End of Fund Life Report
2016

End of Fund Life Project

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The Association of Real Estate Funds

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1.0 Executive Summary

In the past few years, an increasing number of funds have reached the end of their life and the process to liquidate, restructure or extend has been undertaken. The success of this procedure appears to have been somewhat diverse, leaving some investors and fund managers frustrated and disappointed.

While a great deal of energy and deliberation is given to formalising the correct terms and procedures for the creation of a fund, the end of fund life process is not necessarily given the same level of engagement. In addition, individual requirements and circumstances can change radically during the fund's life, which may result in conflict, particularly when communication and transparency are lacking. How can these situations be avoided? What lessons can be learnt from past experiences?

This project has garnered the tremendous amount of knowledge and experience gathered from those who have been involved in the process of winding up or extending real estate funds in the last 10 years to provide tools that will help improve the end of fund life experience for all those involved. A project team was established consisting of senior real estate professionals and over 30 industry representatives were interviewed from the UK, Europe and the US about their experiences. In addition, three workshops were held in Amsterdam, Jersey and London to attain feedback on the initial draft of the report.

Through the interview process, a set of four overriding guiding principles has been created one for each of the key areas of concern that were identified. These principles are:

1. Communication: transparency and timeliness;
2. Fund documentation: explicit, yet flexible;
3. Conflicts of interest: recognise and manage; and
4. Management decisions: be mindful of fund termination date.

Each of these principles is substantiated by a corresponding set of practical best practice guidelines. It is hoped that these guidelines will be utilised to further enhance the guidelines and code of practices of INREV and AREF. Each of the guiding principles and the best practice guidelines are discussed in more depth in the report.

2.0 Introduction

Scope of research

The principles and guidance provided in this report cover any indirect real estate fund coming to the end of its life. These are principally closed-ended vehicles but may also include open-ended funds approaching wind up or that have a fixed rather than indefinite life. In Europe, closed-ended real estate funds tend to fall into two broad categories, private equity (PE) style funds and more institutionalised longer term vehicles.

PE funds generally have very clear terms relating to the life of the fund. In documentation, it is common practice to state the proposed length of the fund, giving a date for termination. Usually, some flexibility at the end of fund life is provided by the possibility of two one-year extensions; the first is usually at the fund manager’s discretion while the second is often by investor agreement. Any further extension is not permitted. All investors exit the fund on a wind-up at the same time.

Institutional-style vehicle documentation will state the length of the fund life. However, documentation is often worded to provide the opportunity for a longer-term extension, of say, five years. It is typical that one or two years before the end of the fund, investors can vote with a 75% majority to extend the fund life for a fixed period. Those voting against have the right to exit at the original term end. When this style of fund became popular around 2001-2004, it was not envisaged that an extension would lead to a restructuring of the fund that could be potentially contentious or take a long time to conclude. However, it was envisaged that providing an exit route to some investors, by selling assets at the end of the fund life, could be challenging. Hence, emphasis was given to:

- allowing secondary trades;
- time to dispose of assets;
- raising debt or seeking new equity; and
- the setting of the exit pricing to the time of payment rather than the date of the original term end.

The scope of this report does not cover redemptions that occur during the life of an open-ended fund, nor does it provide guidance on new commercial terms for extensions for institutional-style vehicles.

On an annual basis, INREV completes a Fund Termination Study that explores the options a fund manager faces as a fund approaches termination date. In the 10 years of its existence, wind-up and extension have constantly been the most popular options with less than 20% of fund managers consistently choosing other strategies such as rollover, mergers, sales or initial public offerings (IPOs). This report therefore focuses on issues around wind-up and extension strategies.

Methodology

A project team (‘the Team’), consisting of senior real estate professionals, was created at the commencement of this project. Following the consultation process, it was the responsibility of the Team to identify simple overriding principles covering the end of fund life period to aid the real estate industry in enhancing its processes. In addition, the Team produced guidance and best practice on the key criteria identified, which may be utilised to further enhance the guidelines and code of practices of INREV and AREF.

To establish the key issues and concerns involved in the end of fund life process, 30 European real estate professionals, including investors, fund managers, administrators and lawyers, were interviewed. In addition, a number of US fund managers were questioned on their experiences to give perspective from the US market. Interviews lasted for approximately an hour and took the form of a free-flowing discussion.

The guiding principles and best practice guidelines recommended by the Team were presented at workshops in Amsterdam, Jersey and London to garner comment from the real estate industry. These events were collectively attended by approximately 200 industry professionals. Feedback has been incorporated into the final recommendations. Note has also been made of written responses received during the consultation phase.

As part of the workshops, delegates were asked to give a ranking to each of the best practice guidelines to provide direction on the relevance of each guideline to the real estate industry. Rankings were from 1 to 5 (with 1 being Very Important, 3 being Relevant and 5 being Irrelevant). All the rankings were collated to give a single rank for each guideline and no best practice guideline ranking was lower than 3. These rankings are detailed in Appendix 1.

Summary of report

Following the introduction, this report details the potential triggers for beginning the end of life phase. The four guiding principles are then set out and are discussed in more depth in the succeeding chapters. The corresponding best practice guidelines for each principle are also highlighted. These guidelines (along with their rankings) are summarised in Appendix 1.

A key aim of this report is to offer practical support to the real estate industry when approaching the end of a fund's life. To this end, Appendix 2 of the report provides an overview of a 'typical' consultation process and Appendix 3 sets out a 'Best Practice Steps Guide for the Fund Extension Process'. Both appendices outline a set of suggested procedures for a fund manager to follow when considering making a request to investors to extend (or wind up) a fund in the longer term.

The issue of tail-end liabilities at the end of a fund's life was a frequent topic of conversation in many interviews. Currently, there appears to be a lack of understanding of the role of insurance in dealing with tail-end liabilities to ensure a more succinct wind-up of funds. To address this, Appendix 4 details how the use of insurance can be beneficial in the end of fund life process and outlines the present state of the market.

Finally, a technical guide is provided in Appendix 5 that sets out issues and procedures for the winding up of some of the most common real estate fund vehicles.

3.0 Triggers for Wind Up

In normal circumstances, a traditional closed-ended fund would be expected to have disposed of its assets prior to the end of the fixed life of the fund. Such funds would generally have a strategy that is dependent upon timing, either through taking advantage of the cyclical nature of real estate to buy at the bottom of the market and to sell at the top, or to undertake active steps to add value to the property prior to disposal. As such timing cannot always be determined with absolute accuracy, it is common for fund documentation to provide for some limited flexibility through the possibility of extension.

There are a variety of events that may trigger a decision as to whether to wind up a fund or to extend. Some of these are planned, but others may be a reaction to unexpected circumstances. This is discussed further below.

Requirement of the documents

The most common trigger for the decision as to whether to wind up a fund or to prolong is simply the requirements set out in the documentation. In PE style funds, the presumption is that the assets will have been sold when value has been maximised through an active strategy and a decision to extend only occurs in exceptional circumstances. This is not the case in all funds. In some of the more institutionalised longer term funds an investor decision to wind up or extend the fund is taken a year or two before the end of the fund life. The fund manager will not have sold the assets prior to this as it does not know if the fund is winding up or continuing. If the investor vote is to wind up then a sales programme is agreed. Investors may agree a limited extension with an exit strategy to be put in place so assets are disposed of over a sufficiently extended period so as not to erode value.

Although the requirements of the documents is the most common experience, in practice particularly during a cyclical downturn, there are a variety of other circumstances that might give rise to either a premature end of a fund or a need to extend beyond the planned life of the fund.

There may also be specific trigger events in the documentation that result in either a change in the fund manager (discussed further below) or a winding up of the fund. These might include key man events, a change in ownership of the fund manager, a major dispute or the insolvency of the fund manager.

Market timing

In normal circumstances, fund managers of closed-ended funds would be expected to sell assets when value has been maximised. In many cases, this will be at the top of the market cycle when the value of assets is generally at their highest. However, for many closed-ended funds that are ‘opportunistic’ or ‘value-add’ in nature for each individual asset there will be a specific business plan in place for maximising value, for example through development or repositioning of the asset. The point at which value is maximised for the asset will not necessarily coincide with the top of the cycle. The fund manager may have completed the asset management strategy prior to the top of the cycle and may maximise the internal rate of return by selling at that point rather than hanging on for further yield compression or the prospect of further rental value growth. On the other hand, the fund manager may not have finished the works at the top of the cycle and value might be maximised by holding the asset and completing the business plan.

In the face of the prolonged market downturn during the global financial crisis, the majority of closed-ended funds coming to the end of their fixed life were extended rather than wound up to avoid selling assets at the bottom of the market. As the market for the underlying assets has improved, the pressure to extend funds to avoid adverse market timing has reduced.

Debt-related issues

Closed-ended funds have often operated with higher levels of gearing than other funds. Debt related issues have been a trigger for funds terminating other than in accordance with the timetable prescribed in the fund documentation. Examples are:

- Leverage accentuating the issues of market timing. As gearing increases gains and losses, in a geared fund it becomes more crucial to achieve the sale when value is maximised (see general comments on market timing above).
- Funds brought to a premature close by the fund manager, investors or lenders, as levels of debt are unsustainable and the fund ceases to be viable.
- Debt terms impose excessive cost in disposing of assets in the normal course of events. There have been examples of loans or swaps entered into with a duration exceeding the length of the fund, resulting in significant break costs if the assets are sold.
- Additional equity required to rectify debt problems, introduced with an extension to the fund and/or other changes to fund terms as a condition.

Case Studies

Contrasting examples of debt related issues are provided by two funds established by the same fund manager. Both funds were created in the early 2000s as closed-ended funds with a fixed life to 2015. Both expanded rapidly in the boom years and were modestly geared but suffered from debt problems in the downturn when asset values fell significantly.

One of the funds had to raise additional equity to deal with loan-to-value (LTV) covenant breaches as debt levels spiralled as values fell. Under a restructuring plan in the late 2000s, a US opportunity fund manager acquired a significant stake and the fund manager injected further capital on favourable terms. Other investors therefore had their interests diluted. According to the fund documents, unanimous investor approval was required. The fund manager was able to obtain legal opinion that a small investor could not block what was in the interest of all investors so the equity injection was able to proceed without unanimous consent.

The restructuring involved a new management structure and a defined business plan for exit from the assets. The LTV covenant was also altered to reflect this. Following the decision to realise the assets and wind up the fund, the final sales were agreed well before the original termination date.

The second fund also had debt problems but the circumstances were somewhat different. Debt finance had originally been provided by banks but the fund was refinanced in the mid 2000s with a significantly sized bond due to be repaid in 2012. Debt now represented a LTV of 50%.

After the market crash, it became apparent that the fund would not be able to repay the bond in 2012. The bond had to be restructured and its life extended to 2015, with an amortisation programme through agreed sales in the meantime. As part of this restructuring, the life of the fund was extended by two years. The process with investors was relatively straight-forward, as there was no real alternative, as there had already been a discounted equity raise on the fund. Bondholder consent was harder to achieve than unit holder approval. The restructuring of the bond and the extension of fund life took effect from the same date. As part of the process, there were governance changes. In particular, an independent board was established.

Performance-related issues/changes of fund manager

Although changes of fund manager in closed-ended funds have been relatively unusual, there have been examples, either at the instigation of investors or due to the failure of the fund manager. Most fund documentation now allows for the removal of the fund manager, both for specific cause and ‘not for cause’. In the case of a matter arising that might result in a change of fund manager, there are often provisions that allow for a plan to remedy the problem. In some circumstances, this in itself may trigger a discussion as to whether or not to wind up the fund prematurely. If there is a subsequent change of fund manager, it may be regarded as desirable to extend the life of the fund to give the incoming fund manager time to resolve the problems that provoked the change.

Change of strategy

Although fund extensions have generally been associated with unexpected problems, there have been recent cases where both the fund manager and investors have wanted to extend the life of funds to continue to exploit the assets in very successful funds. There have been several cases of funds being extended or converted to a more open-ended structure to allow the assets to be retained. There have also been cases where some investors have been bought out to avoid the necessity of selling assets. Possible options for prolonging a fund’s life are discussed further below.

Change in law or regulation

As discussed under ‘Requirement of the documents’ above, there may be specific trigger events in the documentation that result in either a change in the fund manager or a winding up of the fund. It may also be the case that changes to law or regulation make the fund no longer viable. Examples in the past have included changes to the marketing of unauthorised collective investment schemes in the UK or tax changes.

