations

Please note qualifications and limitations to this paper below.

- *The information summarized herein is applicable to fund level IRR's reported for US closed-end commingled funds.*
- Since the research herein is applicable to fund level IRR's only, there may be variances which occur when calculating IRRs at the property level or investment level which are not addressed herein, for example whether a hypothetical cost of sale should be deducted from the unrealized value.
- *This research paper does not address unleveraged IRR* including the concept of whether an unleveraged IRR a better indicator of comparability.
- *This research paper does not address projected returns and their regulatory issues.*
- This research paper only contemplates in place IRRs rather than projected end of fund life IRRs.
- *The research paper does not address the impact of foreign exchange rates on IRR.* Rather, the research conducted in this paper was limited to USD denominated results within commingled funds.
- *The research does not take a position as to whether a private market equivalent (PME) approach should be included*, so that one can compare the IRR to a PME metric, the latter which is based on a benchmark index, so as to measure whether the investment in question has outperformed a passive investment in the market.

Summary

In consort, the research, calculations, disclosures and implementation guidance, detailed herein provide a consistent and transparent framework to address many of the issues associated with inconsistencies in Gross and Net IRR reporting. If adopted, the proposals will serve as a common language for investors, managers and other stakeholders which may be built on over time to further the goals of transparency and comparability. The proposed recommendations are compatible with incoming guidance from the Total Global Expense Ratio (TGER) sponsored by the Reporting Standards, INREV and ANREV as well as the 2020 GIPS standards.

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SECTION 1 INTRODUCTION

The real estate industry does not have a consistent and transparent approach to the presentation, calculation and disclosures of IRR, gross of fees and promote, net of fees and promote. Since IRR is an important performance measure relied on for strategic decision making, this lack of consistency may result in false comparisons or incorrect conclusions.

The Reporting Standards Council approved the formation of a project Task Force to address the topic. Members of the Task Force were divided into sub groups to research and communicate results to the larger group. Sub groups were organized for the following purposes:

- Research and document inconsistencies in current IRR reporting practices.
- Assess stakeholder sentiment including any perceived voids in information; how, when and what type of information facilitates understanding and analysis.
- Review the related standards promulgated by the Reporting Standards Foundational Standards and understand the roles of regulators and legislatures to ensure our guidance can serve to mitigate some of their concerns surrounding transparency and disclosures.
- Review current industry initiatives and leverage key conclusions where possible.
- Develop an easy to understand hierarchy between gross IRR, net IRR, including:
 - a clear identification and definition of IRR, gross of fees and promote, net of fees and promote;
 - components included within each level; and
 - definitions of the components.
- Develop underlying calculations and disclosures and address implementation challenges.

The findings and conclusions of the Task Force are presented herein. Upon completion, public exposure and approval by the Board and Council, resulting changes to RS Volume I will be implemented. Currently, it is expected that changes will be incorporated into RS Volume I as part of the process to reissue the Reporting Standards for 2020.

SECTION 2 RESEARCH FINDINGS AND INDUSTRY FEEDBACK

Identified inconsistencies and Mitigating Events

The Task Force’s research identified inconsistencies with respect to presentation, definition, calculations and disclosures surrounding IRR reporting which are not eliminated by existing guidance. The Foundational Standards⁵ (detailed below in Appendix A) within the Reporting Standards provide some level of guidance to approach a solution. Similarly, the other initiatives described herein provide some components that should be considered.

The inconsistencies are grouped in four broad categories shown below: presentation; definition; calculations; and disclosures. These inconsistencies were considered as a part of the research conducted and the development of the hierarchal approach suggested herein.

Presentation

- *Different accounting treatment for cost of participation in funds*; Fund level accounting of the cost of participation in a fund.
 - Example: GAAP treatment of placement and organization costs for closed-end funds is to capitalize them into the cost of the investment. Fair value reporting would require that the total cost of the investment is compared to fair market value for purposes of recognizing valuation changes. Amortization is not allowed.
 - **Recommendation:** As proposed herein, both direct and indirect fees and expenses should be included in an IRR calculation regardless of accounting treatment.

Definition

- *Inconsistent terminology*: Variance in definitions of terms are frequently noted in Fund governing documents.
 - Example: the term “fees” often includes some level of expenses (fund fees, fund expenses, promotes of operating partners, etc.) and therefore spreads are inconsistent.
 - **Recommendation:** The fees and costs included in TGER have been mapped to the hierarchy levels below. The associated definitions for terms included in each TGER category can be found in the Global Definitions Database.

TGER Category	TGER Inclusion	Mapping to Gross and Net IRR paper
Property related fees	Excluded	Deducted in Level 1
Property related costs	Excluded	Deducted in Level 1
Vehicle Related Costs	Included	Deducted in Level 2

⁵ Collectively, U.S. Generally Accepted Accounting Principles (“U.S. GAAP” or “GAAP”), the Global Investment Performance Standards (“GIPS”) and the Uniform Standards of Professional Appraisal Practices (USPAP) are the Foundational Standards within the Reporting Standards.

Ongoing Management Fees	Included	Deducted in Level 3
Transaction-Based Management Fees	Included	Deducted in Level 3
Performance Fees ⁶	Included	Deducted in Level 4

