

# HANDBOOK VOLUME II: MANUALS



NCREIF PREA  
**Reporting Standards**

Updated

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## FAIR VALUE ACCOUNTING POLICY

This NCREIF PREA Reporting Standards Manual has been developed with participation from NCREIF's Accounting Committee. The Manual has been endorsed and approved by the Reporting Standards Council.

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The Pension Real Estate Association (PREA)

NCREIF and PREA encourages the distribution of these standards among all professional interested in institutional real estate investments. Copies are available for download at [www.reportingstandards.info](http://www.reportingstandards.info)

This NCREIF PREA Reporting Standards Fair Value Accounting Policy Manual is dedicated to the memory of John Venezia, who passed away in May 2020. John was a loving husband and dedicated father, a finance Director at TIAA-CREF, former Chair of the NCREIF Accounting Committee, and a beloved member of our community. Over his many years of involvement, John made significant contributions to this manual and the real estate industry. John was dedicated to the profession and was always willing to creatively find solutions that positively impacted the real estate industry. More importantly, John was a great person, someone everyone wanted to spend time with. John loved spending time with his family, listening to music and playing the guitar with his 4th band since 1978 "Sugarush". He will be missed by all.



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## INTRODUCTION

### 1.01 Purpose

The purpose of the NCREIF PREA Reporting Standards (“Reporting Standards”) Fair Value Accounting Policy Manual (the “Manual”) is to provide a consistent set of accounting standards when preparing financial statements for the institutional real estate investment community. In 1983, in response to the needs of the investor community, the NCREIF Accounting Committee developed guidelines for fair value accounting to be used by the institutional real estate investment industry. These accounting standards are supported by authoritative U.S. GAAP (“GAAP”) and non-authoritative accounting guidance when GAAP does not sufficiently address a particular topic. As noted in the Reporting Standards, Volume I, Fair Value Generally Accepted Accounting Principles (“FV GAAP”) is the foundational standard for fair value accounting used to report by the institutional real estate investment community to both tax-exempt investors (e.g., pension funds) as well as taxable investors (e.g., Funds and international investors). It is the intent of this Manual for users to prepare financial statements that comply with GAAP, while supporting the Reporting Standards in a consistent and transparent manner. Furthermore, the topics within the Manual are limited to those topics specifically relevant to reporting real estate investments at fair value. As an additional resource, there is The NCREIF PREA Reporting Standards Debt Fund Manual that is to provide a consistent set of accounting standards when preparing financial statements for debt funds.

Where applicable guidance is not specified within authoritative GAAP, non-authoritative guidance may be applied. The appropriateness of the sources of non-authoritative guidance depends on its relevance to particular facts and circumstances, and the specificity of the guidance to the facts and circumstances. The lack of applicable authoritative accounting guidance specific to the institutional real estate investment industry has caused certain fair value accounting practices and alternative presentations - prevalent in the industry - to constitute non-authoritative GAAP. These practices are included in the Manual.

The main objective of this Manual and related appendices is to provide a consistent set of accounting standards applicable to those aspects of the preparation of financial statements that are unique or significant to private institutional real estate entities. This Manual and related appendices are not intended to address a comprehensive application of GAAP to the preparation of financial statements of real estate entities. Users of this Manual and the related appendices should consider all recently issued ASUs whether included or excluded in this Manual to determine their effect on the preparation of financial statements.

### 1.02 Organization of manual

In addition to this introduction, this Manual has separate sections that address the three levels of accounting: Fund Level, Investment Level and Property Level. Included in the appendices are illustrative financial statement examples presented under the Operating Model and Non-operating Model.

### 1.03 Terminology

Certain terms as used herein are defined as follows:

- Fund: Includes all commingled funds, co-investments, joint ventures and single-investor investment accounts; a Fund has one or more investments and could include real estate and debt investments.
- Investment: A discrete asset or group of assets held for income, appreciation, or both and tracked separately
- Property: A real estate asset
- Operating Model: A financial statement presentation method in which all investment (property) level assets and liabilities are presented on a gross basis.
- Non-operating Model: A financial statement presentation method in which all investment (property) level assets and liabilities are presented on a net basis.
- Financial Accounting Standards Board (“FASB”): The Financial Accounting Standards Board is the designated organization for establishing standards of financial accounting and reporting. Those standards govern the preparation of financial reports. The FASB is officially recognized as authoritative by the Securities and Exchange Commission (“SEC”) and the American Institute of Certified Public Accountants.
- Accounting Standards Codification (“ASC”): Codification of FASB standards that comprise GAAP.
- Accounting Standards Update (“ASU”): A document issued by the FASB in the United States, which details accounting standards and guidance on selected accounting policies set out by FASB.
- Governmental Accounting Standards Board (“GASB”): The designated organization to establish and improve standards of state and local governmental accounting and financial reporting that will result in useful information for users of financial reports and guide and educate the public, including issuers, auditors, and users of those financial reports.
- American Institute of Certified Public Accountants (“AICPA”): The AICPA represents the CPA profession nationally in regard to rule-making and standard-setting and serves as an advocate before legislative bodies, public interest groups, and other professional organizations. The AICPA develops standards for audits of private companies and other services performed by CPAs.
- Accounting principles generally accepted in the United States of America (“U.S. GAAP” or “GAAP”): The United States Accounting standards established by the FASB. GAAP are the standards, conventions, and rules that accountants follow in recording and summarizing transactions and in preparing financial statements. GAAP, measured at fair value, is the foundational standard for accounting within the Reporting Standards.
- Reporting Entity – The entity that is preparing the financial statements, which is typically a Fund as defined above

## 1.04 Fair value

### 1.04(a) Introduction

The fundamental premise for fair value-based accounting presentation is based on existing authoritative accounting standards which require that certain investments held by certain tax-exempt investors, including defined benefit pension plans and endowments are reported at fair value. FASB ASC 960, which applies to corporate plans, requires that all plan investments be reported at fair value because that reporting provides

the most relevant information about the resources of a plan and its present and future ability to pay benefits when due. In addition, GASB Codification Section Pe5, Pension Plans-Defined Benefit, and Section Pe6, Pension and Other Postemployment Benefit Plans — Defined Contribution, requires government-sponsored pension plans to present investments at fair value in their financial statements. Defined benefit and government-sponsored pension plans often invest in real estate and/or real estate companies. Accordingly, the more traditional historical cost basis of accounting used by other real estate operating companies is not appropriate, as it does not provide these tax-exempt investors with relevant financial information.

#### **1.04(b) Unit of Account for Valuation Purposes**

The unit of account determines what is being recognized for reporting purposes by reference to the level at which the asset or liability is aggregated (disaggregated) for purposes of applying other accounting pronouncements. The unit of account for the asset or liability should be determined in accordance with the provisions of other accounting pronouncements (ASC Topic 820, Subtopic 10, Section 35).

Fund management makes a policy election to determine the Fund's unit of account for valuation purposes. Fund management's policy should be consistently applied to its real estate investments. Real estate investments may include, but are not limited to, Real estate investments and improvements, Unconsolidated real estate joint ventures, Mortgage and other loans receivable and Other real estate investments. The Fund management also should consider the Fair Value Debt Option guidance under ASC Topic 825, Financial Instruments.

##### One Unit of Account

Fund Management can elect to value its real estate investments by valuing its net equity position in its underlying real estate investments.

##### Separate Units of Account

Fund management can elect to fair value its real estate investments by fair valuing each of the assets and liabilities of its real estate investments separately considering the characteristics of the underlying real estate.

The policy election of unit of account for valuation purposes can be made independently of the election of the reporting framework discussed in Section 2 below. Factors for management to consider when making the unit of account election include:

- How a market participant would value the underlying investments.
- The availability of objective and verifiable market evidence to support inputs used to determine the valuation of the underlying investments.

Once management makes the unit of account election, it is management's responsibility to make sure the real estate investment valuations are reported from the appropriate perspective (net equity or assets and liabilities separately).

If a Fund elects to value its real estate investments using one unit of account and presents its financial statements using the Operating Model, management needs to also determine a consistent and rational methodology to allocate the fair value of the net equity position to the underlying assets and liabilities of its real estate investment.

If a Fund elects to value its real estate investments using separate units of account and presents its financial statements using the Non-operating Model, management needs to sum up the fair value of the assets less the fair value of the liabilities to determine the amount to report as its real estate investments on its Statement of Net Assets.

1.04(c) The Reporting Standards require that financial statements report Investments at fair value, for incorporation into the Fund report. Fair value measurements and disclosures under both the Operating and Non-operating presentations are determined in accordance with ASC Topic 820, Fair Value Measurement (ASC 820).

1.04(d) Fair value as defined under ASC 820 is “the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.” Accordingly, assets and liabilities reported at fair value include unrealized gains and losses that would be realized by investors in a hypothetical sales transaction at the date of Statement of Net Assets.

## **1.05 Relevant accounting and auditing guidance**

1.05(a) Relevant accounting guidance contained in authoritative FASB ASC topics have been considered in the development of this edition of the Manual.

## **1.06 International Financial Reporting Standards (IFRS)**

1.06(a) International Financial Reporting Standards (IFRS) is a basis of accounting applied by U.S. and non-U.S. real estate entities. IFRS permits an entity to adopt an accounting policy that elects to report all investment properties either under the fair value or cost accounting model as defined in International Accounting Standards (IAS 40), Investment Properties. An investment property is defined by IAS 40 as land or a building, or part of a building or both held (by the owner or by the lessee under a finance lease) with the intention of earning rental incomes or for capital appreciation or both. The cost model under IFRS is similar to the depreciated cost model under U.S. GAAP.

1.06(b) IFRS defines an investment entity, under IFRS 10, as having similar attributes to those of an investment company defined under U.S. GAAP. However, an entity reporting under IFRS does not need to meet the criteria of an investment entity in order to report real estate under a fair value accounting framework. An essential element of the definition of an investment entity is that it measures and evaluates the performance of substantially all of its investments on a fair value basis in the belief that a fair value framework results in more relevant information than, for example, consolidating its subsidiaries or using the equity method for its interests in associates or joint

ventures. With the issuance of IFRS 13, Fair Value Measurement, the definition of fair value under IFRS generally aligns with the definition of fair value under U.S. GAAP.

## **1.07 Disclaimers**

1.07 GAAP is the primary source when addressing any accounting topic in this Manual. Non-authoritative GAAP is a secondary source when GAAP does not sufficiently address the topic in a comprehensive manner.

As an additional resource for debt funds there is the NCREIF PREA Reporting Standards Debt Fund Manual available.

## FUND LEVEL ACCOUNTING

### 2.01 Introduction

2.01(a) The Fund Level represents the aggregation of all investments (a Reporting Entity may hold only one investment or multiple investments). In addition, it includes other assets, liabilities, income and expenses, as well as portfolio level debt that are not specifically allocated to a single investment.

2.01(b) As indicated previously, the Operating Model and the Non-operating Model provide alternative presentations while generally resulting in the same net asset values; diversity exists when determining which model is presented. The determination of the appropriate fair value reporting presentation to use is made by the entity's management based on a review of the relevant accounting literature. Reporting Standards require FV GAAP through application of either one of these presentations.

2.01(c) The information contained in this section is separated based upon the applicable reporting presentation.

### 2.02 Fair Value Net Asset Value ("FV NAV")

2.02(a) The intent of the Reporting Standards is to report the FV NAV of the Reporting Entity. FV NAV represents the fair value of the Reporting Entity's investment in the underlying investments owned (i.e., the fair value of the investments and other assets in excess of the fair value of the liabilities). While not all assets and liabilities under GAAP are required to be measured at fair value, the investments make up the vast majority of the Statement of Net Assets and both the Operating Model and Non-operating Model presentations require investments to be reported at fair value in accordance with ASC 820. Therefore, the FV NAV reported under both the Operating Model and Non-operating model will generally be the same.

2.02(b) It should be noted that there may be circumstances where the FV NAV may differ under the different financial statement presentations, for example, if a Reporting Entity applying the Operating Model does not elect to record its debt at fair value under the Fair Value Option, as further discussed in Section 4.04.

### 2.03 Overview of Operating and Non-operating Presentations

#### 2.03(a) Operating and Non-Operating Model

This Manual provides a consistent set of accounting standards for the institutional real estate investment community. Entities investing in real estate generally present their financial statements using the Operating Model (i.e., a gross presentation) or Non-operating Model (i.e., a net presentation). Fund management makes an accounting policy election to determine which presentation to utilize. Refer to Sections 2.04 and 2.05 below for further detail on the Non-operating and Operating Models, respectively.

The Reporting Standards require fair value financial information for all investments. The NAV of a Fund should generally be the same under either reporting presentation. Varying interpretations of these two presentations exist. Other bases of presentation that may be used in the global real estate industry are not addressed within this Manual. The determination of the appropriate model to be used by a Fund is made by fund management.

2.03(b) Tax-exempt and taxable Reporting Entities investing in real estate have generally presented their financial statements under the Operating Model and Non-operating Model, respectively. However, diversity in practice exists in how various entities choose or apply either reporting presentation. For example, certain taxable entities may elect to apply the Operating Model (i.e., a gross presentation) in their financial statements for enhanced transparency to the performance of the entity's equity and debt investments. The differences between the two models are generally related to presentation, and therefore the application of both models to the same investment will generally result in the same net asset value of the Reporting Entity.

2.03(c) The fundamental premise for fair value-based accounting presentations is based on existing U.S. GAAP which require that certain investments held by tax-exempt investors, including defined benefit pension plans and endowments, are reported at fair value. This presentation is supported by FASB ASC Topic 960, Plan Accounting — Defined Benefit Pension Plans (ASC 960), and Governmental Accounting Standards Board (GASB) Codification Section Pe5, Pension Plans-Defined Benefit, and Section Pe6, Pension and Other Postemployment Benefit Plans — Defined Contribution, and is referred to throughout the Manual as the Operating Model.

2.03(d) Over the years, investments made by fund managers have become increasingly complex, and it has become apparent that many of these Funds have attributes similar to those of an "investment company," as set forth in ASC Topic 946, Financial Services — Investment Companies (ASC 946), (significant content derived from the AICPA Audit and Accounting Guide — Investment Companies) (the "AICPA Investment Company Guide"). This authoritative guidance also supports the use of a fair value accounting presentation for investment companies when a Fund meets the requirements to report as an investment company under ASC 946.

2.03(e) GAAP hierarchy is defined in two levels known as authoritative guidance and non-authoritative guidance. All authoritative GAAP is codified within a single source known as the ASC. Authoritative guidance takes precedent over non-authoritative guidance. However, non-authoritative guidance is applied for a particular transaction, item, or event when applicable guidance is not specified within authoritative guidance. As indicated above, ASC 960 is the authoritative accounting source for certain tax-exempt investment vehicles that hold real estate investments, and ASC 946 is the primary source for entities that satisfy the criteria of an investment company. Given the lack of specific authoritative GAAP applicable to a single model for the institutional real estate investment industry, a dual-reporting model prevails in the industry.

## 2.03(f) Other Common Fund Structures

Many real estate funds adopt complex fund structures to increase flexibility in pricing, tax synergies and access to alternative distribution channels for their shares. A master-feeder fund structure typically comprises one or more feeder funds that invest substantially all of their assets in a master fund. External investors hold equity interests in the feeder funds, while the master fund pools assets of all of its feeder funds and invests them in accordance with its investment strategy. Under current SEC views, the annual reports of feeder funds should contain two sets of financial statements: one for the master fund and the other for the specific feeder fund. Another common fund structure is fund-of-funds, which are investment companies that invest in other investment companies. A typical fund-of-funds structure involves investments in more than one investee fund. A master-feeder structure can also be viewed as a fund-of-funds, but the feeder usually invests substantially all of its assets into one investee fund (the master fund) and the master fund invests in investee funds.

As noted in the SEC's Investment Management Guidance Update No. 2014-11, in the circumstances of both master-feeder funds as well as fund-of-funds, generally, the SEC staff has taken the position that non-consolidated financial statements are most meaningful. For additional guidance around these structures and financial statement presentation, see Chapter 5 of the AICPA Investment Company Guide.

## 2.03(g) Fund Level Organizational Costs

Newly formed investment companies typically incur organization costs when forming the legal entity to conduct business under the entity's domicile. In accordance with ASC 946, and under ASC paragraph 720-15-25-1, organization costs should be expensed as incurred.

Note: There may be Funds that maintain offering documents or limited partnership agreements that allow the Fund to capitalize and amortize initial organization costs over a pre-determined time period (i.e., 5 years). This could result in differences between US GAAP and FV NAV for the Fund. This Manual recommends that financial statement preparers discuss this scenario, when applicable, with their external auditors and other advisors.

## 2.03(h) Offering (Syndication) Costs

A newly formed entity may incur offering or syndication costs in connection with raising capital for a Reporting Entity. In accordance with ASC 946, offering costs of closed-end funds should be charged to equity/capital. For open-end funds, offering costs should be treated as a deferred charge and deferred until the beginning of operations and amortized to expense over 12 months.

## 2.04 Non-operating Model

### 2.04(a) Introduction

Many investment funds that satisfy the criteria of an Investment Company in accordance with ASC 946 may prepare financial statements under the Non-operating Model. Financial statements prepared under the Non-operating Model report all investments at fair value on a recurring basis. Each presentation may report revenue recognition differently utilizing either the dividend method or the equity in earnings method; however, FV NAV should generally be the same under both methods. ASU 2013-08, Financial Services - Investment Companies (Topic 946): Amendments to the Scope, Measurement, and Disclosure Requirements, was issued in June 2013 and amends the scope, measurements and disclosure requirements in ASC 946. The FASB decided not to address issues related to the applicability of investment company accounting for real estate entities and the measurement of real estate investments at that time. The FASB did not intend for the amendments in this update to change the practice of real estate entities for which it is industry practice to issue financial statements using the measurement principles in ASC 946. As a result, diversity in practice continues to exist where reporting entities may use a combination of presentation attributes of either model. Additionally, the FASB decided to maintain the scope exception in ASC 946 applicable to real estate investment trusts ("REITs"). REITs that exhibit the attributes of an investment company within the framework of ASC 946 may be eligible to report investments at fair value. This Manual recommends that financial statement preparers discuss the applicability of ASU 2013-08 to their financial statements with their external auditors and other advisors.

The Non-operating Model generally utilizes a "net" presentation. The Statement of Net Assets presents real estate investments as a single line item, by presenting the Fund's fair value of its net equity position in each of its real estate investments. The Statement of Operations generally reports investment income as the cash that the Fund receives as Income distributions from real estate equity investments. Any undistributed profits from the investment's operations are reported through change in unrealized gain or loss when the Fund fair values the net working capital of its underlying investment in real estate. However, diversity in practice exists where some Funds reporting under ASC 946 may provide an alternative presentation and the NAV of a Fund should generally be the same under either approach. At this time, authoritative GAAP does not specifically address financial statement presentation as it relates to a real estate entity reporting at fair value.

### 2.04(b) Election of the Fair Value Option under ASC 825-10

The Fair Value Option under ASC 825-10 permits entities to elect a one-time irrevocable option to measure financial instruments including, but not limited to, notes payable and portfolio level debt at fair value in accordance with ASC 820 on an instrument-by-instrument basis. Further information can be found in Sections 4.04 and 4.05.

### 2.04(c) Consolidation - Applicability of ASC 810

ASC 810-10-15-12d states, “Except as discussed in paragraph 946-810-45-3, an investment company within the scope of Topic 946 shall not consolidate an investee that is not an investment company.” Rather, those controlling financial interests held by an investment company shall be measured in accordance with guidance in Subtopic 946-320, which requires investments in debt and equity securities to be subsequently measured at fair value.

The exception referred to above, discussed in paragraph 946-810-45-3, refers to instances in which the investment company has an investment in an operating entity (i.e., does not meet criteria of an investment company under ASC 946) that provides services to the investment company, for example, an investment adviser or transfer agent. In those cases, the purpose of the investment is to provide services to the investment company rather than to realize a gain on the sale of the investment. If an individual investment company holds a controlling interest in such an operating entity, consolidation is appropriate.

Additionally, if an intermediate entity such as a blocker corporation or REIT is wholly owned by an investment company and acts as an extension of the investment company’s operations and to facilitate the investment strategy, it could be considered for consolidation in accordance with ASC 810.

See section 2.05(c) for additional information.

#### **2.04(d) Consolidation - Applicability to Investment in an Investment Company**

GAAP is silent on the topic of when it is appropriate for an investment company to consolidate another investment company in which it holds a controlling financial interest. Accordingly, diversity in practice exists in this area. Refer to the Basis for Conclusion in ASU 2013-08 (BC 62 to 65) for further information on the concerns of the board and stakeholders when they contemplated this issue as part of the Investment Company project.

#### **2.04(e) Equity Method**

Under ASC 946, for the non-operating model an investment company cannot apply the equity method of accounting to a noncontrolling interest in another investment company. Such an investment must be measured by an investment company at fair value in accordance with ASC 946-320.

