NCREIF PREA
Reporting Standards

Handbook Volume II: Manuals

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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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. 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 non-tax-exempt investors (e.g. Funds). 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.

Where applicable guidance is not specified within authoritative GAAP, non-authoritative guidance may be applied. The appropriateness of the sources of non-authoritative GAAP 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.

1.02 Operating and Non-operating Financial Statements

1.02(a) Tax-exempt and non-tax-exempt 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 model, particularly with non-tax-exempt entities applying presentation attributes of the Operating model (i.e. a gross presentation) in their financial statements for enhanced transparency to the performance of the entity’s investments. The differences between the two models are generally related to presentation and therefore the hypothetical application of both models to the same investment will generally result in a similar net asset value of the reporting entity.

1.02(b) 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. The fundamental premise for fair value based accounting models is based on existing U.S. generally accepted accounting principles which require that certain investments held by tax-exempt investors, including defined benefit pension plans and endowments are reported at fair value. This model is supported by ASC 960 and GASB 25 and is referred to throughout the Manual as the Operating Model.

1.02(c) 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 946 *Financial Services — Investment Companies* (significant content derived from the AICPA Audit and Accounting Guide — *Audits of Investment Companies*) (the "Investment Company Guide"). This authoritative guidance supports the use of a fair value accounting model for investment companies. Some Funds use this model as their FV GAAP model for accounting and reporting. This accounting model is referred to throughout the Manual as the Non-operating Model.

1.02(d) 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 Accounting Standards Codification. Authoritative guidance takes precedent over any 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 tax-exempted 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.

Presently, some Funds use the Non-operating Model to report FV GAAP while some Funds use the Operating Model. Varying interpretations of these two models 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.

1.03 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 samples financial statements presented under the Operating Model and Non-operating Model.

1.04 Terminology

Certain terms as used herein are defined as follows:

- Fund: Includes all commingled funds and single-investor investment accounts; a Fund has one or more investments
- Investment: A discrete asset or group of assets held for income, appreciation, or both and tracked separately
- Property: A real estate asset
- Financial Accounting Standards Board: FASB
- Accounting Standards Codification: ASC
- Accounting Standards Update: ASU
- Governmental Accounting Standards Board: GASB
- American Institute of Certified Public Accountants: AICPA
- Accounting principles generally accepted in the United States of America: U.S. GAAP or GAAP.

1.05 Fair value

1.05(a) The Reporting Standards require fair value financial information for all investments, for incorporation into the Fund Report. Fair value measurements and disclosures under both the

Operating and Non-operating models are determined in accordance with ASC 820, Fair Value Measurements.

1.05(b) 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, a primary assumption of fair value accounting is that an asset and or liability reported at fair value include unrealized gains and losses that would be realized by investors in a hypothetical sales transaction at the balance sheet date.

1.06 Relevant accounting and auditing guidance

1.06(a) Relevant accounting guidance contained in authoritative FASB Accounting Standard Codification topics have been considered in the development of this edition of the Manual.

1.07 International Financial and Reporting Standards (IFRS)

1.07(a) International Financial Reporting Standards (IFRS) is a basis of accounting applied by U.S. and non-U.S. real estate funds. 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 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) to earn rentals or for capital appreciation or both.

1.07(b) IFRS defines an *investment entity* as having similar attributes to those of an investment company defined under U.S. GAAP. However, unlike U.S. GAAP 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. The cost model under IFRS is similar to the depreciated cost model under U.S. GAAP.

1.08 Disclaimers

1.08(a) 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 Accounting Standards Updates whether included or not included in this Manual to determine their effect on the preparation of financial statements

1.08(b) 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.

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 and liabilities, 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; diversity exists when determining which model is presented. The determination of the appropriate fair value reporting model 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 models.

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

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

FV NAV represents the fair value of investments owned, cash, receivables and other assets in excess of liabilities of the reporting entity. Notwithstanding different financial statement presentations that exist between the Operating Model and Non-operating Model, FV NAV reported by a reporting entity under both models is generally expected to be similar because both models require investments to be reported at fair value in accordance with ASC 820.

2.03 Non-operating Model

2.03(a) Introduction

Funds are those entities that satisfy the criteria of an Investment Company in accordance with ASC 946 as described in paragraph 1.02c and generally prepare financial statements under the Non-operating Model. However, some entities apply presentation attributes of the Operating Model within their financial statements. Financial statements prepared under the Non-operating Model report all investments at fair value on a recurring basis. Each model may report revenue recognition differently; however, FV NAV should generally be the same under both reporting models. ASU 2013-08: Financial Services - Investment Companies was issued in June 2013 and amends the scope, measurements and disclosure requirements in ASC 946. The Financial Accounting Standards Board 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 this time. The FASB did not intend for the amendments in this Update to change practice for real estate entities for which it is industry practice to issue financial statements using the measurement principles in Topic 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 ("REIT's). REITS that exhibit the attributes of an investment company within the framework of ASC 946 may be eligible to report real estate at fair value. This Manual recommends that financial statement preparers discuss the applicability of ASU 2013-08 to their financial statements with their public accounting firm.

2.03 (a1) The Non-operating Model generally utilizes a “net” presentation; however, diversity in practice exists where some Funds reporting under ASC 946 may provide an alternative presentation that will generally not result in a different FV NAV. At this time authoritative GAAP does not specifically address financial statement presentation as it relates to a real estate entity reporting at FV GAAP.

2.03(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 option that is irrevocable 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.

2.03(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. An exception to the general principle is if 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. See section 2.04(c) for additional information.

2.03(d) GAAP is silent on the topic of when it’s appropriate for an investment company to consolidate another investment company in which it holds a controlling financial interest. Diversity in practice prevails 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 thought through this issue as part of the Investment Company project.

2.03(e) Equity Method

ASU 2013-08 clarified that an investment company cannot apply the equity method 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 Operating Model

2.04(a) Introduction

2.04(a.1) The fundamental premise for fair value based accounting models is based on existing authoritative accounting standards which require that certain investments held by tax-exempt investors, including defined benefit pension plans and endowments are reported at fair value. ASC 960, *Plan Accounting — Defined Benefit Pension Plans* (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, Governmental Accounting Standards Board (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 tax-exempt investors with relevant financial information.

2.04(a.2) Entities that report under ASC 960 are required to follow ASC 810, *Consolidation*, and ASC 323, *Investments – Equity Method and Joint Ventures*. As indicated above, some entities that report under ASC 946 may elect to present their financial statements under the Operating Model. These entities may choose to apply the consolidation guidance in ASC 810. However, 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.

2.04(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 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. Further information can be found in Sections 4.04 and 4.05.

2.04(c) Consolidation: Applicability of ASC 810

2.04(c.1) ASU 2015-02 was issued in 2015 and is effective for all reporting entities. The main provisions of this ASU are:

a. Determing whether limited partnerships or similar legal entities meet the criteria of a variable interest entity

b. Evaluating if fees paid to a decision maker or service provider (e.g. an asset manager or investment advisor) are deemed variable interests

c. The effect of a fee arrangement (see b) on the primary beneficiary determination

d. Application of the related party tiebreaker test when determining the primary beneficiary

e. Application of ASC 810 to series funds (e.g. registered investment companies).

2.04(c.2) Both investors and service providers are required to assess consolidation under ASC 810.