Options for prolonging the life of a fund

Traditionally, fund documents for closed-ended funds provided for a fixed life, by which time the assets would have been sold with the possibility of a relatively short, fixed-term extension. More recently, there have been examples of other options for the end of fund life including:

- a more substantial extension with the possibility of further extensions;
- conversion of the fund into something semi open-ended, for example with periodic liquidity events; and
- conversion to a permanent capital vehicle via an initial public offering (IPO).

4.0 Expectations and Obligations

The table below details the expectations and obligations of the fund manager and investors during the end of fund life consultation process.

Fund Manager Expectations	Investor Expectations
• To deal with senior investor representatives who are permitted to make decisions • For investors to fully engage in the consultation process • For investors to read all relevant documentation • For investor decisions to be made in a timely manner • For investors to be as transparent as possible, being mindful of confidentiality	• To have capital returned at end of fund life as stated in documentation unless investor agreement to pursue another option • To be engaged early in the consultation process • To receive the same level of written information as other investors • To deal with a suitably senior representative from the fund manager • To have the right to be represented (by self, another investor or independent representative) • To meet without the fund manager to discuss extension proposals • To share legal representation with other investors if agreed • For fund documentation to be modernised, if required, should the fund be extended
Fund Manager Obligations	**Investor Obligations**
• To be timely and proactive • To provide the same level of written information to all investors and to put forward any proposal to all investors simultaneously • To treat all investors fairly • To initiate the wind-up or extension process • To ensure any consultation process is transparent • To put investors' interests first ahead of fund manager's interests • To provide suitable senior management time • To modernise fund documentation, if required, should the fund be extended • To wind up the fund unless agreement is reached to extend and return capital to investors in accordance with the fund document terms • To inform investors of any conflict of interest at the earliest opportunity and to enable/support processes by which any conflicts of interest may be resolved • To ensure, during the life of the fund, all management decisions are made mindful of the fund termination date	• To be represented by someone suitably senior, empowered to make decisions • To be fully engaged with the process and respond in a timely manner • To provide clarity of thought and act with integrity as a house • To fully read and understand all relevant documentation • To avoid point scoring for personal gain • To be honest and open about intentions and to inform of any conflict of interest at the earliest opportunity • To support processes by which conflicts of interest may be resolved • To ensure attendance of investor committees • To advise the fund manager on the length of internal processes before proposals are approved

5.0 Guiding Principles and Best Practice Guidelines

Through extensive discussion on the end of fund life process, four key areas have been identified. For each of these areas, a guiding principle has been created. The four guiding principles are:

1. Communication: transparency and timeliness;
2. Fund documentation: explicit, yet flexible;
3. Conflicts of interest: recognise and manage; and
4. Management decisions: be mindful of fund termination date.

Each guiding principle has been expanded upon in the main body of the report and substantiated by a set of best practice guidelines. These guidelines are listed in Appendix 1.

6.0 Communication: Transparency and Timeliness

The importance placed on good communication, transparency and timeliness in the end of fund life phase was very apparent in the interviews undertaken. In contrast to open-ended vehicles, investors' capital in closed-ended funds is tied up for a considerable length of time, unless there is a secondary market exit route but this is not always readily available. It is therefore vital that fund managers ensure the end of fund life process reflects each of these three attributes.

Ensuring a smooth running process is not just the responsibility of the fund manager but is shared by investors as well. It was documented during both fund manager and investor interviews that it was the actions of some investors that caused delays or problems in the wind-up or extension process.

It is acknowledged that there must be a consultation process between fund managers and investors and among investors when extension possibilities are being considered. However, this process can be so variable that it is difficult to provide complete detail in the fund documentation about how it will ensue. Building a strong working relationship between the fund manager and investors throughout the life of the fund is an important factor in ensuring a successful consultation process.

In conversations about end of fund life, it is the consultation process that has caused a lot of issues relating to communication, transparency and timeliness. PE funds have tended to have fewer issues as their procedures are simpler and clearly mapped out in the fund documentation.

From the experience of fund managers and investors interviewed, it is clear that there are a number of different ways of running the consultation process. Some fund managers carry out minimal discussions with investors. Others will organise one-to-one meetings with all or some investors or utilise roundtable discussions to understand investor views and requirements before putting forward proposals.

Some investors like one-to-one communication with fund managers as they feel they can be more open, particularly those with a significant investment at stake. Others may consider it too time-consuming if they only have a small amount of capital invested. In addition, one-to-one communication for funds with a large number of investors is not necessarily practical. However, fund managers have to ensure that all investors have the same quantity and quality of written information and that small investors do not feel excluded from the process. In addition, this information should be receive by all investors at the same time.

The fund manager should initiate the wind up or extension process. Once a proposal has been drawn up, this should be received by all investors concurrently. This can be in writing or via a meeting open to all investors. No investor should obtain additional information that is not shared with all other investors.

Best Practice: All investors should receive the same level of written information.

Best Practice: All written information should be provided to investors simultaneously.

A recurring frustration cited by investors interviewed is that the senior management team in place at the start of the fund is not always there at the end of the fund life. Some staff movement is always inevitable but, on some occasions, it was observed that senior management was replaced by more junior staff not always sufficiently experienced for the role. This was particularly pertinent in cases where the fund was 'under water' i.e. in breach of some of its loans and senior management time was crucial to resolve the myriad of issues.

Fund managers and other investors have been equally aggravated by some investors sending more junior team members to the discussion table, who are unable or unqualified to make decisions related to the fund. In addition, there has been frustration where it is felt the fund manager or some investors are not actively engaged in the consultation process.

Best Practice: Both fund manager and investors are obliged to ensure suitably senior management time is given to the end of fund life process and that they are actively engaged in the consultation process.

In situations where a longer-term extension is being proposed and the administration will be time consuming, it may be appropriate to have another senior staff member take care of the process rather than the fund manager who is responsible for the day-to-day running of the fund. This should ensure that the fund manager is fully focused on the management of the fund at a critical time in the fund's life. This may only be possible in larger fund management firms where there is sufficient staff to cover both positions.

Best Practice: Where possible, an alternative senior manager (appropriately experienced) is responsible for the extension process rather than the individual fund manager.

It is imperative that investors adopt a consistent house view towards each of their fund investments that is then documented. While a stable strategic view is important, this point is particularly pertinent when new fund terms are negotiated during a consultation process. This is important when there is a change of investor representative as the new incumbent may not be clear on what has been agreed so far and decide to re-open negotiations. If an investor has to change its house view, and a change is unavoidable, it should recognise that it may cause inconvenience, uncertainty, costs and delays to others. Having a documented house view is also helpful if the usual investor contact cannot attend a particular meeting and a stand-in is sent in their absence.

Best Practice: Unless there is very good reason, an investor should have a consistent, documented house view of a fund shared by all personnel involved.

Investors should also advise the fund manager on how long internal processes take to approve proposals so that this can be factored into any timetabling of events.

The importance of a transparent consultation process was often observed in interviews. It is essential that fund managers ensure that the terms and processes for wind up or extension are clearly defined and provided to all investors. This is discussed further in the next section of the report. If decisions cannot be reached, the consequences should be highlighted. For example, the fund manager should be prepared to wind up the fund in accordance with the documentation if agreement on an extension is not achieved.

Best Practice: Fund managers and investors should fully engage in any consultation process and ensure it is as transparent as possible.

Best Practice: The fund manager should be prepared to wind up the fund unless agreement is reached.

Investors also have a duty to be transparent and honest in their actions and behave consistently. However, the issue of confidentiality may restrain behaviour at times. For example, a major corporate event, not yet in the public domain, may delay an investor's ability to provide an opinion or decision about a possible extension.

Investors should also have the ability to meet without the fund manager to discuss proposals. All investors should be invited to the meeting(s). In addition, these forums provide an opportunity for investors to discuss and resolve any differences with each other. An independent chair may be an option.

Best Practice: Investors should have the right to meet without the fund manager to discuss proposals.

The issue of transparency is particularly relevant when there is a conflict of interest. This will be explored later in the report in the Conflicts of Interest section.

It is essential for an orderly fund wind-up or extension experience that sufficient time is given to all stages of the process. It is crucial that the fund manager initiates the consultation process early, giving adequate notice of the procedures involved and details of new terms if an extension is proposed. It is recommended that an extension proposal should be provided ideally two years before the end of the fund, but no later than one year. Consideration should be given to the type of assets to be sold, as some will require more disposal time than others.

It is important to note that giving investors too much notice is not necessarily constructive as they may well feel that the fund manager should be focussed on asset management issues rather than considering possible events at the fund termination date. Investors should also inform the fund manager of any internal processes that may delay agreement so this can be factored into the timetable at the outset.

When a formal proposal is put forward by the fund manager, investors should ideally be allowed a minimum period of at least eight weeks to consider all the issues prior to the recommendation being put to a formal vote.

Case Study

A fund manager considering a fund extension to a large, well-performing fund decided to step back from the decision-making process and allow investors to determine the extension arrangement and update some of the terms and corporate governance. The investors formed an advisory committee as one was not already in place. Fortunately, over 90 investors were represented by only 10 advisors and six of these advisors joined the committee, chaired by the fund administrator who also acted on behalf of the other investors. The fund manager's role was restricted to an initial presentation providing recommendations and then attendance of meetings only when invited by investors.

Investor decision-making was eased by the similar profile of investors, all were keen to extend. There was also a strong level of trust between the fund manager and investors. The process was not without fault as it took a considerable length of time and investors had to process huge amounts of paperwork. However, the end result was to everyone's satisfaction and nine resolutions were approved with 100% agreement. Investors felt that they had got what they wanted and the extension agreement had not just been the product of fund manager debate with a few larger investors. The fund manager was also content with the new terms which provided more flexibility.

Best Practice: Fund managers should provide an extension proposal in a timely manner, no later than one year before fund end but ideally two years to ensure there is sufficient time to fully resolve all issues.

Best Practice: Following a formal proposal, fund managers should aim to allow investors a minimum period of at least eight weeks to consider prior to a formal vote.

It is not only the fund manager's responsibility to maintain a timely process. Investors also have a duty to ensure that deadlines are adhered to.

Best Practice: Investors should respond fully to any proposals within the timeframe provided.

It is vital to ensure there is a well thought through and planned consultation process for any fund undergoing a long-term extension. To support this objective, a suggested 'Best Practice Steps Guide for the Fund Extension Process' is provided in Appendix 3. This approach aims to:

- put investors in control, it is their capital invested;
- avoid a 'closed doors, one-to-one' focus of the fund manager and encourage collective discussion;
- allow early identification of conflicts between investors and between investors and the fund manager;
- establish regular debate; and
- ensure key decision makers and influencers from the investors are involved.

7.0 Fund Documentation: Explicit, yet Flexible

When considering winding up or extending a fund, the logical place to commence is the relevant fund documentation, to ensure correct procedures are followed. In the majority of cases the fund documentation is clear and easily understood by both investor and fund manager. However, this is not always the case and in some instances the fund documentation has not been clear, which has created distrust and confusion between the parties. For example, the definitions of applicable terms may be missing or ambiguous and the end of life processes may not be clearly defined. In many instances, the personnel from the fund manager and investors involved in discussions may be completely different from those who were engaged at the start of the fund. The fund manager should be responsible for ensuring that the fund documentation is fit for purpose with investors sharing responsibility only when negotiating terms before first closing.

Best Practice: It is the fund manager's responsibility to ensure documentation is fit for purpose.

It would appear that while a great deal of energy and deliberation is given to formalising the correct terms and procedures for the creation of a fund, the end of fund life process is not always given the same level of engagement. In addition, at the point where end of life discussions begin, the documentation can be many years old and no longer reflect best practice in the market. Best practice or commercially acceptable terms may have changed or evolved since the fund was first launched or last extended.

Fund documentation should be explicit about terms at the outset of a fund. However, it is imperative to balance that with the flexibility to offer some allowance for unforeseen events such as the global financial crisis. As stated earlier in this report, PE style fund documentation usually has clear terms documented relating to the life of the fund, although flexibility is often provided by the possibility of two one-year extensions. Institutional-style vehicle documentation will state the length of the fund life but is frequently worded to provide the flexibility for a longer-term extension. However, often it is not explicit enough to cover all the complex issues involved, to balance exiting and remaining investors' interest in all market conditions.