#### **2.04(f) Revenue Recognition**

As mentioned above there is diversity in practice regarding revenue recognition under the Non-operating Model presentation. However, revenue is typically recognized when dividends are received from the investee to the extent of undistributed earnings by the investee (e.g., tax basis earnings, GAAP earnings). Dividend income is presented as a component of net investment income. In this presentation, any undistributed earnings by the investee are part of the fair value of the investee and therefore are reflected in the unrealized gain or loss.

Changes in fair value from period to period are reported as changes in unrealized gain or loss on the statement of operations, which is presented separately from net investment income. These gains or losses are realized upon the disposal of an investment.

## **2.05 Operating Model**

### **2.05(a.1) Introduction**

Under the Operating Model, the Statement of Net Assets presents the gross assets and gross liabilities of the Fund's investments in real estate as separate line items. The Statement of Operations presents the gross investment/property level revenue and expenses. Note that consolidation guidance per ASC Topic 810, Consolidation, may be considered such that any Equity Method Investments would be presented as an asset balance within a single financial statement line item.

2.05(a.2) Entities that report under ASC 960 are required to follow ASC 810, Consolidation ("ASC 810"), and ASC 323, Investments – Equity Method and Joint Ventures ("ASC 323"). As indicated above, some entities that report under ASC 946 may elect to present their financial statements under the Operating Model. It is recommended that those entities that present their financial statements based on the Operating Model under ASC 946 consider the consolidation guidance in ASC 810 in determining an accounting policy, including an evaluation of whether or not the investee is a variable interest entity ("VIE"), to determine whether it has a controlling financial interest in the investee and therefore whether consolidation under the operating model is appropriate.

2.05(a.3) Investments must be reported at fair value in accordance with ASC 820. The objective of the Statement of Operations is to present the increase or decrease in the net assets resulting from the entity's investment activities and underlying property operations. Net investment income is a measure of operating results. It is primarily intended to provide a measure of operating activity, exclusive of capitalized expenditures, such as leasing commissions, tenant improvement costs, tenant inducements, and other replacement costs that can be capitalized if in accordance with GAAP. Rental revenue is recognized when it is contractually billable to tenants (i.e., straight-lining of rents is not applicable when real estate is reported at fair value). Expenses are generally recognized when the obligation is incurred. Certain expenses may be based on the investment vehicle's unrealized change in net asset value, including, for example, incentive management fees, and are recognized as a component of the unrealized gain or loss.

### **2.05(b) Election of the Fair Value Option Under ASC 825-10**

The Fair Value Option under ASC 825-10 permits entities to elect a one-time irrevocable option to measure financial instruments including, but not limited to, notes payable and portfolio level debt at fair value in accordance with ASC 820 on an instrument-by-instrument basis. Further information can be found in Sections 4.04 and 4.05.

## 2.05(c) Consolidation: Applicability of ASC 810

2.05(c.1) Under the Operating Model, a Reporting Entity should generally assess consolidation under ASC 810. Investments may include direct investments in real estate and debt, as well as holdings of controlling equity interests in separate legal entities, which invest in real estate assets. The Fund manager may consider existing authoritative guidance within ASC 810 to determine whether an investment in an investee (e.g., joint venture) represents a VIE to be assessed for consolidation under the VIE model, or whether the investment in an investee should be consolidated in accordance with the voting interest entity model.

2.05(c.2) Under the scope exception referred to in ASC 810-10-15-12(d), an investment company technically should not consolidate an investee that is not an investment company unless the investee is an operating entity that provides services to the investment company. However, it is suggested that a real estate Reporting Entity that qualifies as an investment company and prepares its financial statements under the Operating Model perform the consolidation analysis under ASC 810, including an evaluation of whether the investee is a VIE, to determine whether it has a controlling financial interest in the investee and therefore whether consolidation under the Operating Model is appropriate. If investments in entities are not deemed to be controlling interests, these investments should be accounted for as investments in non-consolidated joint ventures, in a similar manner to ASC 323.

To the extent that ASC 810 is not followed as a result of the preceding paragraph, preparers should consider adopting and applying a consistent accounting policy, for example, by looking at their ownership percentage, rights of the different partners, etc., to determine the most appropriate and meaningful presentation for presenting the investment on a gross basis (akin to a consolidated JV) or net basis (akin to an equity method investment).

## 2.05(d) Consolidation: Accounting

2.05(d.1) Entities that report under ASC 960 are required to follow ASC 810. While ownership of a greater than 50% voting interest in an investment is generally considered to be an indication of control, many joint venture investments contain complex governance arrangements that make assessments of control difficult. A multitude of factors must be considered in making a determination of whether consolidation of an investee is appropriate, including a determination of whether or not the investee is a VIE. If investments in entities are not deemed to be controlling interests, the equity method of accounting should be followed if the “significant influence” criterion is met in accordance with ASC 323.

2.05(d.2) Under the Operating Model, real estate assets either owned directly by a Fund or reported through the consolidation of an investee are recorded on the Statement of Net Assets at their fair value. If the investee is less than 100% owned, a corresponding credit to noncontrolling interest is recorded at fair value for the noncontrolling interest in the investment. The difference between fair value and the

adjusted cost basis of an investment is the unrealized gain or loss associated with the asset and liability, and if applicable, the noncontrolling interest. Changes in fair value from period to period are reported as changes in unrealized gain or loss on the statement of operations, which is presented separately from net investment income. These gains or losses are realized upon the disposal of an investment; however, in order to record a realized gain, the sale is required to meet the criteria within ASC Subtopic 610-20, Other Income – Gains and Losses from the Derecognition of Nonfinancial Assets, and ASC Topic 976, Real Estate – Retail Land (ASC 976). Under ASC 610-20, sales and partial sales of real estate assets are subject to the same derecognition model as all other nonfinancial assets.

2.05(d.3) The consolidation process outlined in ASC 810 requires that the noncontrolling interest continues to be allocated its share of losses even if that allocation results in a deficit noncontrolling interest balance. This standard also requires the acquirer to measure a noncontrolling interest in the acquiree at its fair value at the acquisition date. The noncontrolling interest would continue to be recorded at fair value assuming a hypothetical liquidation at fair value. An entity should perform an assessment of its noncontrolling interest's rights and consider whether the noncontrolling interest is a redeemable equity security within the scope of ASC 505-10-50.

2.05(d.4) In the footnotes or in the statement of changes in net assets, an entity is required to provide a reconciliation of the beginning and the ending carrying amounts of (1) net assets attributable to the parent entity (2) net assets attributable to the noncontrolling interest, and (3) total net assets.

2.05(d.5) In the footnotes, a separate schedule that shows the effects of any changes in a parent's ownership interest in a subsidiary on the equity attributable to the parent. Entities are required to disclose both a reconciliation of net assets (paragraph c) and a separate schedule of changes in ownership (paragraph d).

2.05(d.6) Revenue Recognition: The difference between the fair value and the adjusted cost basis of an investment is the unrealized gain or loss associated with the asset and liability, and if applicable, the noncontrolling interest. Changes in fair value from period to period are reported as changes in unrealized gain or loss on the statement of operations, which is presented separately from net investment income 2.05 (d.2)

Further, rental revenue is recorded as described in section 4.10 below.

**2.05(e) Accounting for Investments in Non-consolidated Joint Ventures**

Investors with non-controlling investments in investees (e.g., partners in joint ventures) accounted for under the equity method of accounting should record as investment income only their share of the investee's net investment income or loss, determined in accordance with GAAP on the fair value basis of accounting. The investment is recorded at fair value with the difference between the fair value and the basis recorded as an unrealized gain or loss. This amount is exclusive of items such as depreciation, amortization, and deferred rent, but would include promote reallocations, as

appropriate. ASC 970-323-35-17 suggests that stipulated income allocation ratios should not be used if cash distributions and liquidating distributions are determined on some other basis (i.e., income should be allocated first on behalf of any preferred returns or interest, and then to the respective partners in proportion to their contractual ownership interests, etc.). Intercompany items, such as interest on loans by an investor to an investee should be eliminated to the extent of the investor's economic interest in the venture, as if the investee were consolidated.

For all investment companies that follow ASC 946 and utilize the Operating Model presentation, investments in non-consolidated joint ventures are initially recorded at the original investment amounts, are subsequently adjusted for the entity's share of undistributed earnings and losses (including unrealized and realized gains and losses) from the underlying entities from the dates of formation, are increased by additional contributions, and are reduced by distributions received.

## **2.06 Capital / Equity Transactions**

### **2.06(a) Contributions/Redemptions**

Investment partnerships shall record capital contribution and redemption amounts as of the date required by the partnership agreement. Cash received for capital contributions before the required date shall be recorded as an advance capital contribution liability and subsequently reclassified to equity upon the required capital call date.

### **2.06(b) Dividends**

Both closed-end and open-end investment companies record distribution liabilities on the legal date of declaration. For closed-end investment companies, a purchaser typically is not entitled to a dividend for shares purchased on the ex-dividend date. Open-end investment companies record the liability on the ex-dividend date to properly state the net asset value at which sales and redemptions are made.

## **2.07 Accounting for Uncertainty in Income Taxes**

ASC 740, Income Taxes, provides guidance for how uncertain tax positions should be recognized, measured, presented and disclosed in the financial statements. ASC 740 requires the evaluation of tax positions taken in the course of preparing a Fund's tax returns to determine whether tax positions are "more-likely-than-not" of being sustained by the applicable tax authority. Tax benefits of positions not deemed to meet the more-likely-than-not threshold would be recorded as a tax expense in the current year. Many real estate funds are held through transparent or flow through entities so that the taxable income is reported on separate tax filings including investor K-1s. Therefore, the tax impact of certain positions (including the character of income and gains, investor qualifications/status, classification of income for The Employee Retirement Income Security Act of 1974 (ERISA) reporting, etc.) may or may not affect the GAAP basis financial reporting. In preparing financial statements of real estate entities, tax positions to be reviewed and analyzed may include

non-transparent entities at or below the funds, international investments subject to tax in other jurisdictions, and other special considerations including but not limited to the following:

- Tax Exempt Entity Status
- REIT Status
- State and Local Tax Determinations/Nexus
- Unrelated Business Taxable Income

## INVESTMENT LEVEL ACCOUNTING

### 3.01 Introduction

3.01(a) This section outlines the required accounting policies to be followed for accounting at an investment level for interests in real estate investments. At the Fund level, different reporting entities may follow different fair value accounting and reporting presentations (i.e., Operating Model or the Non-operating Model). The topics discussed in this section are generally applicable to both fair value presentations.

3.01(b) See Property Level Accounting in Section 4 for information relating to realized and unrealized gains and losses as well as information regarding the accounting for the various components comprising the underlying real estate assets.

3.01(c) Investments in real estate are made using various investment structures. Included in this section is guidance relating to the following investment structures:

- Investments in Non-Participating Mortgage Loans Receivable
- Investments in Participating Mortgage Loans Receivable
- Investments in Joint Ventures, Limited Partnerships, or Limited Liability Companies.

### 3.02 Investments in mortgages and other loans receivable: General discussion

3.02(a) There are primarily two types of mortgage loan investments held by Funds: non-participating and participating mortgage loans. A non-participating mortgage loan is an investment that generally entitles the lender to payments of contractual principal and interest that do not increase based on the underlying operating results of a property.

3.02(b) A participating mortgage is an investment that generally consists of four parts: (1) "base interest" payments at contractually stated fixed or floating rates; (2) principal; (3) "contingent interest" payments where the lender is paid a percentage of property net operating income or cash flow after debt service; and (4) "additional contingent interest," which is in the form of lender participation in the appreciation in value of the underlying property.

3.02(c) Usually the loan terms of a participating mortgage are set somewhat more favorably to the borrower than those of a non-participating mortgage on the same property. Common terms on a participating mortgage historically include high loan-to-value ratios, base interest rates which are lower than comparable non-participating mortgages, and the occasional structure that may allow for a deferral of interest between the basic interest coupon and some lower "pay rate," typically during development and lease-up. The deferral may be paid when cash flow from net operating income is sufficient or may be added to the loan balance and be payable in full only at maturity.

3.02(d) The contingent interest component of a participating mortgage often represents a lender's right to a portion of the adjusted net cash flow generated by the collateralizing property. Typically, certain

expenses such as but not limited to, legal or other professional fees related to ownership of the property (i.e., not directly related to the operating activities of the property) are not permitted as deductions from gross income for determining the amount in which the lender participates in contingent interest. Often a reserve for replacements, or for tenant improvements, leasing commissions, and capital expenditures, is set aside from net operating income before the lender participates in the remainder.

3.02(e) The additional contingent interest or equity conversion component often specifies a hurdle rate that the lender is entitled to reach from basic interest, contingent interest and additional contingent interest before the borrower participates in any proceeds from sale.

3.02(f) ASC 326, Financial Instruments – Credit Losses does not have a significant impact on investments in mortgages and other loan receivables reported at fair value due to a scope exception for items reported at fair value through the statement of operations.

### 3.03 Accounting for non-participating mortgage loans receivable

3.03(a) Non-participating mortgage loans receivable should be carried on the Statement of Net Assets at their fair value. The difference between fair value and the adjusted cost basis of a mortgage loan is the unrealized gain or loss on investment. Valuation changes in fair value from period to period are reported as unrealized gain or loss on the statement of operations and are presented separately from net investment income. Such unrealized gains or losses are realized upon the disposition of the investment either through a sale of the mortgage note receivable (in accordance with the guidance in ASC 860, Transfers and Servicing) or through paydown of the mortgage note receivable by the borrower at maturity (or prior to maturity in the case of early prepayments.).

3.03(b) The initial cost basis of a non-participating mortgage loan should include all direct costs of originating or acquiring the loan investment. However, the entity's management should assess if such costs are a component of the loan's reported fair value under ASC 820 or should be reported as an unrealized loss upon acquisition of the loan. Such costs include acquisition fees paid to investment advisors, and/or other professional fees (e.g., legal fees) associated with the closing of a new investment.

3.03 (c) ASC 946 does not provide specific guidance pertaining to fee income associated with loan originations. As a result, there are two methodologies that could be considered when determining the appropriate accounting for such fees.

- Recognized as income when received - It is common practice for fair value funds to recognize origination fees when collected, typically at investment inception, in accordance with the terms of the related investment agreements. This is consistent with guidance per ASC 825-10-25-3 (as outlined above) for investments held at fair value.

- Capitalized and deferred, net of origination costs – As outlined above within Section 2.03(b), for loans held at cost, the origination fees are net with origination costs and deferred over the life of the related loan under the effective interest method.

Note: Certain fair value funds may elect to capitalize and amortize loan origination fees over the life of the loan. In these instances, the preparers of the financial statements may choose to analogize the accounting treatment to the treatment of interest for premiums or discounts. Section 2.122, *Interest*, of the *AICPA Audit and Accounting Guide: Investment Companies* dated August 1, 2023 (the "Investment Company Guide") outlines the following:

- As stated in FASB ASC 946-320-35-20, premiums and discounts should be amortized using the interest method. FASB ASC 835-30-35-2 states that the difference between the present value and the face amount of the net investment should be treated as a discount or premium and amortized as interest expense or income over the life of the note in such a way as to result in a constant rate of interest when applied to the amount outstanding at the beginning of any given period.

3.03(d) The carrying amounts of interest receivables currently due (generally one year or less) are generally considered to approximate fair value. Therefore, for fair value reporting, interest receivable currently due may be reported at its undiscounted amount provided that the results of discounting the carrying amount would not be material and that receipt can reasonably be assured.

3.03(e) Interest income associated with any non-participating mortgage loan receivable is reported in net investment income. Valuation adjustments are reported as unrealized gains and losses. The recognition of base interest income should be based on the contractual terms of the loan unless the loan is considered non-performing under GAAP. For mortgage loans with fixed and determinable rate changes, base interest income should be accounted for when the change contractually occurs rather than using an effective interest or straight-line method.

For non-performing loans (e.g., the borrower is unable to fulfill its payment obligations), interest income is recognized under a cash method whereby payments of interest received are recorded as interest income provided that the amount does not exceed that which would have been earned based on the contractual terms of the loan.

3.03(f) The fair value of a non-participating mortgage loan and any accrued non-current interest may be based on the discounted value of the total future expected net cash flows. The selection of an appropriate discount rate should reflect the relative risks involved and interest rates charged for similar receivables. The determination of fair value must also take into consideration the underlying collateral, credit quality of the borrower, and any related guarantees, as well as the specific terms of the loan agreement. The fair value of the mortgage loan and any accrued non-current interest should not exceed the value of the underlying collateral and any related guarantees. Accrued non-current interest is typically added to the principal amount, whereas current interest receivable is separately disclosed.

3.03(g) Modification of mortgage terms should be accounted for through an adjustment of fair value and recorded through unrealized gain or loss in the statement of operations.

### 3.04 Accounting for participating mortgage loans receivable

3.04(a.1) Because of the participation feature inherent in these loans, and the fact that the lender usually provides a significant portion, if not all, of the funds necessary to acquire, develop, or construct the property, accounting for participating mortgages should be determined based upon the following guidance, if applicable.

3.04(a.2) A participating mortgage may have the characteristics (see ASC 310-10-25, paragraphs 19-20) of either a loan, a noncontrolling equity investment in a joint venture, or a controlling interest subject to consolidation for accounting purposes, depending on the facts and circumstances. For the latter two categories, the investment should be accounted for using the guidance provided in the discussion of joint ventures appearing in Section 3.05 and 3.06 or in the discussion on real estate in Section 4.02.

3.04(b) Participating mortgages not considered joint ventures, or investments in real estate in accordance with ASC 310 should also be carried on the Statement of Net Assets at their fair value. The difference between fair value and the adjusted cost basis of a mortgage loan is the unrealized gain or loss associated with the asset. Changes in fair value from period to period are reported as changes in unrealized gain or loss on the statement of operations, which is presented separately from net investment income. Such unrealized gains or losses are realized upon the disposition of the investment, either through a sale of the mortgage note (in accordance with the guidance in ASC 860, Transfers and Servicing) or through paydown of the mortgage note by the borrower at maturity (or prior to maturity in the case of early prepayments).

3.04(c) The initial cost basis of a participating mortgage loan should include all direct costs of originating or acquiring the loan consistent with ASC 310-20. Such costs include acquisition fees paid to investment advisors and/or other professional fees (e.g., legal fees) associated with the closing of a new investment. However, the entity's management needs to assess the fair value of the loan under ASC 820 and whether an unrealized loss should be recognized on day one of holding the loan.

3.04(d) See Section 3.03(c) in this Manual for additional information pertaining to fee income associated with loan originations.

3.04(e) Interest income associated with any participating mortgage loan is reported in net investment income. Valuation adjustments are reported as unrealized gains and losses. The recognition of base interest income should be based on the contractual terms of the loan unless the loan is considered non-performing under GAAP. For mortgage loans with fixed and determinable rate changes, interest income should be accounted for based on when the change contractually occurs rather than using an effective interest or straight-line method.

For non-performing loans, generally the method for interest recognition is the cash method where payments of interest received are recorded as interest income provided that the amount does not exceed that which would have been earned based on the contractual terms of the loan.

Contingent interest income from operating cash flows is also recorded by the lender as part of net investment income. Additional contingent interest received from disposal or refinancing of the underlying property is recorded as part of realized gains and losses.

3.04(f) The fair value of a participating mortgage investment is equal to the discounted value of the total future cash flows expected from the investment. The value of the mortgage loan may not exceed the value of the underlying real estate plus any qualifying guarantees. The discount rate used in the valuation should reflect the risk/return characteristics of the participating investment structure. The valuation may be performed with different discount rates for the different sources of the anticipated cash flows; a “debt” rate may be associated with the nonparticipating cash flows, and an “equity” rate may be associated with the participation cash flows. In all cases the economic substance of the transaction must be taken into account in determining the value of the investment.

3.04(g) Modification of mortgage terms should be accounted for through an adjustment of fair value and recorded through unrealized gain or loss in the statement of operations.

### **3.05 Investments in joint ventures: General**

3.05(a) Joint ventures are a common form of ownership for Funds and institutional investors in real estate. The venture is typically a legally formed limited partnership or limited liability company between the Fund/institutional investor and a real estate developer/operator.

3.05(b) Real estate investments are often structured as joint ventures because these structures provide the ability to share risks and rewards among the participants. The Fund/institutional investor typically own the greater share of the joint venture and provide most of the equity invested into the project. Such investment may be in the form of equity capital, loans to the venture, or both. The Fund/institutional investor’s operating partner is typically the real estate developer/operator for the joint venture. Depending on the terms of the venture agreement, distributions of the venture’s cash flows may not align with the legal ownership interests of the partners and will instead follow the hypothetical liquidation terms of the venture agreement. These clauses may give preferential return of cash flows to either the institutional investor or the developer/operator partner depending on the agreement terms.

