Appendix 1: Partners Group Overseas Property Portfolio Structure

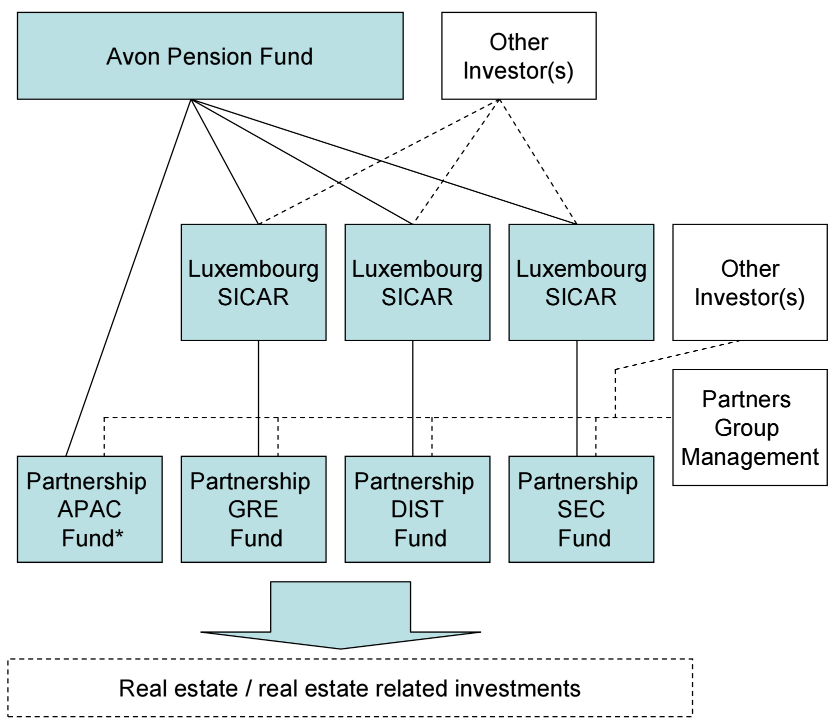
Approach

The investment approach adopted by Partners Group is to invest in closed end funds with a finite life, typically 10 – 12 years, similar to that which is commonly used with private equity investments. This is designed for long term investors but the main disadvantage is that the investment is less liquid than an open ended property fund (where the client may buy/sell units at any time). This structure does have several advantages, for example, the investment program is not disrupted by large scale redemption requests and it enables the manager to invest across different "vintage" years. A "vintage" year refers to the year in which the committee capital is drawdown and invested. By investing across different years the manager is able to "market time" a particular investment across the property cycle rather than invest all the capital at the same time. This contrasts to more liquid assets such as bonds and equities, where managers are able to market time the investment cycle on a constant basis.

Legal Structure

The closed end fund is in the form of a Scottish limited partnership. Were it not for the need to minimise the Fund's tax administration burden (which can be significant for property in some overseas jurisdictions), the Fund would be investing directly in the partnership. However, since the Avon Pension Fund (APF) wishes to minimise the tax payable and avoid the time and effort involved in recovering with-holding tax on its income, particularly from the United States, it has invested in the Partnerships via a SICAR (Societe d'investissement en capital a risqué), i.e. the SICAR serves as a 'feeder fund' and is a limited partner in the Partnerships, not the APF. The advantage of this is that the manager of the SICAR will take responsibility for tax recovery on a corporate basis. Only in the case of investment in Asia-Pacific & Emerging Markets, where there is less withholding tax that can be reclaimed and recovery is easier, will the APF be investing directly in a Partnership. The structure is summarised in Figure 1 below.

Fig1: **Structure of APF investments with Partners**



*NB APF invests directly in the APAC Fund Partnership.

Notes:

APF invest in a pooled 'feeder' vehicle, a SICAR.

The SICAR invests in a Limited Partnership which is the master fund. As such, the SICAR itself becomes a partner in the Partnership.

Each SICAR only invests in one individual Limited Partnership (APF have investments with 4 limited partnerships, 3 via SICARs, 1 directly).

Each Limited Partnership invests in various property funds and direct assets, and realises those assets within a 10 -12 year period.

Each Partnership is managed by a 'general partner'. In each case this is Partners Group.

A Partnership is similar to a fund of funds in that it will invest principally in a range of funds. The General Partner invests money which it has received from the Limited Partners in instalments (so-called capital calls or drawdowns) during its investment period, sells the investments within a finite period and then returns cash to the Limited Partners. Where the Partners Group funds invest in underlying real estate funds, these underlying funds (i.e. portfolio funds of the Partners Group funds) operate in the same way. In the case of the Fund's overseas property investment Partners Group are the General Partner. The Limited Partnerships in which the Avon Pension Fund has invested have a finite life of 10 – 12 years with a facility to extend this by three one-year extensions if not all investments have been realised by the underlying partnerships during the initial term of 10 – 12 years. In practice investments may be realised at any time but will normally be held for at least 5 years.

All 3 SICARs have independent auditors (PwC), custodians (KBL European Bankers) and registrars (Kredietrust). The Asia-Pacific & Emerging Markets Limited Partnership is audited by PwC.

Implications for Control

In addition to the tax advantages, this legal structure has the following implications for control:

i) Termination in the event of underperformance

In the event of underperformance, the Avon Pension Fund has a limited course of action. The only way of terminating the mandate is to transfer the Fund's interests in the Partnership to a third party. However, this facility may be more theoretical than real because the probability of a third party wishing to invest with an underperforming manager is not high.

This is mitigated by the fact that cash is automatically returned to investors when an investment is sold and there is some scope to reduce our holdings with Partners Group by choosing not to re-invest this cash with them. In these circumstances, if the Fund wanted to maintain its overseas property exposure, it would have to appoint a new manager.

ii) Representation and control of the SICAR

Legally, the SICAR is required to be 50% owned by the manager (i.e. the equivalent of a general partner in connection with a limited partnership) (who is Partners Group). Accordingly, a SICAR issues manager shares and ordinary shares which carry each one vote per share. This means that Partners Group are potentially able to exercise a majority of votes and theoretically control the SICAR as well as advising on the investment strategy. In practice they have agreed to vote their 50% share in line with the will of the majority of the other investors. Further, the manager must have regard to its fiduciary duties as manager of the SICAR.