Investors will require additional material from the fund manager during the wind-up or extension discussion phase which includes, but is not all encompassing:

Suggested inclusions	Comment
Schedule of sales	
Individual asset business plans	To include market analysis
Fund business plan	To support any proposed extension against winding up the fund. Will also include details of administration requirements for extending and cost implications
Liquidity mechanism	For exiting investors when an extension is proposed
Exit costs for any investors wishing to remove capital from the fund	
Revised fund terms	To reflect updated corporate governance
Terms of appointment for fund manager	For the extension period, including fee proposals
Financial analysis of performance and returns	
Note on conflicts of interest and risk management	

Case Study

A well-regarded, sector-focussed fund was coming to the end of its life. There was widespread support among investors to extend and the need to modernise the fund documentation. The fund manager and investors began what turned out to be protracted discussions about the terms of a fund extension. Agreement was eventually reached, however problems arose with the pricing of units for those investors who looked to fully or partially exit the fund.

There was a lack of transparency/clarity in the documentation about specific costs that were included in the exit price calculated by the fund manager. Items were eventually included in the exit price that had not been expressly stated by the fund manager when the fund manager had initially provided worked examples of the projected redemption price without such inclusion.

The fund manager believed that they were entitled to apply the costs that were charged to exiting investors. Many investors felt that the charges were unfair and that their inclusion had been poorly communicated and the fund manager received a number of complaints from investors on the matter. The incident inevitably placed a strain on the relationship between the fund manager and investors.

This case study highlights the importance of the need for clear and transparent documentation.

While fund managers provide all the relevant documentation, it is important that investors ensure they have properly reviewed and understood all the material. The case studies in this section highlight that issues have occurred where there is ambiguity in the documentation and differing assumptions have been made. Documentation should be drafted to avoid any ‘grey areas’ where there could be differences of opinion as to how certain clauses are interpreted or applied.

Best Practice: It is the responsibility of all investors to ensure they fully read all relevant fund documentation and material provided as part of the termination or extension process.

Best Practice: It is incumbent on the fund manager to provide a clear definition of terms, particularly around the areas of liquidity, fees and exit charges.

In terms of the end of fund life, fund managers should consider the following when drafting their documentation

Issue	Management
Duration: Initial term	**Best Practice: The overriding assumption on any closed-ended fund is that the fund will wind up within the length of the fund life as stated in the fund documents. Any derogation from this assumption needs to be agreed by investors, with dissenting investors given the option to exit.** • Clearly state the date on which the fund terminates. • Clearly identify if there are any other situations when the fund can be terminated early. This could include: vote by investors; change of law relevant to the fund; NAV so low that not efficient to operate; substantial change in political, economic or monetary situation; or the equity multiple having been achieved earlier than projected. • Clarity should be given as to whether the fund manager can sell the assets early (without investor approval) thereby bringing the fund to an early close. • There should also be transparency regarding situations in which a fund life can be extended and for how long.
Return of Capital	• When assets are sold, be specific about the circumstances in which cash can be: re-invested; used to repay debt; used to redeem investors in a redemption queue; held for future capital expenditure; used for expenses; or distributed by way of return of capital. What flexibility does the fund manager have? • Be clear on the timing for distributions after an asset sale. • Check the 'distribution waterfall' reflects what is intended in relation to the fund manager receiving the carried interest. Have worked examples attached to the documents. • Be clear as to what happens to those in any redemption queue if the fund decides to wind up. • State if cash or payment in kind is a possibility. • Once the fund has decided to wind up, provide for a longstop date for return of capital but consider the need for flexibility in uncertain market conditions. Allow for any regulatory restrictions.
Short-term Extensions	• If the fund manager has the discretion to extend, the requirement for an extension should be noted in quarterly and annual reporting. • State for how long and who is responsible for the extension (fund manager or investors). • Provide a timetable for the fund manager to initiate the extension giving investors time to consider the proposals. Ensure sufficient information is provided on which a decision can be made. Provide for investor meetings to allow a forum to discuss the extension.
Key Person Clause	• The clause should cover the entire length of the fund not just the investment period because the exit process creates value. Be clear to investors who in the fund management business is responsible for the extension process. • Ensure that the Key Person commits sufficient time to the management of the fund.

Who winds up the fund	• Be clear on the regulations relating to the wind up of the fund. Reflect the role of the fund manager, liquidating trustee or liquidator, as applicable.
Fees	• Once assets are sold, the fund manager often earns no more fees but still has the tail end of the fund to deal with. Should a wind-up fee be paid for this service? This is discussed further in the Management Decisions: Be Mindful of Fund Termination Date' section.
Tail-end Liabilities	• Be clear on the provisions for making a reserve for liabilities. Be clear tail-end unknown liabilities can be insured against as a fund cost. Make clear to investors who is dealing with the wind-up of the fund; the fund manager may not be best suited. Due to the fund structure, wind-up may require a different skill set. • What is the clawback on investors' distributions in relation to on-going liabilities? • Make sure there is a limit on time and quantum. Typically, in PE funds, it is two years and 25% of distributions. The fund manager should minimise the amount of distributions that can be recalled. • Liabilities should be reported as a percentage of capital commitments to each project and in aggregate.
Carried Interest Clawback	• If there is a possibility of a clawback of distributions ensure there is a clawback on the carried interest or any performance fees. Provide timings.
No Fault Divorce Clause	• This is becoming much more common place. • A suitable voting threshold and adequate compensation offered on termination should be stipulated
Force Majeure	• Include some provision if the fund manager is unable to deal with the end of fund life under unforeseen circumstances.

For funds potentially undergoing a longer-term extension and restructuring, the following should be considered (this assumes that dissenting investors can exit following an extension vote):

Issue	Management
Declaration of Extension Possibility	• Where the fund manager has discretion to extend the fund life, the fund manager should disclose in annual and quarterly reporting throughout the fund's life whether it believes such an extension will be necessary.
Timetable	**Best Practice: Documentation should contain a clear timetable for the extension process giving sufficient time for decisions to be made. Details of the information required from the fund manager should also be provided.** • A timetable for discussions and voting should clearly be set out. This should include what information the fund manager is to provide for a decision to be made and when. Provisions should be included for consultation and meetings of investors and fund managers. The ability for investors to meet without the fund manager should be offered.
Exit Price	• Definition should include: • calculation of exit price; • details of any deductions made for costs; • when exit price is to be calculated (at time of payment, not based on earlier pricing); • clarity on how any carried interest or performance fees will be dealt with; • clarity on the ability of the fund manager to amend the exit price to reflect rising or falling market if exit price based on NAV; • ability for the fund manager to provide liquidity for exiting investors by way of a secondary market trade; • consideration if investors are to have pre-emption rights and set out how these will operate; • possible requirement to have a second valuer in place; and • the documentation should allow for sufficient time to pay the exiting investors, enabling a range of assets to be sold, not leaving the fund with poorer assets and any debt requirements are complied with.
Investor Advisory Committee	**Best Practice: At end of fund life, it is recommended that an investor advisory committee be put in place, if it does not already exist, to participate in the wind-down or extension process.** **Best Practice: Investors should have the right to be represented on an investor advisory committee if so desired. However, the composition of the committee will vary from one fund to another as ideally the fund manager will want a panel of investors that are well informed, well read and, can provide a constructive forum for the fund manager.** • Consider creating a committee for extension discussions, if not already in place. Ensure all groups of investors are properly represented.

	• It is expected that investors represent their own or their client's interests on a committee ahead of the interests of the fund as a whole. • Smaller investors should be represented by one of themselves or an independent person.
Independent Representative	• Using an experienced independent representative may be advantageous when undergoing extension discussions. • It is imperative that the right representative is chosen to avoid adding another layer to the communication process or acting as an extension of the fund manager. Ensure there is no conflict of interest and that the representative is truly independent. • Such fees should be recoverable as a fund cost.
Legal Representation	**Best Practice: Investors should be offered the opportunity to share legal representation, if it is deemed necessary, at the expense of the fund.** • In wind-up or extension cases where legal advice is necessary to resolve issues, it is recommended the fund employ a lawyer to represent all investors. This is usually a fund cost. • The fund manager may suggest a lawyer to advise investors, but the decision as to who to appoint should be made by the investors.
Voting Process	**Best Practice: The voting threshold should reflect the nature of the issue being voted on. A 75% threshold is recommended for an extension decision. However, if an investor is entitled to exit then this cannot be prevented unless they concur. A 100% voting threshold is only recommended when investors' entitlement to exit is being challenged.** • Decide on the voting threshold to extend the fund – 50%, 75%, 90%, 100% of units in issue. • Recognise 100% vote will be difficult to achieve and is not recommended except when entitlement to exit is being challenged. • 75% support is generally considered acceptable as it reflects a significant majority and recognises the difficulty of achieving 100% investor participation/support. • The timetable for the voting process should be clear. Investors should have sufficient time to consider the motion and deal with internal administration to secure the voting process. Ensure resolutions are not connected. • Clarify where voting should be off-shore and why. Ensure the best procedures are in place to achieve this. • A sensible recommendation is if the fund manager's commitment is less than 5% of fund value then the fund manager has no right to vote. • Any restrictions on the ability of 'in-house' funds of the fund manager to vote, particularly where there is a conflict, should be noted in the original fund documentation. Otherwise, these funds should not be treated differently from other investors. • Information should be in an investor-friendly format so it is simple to review. • If the fund is to be restructured, consider if resolutions should be connected or not i.e. the extension only happens if the investors agree the revised terms and fees.

These considerations may be included in the original documentation or supplied in the information given to investors at the beginning of the extension process.

Best Practice: If required, fund documentation should be modernised if the fund is extended beyond its original fund life (excluding any short-term extensions agreed in the original documentation).

Case Study

A closed-ended fund invested in shopping centres was launched in the mid 2000s and successfully raised considerable amounts of capital. However, the fund terms were not well defined in the documentation and no clear details were given about the exit mechanism or price. The longer-term goal of the fund manager was to create a fund of 'trophy assets' with a more open-ended fund structure.

An extensive portfolio of assets was created. However, the quality of the properties was variable and some investors became unhappy. The fund manager proposed splitting the fund into two, in terms of quality, but this proved unpopular. The fund was a major source of revenue for the fund manager hence there were concerns the fund manager was not always acting in the best interests of all investors. Because of the lack of explicit documentation, dissatisfied investors did not have clear sight of how they could exit the fund.

Fortunately, the investor advisory committee was very active and eventually buyers on the secondary market were found for investors wanting to leave.

It is not part of the remit of this project to suggest terms for new fund extensions. However, it is apparent that a number of areas should be given careful consideration and may require renegotiation before a longer-term extension can be realised.

8.0 Conflicts of Interest: Recognise and Manage

Conflict management is not a new topic to the real estate fund industry. There are potentially conflicts of interest at the end of a fund's life and it is important that these conflicts are declared by the conflicted party at the earliest opportunity. Below are highlighted the main conflicts of interest that are likely to arise, with examples and best practice proposals.

Best Practice: All conflicts should be declared by the conflicted party at the earliest opportunity.

It is recognised that most organisations will have their own conflict of interests' policy. However, these are often general rather than specific to a set of circumstances. Fund managers and investors should consider which conflicts of interest are relevant to the particular fund and plan how each conflict should be handled as the termination phase is reached. Potential conflicts should be reviewed regularly, during the life of the fund, to ensure that they are being appropriately managed.

When approaching the end of fund life stage, it is good practice for the fund manager to prepare a report outlining potential areas of conflict, the risks associated with them and how those conflicts will be avoided or managed. Investors and external consultants may well have conflicts in the process too. These parties should be invited to be transparent and declare their conflicts of interest, which could be added to the matrix for risk assessment, avoidance and management.

Conflict	Issues	Management

Need of the fund manager to maintain assets under management to preserve fee income.	• Fund manager pushes to extend the fund, when no clear benefit to investors.
	• Exiting investors have to undertake secondary trades rather than redemptions: issues around pricing, placement fees.
	• Strategy not fully formulated for exit on the due date.
	• Fees continue on the same basis after the end of fund life.
		Best Practice: The fund manager to have a clear business case to match strategy with the proposed extension, showing how investors' interests are enhanced.
		