### **3.06 Investments in joint ventures: Accounting**

3.06(a) The appropriate fair value accounting for investments in joint ventures in the primary financial statements depends upon the reporting presentation utilized. See Section 2, Fund Level Accounting, in this Manual for a discussion of the appropriate accounting presentations and sources of additional guidance.

3.06(b) When investments in joint ventures are reported at fair value, the difference between fair value and the adjusted cost basis of an investment is reported as unrealized gain or loss. As discussed in greater detail below, changes in fair value from period to period are reported as changes in unrealized gain or loss on the statement of operations, which is presented separately from net investment income. Unrealized gains or losses are recognized as realized gains or losses upon the disposal of an investment.

3.06(c) The initial cost basis of an investment in a joint venture should include all direct costs of obtaining the investment. Such costs include acquisition fees paid to investment advisors and/or other professional fees (e.g., legal fees) associated with the closing of a new investment. However, the entity's management needs to assess the fair value of the investment under ASC 820 and whether an unrealized loss should be recognized on day one of holding the investment.

3.06(d) An investment in a joint venture is subsequently adjusted to report changes in fair value that may include, but are not limited to, undistributed net investment income and/or changes in the fair value of the underlying net assets. Such changes in fair value are reported in the statement of operations as an unrealized gain or loss during the period in which the change in fair value occurs.

3.06(e) To the extent that the investor has advanced funds to the joint venture in the form of loans, all outstanding principal and non-current interest receivable should also be included in the cost basis. The aggregate investment should be presented on the statement of net assets as a single caption, (i.e., "Investment in Joint Venture") and presented as a single investment on the schedule of investments.

3.06(f) The determination of the fair value of an investment in a joint venture requires: (1) the valuation of the underlying assets and liabilities of the joint venture; and (2) the analysis of a hypothetical liquidation as of the reporting date at fair value in accordance with the distribution provisions of the joint venture agreement. Consideration should be given to all incentive fees and preferred returns included in the joint venture agreement in determining the hypothetical liquidation at fair value of the joint venture. Fair value is defined by ASC 820-10-20 as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Transaction costs are not included in determining the fair value of the investment. Hypothetical liquidation at fair value may not necessarily reflect the exit price of an entity's joint venture investment. Consideration should be given to what a market participant would be willing to pay as of the reporting date.

3.06(g) ASC 820-10-35-59 permits, as a practical expedient, a Reporting Entity to measure fair value of an investment, that is within the scope of the amendments, on the basis of net asset value per share of the investment (or its equivalent) if the net asset value of the investment (or its equivalent) is calculated in a manner consistent with the measurement principles of ASC 946 as of the Reporting Entity's measurement date.

Note: The scope is defined in ASC 820-10-15-4 through 15-5

3.06(h) ASC 820-10-50-2 discusses that reporting entities with investments measured at NAV as a practical expedient need not disclose the investment's level in the fair value hierarchy or any of the related disclosures. For investments measured using NAV as a practical expedient, see ASC 820-10-50-6A for required disclosures. Please note that such investments are excluded from the quantitative disclosure (i.e. tabular format) referenced in section 4.02 (d).

3.06(i) ASC 230-10-45 clarifies the treatment of distributions received from investments in joint ventures due to diversity in practice.

An entity can make an accounting policy election to evaluate distributions received from investments in joint ventures based on either: (1) the “look-through approach” or (2) the “cumulative earnings” method.

Under the look-through approach, the classification of cash distributions within operating activity (return on investment) or within investing activity (return of investment) is based on specific facts and circumstances and the nature of the actual distribution. For example, distributions made from the sale of real estate or a refinancing would typically be classified as an investing activity, whereas distributions made from excess operations would typically be classified as an operating activity.

Under the cumulative earnings approach, cash dividends received are classified as returns on investment (i.e., operating cash inflows) unless the amount of cumulative dividends received exceeds the entity's share of the investee's cumulative earnings, in which case they are classified as returns of investment (i.e., investing cash inflows).

### 3.07 Accounting for Non-Controlling Interest

3.07(a) The appropriate fair value accounting for a noncontrolling interest in the primary financial statements depends upon the reporting presentation utilized. See Section 2, Fund Level Accounting, in this Manual for a discussion of the appropriate accounting presentations and sources of additional guidance.

3.07(b) When a consolidated joint venture is reported at fair value, the noncontrolling interest for the portion not owned by the Fund should be reported at fair value. ASC 810 requires noncontrolling interests to be classified as a separate component of equity, distinct from the equity attributable to the controlling shareholders, on the statement of net assets and statement of changes in net assets.

3.07(c) The initial cost basis of a noncontrolling interest should include all amounts funded from the noncontrolling interest member into the joint venture. Such costs include acquisition fees paid to investment advisors and/or other professional fees (e.g., legal fees) associated with the closing of a new investment.

3.07(d) The noncontrolling interest is subsequently adjusted to report changes in fair value that may include, but are not limited to, undistributed net investment income and/or changes in the fair value of the

underlying net assets. Such changes in fair value are reported in the statement of operations as income attributable to noncontrolling interests during the period the change in fair value occurs.

3.07(e) The determination of the fair value of a noncontrolling interest requires: (1) the valuation of the underlying assets and liabilities of the joint venture; and (2) the analysis of a hypothetical liquidation as of the reporting date at fair value in accordance with the distribution provisions of the joint venture agreement. Consideration should be given to all incentive fees and preferred returns included in the joint venture agreement in determining the hypothetical liquidation at fair value of the noncontrolling interest.

3.07(f) ASC 810-10-45-18 to ASC 810-10-45-21 requires net income or loss attributable to the controlling and noncontrolling investors to be presented separately on the statement of operations. The portion attributable to the noncontrolling interest member would typically include the proportionate share of net income and unrealized/realized gain or loss attributable to the noncontrolling interest member.

3.07(g) A noncontrolling interest member is considered an owner. In accordance with ASC 230, dividends paid to a noncontrolling interest member should be classified as financing activities. Cash paid to acquire a noncontrolling interest, or cash received from the sale of a noncontrolling interest, should be classified as a financing activity when the Fund maintains control of the investment. Cash received from a sale should be classified as an investing activity when the Fund loses control of the investment.

3.07(h) When calculating the net investment income and expense ratios for Financial Highlights, the Fund should consider whether it is appropriate to adjust the numerator to remove the noncontrolling interest member's proportionate share of net investment income and expenses, respectively.

### **3.08 Accounting for contingencies**

3.08(a) For all acquisitions, the acquirer should recognize as of the acquisition date, all of the assets acquired, and liabilities assumed that arise from contingencies related to contracts (referred to as contractual contingencies) and measure them at their acquisition-date fair values.

3.08(b) For all other contingencies (referred to as noncontractual contingencies), the acquirer shall assess the contingency in accordance with ASC 450, Contingencies, as appropriate.

3.08(c) It may be necessary to utilize probability weighted discounted cash flows or other complex valuation models in order to value such contingent considerations. The acquirer needs to further determine if such consideration should be recorded as an asset, liability, derivative instrument or equity.

### **3.09 Accounting for forward purchase commitments**

3.09(a) An entity should assess whether entering into a forward purchase commitment results in holding a variable interest in a variable interest entity, or "VIE" (i.e., the entity that holds the real estate). ASC 810-10-55-80 through ASC 810-10-55-86 should be reviewed when concluding on this matter.

Particular consideration should be given as to whether the Reporting Entity: a) has rights to terminate the forward purchase commitment for any reason, including if the third party, (i.e., the developer), does not perform, AND, b) whether those rights are substantive. If the entity determines it holds a variable interest, it must then determine if it is the primary beneficiary of the VIE under the provisions of ASC 810, and accordingly consolidate the accounts of the VIE. An entity should also consider whether the forward purchase commitment should be valued based on the nature of the agreement. It would generally be appropriate to record unrealized gains (losses) on the forward commitment if there is a change in the value of this agreement.

3.09(b) Some disclosures a Fund might consider for its forward purchase commitments are as follows: project name, property type, location, authorized commitment, costs spent to date, expected funding date, and any other significant terms or considerations.

### 3.10 Accounting for financing costs

3.10(a) Costs may be incurred in connection with obtaining financing for the Fund or the investment — either secured or unsecured. The Fair Value Option under ASC 825-10 permits entities to elect a one-time option that is irrevocable to measure financial instruments including, but not limited to, notes payable and portfolio level debt at fair value on an instrument-by-instrument basis (see Sections 4.04 and 4.05). ASC 825-10-25-3 states that “upfront costs and fees related to items for which the Fair Value Option is elected shall be recognized in earnings as incurred and not deferred”. Under GAAP, for those entities that have not adopted the Fair Value Option under ASC 825-10, debt costs will continue to be deferred and amortized to interest expense using the effective interest method (see 3.10(b)).

3.10(b) ASC 835-30 requires that unamortized financing costs be presented as a reduction of the carrying amount of the related debt balance on the Statement of Net Assets, rather than separately presented as an asset. For those entities that do not elect the Fair Value Option, the amortization of financing costs will continue to be recorded as a component of interest expense on the statement of operations.

3.10(c) ASC 835-30-S35-1 and ASC 835-30-S45-1 relates to financing costs associated with a line-of-credit arrangement. These costs will continue to be presented as an asset and amortized over the term of the arrangement.

### 3.11 Investment Advisory fees

3.11(a) General

Real estate investment advisory fees may include acquisition, asset management, disposition, financing, and incentive fees. These fees are generally paid by the Fund to the Advisor and reflected in the Fund financial statements. However, if these fees are paid from the investor(s) to the Advisor

directly, they would not be reflected in the Fund financial statements, but should be considered for disclosure in the footnotes

### **3.11(b) Acquisition, Origination and Financing fees**

Acquisition fees are considered a component of the acquisition cost of a property and, therefore, are included in the cost basis of the real estate asset as are other acquisition-related costs. They are included as part of the cost when comparing cost to value to determine realized or unrealized gain or loss under both the Operating Model and Non-operating Model. In circumstances where an investment company is acquiring an investment, the acquisition or transaction costs associated with the investment acquisition should be capitalized as part of the cost of the investment. However, reporting a newly acquired property at fair value may result in an unrealized loss on day one because the reported fair value of a property would not take into account related acquisition costs if there are no other valuation changes (see 4.02b).

Origination Fees paid to an advisor by the Fund generally compensate an advisor for their services rendered in originating mortgage loans receivable. These fees are generally accounted for as described by 3.03(b).

Financing Fees generally compensate an advisor for their services rendered for a loan payable that the advisor arranges on behalf of the investment. These fees are generally accounted for as described by 3.10.

### **3.11(c) Asset Management Fees**

Asset management fees are generally expensed as incurred and reported as a component of net investment income.

### **3.11(d) Disposition Fees**

Disposition fees are typically paid when an investment is sold and calculated as a percentage of the sales price. The fee generally compensates a real estate advisor for their services rendered in an investment disposition, including sales marketing, negotiating, and closing. As this fee is not earned until the work is performed or substantially performed, the fee is generally recognized as a cost of sale in the period in which the investment is sold and is not considered as a component of fair value prior to the sale date. (Disposition fees that are substantively incentive fees should be measured and recognized as incentive fees).

### **3.11(e) Incentive Fees and Promote Reallocations**

3.11(e.1) Incentive fee arrangements and calculations vary widely, but generally these fees are paid after a predetermined investment performance return has been attained. For example, these fees may be payable upon, actual or constructive sale of a real estate investment or portfolio, when cash flows from operating or capital distributions exceed some threshold, or at certain measurement dates during the hold period based upon a hypothetical sale of a real estate investment or portfolio.

3.11(e.2) Incentive fees earned by an investment advisor should be recognized as a payable as if all assets were sold and liabilities were settled at the date of the Statement of Net Assets. The calculation of the amount earned is specific to the related real estate advisory agreement, but generally the calculation should assume that the investment or Fund is liquidated at its fair value as of the reporting date and cash proceeds are distributed to the investors. An expense and liability should be recorded for the amount of the incentive fee, although not necessarily currently payable.

3.11(e.3) The related impact of recording a liability for an incentive fee should be either (1) *Changes in incentive fees that result from meeting and exceeding operating result goals are expensed as a component of net investment income*; or (2) *Changes in incentive fees and promotes (carried interest) that are earned based on changes in an investment's fair value are recorded as a change in unrealized gain or loss*.

3.11(e.4) In the real estate industry, incentive fees are typically based on changes in fair value and therefore reduce the realized or unrealized gains, as opposed to the net investment income of the fund. Incentive fees based on components of investment income, are included in net investment income.

3.11(e.5) Promote reallocations that would be due to a general partner or managing member in the manner described in 3.11(e.2) should not be expensed, but rather should be reflected as a reallocation of capital from the limited partners to the general partner in the Statement of Changes in Net Assets. However, within the ratio calculations of the financial highlight's disclosure, regardless of whether the promote allocations are presented as an expense or a reallocation of capital between partners, the impact of the incentive fee should be presented as a separate expense line item within the calculation. See chapter 7 of the AICPA Investment Company Guide for more detail.

### 3.11(f) Related Party Fees and Affiliate Transactions

3.11(f.1) Related parties are defined in the glossary to the FASB Codification and include, but are not limited to: affiliates of the entity, principal owners of the entity, management of the entity, parties over which the entity has significant influence and parties that have significant influence over the entity. An affiliate is defined in the glossary as a party that, directly or indirectly through one or more intermediaries, controls, is controlled by, or is under common control with an entity.

3.11(f.2) Related party fees and affiliate transaction arrangements should be properly disclosed in the financial statements, regardless of how significant or quantitatively immaterial the amounts involved are. The investment advisor or manager should seek to provide full transparency to fund investors regarding all fees and arrangements where an affiliate entity provides services or is otherwise involved in a particular fund or separate account.

Per the AICPA Investment Company Guide paragraph 7.118, "Amounts paid to affiliates or related parties (such as advisory fees, administration fees, distribution fees, brokerage commissions, and sales charges) should be disclosed, in accordance with FASB ASC 850. Significant provisions of related-party agreements, including the basis for determining management, advisory, administration, or

distribution fees, and, also, other amounts paid to affiliates or related parties should be described in a note to the financial statements."

3.11(f.3) ASC 850 also states that transactions between related parties are considered to be related party transactions even though they may not be given accounting recognition. For example, an entity may receive services from a related party without charge and not record receipt of the services. While not recorded, their disclosure is required, nonetheless. Refer to the related party fees and affiliate transactions footnote in the illustrative financial statements.

## PROPERTY LEVEL ACCOUNTING

### 4.01 Introduction

4.01(a) This section outlines the required accounting policies to be followed for underlying real estate investments accounted for at the property level, in order to provide consistent accounting information across Funds for attribution analysis, benchmark reporting, and reporting to the NCREIF Property Index (NPI). In addition, under the Operating Model, financial statements prepared for properties are accounted for in this manner and utilized accordingly for consolidation purposes.

4.01(b) Regardless of the form of investment held, the underlying real estate assets include all investments in land, buildings, construction in progress, tenant improvements, tenant allowances, furniture, fixtures and equipment, leasing commissions, capitalized leasehold interests, capitalized interest, capitalized real estate taxes, and real estate to be disposed. Under the fair value basis of accounting, real estate assets are carried on the Statement of Net Assets at their estimated fair value. Changes in fair value from period to period are recognized as unrealized gains or losses until sale or disposition of an interest in the real estate investment.

4.01(c) Under the fair value accounting presentations, net investment income is not intended to approximate net income that would be reported under the historical cost basis accounting model. Among other differences, net investment income under the fair value accounting presentations does not include the effect of rent normalization (i.e., straight-line rent) under ASC 842-30-25, cost-based depreciation or amortization of most capitalized expenditures, or impairment accounting provisions.

### 4.02 Determination of real estate fair value

4.02(a) ASC 820 focuses on how to measure fair value. ASC 820 does not introduce any new requirements mandating the use of fair value; instead, it unifies the meaning of fair value within GAAP and expands disclosures about fair value measurements. It also introduces a fair value hierarchy to classify the source of information used in fair value measurements (i.e., market based or non-market-based inputs).

4.02(b) ASC 820-10-20 defines fair value as, “the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.” This definition retains the exchange price notion in earlier definitions of fair value. However, the definition focuses on the price that would be received to sell the asset or paid to transfer the liability (an exit price), not the price that would be paid to acquire the asset or received to assume the liability (an entry price). The fair value of an asset or liability is a market-based measurement. Therefore, the fair value measurement should be based on the highest and best use assumptions that market participants would use in pricing a nonfinancial asset such as real estate, regardless of whether the use by the Reporting Entity is different.

4.02(c) The fair value measurement in ASC 820 assumes that the transaction to sell the asset occurs in the principal market for the asset or in the absence of a principal market, the most advantageous market for the asset. The principal (or most advantageous) market is the market with the greatest volume and level of activity for the asset or liability, presumably the market in which the Reporting Entity transacts.

4.02(d) ASC 820 requires that a fair value measurement should maximize the use of observable inputs and minimize the use of unobservable inputs. Disclosure of the valuation techniques and inputs are required for each class of Level 2 or Level 3 assets or liabilities. If the fair value measurement has significant Level 3 inputs, related footnote disclosures are required to be included on a gross presentation basis (i.e., real estate investments and mortgage loans payable shown separately). Most real estate valuations generally include significant unobservable inputs, and the related. Valuations should reflect the Reporting Entity's assumptions that market participants would use, including assumptions about risk. Such assumptions should be developed based on the best information available without undue cost and effort. It is the source of the input that drives the classification, not approach or specialist used to determine fair value. For instance, an external appraiser's valuation of a property utilizing a discounted cash flow model based on the specific cash flows of said property would be considered a technique that uses Level 3 inputs.

The class of the asset or liability is determined by the nature and risks of the instruments and will often be at a more disaggregated level than the financial statement line-item level.

All disclosures indicated below are required by public entities. Private entities are required to disclose only items (1) and (3):

1. Quantitative disclosure (i.e., tabular format) about unobservable inputs used for all Level 3 fair value measurements;
2. For fair value measurements categorized as Level 3, qualitative disclosures (i.e., narrative form) about the sensitivity of the fair value measurement to changes in unobservable inputs used if a change in those inputs to a different amount might result in a significantly higher or lower fair value measurement;
3. If applicable, a Reporting Entity's use of a nonfinancial asset in way that differs from the asset's highest and best use when that asset is measured or disclosed at fair value;
4. For fair values disclosed but not reported in the financial statements include:
  - a. the level in which the fair value is categorized;
  - b. for Level 2 and 3 fair values a description of the valuation techniques and inputs used, and the reason for any change in the valuation technique, if applicable;
  - c. if the highest and best use of a nonfinancial asset differs from its current use, disclose that fact and why the nonfinancial asset is being used in a manner that differs from its highest and best use;
5. The changes in unrealized gains and losses for the period included in other comprehensive income for recurring Level 3 fair value measurements held at the end of the reporting period.

6. The range and weighted averages of significant unobservable inputs used to develop Level 3 fair value measurements (or other quantitative information such as the median or arithmetic average in lieu of the weighted average if determined more appropriate).

ASC 820 clarifies the meaning of the terms “valuation technique” and “valuation approach” as used in fair value literature. The guidance indicates that valuation techniques are more granular than valuation approaches and explains that valuation techniques are used consistent with a particular approach. Companies are required to disclose changes in either (or both) a valuation approach or technique for each class of instrument (not for each individual instrument).

4.02(e) The fair value of property generally held for investment should be valued in a manner consistent with the Reporting Standards Property Valuation Standards. (See the Reporting Standards Property Valuation Standards for more information.)

4.02(f) Under ASC 820, the price in the principal (or most advantageous) market used to measure the fair value of the asset or liability shall not be adjusted for transaction costs. Transaction costs shall be accounted for separately, however for entities that follow ASC 960, Plan Accounting — Defined Benefit Pension Plans, ASC 960-325-35 provides guidance on fair value and requires fair value to include an estimate of costs to sell.

4.02(g) The fair value of a real estate asset should not include any effects of a related above- or below-market mortgage debt, except when debt is assumed on acquisition. For debt assumed at acquisition, the impact of above/below fair value debt is assigned to the cost basis of the related debt with an offset to the related real estate asset acquired (this is applicable whether or not the debt is reported at fair value under the Fair Value Option). The real estate and the related mortgage are to be shown separately on the Statement of Net Assets at their initial fair value.

4.02(h) The AICPA’s guide “Valuation of Portfolio Company Investments of Venture Capital and Private Equity Funds and Other Investment Companies” published in August 2019, contains non-authoritative guidance intended to harmonize views of industry participants, auditors and valuation specialists. The guide is applicable for real estate valuation.