Calculation

- *Inconsistent treatment of General Partner (and/or its affiliates) interest in IRR calculations:* Variations exist in current IRR reporting. In some cases, these are included in fund net IRR, sometimes excluded and sometimes only excluded at the LP only level. Therefore, performance of a fund that typically do not pay management fees or carried interest, can (when included in the IRR calculation) inflate the overall IRR, because typically, the entity receiving the incentive fee or carried interest only has a minimal commitment.
 - **Recommendation:** The research paper recommends that the reported net IRR (Level 4) should represent the return of the LPs in the fund and therefore should exclude the GP⁷.
- *Waterfalls:* Waterfalls form the basis for certain fees charged by the general partner and/or its capital account balance (i.e., carried interest calculations). Care must be taken to ensure waterfall calculations, which form the basis for certain types of fees and distributions follow the intent of the limited partnership agreement. Limited partnership agreements outline the definitions, terms and calculations for the waterfall and it is known that these agreements can be unique and can pose significant challenges to facilitate apples to apples comparisons across funds. Although not in the scope of this research paper, caution should be exercised when performing comparative analysis.
 - **Recommendations:** Differing fee terms and structures across managers will always be embedded within IRR calculations. Drafting of waterfall provisions should include an example that attempts to illustrate all nuances of the incentive structure. Prospectively, terms utilized within waterfall calculations can be defined using the Global Definitions Database. Consider SEC recommendations for clarification of the calculation of the performance fees through the waterfall including: narrative examples in fund offerings on how performance fees are calculated; and providing performance fee calculation templates in the appendices to the fund documents in order to mitigate ambiguities concerning how the waterfall will be calculated.
- *In lieu of or on top (in addition to) of fees and costs:* Care must be taken to ensure that costs are considered and incorporated into the hierarchy in a manner consistent with the underlying nature of the charge.

⁶ In the context of the TGER paper, Performance Fees includes fund carried interest which may not be a “fee” for financial reporting purposes but generally serves to compensate the manager for performance over a threshold.

⁷ Note that in cases where the General Partner invests all or a portion of its interest in the fund pari passu to the limited partners, that portion which is pari passu is included in the limited partner amount. By deducting the non-pari passu GP interests between level 3 and level 4, the level 4 IRR should reflect the LP IRR excluding the GP entity, or portion of the GP entity, that receives incentive fee/carried interest economics. To the extent the carried interest portion of the GP cannot be separated from the pari passu GP interests, the deduction of the entire entity would be appropriate (to reflect the net LP IRR) but should be disclosed for consistency.

- Example: An investment manager may provide brokerage services in lieu of a third party and charge market rates or better for these services. This fee would be included in Level 1 with other third-party expenses. However, if the brokerage service fee charged by the investment manager was in addition to a third-party broker, that would be included in Level 3 as a fee to the investment manager.
- *Timing of capital calls-use of subscription lines:* The impact of debt on IRR, most notably due to use of subscription lines of credit and the associated timing of investor level cash flows can result in an increase to reported IRR in a Fund's life and can entitle a manager to receive carried interest.
 - **Recommendation:** Consistent with the requirements for IRR reporting and disclosures within the Reporting Standards, the inclusion or exclusion of subscription line usage in IRR calculations must be disclosed. Subscription line disclosures should highlight: (1) Any impact to the fund vintage year; and (2) Any costs involved in the subscription line. While still in early discussion, a possible framework for disclosing the impact of the subscription line at level 1 (See level 1a and 1b spread) has been included in the illustrative Examples in Appendix B.
- *Impact of Fund Structure on IRR Calculations and Treatment of Feeder Vehicles.* With respect to IRR, feeder vehicles add additional complexity in IRR calculations. Feeder vehicles typically have regulatory or taxation purposes which may lead to differences in cash flow timing and amounts which have implications to IRR calculations.
 - **Recommendation:** The hierarchy attempts to address this issue of timing in two pieces. Investor specific reporting (level 5) specifically address the timing of flows and amounts specific to a single investor. Levels 1-4 utilize the cash flow timing of the fund.
 - It should be noted that within TGER, related vehicles fees are included regardless of whether they are occurring at the feeder level, the main fund, or directly by investors to provide a full picture of the fee load of the entire fund structure. The Gross and Net IRR Task Force agrees with this methodology for fees (level 3 and level 4) but differentiated when it came to feeder specific expenses (otherwise would be deducted in level 2). Feeder related expenses generally apply only the investors in a specific vehicle and may or may not be reflective of the cost of running a fund. The issue is somewhat similar in nature to the determination of whether a transaction fee is a transaction cost or a fee (with the differentiator being whether it is market or above market). For example, transfer agent fees are typically charged to a feeder fund to record changes in ownership. If the feeder structure didn't exist and investors went directly into the fund, it's likely the transfer agent services would still be provided at a similar level of service in the main fund. This should be part of Fund load reflected in Gross and Net Fund IRR (Level 2 and 4). In contrast, however, feeder legal entity setup costs are an added cost on top of the fund load and arguably should not impact Gross IRR. Ultimately, the Task Force considered several factors including materiality and difficulty of implementation and decided to keep feeder fund expenses at level 5 at this time but may revisit in a future phase once more feedback is received on this topic.
- *Vertically Integrated vs Allocator Models:* The framework provided in the hierarchy addresses differences in these two models in several ways

- “Property level” fees charged by a vertically integrated manager for property management, development management and transactional fees, should be deducted in level 1 to the extent that they reflect market related charges. If they are in addition to, they should be reflected in level 3.
- Level 3-5 should include deductions for both fees and components of fund costs which should make them comparable across vertically integrated and allocator models.

Investors Perspective and Takeaways

In order to develop, transparent measures and meaningful disclosures surrounding gross and net IRRs which will be most useful to investors and which will be readily embraced by the real estate investment industry, a sub Task Force was formed to:

- Determine how investors assess fees and expenses in real estate funds;
- Understand challenges faced by investors when making evaluations and comparisons within and across funds;
- Assess the impact and effectiveness of industry standards and best practices; and
- Identify investor needs that are not yet being met.

The sub Task Force conducted 12 interviews of selected stakeholders including: small and large general and limited partners; fund of funds; sovereign wealth funds; foreign firms; and real estate and private equity lawyers, auditors and consultants. The sub Task Force concluded that such a wide cross-section of stakeholders would help identify the size and scope of the problem and identify the limitations of currently available information.