2.04(c.3) Under the Operating Model real estate investments include direct investments in real estate, as well as holdings of controlling equity interests in separate legal entities, which invest in real estate assets. The Fund manager should consider existing authoritative guidance to determine whether an investment in an investee (e.g., joint venture) is controlling or not in accordance with ASC 810. In a historical cost reporting environment, GAAP generally requires an investor to initially determine whether the investee is a variable interest entity under ASC 810-10. =

2.04(d) Consolidation: Accounting

2.04(d.1) Entities that report under ASC 960 are required to follow ASC 810, *Consolidation.* While in general the ownership of a greater than 50% voting interest in an investment is considered to be an indication of control, many joint venture real estate investments contain complex governance arrangements that make assessments of control difficult. All factors must be considered in making a determination of whether consolidation of an investee is appropriate. If investments in entities are not deemed to be controlling interests then the equity method of accounting should be followed if the “significant influence” criterion is met in accordance with ASC 323, *Investments — Equity Method and Joint Ventures*.

2.04(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 balance sheet 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 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 of ASC 360-20, *Real Estate Sales*, and ASC 976, *Real Estate-Retail Land.* Gains, which are deferred in accordance with ASC 360-20, continue to be reported as unrealized. ASU 2014-09 *(ASC 606 - Revenue from Contracts with Customers*) was issued in May 2014 and is effective for public entities for annual reporting periods beginning after December 15, 2017, including interim periods within those reporting periods. For all other entities, the amendments are effective for annual reporting periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 15, 2019. Subtopic 610-20 *Other Income – Gains and Losses from Derecognition of Nonfinancial Assets* was issued as part of ASU 2014-09, the subtopic provides guidance for recognizing gains and losses from the transfer of nonfinancial assets in contracts with noncustomers (i.e. Real estate sales), as a result, the guidance specific to real estate sales in ASC 360-20 will be eliminated. As such, sales and partial sales of real estate assets will be subject to the same derecognition model as all other nonfinancial assets. The new guidance will also impact the accounting for partial sales of nonfinancial assets (including in substance real estate).

2.04(d.3) The consolidation process required by ASC 810 includes that the noncontrolling interest continues to be attributed its share of losses even if that attribution 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. An entity should perform an assessment of their noncontrolling interests’ rights and consider whether the noncontrolling interest is a redeemable equity security within the scope of ASC 505-10-50. The disclosures in ASU 2013-08 are required to be provided (See Appendix 1).

2.04(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.

2.04(d.5) In the footnotes, ASU 2013-08 also requires a separate schedule to be provided 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).

2.04(d.6) The financial statements should include the disclosures required by ASU 2013-08.

2.04(e) Equity Method Accounting

Noncontrolling 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 income or loss, determined in accordance with GAAP on the fair value basis of accounting (exclusive of items such as depreciation, amortization and free rent, as appropriate). ASC 970-323-35-17 suggests that stipulated 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.

2.05 Capital / Equity Transactions

2.05(a) Subscriptions/Contributions

Investment partnerships shall record capital subscription and redemption commitments as of the date required by the partnership agreement. Cash received before this date shall be recorded as an advance capital contribution liability.

2.05(b) Dividends

Both closed-end and open-end investment companies record distribution liabilities on the ex-dividend date rather than the declaration date. 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.

2.06 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. In preparing financial statements of real estate entities, tax positions to be reviewed and analyzed may include the following:

- Tax Exempt Entity Status
- REIT Status
- State 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 models (i.e., Operating Model or the Non-operating Model). The following are items that are generally applicable to both fair value models.

3.01(b) See the Property Level Accounting in Section 4 for information relating to realized and unrealized gains and losses.

3.01(c) The underlying real estate assets of a Fund 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.

3.01(d) 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 secured by a lien on real estate 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 also secured by a lien on real estate that generally consists of three parts: (1) ”base interest” payments at contractually stated fixed or floating rates; (2) ”contingent interest” payments where the lender is paid a percentage of property net operating income or cash flow after debt service; and (3) ”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 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) See ASC 310-40, *Receivables — Troubled Debt Restructurings by Creditors*, for guidance on troubled debt restructurings, foreclosures, and receipt of assets in full satisfaction of receivables.

3.03 Accounting for non-participating mortgage loans receivable

3.03(a) Non-participating mortgage loans receivable should be carried on the balance sheet 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. The ability to recognize a sale of a mortgage loan is governed by the guidance for financial assets provided in ASC 860, *Transfers and Servicing*.

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) 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(d) 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, 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.

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.

3.03(e) 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(f) Modification of mortgage terms should be accounted for through an adjustment of value and recorded through the unrealized gain/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 guidance in ASC 815-15-55, 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 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 balance sheet 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. These gains or losses are realized upon the disposal of an investment. The ability to recognize a sale of a mortgage loan is governed by the guidance provided in ASC 860.

3.04(c) The initial cost basis of a participating mortgage loan should include all direct costs of making the loan consistent with ASC 310-20. However, the entity's management needs to assess the fair value of the loan under ASC 820 or if an unrealized loss should be recognized on day one of holding 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.

3.04(d) 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 impaired 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(e) 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 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(f) Modification of mortgage terms should be accounted for through an adjustment of value and recorded through the unrealized gain/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 general partner in the venture who is a real estate developer/operator in the specific project type. In consideration for the cash investment that is disproportionate to its stipulated ownership interest, the institutional partner is generally entitled to a preferential distribution of cash flow equal to a preferred return on the capital invested and interest on loans, and to a priority return of its capital investment from a sale or refinancing. Amounts generated by the joint venture in excess of these preferences and priorities are distributed to the participants in accordance with the sharing ratios stipulated in the joint venture agreement.

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 model utilized. See Section 2, Fund Level Accounting, in this Manual for a discussion of the appropriate accounting models 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 distributions of net investment income, or dividends. 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. Management should assess if such costs are a component of the investment's reported fair value under ASC 820, or should be reported as an unrealized loss upon acquisition. 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.

3.06(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 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 balance sheet as a single caption, "Investment in Joint Venture."

3.06(f) ASC 230-10-45, requires dividends received (returns on investments) to be classified as cash inflows from operating activities. Cash receipts that represent returns of investments are classified as cash inflows from investing activities.

3.06(g) The investment in a joint venture is then subsequently adjusted to include the changes in fair value as measured in accordance with ASC 820. 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 investment account. The aggregate investment should be presented on the schedule of investments as a single investment.

3.06(h) The determination of the fair value of an investment in a joint venture may require: (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(i) Amendments to ASC 820 included in ASU No. 2009-12 permit, 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.

3.06(j) In May 2015, the FASB issued ASU No. 2015-07, *Disclosures for Investments in Certain Entities That Calculate Net Assets Value per Share (or Its Equivalent)*. This ASU removes the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value per share as a practical expedient. This ASU also removes the requirement to make certain disclosures for all investments that are eligible to be measured at fair value using the net asset value per share practical expedient. Rather, those disclosures are limited to investments for which the entity has elected to measure the fair value using the practical expedient. For public business entities, this guidance is effective for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. For all other entities, the guidance is effective for fiscal years beginning after December 15, 2016, and interim periods within fiscal years. Early adoption is permitted.

3.07 Accounting for contingencies

3.07(a) For all acquisitions one 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.