### **4.03 Determination of the cost basis of real estate assets**

4.03(a) The initial cost basis of a real estate asset includes direct costs of acquiring the real estate asset under both the Operating Model and the Non-operating Model. For development properties, the cost basis of these assets should also include costs capitalized during the development period including interest, insurance, and real estate taxes, reduced by income from incidental operations. Authoritative accounting literature, including ASC 835-20, Capitalization of Interest, and ASC 970, Real Estate-General, provides guidance relating to the appropriate cost capitalization criteria. Direct costs of acquisition are considered part of the acquisition cost of a property. They are included as part of the cost when comparing cost to value to determine realized or unrealized gain or loss. Regardless of whether an entity follows the Operating or Non-operating presentation for its financial statements,

acquisition costs should generally be capitalized. However, the valuation of the underlying investment under ASC 820 may result in an unrealized loss on day one.

4.03(b) Because real estate investments are reported at fair value each reporting period and valuations take into account the effect of physical depreciation, none of the capitalized components (building, equipment, improvements, lease costs, in-place lease value, lease inducements, lease origination costs, etc.) are depreciated or amortized.

4.03(c) The initial cost basis of a real estate asset should be subsequently adjusted for additional capital costs such as tenant and building improvements, tenant allowances, tenant inducements, tenant leasing commissions, and tenant buyouts (if the buyout meets accounting guidance criteria for capitalization). These capital costs are generally incurred to maximize cash flows and generate additional income, which, in turn, influence the fair value of the real estate asset. Because the nature of these costs is such that they have benefits that extend beyond one year, the addition of these items to an asset's cost basis is considered appropriate.

4.03(d) This treatment extends to the reporting of tenant related capital costs, even after a tenant has vacated a property. These types of property-related costs represent additional investments in the property, which should be considered in any determination of the current fair value of the asset against an investor's investment in it.

#### **4.04 Loans payable**

4.04(a) Real estate investments are often partially financed using long- or intermediate-term loans whereby the real estate property is pledged as collateral for the loan. In many loan arrangements, the lender has no other recourse against the borrower; however, some arrangements provide for credit enhancements in the form of guarantees or additional pledges from the borrower. Real estate investments can also be financed through loans whereby owners with high credit standing or prearranged lines of credit may be able to borrow on an unsecured basis or by a loan which is secured by collateral other than the underlying real estate investments.

4.04(b) The Fair Value Option under ASC 825-10 permits entities to elect a one-time irrevocable policy election to measure financial instruments at fair value on an instrument-by-instrument basis.

4.04(c) Subsequent to the initial measurement, adjustments to the estimated fair value of loans payable should be reported as unrealized gain (loss) in the statement of operations. Gains and losses realized upon settlement of loans payable, net of transaction and prepayment costs, if any, should be reported separately as realized gain (loss) in the statement of operations.

4.04(d) If the Fair Value Option is elected for loans payable, the fair value is determined by ASC 820 and is based on the amount, from the market participant's perspective, at which the liability could be transferred in an orderly transaction between market participants at the measurement date, exclusive of transaction costs. The fair value definition within ASC 820 focuses on the price that would

be paid to transfer the liability (an exit price), not the price that would be received to assume the liability (an entry price). Therefore, if a market participant was to assume debt, interest expense incurred to date would not be assumed by the buyer and would remain the liability of the entity. In accordance with ASC 820, when measuring the fair value of a note payable (i.e., financial liability), the Reporting Entity must not attempt to compensate for any transfer restrictions contained in the loan documents because the existing valuation inputs tend to reflect such restrictions and require no further adjustment. Additionally, when applying a present value technique to value liabilities the Reporting Entity should, if applicable, include market participant assumptions related to compensation a market participant would expect when taking on the obligations and risks associated with such activities; however, this generally applies when the liability is not held by another party as an asset (e.g., asset retirement obligation).

Note: in instances where the value of an underlying real estate investment declines to a point that the principal amount of a property mortgage loan (if non-recourse) is greater than the value of the investment, it is generally appropriate to report the fair value of the loan at an amount equal to the fair value of the real estate to reduce FV NAV to zero.

4.04(e) If the Fair Value Option is not chosen for loans payable, the guidance as described in ASC 835-30 related to imputed interest should be followed.

Note: In instances where the value of an underlying real estate investment declines to a point that the principal amount of a property mortgage loan (if non-recourse) is greater than the value of the investment, it would generally not be appropriate to change the value of the loan because the fair value option was not elected. This can result in negative equity for an investment as the loan will continue to be presented at cost.

4.04(f) Refer to Reporting Standards Guidance Document, FASB ASC Topic 820, Fair Value Measurements and Disclosures: Implementation Guidance for Real Estate Investments for more information on applying ASC Topic 820.

4.04(g) Often times loans payable have debt covenants and in certain instances real estate funds/sponsors may provide guaranties on property level financing. Consider ASC 470-10-50 for disclosure requirements for debt, including major terms of borrowings, defaults or violations of debt covenants existing at the balance sheet date, and subjective acceleration clauses or cross-default provisions. ASC 860-30-50-1A requires disclosure of the fact that assets are pledged as collateral against liability. ASC 460-10-50 requires disclosure of the nature and terms of guarantees (including maximum potential future payments), circumstances triggering performance, any collateral or recourse provisions, and recognition of the fair value of any liability for guarantees.

## **4.05 Direct Transaction Costs of Loans Payable**

4.05(a) ASC 825-10-25-3 states that “upfront costs and fees related to items for which the Fair Value Option is elected shall be recognized in earnings as incurred and not deferred.” Therefore, transaction costs

related to loans payable for operating properties are recorded as a reduction in earnings incurred in the statement of operations. Subsequent to the election of The Fair Value Option under ASC 825-10, transaction costs should be expensed as incurred.

4.05(b) Subsequent to the election of the fair value option, unrealized gains and losses on notes payable should generally be recognized when market interest rates or credit spreads fluctuate relative to contractually fixed rates or variable rate credit spreads.

## **4.06 Derivative financial instruments**

4.06(a) Real estate is often financed through variable rate loans. In an effort to manage the risks associated with fluctuations in market interest rates and to maintain a more neutral position during market interest rate fluctuations, the borrower may purchase derivative financial instruments (derivatives), such as interest swaps, collars, Treasury locks, floors, or capping contracts. The contract can be assigned to a specific property or loan, or they can be established in connection with a portfolio of investments. These contracts also involve an up-front cost and generally are transferable to other parties.

4.06(b) All derivative financial instruments should be carried at estimated fair value with the change in fair value being recorded to earnings in accordance with ASC 815, Derivatives and Hedging.

4.06(c) The approach used for estimating the fair value of interest rate protection contracts should be consistent with ASC 820. The contract should be carried as an asset or liability, as fair value indicates, and should be adjusted to fair value each reporting period with the change in fair value recorded to earnings. Diversity in practice exists where the change in fair value is presented within the income statement. Any transaction costs associated with obtaining the contracts should be recognized in earnings as incurred and not deferred. For cash outlays, consider ASC 815 to determine if the cash outlay represents a financing expense. For cash flow classification considerations, initial outlay and periodic settlements related to the interest rate protection contracts should generally be consistent with the nature of the derivative and the hedged item.

## **4.07 Other assets and liabilities**

4.07(a) There are a variety of other assets and liabilities that may result from the acquisition of income producing property, or day-to-day operations of the property. Examples of other assets include prepaid expenses, such as taxes and insurance, supplies inventory, utility deposits, escrow deposits, equipment, etc. Examples of other liabilities include accounts payable, accrued expenses, such as accrued real estate taxes, insurance, repairs and maintenance, property management fees, interest, compensation, utilities and professional fees, and other liabilities, such as security deposits, unearned rental income, and fees payable in the ordinary course of operations.

4.07(b) Other assets or liabilities that are short-term in nature (i.e., expected to be settled within one year of the date of the financial statements) may be reported on the Statement of Net Assets at their

undiscounted values. This is because of the short-term nature of these items; their undiscounted balances are considered to approximate their fair values.

- 4.07(c) Other assets or liabilities should be accounted for in accordance with other GAAP, electing to report the assets and liabilities at fair value wherever permitted by GAAP.
- 4.07(d) Regardless of the methodology utilized, care must be exercised in evaluating other assets and liabilities to ensure that they have not already been included in the valuation of the real property or the investment.
- 4.07(e) Changes in the fair value of other assets and liabilities from period to period are reported on the statement of operations as unrealized gains and losses, which are reported separately from net investment income. Unrealized gains and losses become realized when the underlying asset or liability is settled or resolved.
- 4.07(f) Other liabilities may include contingent consideration that is part of an investment at the time of the acquisition. Contingent consideration should be recognized and measured at fair value at the acquisition date and each reporting date, rather than recognized and measured as an adjustment to the purchase price in the subsequent period in which the contingency is resolved. Other liabilities may also include such liabilities that result from day-to-day operations of a property

## **4.08 Receivables**

- 4.08(a) Various operating transactions may result in notes or accounts receivable. These receivables may be short-term (less than one year to maturity) or long-term in nature.
- 4.08(b) The undiscounted carrying value of short-term receivables generally approximates fair value due to the relatively short period of time between the reporting date and the expected realization. The use of an undiscounted value is acceptable provided that the results of discounting would be immaterial. For receivables derived from rental income, an allowance should be established based upon the amount of the receivable expected to be uncollectible. Any such allowance should be charged against net investment income as a reduction to revenue in accordance with ASC 842-30-25-13. For non-rental receivables, the current expected credit losses (CECL) (Topic 326) model should be considered. Any receivables that are considered in the valuation of the real estate asset should not be established as such amounts are already included in the valuation of the real estate asset.
- 4.08(c) The fair value of longer-term receivables should be estimated by discounting the expected future cash flows to be received (including interest payments) using a current market rate of similar receivables commensurate with the risks of the specific receivables. Similar receivables are those that have comparable credit risk and maturities. When assessing collectability, the Current Expected Credit Losses (CECL) model under ASC Topic 326 should be applied. In making this assessment, consideration should be given to the value of any underlying collateral securing the asset.

## 4.09 Real estate revenues and expenses

4.09(a) The ownership of income producing property encompasses real estate revenues directly associated with the underlying property or properties and may include the following: rental income, as well as funds receivable for the recovery of real estate expenses, percentage rent, and miscellaneous tenant charges. Real estate operating expenses may include utility costs, property management fees, real estate taxes, and normal maintenance expenses.

4.09(b) When reporting property specific information, real estate revenues should be recorded when contractually earned. Rent concessions (such as free rent, stepped rent) should not be recorded as income until the rent payments are earned and billable. This process matches appraisal methodology which factors in the future rental income in the determination of the property value. Accruing for free rent/stepped rent would in essence be accounting for the same item twice (i.e., once in the property's valuation and again in an accounts receivable/other asset account outside the property base).

4.09(c) Lease cancellation, termination fees, and penalties or other lump-sum payments received or receivable from tenants who choose to terminate their lease prior to the end of the lease term should be recorded as income when the following criteria have been met: The tenant loses their right to use the space; the owner has no further obligation to provide services; and when payment is determined to be probable.

4.09(d) Real estate expenses should be recognized when incurred. Companies should consider authoritative accounting literature such as ASC 606-10-55-37A, for recording of revenues and expenses gross or net.

## 4.10 Realized and unrealized gains and losses

4.10(a) The periodic valuation of real property, real estate investments, and other non-current assets and liabilities, pursuant to the fair value basis of accounting, results in changes in the reported value of investments, other assets owned, and liabilities owed. These changes are reported in the statement of operations as unrealized gains and losses. While not a required disclosure, the allocation of unrealized gains and losses by the accounts as shown on the statement of net assets can be valuable information for investors. Gains and losses are realized upon disposition of the investments or assets, or the settlement of liabilities; however, sales transactions must also meet the gain recognition criteria set forth in ASC 610-20 See sections 2.04(f) and 2.05(d.2) above for further detail.

4.10(b) Realized gains and losses and the change in unrealized gains and losses are reported separately from net investment income in the statement of operations. Further, the portion of the change in unrealized gains and losses attributable to dispositions or the settlement of liabilities (i.e., the realization of previously reported unrealized gains/losses) is separately reported or otherwise disclosed, as appropriate, for each period presented in the financial statements.

4.10 (c) The distinctions between realized and unrealized recognition are not applied to items of net investment income (i.e., revenue and expenses), even if such items are not currently recorded as a receivable or payable.

4.10(d) A separately disclosed realized gain should be recognized on the extinguishment of debt when real estate is transferred to a lender in satisfaction of non-recourse debt. This gain may be recognized as an unrealized gain prior to reconveyance.

## **4.11 Lease Accounting, including Right of Use (RoU) Assets and Lease Liabilities (ASC 842)**

4.11(a) ASC Topic 842 prescribes the accounting guidance and treatment for lease accounting, including requiring lessees to recognize most leases on their Statement of Net Assets by recording a right-of-use asset ("RoU asset") and a corresponding lease liability for the rights and obligations associated with all lessee leases. ASC 842 also provides guidance related to lessor accounting.

### **4.11(b) Lessee Accounting**

Real estate funds may recognize RoU assets and lease liabilities on the Statement of Net Assets for any ground leases or other contracts classified as leases if the Fund is in the position of lessee. The RoU asset and corresponding lease liability will be measured at fair value at the end of each reporting period. The fair value of the RoU asset is expected to equal the lease liability because the value of the leasehold interest is included in the fair value of the real estate investment and therefore, is not expected to have any net impact on overall net asset value.

Ground lease payments are recommended to be expensed as incurred and reported within the statements of operations. The change in value of the RoU asset and corresponding lease liability will be reported as unrealized gain (loss) within the statements of operations.

Ground leases were classified as operating leases under legacy GAAP, ASC 840, and within comparative financial statements, the current classification and related disclosures will be carried forward for existing leases upon adoption of ASC 842 if the practical expedient transition package was elected.

The leasing standard requires an assessment of the classification of each lease and all new leases in accordance with ASC 842.

### **4.11(c) Lessor Accounting**

ASC 842 changed the definition of a lease component, resulting in certain services being subject to the accounting guidance of ASC 606. ASC 842 requires lessors to allocate the consideration in a contract between the lease component (right to use an underlying asset) and non-lease component (transfer of a good or service that is not a lease – e.g. common area maintenance services). However,

ASU 2018-11, Leases (Topic 842): Targeted Improvements, provided lessors with a practical expedient, elected by class of underlying asset, to account for the lease and non-lease components of a contract as a single lease component, provided that the associated non-lease component(s) otherwise would be accounted for under the revenue guidance within ASC 606 and both of the following criterion are met:

- The timing and pattern of transfer for the lease components and non lease component(s) . . . are the same.
- The lease component, if accounted for separately, would be classified as an operating lease under ASC 842.

Upon making this election, funds should account for the combined component as rental income under ASC 842.

The leasing standard included a change to the treatment of internal leasing costs and legal costs, which can no longer be capitalized. Under ASC 842, only incremental costs of a lease that would not have been incurred if the lease had not been obtained may be deferred as initial direct costs. In addition, the standard requires changes to the provision policy for lease receivables. Under ASC 842, the Fund must assess whether it is probable that it will collect substantially all of the remaining lease payments based on credit risk factors of tenants or other considerations. Changes to the collectability of operating leases will be recorded as adjustments to revenue from real estate investments on the consolidated statements of operations.

Funds will also be required to exclude from variable payments any reimbursements of the fund's costs (e.g., property taxes and insurance) that are paid directly by lessees to a third party (e.g., property taxes that are paid by an outparcel tenant directly to the taxing authority). As a result, revenue and expense related to such cost reimbursements will be presented on a net basis.

# NCREIF PREA Reporting Standards

## Fair Value Accounting Policy

### Manual

## APPENDICES

**Appendix 1:**

**Illustrative financial statements for Operating Model**

The accompanying financial statements are illustrative only and provide a general format for annual financial statements prepared on a fair value basis of accounting using the Operating Model. Disclosures included in the illustrative financial statements are not intended to be comprehensive and are not intended to establish preferences among alternative disclosures.

Note: The accompanying financial statement example is presented on a comparative basis; however, some entities may utilize a single year presentation within their financial statements.

# XYZ Real Estate Account

Financial Statements for the Years Ended December 31, XXCY and XXPY

## XYZ REAL ESTATE ACCOUNT

CONSOLIDATED STATEMENTS OF NET ASSETS  
AS OF DECEMBER 31, XXCY AND XXPY (in thousands)

	XXCY	XXPY
<b>Assets:</b>		
Real estate investments - at fair value:		
Real estate investments and improvements (cost of \$116,000 and \$111,300, respectively)	\$ 139,650	\$ 121,500
Unconsolidated real estate joint ventures (cost of \$46,850 and \$43,500, respectively)	53,200	46,600
Mortgage and other loans receivable (cost of \$11,200 and \$11,150, respectively)	12,100	11,800
Marketable securities - at fair value (cost of \$61,650 and \$52,700, respectively)	65,225	54,100
Total real estate investments	270,175	234,000
Cash and cash equivalents	80,635	49,255
Restricted cash	10,000	10,000
Accounts receivable (net of allowance for doubtful accounts of \$580 and \$500, respectively)	18,620	16,200
Right of use assets - ground leases, at fair value	5,000	-
Prepaid and other assets	42,000	29,200
<b>Total assets</b>	<b>426,430</b>	<b>338,655</b>
<b>Liabilities:</b>		
Mortgage loans and fund level notes payable - at fair value (cost of \$80,760 and \$70,290, respectively)	77,220	64,870
Accrued real estate expenses and taxes	1,350	1,330
Accrued incentive fees (*)	260	250
Lease liabilities - ground leases, at fair value	5,000	-
Other liabilities	2,900	2,055
<b>Total liabilities</b>	<b>86,730</b>	<b>68,505</b>
<b>Net assets:</b>		
XYZ Real Estate Account net assets	318,162	253,356
Noncontrolling interests	21,538	16,794
<b>Net assets</b>	<b>\$ 339,700</b>	<b>\$ 270,150</b>

See accompanying notes to the consolidated financial statements.

For illustrative purposes only - operating model financial statements

\* - This presentation assumes the manager is eligible for an incentive fee that would be reflected on statement of net assets and statement of operations. Alternatively, if the manager, GP or affiliate was a member of the JV and eligible for a promote distribution then the presentation on the statement of changes in net assets would be appropriate.

XYZ REAL ESTATE ACCOUNT

**SCHEDULE OF INVESTMENTS**  
AS OF DECEMBER 31, XXCY AND XXPY (in thousands)

Investment	Ownership	City, State	Acquisition Date	Square Feet Unless Otherwise Indicated (Unaudited)	December 31, XXCY		December 31, XXPY	
					Cost	Fair Value	Cost	Fair Value
Real estate investments and improvements								
Apartment								
Apt 1	WO	City, State	1/1/XXXX	xxx units	\$ 24,800	\$ 24,850	\$ 24,500	\$ 23,000
Apt 2	CJV	City, State	1/1/XXXX	xxx units	22,400	27,700	22,200	25,000
Total apartment				16.52% of NAV as of 12/31/XXCY	47,200	52,550	46,700	48,000
Hotel								
Hotel 1	CJV	City, State	1/1/XXXX	xxx rooms	38,500	45,200	36,500	39,700
Total hotel				14.21% of NAV as of 12/31/XXCY	38,500	45,200	36,500	39,700
Industrial								
Industrial 1	WO	City, State	1/1/XXXX	xxx	6,200	9,000	6,100	6,000
Total industrial				2.83% of NAV as of 12/31/XXCY	6,200	9,000	6,100	6,000
Retail								
Retail 1	CJV	City, State	1/1/XXXX	xxx	24,100	32,900	22,000	27,800
Total retail				10.34% of NAV as of 12/31/XXCY	24,100	32,900	22,000	27,800
<b>Total real estate investments and improvements</b>					<b>116,000</b>	<b>139,650</b>	<b>111,300</b>	<b>121,500</b>
Unconsolidated real estate joint ventures								
Other investments								
Other	EJV	City, State	1/1/XXXX	N/A	12,500	14,500	12,400	13,200
Total other investments				4.56% of NAV as of 12/31/XXCY	12,500	14,500	12,400	13,200
Office								
Office 1	EJV	City, State	1/1/XXXX	xxx	34,350	38,700	31,100	33,400
Total office				12.16% of NAV as of 12/31/XXCY	34,350	38,700	31,100	33,400
<b>Total unconsolidated real estate joint ventures</b>					<b>46,850</b>	<b>53,200</b>	<b>43,500</b>	<b>46,600</b>
Mortgage and other loans receivable								
Loan 1	Loan	City, State	1/1/XXXX	N/A	5,400	5,775	5,350	5,600
Loan 2	Loan	City, State	1/1/XXXX	N/A	5,800	6,325	5,800	6,200
<b>Total mortgage and other loans receivable</b>					<b>11,200</b>	<b>12,100</b>	<b>11,150</b>	<b>11,800</b>
Marketable securities								
Bond 1	Other	City, State	1/1/XXXX	xx shares	61,650	65,225	52,700	54,100
<b>Total marketable securities</b>					<b>61,650</b>	<b>65,225</b>	<b>52,700</b>	<b>54,100</b>
<b>Total real estate investments</b>					<b>\$ 235,700</b>	<b>\$ 270,175</b>	<b>\$ 218,650</b>	<b>\$ 234,000</b>

WO - Wholly Owned Investment

CJV - Consolidated Joint Venture

EJV - Joint Venture Investment accounted for under the equity method

Other - Marketable securities real estate related

See accompanying notes to the consolidated financial statements.