Key observations, conclusions and considerations from that detailed report are summarized as follows:

1. The lack of consistency in classification, definition and reporting of fees and expenses makes comparisons difficult. The respondents provided some insights into the types of fund fees and expenses which require additional transparency including:
 - Carried interest-calculation methodology and whether/when it is accrued or withheld from distributions;
 - Offsets and waivers;
 - Dead deal costs;
 - Insourced and outsourced fees and expenses; and
 - Related party fees.
2. Current industry standards and guidance are not well known and therefore, not universally adopted.
3. The size of the investor’s organization will substantially impact how internal reviews of performance and associated fees and expenses are conducted and resourced.
4. The attention to fees and expenses waxes and wanes depending on macro and micro economic factors.

5. Prospective application of standards and best practices will mitigate perceived data gathering hurdles.

Regulators and Legislatures

The Role of the SEC

For real estate managers that are registered investment advisers with the Securities and Exchange Commission (“SEC”), they will need to comply with the requirements under the Investment Advisers Act of 1940 and may also rely on applicable no-action letter guidance when disseminating performance return information. The SEC has taken the view that performance return calculations shown to current and/or prospective clients or investors may have a large impact on the client’s investment decision-making process. As such, performance returns need to be accurate and disclosures need to properly inform the current or prospective client and investors of any material facts with regard to the calculation or presentation of the performance returns shown. Below is a brief summary of the rules under the Advisers Act that can be cited in the event of an SEC examination that results in a deficiency letter or enforcement action regarding performance return calculations and the dissemination of such information. Rule 206(4)-1 under the Act applies the Section 206 antifraud provision specifically to advertising by registered advisers and advisers required to register. The rule defines certain advertising practices deemed to violate Section 206(4), including advertisements which may contain untrue statements of fact, or may be otherwise false or misleading. Enforcement actions have stated violations of Section 206(4) when advisers have directly or indirectly published, circulated, or distributed advertisements which contain any untrue statement of material fact, or which is otherwise false or misleading. Further, Rule 206(4)-8 of the Advisers Act broadly prohibits an investment adviser from engaging in fraudulent, deceptive, or manipulative activities against investors in pooled investment vehicles. Rule 206(4)-7 requires advisers to develop written policies and procedures designed to comply with the Advisers Act.

Rule 206(4)-1(b) under the Advisers Act defines the term “advertisement” to generally mean any written communication addressed to more than one person which offers advisory services, or any notice or other announcement in any publication or by radio or television. However, the SEC has described in the *Investment Counsel Association of America, Inc.* no action letter (ICAA Letter) (March 1, 2004) that whether any particular communication – or series of communications – constitutes an advertisement under Rule 204(4)-1(b) under the Advisers Act depends upon all of the facts and circumstances. In general, a written communication by an investment adviser that responds to an unsolicited request by a client, prospective client or consultant for specific information is not an “advertisement.”

The ICAA letter also stated that the SEC Staff contends, “that a written communication by an investment adviser to its existing clients generally would not be an advertisement within the meaning of rule 206(4)-1(b) merely because it discusses the adviser's past specific recommendations concerning securities that are or were recently held by each of those clients. In general, written communications by advisers to their existing clients about the performance of the securities in their accounts are not offers of investment advisory services but are part of the adviser's advisory services. If, however, the context in which the past specific

recommendations are presented by the investment adviser to an existing client suggests that a purpose of the communication is to offer advisory services, we would conclude that the communication was an advertisement”.

In other words, whether a document is considered to be an “advertisement” is a facts and circumstances case. Client or investor reporting documents or letters could potentially fall outside the definition of an advertisement if they are only provided to current investors. However, if letters or reports are provided to prospects or third parties that are not clients and it can be construed that the intent of the piece is to offer advisory services, then the documents could be considered to be advertisements. Given the subjective nature, the best practice would be to consider investor reporting information to be an advertisement and follow the advertising rules under the Advisers Act and related disclosures obligations for all communications (particularly those documents that contain performance return information).

The Advisers Act does not specifically address performance advertising. However, the SEC staff letter issued to *Clover Capital Management, Inc.* (October 28, 1986) (“Clover letter”), discusses disclosure and the use of model and actual performance results in advertisements. The Clover Letter specifies that advisers should show performance returns on a net of fees basis. In a letter to *Investment Company Institute* (September 23, 1988) (“ICI”), the SEC staff indicated that advisers could present performance on a gross basis in a one-on-one presentation to sophisticated clients, if the adviser provides certain disclosures at the same time. The SEC’s no-action letter to *Association for Investment Management and Research* (December 18, 1996) (“AIMR Letter”) permits advisers to use gross of fee results provided that the results are presented in equal prominence with net of fee results.

While not the focus of this paper, real estate investment advisers have a tendency to disseminate projected performance returns in marketing materials. While not specifically described under the Advisers Act or in relevant no-action letters, advisers should ensure the use of substantial disclosures when disseminating any sort of projected returns. Such returns may be considered to be hypothetical in nature and are subject to inherent limitations such as changes in economic and market conditions that will have a material impact on the calculations of the projected returns shown. The SEC has shown interest in evaluating the assumptions used in such projected returns to ensure that they are not misleading in any way. In addition, the SEC has been reviewing projections compared to actual realized returns to look for evidence of an adviser intentionally trying to mislead investors if the projections are always substantially higher than actual returns. The assumptions used in the underlying performance calculations and the accompanying disclosures will likely be heavily scrutinized. Currently, the Reporting Standards do not address projected performance and accordingly, issues surrounding the calculation and presentation of projected IRR’s is specifically excluded from this paper. The use of leverage and its impact on the calculation of performance returns has also been scrutinized in SEC examinations of real estate managers. For example, the use of a subscription line of credit and the effect of the line on the calculation of IRR should be disclosed (and as such is presented as a required disclosure herein). The timing of the cash flows when utilizing a subscription line vs. calling capital from underlying investors will also affect the calculations of the IRR. The impact of any sort of leverage used should be disclosed to investors.