		• Review fees and corporate governance terms of fund with extensions over 12 months.
		• Transparent documentation where secondary trades are the preferred route, rather than redemptions, detailing:
		  • a consistent valuation approach; a net asset value (NAV) calculation, adjustments, spread and/or discounts;
		  • pricing if market value above NAV;
		  • exit penalties; and
		  • sale fees on secondary trades.
		• Exit plan to be prepared two years before stated termination date. Fund manager and investors to declare intentions on extension or exit.
		• Some funds have a minimum asset management charge which assumes that there are assets to be managed. During the wind-up phase, when all properties have been sold, the fee may

Conflict	Issues	Management
		not appropriately reflect the amount of work the fund manager is required to undertake. It is suggested that an alternative wind-up fee arrangement is secured for this period. • If no agreed extension, consider a fee reduction if fund goes beyond end of fixed life.

The fund manager wants to maximise carried interest or performance fees. Normally this aligns investors and fund managers' interests, but there are examples, which are explained, where this may not always be the case.	• Early end of fund but investors prefer to be invested in assets.
	• Tax implications on carried interest if not treated as capital return. In the UK, legislation was recently brought in asserting that an asset held for less than three years will not benefit from capital treatment for carried interest. There is a sliding scale between 36 and 40 months.
	• With open-ended funds, any carried interest is usually on a rolling basis, often three-yearly. There are opportunities for conflicts around:
	  • returns being managed into a preferred performance period;
	  • valuations;
	  • distributions of unrealised cash;
	  • recovery from a downturn; and
	• attributing carry between incoming and outgoing investors.
		• An early exit at the right time in the market can be positive for all. State clearly in the documents if the fund can be brought to an end early by the fund manager selling the assets without investor or investor advisory committee consent. However, if investors are more concerned with property exposure rather than super profit returns consider a multiple and/or an asset level performance hurdle (IPD/MSCI) in the carry as well as an IRR return.
		• Recognise that assets held for less than four years will have implications on the carried interest. Investor reporting to be clear and transparent about the impact on carried interest so that the fund manager is demonstrating to the investors that it is putting the fund's interests first.
		• Transparency on all steps of the process from valuation through to distribution.
		• Consider rotation of the valuer with the approval of the investor advisory committee on open-ended funds and funds with a life of over eight years.
		• Do not distribute un-invested capital as income; this should be treated as capital.
		• Have clarity in the documents as to allocation of carry between investors and the fund management team. Investors' duty to understand this on their due diligence on a fund.

Conflict	Issues	Management
Sale of assets where the fund manager will continue to manage assets for the buyer	• The fund manager may be influenced to deal with a party who will continue to instruct them.	**Best Practice: Where there is a conflict of interest in the sale process, ensure an independent representative is involved, investor agreement is reached and valuations properly reflect market conditions.** **Best Practice: Declare the conflict to the investors as soon as it arises.** • If possible, consider proposals from a number of buyers to ensure best price is achieved. • Consider the appointment of an independent representative to represent the investors' interests, particularly when deciding on a proposal where the fund manager is conflicted. Investors should decide on the appointment. • Obtain an external valuation for the benefit of investors by a valuer approved by the investor advisory committee. Ensure the appointment complies with AIFMD delegation requirements. • Obtain the consent of the investors for the sale. **Best Practice: When a portfolio is to be sold and the fund manager potentially retained by the buyer, two deal teams should be created by the fund manager with information barriers in place and senior representation on each team.**
A related party to the fund manager, such as a group pension or life fund, is an investor	• In-house money has been a big feature of funds launched by institutions. This includes multi-manager teams within the fund manager's house. • The FCA in the UK and regulatory authorises in other jurisdictions have imposed strict regulations on the separation of these businesses, so it is not as critical as in the past.	• Fund managers will have their in-house policies and information barriers to comply with. Multi-manager teams should be run with independence for decision-making. • Fund managers to be vigilant that they do not provide their colleagues with more information than other investors. • Highlight presence of in-house monies investing in a fund. Emphasise any voting matters that may not be pertinent to the in-house fund manager.

Conflict	Issues	Management
Assets used to seed a new fund managed by the fund manager.	• This could include an IPO exit with part of the fund manager's business moving to an internally managed vehicle, for example, a REIT.	**Best Practice: Where there is a conflict of interest in the deal process, ensure an independent representative is involved, investor agreement is reached and valuations properly reflect market conditions.** • Obtain the consent of investors for the seeding of the new fund **Best Practice: Avoid allowing the fund manager or any investors having pre-emption rights on any asset.** • Consider the appointment of an independent representative to represent the outgoing investors' interests. The appointment should be approved by the investor advisory committee or by the investor group as a whole. • Obtain an independent external valuation for the benefit of investors by a valuer approved by the investor advisory committee.
An investor seeks to buy the fund's assets.	• An investor could acquire interests of other investors with a view to acquiring the fund's assets. • Individual assets could be sold to an investor.	**Best Practice: Where assets are to be sold to an investor(s), ensure investor agreement is reached and valuations properly reflect market conditions.** • Obtain the consent of investors (excluding the investor seeking to buy) for the sale. • Obtain an independent valuation for the benefit of investors by a valuer approved by the investor advisory committee. • Ensure all interested parties receive the same level of information.
An investor has a mandate with the fund manager across a number of investments.	• Large investors do give large mandates to a few fund managers. These investors' requirements could be given undue weight.	• Give no greater weight to that investor's views than any other similar-sized investor or group of investors in the specific fund. • Be transparent with all investors about the relationship between the fund manager and the investor's mandate.
External consultants secure more fees from extensions and	• Fund managers tend to rely on external consultants to advise on the market, legal implications, tax, procedures and governance. Consultants often offer a	• Consultants, such as lawyers, accountants and tax advisors, will be governed by the strict regimes within their own governing body on how to handle conflicts of interest. • Be mindful of the consultant's advice, but need to bear in mind that the key priority is the commercial case for extending the fund or winding it up.

Conflict	Issues	Management
restructures than fund terminations.	recommendation on the course of action to take.	• Additional advisory costs should not be de facto charged to the fund. In such cases, it may be more appropriate to charge part to the actual fund manager.
Consultants become independent representatives on their recommendation for independence.	• Independent representative to represent the investors or steer the fund manager around the conflicts of interests can be vital and add value to the whole process. • This will be an additional cost to the fund.	**Best Practice: Consider carefully the appointment of an independent representative who has had any prior professional connection with the fund and could be seen as an extension of the fund manager.** **Best Practice: Investors to approve any independent representative to the board of the general partner, fund manager's investment committee or the investor advisory committee for the fund.**

Case Study

As the wind-up period for a fund approached, it became evident that a portfolio sale offered the best disposal route for assets. The portfolio was marketed externally and a number of prospective buyers came forward, one an existing investor in the current fund. This created a conflict between investors, being sellers and a potential buyer. Further, an additional conflict was established as the prospective buyer wanted to retain the fund manager to manage the portfolio.

The fund manager informed investors of the potential conflict at a very early stage. In addition, two teams were set up within the fund manager's organisation to manage the process, one handing the selling process and the other, the buying process. Information barriers were created so effectively the teams acted as two separate companies and both teams were led by suitably senior management. Investors, including the independent chair, were satisfied with this arrangement and the deal went ahead, with the purchasing investor paying slightly over valuation for the portfolio, ahead of other offers received.

Case Study

Documentation of a fund approaching the end of its life contained a pre-emption right for the fund manager to buy out the existing investors. Investors were aware of this clause but the original documentation had been poorly drafted such that a conflict of interest had potentially arisen.

It transpired that the fund manager was seeking a new investor to buy the portfolio and retain the fund manager to continue to manage the assets. There were concerns from the original investors that the fund manager may not look to achieve best price for them. Investors were concerned that it may be in the fund manager's interest to recommend a price to existing investors below fair market value as this would potentially enhance the performance of the prospective client going forward.

There was also a concern that some information may be withheld from other potential external buyers, providing the fund manager with a commercial advantage. In the end, investors insisted that multiple agents be asked to provide a sale valuation price and then one be employed to support the fund manager in selling the portfolio on the open market.

This situation could have been avoided if the original trust documentation had anticipated a potential conflict of interest around the pre-emption right of the fund manager and suitable wording been included to avoid it.

9.0 Management Decisions: Be Mindful of Fund Termination Date

When making any type of management decision throughout the life of a fund, it is important for the fund manager to be mindful of the fund's termination date. A wind-up or extension is much more straightforward and timely if all the elements of the fund, for example, asset sales or debt arrangements, are resolved before the fund ends or appropriately structured for an extension. However, there are circumstances when this is not possible and the fund manager should consider how best to ensure procedures are not unduly delayed by unresolved or ill-timed issues.

This section of the report outlines issues that the fund manager should consider that may cause concern at the end of fund life if not reconciled or additional provision established. These issues may arise at fund creation, during the life of the fund or as the fund is coming to the end of its life.

Strategic Issues and Timings

The strategy of a fund is usually defined when the fund is created and outlined in the original fund documentation. Considerable thought is usually given to formulising the initial strategy and this is then commonly employed as one of the main marketing tools of a fund. However, it is just as imperative to give consideration to strategic issues arising in the final stages of the fund as these may impact on how easily and quickly a fund is wound up. As this can be many years out, there should be a level of flexibility given to deal with unforeseen events.

A timetable of the main fund events should be provided with the original fund documentation which includes a timeline for end of fund life procedures.

The fund manager may want to consider the following points when devising the strategy and timings for a fund:

Issue	Management
Fund Strategy	**Best Practice: Any potential change in fund strategy that may cause a delay in the end of fund life process should be communicated to all investors at the earliest opportunity. Investors should decide if the additional value creation is worth the postponement.** • The end of fund life may not always be the ideal time to sell assets for a number of reasons, for example, poor market conditions, incomplete business plans or additional value creation opportunities. The fund manager should communicate this to investors at the earliest opportunity. Investors may decide they want liquidity and will accept a lesser price or give the fund manager more time to maximise value. • Both the fund manager and investors may decide on a change of strategy as they wish to continue to exploit assets in very successful funds. A more open-ended fund may therefore be created. • Any potential requirement for additional capital from investors to maximise realisable returns should be communicated as soon as possible.
Individual Asset Plans	**Best Practice: Ensure individual asset plans are completed and maximum value created before the end of the fund's life.** • When acquiring development or added value opportunities, the fund manager should ensure there is sufficient time to extract maximum value from the site before the end of the fund life.
Timetable of Events	• To be provided as part of fund documentation. • The fund manager should communicate intentions regarding a fund expiry/potential extension well in advance of the fund termination date.
Investment Restrictions	• During the wind down process, fund documentation should state that investment restrictions that may have previously operated will no longer apply.