3.07(b) For all other contingencies (referred to as noncontractual contingencies), the acquirer shall assess, as of the acquisition date, whether it is more likely than not that the contingency gives rise to an asset or a liability. If that criterion is met as of the acquisition date, the asset or liability arising from a noncontractual contingency shall be recognized at that date, measured at its acquisition-date fair value. If that criterion is not met as of the acquisition date, the acquirer shall not recognize an asset or a liability at that date. The acquirer shall instead account for a noncontractual contingency that does not meet the more-likely-than-not criterion as of the acquisition date in accordance with other GAAP, including ASC 450 *Contingencies*, as appropriate.

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

3.08 Accounting for forward purchase commitments

3.08(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) 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 3.08(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.

3.09 Accounting for financing costs

3.09(a) Costs may be incurred in connection with obtaining financing for the Fund or the investment — either secured or unsecured. 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". 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). In order to remain comparable to other institutional investment classes, it is recommended that, subsequent to the adoption of the Fair Value Option under ASC 825-10, related financial costs are not deferred and continue to be fully expensed as a component of net investment income. 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 3.09(b)).

3.09(b) ASU 2015-03 amended ASC 835-30 to require that unamortized financing costs be presented as a reduction of the carrying amount of the related debt balance on the statement of assets and liabilities, 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. For public business entities, this guidance is effective for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. For all other entities, the guidance is effective for fiscal years beginning after December 15, 2015, and interim periods within fiscal years beginning after December 15, 2016. Early adoption of ASU 2015-03 is permitted for financial statements that have not been previously been issued, and it should be applied retrospectively.

3.09(c) ASU 2015-15 added SEC paragraphs 835-30-S35-1 and 835-30-S45-1 related 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.

3.10 Investment Advisory fees

3.10(a) General

Real estate advisory fees may include acquisition, asset management, disposition, financing, and incentive fees.

3.10(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 or pension plan is making 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 support related acquisition costs (see 4.02b).

Upon acquisition of a property the related acquisition costs are typically capitalized (i.e. included in the cost basis) along with the purchase price. Because these costs are not a component of fair value, the property's initial recorded value must be adjusted to reflect the property's true fair value. If there are no other valuation changes, the resulting effect would be an unrealized loss.

Origination Fees generally compensate an advisor for their services rendered for originating a mortgage note receivable and are included in the initial cost basis. Because these costs are not a component of fair value, the mortgage note receivable's initial recorded value must be adjusted to reflect the mortgage note receivable's true fair value. If there are no other valuation changes, the resulting effect would be an unrealized loss.

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 considered transaction costs and are recorded as a reduction in earnings incurred in the statement of operations. (See 4.05(a)).

3.10(c) Asset management fees

Asset management fees are generally expensed in the current period and reported as a component of net investment income.

3.10(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. Disposition fees that are substantively incentive fees should be measured and recognized as incentive fees.

3.10(e) Incentive fees and Promote reallocations

3.10(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.

3.10(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 balance sheet date. 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.

3.10(e.3) The related impact of recording a liability for an incentive fee should be either (1) reflected as a component of the investment's net investment income, if the fee resulted from operating results; or (2) reflected as a component of the investment's unrealized gain/loss, if the fee resulted from changes in fair value.

3.10(e.4) Where incentive fees are based on both operating results and changes in fair value, the related impact should be allocated to the applicable components based on the substance of the incentive fee arrangements.

3.10(e.5) Promote reallocations that would be due to a general partner or managing member in the manner described in 3.10(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.

3.10(f) Related parties and Affiliate transactions

3.10(f.1) Per the AICPA Audit & Accounting Guide for Investment Companies 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.

3.10(f.2) 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 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.

3.10(f.3) ASC 850 also state that transaction 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 providing accounting or measurement guidance for such transactions, their disclosure is required nonetheless.

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 wholly owned 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 balance sheet 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 models, 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 models does not include the effect of rent normalization (i.e. straight-line rent) under ASC 840-20-25, 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. 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. 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. Such 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 Level 3 input.

All disclosures indicated below are required by public entities. Private entities are required to disclose only items (1), (3), (6), and (7):

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. All transfers between Level 1 and Level 2 fair value measurements on a gross basis, including the reasons for those transfers;
6. In addition to the existing disclosures for the transfers in and out of Level 3, the related policy supporting such transfers.
7. For recurring and nonrecurring fair value measurements categorized within Level 3, a description of the valuation process used by the reporting entity.

The Financial Accounting Standards Board released ASU 2016-19 which clarified the meaning of the terms "valuation technique" and "valuation approach" as used in fair value literature. It also amended a related disclosure requirement, which is effective the first quarter of 2017 for most companies. The new guidance indicates that valuation techniques are more granular than valuation approaches, and explains that valuation techniques are used consistent with a particular approach. Along with clarifying the terms, the technical correction amended the disclosure requirement pertaining to changes in valuation technique or approach. Companies are now 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 in accordance with other guidance. 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 balance sheet at their initial fair value.

4.02(h) 4.02(i)

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. 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 Model for the presentation of 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. These capital items are generally made 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 the tenant 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.

4.03(e)

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 using 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 option that is irrevocable to measure financial instruments at fair value on an instrument-by-instrument basis.

4.04(c) Subsequent to the initial adoption, 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 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 of 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. ASU 2011-04 (See 4.02d) clarified that 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). These concepts are consistent with current fair value measurement practices and are not expected to result in material changes to a reporting entity's valuation methodologies. 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(e) If the Fair Value Option is not chosen for loans payable, the guidance as described in ASU 2015-03 should be followed.

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. Transaction costs refer to the incremental direct costs to transact in the principal (or most advantageous) market for the liability. Subsequent to the election of The Fair Value Option under ASC 825-10, transactions costs should be expensed as incurred.

4.05(b) 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. Any transaction costs associated with obtaining the contracts should be recognized in earnings as incurred and not deferred.

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 balance sheet 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 which are longer-term in nature (i.e., expected to be settled greater than one year from the date of the financial statements) should be reported at their fair value. These other assets and liabilities should be recorded in accordance with standards promulgated in ASC 820. If there is an active market with quoted market prices for other assets and liabilities held, this information should be used in determining fair value. In the absence of quoted market prices, fair values should be determined using a discounted cash flow analysis as long as such values approximate the amount that would be received or paid in a current transaction. The amounts and timing of the cash inflows and outflows associated with other assets and liabilities must be estimated and discounted back to a present value. The discount rate used should reflect a current market rate commensurate with the risks of the specific asset (i.e., risk-free interest rate plus applicable credit spread, or the current market rates applicable to liabilities of similar duration or risk).

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.

4.08 Receivables

4.08(a) Various operating transactions may result in notes or accounts receivable. These receivables may be short-term or long-term in nature.

4.08(b) The undiscounted carrying value of short-term receivables (e.g., less than one year to maturity) 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. An allowance should be established based upon the amount of the receivable expected to be uncollectible. Any such allowance is charged against net investment income; however, industry practice varies as to whether the allowance is charged against revenue or as an operating expense. Generally, allowances related to bad debts should be recorded as an operating expense. 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. An allowance should be established based upon the present value of the ultimate amount to be uncollectible. Consideration should be given to any underlying collateral.

4.09 Other liabilities

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.

4.10 Real estate revenues and expenses

4.10(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.

4.10(b) When reporting property specific information, or when utilizing such 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).

4.10(c) 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 his right to use the space; the owner has no further obligation to provide services; and when payment is determined to be probable.

4.10(d) Real estate expenses should be recognized when incurred. Companies should consider authoritative accounting literature such as ASC 605-45, *Principal Agent*, for recording of revenues and expenses gross or net.