The SEC has rigorously reviewed fees and expenses during examinations of real estate managers to ensure that the fees and expenses were adequately disclosed to clients and investors. There have been a number of SEC enforcement actions regarding fees and expenses such as proper disclosure, allocations among more than one client and/or the adviser, allocations of dead deal expenses, an adviser's use of affiliated service providers and the claims that services will be provided at or below "market rates" for such services, among other issues. The reviews were conducted at both the Fund and property level accounts. The SEC asked many advisers to reimburse fees and expenses that were not properly disclosed to clients or investors.

At times, real estate managers may be unwilling to disclose a negative IRR calculation, or determine that they do not feel that they are meaningful. The SEC staff has commented on the examination of a real estate manager that the adviser failed to disclose the specific negative gross IRR for a fund level return. Even though the adviser included a gross multiple of capital alongside the IRRs shown in the presentation, the adviser did not include the specific negative IRR. The SEC staff cited in a deficiency letter that the adviser should include both positive and negative IRRs for its fund vehicles to comply with the requirements of Section 206 and Rule 206(4)-8.

State Legislative Actions

Some state legislatures are proposing or have instituted actions which will require reporting by alternative investment firms investing on behalf of state pension funds to provide more transparency and accountability on the fees they charge. This information is required to be presented by the pension funds to the public. Of particular note, California Assembly Bill (AB) 2833 targets additional transparency with respect to specific fees and expenses charged including: fees paid directly to the alternative investment vehicle, the fund manager or related parties; carried interest; and gross and net returns. AB 2833 requires annual reporting on all existing alternative investment funds. As fiduciaries to their beneficiaries, state legislatures contend that investors need to understand the full extent of compensation to the alternative investment firms and their affiliates in order to assess the reasonableness of compensation in light of market conditions and services rendered.

Proponents of AB 2833 suggest that more transparency and uniform reporting to the private equity industry will result from a level of government intervention. Others suggest that these goals can be achieved through self-regulation. As described herein, there are industry efforts which can facilitate additional transparency. Those opposing AB 2833 also suggest that reporting of such information on existing alternative investment funds may be challenging as current document provisions may not include this level of reporting thereby requiring either separate negotiations with the general partner or exiting from funds-all at substantial costs. Implementation of any new measures and level of reporting within existing frameworks can often be challenging. Future obstacles to compliance start with clearly defined reporting within the LP agreements.

California is not the only state taking legislative action. Other state bills are in varying stages of completion.

Key Conclusions

Actions by regulatory bodies, including the SEC and some state legislatures have heightened the need for appropriate disclosures and transparency surrounding fees and expenses and gross rates of return within the

real estate industry. A review of these federal and state regulatory bodies highlights the areas where additional guidance would be beneficial to the real estate investment industry.

SEC and Legislatures	Considerations for added guidance
Broader interpretation of advertising rules and applicability	Ensuring calculations, presentations and disclosures in current fund reporting sufficiently cover advertising rules.
Presentation of both gross and net IRRs is acceptable	(See Foundational Standards section)
Use of leverage and impact on performance is being scrutinized	Providing consistency in treatment of subscription lines
Regulations may follow if self-regulation is unsuccessful	Ensuring guidance developed can be made broadly accepted by the real estate industry

Review of Foundational Standards, current industry initiatives and other publications

Review of Foundational Standards, please see Exhibit A.

Current industry initiatives

NCREIF and PREA, as sponsors of the Reporting Standards and INREV (and by license ANREV), as sponsor of the INREV Guidelines, executed a Memorandum of Understanding (MoU) for the purpose of collaborating to develop global reporting standards. The intent of this collaboration is to converge standards wherever possible and when not, to provide a path to navigate from one to the other. One of the most significant projects undertaken is the **Global Definitions Database (GDD)**. The GDD houses definitions for globally converged terms, as well as those specific to the individual sponsorship where convergence has not been achieved, either due to regional differences which preclude convergence or where convergence is targeted but has not yet been achieved. The terms used for the calculations of gross IRR, net IRR and gross to net spreads will be included in the GDD.

In addition to the above, three different but complementary initiatives provide important insights into the need for transparency with respect to fees and expenses and key takeaways utilized for this gross and net IRR research paper: **1) the global reporting standards convergence project relating to fees and expenses, sponsored by INREV, ANREV, NCREIF, and PREA known as the Total Global Expense Ratio (TGER) ; and 2) the Reporting Standards supplement the Reporting Template, sponsored by the Institutional Limited Partners Association (ILPA). Finally, an independent publication summarized below, suggests a hierarchal approach to gross and net IRR analysis.**

1) Total Global Expense Ratio (TGER)

One of the projects undertaken by the Council, through its global collaboration with INREV and ANREV, relates to providing transparency with respect to fees and expenses. This is a two -phased project, with phase

1 issued in the 2nd quarter of 2016, and phase two completed in quarter 3 of 2019. The phase 1 work, entitled *Setting the Right Path for Global Fee and Expense Metrics-Phase 1 results* provided for the identification and definition of common fees between the investment manager and the investor and costs charged by the funds to external service providers. Phase 2 expanded on the work done and conclusions reached in Phase 1. Phase 2, *Total Global Expense Ratio: a globally comparable measure of fees and costs for real estate investment vehicles* was released for public comment in 2018 and provided calculations and associated disclosures for TGER. The public response was very supportive and as such, TGER is expected to be released in final form in 2019.

2) ILPA's Reporting Template and RS supplement

In 2016, ILPA published the Reporting Template for fees and expenses. As illustrated in the chart below, a primary goal of the ILPA Fee Reporting template and the Gross Net IRR and the global fee and expense initiatives (TGER) is the same: to provide transparency in reporting of fees and expenses for all investors to facilitate investment decision making. In order to provide for comparability, the approaches vary.

