

### Overview

- **Crocker Partners Fund IV** – We continue our disciplined approach to investing by patiently waiting on the sidelines for market pricing to reflect market realities. Recent activity indicates that the initial deals to emerge will be highly structured transactions involving defaulting loans, rather than traditional fee simple purchases. Due to the current dislocation in the capital markets, we believe that these value-add opportunities will provide us with outsized opportunistic returns. Deal volume should dramatically increase in 2011-13, during which period there should be a confluence of record debt maturity defaults, weak real estate market fundamentals, and a relatively small amount of capital available to recapitalize these transactions.
- **Property Trades** – The Fourth Quarter experienced a modest uptick in the volume of sale activity in the commercial office market, although the levels remained anemic. Stabilized assets and/or those located within core submarkets experienced the most success. Disappointed sellers eventually pulled most of the other marketed properties when pricing failed to meet their unrealistic expectations.
- **Debt Markets** – The most notable change in our industry has been the revival of the debt market. This is not to say that we are anywhere near the 2007 heyday; rather, modest levels of debt are now available for stabilized, cash-flowing assets. Nonetheless, for all practical purposes, the refinancing market remains non-existent due to these significantly lower debt proceeds. With respect to maturing debt, lenders continue to “kick the can down the road” by providing borrowers with loan extensions to avoid marking down the value of their mortgages and risking insolvency. In October, the FDIC supported this novel approach to balance sheet management by issuing regulations that encourage lenders to maintain existing loan values.<sup>1</sup>
- **Real Estate Market Fundamentals** – Vacancy rates continue to climb toward historic highs and effective rents remain between 20% and 35% off peak rates. Fundamentals should continue to weaken over the next 12 to 24 months due to the abundance of currently leased but unutilized space that will return to market as the underlying leases expire. Since we expect

employment gains to be weak for several years, we do not anticipate that most of our markets will stabilize until 2014-15.

### ILPA – Private Equity Principles

The recent massive decline in private equity fund values has led to a reexamination of the prevailing private equity partnership structure and many participants (chiefly institutional investors) believed that in certain instances this structure failed to ensure the following primary goals:

- Alignment of Interests** (e.g., certain general partners garnered substantial profits from asset management fees despite a precipitous decline of the value of the underlying fund assets);
- Governance** (e.g., certain general partners made decisions that were inconsistent with the original investment strategy of the fund); and
- Transparency.**

As a result, the Institutional Limited Partners Association has promulgated the “ILPA Private Equity Principles” to provide best practices.<sup>2</sup> Crocker Partners has reviewed these principles and supports the vast majority of them (*see next page*).

### About Crocker Partners

Crocker Partners is a private equity fund manager that invests capital in office product located in primary submarkets along the East Coast of the United States. We are currently investing capital on behalf of Crocker Partners IV, a closed-end fund focusing on value-add and opportunistic office investments located within the Southeast U.S.



Our investors include some of the largest and most respected institutional investors in the world.

<sup>2</sup> For a copy of the principles, please visit the ILPA website, <http://www.ilpa.org>.

<sup>1</sup> <http://www.fdic.gov/news/news/financial/2009/fil09061.html>

The ILPA Private Equity Principles consist of three core concepts - the alignment of interests between fund sponsors and investors, sound governance, and greater transparency - that suggest a number of practices and terms designed to further dialog among fund sponsors and investors. Crocker Partners considers this a worthy objective and a benefit to investors and fund sponsors. Indeed, many of the suggestions are consistent with the terms reflected in our current fund and the manner in which Crocker Partners conducts business. In the spirit of contributing to these discussions, we have outlined our thoughts on certain of the suggested terms from our perspective as an emerging manager.<sup>‡</sup>

### Alignment Of Interest

- Joint and Several Clawbacks – This structure would impose a substantial burden on the less wealthy individual senior management team members who could be “wiped out” due to a default by a larger partner. Each individual partner, however, will personally guaranty his portion of the clawback.
- Management Fee Structure – As a smaller fund manager, we rely on asset management fees to cover overhead expenses and the cost to raise and operate our funds (including any placement agent fees). The only profits we generate from asset management fees are to compensate management for the risk-based capital used to finance the reasonable overhead costs. As an example, the size of the general partners’ investment in our management company is already twice as large as our substantial limited partnership investment. The only other fees we charge to the limited partnership are market-based leasing and property management fees.

### Governance

- Do Not Throw the Baby Out With the Bath Water – Although we agree with many of these general principals, we do not support those that would eviscerate the base structure of the fund vehicle (*e.g.*, the ability to terminate the fund or management based on a simple majority vote or the ability to remove managers on alleged bad acts without due process or cure rights), place a large burden on the shoulders of management (*e.g.*, limiting their indemnification rights), or unduly restrict the ability of management to operate a discretionary fund (*e.g.*, although we agree to the importance of time-diversification, we could not agree to fixed caps – concerns over manager discretion should be crafted into the fund’s mandate upon formation). Our managers make significant long-term personal commitments to the operation and management of our funds and many of our investment strategies are long-term (5 to 7 years). Designing a fund structure that would allow an arbitrary early termination of the fund or prevent management from making investments that are in the best interest of the fund would unjustly deprive management and the non-voting limited partners the ability to maximize their returns. ***Built-In LP Protections Exist*** – The super-majority voting rights already provided to the limited partners (those that require 75% or 80% of the vote) to remove management, prematurely end the investment period, or wind-down the fund without cause provide the necessary protections to the limited partners without hamstringing management’s ability to maximize fund returns.
- Other Issues
  - Regarding amendments to the limited partnership agreement, we agree that material amendments should require super-majority consent, but non-material amendments should only require a simple majority vote.
  - The external auditor of the fund should be able to provide tax services for management since it would pose no conflicts and provide substantial efficiencies.

### Transparency

We support all of the transparency goals set forth in the ILPA standards; however, the respective limited partner may prevent us from disclosing the terms of a side letter agreement.

<sup>‡</sup> This update does not modify the terms set forth in the Crocker Partners Fund IV operative documents or otherwise alter the rights or obligations of any person thereunder or impose any new obligations on Crocker Partners or its affiliates.