Sale of Assets Process

It is the case for most funds that the majority of assets are sold as the fund approaches the end of its life. The main aim of the sales process should be to return all funds to investors and wind up all the vehicles, with no liabilities remaining, in a timely manner. The fund manager should consider the following when approaching a large sales programme:

Issue	Management
Market timing	• The fund manager should be cognisant of the impact of market conditions on the sale of assets. • A prolonged market downturn may result in a fund being extended rather than wound up to avoid selling assets at the bottom of the market. • See also Fund Strategy above.
Timetable of Sales	• Ensure a clear timetable of sales is provided to investors. Keep updated to reflect any changes in the agenda. • Be aware of bank holidays in all jurisdictions involved.
Sales Strategy	• Consider who the most likely buyers of the fund's assets are and tailor the sales strategy accordingly, particularly if overseas investors are involved. • Ensure assets are marketed to reflect their key characteristics and attractions, for example, a portfolio with high vacancy may be considered an 'opportunity' fund given the potential upside. • Review whether a portfolio sale or an individual asset sale programme is most appropriate. A portfolio sale may allow for a quicker wind-up and poorer quality assets may be combined with stronger properties that may be difficult to sell in isolation. Depending on market cycles, a portfolio sale may achieve higher or lower prices compared to selling off assets individually.
Conflict of Interests	• The fund manager should declare any conflicts connected with asset sales as soon as they arise. • Any agent or broker approached to advise on the sale of assets should declare any conflicts as soon as they arise. • If the fund manager has any pre-emption rights, they must ensure that all prospective purchasers are provided with sufficient and identical information. • Conflicts of Interest are covered in more detail in the previous section of the report.
Selection of Broker	• Consider approaching at least four brokers to ensure the most suitable is selected. • Multiple brokers may be employed if the fund manager can demonstrate that this will maximise value and liquidity for investors.
Transaction Team	• Ensure experienced negotiators are in place with extensive knowledge of the relevant assets. This may be an in-house team or from a broker.
Data Room/Site	• Ensure the Data Room/Site is well prepared and organised. All relevant documentation should be up-to-date and provided upfront.
Warranties on Sale	**Best Practice: Avoid creating liabilities that run beyond the end of fund life. If this is not possible, ensure appropriate action is taken to make certain the fund is wound up as soon as possible.**

	• On the sale of a property asset where land is transferred, warranties are not given as a rule. However, it is standard practice on a sale of an asset in a holding structure to give sellers warranties on the holding structure. The warranties fall into three categories: capacity, corporate and tax.
	  • A capacity warranty is just warranting that the seller and vehicle exist and that the seller has capacity to transact.
	  • A corporate warranty relates to the vehicle and includes matters such as compliance with laws during its life and not having liabilities other than those disclosed.
	  • A tax warranty is warranting there are no liabilities to tax other than what has been disclosed.
	• All warranties have a time period in which a claim has to be made and there is always a minimum and maximum claim amount. The time period would normally go beyond the end of the fund life. For example, in the UK up to three years for corporate warranties and six years for tax warranties is fairly typical.
	• Solutions for dealing with these liabilities are:
	  • Clawback from investors. The provision will be in the original documentation. This is common in PE funds but unusual in core or open-ended vehicles. A fund cannot be wound up until all matters are resolved.
	  • Hold back distributions from investors. Again the fund cannot be wound up until all matters are resolved. It is unsatisfactory for investors' money to be withheld for a significant period. It is difficult to know how much to hold back.
	  • Insurance. Replace the fund's liability as the seller with buyer side insurance. The seller pays the insurance premium as a deduction from the sale price. Insurance is capped to a realistic amount of the potential liability. With insurance in place, the buyer has no claim against the seller and fund can be wound up. See Appendix 4 – End of Fund Life Insurance.

Legal and Tax Advice	• Ensure legal and tax advisors are consulted to address and clarify any issues ahead of the sales process. • Be aware of any changes in tax law or other regulatory issues.
Additional Performance Fee	• Where a fund manager does not qualify for performance related fee and is relinquishing a meaningful annual management fee as assets are sold, additional incentivisation may be considered. • This is unlikely to be acceptable to many investors.

When a fund is to be extended and there are exiting investors, a partial sale of assets may be required. The fund manager may want to consider the following issue:

Issue	Management
Composition of a partial sale	**Best Practice: In situations where a fund is extended but assets are to be sold to provide liquidity to exiting investors, the fund manager must ensure that it treats both exiting and continuing investors fairly.** • This can potentially be a very contentious situation as the best assets are easiest to sell. This could leave the fund with weaker assets, maybe those that cannot be sold at their valuation. The exiting investor will be paid out on NAV and if the assets sold are not meeting their valuation, this will disadvantage continuing investors. The fund manager must be very careful to ensure the assets can be sold at their valuation. • The documentation should allow sufficient time to pay out the exiting investors so a range of assets can be sold, not leaving the fund with poorer properties. • In adverse market conditions, where sale prices cannot achieve their valuation, consideration should be given to adjusting the exit price if this is permitted in the documentation. Adverse market conditions can be defined in a number of ways, including through markets falling, queue size, difficulty in pricing, variance between the secondary market and exit price being greater than 10%.

Debt Issues

Many funds have debt facilities and fund managers of these funds therefore have additional issues to consider. When establishing a debt facility for a fund, the fund manager may want to deliberate on the following:

Issue	Management
Flexibility	**Best Practice: The fund manager should seek maximum flexibility, weighed against cost, for any debt facility.** • Maximum flexibility on debt facilities should be sought by the fund manager, whether the aim is to wind up a fund or extend it. Deliberation needs to be given to the cost for this flexibility. • Consider revolving credit facilities or loans on an asset-by-asset basis rather than at fund level or on a pool of assets
Debt Facility Expiry Date	• Consider a co-terminus arrangement with the expiry date of the fund.
Compliance	• When considering additional debt, the fund manager should be aware of compliance or non-compliance with LTV covenants already in place.

As a fund approaches the end of its life, and particularly if an extension is proposed, the fund manager may also want to consider the following issues relating to debt:

Issue	Management
Reduction in Debt Levels	• As an expiry approaches, the fund manager may consider reducing gearing levels, particularly if there is the possibility of partial equity redemptions if a fund is to be extended (potentially leading to higher LTV levels).
Breakage Costs	• The fund manager should be mindful of loan or swap breakage costs as fund expiry approaches. • How can they be minimised?
Debt Strategy	• Consider a review if the fund is to continue and there is a change of structure or strategy (such as from closed-ended to open-ended or evergreen)
Additional Equity Requirement	• The fund manager may need to request additional equity from investors to rectify debt problems.
Impact on Performance	• The fund manager should be aware of any debt terms that may impact on fund performance following an extension (such as non-utilisation fees).
Liquidity Provision	• The fund manager may need to consider how to provide liquidity for any exiting investors if there is a fund extension. • The use of leverage is one way to offer liquidity and potentially avoids asset sales if secondary market buyers are not forthcoming. However, it will result in higher LTV levels and, in markets where values are falling, may disadvantage remaining investors. It is therefore not commonly used to provide an exit strategy.

Fund Administration

There are administration issues that can have the potential to cause problems and delays when a fund is being wound up if due care is not taken. These issues may occur at any time during the fund life and are not necessarily restricted to the end of fund life period. The fund manager should consider the following issues:

Issue	Management
Rental Guarantees	• If a rental guarantee on a sale is required and the arrangement runs beyond the end of the fund life, consider capitalising the cost and deducting off the asset sale price to ensure there is no outstanding liability.
Asset Management Fees	**Best Practice: During the end of fund life process, asset management and wind-up fees should appropriately reflect the amount of work required**. • Asset management fees are usually based on funds under management. When an asset sale programme has been completed, at least a year of administration is required to wind up the fund following the sale, so the fund wrapper can be collapsed. The fund manager needs to ensure that either a wind-up fee is received to reflect this work or the on-going asset management fees include a charge to cover this period. • Some funds have a minimum asset management fee in place which assumes that there are assets to be managed. During the wind-up phase, when all properties have been sold, the fee may not appropriately reflect the amount of work the fund manager is required to undertake. It is suggested that an alternative wind-up fee arrangement is secured for this period.
Holding Vehicles	• If holding vehicles in the fund structure are not sold with the asset, ensure any nominees or special purpose vehicles are wound up at point of asset sale and not retained until end of fund life. There is a risk that the vehicle will be forgotten and will then take administration time to strike off or liquidate. • It takes approximately three months to strike off a vehicle once an application has been filed. Liquidation will take longer and is considerably more costly.
Tax Issues	• The fund manager should try to ensure any open items with the tax authorities are resolved as unnecessary delays may arise. (Sometimes these items can be covered with insurance but it can be unduly expensive.)
‘Stub’ Position Acquisition	• In a number of instances fund managers are realising that there are merits in a fund structure being internalised, with investors being bought out at a slight discount to valuation to their de minimis holding, so as to ensure that these ‘stub’ positions are extinguished quickly.

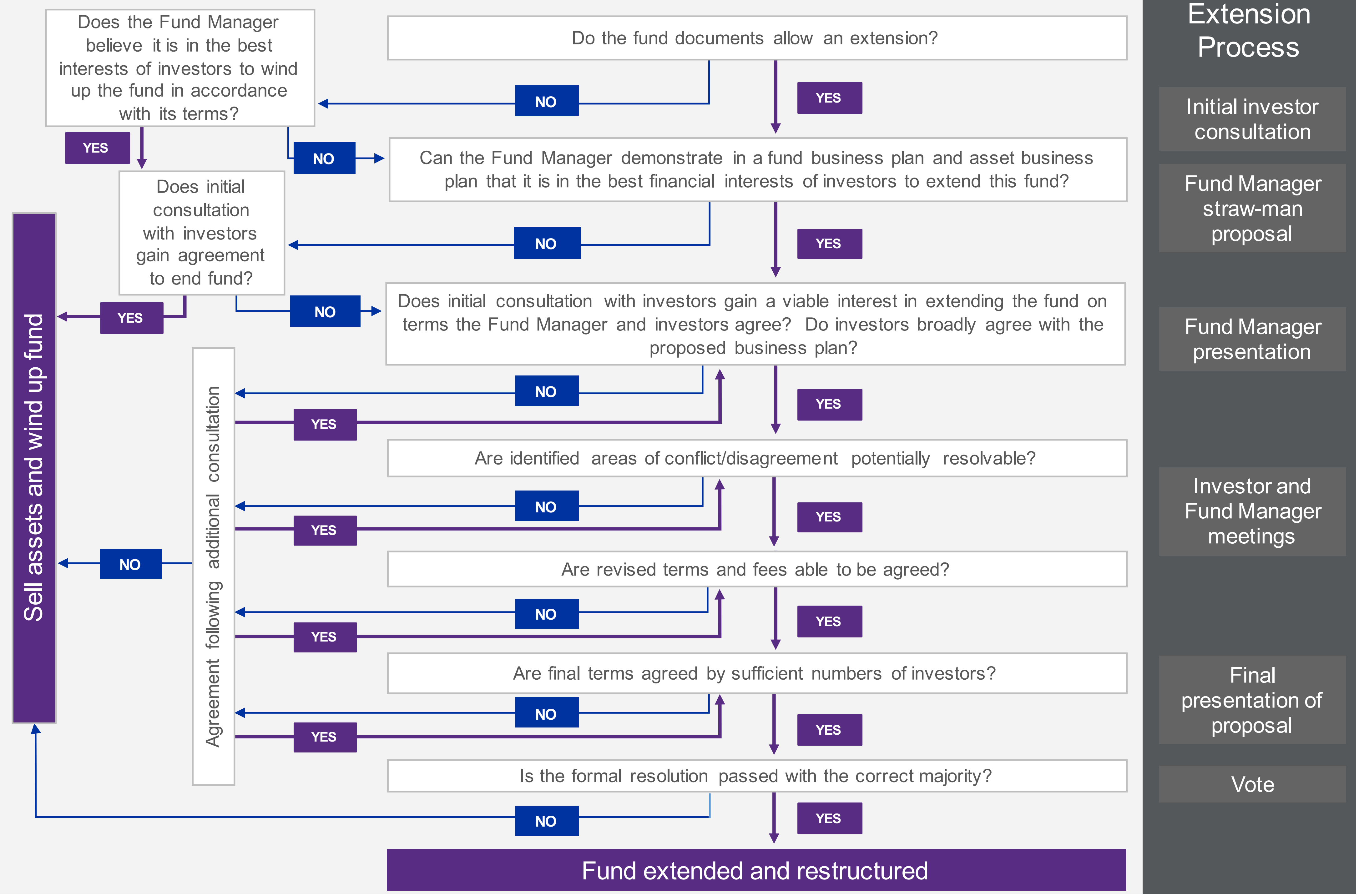
Appendix 1 – Best Practice Guidelines

Guidelines		Ranking
1.	**Communication, transparency and timeliness**	
1.1	All investors should receive the same level of written information.	**1**
1.2	All written information should be provided to investors simultaneously.	**2**
1.3	Both fund manager and investors are obliged to ensure suitably senior management time is given to the end of fund life process and that they are actively engaged in the consultation process.	**2**
1.4	Where possible, an alternative senior manager (appropriately experienced) is responsible for the extension process rather than the individual fund manager.	**3**
1.5	Unless there is very good reason, an investor should have a consistent, documented house view of a fund shared by all personnel involved.	**2**
1.6	Fund managers and investors should fully engage in any consultation process and ensure it is as transparent as possible.	**1**
1.7	The fund manager should be prepared to wind up the fund unless agreement is reached.	**2**
1.8	Investors should have the right to meet without the fund manager to discuss proposals.	**2**
1.9	Fund managers should provide an extension proposal in a timely manner, no later than one year before fund end but ideally two years to ensure there is sufficient time to fully resolve all issues.	**2**
1.10	Following a formal proposal, fund managers should aim to allow investors a minimum period of at least eight weeks to consider prior to a formal vote.	**2**
1.11	Investors should respond fully to any proposals within the timeframe provided.	**2**
2.	**Explicit yet flexible fund documentation**	
2.1	It is the fund manager's responsibility to ensure documentation is fit for purpose.	**1**
2.2	It is the responsibility of all investors to ensure they fully read all relevant fund documentation and material provided as part of the termination or extension process.	**2**
2.3	It is incumbent on the fund manager to provide a clear definition of terms, particularly around the areas of liquidity, fees and exit charges.	**1**
2.4	The overriding assumption on any closed-ended fund is that the fund will wind up within the length of the fund life as stated in the fund documents. Any derogation from this assumption needs to be agreed by investors, with dissenting investors given the option to exit.	**2**
2.5	Documentation should contain a clear timetable for the extension process giving sufficient time for decisions to be made. Details of the information required from the fund manager should also be provided.	**1**
2.6	At end of fund life, it is recommended an investor advisory committee be put in place, if it does not already exist, to participate in the wind-down or extension process.	**2**
2.7	Investors should have the right to be represented on an investor advisory committee if so desired. However, the composition of the committee will vary from one fund to another as ideally the fund manager will want a panel of investors that are well informed, well read and can provide a constructive forum for the fund manager.	**2**