4.11 Realized and unrealized gains and losses

4.11(a) The periodic valuation of real property, real estate investments, and Funds and other non-current assets and liabilities, pursuant to the fair value basis of accounting, results in changes in the reported value of investments and 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 transaction or the settlement of liabilities; however, sales transactions must also meet the gain recognition criteria set forth in ASC 360-20 and ASC 976. Gains that are deferred in accordance with ASC 360-20 continue to be reported as unrealized. ASU 2014-09 *(ASC 606 - Revenue from Contracts with Customers*) was issued in May 2014 and is effective for public entities for annual reporting periods beginning after December 15, 2017, including interim periods within those reporting periods. For all other entities, the amendments are effective for annual reporting periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 15, 2019. Subtopic 610-20 *Other Income – Gains and Losses from Derecognition of Nonfinancial Assets* was issued as part of ASU 2014-09, the subtopic provides guidance for recognizing gains and losses from the transfer of nonfinancial assets in contracts with noncustomers (i.e. Real estate sales), as a result, the guidance specific to real estate sales in ASC 360-20 will be eliminated. As such, sales and partial sales of real estate assets will be subject to the same derecognition model as all other nonfinancial assets. The new guidance will also impact the accounting for partial sales of nonfinancial assets (including in substance real estate).

4.11(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.

4.11 (c) The distinctions between realized and unrealized recognition is 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.

4.11(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.

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. While the illustrative statements in this appendix reflect a financial statement presentation commonly used by pension funds or other tax-exempt entities, diversity in practice has evolved over time in which non-pension real estate funds meeting the criteria of an investment company 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 among alternative disclosures.

Revenue Recognition Standard

In May 2014, the FASB issued Accounting Standards Update ("ASU") 2014-09 *Revenues from Contracts with Customers* (Topic 606). The standard's core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. In doing so, companies will need to use more judgment and make more estimates than under today's guidance. These may include identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation. The standard is effective for fiscal years beginning after December 15, 2018 for public companies and December 15, 2019 for private companies. Additionally, during 2016, the FASB issued ASU 2016-08 Revenue from Contracts with Customers, Principal versus Agent Considerations, ASU 2016-10 Revenue from Contracts with Customers, Identifying Performance Obligations and Licensing and ASU 2016-12 Revenue from Contracts with Customers, Narrow-Scope Improvements and Practical Expedients, which clarify the guidance on reporting revenue as a principal versus agent, identifying performance obligations, accounting for intellectual property licenses, and how to assess collectability, present sales tax and treat noncash consideration. Fund managers should evaluate the impact of the guidance on their financial statements in consultation with their external auditors and other advisors.

Leasing Standard

In February 2016, the FASB issued ASU 2016-02, *Leases*. This standard amends the existing accounting standards for lease accounting, including requiring lessees to recognize most leases on their balance sheets and making targeted changes to lessor accounting. The standard is effective for fiscal years beginning after December 15, 2018 for public companies and December 15, 2019 for private companies. Early adoption is permitted. The new leases standard requires a modified retrospective transition approach for all leases existing at, or entered into after, the date of initial application, with an option to use certain transition relief. Fund managers should evaluate the impact of the guidance on 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
Assets:		
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 plus equity in undistributed		
earnings: $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
Other real estate investments (cost of $18,550 and $14,200, respectively)	22,125	15,600
Total real estate investments	227,075	195,500
Cash and cash equivalents	90,635	59,255
Marketable securities - at fair value (cost of $43,100 and $38,500, respectively)	43,100	38,500
Accrued investment income (net of allowance for doubtful accounts of $580 and $500)	18,620	16,200
Prepaid and other assets, net	42,000	29,200
Total assets	**421,430**	**338,655**
Liabilities:		
Mortgage loans and notes payable - at fair value	77,220	64,870
(cost of $80,760 and $70,290, respectively)		
Accrued real estate expenses and taxes	1,350	1,330
Accrued incentive fees	260	250
Other liabilities	2,900	2,055
Total liabilities	**81,730**	**68,505**
Net assets:		
XYZ Real Estate Account net assets	318,162	253,356
Noncontrolling interests	21,538	16,794
Net assets	**$ 339,700**	**$ 270,150**

See accompanying notes to the consolidated financial statements.
For illustrative purposes only - 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
Investment income:		
Revenue from real estate investments	$ 32,150	$ 31,750
Equity in income of unconsolidated real estate joint ventures	21,450	20,500
Interest and equity income on mortgage and other loans receivable	8,300	7,800
Income from other real estate investments	7,100	6,900
Other income	4,600	4,100
Total investment income	**73,600**	**71,050**
Expenses:		
Real estate expenses and taxes	12,250	12,100
Interest expense	3,600	3,250
Administrative expenses	5,400	5,100
Investment management fees	1,250	1,000
Total expenses	**22,500**	**21,450**
Net investment income	**51,100**	**49,600**
Net realized and unrealized gain (loss):		
Realized gain from sales of real estate investments	1,100	800
Less: previously recorded unrealized (gain) loss 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 other real estate investments	2,175	1,500
Unrealized (loss) gain on mortgage loans and notes payable	(1,880)	1,000
Net realized and unrealized gain (loss)	**18,650**	**(6,220)**
Increase in net assets resulting from operations	**69,750**	**43,380**
Less: Portion attributable to noncontrolling interests	(4,754)	(4,230)
Increase in net assets resulting from operations	**$ 64,996**	**$ 39,150**

Amounts attributable to XYZ Real Estate Account

	XXCY	XXPY
Net investment income	$ 48,847	$ 45,059
Net realized and unrealized gain (loss)	16,149	(5,909)
Increase in net assets resulting from operations attributable to XYZ Real Estate Account	**$ 64,996**	**$ 39,150**

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

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
Net assets - December 31, XXPY-1	**$ 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)
Increase in net assets resulting from capital transactions	190	10	200
Increase in net assets	39,340	4,240	43,580
Net assets - December 31, XXPY	**253,356**	**16,794**	**270,150**
From operations:			
Net investment income	48,847	2,253	51,100
Net realized and unrealized gain	16,149	2,501	18,650
Increase in net assets resulting from operations	64,996	4,754	69,750
From capital transactions:			
Contributions	285	15	300
Distributions	(475)	(25)	(500)
Increase in net assets resulting from capital transactions	(190)	(10)	(200)
Increase in net assets	64,806	4,744	69,550
Net assets - December 31, XXCY	**$ 318,162**	**$ 21,538**	**$ 339,700**

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

XYZ REAL ESTATE ACCOUNT

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

	XXCY	XXPY
Cash flows from operating activities:		
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 (gains) loss	(18,650)	6,220
Amortization	250	250
Bad debt	80	
Equity in income of unconsolidated real estate joint ventures	(21,450)	(20,500)
Income distributions from unconsolidated real estate joint ventures	18,100	14,550
Changes in other assets and liabilities:		
Accrued investment income	(2,500)	3,050
Prepaid and other assets	(13,050)	(1,800)
Accrued real estate expenses and taxes	20	(55)
Accrued incentive fees	10	5
Other liabilities	845	(110)
Net cash flow provided by operating activities	**33,405**	**44,990**
Cash flows from investing activities:		
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	800
Funding of mortgage and other loans receivable	(50)	(45)
Principal payments on mortgage and other loans receivable	(4,350)	(3,000)
Purchase of marketable securities	(4,600)	(3,900)
Sales and maturities of marketable securities	-	5,000
Net cash flow used in investing activities	**(12,295)**	**(8,345)**
Cash flows from financing activities:		
Proceeds from mortgage loans payable	-	2,500
Principal borrowings (repayments) on mortgage loans payable	10,470	(1,900)
Payment of financing costs	-	(690)
Contributions	285	570
Distributions	(475)	(380)
Contributions from noncontrolling interests	15	30
Distributions to noncontrolling interests	(25)	(20)
Net cash flow provided by financing activities	**10,270**	**110**
Net change in cash and cash equivalents	**31,380**	**36,755**
Cash and cash equivalents — Beginning of year	59,255	22,500
Cash and cash equivalents — End of year	**$ 90,635**	**$ 59,255**
Supplemental cash flow information:		
Cash paid for interest, net of amounts capitalized of $1	$ 2	$ 1
Cash paid for income taxes	12	10