Goal: Provide transparency in reporting of fees and expenses for all investors to facilitate investment decision making	
Gross Net IRR and TGER	ILPA [Fee] Reporting Template
<i>Target audience</i>	
Fund level and Investor level	Investor level
<i>Product</i>	
Performance indicators	Cost aggregation schedule
Gross IRR, net IRR and spreads; total fund fee load metric	Net asset value continuity schedule showing all economic transfers
Single metric comparison (%)	Currency based schedule
Supported by accompanying research	
<i>Utility</i>	
Comparability across funds	Not comparable across funds
Summary analysis	Detailed analysis, line by line itemization

Our approaches are different but complementary, so connecting both provides real estate investors with useful information to facilitate investment decision-making. The ILPA template is much like an investor-level capital account statement with a focus on fees and expenses, whereas the focus of the gross and net IRR guidance described herein involves the calculation of IRR, together with accompanying disclosures which are provided to detail the components of fees and expenses tied to each IRR level, provide clear definitions of each, and therefore result in consistent and comparable IRRs. In 2018, the Reporting Standards Council, with support from ILPA, embarked on the development of the Reporting Standards Supplement to the ILPA Template. This project utilizes the information required to calculate gross net IRR as suggested within the paper and other elements included in a capital call statement and maps the information to the ILPA Reporting template. The Reporting Standards Supplement is currently available for use and can be found on the Reporting Standards website (www.reportingstandards.info).

Other publications

Presenting and Reporting Performance for Private and Illiquid Assets

An approach to provide much needed transparency in gross and net IRR calculation and analysis was presented in the paper: Best Practice Considerations: *Presenting and Reporting Performance for Private and Illiquid Assets*⁸.

In the section of the paper entitled *The Performance Reporting Fee Hierarchy*, the author contends that there are five ways to present performance, each considering various levels of fees and expenses. To quote: “Each of these methods, though common practices become organized into a hierarchy.”⁹ The hierarchy is as follows:

- Pure Gross: performance at its maximum level where nothing is deducted-not fees, expenses, assumed or actual transaction costs.
- Gross: pure gross less actual transaction costs
- Net: Gross less management fee only
- Net-Net: Net less performance incentive fee and/or carried interest
- Pure Net: Net-Net less all remaining fees and expenses, typically administrative fees and expenses associated with operating a fund

Despite current industry initiatives and the Hierarchal Approach referenced the paper: Best Practice Considerations: *Presenting and Reporting Performance for Private and Illiquid Assets*¹⁰, other factors remain open for interpretation and are addressed further as part of the proposed hierarchy.

Key Conclusions

Based upon the research and analysis conducted, the Council concluded that a hierarchal approach (levels), coupled with clear identification, definition and mapping of fees and costs would result in much needed additional transparency on gross and net IRR reporting and allow for cross comparability of closed- end funds for investors.

A hierarchal approach to the presentation of gross and net IRRs and gross to net spreads provides much needed transparency into this important performance metric. The approach would not contradict, but rather complement the principles and standards promulgated by the Foundational Standards identified within the Reporting Standards. From the extensive research we undertook, we are not aware of any authoritative guidance on the consistent and transparent approach to the presentation, calculation and disclosures of IRR,

⁸ By Timothy F. Peterson, CFA, CAIA, CIPM, March 18, 2015

⁹ Page 16 of paper

¹⁰ By Timothy F. Peterson, CFA, CAIA, CIPM, March 18, 2015

gross of fees and promote, net of fees and promote. Using consistent terms and definitions provided through our global collaboration efforts fosters much needed consistency and comparability by and between funds and other performance measures.

As with any performance reporting, meaningful disclosures are a critical supplement to the analysis. As many of the investment managers in our industry are registered investment advisors, care must be taken that such disclosures comply with SEC advertising rules.

SECTION 3 PROPOSED HIERARCHY, DISCLOSURES AND EXAMPLES

Proposed Hierarchy

Based upon the research and analysis conducted, the Task Force proposed the following hierarchical approach.

Level 1

Within this hierarchy, Level 1 is the IRR of the Fund without regard to advisory fees (Ongoing, Transactional and Performance-Based) and fund costs (sometimes referred to as Fund Load). Level 1 should be net of all transaction specific costs which would be incurred during the normal investment process. Any transaction-based fees, which are not in lieu of a market transaction cost (such as a broker's fee), should not be deducted at this level (these fees will be incorporated at level 3). Additionally, level 1 should be presented net of all deal-level promote structures with joint venture partners.

During the research phase, there was substantial discussion surrounding the starting point of level 1 returns. The differences primarily landed in two camps, with the first looking first at deal-level flows (flows from the fund to individual investments) and the second focusing on investor level flows (flows from investors to the fund). As there was no clear consensus, the Task Force provided optionality at this level to address the concerns of both camps within the hierarchy framework. Some key differences between the two methods are presented below and detailed in Appendix B.

- Level 1a
 - Utilizes fund to investment flows.
 - Is unleveraged to the extent that fund to investment cash flows include cash derived from subscription line and fund level leverage.
 - More directly comparable to individual deal IRR's (See investment level IRR guidance in the RS Performance and Risk Manual).
- Level 1b
 - Utilizes investor to fund flows.
 - Net of all forms of leverage¹¹ (fund, subscription and deal-level) utilized by the fund.
 - When compared to Level 2, this method isolates the impact of "fund costs" without other noise generated from cash flow timing differences (internal fund cash management, subscription line usage, etc.).

Level 2

The Level 2 IRR builds further on the Level 1b IRR return and deducts fund related costs¹². This IRR reflects investor's experience with respect to the investments in the fund without regard to how the investment

¹¹ Contemplates all forms of leverage managed through the fund structure and its feeders. As financing structures are very diverse, this is not intended to address fund leverage occurring outside the investment vehicle, such as individuals using levered lines or other sources of leverage to fund capital calls.

¹² As further discussed in the TGER framework as "vehicle-related costs".

manager is compensated. Level 2 considers items of fund load (without fees) and is net of both fund, subscription, and investment leverage, interest expense/income from credit facilities or cash deposits.