For illustrative purposes only - operating model financial statements

Note: GAAP requirement is to only disclose assets that are greater than 5% of NAV but funds may elect to disclose all assets

**\*The below represents an example Schedules of Investment presentation for Debt Funds following this reporting model. This schedule would replace the Schedule of Investments on the previous page and reflect the loan assets consolidated on the account's Statement of Net Assets\***

XYZ Debt Fund  
 Schedules of Investments  
 As of December 31, 20CY AND 20PY (in thousands)

Investment - Loans Receivable	City, State	Loan Type	Investment Date	Maturity Date	Interest Rate (fixed/variable)	Total Commitment	December 31, 20CY		December 31, 20PY		
							Unfunded Commitments	Investment at Cost	Investment at Fair Value	Unfunded Commitments	Investment at Cost
Apartment											
Loan 1	City, State	LoC	1/1/XXXX	1/1/XXXX	xx.x%/xx.x%	\$ xxx,xxx	\$ xxx,xxx	\$ xxx,xxx	\$ xxx,xxx	\$ xxx,xxx	\$ xxx,xxx
Loan 2	City, State	Mezz	1/1/XXXX	1/1/XXXX	xx.x%/xx.x%	xxx,xxx	xxx,xxx	xxx,xxx	xxx,xxx	xxx,xxx	xxx,xxx
Total apartment						xxx,xxx	xxx,xxx	xxx,xxx	xxx,xxx	xxx,xxx	xxx,xxx
Industrial											
Loan 3	City, State	Bridge loan	1/1/XXXX	1/1/XXXX	xx.x%/xx.x%	xxx,xxx	xxx,xxx	xxx,xxx	xxx,xxx	xxx,xxx	xxx,xxx
Total industrial						xxx,xxx	xxx,xxx	xxx,xxx	xxx,xxx	xxx,xxx	xxx,xxx
<b>Total loans receivable investments</b>						<b>\$ xxx,xxx</b>	<b>\$ xxx,xxx</b>	<b>\$ xxx,xxx</b>	<b>\$ xxx,xxx</b>	<b>\$ xxx,xxx</b>	<b>\$ xxx,xxx</b>

LoC - Line of credit  
 Mezz - Mezzanine loan

See accompanying notes to the consolidated financial statements.  
 For illustrative purposes only - DEBT FUND operating model financial statements

## XYZ REAL ESTATE ACCOUNT

CONSOLIDATED STATEMENTS OF OPERATIONS  
FOR THE YEARS ENDED DECEMBER 31, XXCY AND XXPY (in thousands)

	XXCY	XXPY
<b>Investment income:</b>		
Revenue from real estate investments	\$ 32,150	\$ 31,750
Equity in income of unconsolidated real estate joint ventures	21,450	20,500
Interest income on mortgage and other loans receivable	8,300	7,800
Income from other real estate investments	7,100	6,900
Other income	4,610	4,100
<b>Total investment income</b>	<b>73,610</b>	<b>71,050</b>
<b>Expenses:</b>		
Real estate expenses and taxes	12,250	12,100
Interest expense	3,600	3,250
Administrative expenses	5,390	4,410
Financing costs	10	690
Investment management fees	1,250	1,000
<b>Total expenses</b>	<b>22,500</b>	<b>21,450</b>
<b>Net investment income</b>	<b>51,110</b>	<b>49,600</b>
<b>Net realized and unrealized gain (loss):</b>		
Realized gain from sales of real estate investments	1,100	800
Less: previously recorded unrealized gain on sale of real estate investments	(795)	(500)
Net realized and unrealized gain from the sale of real estate investments	305	300
Unrealized gain (loss) on real estate investments and improvements	14,550	(8,000)
Unrealized gain (loss) on unconsolidated real estate joint ventures	3,250	(1,120)
Unrealized gain on mortgage and other loans receivable	250	100
Unrealized gain on marketable securities	2,175	1,500
Unrealized loss on right of use assets	(1,000)	-
Unrealized gain on interest rate caps and swaps	-	-
Unrealized (loss) gain on mortgage loans and notes payable	(1,880)	1,000
Unrealized gain on lease liabilities	1,000	-
Unrealized incentive fee (*)	(10)	-
<b>Net realized and unrealized gain (loss)</b>	<b>18,640</b>	<b>(6,220)</b>
<b>Increase in net assets resulting from operations</b>	<b>69,750</b>	<b>43,380</b>
Less: Portion attributable to noncontrolling interests	(4,754)	(4,230)
<b>Increase in net assets resulting from operations attributable to XYZ Real Estate Account</b>	<b>\$ 64,996</b>	<b>\$ 39,150</b>
<b>Amounts attributable to XYZ Real Estate Account</b>		
Net investment income	\$ 48,857	\$ 45,059
Net realized and unrealized gain (loss)	16,139	(5,909)
<b>Increase in net assets resulting from operations attributable to XYZ Real Estate Account</b>	<b>\$ 64,996</b>	<b>\$ 39,150</b>

See accompanying notes to the consolidated financial statements.

For illustrative purposes only - operating model financial statements

\* - This presentation assumes the manager is eligible for an incentive fee that would be reflected on statement of net assets and statement of operations. Alternatively, if the manager, GP or affiliate was a member of the JV and eligible for a promote distribution then the presentation on the statement of changes in net assets would be appropriate.

**XYZ REAL ESTATE ACCOUNT**

**CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS  
FOR THE YEARS ENDED DECEMBER 31, XXCY AND XXPY (in thousands)**

	XYZ Real Estate Account		Noncontrolling Interest	Total
	Limited Partners	General Partners		
<b>Net assets - December 31, XXPY-1</b>	\$ 214,016	\$ -	\$ 12,554	\$ 226,570
From operations:				
Net investment income	45,059	-	4,541	49,600
Net realized and unrealized loss	(5,909)	-	(311)	(6,220)
Increase in net assets resulting from operations	39,150	-	4,230	43,380
From capital transactions:				
Contributions	570	-	30	600
Distributions	(380)	-	(20)	(400)
Promote allocation (*)	-	-	-	-
Increase in net assets resulting from capital transactions	190	-	10	200
Increase in net assets	39,340	-	4,240	43,580
<b>Net assets - December 31, XXPY</b>	<b>253,356</b>	-	<b>16,794</b>	<b>270,150</b>
From operations:				
Net investment income	48,857	-	2,253	51,110
Net realized and unrealized gain	16,139	-	2,501	18,640
Increase in net assets resulting from operations	64,996	-	4,754	69,750
From capital transactions:				
Contributions	285	-	15	300
Distributions	(475)	-	(25)	(500)
Promote allocation (*)	-	-	-	-
Decrease in net assets resulting from capital transactions	(190)	-	(10)	(200)
Increase in net assets	64,806	-	4,744	69,550
<b>Net assets - December 31, XXCY</b>	<b>\$ 318,162</b>	<b>\$ -</b>	<b>\$ 21,538</b>	<b>\$ 339,700</b>

See accompanying notes to the consolidated financial statements.

*For illustrative purposes only - operating model financial statements*

\* - If the GP was eligible for a promote distribution then this presentation on the statement of changes in net assets would be appropriate. Alternatively, there could be an incentive fee as reflected on statement of net assets and statement of operations.

**XYZ REAL ESTATE ACCOUNT**
**CONSOLIDATED STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED DECEMBER 31, XXCY AND XXPY (in thousands)**

	<b>XXCY</b>	<b>XXPY</b>
<b>Cash flows from operating activities:</b>		
Increase in net assets resulting from operations	\$ 69,750	\$ 43,380
Adjustments to reconcile increase in net assets resulting from operations to net cash flows from operating activities:		
Net realized and unrealized (gain) loss	(18,640)	6,220
Bad debt expense	80	-
Equity in income of unconsolidated real estate joint ventures	(21,450)	(20,500)
Income distributions from unconsolidated real estate joint ventures	13,100	11,550
Changes in other assets and liabilities:		
Accounts receivable	(2,500)	(1,050)
Prepaid and other assets	(12,800)	(8,050)
Accrued real estate expenses and taxes	20	(155)
Accrued incentive fees	10	1,005
Other liabilities	845	(110)
<b>Net cash flow provided by operating activities</b>	<b>28,415</b>	<b>32,290</b>
<b>Cash flows from investing activities: (*)</b>		
Capital expenditures on real estate investments	(5,495)	(4,700)
Investment in real estate joint ventures	-	(2,500)
Net proceeds from real estate investments sold	2,200	1,100
Return of capital from unconsolidated real estate joint ventures	5,000	3,000
Funding of mortgage and other loans receivable	(60)	(45)
Purchase of marketable securities	(8,950)	-
Sales and maturities of marketable securities	10	-
<b>Net cash flow used in investing activities</b>	<b>(7,295)</b>	<b>(3,145)</b>
<b>Cash flows from financing activities:</b>		
Proceeds from mortgage loans and fund level notes payable	10,470	-
Principal repayments on mortgage loans and fund level notes payable	-	(1,900)
Payment of financing costs	(10)	(690)
Contributions	285	570
Distributions	(475)	(380)
Contributions from noncontrolling interests	15	30
Distributions to noncontrolling interests	(25)	(20)
<b>Net cash flow provided by (used in) financing activities</b>	<b>10,260</b>	<b>(2,390)</b>
<b>Net change in cash and cash equivalents and restricted cash</b>	<b>31,380</b>	<b>26,755</b>
Cash and cash equivalents and restricted cash— Beginning of year	59,255	32,500
<b>Cash and cash equivalents and restricted cash — End of year</b>	<b>\$ 90,635</b>	<b>\$ 59,255</b>
<b>Supplemental cash flow information:</b>		
Cash paid for interest, net of amounts capitalized of \$1	\$ 3,600	\$ 3,250
Cash paid for income taxes	12	10
<b>Supplemental non-cash cash flow information:</b>		
Recognition of RoU assets and corresponding lease liabilities under ASC 842	6,000	-
Accrued capital expenditures	4,000	-

See accompanying notes to the consolidated financial statements.

*For illustrative purposes only - operating model financial statements*

\*If the entity reports as an investment company under ASC 946, the investing activities section may be included in the operating activities section

## **XYZ REAL ESTATE ACCOUNT**

### **NOTES TO CONSOLIDATED FINANCIAL STATEMENTS** **YEARS ENDED DECEMBER 31, 20XX AND 20XX**

#### **1. ORGANIZATION**

Example A: Separate Account financial statements with single institutional investor:

The XXXX Retirement Association has approved certain asset allocations in core equity real estate (the “Account”) for which Real Estate Account LLC is the Investment Advisor (“ABC” or “Investment Advisor”). The Account is an investment account in the business of acquiring, improving, operating, and holding for investment, income-producing industrial, retail, office, and residential properties. The Account may also invest in real estate loans or other marketable securities.

The Account’s total equity commitments are \$xxx,xxx,xxx, of which \$xx,xxx,xxx and \$xx,xxx,xxx remains unfunded as of December 31, CY and PY, respectively.

Example B: Commingled fund with limited partner(s) and general partner.

XYZ Real Estate Account, LP (the “Account”) is a Delaware limited partnership formed on XXXXXX (the “Initial Agreement”) between General Partner LLC (the “General Partner”), a Delaware limited liability company, and other investors (the “Limited Partners”).

The Account is an investment account in the business of acquiring, improving, operating, and holding for investment, income-producing industrial, retail, office, and residential properties. The Account may also invest in real estate loans or other marketable securities.

The managing member of the General Partner is a wholly-owned subsidiary of the Investment Advisor (“ABC” or “Investment Advisor”) and has ultimate responsibility for the management and operations of the Account.

The Account’s total equity commitments are \$xxx,xxx,xxx, of which \$xx,xxx,xxx and \$xx,xxx,xxx remains unfunded as of December 31, CY and PY, respectively.

#### **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Basis of Presentation** — The accompanying consolidated financial statements of the Account have been presented in conformity with accounting principles generally accepted in the United States of America.

The Account is a public employees’ retirement system. Accounting principles for public employee retirement systems require that, among other things, investments in real estate be stated at fair value.

OR

Under ASC 946, *Financial Services – Investment Companies*, the Account qualifies as an investment company.

The accompanying consolidated financial statements include the accounts of the Account and all subsidiaries over which the Account is able to exercise control. The equity interests in those consolidated subsidiaries not owned by the Account are reflected as noncontrolling interests. The Account does not consider itself to be in control when other partners have important approval rights over major activities. Investments in noncontrolled entities are accounted for using the equity method [are not consolidated]. All intercompany balances and transactions have been eliminated in consolidation.

**Variable Interest Entities** — VIEs are defined as entities in which equity investors (i) do not have the characteristics of a controlling financial interest, and/or (ii) do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. The entity that consolidates a VIE is known as its primary beneficiary, and is generally the entity with (i) the power to direct the activities that most significantly impact the VIE's economic performance, and (ii) the right to receive benefits from the VIE or the obligation to absorb losses of the VIE that could be significant to the VIE.

The VIEs of the Account acquire, develop, lease, manage, operate, improve, finance, and sell real estate property.

#### Consolidated VIEs

As of December 31, XXCY, and XXPY the Account consolidated XX and XX VIEs, respectively.

The total assets and liabilities of the VIE's as of December 31, XXCY and XXPY are as follows:

[disclose total assets and liabilities either in sentence above or tabular format]]

**Noncontrolling Interests** - Noncontrolling interests in the Account's consolidated subsidiaries are classified to net assets and the net increase or decrease in net asset value from operations is adjusted to include amounts attributable to noncontrolling interests.

Additionally, losses attributable to the noncontrolling interest in a subsidiary may exceed their interests in the subsidiary's equity. Therefore, the noncontrolling interest shall continue to be allocated their share of losses even if that allocation results in a deficit noncontrolling interest balance.

**Use of estimates** — The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from these estimates.

The real estate and capital markets are cyclical in nature. Property and investment values are affected by, among other things, the availability of capital, occupancy rates, rental rates and interest and inflation rates. As a result, determining real estate and investment values involves many assumptions. Amounts ultimately realized from each investment may vary significantly from the fair values presented.

**Real estate investments and improvements** — Investments in real estate are carried at fair value. Properties owned are initially recorded at the purchase price plus acquisition costs. Development costs and major renovations are capitalized as a component of cost, and routine maintenance and repairs are charged to expense as incurred.

**Unconsolidated real estate joint ventures** — Investments in unconsolidated joint ventures are carried at fair value and are presented in the financial statements using the equity method of accounting [on a non-consolidated basis] as the Account exercises significant influence over operating, investing, and financial policies of such ventures, but does not maintain overall control. The investment is initially recorded at the original investment amount, plus additional amounts invested, and is subsequently adjusted for the Account's share of undistributed earnings or losses (including unrealized appreciation and depreciation) from the underlying entity. In addition, the Account classifies and accounts for investments in certain participating loans as investments in joint ventures where arrangements have virtually the same risks and rewards of ownership. The Account accounts for distributions from non-consolidated joint ventures using the [look-through method / cumulative earnings and profits method] for determining classification within the consolidated statements of cash flows.

**Mortgage and other loans receivable** — Investments in mortgage loans receivable are carried at fair value. Loan acquisition and origination costs are capitalized as a component of cost.

**Investment valuation** — Real estate values are based upon independent appraisals, estimated sales proceeds or the Investment Advisor's opinion of value. Such values have been identified for investment and portfolio management purposes only; the Account reserves its right to pursue full remedies for the recovery of its investments and other rights. The fair value of real estate investments does not reflect transaction sale costs, which may be incurred upon disposition of the real estate investments.

As described above, the estimated fair value of real estate related assets is determined through an appraisal process. These estimated fair values may vary significantly from the prices at which the real estate investments would sell as market prices of real estate investments can only be determined by negotiation between a willing buyer and seller. Although the estimated fair values represent subjective estimates, management believes these estimated fair values are reasonable approximations of market prices and the aggregate estimated value of investments in real estate is fairly presented at December 31, XXCY and XXPY.

**Concentration of credit risk** — The Account invests its cash primarily in deposits and money market funds with commercial banks. At times, cash balances at a limited number of banks and financial institutions may exceed federally insured amounts. The Investment Advisor believes it mitigates credit risk by depositing cash in or investing through major financial institutions. In addition, in the normal course of business, the Account extends credit to its tenants, which consist of local, regional and national based tenants. The Investment Advisor does not believe this represents a material risk of loss with respect to its financial position.

**Cash and cash equivalents** — Cash and cash equivalents are comprised of cash and short-term investments with original maturity dates of less than ninety days from the date of purchase.

**Restricted cash** — Restricted cash includes escrow accounts held by lenders for real estate taxes. The following table provides a reconciliation of cash and cash equivalents and restricted cash reported within the consolidated statements of net assets to the total of the same such amounts shown in the consolidated statements of cash flows for the years ended December 31, XXCY and XXPY (in thousands):

Year Ended	December 31, XXCY	December 31, XXPY
Cash and cash equivalents	\$ 80,635	\$ 49,255
Restricted cash	<u>10,000</u>	<u>10,000</u>
Cash, cash equivalents, and restricted cash	<u><u>\$ 90,635</u></u>	<u><u>\$ 59,255</u></u>

**\*Note> Preparer of the consolidated financial statements has the option to present this tabular reconciliation on the face of the consolidated statement of cash flows prior to the supplemental cash flow information section.**

**Mortgage loans and notes payable** — Mortgage loans and notes payable are shown at fair value. Subsequent to the adoption of The Fair Value Option under ASC subtopic 825-10 (“ASC 825-10”), deferred financing costs are charged to expense as incurred and not deferred. For the years ended December 31, XXCY and XXPY the Account incurred financing costs of \$xx,xxx and \$xx,xxx, respectively. Such amounts are included in interest expense in the accompanying consolidated statements of operations.

**Interest rate swaps and caps** — The Account records derivative financial instruments, primarily interest rate caps and swaps, at fair value, which is the estimated amounts that the Account would receive or pay in a current exchange transaction at the reporting date, taking into account current interest rates and the current credit worthiness of the respective counter-parties. The Account uses interest rate swaps and caps in order to reduce the effect of interest rate fluctuations of certain real estate investments’ interest expense on variable debt. See Note 6.

**Income and expense recognition** — Rental income is recognized on an accrual basis in accordance with the terms of the underlying lease agreements. Other lease rental income, such as adjustments based on the Consumer Price Index, charges to tenants for their share of operating expenses, and percentage rents based on sales, are recognized when earned. Interest income is accrued as earned in accordance with the contractual terms of the loan agreements. Operating expenses are recognized as incurred.

#### Leases –

##### *Lessor Accounting*

The Account combines the lease component (right to use an underlying asset) and non-lease components (transfer of a good or service that is not a lease such common area maintenance services) of its leases as revenue from real estate investments within the consolidated statements of operations. The Account combines these components given that the following criteria are met: (1) both the timing and pattern of

transfer are the same for the non-lease component(s) and related lease component, and (2) the lease component would be classified as an operating lease if accounted for separately.

#### *Lessee Accounting*

The Account's leases where it is the lessee primarily consist of ground leases which are classified as operating leases [finance leases]. The Account has recorded a RoU asset and related lease liability for the rights and obligations associated with these operating leases. During the year ended December 31, CY, the Account recognized lease liabilities of \$6,000 and RoU assets of \$6,000 for new ground lease arrangements in which the Account is the lessee. At December 31, CY, the balance of lease liabilities was \$5,000 and RoU assets was \$5,000. These lease liabilities and RoU assets are shown as a separate line item on the consolidated statements of net assets.

The lease liabilities and corresponding RoU assets are recorded at fair value. \*[The fair value of the lease liabilities is determined using a discounted cash flow approach with a discount rate and other assumptions that approximate current market conditions. The fair value of lease liabilities is determined by discounting the future contractual cash flows to the present value using a discount rate that is commensurate with the rate utilized in the underlying valuation of the real estate investment for each ground lease. The discount rate is determined by giving consideration to one or more of the following criteria as appropriate: (i) rates for similar property types, quality, and maturity, and (ii) the fair value of the underlying collateral.]\*

*\*Note – to be updated based on the valuation methodology elected\**

The Account values the lease liabilities and RoU assets on a quarterly [annual] basis and the amount of unrealized gain (loss) between the lease liabilities and RoU assets offset to have no material impact on net assets. For the years ended December 31, XXCY and XXPY, the Account recorded unrealized gain of \$1,000 and \$0, respectively, on the lease liabilities and unrealized loss of \$1,000 and \$0, respectively, on the RoU assets.

Our current lessee lease portfolio is comprised primarily of operating leases [finance leases].

**Investment management fees** — Investment management fees include asset management fees and investment acquisition fees charged by ABC. Such amounts are reflected in the accompanying consolidated financial statements when incurred.