	2.8 Investors should be offered the opportunity to share legal representation, if it is deemed necessary, at the expense of the fund.	**3**
	2.9 The voting threshold should reflect the nature of the issue being voted on. A 75% threshold is recommended for an extension decision. However, if an investor is entitled to exit then this cannot be prevented unless they concur. A 100% voting threshold is only recommended when investors' entitlement to exit is being challenged.	**1**
	2.10 If required, fund documentation should be modernised if the fund is extended beyond its original fund life (excluding any short-term extensions agreed in the original documentation).	**2**
3.	**Recognition and management of conflicts of interest**	
	3.1 All conflicts should be declared by the conflicted party at the earliest opportunity.	**1**
	3.2 The fund manager to have a clear business case to match strategy with the proposed extension, showing how investors' interests are enhanced.	**2**
	3.3 Where there is a conflict of interest in the sale process, ensure an independent representative is involved, investor agreement is reached and valuations properly reflect market conditions.	**2**
	3.4 When a portfolio is to be sold and the fund manager potentially retained by the buyer, two deal teams should be created by the fund manager with information barriers in place and senior representation on each team.	**2**
	3.5 Avoid allowing the fund manager or any investors having pre-emption rights on any asset.	**3**
	3.6 Where assets are to be sold to an investor(s), ensure investor agreement is reached and valuations properly reflect market conditions.	**2**
	3.7 Consider carefully the appointment of an independent representative who has had any prior professional connection with the Fund and could be seen as an extension of the fund manager.	**2**
	3.8 Investors to approve any independent representative to the board of the general partner, the fund manager's investment committee or the investor advisory committee for the fund.	**2**
4.	**Management decisions: be mindful of fund termination date**	
	4.1 Any potential change in fund strategy that may cause a delay in the end of fund life process should be communicated to all investors at the earliest opportunity. Investors should decide if the additional value creation is worth the postponement.	**1**
	4.2 Ensure individual asset plans are completed and maximum value created before the end of the fund's life.	**2**
	4.3 Avoid creating liabilities that run beyond the end of fund life. If this is not possible, ensure appropriate action is taken to make certain the fund is wound up as soon as possible.	**2**
	4.4 In situations where a fund is extended but assets are to be sold to provide liquidity to exiting investors, the fund manager must ensure that it treats both exiting and continuing investors fairly.	**1**
	4.5 The fund manager should seek maximum flexibility weighed against cost for any debt facility.	**2**
	4.6 During the end of fund life process, asset management and wind-up fees should appropriately reflect the amount of work required.	**2**

Rankings: As part of the workshops, delegates were asked to give a ranking to each of the best practice guidelines from 1 to 5 (with 1 being Very Important, 3 being Relevant and 5 being Irrelevant). All the rankings were collated to give a single rank for each guideline.

Appendix 2 - Overview of Consultation Process



Appendix 3 – Best Practice Steps Guide for the Fund Extension Process

Stage	Action	Recommended Timing
Pre-Proposal	**Initial Investor Consultation**	**Up to two years before formal vote**
	Purpose: Fund manager 'listening stage' to gain a broad understanding of investor requirements. May involve 1:1 meetings or a questionnaire No information is imparted by fund manager at this stage	
Stage 1	**Fund Manager Straw-man letter proposal**	
	Purpose: To provide initial proposal to all investors simultaneously in writing. A comparison should be made between the cases for extension and termination. **Information provided:** • Fund business plan • Individual asset business plans • Financial analysis of performance and returns • Fund manager conflicts and risk management • Proposed timetable	
Stage 2	**Fund Manager Presentation**	**c. 4 weeks after Stage 1**
	Purpose: To present draft proposal to all investors and seek agreement to pursue extension or termination and identify principal areas of conflict between fund manager and investors. If required, fund manager may propose an investor chairman (may be independent). The appointment should be agreed by investors.	
Stage 3	**Provision of Detailed Proposal**	**c. 2 weeks after Stage 2**
	Purpose: To provide additional information in writing once the draft proposal to extend has been accepted. **Information provided:** • Liquidity mechanism • Costs for exiting investors • Revised fund terms	

	• Terms of appointment for fund manager	
Stage 4	**Investor Meeting**	**c. 2 weeks after Stage 3**
	Purpose: For investors to discuss and negotiate detailed proposal amongst themselves and identify their own conflicts and possible solutions. Fund manager attends by investor request only, possibly to present detailed proposal. Minute proposals from meeting shared with all investors and fund manager.	
Stages 4b/c/d	**Additional Investor Meetings (as required)**	
	Purpose: To provide additional occasions for investors to discuss detailed proposal. Fund manager has the opportunity to respond to each meeting's proposals and provide revised proposals for discussion	
Stage 5	**Presentation of Final Proposal**	
	Purpose: To present final proposal to investors following investor meetings.	
Stage 6	**Vote**	**At least 8 weeks after Stage 3**
	Investors have a minimum 10 days to respond.	

Appendix 4 – End of Fund Life Insurance – A Strategic Alternative?

When the decision is made to wind up a fund there are a number of issues that the fund manager will have to deal with. One of these is how to address any residual liabilities that remain within the fund. This is where an End of Fund Life ("EFL") insurance policy can provide significant benefit and ensure a clean exit.

A fund, when disposing of assets whether by corporate or asset sales, will be left with numerous contingent liabilities that have either arisen out of the acquisition agreement (e.g. warranties and indemnities) or remained with the selling entity after an asset sale. Some of these residual liabilities will expire during the period of disposals and the time it takes to wind up a fund but some, for example, those arising in relation to tax or title under a share purchase agreement, will have a longer tail (typically seven years). It should also be noted that an allegation of fraud, however unfounded, can potentially mean that the time limit for warranty or indemnity claims is disapplied.

Unexpected tax liabilities can arise and prevent distributions to investors or otherwise prevent a liquidation. They can arise several years after disposals of fund assets due to the time taken to file returns and for the authorities to start an enquiry. The enquiry can then take a number of years to resolve given tax authorities' high profile willingness to litigate tax disputes in recent years.

Such contingent liabilities can mean that the liquidator of the fund is unable or unwilling to wind up the fund. They can also give rise to concerns that such liabilities could fall, or be alleged by a third party to fall, on investors, fund managers and/or other parts of the fund manager's portfolio. Any such allegation will give rise to defence costs which are not properly chargeable to other parts of the fund manager's portfolio.

Ideally, warranty and indemnity ("W&I") insurance can be utilised strategically on a deal-by-deal basis to mitigate the residual liabilities and ensure that the seller's liability is minimal, or negated, and any recourse is directly against the insurer. However, this is often not the case and some legacy exposure remains, especially in relation to the most recent transactions where a significant number of the warranties and indemnities are yet to expire.

A solution to these issues would be for the fund manager to hold funds in escrow until such liabilities have expired and then look to wind up the fund. However, the consequences of this is that investors will have to wait longer until these residual liabilities have expired before they can realise their full investment and incur additional administration costs.

An alternative solution would be to put in place an EFL insurance policy to 'wrap up' any residual liabilities into an insurance policy. The insurer would therefore become liable for these liabilities enabling the remaining entities to be wound up. It can therefore enable prompt distributions to investors and protect the fund's IRR. The policy can also name a liquidator as a policyholder which can provide liquidators with the protection they seek in order to allow an orderly wind up of the fund. As most funds use offshore structures, tidying up the group by removing redundant entities saves often significant running costs and management time in maintaining that structure.

An EFL policy is essentially similar to a seller-side W&I insurance policy. The chosen insurer would due diligence the fund structure, the history of the assets, the disposals and the remaining liabilities, including those warranties and indemnities that are still 'alive'. It will analyse the intended winding up process and, in particular, concentrate on the tax exposures. In addition, the insurer will request any third party advice and have an 'underwriting call' with the manager and any relevant third party advisers to gain as much information as possible.

Appendix 5 – Wind-up Process Guide for Common Fund Vehicles

When a fund is terminated, the corresponding vehicle(s) should be wound up.

While asset holding vehicles may be sold as part of the sales process, it is unusual that the fund vehicles are sold as part of the exit route. Therefore, the fund manager needs to address the processes involved.

This appendix is a technical guide setting out the issues and procedures for some of the most common fund vehicles: Jersey Unit Trusts, English and Scottish, limited partnerships, German limited partnerships and Luxembourg Special Investment Funds.

Jersey Unit Trust

1. Introduction

There is no public register of Jersey Unit Trusts (JUTs) in Jersey and minimal law applies to the creation, operation and termination of a JUT. JUTs are regulated almost exclusively by the terms of their trust instrument and to which regard must be had in determining: the procedure for terminating and thereafter winding-up a JUT; and distributing its assets.

The JUT wind-up process, and therefore the time required to wind-up, will depend on two main factors:

- the number of investors. Is the JUT a single key investor holding vehicle, a joint venture or a club or multiple investor fund vehicle?
- the number and type of assets held. For property funds using a JUT, the assets will typically consist of property with some cash/income. There may be complex arrangements in place in relation to past and future liabilities that need to be unwound.

The JUT could be the fund vehicle, a feeder to a limited partnership that holds the fund assets or an asset holding vehicle that has not been sold with the property in it.

It is imperative that any meeting of investors required as part of the termination and wind-up process should be physically held in Jersey so as not to prejudice central management and control of the JUT being exercised offshore, and consequently the income tax transparency and offshore status of the JUT.

2. Triggers to Wind Up

The termination and resulting wind-up of a JUT may occur as a result of any of the circumstances set out in the Triggers section at the front of this report or specified events set out in the trust instrument.

3. Sequence of Steps

The procedure for terminating and winding up a JUT will commonly involve the following steps:

3.1 Step 1 – ‘Decide’ to Terminate

Termination of a JUT commences with either:

- the express decision of the trustee, fund manager or investors when the natural life of the fund has come to an end and the fund manager and investors have not agreed to extend the life of the fund; or
- automatic termination caused by a trigger event.

The wind-up process commences on termination of the JUT and the JUT continues to exist as a matter of law until all its debts (if any) have been discharged and all assets have been distributed to investors.

An investors' ‘decision’ must be evidenced as taking place in Jersey, by holding an investors' meeting in Jersey.

The trustee will be independent of the fund manager and it is prudent, from a commercial point of view, to secure the cooperation of the trustee, especially if wind-up and handover procedures in the trust instrument are not clear.

3.2 Step 2 - Pre-dissolution Considerations

If the fund is not to be extended, the best practice recommendations should still be followed as part of the wind-up process. This will include good communication with investors by the fund manager on the processes involved and the timing on the return of capital and final distributions.

This checklist is an indication of matters requiring action and/or consideration but is not exhaustive:

- Notifications. Notice of termination will need to be given to investors, service providers (administrator, property manager, investment manager, fiscal agent and managing agent), government authorities (Jersey Financial Services Commission (JFSC)), insurers, lenders and third parties.