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

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 Cost	December 31, XXCY Fair Value	December 31, XXPY Cost	December 31, XXPY Fair Value
Real estate investments and joint ventures								
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		15.47% 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		13.31% 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		2.65% as of 12/31/XXCY			6,200	9,000	6,100	6,000
Other investments								
Other	EJV	City, State	1/1/XXXX	N/A	12,500	14,500	12,400	13,200
Total other investments		4.27% 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		11.39% as of 12/31/XXCY			34,350	38,700	31,100	33,400
Retail								
Retail 1	CJV	City, State	1/1/XXXX	xxx	24,100	32,900	22,000	27,800
Total retail		9.69% as of 12/31/XXCY			24,100	32,900	22,000	27,800
Total real estate investments and joint ventures					**162,850**	**192,850**	**154,800**	**168,100**
Mortgage and other loans receivable								
Loan 1	Loan		1/1/XXXX	N/A	5,400	5,775	5,350	5,600
Loan 2	Eloan	City, State	1/1/XXXX	xxx	5,800	6,325	5,800	6,200
Total mortgage and other loans receivable		3.56% as of 12/31/XXCY			**11,200**	**12,100**	**11,150**	**11,800**
Other real estate investments								
Other	Other	City, State	1/1/XXXX	N/A	18,550	22,125	14,200	15,600
Total other real estate investments		6.51% as of 12/31/XXCY			**18,550**	**22,125**	**14,200**	**15,600**
Total real estate investments					**$ 192,600**	**$ 227,075**	**$ 180,150**	**$ 195,500**

WO - Wholly Owned Investment
CJV - Consolidated Joint Venture
EJV - Joint Venture Investment accounted for under the equity method
Eloan - Mezzanine loan 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

XYZ REAL ESTATE ACCOUNT

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

1. ORGANIZATION

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, office, and residential properties.

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.

In accordance with Accounting Standards Codification 810, *Consolidation* (ASC 810), the accompanying consolidated financial statements include the accounts of the Account, real estate partnerships for which the Account has control of the major operating and financing policies and its real estate partnerships which are deemed to be variable interest entities, or VIEs, in which the Account was determined to be the primary beneficiary. 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.

<u>Consolidated VIE's</u>

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

The consolidated investments in real estate and mortgages payable of the VIE's as of December 31, XXCY and XXPY are as follows:

[disclose range of values, cost and debt balances and total carrying amount, cost and debt balances]

Total consolidated carrying value and historical cost of real estate investments are classified in XX in the accompanying consolidated statements of net assets. Consolidated debt is classified in XX in the accompanying statements of net assets. The mortgage encumbrances are collateralized by the underlying real estate assets and in some cases guaranteed by the noncontrolling interests. Creditors of the consolidated VIEs have no recourse to the general credit of the Account.

<u>Unconsolidated VIE's</u>

On January 1, XXCY the Account (de)consolidated XX VIEs which were consolidated as of December 31, XXCY because the Account does not have the power to direct the activities that most significantly impact the VIE's economic performance. These VIE's are now reported under the equity method in the accompanying consolidated financial statements.

Noncontrolling Interests - ASC 810-10 requires that noncontrolling interests in the Account's consolidated subsidiaries, be reclassified to net assets and that the net increase or decrease in net asset value from operations be 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. Prior to adoption of the new standards, in cases where losses applicable to minority interests exceeded the minority interest's equity capital of the subsidiary such excess and any further losses were charged against the parent's interest.

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 closing 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 since control of the investment is shared with the respective venture member. Under the equity method, the investment is initially recorded at the original investment amount, plus additional amounts invested, and are 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.

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 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, since 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 general partner 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 general partner 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.

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 Accounting Standards Codification 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 statement 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. Interest income is accrued as earned in accordance with the contractual terms of the loan agreements. Operating expenses are recognized as incurred.

Investment advisory fees — Investment advisory fees include asset management fees and investment acquisition fees charged by ABC. Such amounts are reflected in the accompanying 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 Accounting Standards Codification topic 450, *Contingencies*.

Accounting Standards Codification topic 740, *Income Taxes* (ASC 740), 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 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 balance sheet date. 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 statement 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 statement of operations. A transaction gain or loss (measured from the transaction date or the most recent intervening balance sheet date, 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 statement 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 (ASU) recently issued that may be applicable to users of this manual include the following[1]:]

- o ASU 2014-09, *Revenue from Contracts with Customers* (including subsequent amendments)
- o ASU 2016-02, *Leases*
- o ASU 2016-13, *Financial Instruments – Credit Losses: Measurement of Credit Losses on Financial Instruments*
- o ASU 2016-15, *Statement of Cash Flows: Classification of Cash Receipts and Cash Payments*
- o ASU 2106-18; *Statement of Cash Flows: Restricted Cash*

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

3. FAIR VALUE MEASUREMENTS

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 the market and 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, *Financial Instruments*, 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 Fund 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 Fund's net asset value.

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

<u>Real estate investments</u> — 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

[1] Additional ASUs may be applicable, as determined by management.

approach provides a check 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.][2]

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.

Since 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.

<u>Unconsolidated real estate joint ventures</u> — 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.

<u>Marketable securities</u> — 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.

<u>Mortgage and other loans receivable</u> — The fair value of mortgage loans and notes 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 loans and notes receivable are classified within level 3 of the valuation hierarchy. The fair value of mortgage loans and notes 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

[2] Bracketed wording required for SEC registrants.

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.][3]

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.][4]

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
Other real estate investments	22,125			22,125
Marketable securities	43,100			43,100
Total real estate investments	$ 65,225	$ -	$ 204,950	$ 270,175
Mortgage loans and notes payable	$ -	$ -	$ (77,220)	$ (77,220)

[3] Bracketed wording required for SEC registrants.

[4] Bracketed wording required for SEC registrants.