**Income taxes** — The Account has been classified as a qualified trust under Section 401(a) of the internal Revenue Code of 1986 (the "Code") and management believes it continues to comply with the requirements of Section 501(a) of the Code. Accordingly, the Account is exempt from income taxes, and no income tax provision is provided. If an uncertain income tax position were to be identified, the Account would account for such in accordance with Subtopic 450, Contingencies.

ASC Subtopic 740, Income Taxes (ASC 740), provides guidance for how uncertain tax positions should be recognized, measured, presented and disclosed in the consolidated financial statements. ASC 740 requires the evaluation of tax positions taken in the course of preparing the Account's tax returns to determine

whether tax positions are “more-likely-than-not” of being sustained by the applicable tax authority. Tax benefits of positions not deemed to meet the more-likely-than-not threshold would be recorded as a tax expense in the current year.

**Guarantees** — The Account is required to recognize, at inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing a guarantee. At the inception of guarantees issued, the Account will record the fair value of the guarantee as a liability, with the offsetting entry being recorded based on the circumstances in which the guarantee was issued. The Account did not have any material guarantee liabilities at December 31, XXCY and XXPY.

**Foreign currency** — For investments held outside the United States of America (the “USA”), the Account uses the local currency of the place of operations as its functional currency. Assets and liabilities are translated to U.S. dollars using current exchange rates at the date of the Statement of Net Assets . Revenue and expenses are translated to U.S. dollars using a weighted average exchange rate during the year. The gains and losses resulting from such translation are reported as a component of unrealized gains and losses on the consolidated statements of operations. The cumulative translation gain (loss) as of December 31, XXCY and XXPY was \$xx,xxx and \$xx,xxx, respectively. Foreign currency transactions may produce receivables or payables that are fixed in terms of the amount of foreign currency that will be received or paid. A change in the exchange rates between the functional currency and the currency in which the transaction is denominated increases or decreases the expected amount of functional currency cash flows upon settlement of that transaction. That increase or decrease in the expected functional currency cash flows is a foreign currency transaction gain or loss that generally will be included in determining total unrealized gains and losses on the consolidated statements of operations. A transaction gain or loss (measured from the transaction date or the most recent intervening date of the Statement of Net Assets, whichever is later), realized upon settlement of a foreign currency transaction generally will be included as a component of realized gains and losses on the consolidated statements of operations. The real estate investments were funded partially through financing based arrangements that are scheduled for settlement, consisting primarily of accrued interest and intercompany loans with scheduled principal payments. For the years ended December 31, XXCY and XXPY, the Account recognized realized gains of \$xx,xxx and \$xx,xxx, respectively on foreign currency transactions in connection with the distribution of cash from foreign operating investees to the Account.

**Risk management** — In the normal course of business, the Account encounters economic risk, including interest rate risk, credit risk, foreign currency risk and market risk. Interest rate risk is the result of movements in the underlying variable component of the mortgage financing rates. Credit risk is the risk of default on the Account’s real estate investments that results from an underlying tenant’s inability or unwillingness to make contractually required payments. Foreign currency risk is the effect of exchange rate movements of foreign currencies against the dollar. Market risk reflects changes in the valuation of real estate investments held by the Account.

The Account has not directly entered into any derivative contracts for speculative or hedging purposes against these risks. One of the Account’s investments (\_\_\_\_\_), which owns a facility in \_\_\_\_\_, has entered

into a pay-fixed interest rate swap to manage interest rate risk exposure on its variable rate financing. The investee (\_\_\_\_\_) is potentially exposed to credit loss in the event of non-performance by the counterparty; however, due to the counterparty's credit rating, the Account does not anticipate that the counterparty will fail to meet their obligations.

### **Recently issued accounting standards**

Accounting Standard Updates (ASUs) recently issued that may be applicable to users of this manual include the following<sup>1</sup>:

- None noted for the year ending December 31, 2025. Open to update in future periods.

**Impact of accounting standards not yet adopted** — [to be tailored to each year at management's discretion.]

### **3. FAIR VALUE MEASUREMENTS<sup>2</sup>**

In determining fair value, the Account uses various valuation approaches. ASC 820 establishes fair value measurement framework, provides a single definition of fair value, and requires expanded disclosure summarizing fair value measurements. ASC 820 emphasizes that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing an asset or liability.

The standard establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable input be used when available. Observable inputs are inputs that the market participants would use in pricing the asset or liability developed based on market data obtained from sources independent of the Account. Unobservable inputs are inputs that reflect the Account's assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. The hierarchy is measured in three levels based on the reliability of inputs:

*Level 1* — Valuations based on quoted prices in active markets for identical assets or liabilities that the Account has the ability to access. Valuation adjustment and block discounts are not applied to Level 1 instruments.

*Level 2* — Valuations based on quoted prices in less active, dealer or broker markets. Fair values are primarily obtained from third party pricing services for identical or comparable assets or liabilities.

*Level 3* — Valuations derived from other valuation methodologies, including pricing models, discounted cash flow models and similar techniques, and not based on market, exchange, dealer, or broker-traded transactions. Level 3 valuations incorporate certain assumptions and projections that are not observable in

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<sup>1</sup> Additional ASUs may be applicable, as determined by management.

<sup>2</sup> This footnote highlights disclosures that are optional after the adoption of ASU 2018-13, *Fair Value Measurement (Topic 820): Disclosure Framework — Changes to the Disclosure Requirements for Fair Value Measurement*.

the market and use significant professional judgment in determining the fair value assigned to such assets or liabilities.

In instances where the determination of the fair value measurement is based on inputs from different levels of the fair value hierarchy, the level in the fair value hierarchy within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety.

ASC 825 provides entities with a one-time irrevocable option to fair value eligible assets and liabilities and requires both qualitative and quantitative disclosures to those for which an election is made. Unrealized gains and losses on items for which the Fair Value Option has been elected are reported in earnings. The Account has elected the Fair Value Option for all of its mortgages to better align the measurement attributes of both the assets and liabilities while providing investors with a more meaningful indication of the fair value of the Account's net asset value.

The following is a description of the valuation techniques used for items measured at fair value:

Real estate investments and improvements— The values of real estate properties have been prepared giving consideration to the income, cost and sales comparison approaches of estimating property value. The income approach estimates an income stream for a property (typically 10 years) and discounts this income plus a reversion (presumed sale) into a present value at a risk adjusted rate. Yield rates and growth assumptions utilized in this approach are derived from market transactions as well as other financial and industry data. The cost approach estimates the replacement cost of the building less physical depreciation plus the land value. Generally, this approach provides a validation on the value derived using the income approach. The sales comparison approach compares recent transactions to the appraised property. Adjustments are made for dissimilarities which typically provide a range of value. The income approach was used to value all of the Account's real estate investments for the years ended December 31, XXCY and XXPY. The terminal cap rate and the discount rate are significant inputs to these valuations. These rates are based on the location, type and nature of each property, and current and anticipated market conditions. [Significant increases in discount or capitalization rates in isolation would result in a significantly lower fair value measurement. Significant decreases in discount or capitalization rates in isolation would result in a significantly higher fair value measurement.]<sup>3</sup>

Investment values are determined quarterly from limited restricted appraisals, in accordance with the Uniform Standards of Professional Appraisal Practice ("USPAP"), which include less documentation but nevertheless meet the minimum requirements of the Appraisal Standards Board and the Appraisal Foundation and are considered appraisals. In these appraisals, a full discounted cash flow analysis, which is the basis of an income approach, is the primary focus. Interim monthly valuations are determined by giving consideration to material investment transactions. Full appraisal reports are prepared on a rotating basis for all properties, so each property receives a full appraisal report at least once every three years.

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<sup>3</sup> Bracketed wording required for SEC registrants.

As fair value measurements take into consideration the estimated effect of physical depreciation, historical cost depreciation and amortization on real estate related assets has been excluded from net investment income.

The values of real estate properties undergoing development have been prepared giving consideration to costs incurred to date and to key development risk factors, including entitlement risk, construction risk, leasing/sales risk, operation expense risk, credit risk, capital market risk, pricing risk, event risk and valuation risk. The fair value of properties undergoing development includes the timely recognition of estimated entrepreneurial profit after such consideration.

During XXCY and XXPY, all appraisals for the Account were prepared by independent external appraisers and reviewed and approved by management. The external appraisals are reviewed by an external appraisal management firm. All appraisal reports and appraisal reviews comply with the currently published USPAP, as promulgated by the Appraisal Foundation. The Account's real estate properties are generally classified within level 3 of the valuation hierarchy.

**Unconsolidated real estate joint ventures** — Real estate joint ventures and certain limited partnerships are stated at the fair value of the Account's ownership interests of the underlying entities. The Account's ownership interests are valued based on the fair value of the underlying real estate, any related mortgage loans payable, and other factors, such as ownership percentage, ownership rights, buy/sell agreements, distribution provisions and capital call obligations. The underlying assets and liabilities are valued using the same methods as the Account uses for those assets and liabilities it holds directly. Upon the disposition of all real estate investments by an investee entity, the Account will continue to state its equity in the remaining net assets of the investee entity during the wind down period, if any that occurs prior to the dissolution of the investee entity. The Account's real estate joint ventures and limited partnerships are generally classified within level 3 of the valuation hierarchy.

**Mortgage and other loans receivable** — The fair value of mortgage and other loans receivable held by the Account have been determined by one or more of the following criteria as appropriate: (i) on the basis of estimated market interest rates for loans of comparable quality and maturity, (ii) by recognizing the value of equity participations and options to enter into equity participations contained in certain loan instruments and (iii) giving consideration to the value of the underlying collateral. The Account's mortgage and other loans receivable are classified within level 3 of the valuation hierarchy. The fair value of mortgage and other loans receivable are determined by discounting future contractual cash flows to the present value using a current market interest rate, which is updated quarterly by personnel responsible for the management of each investment and reviewed by senior management at each reporting period. Many methods are used to develop and substantiate unobservable inputs such as analyzing discount and capitalization rates as well as researching revenue and expense growth. [Significant increases in discount or capitalization rates in isolation would result in a significantly lower fair value measurement while significant increases in revenue growth rates in isolation would result in a significantly higher fair value measurement. Significant decreases in discount or capitalization rates in isolation would result in a significantly higher fair value measurement while

significant decreases in revenue growth rates in isolation would result in a significantly lower fair value measurement.]<sup>4</sup>

Marketable securities — Equity securities listed or traded on any national market or exchange are valued at the last sale prices as of the close of the principal securities exchange on which such securities are traded or, if there is no sale, at the mean of the last bid and asked prices on such exchange, exclusive of transaction costs. Such marketable securities are classified within level 1 of the valuation hierarchy.

Debt securities, other than money market instruments, are generally valued at the most recent bid price of the equivalent quoted yield for such securities (or those of comparable maturity, quality, and type). Money market instruments with maturities of one year or less are valued in the same manner as debt securities or derived from a pricing matrix. Debt securities are generally classified within level 2 of the valuation hierarchy.

Interest rate swaps and caps — The fair value of interest rate swaps and caps held by the Account are determined by using market standard methodology of netting the discounted future fixed cash receipts or payments. The variable cash payments or receipts are based on an expectation of future interest rates (forward curves) derived from observable market interest rate curves. Interest rate caps and swaps are generally classified within level 2 of the valuation hierarchy.

Mortgage loans and notes payable — The fair values of mortgage loans and notes payable are determined by discounting the future contractual cash flows to the present value using a current market interest rate, which is updated quarterly by personnel responsible for the management of each investment and reviewed by senior management at each reporting period. The market rate is determined by giving consideration to one or more of the following criteria as appropriate: (i) interest rates for loans of comparable quality and maturity, and (ii) the value of the underlying collateral. The Account's mortgage loans and notes payable are generally classified within level 3 of the valuation hierarchy. The significant unobservable inputs used in the fair value measurement of the Account's mortgage loans payable are the loan to value ratios and the selection of certain credit spreads and weighted average cost of capital risk premiums. [Significant increases (decreases) in any of those inputs in isolation would result in a significantly lower (higher) fair value, respectively.]<sup>5</sup>

RoU assets and lease liabilities — The fair value of lease liabilities is determined \*[using a discounted cash flow approach with a discount rate and other assumptions that approximate current market conditions. The fair value of lease liabilities is determined by discounting the future contractual cash flows to the present value using a discount rate that is commensurate with the rate utilized in the underlying valuation of the real estate investment for each ground lease. The discount rate is determined by giving consideration to one or more of the following criteria as appropriate: (i) rates for similar property types, quality, and maturity, and (ii) the fair value of the underlying collateral. The fair value of the RoU asset is equal to the corresponding value of each respective lease liability.]\*

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<sup>4</sup> Bracketed wording required for SEC registrants.

<sup>5</sup> Bracketed wording required for SEC registrants.

\*Note - to be updated based on the valuation methodology elected\*

The following are the classes of assets and liabilities measured at fair value on a recurring basis during the year ended December 31, XXCY, using unadjusted quoted prices in active markets for identical assets (Level 1); significant other observable inputs (Level 2); and significant unobservable inputs (Level 3):

Description	Level 1: Quoted Prices in Active Markets for Identical Assets	Level 2: Significant Other Observable Inputs	Level 3: Significant Unobservable Inputs	Total at December 31, XXCY
Real estate investments and improvements	\$ -	\$ -	\$ 139,650	\$ 139,650
Unconsolidated real estate joint ventures	-	-	53,200	53,200
Mortgage and other loans receivable	-	-	12,100	12,100
Marketable securities	-	65,225	-	65,225
 Total real estate investments	 \$ -	 \$ 65,225	 \$ 204,950	 \$ 270,175
Right of use assets - ground leases, at fair value	\$ -	\$ -	\$ 5,000	\$ 5,000
Interest rate caps and swaps	\$ -	\$ 2,600	\$ -	\$ 2,600
Mortgage loans and fund level notes payable	\$ -	\$ -	\$ (77,220)	\$ (77,220)
Lease liabilities - ground leases, at fair value	\$ -	\$ -	\$ (5,000)	\$ (5,000)

The following are the classes of assets and liabilities measured at fair value on a recurring basis during the year ended December 31, XXPY, using unadjusted quoted prices in active markets for identical assets (Level 1); significant other observable inputs (Level 2); and significant unobservable inputs (Level 3):

Description	Level 1: Quoted Prices in Active Markets for Identical Assets	Level 2: Significant Other Observable Inputs	Level 3: Significant Unobservable Inputs	Total at December 31, XXPY
Real estate investments and improvements	\$ -	\$ -	\$ 121,500	\$ 121,500
Unconsolidated real estate joint ventures	-	-	46,600	46,600
Mortgage and other loans receivable	-	-	11,800	11,800
Marketable securities	-	54,100	-	54,100
 Total real estate investments	 \$ -	 \$ 54,100	 \$ 179,900	 \$ 234,000
Interest rate caps and swaps	\$ -	\$ 2,600	\$ -	\$ 2,600
Mortgage loans and fund level notes payable	\$ -	\$ -	\$ (64,870)	\$ (64,870)

The following is a reconciliation of the beginning and ending balances for assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) during the year ended December 31, XXCY and XXPY:

Description	Real Estate and Improvements	Unconsolidated Real Estate Joint Ventures	Mortgage and Other Loans Receivable	Mortgage Loans and Fund Notes Payable	RoU Assets - Ground Leases <sup>2</sup>	Lease Liabilities - Ground Leases <sup>2</sup>
<b>Beginning balance December 31, XXPY</b>	\$ 121,500	\$ 46,600	\$ 11,800	\$ (64,870)	\$ -	\$ -
Acquisition of new ground lease - RoU asset and lease liability					6,000	(6,000)
<i>Realized and unrealized gain (loss) on real estate investments <sup>1</sup></i>	14,855	3,250	250	(1,880)	(1,000)	1,000
<i>Equity in income of unconsolidated real estate joint ventures <sup>1</sup></i>	-	21,450	-	-	-	-
<i>Income distributions from unconsolidated real estate joint ventures</i>	-	(13,100)	-	-	-	-
<i>Return of capital from unconsolidated real estate joint ventures <sup>1</sup></i>	-	(5,000)	-	-	-	-
<i>Purchases of real estate investments/capital improvements</i>	5,495	-	-	-	-	-
<i>Proceeds from sale of real estate investments <sup>1</sup></i>	(2,200)	-	-	-	-	-
<i>Issuances of mortgage and other loans receivable</i>	-	-	50	-	-	-
<i>Borrowings on mortgage loans and notes payable</i>	-	-	-	(10,470)	-	-
<b>Ending balance December 31, XXCY</b>	<b>\$ 139,650</b>	<b>\$ 53,200</b>	<b>\$ 12,100</b>	<b>\$ (77,220)</b>	<b>\$ 5,000</b>	<b>\$ (5,000)</b>
	-	-	-	-	-	-
<b>Beginning balance December 31, XXPY-1</b>	<b>\$ 125,900</b>	<b>\$ 39,270</b>	<b>\$ 11,655</b>	<b>\$ (67,770)</b>	<b>\$ -</b>	<b>\$ -</b>
<i>Unrealized gain (loss) on real estate investments <sup>1</sup></i>	(8,000)	(1,120)	100	1,000	-	-
<i>Equity in income of unconsolidated real estate joint ventures <sup>1</sup></i>	-	20,500	-	-	-	-
<i>Income distributions from unconsolidated real estate joint ventures</i>	-	(11,550)	-	-	-	-
<i>Return of capital from unconsolidated real estate joint ventures <sup>1</sup></i>	-	(3,000)	-	-	-	-
<i>Purchases of real estate investments/capital improvements</i>	4,700	2,500	-	-	-	-
<i>Proceeds from sale of real estate investments <sup>1</sup></i>	(1,100)	-	-	-	-	-
<i>Issuances of mortgage and other loans receivable</i>	-	-	45	-	-	-
<i>Borrowings on mortgage loans and notes payable</i>	-	-	-	1,900	-	-
<b>Ending balance December 31, XXPY</b>	<b>\$ 121,500</b>	<b>\$ 46,600</b>	<b>\$ 11,800</b>	<b>\$ (64,870)</b>	<b>\$ -</b>	<b>\$ -</b>

<sup>1</sup> Optional after the adoption of ASU 2018-13

<sup>2</sup> RoU assets and lease liabilities are recognized upon acquisition of new ground lease during the year ended December 31, CY (See Note 2)

The following table shows quantitative information about significant unobservable inputs related to the level 3 fair value measurements used at December 31, XXCY and XXPY:

## Footnote 3 - Fair Value Measurements

	December 31, XXCY Fair Value	December 31, XXPY Fair Value	Valuation Technique(s)	Unobservable Inputs	December 31, XXCY Ranges (Weighted Average)	December 31, XXPY Ranges (Weighted Average)
<b>Real estate investments and improvements</b>						
Apartment	\$ 52,550	\$ 48,000	Discounted cash flows (DCF)	Discount rate Capitalization rate DCF term (years) Revenue growth rate	xx% to xx% (xx%) xx% to xx% (xx%) 10 years (10 years) xx% to xx% (xx%)	xx% to xx% (xx%) xx% to xx% (xx%) 10 years (10 years) xx% to xx% (xx%)
Hotel	\$ 45,200	\$ 39,700	Direct capitalization method	Direct cap rate	xx% to xx% (xx%)	xx% to xx% (xx%)
Industrial	\$ 9,000	\$ 6,000	Discounted cash flows (DCF)	Discount rate Capitalization rate DCF term (years) Revenue growth rate	xx% to xx% (xx%) xx% to xx% (xx%) 10 years (10 years) xx% to xx% (xx%)	xx% to xx% (xx%) xx% to xx% (xx%) 10 years (10 years) xx% to xx% (xx%)
Retail	\$ 32,900	\$ 27,800	Direct capitalization method	Direct cap rate	xx% to xx% (xx%)	xx% to xx% (xx%)
<b>Unconsolidated real estate joint ventures<sup>1</sup></b>						
Other	\$ 14,500	\$ 13,200	Discounted cash flows (DCF)	Discount rate Capitalization rate DCF term (years) Revenue growth rate	xx% to xx% (xx%) xx% to xx% (xx%) 10 years (10 years) xx% to xx% (xx%)	xx% to xx% (xx%) xx% to xx% (xx%) 10 years (10 years) xx% to xx% (xx%)
Office	\$ 38,700	\$ 33,400	Discounted cash flows (DCF)	Discount rate Capitalization rate DCF term (years) Revenue growth rate	xx% to xx% (xx%) xx% to xx% (xx%) 10 years (10 years) xx% to xx% (xx%)	xx% to xx% (xx%) xx% to xx% (xx%) 10 years (10 years) xx% to xx% (xx%)
<b>Mortgage and other loans receivable</b>						
Industrial	\$ 5,775	\$ 5,600	Discounted cash flows (DCF)	Loan to value ratio	xx% to xx% (xx%)	xx% to xx% (xx%)
Office	\$ 6,325	\$ 6,200	Net present value	Credit spreads Loan to value ratio Weighted average cost of capital risk premiums	xx% to xx% (xx%) xx% to xx% (xx%) xx% to xx% (xx%)	xx% to xx% (xx%) xx% to xx% (xx%) xx% to xx% (xx%)
<b>Mortgage loans and fund level notes payable</b>						
Property	\$ 57,720	\$ 55,840	Discounted cash flows (DCF)	Loan to value ratio	xx% to xx% (xx%)	xx% to xx% (xx%)
Fund	\$ 19,500	\$ 9,030	Net present value	Credit spreads Loan to value ratio Weighted average cost of capital risk premiums	xx% to xx% (xx%) xx% to xx% (xx%) xx% to xx% (xx%)	xx% to xx% (xx%) xx% to xx% (xx%) xx% to xx% (xx%)
<b>RoU assets and lease liabilities - ground leases</b>						
Property Type	\$ 5,000	\$ -	Discounted cash flows (DCF)	Discount rate DCF term (years)	xx% to xx% (xx%) X years (X years)	xx% to xx% (xx%) X years (X years)

<sup>1</sup> The unobservable inputs for unconsolidated real estate joint ventures are calculated based upon 100% of property fair values regardless of the Account's ownership interest.