- Consents. Has any investor used its interest in the JUT as security which requires the prior consent of the lender before that investor is able to vote for the JUT's termination? Does the JUT need prior consent from any of its lenders?
- Appointments. No liquidating trustee is required to be appointed.
- Terminations of Service Providers. Do any contracts with services providers automatically terminate? Do they require an ordinary resolution of investors (in Jersey) to terminate, novate or waive notice periods.
- Corporate Authorisations. Are any meetings of investors and the trustee (in Jersey) required? What are the resolution thresholds?
- Valuations. Identify any property assets which have not been sold and obtain independent valuations. Usually these can be prepared by the appointed valuer of the JUT.
- Ascertain Liabilities. Identify current and expected future liabilities, including permitted/revenue expenses, capital/income items and estimated wind-up costs. Check historical documentation to confirm there are no on-going liabilities. In particular check there are no outstanding warranty liabilities on past sales that have not expired and are not insured. Consider establishing a cash pool in order to provide a prudent reserve for contingent liabilities or obtain an insurance proposal to cover the potential liabilities.

3.3 Step 3 - Realise Assets

Following the decision to terminate, the JUT's assets may be distributed in specie but it is more usual that cash proceeds are distributed from the sale of those assets. Typically, one to two years will be provided for this process and fund managers should comply with the best practice recommendations to ensure investors receive regular updates on the sale process.

If investors have already agreed not to extend the fund, the sales should take place during the given wind-up period. If this does not happen, depending on the wording in the fund documents, the trustee, fund manager or investment advisor could be in breach of their obligations. This is a point that needs to be considered on drafting – what happens if the assets are not or cannot be sold in the given period and the investors have not consented to an extension?

From a tax perspective, extreme care should be taken to ensure that the decision to terminate and sell assets is not seen as taking place prior to any formal meetings in Jersey and therefore on-shore in a tax jurisdiction.

3.4 Step 4 - Discharge Liabilities

It is very important to carefully analyse the accounts of the JUT prior to termination and to ensure there are sufficient assets to discharge present and future liabilities. The estimated costs of winding up a fund i.e. legal and administrative costs should be provided for in the accounts. Doing this in advance can avoid additional delays during the wind-up process. Identified liabilities can be settled, insured or assigned. This will assist in avoiding the trustee requiring a retention to meet liabilities that may arise after the JUT assets have been distributed.

If the JUT to be wound up is a property-owning JUT, it is important to ensure that all property matters have been dealt with and that there are no inherent liabilities which remain in the JUT.

3.5 Step 5 – Filings

There is no Jersey law requirement for any advertisements to be placed with creditors or for any filings to be made. The JFSC should be notified that the JUT has been terminated and wound up.

3.6 Step 6 – Distribute Any Remaining Cash and Income

Once the trustee is satisfied that all liabilities of the JUT have been discharged it will usually hold a final meeting and resolve to distribute any remaining cash/income to investors. This generally takes place one to two years after termination.

3.7 Step 7 – Trustee Indemnity

Under Jersey law, a trustee may require reasonable security for liabilities whether existing, future, contingent or otherwise before distributing the final cash from the JUT. The form of such security is usually an indemnity in favour of the trustee from the investors and could be up to 10 years. This requirement is not going to be acceptable in a fund situation as investors could be numerous and would not be prepared to take on this ‘tail liability’.

There are three possible solutions:

1. The trustee accepts there are no on-going liabilities and no indemnity or retention is required. This does sometimes happen.
2. The trustee retains a retention to meet potential liabilities. As these, by their nature, are unknown it is difficult to quantify and a trustee could ask for it to be held for 10 years.
3. The fund manager arranges insurance to cover the risk. This is becoming more popular.

3.8 Step 8 – Finalise Accounts

Subject to the terms of the trust instrument, the trustee will usually prepare closing accounts detailing the JUT's assets and liabilities (if any) at the end of the wind-up process.

English and Scottish Limited Partnerships

1. Introduction

The limited partnership deed should set out the circumstances in which a limited partnership can be terminated, for example a limited partnership may terminate on a set date or after a set term, on the direction of an agreed majority of the limited partners or on the disposal of all limited partnership assets.

While a limited partnership may have terminated under the terms of the limited partnership deed, it will not be formally wound up until the termination has been registered at Companies House.

Importantly, the future liability of the partners will remain until the termination has been advertised, both publicly (through the publication of a London or Edinburgh Gazette notice, as appropriate) and privately to any third parties who may have dealt with the limited partnership in the past. The dissolution of the limited partnership will not extinguish any historic liabilities of the limited partnership. The timings and complexity in winding up limited partnerships can vary depending on the nature of the underlying assets.

2. Triggers to Wind-Up

The termination and resulting wind-up of a limited partnership may occur as a result of any of the circumstances set out in the Triggers section at the front of this report or specified events set out in the limited partnership agreement.

3. Sequence of Steps

The procedure for terminating and winding-up a limited partnership will commonly involve the following steps:

3.1 Step 1 – 'Decide' to Terminate

The limited partnership terminates in accordance with the limited partnership deed and although the limited partnership will cease to be a going concern during the wind-up process, it will continue to exist as a matter of law until all its debts have been discharged and the termination has been registered at Companies House.

3.2 Step 2 – Pre-dissolution Considerations

It is important that the operator/fund manager, as liquidating trustee, deals with all matters required to be dealt with prior to the dissolution of the limited partnership to ensure that the dissolution is not delayed for any reason. Below is a checklist of matters which the operator/fund manager must consider/action.

If the fund is not to be extended, the best practice recommendations should still be followed as part of the wind-up process. This will include good communication with investors by the fund manager on the processes involved and the timing on the return of capital and final distributions.

Once the assets of the limited partnership have been sold, this checklist is an indication of matters requiring action and/or consideration but is not exhaustive in all cases:

- Liquidating Trustee. A liquidating trustee should be appointed to realise the assets of the limited partnership on termination and to distribute the proceeds to the partners in accordance with the limited partnership deed. The limited partnership deed may provide for the operator/fund manager to be appointed. Winding up a collective investment scheme is a regulated activity so the liquidating trustee must hold the relevant permissions.
- Outstanding Liabilities. All outstanding liabilities should be settled.

- Distributions. To the extent possible, distributions of all cash balances in the limited partnership, other than capital contributions, must be completed before any documentation formalising the dissolution is entered into. Distributions should be made in accordance with fund documentation.
- Cash Pool. The liquidating trustee may wish to consider establishing a cash pool in order to provide a prudent reserve for contingent liabilities. Sometimes the fund documentation will have clawback provisions for unknown liabilities which mean a reserve may not be required.
- Capital Contributions. The limited partners must not be repaid their capital contributions prior to dissolution as that will affect their limited liability status. Usually the capital contribution is a nominal amount and the balance of investment is loan contribution which can be repaid.
- Gazette Notice. The partners will continue to be liable for future debts of the limited partnership until a notice of the dissolution of the limited partnership (the 'Gazette Notice') is filed with the London or Edinburgh Gazette. It is also recommended that all third parties who have dealt with the limited partnership in any capacity are notified in writing of the pending dissolution
- Third Party Notices. All third parties with whom the limited partnership has dealt with should be identified so that Third Party Notices can be sent to them.
- Value Added Tax De-registration. This should be dealt with.
- Other consents. Consider if any other consents are required, for example, the lender.

3.3 Step 3 – Realise Assets

Following the decision to terminate, the limited partnership's assets may be distributed in specie but it is more usual that cash proceeds are distributed from the sale of those assets. Typically, one to two years will be provided for this process and fund managers should comply with the best practice recommendations to ensure investors receive regular updates on the sale process.

If investors have already agreed not to extend the limited partnership, the sales should take place during the given wind-up period. If this does not happen, depending on the wording in the fund documents, the general partner, fund manager or investment advisor could be in breach of their obligations. This is a point that needs to be considered on drafting – what happens if the assets are not or cannot be sold in the given period and the investors have not consented to an extension?

3.4 Step 4 – Discharge Liabilities

Once terminated, the liabilities of the limited partnership must be confirmed in the closing accounts of the limited partnership, which will be agreed by the general partner and/or the operator/fund manager with the assistance of the limited partnership's auditors.

Creditors of the limited partnership (if any) should be approached. Any outstanding debts of the limited partnership should be settled prior to the dissolution, to reduce the number of contingent liabilities.

If the limited partnership is to be wound up before all of its debts have been discharged, then any debt owed by the limited partnership could be assigned to its general partner. Notice must be given to any debtor of the limited partnership of the assignment of the debt. This is unusual and would normally be dealt with by setting aside a reserve fund to be held by the operator/fund manager, to settle any historic (as opposed to future) liabilities.

Assuming that the limited partnership to be wound up is a property owning limited partnership, it is important to ensure that all property matters have been dealt with and that there are no inherent liabilities which remain in the limited partnership. For example, any contractual warranties and environmental reports should be assigned, together with all property assets and rights. Also, check that any historic structuring issues have been dealt with (for example, all nominee companies have been dealt with, any 'resting on contract' legacy issues are clear).

3.5 Step 5 – Board Meetings and Approval of Documents

The general partner will need to hold a board meeting to approve:

- the dissolution itself;
- a letter of notification of the termination of the limited partnership and of direction to the operator/fund manager to act as liquidating trustee of the limited partnership (where relevant) (the 'Letter of Direction');
- notice of termination from the liquidating trustee to the limited partners (the 'Notice of Termination');
- the Gazette Notice;
- the Third Party Notices;
- the Form LP6;
- the termination of the operator's agreement in accordance with the limited partnership deed (or otherwise); and
- the Deed of Termination (if required).

Once the board meeting has been held:

- The minutes should be signed by the chairman of the meeting.
- The Letter of Direction should be signed by the general partner and sent to the liquidating trustee.
- The liquidating trustee should send the Notice of Termination to the limited partners.
- The Gazette Notice should be signed by the general partner.
- The Form LP6 should be signed by the general partner.
- The Third Party Notices should be signed by the general partner and sent to the relevant limited partners.

3.6 Step 6 – Distributions to Partners

The limited partnership deed will set out the order in which distributions are to be made to the partners and the liquidating trustee will arrange these payments.

3.7 Step 7 – Filing Notices and Form LP6

The Gazette Notice will be sent to the London or Edinburgh Gazette to be published in the next possible publication and a Companies House form LP6 (Form LP6) should be filed at Companies House at the end of the wind up period.

It should be noted that following the filing of the Form LP6 at Companies House, limited partnerships are not removed from the Companies House register. Further, Companies House does not amend its on-line records to show that a limited partnership has been dissolved. However, the paper records at Companies House show that the dissolution has taken place and no third party limited partnership is then able to re-use the limited partnership's name or registration number.

3.8 Step 8 – Operator's/Fund Management Agreements

These agreements will need to be terminated and may in fact terminate automatically on the dissolution of the limited partnership i.e. on the filing of the Form LP6.

3.9 Step 9 – Filing of Accounts

The Regulations provide that final accounts must be prepared and filed for the final accounting period of the limited partnership.

Unless the limited partnership is ‘small’ or dormant (as defined in the Companies Act) or exempt under Regulation 7 of the Regulations (i.e. it prepares consolidated accounts with the General Partner), it has to prepare and file audited accounts at Companies House on its dissolution. If the limited partnership prepares consolidated accounts under Regulation 7, it will still need to have these audited but they will not need to be filed at Companies House.

The limited partnership agreement should be checked for any specific provisions, whether a consolidation exemption applies or not, and the final accounts prepared accordingly.

German Limited Partnership

1. Introduction

In general, a German Limited Partnership, set up as a fully regulated closed-end investment limited partnership under the German 'Capital Investment Act' ('Geschlossene Investment-KG' gemäß KAGB) will be terminated as of the set date under the limited partnership agreement or upon a specific majority decision by the shareholders/investors of the German Limited Partnership (limited partnership).

Importantly, the future liability of the partners will remain until the limited partnership is dissolved. The dissolution of the limited partnership will not extinguish any historic liabilities.

2. Triggers to Wind-Up

The termination and resulting wind-up of a limited partnership may occur as a result of any of the circumstances set out in the Triggers section at the front of this report or specified events set out in the limited partnership agreement.

3. Sequence of Steps

The procedure for terminating and winding up a limited partnership will commonly involve the following steps:

3.1 Step 1 – 'Decide' to Terminate

The limited partnership terminates in accordance with a limited partnership agreement and although the limited partnership will cease to be a going concern during the wind-up process, it will continue to exist as a matter of law until all its debts have been discharged and the set termination has been registered with the local commercial trade register at the seat of the company.