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, 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
Other real estate investments	15,600			15,600
Marketable securities	38,500			38,500
Total real estate investments	$ 54,100	$ -	$ 179,900	$ 234,000
Mortgage loans and 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 2 and 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	Total Level 3 Investments	Mortgage Loans and Notes Payable
Beginning balance December 31, XXPY	**$ 121,500**	**$ 46,600**	**$ 11,800**	**$ 179,900**	**$ (64,870)**
Unrealized gain (loss) on real estate investments	14,550	3,250	250	18,050	(1,880)
Equity in income of unconsolidated real estate joint ventures		21,450		21,450	
Distributions from unconsolidated real estate joint ventures		(18,100)		(18,100)	
Purchases of real estate investments	5,800			5,800	
Proceeds from sale of real estate investments	(2,200)			(2,200)	
Issuances of mortgage and other loans receivable			50	50	
Borrowings on mortgage loans and notes payable					(10,470)
Ending balance December 31, XXCY	**$ 139,650**	**$ 53,200**	**$ 12,100**	**$ 204,950**	**$ (77,220)**
	-	-	-	-	-
Beginning balance December 31, XXPY-1	**$ 125,900**	**$ 39,270**	**$ 11,655**	**$ 176,825**	**$ (67,770)**
Unrealized gain (loss) on real estate investments	(8,000)	(1,120)	100	(9,020)	1,000
Equity in income of unconsolidated real estate joint ventures		20,500		20,500	
Distributions from unconsolidated real estate joint ventures		(14,550)		(14,550)	
Purchases of real estate investments	4,700	2,500		7,200	
Proceeds from sale of real estate investments	(1,100)			(1,100)	
Issuances of mortgage and other loans receivable			45	45	
Borrowings on mortgage loans and notes payable				-	1,900
Ending balance December 31, XXPY	**$ 121,500**	**$ 46,600**	**$ 11,800**	**$ 179,900**	**$ (64,870)**

Total unrealized gains of $____ for XXCY included above are attributable to real estate properties held at December 31, XXCY and are included in unrealized gain on real estate and improvements in the accompanying consolidated statement of operations.

Total unrealized gains of $_______ for XXCY included above are attributable to unconsolidated real estate joint ventures investments held at December 31, XXCY and are included in net unrealized gain on unconsolidated real estate joint ventures in the accompanying consolidated statement of operations.

Total unrealized losses of $______for XXCY included above are attributable to mortgage loan and other notes receivable held at December 31, XXCY and are included in unrealized losses on mortgage loans and other notes receivable in the accompanying consolidated statements of operations.

Total unrealized losses of $______for XXCY included above are attributable to mortgage notes payable held at December 31, XXCY and are included in unrealized losses on mortgage loans and note payable in the accompanying consolidated statements of operations.

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

	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)
Real estate investments and improvements						
Apartment	$ 52,550	$ 48,000	Discounted cash flows (DCF)	Discount rate	xx% to xx% (xx%)	xx% to xx% (xx%)
				Capitalization rate	xx% to xx% (xx%)	xx% to xx% (xx%)
				DCF term (years)	10 years (10 years)	10 years (10 years)
				Revenue growth rate	xx% to xx% (xx%)	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	xx% to xx% (xx%)	xx% to xx% (xx%)
				Capitalization rate	xx% to xx% (xx%)	xx% to xx% (xx%)
				DCF term (years)	10 years (10 years)	10 years (10 years)
				Revenue growth rate	xx% to xx% (xx%)	xx% to xx% (xx%)
Retail	$ 32,900	$ 27,800	Direct capitalization method	Direct cap rate	xx% to xx% (xx%)	xx% to xx% (xx%)
Unconsolidated real estate joint ventures						
Industrial	$ 57,000	$ 51,000	Discounted cash flows (DCF)	Discount rate	xx% to xx% (xx%)	xx% to xx% (xx%)
				Capitalization rate	xx% to xx% (xx%)	xx% to xx% (xx%)
				DCF term (years)	10 years (10 years)	10 years (10 years)
				Revenue growth rate	xx% to xx% (xx%)	xx% to xx% (xx%)
Office	$ 45,000	$ 40,000	Discounted cash flows (DCF)	Discount rate	xx% to xx% (xx%)	xx% to xx% (xx%)
				Capitalization rate	xx% to xx% (xx%)	xx% to xx% (xx%)
				DCF term (years)	10 years (10 years)	10 years (10 years)
				Revenue growth rate	xx% to xx% (xx%)	xx% to xx% (xx%)
Mortgage and other loans receivable						
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	xx% to xx% (xx%)	xx% to xx% (xx%)
				Loan to value ratio	xx% to xx% (xx%)	xx% to xx% (xx%)
				Weighted average cost of capital risk premiums	xx% to xx% (xx%)	xx% to xx% (xx%)
Mortgage loans and notes payable						
Industrial	$ 57,720	$ 55,840	Discounted cash flows (DCF)	Loan to value ratio	xx% to xx% (xx%)	xx% to xx% (xx%)
Retail	$ 19,500	$ 9,030	Net present value	Credit spreads	xx% to xx% (xx%)	xx% to xx% (xx%)
				Loan to value ratio	xx% to xx% (xx%)	xx% to xx% (xx%)
				Weighted average cost of capital risk premiums	xx% to xx% (xx%)	xx% to xx% (xx%)

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 Fund'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, and Overall Capitalization 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.

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:

Year Ended		**December 31, XXCY**		**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 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 of 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. It is estimated that the underlying assets of the funds will be liquidated over the next XX to XX years. XX% of the total investment is planned to be sold. 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.

5. MORTGAGE LOANS AND NOTES PAYABLE

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

	XXCY Fair Value	XXCY Cost	XXPY Fair Value	Interest Rate [1]	Maturity Date	Terms [3]
Mortgage lons						
Apt 1	$ -	$ -	$ 1,000	x.xx%[2]	XXXX	P&I, PP
Apt 2	14,760	15,540	14,020	LIBOR (30-day) + x.xx%	XXXX	I
Hotel 1	24,270	25,550	23,060	LIBOR (30-day) + x.xx%	XXXX	I
Industrial 1	4,060	4,270	3,860	LIBOR (30-day) + x.xx%	XXXX	I
Retail 1	14,630	15,400	13,900	LIBOR (30-day) + x.xx%	XXXX	I
Total Mortgage Loans Payable	**$ 57,720**	**$ 60,760**	**$ 55,840**			
Notes Payable						
Apt1	$ 9,500	$ 10,000	$ 9,030	Weekly Variable [4]	XXXX	I
XYZ Real Estate Fund	10,000	10,000		LIBOR (30-day) + x.xx%	XXXX	I
Total Notes Payable	**$ 19,500**	**$ 20,000**	**$ 9,030**			

[1] As of December 31, XXCY, 30 day LIBOR was x.xxxx%.

[2] The loan has a floating interest rate of x.xx% over LIBOR however the venture is obligated to pay a fixed rate of x.xx% with the venture partner assuming all interest rate risk or benefit.

[3] Loan Terms PP=Prepayment penalties applicable to loan, I=Interest only, P&I=Principal and Interest

[4] 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 as of December 31, XXCY. The loans 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	80,760
Total	**$ 80,760**

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 "Unconsolidated Real Estate joint ventures" for equity joint ventures and "Other liabilities" or "Prepaid and other assets" for consolidated ventures on the Consolidated Statements of Net Assets. The resulting unrealized gain (loss) on the equity Accounts is reflected in the Consolidated Statements of Operations in "Change in unrealized gain (loss) on real estate investments". The resulting unrealized gain (loss) for consolidated ventures 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
Real estate investments						
Property 1	Pay-fixed swap	$ -	x.xx%	$ -	$ -	July XXXX
Property 2	Pay-floating swap	-	x.xx%	-	-	July XXXX
Property 3	Cap	-		-	-	July XXXX
Total real estate investments		**$ -**		**$ -**	**$ -**	
Unconsolidated real estate joint ventures						
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	-		-	-	April XXXX
Total unconsolidated real estate joint ventures		**$ -**		**$ -**	**$ -**	
Total		**$ -**		**$ -**	**$ -**	