Senior management, the asset management team and the accounting team review the valuations quarterly. This consists of comparing unobservable inputs to observable inputs for similar positions, reviewing subsequent market activities, performing comparisons of actual versus projected cash flows, and discussing the valuation methodology, including pricing techniques, when applicable, and key assumptions for each investment. Independent pricing services may be used to corroborate the Account's internal valuations. The approach and resulting value for similar investments is compared as part of the overall review of the portfolio. These valuations are reviewed by the accounting team, which is then presented to senior members of management for approval.

*Real estate investments and joint ventures:* The significant unobservable inputs used in the fair value measurement of the Account's real estate property and joint venture investments are the selection of certain investment rates (Discount Rate, Terminal Capitalization Rate, Overall Capitalization Rate, and Revenue Growth Rate). [Significant increases or decreases in any of those inputs in isolation would result in significantly lower or higher fair value measurements, respectively.]

*Mortgage loans receivable and payable:* The significant unobservable inputs used in the fair value measurement of the Account's mortgage loans receivable and payable are the loan to value ratios and the selection of certain credit spreads and weighted average cost of capital risk premiums. [Significant increases (decreases) in any of those inputs in isolation would result in a significantly lower (higher) fair value, respectively]<sup>7</sup>.

<sup>7</sup> Bracketed wording required for SEC registrants.

#### **4. UNCONSOLIDATED REAL ESTATE JOINT VENTURES**

The following is a summary of the fair value basis of assets, liabilities and operating results underlying the Account's unconsolidated real estate joint ventures at December 31, XXCY and XXPY:

	As of December 31, XXCY	As of December 31, XXPY
Land and buildings	\$ 102,000	\$ 91,000
Other assets	9,000	5,300
Mortgage loans	1,000	-
Other liabilities	3,600	3,100
Net assets	\$ 106,400	\$ 93,200
Account's share of unconsolidated real estate joint venture net assets	\$ 53,200	\$ 46,600
Year Ended	December 31, XXCY	December 31, XXPY
Revenues	\$ 72,000	\$ 71,050
Property operating expenses	27,900	28,750
Interest expense	1,200	1,300
Net investment income	\$ 42,900	\$ 41,000
Realized and unrealized gain (loss)	\$ 6,500	\$ (2,240)
Account's equity in income and unrealized gain of unconsolidated real estate joint ventures	\$ 24,700	\$ 19,380

The real estate joint ventures include investments in several real estate funds that invest primarily in U.S. commercial real estate. The fair values of the investments in this category have been estimated using the net asset value of the Account's ownership interest in partners' capital. These investments can never be redeemed with the funds (or these investments may be redeemed quarterly with XX days' notice). Distributions from each fund will be received as the underlying investments of the funds are liquidated. However, the individual investments that will be sold have not yet been determined. Because it is not probable that any individual investment will be sold, the fair value of each individual investment has been estimated using the net asset value of the Account's ownership interest in partners' capital. The Fund's unfunded commitments related to real estate joint ventures were \$XXX, XXX at December 31, XXCY.

*[If there are ground leases within the unconsolidated real estate joint ventures owned by the Account, fund managers should discuss the appropriate level of disclosure with their respective advisors. Options could include disclosing the RoU asset and lease liabilities in the condensed schedules outlined above, or parenthetically disclosing these amounts if deemed material.]*

## 5. MORTGAGE LOANS AND NOTES PAYABLE

Mortgage loans and notes payable consist of the following as of December 31, XXCY and XXPY:

## Footnote 5 - Mortgage Loans and Notes Payable

	XXCY Fair Value	XXCY Cost	XXPY Fair Value	XXPY Cost	Interest Rate <sup>1</sup>	Maturity Date	Terms <sup>3</sup>
Mortgage loans							
Apt 1	\$ -	\$ -	\$ 1,000	\$ -	x.xx% <sup>2</sup>	XXXX	P&I, PP
Apt 2	\$ 14,760	\$ 15,540	\$ 14,020	\$ 15,540	SOFR (30-day) + x.xx%	XXXX	I
Hotel 1	\$ 24,270	\$ 25,550	\$ 23,060	\$ 25,550	SOFR (30-day) + x.xx%	XXXX	I
Industrial 1	\$ 4,060	\$ 4,270	\$ 3,860	\$ 4,340	SOFR (30-day) + x.xx%	XXXX	I
Retail 1	\$ 14,630	\$ 15,400	\$ 13,900	\$ 16,870	SOFR (30-day) + x.xx%	XXXX	I
<b>Total mortgage loans payable</b>	<b>\$ 57,720</b>	<b>\$ 60,760</b>	<b>\$ 55,840</b>	<b>\$ 62,300</b>			
Fund Level Notes Payable							
Line of credit	\$ 9,500	\$ 10,000	\$ 9,030	\$ 7,990	Weekly Variable <sup>4</sup>	XXXX	I
Private placement notes	\$ 10,000	\$ 10,000			SOFR (30-day) + x.xx%	XXXX	I
<b>Total fund level notes payable</b>	<b>\$ 19,500</b>	<b>\$ 20,000</b>	<b>\$ 9,030</b>	<b>\$ 7,990</b>			
<b>Total mortgage loans and fund level notes payable</b>	<b>\$ 77,220</b>	<b>\$ 80,760</b>	<b>\$ 64,870</b>	<b>\$ 70,290</b>			

<sup>1</sup> As of December 31, XXCY, SOFR was x.xxxx%.<sup>2</sup> The loan has a floating interest rate of x.xx% over SOFR however the venture is obligated to pay a fixed rate of x.xx% with the venture partner assuming all interest rate risk or benefit.<sup>3</sup> Loan Terms PP=Prepayment penalties applicable to loan, I=Interest only, P&I=Principal and Interest<sup>4</sup> The Weekly Variable Rate shall be the minimum rate of interest necessary, in the professional judgment of the Remarketing Agent, taking into consideration prevailing market conditions, to enable the Remarketing Agent to remarket all of the Bonds on the applicable Rate Determination Date at par plus accrued interest on the bonds for that week.

Mortgage loans payable for wholly owned properties and consolidated partnerships are collateralized by real estate investments with an aggregate estimated value of \$xxx,xxx and \$xxx,xxx as of December 31, XXCY and XXPY, respectively. The loan agreements contain financial and non-financial covenants, including requirements regarding net assets, leverage ratio, and debt service coverage ratio. The Account believes it was in compliance with all covenants as of and for the year ended December 31, XXCY.

As of December, XXCY principal amounts of mortgage loans and notes payable on wholly-owned properties and consolidated accounts are payable as follows:

**Year Ended December 31**

XXCY+1	\$ -
XXCY+2	\$ -
XXCY+3	\$ -
XXCY+4	\$ -
XXCY+5	\$ -
Thereafter	<u>\$ 80,760</u>
<b>Total</b>	<b><u>\$ 80,760</u></b>

The Account has evaluated its debt instruments to identify those maturing over the next 12 months. The Account has \$XX of debt maturing within the next 12 months, which it intends to settle through refinance or repayment with cash from financings, net cash flows from operations, or proceeds from property dispositions.

## 6. INTEREST RATE SWAPS AND CAPS

Certain of Account's equity method and consolidated joint ventures entered into interest rate swap and cap transactions ("Swaps and Caps") with unrelated major financial institutions. The Account has agreements with each derivative counterparty that contain a provision where if the Account defaults on any of its indebtedness, then the Account could also be declared in default on its derivative obligations.

The Account has recorded the fair values of the Swaps and Caps as of December 31, XXCY and XXPY, which have been reflected in "Other liabilities" or "Prepaid and other assets" on the Consolidated Statements of Net Assets. The resulting unrealized gain (loss) is reflected in the consolidated statements of operations in "Change in unrealized gain (loss) on interest rate swaps and caps" and "Portion attributable to noncontrolling interests".

As of December 31, 20XX and 20XX, interest rate Swaps and Caps are summarized as follows:

Type of contract	Notional Amount	Rate	Fair Value XXCY	Fair Value XXPY	Maturity Date
<b>Real estate investments</b>					
Property 1	Pay-fixed swap	\$ -	x.xx%	\$ -	\$ - July XXXX
Property 2	Pay-floating swap	-	x.xx%	-	- July XXXX
Property 3	Cap	<u>      </u>	<u>      </u>	<u>      </u>	- July XXXX
<b>Total real estate investments</b>	<b>\$ -</b>		<b>\$ -</b>	<b>\$ -</b>	
<b>Unconsolidated real estate joint ventures</b>					
Property 1	Pay-fixed swap	\$ -	x.xx%	\$ -	\$ - January XXXX
Property 2	Pay-fixed swap	-	x.xx%	-	- March XXXX
Property 3	Pay-fixed swap	-	x.xx%	-	- February XXXX
Property 4	Cap	<u>      </u>	<u>      </u>	<u>      </u>	- April XXXX
<b>Total unconsolidated real estate joint ventures</b>	<b>\$ -</b>		<b>\$ -</b>	<b>\$ -</b>	
<b>Total</b>	<b><u>\$ -</u></b>		<b><u>\$ -</u></b>	<b><u>\$ -</u></b>	

## 7. PORTFOLIO DIVERSIFICATION (Optional to include below or in SOI)

At December 31, XXCY, the Account had real estate investments located throughout the United States of America. The diversification of the Account's holdings based on the estimated fair values and established NCREIF divisions is as follows:

Region	Fair Value	Region %
East North Central	\$ 75,649	28
Mideast	48,631	18
Mountain	48,631	18
Northeast	24,316	9
Pacific	24,316	9
Southeast	24,316	9
Southwest	24,316	9
<b>Total</b>	<b>\$ 270,175</b>	<b>100</b>

## 8. RELATED PARTY FEES AND AFFILIATE TRANSACTIONS

**Note:** The below examples are illustrative only and may not represent a comprehensive list of related party/affiliate transactions for a specific Account. The intent is to provide full transparency of related party and affiliate transactions of each Account. Some Investment Managers or General Partners may decide to disclose additional detailed information about related party or affiliate transactions in a separate report to investors.

Third-party payments facilitated by the Investment Advisor/General Partner that are subsequently reimbursed by the Account do not meet the definition of related party transactions under ASC 850.

The examples include various fees and expenses that may be paid to the Investment Advisor/General Partner and do not necessarily correspond to the types of fees used to calculate the net of fee returns or for performance assessments.

This disclosure is not a tool to be used for comparison across Accounts.

The Account incurred Investment Management Fees, Reimbursements, Property Service Fee & Expenses and Other Related Party Transactions of \$xxx,xxx, \$xxx,xxx, \$xxx,xxx and \$xxx,xxx, respectively, for the year ended December 31, XXCY and \$xxx,xxx, \$xxx,xxx, \$xxx,xxx and \$xxx,xxx, respectively, for the year ended December 31, XXPY as illustrated below.

**Investment Management Fees** - The Account has engaged the [Investment Advisor] [General Partner] to provide acquisition, disposition, investment management and other services. Below is a detailed summary of the fees incurred for these services for the years ended December 31, XXCY and XXPY as well as where they are recorded in the financial statements:

Investment Management Fees:	Financial Statement Caption	Year Ended XXCY	Year Ended XXPY	Fee Description
Acquisition	Cost basis of real estate investments	\$xxx,xxx	\$xxx,xxx	XX bp of Total capital committed
Development	Cost basis of real estate investments	xxx,xxx	xxx,xxx	XX bp of Total development costs
Financing	Financing costs	xxx,xxx	xxx,xxx	XX bp of Original principal balance
Loan Origination	Financing costs	xxx,xxx	xxx,xxx	XX bp of Projected principal balance
Investment Management	Investment management fees	xxx,xxx	xxx,xxx	X% of Net operating income
Disposition	Realized gain (loss) from sales of real estate investments	xxx,xxx	xxx,xxx	XX bp of Gross sale price
Incentive <sup>(1)</sup>	Unrealized gain (loss) on real estate investments	xxx,xxx	xxx,xxx	XX% over XX% IRR <sup>(1)</sup>
<b>Total Investment Management Fees</b>		<b>\$xxx,xxx</b>	<b>\$xxx,xxx</b>	

[Add additional fee description details as appropriate]

<sup>(1)</sup>Incentive Fee - In accordance with the Fund's governing documents, the Investment Advisor of the Account, is entitled to earn an incentive fee equal to XX% of investment returns after the Limited Partners achieve a XX% internal rate of return. The incentive fee is only payable upon certain events in accordance with the Account's governing documents.

Investment Management fees, Acquisition fees, Development fees and Financing fees totaling \$xx,xxx and \$xx,xxx were payable at December 31, XXCY and XXPY, respectively and are included in other liabilities within the consolidated statements of net assets.

Incentive fees of \$xx,xxx and \$xx,xxx were payable at December 31, XXCY and XXPY, respectively and are included in accrued incentive fees within the consolidated statements of net assets.

[This is an example disclosure that is not reflected in the Statement of Changes in Net Assets] General Partner Promote -The Partnership agreement provides for distributions to the investors disproportionate to their pro-rata invested capital in the event that the preferred return, as defined, has been paid and all invested capital has been returned. Distributions are first allocated 100% to all investors, in accordance with their ownership interest until invested capital has been returned and the investors have achieved a X% preferred return accrued on its invested capital. Distributions are then allocated XX% to Limited Partners and XX% to the General Partner. An incentive reallocation in the amount of \$x,xxx,xxx would be due to the General Partner based on a hypothetical liquidation of the Account as of December 31, XXCY and is included in the consolidated statement of changes in net assets.

**Reimbursements** - In accordance with the Account's Limited Partnership Agreement, the Partnership will reimburse the [Investment Advisor] [General Partner] for costs and services that are incurred by the [Investment Advisor] [General Partner] on behalf of the Account. Below is a summary of the costs and services that the Partnership reimbursed to the [Investment Advisor] [General Partner] for the years ended December 31, XXCY and XXPY as well as where they are recorded in the financial statements:

Reimbursements	Financial Statement Caption	Year Ended XXCY	Year Ended XXPY
In-house Legal	Administrative expenses	\$xxxx,xxx	\$xxx,xxx
In-house Accounting	Administrative expenses	xxx,xxx	xxx,xxx
In-house Proprietary Software	Administrative expenses	xxx,xxx	xxx,xxx
<b>Total Reimbursements</b>		<b>\$xxx,xxx</b>	<b>\$xxx,xxx</b>

[Add additional Account/Partnership reimbursement description details as appropriate]

Of the reimbursement amounts incurred above, \$xxx and \$xxx were included in other liabilities as of December 31, XXCY and XXPY, respectively.

**Property Service Fees & Expenses** –The Account receives services under various agreements from an [affiliate] or [entity that the General Partner holds an ownership interest in], associated with the ongoing operations of the investments. Below is a detailed summary of the fees incurred for these services for the years ended December 31, XXCY and XXPY as well as where they are recorded in the financial statements:

Property Service Fees & Expenses:	Financial Statement Caption	Year Ended XXCY	Year Ended XXPY	Fee Description
Property Management	Administrative expenses	\$xxx,xxx	\$xxx,xxx	XX-XX bp of Gross receipts
Construction Management	N/A	xxx,xxx	xxx,xxx	XX bp of Development budget
Leasing	N/A	xxx,xxx	xxx,xxx	XX bp of Contract rent
Brokerage	N/A	xxx,xxx	xxx,xxx	XX bp of Sales price
Financing	Financing costs	xxx,xxx	xxx,xxx	XX bp of Projected principal balance
Payroll/benefits for on-site management	Administrative expenses	xxx,xxx	xxx,xxx	N/A
<b>Total Property Service Fees &amp; Expenses</b>		<b>\$xxx,xxx</b>	<b>\$xxx,xxx</b>	

[Add additional Service Fees & Expenses description details as appropriate]

Of the service fees & expense amounts incurred above, \$xxx and \$xxx were included in other liabilities as of December 31, XXCY and XXPY, respectively.

[Note that Financial Statement Captions above will be different for Non-Operating model reporters]

#### **Other Related Party Transactions with the [Investment Advisor] [General Partner]**

The [Investment Advisor] [General Partner] occupies space in a building that is owned by the Account. The contractual lease is for a period of X years at an annual rental amount of \$xxx.

Certain employee investors affiliated with the [Investment Advisor] [General Partner] have invested alongside the Account for purposes of acquiring underlying properties. The contractual terms and requirements of the employee investors are generally consistent with all third-party investors, except employee investors are not charged investment management fees or promote.

Certain non-consolidated joint ventures have incurred property management fees of \$xxx and \$xxx to the Investment Advisor for the years ended December 31, XXCY and XXPY, respectively.

[Add more details for related party transactions where the manager allocates expenses across multiple Accounts as appropriate]

#### **9. LEASING**

At December 31, XXCY, minimum future rental payments to be received (as lessor) under non-cancelable operating leases having a term of more than one year are as follows:

**Year Ending December 31**

XXCY+1	\$ 107,270
XXCY+2	110,480
XXCY+3	113,790
XXCY+4	117,200
XXCY+5	120,720
Thereafter	<u>621,700</u>
<b>Total</b>	<b><u>\$ 1,191,160</u></b>

The above future minimum base rentals exclude residential lease agreements with terms of less than one year, which accounted for approximately xx% and xx% of the Account's annual rental income for the years ended December 31, XXCY and XXPY, respectively. Rental income for the years ended December 31, XXCY and XXPY included approximately \$xxx,xxx and \$xxx,xxx, respectively, recovered from tenants for common area expenses, other reimbursable costs, and percentage rents.

Certain properties within the Account are subject to a ground lease agreement. These ground leases have lease expiration dates that range from 20XX to 20XX, with a weighted average remaining non-cancelable term of X years across the Account. The amount of ground lease rent expense incurred during the years ended December 31, XXCY and XXPY was \$250 in both years, which is presented within real estate expenses and taxes on the accompanying consolidated statements of operations.

At December 31, XXCY, minimum future ground lease rent payments to be made (as lessee) under non-cancellable ground leases are as follows:

**Year Ending December 31**

XXCY+1	\$ 250,000
XXCY+2	250,000
XXCY+3	250,000
XXCY+4	250,000
XXCY+5	275,000
Thereafter	<u>20,625,000</u>
<b>Total</b>	<b><u>\$ 21,900,000</u></b>

**10. FINANCIAL HIGHLIGHTS — Open End, Unitized Fund Example (Required only for entities reporting as investment companies within the scope of ASC 946)** *[Inconsistencies have arisen in determining the total expense ratio for non-operating model funds and operating model funds. Non-operating model funds typically include expenses as presented on the income statement in the numerator for calculating the total expense ratio. Diversity in practice exists for operating model funds where some present the expense ratio only including fund level expenses (i.e., management fees, etc. and exclude property operating expenses) in the numerator while others present the expense ratio using expenses*

*in the numerator as they are presented on the income statement (inclusive of both fund and property level expenses, often times adjusted for amounts attributable to noncontrolling interests). Fund managers should consider whether fund level expenses only should be included in the numerator to provide for greater comparability across operating model and non-operating model funds.]*

The Account computes net assets on a quarterly [monthly] basis. An individual limited partner's total return and average net assets may differ due to the timing of contributions and redemptions. The financial highlights for the years ended December 31, XXCY and XXPY are as follows:

	December 31, XXCY	December 31, XXPY
<b>Net assets, beginning of period</b>	<b>\$ 253,356</b>	<b>\$ 322,715</b>
Income in net assets resulting from operations:		
Investment income, before management fees	50,045	46,009
Net realized and unrealized gain (loss) on investments	16,139	(5,909)
Total income from investment operations, before management fees	66,184	40,100
Management fees	1,188	950
Total income from investment operations	64,996	39,150
Net increase (decrease) resulting from capital transactions	(190)	190
<b>Net assets, end of period</b>	<b>\$ 318,162</b>	<b>\$ 253,356</b>
<b>Total return, before management fees<sup>1</sup>:</b>	<b>23.8%</b>	<b>23.5%</b>
<b>Total return, after management fees<sup>1</sup>:</b>	<b>23.4%</b>	<b>23.5%</b>
<b>Ratios to average net assets<sup>2</sup>:</b>		
Total expenses	8.1%	7.6%
Incentive allocation	0 %	%
Total expenses and incentive allocation	8.1 %	7.6 %
Net investment income	18.4%	17.2%

All amounts are shown net of amounts allocated to noncontrolling interests

<sup>1</sup>Total Return, before/ after management fees is calculated by geometrically linking quarterly returns which are calculated using the formula below:

$$\frac{\text{Investment Income before/after Management Fees} + \text{Net Realized and Unrealized Gains/Losses}}{\text{Beg. Net Asset Value} + \text{Time Weighted Contributions} - \text{Time Weighted Distributions}}$$

<sup>2</sup> Average net assets are based on beginning of quarter net assets.