Level 2 should be consistent with fund or account level gross time weighted return calculations required in the Reporting Standards as they are net of transaction costs and fund costs but are before investment management fees. They would be different solely due to calculation differences such as TWR start and end dates and calculation methodology (Linked Modified Dietz vs IRR).

Level 3

Level 3 begins with Level 2 and deducts ongoing investment management fees and transaction fees which are not classified as transaction costs and deducted in level 1. Any fee rebates or refunds are to be included here, regardless of where they occur. If, certain fee rebates or refunds cannot be included for whatever reason (e.g. confidentiality, difficult to allocate combined fund balances rebates, etc.), it is recommended that a general footnote be included describing the reason.

Level 4

Level 4 begins with level 3 and deducts performance-based investment management compensation, such as incentive fees and carried interest (promotes), net of any claw backs. Any GP Interests which are pari passu to the LP interests are included in level 1-4. In this step, the carried interest entity or portion of the GP should be deducted to produce a net LP IRR. If the GP interest contains both pari passu and carried interest elements and cannot be segregated, the entire GP interest should be deducted at this level. While not common, if a substantial portion of the fund is non-fee paying, it is recommended that this fact be noted in the IRR disclosures due to the potential impact on the Net IRR.

Investor specific (Level 5)

Individual Limited Partner specific reporting which captures the experience of a single investor. To include investor specific side letter negotiations or other investor specific matters such as the timing of investor cash flows, tax, and feeder vehicles. This information would only be reported to the specific investor.

Disclosure Considerations

The Task Force makes the following implementation recommendation to the NCREIF PREA Reporting Standards:

- PR.06 – Gross and Net IRR requirement
 - Require that the Gross and Net IRR include a reference to the reporting hierarchy.
 - Recommend that the Gross IRR reflect a Level 1a, 1b or Level 2 Fund level IRR with specific disclosure required in PR.06.1 for consistency and comparability across closed-end funds.
 - Recommend that the Net IRR reflect a Level 4 Fund level IRR for IRR for consistency across closed-end funds.

- PR.06.1 – Gross IRR disclosures
 - Move the existing language “The Account Report must clearly disclose what types of fees are deducted from the gross return to arrive at the net return.” to PR.06.2.
 - Require disclosure of level 1 or 2. If using level 1, user should specify the cash flow starting point (Level 1a or Level 1b).
 - Where a subscription line is used, require the disclosure of (1) the year of the first investment of the fund, (2) the length of time between the first investment and the first investor capital call.
- PR.06.2 – Net IRR disclosures
 - Move the existing language from PR.06.1 to PR.06.2 “The Account Report must clearly disclose what types of fees are deducted from the gross return to arrive at the net return.”
 - If a level 1 IRR is provided to satisfy the Gross IRR requirement, require that the spread between gross and net mention vehicle related costs (aka “fund load” or “Fund costs”) as part of the spread.
 - The existing RS requirements require disclosures for net IRR where different fee arrangements exist (“the Account Report must disclose the impact of these fees on IRR expressed, at a minimum, as a basis points range”). Since the Task Force is recommending level 4a to be used as a fund Net IRR, any non-fee-paying class (e.g. GP pari passu investment or “Friends and family” investors, etc.), would need to be part of this disclosure.
- PR.06.3
 - No changes recommended

Illustrative Examples

Appendix B contains illustrative examples and disclosure recommendations which may help with implementation.

SECTION 4 POTENTIAL TOPICS FOR FUTURE PHASES

Future phases of this project may include:

- Property and Investment level IRR.
- Unleveraged IRR and other theoretical IRR calculations
- Investment Multiples
- Side Pockets and Side Cars

APPENDIX A

Foundational Standards Reviewed

The Reporting Standards are intended to supplement, but not contradict, standards established by authoritative organizations including U.S. Generally Accepted Accounting Principles (GAAP) established by the Financial Accounting Standards Board (FASB), the Global Investment Performance Standards (GIPS®) promulgated by the CFA Institute and the Uniform Standards of Professional Appraisal Practices (USPAP) established by the Appraisal Foundation. Collectively, these standards are known as the Foundational Standards within the Reporting Standards.

As summarized herein, the Foundational Standards organizations provide some information to guide the conclusions reached by the Council on this subject matter. It should be noted that USPAP does not address internal rates of return and is therefore not included within this review.

US GAAP

Within the US private institutional real estate investment industry, performance measures generally use the fair value based financial statement information as inputs. Accordingly, a review of the accounting principles and disclosures provides important insights into the presentation and of gross and net IRRs.

Investment managers issue fund reports to investors which follow either the FASB Accounting Standards Codification (ASC) 946, *Financial Services-Investment Companies* (Investment Company Accounting) or ASC 960, *Plan Accounting-Defined Benefit Plans* or the Government Accounting Standards Board (GASB) 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans* (Pension Fund Accounting). Within the Reporting Standards, two models are used to present and report information in accordance with US GAAP-the Operating Model and the Non-operating Model. The *NCREIF PREA Reporting Standards Fair Value Accounting Policy Manual* (Accounting Policy Manual) provides interpretive accounting guidance as well as sample financial statements for reporting.

Investment Company Accounting requires the presentation and disclosure of certain financial highlights. Within these disclosures is a requirement to report an “investment return” which can be either a time-weighted return or an IRR. US GAAP dictates when IRR reporting is required. Generally, closed-end real estate funds which are classified as investment companies will be required to report an IRR. The open-end real estate funds which are also investment companies generally report time-weighted returns (TWR) within their financial highlights. Regardless of whether TWR or IRR is reported, both must be reported both gross and net of all fees and incentives.¹³

¹³ FASB Accounting Standards Codification (ASC) 946, *Financial Services, Investment Companies*; 946-205 *Presentation of Financial Statements* and 946-204-50 *Disclosure*.

Pension Fund Accounting under US GAAP does not require reporting of financial highlights (to include returns).