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 regions is as follows:

Region	Fair Value	Region %
East North Central	$ 63,581	28
Mideast	40,873	18
Mountain	40,873	18
Northeast	20,437	9
Pacific	20,437	9
Southeast	20,437	9
Southwest	20,437	9
Total	$ 227,075	100

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	Unrealized gain (loss) on real estate investments	$xxx,xxx	$xxx,xxx	XX bp of Total capital committed
Development	Investment management fees	xxx,xxx	xxx,xxx	XX bp of Total development costs
Financing	Administrative expenses	xxx,xxx	xxx,xxx	XX bp of Original principal balance
Loan Origination	Administrative expenses	xxx,xxx	xxx,xxx	XX bp of Projected principal balance
Investment Management	Investment management fees	xxx,xxx	xxx,xxx	X% of Net operating income
Disposition	Realized gain (loss) from sales of real estate investments	xxx,xxx	xxx,xxx	XX bp of Gross sale price
Incentive (1)	Unrealized gain (loss) on real estate investments	xxx,xxx	xxx,xxx	XX% over XX% IRR (1)
Total Investment Management Fees		**$xxx,xxx**	**$xxx,xxx**	

[Add additional fee description details as appropriate]

(1)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 achieving 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.

Incentive fees of $xx,xxx and $xx,xxx were payable at December 31, XXCY and XXPY, respectively and are included in Accrued Incentive fees.

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	$xxx,xxx	$xxx,xxx
In-house Accounting	Administrative expenses	xxx,xxx	xxx,xxx
In-house Proprietary Software	Administrative expenses	xxx,xxx	xxx,xxx
Total Reimbursements		**$xxx,xxx**	**$xxx,xxx**

[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	$xxx,xxx	XX-XX bp of Gross receipts
Construction Management	N/A	xxx,xxx	xxx,xxx	XX bp of Development budget
Leasing	N/A	xxx,xxx	xxx,xxx	XX bp of Contract rent
Brokerage	N/A	xxx,xxx	xxx,xxx	XX bp of Sales price
Financing	Administrative expenses	xxx,xxx	xxx,xxx	XX bp of Projected principal balance
Payroll/benefits for on-site management	Administrative expenses	xxx,xxx	xxx,xxx	N/A
Total Property Service Fees & Expenses		**$xxx,xxx**	**$xxx,xxx**	

[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.

[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 under non-cancelable operating leases having a term of more than one year are as follows:

Year Ending December 31	Properties	Joint Ventures
XXCY+1	$ 33,110	$ 74,160
XXCY+2	34,100	76,380
XXCY+3	35,120	78,670
XXCY+4	36,170	81,030
XXCY+5	37,260	83,460
Thereafter	191,900	429,800
Total	$ 367,660	$ 823,500

The above future minimum base rentals exclude residential lease agreements with terms of less than one year, which accounted for approximately xx% of the Account's annual rental income for the years ended December 31, XXCY. 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.

10. FINANCIAL HIGHLIGHTS — EXAMPLE 1 (Generally required for investment companies within scope of Topic 946)

	December 31, XXCY	December 31, XXPY
Net assets, beginning of period	**$ 253,356**	**$ 215,242**
Income in net assets resulting from operations:		
Investment income, before management fees	50,035	46,009
Net realized and unrealized gain (loss) on investments	16,149	(5,909)
Total from investment operations, before management fees	66,184	40,100
Management fees	1,188	950
Total from investment operations	64,996	39,150
Net increase (decrease) resulting from capital transactions	(190)	190
Net assets, end of period	**$ 318,162**	**$ 253,356**
Total return, before management fees[2]:	**23.8%**	**23.5%**
Total return, after management fees[2]:	**23.4%**	**23.5%**
Ratios to average net assets[3]:		
Total expenses	8.1%	7.6%
Net investment income	18.4%	17.2%

[1] All amounts are shown net of amounts allocated to noncontrolling interests

[2] Total Return, before/ after management fees is calculated by geometrically linking quarterly returns which are calculated using the formula below:

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

[3] Average net assets are based on beginning of quarter net assets.

FINANCIAL HIGHLIGHTS (CLOSED END/FINITE LIVED) — EXAMPLE 2

	December 31, XXCY	December 31, XXPY
Total return:		
Internal rate of return [1]	15.0 %	14.0 %
Ratios/supplemental data:		
Net assets, end of period	$ 318,162	$ 253,356
Ratios to average net assets[2]:		
Total expenses	8.1 %	7.9 %
Incentive allocation	%	%
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 %

[1] 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.

[2] Average net assets are calculated based on an average of beginning quarterly net assets.

11. COMMITMENTS AND CONTINGENCIES

Accounting Standards Codification topic 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 [1]
Apartment 1	6/30/XXXX	$ 1,140	$ 2,900

[1] 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 outstanding 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	8,300
Total	$ 21,000

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 assets, liabilities, and equity.

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.

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
Assets:		
Real estate investments	$ 273,913	$ 229,841
Cash and cash equivalents	40,635	19,255
Other assets	31,120	18,400
Total assets	**345,668**	**267,496**
Liabilities:		
Loans payable	10,000	-
Other liabilities	760	805
Total liabilities	**10,760**	**805**
Net assets	**$ 334,908**	**$ 266,691**

See accompanying notes to the financial statements
For illustrative purposes only - Non-operating model financial statements

XYZ REAL ESTATE FUND, LP

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

	XXCY	XXPY
Income		
Income distributions from real estate equity investments	$ 28,060	$ 41,057
Interest income on real estate debt investments	8,300	1,268
Other	3,170	120
Total income	**39,530**	**42,445**
Expenses		
Interest expense	-	-
Administrative expenses	1,185	4,500
Investment management fees	1,250	1,000
Total expenses	**2,435**	**5,500**
Net investment income	**37,095**	**36,945**
Net realized and unrealized gain (loss):		
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 on real estate investments held at year end	31,322	3,981
Unrealized incentive fees	-	-
Net realized and unrealized gain	**31,322**	**4,266**
Increase in net assets resulting from operations	**$ 68,417**	**$ 41,211**

See accompanying notes to the financial statements
For illustrative purposes only - Non-operating model financial statements

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
Net assets - December 31, XXPY-1	**$ 11,264**	**$ 214,016**	**$ 225,280**
Increase in net assets resulting from operations	2,061	39,150	41,211
Contributions	30	570	600
Distributions	(20)	(380)	(400)
Net assets - December 31, XXPY	**13,335**	**253,356**	**266,691**
Increase in net assets resulting from operations	3,421	64,996	68,417
Contributions	15	285	300
Distributions	(25)	(475)	(500)
Net assets - December 31, XXCY	**$ 16,746**	**$ 318,162**	**$ 334,908**

See accompanying notes to the financial statements
For illustrative purposes only - Non-operating model financial statements