**FINANCIAL HIGHLIGHTS Closed End, Finite-lived, Non-unitized Fund Example (Required only for entities reporting as investment companies within the scope of ASC 946)**

The Account computes net assets on a quarterly [monthly] basis. The financial highlights for the years ended December 31, XXCY and XXPY are as follows:

	December 31, XXCY	December 31, XXPY
<b>Total return:</b>		
Beginning of year - Internal rate of return <sup>1</sup>	14.0 %	12.5 %
End of year - Internal rate of return <sup>1</sup>	15.0 %	14.0 %
<b>Ratios/supplemental data:</b>		
Net assets, end of period	\$ 318,162	\$ 253,356
<b>Ratios to average net assets<sup>2</sup>:</b>		
Total expenses	8.1 %	7.9 %
Incentive allocation	0.0 %	%
Total expenses and incentive allocation	8.1 %	7.9 %
Net investment income	18.4 %	17.5 %
Ratio of total contributed capital to committed capital	90 %	89 %

<sup>1</sup> Total return is calculated based on a dollar-weighted internal rate of return methodology net of fees and incentive allocations. Internal rate of return is computed on a cumulative, since inception basis using annual compounding and the actual dates of cash inflows received by and outflows paid to limited partners and including ending net asset value as of each measurement date.

<sup>2</sup> Average net assets are calculated based on an average of beginning quarterly net assets.

## 11. COMMITMENTS AND CONTINGENCIES

ASC 460, *Guarantees* ("ASC 460"), specifies the accounting for and disclosures to be made regarding obligations under certain guarantees.

The Account may issue loan guarantees to obtain financing agreements and/or preferred terms related to its investments. These guarantees include mortgage and construction loans and may cover payments of principal and/or interest. These guarantees have fixed termination dates and become liabilities of the Account in the event the borrower is unable to meet the obligations specified in the guarantee agreement. The Account may also be liable under certain of these guarantees in the event of fraud, misappropriation, environmental liabilities, and certain other matters involving the borrower.

The Account is a guarantor of the following outstanding recourse obligations:

Real Estate Investment	Expiration Date	Maximum Obligation	Fair Value of Guarantee Liability <sup>1</sup>
Apartment 1	6/30/XXXX	\$ 1,140	\$ 2,900

<sup>1</sup> The fair value of guarantees are included in other liabilities on the balance sheet with a corresponding adjustment to the cost basis of the related investment.

In the normal course of business, the Account enters into other contracts that contain a variety of representations and warranties and which provide general indemnifications. The Account's maximum exposure under these arrangements is unknown, as this would involve future claims that may be made against the Account that have not yet occurred. However, based on experience, management expects the risk of loss to be remote.

As of December 31, XXCY, the Account had the following contractual commitments to purchase real estate or fund additional expenditures on previously acquired properties, which are expected to be funded in XXCY+1:

Property Type	Commitment
Apartment	\$ 1,550
Retail	5,200
Office	3,900
Industrial	2,050
Loan	<u>8,300</u>
 Total	 <u>\$ 21,000</u>

Certain purchases of real estate are contingent on a developer building the real estate according to plans and specifications outlined in the pre-sale agreement and other conditions precedent. It is anticipated that funding will be provided by operating cash flow, real estate sales, deposits from clients and Account's line of credit.

The Account purchased various real estate investments during XXCY that include earn-out provisions. An amount of \$xxx,xxx has been accrued as of December 31, XXCY and is included in accrued real estate expenses and taxes on the consolidated statements of net assets.

There were various legal actions relating to the properties in the Account in the ordinary course of business. In the opinion of the Account's management, the outcome of such matters will not have a material effect on the Account's financial condition or results of operations.

## 12. FORWARD COMMITMENTS

On October 3, XXCY, the Account entered into a forward purchase agreement with ABC, LLC (Seller) to purchase upon the construction completion of a 200,000 square foot office building located in Miami, Florida.

The purchase price for the property shall be \$xx million subject to adjustments per the purchase and sale agreement. As of December 31, XXCY, the Account made a total of \$X million escrow deposit, which is included in prepaid expenses and other assets in the accompanying combined statements of net assets.

### **13. SUBSEQUENT EVENTS**

The Account has evaluated events subsequent through XXXX X, XXCY+1

\* \* \* \* \*

## Appendix 2:

### Illustrative financial statements for Non-operating Model

The accompanying financial statements are illustrative only and provide a general format for annual financial statement prepared on a fair value basis of accounting using the Non-operating Model. While the illustrative statements in this appendix reflect a financial statement presentation commonly used by investment companies, diversity in practice has evolved over time in which non-pension real estate funds meeting the criteria of an investment companies may elect to apply certain presentation or disclosure attributes of the Operating Model (e.g. gross financial statement presentation). Disclosures included in the illustrative financial statements are not intended to be comprehensive and are not intended to establish preferences amongst alternative disclosures.

Note: The accompanying financial statement example is presented on a comparative basis; however, some entities may utilize a single year presentation within their financial statements.

# XYZ Real Estate Fund, LP

Financial Statements for the Years Ended December 31, XXCY and XXPY

## XYZ REAL ESTATE FUND, LP

STATEMENTS OF NET ASSETS  
AS OF DECEMBER 31, XXCY AND XXPY (in thousands)

	XXCY	XXPY
<b>Assets:</b>		
Real estate investments - at fair value (cost of \$XXX and \$XXX, respectively)	\$ 325,687	\$ 253,586
Cash and cash equivalents	12,450	9,255
Other assets	160	125
<b>Total assets</b>	<b>338,297</b>	<b>262,966</b>
<b>Liabilities:</b>		
Fund level notes payable - at fair value (cost of \$XXX and \$XXX, respectively)	19,500	9,030
Other liabilities	375	330
Accrued incentive fees	260	250
<b>Total liabilities</b>	<b>20,135</b>	<b>9,610</b>
<b>Net assets</b>	<b>\$ 318,162</b>	<b>\$ 253,356</b>

See accompanying notes to the financial statements

For illustrative purposes only - Non-operating model financial statements

\* - This presentation assumes the manager is eligible for an incentive fee that would be reflected on statement of net assets and statement of operations. Alternatively, if the manager, GP or affiliate was a member of the JV and eligible for a promote distribution then the presentation on the statement of changes in net assets would be appropriate.

XYZ REAL ESTATE FUND, LP

## SCHEDULES OF INVESTMENTS

FOR THE YEARS ENDED DECEMBER 31, XXCY AND XXPY (in thousands)

Investment	City, State	Acquisition Date	Square Feet Unless Otherwise Indicated (Unaudited)	December 31, XXCY		December 31, XXPY	
				Cost	Fair Value	Cost	Fair Value
Real estate owned and joint ventures							
Apartment							
Apt 1 Legal Entity Name	City, State	1/1/XXXX	xxx units	\$ 24,800	\$ 44,850	\$ 24,500	\$ 39,725
Apt 2 Legal Entity Name	City, State	1/1/XXXX	xxx units	6,860	37,460	6,660	37,284
Total apartment		25.87% of NAV as of 12/31/CY		31,660	82,310	31,160	77,009
Hotel							
Hotel 1 Legal Entity Name	City, State	1/1/XXXX	xxx rooms	12,950	44,522	10,950	39,863
Total hotel		13.99% of NAV as of 12/31/CY		12,950	44,522	10,950	39,863
Industrial							
Industrial 1 Legal Entity Name	City, State	1/1/XXXX	xx	1,930	21,060	1,760	12,139
Total industrial		6.62% of NAV as of CY		1,930	21,060	1,760	12,139
Retail							
Retail 1 Legal Entity Name	City, State	1/1/XXXX	xx	8,700	26,270	5,130	21,075
Total retail		8.26% of NAV as of 12/31/CY		8,700	26,270	5,130	21,075
Other investments							
Other 1 Legal Entity Name	City, State	1/1/XXXX	N/A	12,500	27,500	12,400	10,200
Total other investments		8.64% of NAV as of CY		12,500	27,500	12,400	10,200
Office							
Office 1 Legal Entity Name	City, State	1/1/XXXX	xx	34,350	46,700	31,100	27,400
Total office		14.68% of NAV as of CY		34,350	46,700	31,100	27,400
<b>Total real estate owned and joint ventures</b>				<b>102,090</b>	<b>248,362</b>	<b>92,500</b>	<b>187,686</b>
Mortgage and other loans receivable							
Loan 1 Legal Entity Name	City, State	1/1/XXXX	N/A	5,400	5,775	5,350	5,600
Loan 2 Legal Entity Name	City, State	1/1/XXXX	xx	5,800	6,325	5,800	6,200
<b>Total mortgage and other loans receivable</b>		3.8% of NAV as of CY		<b>11,200</b>	<b>12,100</b>	<b>11,150</b>	<b>11,800</b>
Marketable securities							
Marketable Securities Legal Entity Name	City, State	1/1/XXXX	N/A	61,650	65,225	52,700	54,100
<b>Total marketable securities</b>		20.5% of NAV as of CY		<b>61,650</b>	<b>65,225</b>	<b>52,700</b>	<b>54,100</b>
<b>Total real estate investments</b>				<b>\$ 174,940</b>	<b>\$ 325,687</b>	<b>\$ 156,350</b>	<b>\$ 253,586</b>

See accompanying notes to the financial statements

For illustrative purposes only - Non-operating model financial statements

Note: GAAP requirement is to only disclose assets that are greater than 5% of NAV but funds may elect to disclose all assets

## XYZ REAL ESTATE FUND, LP

**STATEMENTS OF OPERATIONS**  
**FOR THE YEARS ENDED DECEMBER 31, XXCY AND XXPY (in thousands)**

	<b>XXCY</b>	<b>XXPY</b>
<b>Income</b>		
Income distributions from real estate equity investments	\$ 43,417	\$ 39,909
Interest income from real estate debt investments	8,300	7,800
Other	-	120
<b>Total income</b>	<b>51,717</b>	<b>47,829</b>
<b>Expenses</b>		
Interest expense	425	395
Administrative expenses	1,185	1,375
Investment management fees	1,250	1,000
<b>Total expenses</b>	<b>2,860</b>	<b>2,770</b>
<b>Net investment income</b>	<b>48,857</b>	<b>45,059</b>
<b>Net realized and unrealized gain (loss):</b>		
Realized gain from sales of real estate investments	-	760
Less: previously recorded unrealized gain on sales of real estate investments	-	(475)
Net realized and unrealized gain from the sale of real estate investments	-	285
Unrealized gain (loss) on real estate investments held at year end	16,149	(6,194)
Unrealized incentive fees	(10)	-
<b>Net realized and unrealized gain (loss)</b>	<b>16,139</b>	<b>(5,909)</b>
<b>Increase in net assets resulting from operations</b>	<b>\$ 64,996</b>	<b>\$ 39,150</b>

See accompanying notes to the financial statements

*For illustrative purposes only - Non-operating model financial statements*

\* - This presentation assumes the manager is eligible for an incentive fee that would be reflected on statement of net assets and statement of operations. Alternatively, if the manager, GP or affiliate was a member of the JV and eligible for a promote distribution then the presentation on the statement of changes in net assets would be appropriate.

## XYZ REAL ESTATE FUND, LP

STATEMENTS OF CHANGES IN NET ASSETS  
FOR THE YEARS ENDED DECEMBER 31, XXCY AND XXPY (in thousands)

	General Partner	Limited Partners	Total
<b>Net assets - December 31, XXPY-1</b>	\$ -	\$ 214,016	\$ 214,016
Increase in net assets resulting from operations	-	39,150	39,150
Contributions	-	570	570
Distributions	-	(380)	(380)
<b>Net assets - December 31, XXPY</b>	-	<b>253,356</b>	<b>253,356</b>
Increase in net assets resulting from operations	-	64,996	64,996
Contributions	-	285	285
Distributions	-	(475)	(475)
<b>Net assets - December 31, XXCY</b>	<b>\$ -</b>	<b>\$ 318,162</b>	<b>\$ 318,162</b>

See accompanying notes to the financial statements

*For illustrative purposes only - Non-operating model financial statements*

\* - This presentation assumes the manager is eligible for an incentive fee that would be reflected on statement of net assets and statement of operations. Alternatively, if the manager, GP or affiliate was a member of the JV and eligible for a promote distribution then the presentation on the statement of changes in net assets would be appropriate.

## XYZ REAL ESTATE FUND, LP

STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED DECEMBER 31, XXCY AND XXPY (in thousands)

	XXCY	XXPY
<b>Cash flows from operating activities:</b>		
Increase in net assets resulting from operations	\$ 64,996	\$ 39,150
Adjustments to reconcile increase in net assets resulting from operations to net cash flows provided by (used in) operating activities:		
Net realized and unrealized (gain) loss	(16,139)	5,909
Change in other assets	(35)	200
Change in other liabilities	45	50
Change in accrued incentive fee	10	1,005
Return of capital distributions from real estate investments	-	-
Funding of real estate investments	(55,962)	(40,168)
Proceeds from real estate investments sold	-	760
<b>Net cash flow provided by (used in) operating activities</b>	<b>(7,085)</b>	<b>6,906</b>
<b>Cash flows from financing activities:</b>		
Proceeds from loans payable	10,470	-
Distributions	(475)	(380)
Contributions	285	570
<b>Net cash flow provided by financing activities</b>	<b>10,280</b>	<b>190</b>
<b>Net change in cash and cash equivalents</b>	<b>3,195</b>	<b>7,096</b>
Cash and cash equivalents — Beginning of year	9,255	2,159
<b>Cash and cash equivalents — End of year</b>	<b>\$ 12,450</b>	<b>\$ 9,255</b>
<b>Supplemental cash flow information:</b>		
Cash paid for interest on loans payable	\$ 425	\$ 395
Cash paid for income taxes	12	10

See accompanying notes to the financial statements

For illustrative purposes only - Non-operating model financial statements

**XYZ REAL ESTATE FUND LP****NOTES TO FINANCIAL STATEMENTS  
FOR THE YEARS ENDED DECEMBER 31, XXCY AND XXPY****1. ORGANIZATION**

XYZ Real Estate Fund LP (the "Fund") was formed on January 1, XXXX for the purpose of generating income and appreciation on real estate investments in the United States of America. The investment advisor of the Fund is ABC Real Estate Advisors, L.P. ("ABC" or the "Advisor"). The aggregate committed capital for the Fund is \$200 million. The limited partners committed \$190 million and the general partner committed \$10 million. The terms of the partnership agreement do not generally provide for new subscription or redemption of partners' interests. The general partner of the Fund is ABC, L.P., an affiliate of the Advisor. At December 31, XXCY, the ratio of total contributed capital to committed capital was 90%.

The Fund is an investment company as described in Accounting Standards Codification ("ASC") 946, *Financial Services – Investment Companies*.

*See standard disclosures in the Operating model illustrative financial statements. Disclosures unique to the Non-operating model are provided below.*

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Basis of presentation** — *See Operating Model illustrative financial statements.*

**Use of estimates** — *See Operating Model illustrative financial statements.*

**Real estate investments** — Investments in real estate are carried at fair value. Cost to acquire real estate investments are capitalized as a component of investment cost. In certain investment arrangements, the Fund's equity percentage interest in the investment may be reduced by third party residual interests for returns realized in excess of specific hurdle rates of return. Such residual interests have been considered in the related investment valuation.

**Investments in mortgage and other notes receivables** — *See Operating Model illustrative financial statements.*

**Investment valuation** — The fair values of real estate investments are estimated based on the price that would be received to sell an asset in an orderly transaction between marketplace participants at the measurement date. Investments without a public market are valued based on assumptions made and valuation techniques used by the Advisor. Such valuation techniques include discounted cash flow analysis, prevailing market capitalization rates or earnings multiples applied to earnings from the investment, analysis of recent comparable sales transactions, actual sale negotiations and bona fide purchase offers received from third parties, consideration of the amount that currently would be required to replace the asset, as adjusted for obsolescence, as well as independent external appraisals. In general, the Advisor considers multiple

valuation techniques when measuring the fair value of an investment. However, in certain circumstances, a single valuation technique may be appropriate. The Fund's policy is to obtain independent external appraisals for investments every 12 months. Investments in publicly traded equity securities are valued based on their quoted market prices.

The fair value of real estate investments does not reflect the Fund's transaction sale costs, which may be incurred upon disposition of the real estate investments. Such costs are estimated to approximate 2% - 3% of gross property fair value. The Fund also reflects its real estate equity investments net of investment level financing. Valuation adjustments attributable to underlying financing arrangements are considered in the real estate equity valuation.

The Fund may invest in real estate and real estate related investments for which no liquid market exists. The market prices for such investments may be volatile and may not be readily ascertainable. In addition, there continues to be significant disruptions in the global capital, credit and real estate markets. These disruptions have led to, among other things, a significant decline in the volume of transaction activity, in the fair value of many real estate and real estate related investments, and a significant contraction in short-term and long-term debt and equity funding sources. This contraction in capital includes sources that the Fund may depend on to finance certain of its investments. These market developments have had a significant adverse impact on the Fund's liquidity position, results of operations and financial condition and may continue to adversely impact the Fund if market conditions continue to deteriorate. The decline in liquidity and prices of real estate and real estate related investments, as well as the availability of observable transaction data and inputs, may have made it more difficult to determine the fair value of such investments. As a result, amounts ultimately realized by the Fund from investments sold may differ from the fair values presented, and the differences could be material.

**Concentrations of credit risk** — *See Operating Model illustrative financial statements.*

**Cash and cash equivalents** — *See Operating Model illustrative financial statements.*

**Mortgage loans and fund level notes payable** — *See Operating Model illustrative financial statements.*

**Interest rate swaps and caps** — *See Operating Model illustrative financial statements.*

**Income and expense recognition** — Distributions from real estate equity investments are recognized as income when received to the extent such amounts are paid from earnings and profits of the underlying investee. Interest income on real estate debt investments is generally accrued as earned in accordance with the effective interest method. For loans in default, interest income is not accrued but is recognized when received. Expenses are recognized as incurred.

**Investment advisory fees** — *See Operating Model illustrative financial statements.*

**Income taxes** — As a partnership, the Fund itself is not subject to U.S. Federal income taxes. Accordingly, income taxes are not considered in the accompanying financial statements since such taxes, if any, are the responsibility of the individual partners. Income from non-U.S. sources may be subject to withholding and

other taxes levied by the jurisdiction in which the income is sourced. If an uncertain income tax position were to be identified, the Fund would account for such in accordance with ASC 450, *Contingencies*.

ASC Subtopic 740, *Income Taxes*, provides guidance for how uncertain tax positions should be recognized, measured, presented and disclosed in the financial statements. ASC 740 requires the evaluation of tax positions taken in the course of preparing the Fund's tax returns to determine whether tax positions are "more-likely-than-not" of being sustained by the applicable tax authority. Tax benefits of positions not deemed to meet the more-likely-than-not threshold would be recorded as a tax expense in the current year.

**Guarantees** — *See Operating Model illustrative financial statements.*

**Foreign currency** — *See Operating Model illustrative financial statements.*

**Risk management** — *See Operating Model illustrative financial statements.*

**3. Recently issued accounting standards** - *See Operating Model illustrative financial statements.*

**4. FAIR VALUE MEASUREMENTS** – *See Operating Model illustrative financial statements.*

**5. LOANS PAYABLE** — *See Operating Model illustrative financial statements.*

**6. INTEREST RATE SWAPS AND CAPS** — *See operating Model illustrative financial statements.*

**7. PORTFOLIO DIVERSIFICATION** — *See Operating Model illustrative financial statements.*

**8. RELATED PARTY FEES AND AFFILIATE TRANSACTIONS** - *See Operating Model illustrative financial statements.*

**9. FINANCIAL HIGHLIGHTS** - *See Operating Model illustrative financial statements.*

**10. COMMITMENTS AND CONTINGENCIES** - *See Operating Model illustrative financial statements.*

**11. FORWARD COMMITMENTS** - *See Operating Model illustrative financial statements.*

**12. SUBSEQUENT EVENTS** - *See Operating Model illustrative financial statements.*

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