Irrespective of the underlying US GAAP accounting, investment management fees are reflected in the statement of operations and there is accompanying disclosure concerning a description of the fees incurred and manner in which these fees are calculated. Certain management fees are paid outside of the fund, directly to the investment manager. In that case the fees are not reflected in the statement of operations, but are disclosed in the footnotes. Within the Accounting Policy Manual, investment management fees are included within the broader category of real estate advisory fees. Other real estate advisory fees include acquisition, disposition, asset management, financing, incentive fees and carried interest. Although generally recognized in the financial statements as a payable to the investment manager when earned, the fee incurred may be reported as an asset on the balance sheet (as is the case of acquisition, disposition and financing fees) or as an expense in the statement of operations (as is the case with asset management and investment management) or apportioned between the balance sheet and income statement if the calculation has both an income and appreciation component (as is the case with incentive fees).

When paid to affiliated entities, other costs charged to the fund by the investment manager are reflected within disclosures surrounding related party transactions. All related party transactions are required to be disclosed regardless of financial statement materiality. A word of caution however is that not all fees and costs paid to affiliates should be included in the spread between gross and net IRR tiers. For example, a market-based leasing commission paid to an affiliate in a vertically integrated firm is a normal cost of operating a property and as such would not be included in the spread between gross and net IRR tiers.

As expected, any fees or costs billed separately to the fund investors would not be reported within the financial statements of the fund, something which constitutes an inconsistency in gross and net IRRs highlighted above. As an example, if the investment manager billed its fee outside of the fund and the fund had ongoing distributions to its investors, the manager may reduce the payment to the investor by the fee. The financial statements however would reflect the distribution at its full amount, not the amount of the net payment the investor received. In order to promote comparability across funds, when fees are charged outside of the fund, the Reporting Standards require disclosure of the impact of these fees on IRR to be expressed, at a minimum, as a basis points range¹⁴.

Frequently, specific investors in funds may negotiate side agreements which provide for complicated fee structures and/or fee rebates.

In conclusion, US GAAP does not specifically require IRR for all types of funds. When IRR is required, GAAP requires both gross and net IRR with net IRR after deduction of all fees and promotes. As certain fees and costs can be paid outside of the fund or inside of the fund, the gross net spreads across funds may not be comparable. Finally, care should be exercised understanding the nature of the fees and costs incurred by the

¹⁴ Section PR.06.2, NCREIF PREA Reporting Standards Handbook Volume 1, March 31, 2014.

fund, so that such fees and costs which are typically incurred as a part of property operations should be excluded from gross to net spreads.

To summarize:

- When IRR is required, both gross and net IRR must be presented
- Net IRR must be calculated after deduction of all fees and promotes
- Certain fees can be paid inside or outside of the fund and U.S. GAAP captures only those inside of the fund, so gross to net IRR spread across funds may not be comparable
- Fees and costs incurred as part of property operations are excluded from gross to net spreads

GIPS®

General

As stated in the Reporting Standards Handbook Volume I, the performance and risk elements draw upon the GIPS standards for basic ethical principles such as full disclosure and fair representation of investment performance and for other specific methodologies and disclosures. The Reporting Standards do no conflict with the GIPS standards, and compliance with the Reporting Standards is not predicated on compliance with the GIPS standards. However, it is important to note that the GIPS standards apply on a firm-wide basis only, while the Reporting Standards apply more specifically to Account/Fund reporting. As such, the performance and risk measurement elements of the Reporting Standards do not incorporate all elements of the GIPS standards. Similarly, the Reporting Standards contain elements which the GIPS standards do not address.

An exposure draft, encompassing a complete overhaul of the GIPS standards was released for comment in 2018 (2020 GIPS Exposure Draft). Included in 2020 GIPS Exposure Draft is the elimination of real estate chapter (and other specific chapters like private equity) in favor of a single set of standards applicable to all private market investments. The Reporting Standards Board and Council provided a detailed [response](#) to the 2020 GIPS Exposure Draft. The 2020 version of the GIPS standards was released in June 2019. The information presented herein does not contradict the 2020 version of the GIPS standards.

Key Conclusions from Review of Foundational Standards

The intent of this research is to supplement, but not contradict either U.S. GAAP or the GIPS standards.