XYZ REAL ESTATE FUND, LP

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

		XXCY		XXPY
Cash flows from operating activities:				
Increase in net assets resulting from operations	$	68,417	$	41,211
Adjustments to reconcile net assets resulting from operations to net cash flows provided by (used in) operating activities:				
Net realized and unrealized gain		(31,322)		(4,266)
Change in other assets		(12,720)		200
Change in other liabilities		(45)		50
Distributions from real estate investments		25,705		-
Funding of real estate investments		(38,455)		(39,163)
Proceeds from real estate investments sold		-		760
Net cash flow provided by (used in) operating activities		**11,580**		**(1,208)**
Cash flows from investing activities:				
Proceeds from loans payable		10,000		-
Distributions		(500)		(400)
Contributions		300		600
Net cash flow (used in) provided by financing activities		**9,800**		**200**
Net change in cash and cash equivalents		**21,380**		**(1,008)**
Cash and cash equivalents — Beginning of year		19,255		20,263
Cash and cash equivalents — End of year	**$**	**40,635**	**$**	**19,255**
SUPPLEMENTAL CASH FLOW INFORMATION:				
Cash paid for interest on loans payable	$	2	$	1
Cash paid for income taxes		12		10

See accompanying notes to the financial statements
For illustrative purposes only - Non-operating model financial statements

SCHEDULE 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 Cost	December 31, XXCY Fair Value	December 31, XXPY Cost	December 31, XXPY Fair Value
Real estate owned and joint ventures							
Apartment							
Apt 1	City, State	1/1/XXXX	xxx units	$ 70,000	$ 78,450	$ 65,000	$ 67,970
Apt 2	City, State	1/1/XXXX	xxx units	17,575	28,110	17,575	22,943
Total apartment	31.82% as of 12/31/2012			87,575	106,560	82,575	90,913
Hotel							
Hotel 1	City, State	1/1/XXXX	xxx rooms	20,900	35,179	20,900	29,583
Total hotel	10.5% as of 12/31/2012			20,900	35,179	20,900	29,583
Industrial							
Industrial 1	City, State	1/1/XXXX	xxx	13,500	27,940	13,500	22,140
Total industrial	8.34% as of 12/31/2012			13,500	27,940	13,500	22,140
Other investments							
Other	City, State	1/1/XXXX	N/A	12,500	14,500	12,400	13,200
Total other investments	4.33% as of 12/31/2012			12,500	14,500	12,400	13,200
Office							
Office 1	City, State	1/1/XXXX	xxx	34,350	38,700	31,100	33,400
Total office	11.56% as of 12/31/2012			34,350	38,700	31,100	33,400
Retail							
Retail 1	City, State	1/1/XXXX	xxx	7,125	16,809	7,125	13,205
Total retail	5.02% as of 12/31/2012			7,125	16,809	7,125	13,205
Total real estate owned and joint ventures				**175,950**	**239,688**	**167,600**	**202,441**
Mortgage and other loans receivable							
Loan 1		1/1/XXXX	N/A	5,400	5,775	5,350	5,600
Loan 2	City, State	1/1/XXXX	xxx	5,800	6,325	5,800	6,200
Total mortgage and other loans receivable	3.61% as of 12/31/2012			**11,200**	**12,100**	**11,150**	**11,800**
Other real estate investments							
Other	City, State	1/1/XXXX	N/A	18,550	22,125	14,200	15,600
Total other real estate investments	6.61% as of 12/31/2012			**18,550**	**22,125**	**14,200**	**15,600**
Total real estate investments				**$ 205,700**	**$ 273,913**	**$ 192,950**	**$ 229,841**

See accompanying notes to the financial statements
For illustrative purposes only - Non-operating model financial statements

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 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 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.

The Fund generally records realized gains and losses on sales of real estate investments pursuant to the provisions of Accounting Standards Codification subtopic 360-20, *Real Estate Sales* ("ASC 360-20"). The specific timing of a sale is measured against various criteria in ASC 360-20 related to the terms of the transaction and any continuing involvement in the form of management or financial assistance associated with the property.

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

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

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

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

7. 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	Unrealized gain (loss) on real estate investments	$xxx,xxx	$xxx,xxx	XX bp of Total capital committed
Development	Investment management fees	xxx,xxx	xxx,xxx	XX bp of Total development costs
Financing	Administrative expenses	xxx,xxx	xxx,xxx	XX bp of Original principal balance
Loan Origination	Administrative expenses	xxx,xxx	xxx,xxx	XX bp of Projected principal balance
Investment Management	Investment management fees	xxx,xxx	xxx,xxx	X% of Net operating income
Disposition	Realized gain (loss) from sales of real estate investments	xxx,xxx	xxx,xxx	XX bp of Gross sale price
Incentive (1)	Unrealized gain (loss) on real estate investments	xxx,xxx	xxx,xxx	XX% over XX% IRR (1)
Total Investment Management Fees		**$xxx,xxx**	**$xxx,xxx**	

[Add additional fee description details as appropriate]

(1)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 achieving 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.

Incentive fees of $xx,xxx and $xx,xxx were payable at December 31, XXCY and XXPY, respectively and are included in Accrued Incentive fees.

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	$xxx,xxx	$xxx,xxx
In-house Accounting	Administrative expenses	xxx,xxx	xxx,xxx
In-house Proprietary Software	Administrative expenses	xxx,xxx	xxx,xxx
Total Reimbursements		**$xxx,xxx**	**$xxx,xxx**

[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. These amounts are a component of the Account's Investment position in the accompanying financial statements.

Property Service Fees & Expenses:	Year Ended XXCY	Year Ended XXPY	Fee Description
Property Management	$xxx,xxx	$xxx,xxx	XX-XX bp of Gross Receipts
Construction Management	xxx,xxx	xxx,xxx	XX bp of Development Budget
Leasing	xxx,xxx	xxx,xxx	XX bp of Contract Rent
Brokerage	xxx,xxx	xxx,xxx	XX bp of Sales Price
Financing	xxx,xxx	xxx,xxx	XX bp of Projected Principal Balance
Payroll & Benefits for on-site management	xxx,xxx	xxx,xxx	N/A
Total Property Service Fees & Expenses	**$xxx,xxx**	**$xxx,xxx**	

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

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.

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

8. FINANCIAL HIGHLIGHTS (GENERALY N/A TO SEPARATE OR UNITIZED ACCOUNTS

The following summarizes the Fund's financial highlights, consisting of total return and expense and net investment income ratios, for the years ended December 31, XXCY and XXPY:

	XXCY Limited Partners	XXPY Limited Partners
Total return [1]		
End of period since-inception internal rate of return	15.00 %	14.00 %
Beginning of period since-inception internal rate of return	14.00 %	13.75 %
Expense ratios [2]		
Operating expense	0.87 %	1.05 %
Incentive allocation	%	%
Total expenses and incentive allocation	0.87 %	1.05 %
Net investment income ratio [3]	**13.23 %**	**15.99 %**

1 Total return is calculated based on a dollar-weighted internal rate of return methodology net of fees and incentive allocations. The internal rate of return is computed on a since-inception basis using annual compounding and the actual dates of cash inflows received by and outflows paid to investors and including ending net asset value as of each measurement date. Because total return is calculated for the limited partners taken as a whole, an individual limited partner's return may vary from these returns based on different management fee and incentive arrangements (as applicable) and the timing of capital transactions.

2 The expense ratios are calculated for the Limited Partners taken as a whole using weighted average net assets for the period. The computation of such ratios based on the amount of expenses and incentive allocations assessed to an individual Limited Partner's capital may vary from these ratios based on different management fee and incentive arrangements (as applicable) and the timing of capital transactions.

3 The net investment income ratios are calculated for the Limited Partners taken as a whole using weighted average net assets for the period. The computation of the net investment income ratio based on the amount

of net investment income assessed to an individual Limited Partner's capital may vary from these ratios based on different management fee arrangements (as applicable). The net investment income ratio does not reflect the effects of any incentive allocation.

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

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

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

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