3.2 Step 2 – Pre-dissolution Considerations

Depending on the regulations of the limited partnership agreement, the general partner or the managing limited partner will act as liquidator of the limited partnership. Below is a checklist of matters which the managing limited partner (future 'liquidator') must consider.

If the fund is not to be extended according to a specific majority vote of all shareholders/investors, best practice recommendations should still be followed as part of the wind-up process. This will include good communication with investors by the fund manager on the processes involved and the timing on the return of capital and final distributions.

Once the assets of the limited partnership have been fully sold, this checklist is an indication of matters requiring action and/or consideration but is not exhaustive in all cases:

- Liquidator. A liquidator should be appointed to realise the assets of the limited partnership on termination and to distribute the proceeds to the (limited) partners in accordance with the limited partnership agreement. In some cases, the limited partnership agreement will provide for the managing limited partner or the general partner to be appointed as a liquidator.
- Outstanding Liabilities. All outstanding liabilities should be settled.
- Distributions. To the extent possible, distributions of all cash balances will be made to the partners. Distributions should only be made in accordance with the fund documentation. If, for any reason, distributions shall be made differently from the fund documentation, the required majority vote of the partners/investors is required.
- Capital Contributions. The limited partners must not be repaid their capital contributions prior to the dissolution as that may affect their limited liability status. Usually the capital contribution is a nominal amount and the balance of investment is a contribution which can be repaid.
- Deletion from Local Commercial Register. The entering into the liquidation process has to be registered with the locally competent German commercial register at the seat of the partnership. The final dissolution, after full payments and discharge of all liabilities (including

tax and all others), also has to be registered with such a German commercial register.

3.3 Step 3 – Realise Assets

Following the decision to terminate, the limited partnership assets may be distributed in specie (also depending on the terms of the limited partnership agreement) but it is much more usual that cash proceeds are distributed from the sale of those assets. Depending on the type of assets and the (real estate) market conditions, the sale of the assets can easily take one to two years or even more and fund managers should comply with the best practice recommendations to ensure investors receive regular updates on the sales process. Such updates will, as a general rule, always be provided at an investment committee or shareholder meeting on a regular, mostly yearly, basis. In specific cases, such updates will be given more regularly during the ongoing sales process of the limited partnership assets.

3.4 Step 4 – Discharge Liabilities

Once terminated, the liabilities of the limited partnership will be set out in the closing accounts of the limited partnership, which will be agreed with the general partner and/or the liquidator with the assistance and the final confirmation by the limited partnership auditors, to the extent they exist.

Creditors of the limited partnership (if any) should be approached. Any outstanding debts of the limited partnership should be settled prior to the dissolution, to reduce the number of contingent liabilities, if feasible.

Assuming that the limited partnership, to be wound up, is a property-owning limited partnership, it is important to ensure that all property matters have been dealt with and that there are no inherent liabilities which remain in the limited partnership. For example, any contractual warranties and environmental reports should be either settled or assigned to another entity, together with all property assets and rights. This, however, may only be executed, as a general rule, if any creditor rights/claims are not limited by such action.

3.5 Step 5 – Shareholder Meetings and Approval of Documents

The fund manager/limited managing partner will need to hold shareholder meetings to approve:

- the liquidation dissolution itself and the appointment of the general partner or managing limited partner as liquidator of the limited partnership, unless already stated specifically in the limited partnership agreement;
- the registration of liquidation of the limited partnership in the locally competent commercial register; and
- the termination of the operator’s/fund manager’s agreement in accordance with the limited partnership agreement (or in accordance with all shareholders/investors of the limited partnership, based on a majority vote).

Once the shareholder meeting has been held:

- the minutes should be signed by the chairman of the meeting;
- the minutes should be sent to all shareholders/investors of the limited partnership; and
- the appointment of the liquidator should be sent to the commercial register for registration.

3.6 Step 6 – Distributions to Partners

The limited partnership agreement may set out the order in which distributions are to be made to the partners; the liquidator will arrange for these payments.

3.7 Step 7 – Operator/Fund Management Agreements

This agreement will either need to be terminated or may in certain cases terminate automatically under the dissolution of the limited partnership or prior to that.

3.8 Step 8 – Final Accounting

The final accounts (the 'Accounts') must be prepared and filed for the final accounting period of the limited partnership. Generally, such final accounts will also be published in the German Federal Gazette ('Bundesanzeiger').

If the limited partnership agreement regulates auditing of the (final) accounts of the partnership, such final accounts still have to be audited before their publication.

The limited partnership agreement should be checked for any specific provisions, whether consolidation exemption applies or not, and the final accounts prepared accordingly.

Note: When a German closed-end public investment KG is wound up, the liquidator has to prepare a winding-up report on a yearly basis and as of the exact day when the total liquidation process is terminated (see Section 161 of the German Capital Investment Code/KAGB). The specific requirements of Section 158 of the German Capital Investment Code must also be complied with.

As a general rule, the limited partners/investors will not be liable after the termination of the limited partnership for any liabilities of the closed-end investment limited partnership (see Section 161, Subsection 3 of the German Capital Investment Code/KAGB).

Luxembourg Special Investment Fund

1. Introduction

All Luxembourg Investments Funds are regulated vehicles and under the supervision of the Commission de Surveillance du Secteur Financier (CSSF); they must obtain authorisation from the Luxembourg regulator before the investment vehicle is launched.

Historically, two regulated Luxembourg investment vehicles have been used by real estate fund managers: the UCIs Part II under the 2002 Luxembourg Fund Law and the Special Investment Fund (SIF) under the 2007 Luxembourg Fund Law. More recently, limited partnerships have become available and are gaining popularity. This report focuses on the termination process of SIFs during the period 2010–2015.

The Offering Memorandum and all the agreements (investment management, depository and central administration agreement) set out the circumstances of terminating a SIF vehicle. There are two types of termination in Luxembourg: voluntary and judiciary termination.

Closed-ended vehicles set a clear date of termination that can be further extended for a short period of time, upon approval by the CSSF. The sale of the assets under management takes place normally before the vehicle is wound up.

The SIF wind-up process, and therefore the time required to wind-up, will depend on two main factors:

- the number of (remaining) shareholders of the SIF. SIFs that have only one (remaining) ultimate shareholder/unitholder may be dissolved if the shareholder decides to dissolve. If this is the case, a liquidator is not required; however, the SIF auditor is necessary to issue an independent report on the financial statements of the SIF covering the period from the beginning of the accounting period to the beginning of the liquidation period. The dissolution of the SIF is formalised by a notarial deed. If more than one shareholder exists upon liquidation, a liquidator is appointed, whose main responsibility is to realise the assets and to settle the liabilities.
- the number and type of assets held. For property funds using a Luxembourg SIF, the assets will typically consist of property with some cash/income. There may be complex arrangements in place in relation to past and future liabilities that need to be unwound.

2. Triggers to Wind-Up – Termination Decisions

The termination and resulting wind-up of a limited partnership may occur as a result of any of the circumstances set out in the Triggers section at the front of this report or specified events set out in the offering memorandum.

3. Sequence of Steps

The procedure for terminating and winding-up a SIF will commonly involve the following steps:

3.1 Step 1 – ‘Decide’ to Terminate

A SIF terminates in accordance with the Offering Memorandum and agreement with all services providers. Although the SIF will cease to be a going concern during the winding-up process, it will continue to exist as a matter of company law and remain registered by the CSSF until all its assets have been disposed of and all its debts discharged. Finally, the termination is registered at the CSSF and at the Trade Register (Registre de Commerce des Société).

3.2 Step 2 – Pre-liquidation Considerations

If a SIF is not to be extended at the end of its life, best practice recommendations should still be followed as part of the wind up process. This will include good communication with investors by the fund manager on the processes involved and the timing on the return of capital and final distributions.

It is important that the fund manager deals with all matters required to be dealt with prior to the liquidation of the SIF vehicle to ensure that the liquidation is not delayed for any reason. Initial considerations to follow are:

- a review of NAV and assess value of assets in the context of liquidation;
- an assessment of liquidation costs and the proper recording of NAV;
- analysis of specific transactions close to the liquidation date; and
- analysis of related party transactions and significant redemptions.

3.3 Step 3 – Realise Assets

Following the decision to terminate, the SIF's assets may be distributed in specie but it is more usual that cash proceeds are distributed from the sale of those assets. Depending on the type of liquidation, typically up to one year will be provided for this process and the liquidator should comply with the best practice recommendations to ensure investors receive regular updates on the sale process.

Once the assets of the fund have been disposed, the following checklist is an indication of matters requiring action and/or consideration but is not an exhaustive in all cases:

- Liquidator. A liquidator should be appointed to realise the assets of the SIF on termination and to distribute the proceeds to the investors in accordance with the offering memorandum. Winding up a collective investment scheme is a regulated activity so the liquidator must hold the relevant permissions.
- Outstanding Liabilities. All outstanding liabilities should be settled.
- Distributions. To the extent possible, distributions of all cash balances in the SIF, other than capital contributions, must be completed before any documentation formalising the liquidation is entered into. Distributions should be made in accordance with fund documentation.
- Contingent Liabilities and Assets. The liquidator may wish to consider establishing an escrow account in order to provide a prudent reserve for contingent assets and liabilities. Sometimes the fund documentation will have clawback provisions for unknown liabilities which mean a reserve may not be required.
- Capital Contributions. Capital contribution to the limited partners takes place upon liquidation.
- Memorial Publication. A notice of the liquidation is filed with the Luxembourg Memorial after the first notarial meeting is held. All third parties who have dealt with the SIF in any capacity are notified in writing of the pending liquidation.
- Third Party Notices. All third parties with whom the UCI has dealt with should be identified so that Third Party Notices can be sent to them.

3.4 Step 4 – Discharge Liabilities

Once terminated, the liabilities of the SIF must be confirmed in the closing accounts of the fund, which will be agreed by the liquidator with the assistance of the SIF's auditors.

Creditors of the SIF (if any) should be approached. Any outstanding debts of the SIF should be settled prior to the liquidation, to reduce the number of contingent liabilities.

Assuming that the SIF to be wound up is a property owning real estate fund, it is important to ensure that all property matters have been dealt with and that there are no inherent liabilities which remain in the fund. For example, any contractual warranties and environmental reports should be assigned, together with all property assets and rights.

3.5 Step 5 – Board Meetings and Approval of Documents

The fund will hold a board meeting to approve:

- the liquidation of the fund; and
- the proposal of an agenda for the extraordinary general meeting (shareholder meeting to be held in front of a notary) to appoint a liquidator and agree the date of the liquidation.

Once the board meeting has been held and the liquidator is appointed, then the liquidator takes charge of the fund termination process.

3.6 Step 6 – Filing Notices

The minutes of extraordinary general meeting are filed with the Trade Register (RCS).

3.7 Step 7 – Third Party Agreements

The agreements with third parties originally signed by the fund will need to be terminated on the date of liquidation.

3.8 Step 8 – Preparation of the Liquidation Accounts

At the end of the liquidation, the final liquidation accounts are prepared by the liquidator and form part of the overall liquidation report.

3.9 Step 9 – Second Extraordinary General Meeting

During this meeting, the shareholders validate the liquidation report and provide discharge to the liquidator, to the external auditor and to the members of the board. A copy of the minutes of this meeting is filed with the Trade Register and the CSSF.

3.10 Step 10 – Distributions to Investors

The liquidator will determine, according to the law, the order in which distributions are to be made to investors. The liquidator will arrange for these payments to be made.

Participants in the End of Fund Life Project

The Sponsors

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AREF

INREV

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The Project Team

The Project Team took responsibility for identifying guiding principles and best practice guidelines for this project, as well as being interviewed.

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Representatives from the following organisations kindly gave their time to be interviewed.

Aviva Investors	Nabarro LLP
AXA Real Estate Investment Managers	Northern Horizon Capital
Aztec Group	Oak Street Real Estate Capital
Blue Sky Group	Pramerica Real Estate Investors
Bouwinvest Real Estate Investment Management	Provinzial NordWest Asset Management GmbH
pbb Deutsche Pfandbriefbank	Rockspring
Europa Capital Partners LLP	Schroders Property Investment Management Limited
Harrison Street Real Estate Capital	SGG Group
HSBC Global Banking and Markets	TH Real Estate
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