APPENDIX B

Illustrative Example - The Gross - Net Heirarchy^{1,2,3}

Level	Level Description	TGER Alignment and Other Notes ⁴	IRR (%)	Nominal Amount (\$)	3/31/2015	6/30/2015	9/30/2015	12/31/2015	3/31/2016	6/30/2016	9/30/2016	12/31/2016	3/31/2017	6/30/2017	9/30/2017	12/31/2017	3/31/2018	6/30/2018	9/30/2018	12/31/2018	3/31/2019
Level 1a	Gross IRR before investment management fees and fund Costs but net of transaction costs.	Consistent with TGER, Fund Gross IRR should be net of property-related costs and property related "fees in lieu" of costs. See TGER detailed Fee and Cost Matrix for details.	16.73%	794	(500.00)	(500.00)	-	-	6.50	6.50	10.00	7.50	7.50	6.50	10.00	7.50	10.00	6.50	10.00	7.50	1,697.50
Subtract:	Cash flow Adjustments related to fund or subscription leverage or timing differences of investor capital flows vs investment capital flows.	In the instance of fund leverage, Draws, Principal repayments and interest are treated as if it were equity.																			
Level 1b	Gross IRR before investment management fees and fund Costs but net of transaction costs.	Consistent with TGER, Fund Gross IRR should be net of property-related costs and property related "fees in lieu" of costs. See TGER detailed Fee and Cost Matrix for details.	19.40%	790.00			503.50	500.00	6.50	6.50	10.00	7.50	7.50	6.50	10.00	7.50	10.00	6.50	10.00	7.50	1,697.50
Subtract:	Vehicle-related costs	See TGER detailed Fee and Cost Matrix		(2.50)					(0.50)				(0.50)			(0.50)			(0.50)		(0.50)
Subtract:	Vehicle-related taxes	See TGER detailed Fee and Cost Matrix		(1.00)					(0.25)	(0.25)				(0.25)				(0.25)		(0.50)	(0.50)
Level 2	Fund Gross IRR after deduction for fund costs but before deduction of recurring, transactional and Performance fees	IRR after the deduction of vehicle related costs.	19.30%	786.50			(503.50)	(500.00)	5.75	6.25	10.00	7.50	7.00	6.25	10.00	7.00	10.00	6.25	9.50	7.50	1,697.00
Subtract:	Investment management fees	See TGER detailed Fee and Cost Matrix		(45.31)			(1.56)	(3.13)	(3.13)	(3.13)	(3.13)	(3.13)	(3.13)	(3.13)	(3.13)	(3.13)	(3.13)	(3.13)	(3.13)	(3.13)	(3.13)
		Includes all ongoing and transactional based fees, regardless of whether paid in fund, directly to to manager, or through feeder vehicle. Transaction fees charged by manager above market transaction costs should be deducted here. Transaction fees in lieu of transaction costs, should be included in the Fund Gross IRR (Level 1)																			
Level 3	Fund Net IRR before Performance-based fees. Level 2 less ongoing and transactional investment management fees		18.06%	741.19			(505.06)	(503.13)	2.63	3.13	6.88	4.38	3.88	3.13	6.88	3.88	6.88	3.13	6.38	4.38	1,693.88
Subtract:	GP Incentive Fees and Carried Interest	Includes all performance related fees (incentive, promotes, carried interest, etc, net of rebates, regardless of whether paid in fund, directly to to manager, or through feeder vehicle.		(133.41)			-	-	-	-	-	-	-	-	-	-	-	-	-	-	(133.41)
Level 4	Fund Net IRR. Net of transaction costs, Fund costs, Ongoing, Transactional and Performance fees		15.29%	607.77			(505.06)	(503.13)	2.63	3.13	6.88	4.38	3.88	3.13	6.88	3.88	6.88	3.13	6.38	4.38	1,560.46
Adjust	Investor specific adjustments	Filter level 5 to individual investor specific timing, costs and fees.		(508.81)			429.30	427.66	(2.23)	(2.66)	(5.84)	(3.72)	(3.29)	(2.66)	(5.84)	(3.29)	(5.84)	(2.66)	(5.42)	(3.72)	(1,138.59)
Level 5	Individual Investor Net IRR	Net of fund load, fees and promote as experienced by the individual investor.	16.39%	98.97			(75.76)	(75.47)	0.39	0.47	1.03	0.66	0.58	0.47	1.03	0.58	1.03	0.47	0.96	0.66	241.87

Illustrative Example Notes:

¹The simplified example has been provided solely for the purpose of understanding the components of performance within the Gross-Net IRR hierarchy. Performance results are not intended to represent actual or representative results of any fund, investment or strategy. Similarly, the differences between levels are not intended to be representative of spreads which would be achieved with actual fund results.

²The examples utilize quarterly cash flows for simplicity. Existing guidance within the NCREIF/PREA Reporting standards or other foundational standards would typically dictate the minimum required cash flow frequency (daily, monthly, quarterly).

³The paper and related examples do not address characterization of cash inflows and outflows for investment multiple purposes.

⁴The examples reference the "Detailed Fee and Cost Matrix" in the appendices of the Total Global Expense Ratio consultation paper dated April 2018.

Presentation Example 1 - SI IRR and Disclosures

Fund XYZ

Since Inception Internal Rate of Return (IRR)

	Inception to date
Gross of Fee ^{1, 2}	#REF!
Net of Fee ³	#REF!

Example of recommended and required disclosures with proposed RS amendments.

¹Gross IRR

The Gross Fund IRR has been calculated using the level 2 Fund IRR methodology described by the NCREIF PREA Reporting Standards. Gross returns are presented net of transaction costs and fund costs but do not reflect the deduction of investment management fees. Results are presented net of all leverage.

²Subscription Line

The fund utilizes a subscription line of credit. In January 2015 the fund utilized a subscription line of credit to purchase its first investment. The first capital call from investors was September 2015.

³Net IRR

The Net Fund IRR has been calculated using the level 4 Fund IRR methodology described by the NCREIF PREA Reporting Standards. The Net IRR reflects the deduction of all fund costs, transaction costs, and investment management fees. Carried interest to the general partner and its affiliates has been accrued based on the hypothetical liquidation value of the fund at fair value. Limited partners pay ongoing asset management fees ranging between 0 and 150 basis points. Carried interest is charged to investors based on the waterfall hurdle and range between 0 and 200 basis points based on the hypothetical liquidation of the fund at fair value.

Presentation Example 2 - SI IRR and Disclosures

Fund XYZ

Since Inception Internal Rate of Return (IRR)

	Inception to date
Gross of Fee ^{1, 2}	#REF!
Net of Fee ³	#REF!

Example of recommended and required disclosures with proposed RS amendments.

¹Gross IRR

The Gross Fund IRR has been calculated using the level 1a Fund IRR methodology described by the NCREIF PREA Reporting Standards. Gross returns are presented net of transaction costs but do not reflect the deduction of investment management fees or fund costs. Results are presented gross (before the impact) of the subscription line but net (after the impact) of all property leverage.

²Subscription Line

The fund utilizes a subscription line of credit. In January 2015 the fund utilized a subscription line of credit to purchase it's first investment. The first capital call from investors was September 2015.

³Net IRR

The Net Fund IRR has been calculated using the level 4 Fund IRR methodology described by the NCREIF PREA Reporting Standards. The Net IRR reflects the deduction of all fund costs, transaction costs, and investment management fees. Carried interest to the general partner and its affiliates has been accrued based on the hypothetical liquidation value of the fund at fair value. Limited partners pay ongoing asset management fees ranging between 0 and 150 basis points. Carried interest is charged to investors based on the waterfall hurdle and range between 0 and 200 basis points based on the hypothetical liquidation of the fund at fair value.