DEVELOPMENT OF REAL ESTATE FUNDS IN EUROPE AND LITHUANIA

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Due to the growing economy in Lithuania as well its a rapid integration into the European Union and global markets, improvement of the investment process in real estate has been and will continue to be a topic of great interest. The article presents an analysis of the investment process in real estate. It aims at presenting a theoretical and practical evaluation of real estate as an investment object. To this end, the first part of the paper singles out the most important concepts related to real estate, compares real estate with other types of investment, analyses real estate in the investment portfolio. The second part explores the importance of real estate investment funds in order to ensure an efficient and expansive functioning of the investment market in the European Union and to expand the Lithuanian market of investment goods. It also investigates the legal basis and development of real estate funds in the European Union. Lithuanian legislation provided a possibility for real estate funds to operate only at the end of 2007: on 15 November 2007 a new edition of the Law on Collective Investment Undertaking of the Republic of Lithuania was adopted, stipulating a possibility for specialized funds to appear in Lithuania from 1 March 2008.

Key words: *real estate, collective investment, investment portfolio, real estate investment funds*

Introduction

In theory and practice, the classification of real estate is based on different criteria and described in different senses. The Property Valuation Methodology (1996), effective in Lithuania, describes property as "economic resources that have a value and an owner and are disposed by an economic entity". Real estate is a type of property defined as "a land and related objects the place of which cannot be changed without changing their use or reducing their value and economic use, or property that is recognized by law as such".

Real estate can also be perceived as a physical object (land and its appurtenances, i.e. structures), legal (legally, real estate encom-

passes all property interests, privileges and rights related to ownership of physical real estate) or economic category. More detailed definitions of real estate help to have a comprehensive perception about the nature and characteristics of this specific type of property, however, in practice there is no so strict division among conceptions, and real estate is usually realized as a physical object with legal and socio-economic features. This approach is also common while analysing the real estate market which may be described as a certain set of mechanisms according to which property rights and related interests are transferred, prices set and different land uses distinguished (Galiniene, 2004). The real estate market may be analysed by various sections: types of real estate, regions, the nature of operations related to real estate, etc. A concrete distinction of real estate enables a more accurate determination of real estate value (Galiniene et al., 2006).

The article *aims* at providing a theoretical (real estate as an investment object) and practical analysis of investments into real estate (real estate funds). To this end, it compares real estate with other investment instruments, examines real estate allocation in the investment portfolio and investigates diversification strategies inside the real estate portfolio. The last section of the article analyses the instrument of real estate fund as one of the possible means of investments into real estate, presents the regulation peculiarities of the abovementioned funds in the European Union (hereinafter – the EU) and Lithuania. The article also employs such methods as systemic comparative analysis and synthesis of scientific literature, comparative historic analysis and deduction.

Real estate as an investment object

Investments into real estate

Real estate is ascribed to one of the main investment instruments. Traditionally, five key investment instruments are distinguished: 1) deposits and cash (an instrument of the monetary market is considered to be an instrument that can be turned into money in a short period of time and without any losses to the equity invested. Instruments of the monetary market are cash deposits in banks, Treasury bills (short-term – up to one year – securities), and units of monetary market funds); 2) shares (equities provide the investor with certain rights, e.g. to participate in the company's management, i.e. vote in general meetings of shareholders, a right to dividends, a right to a share of the company's assets remaining after its liquidation, etc.); 3) bonds (debt securities); 4) real estate (residential buildings, flats, land, commercial buildings – warehouses, offices, shopping malls, etc.).

Financial assets related to real estate confirm ownership of real estate as well as a right to income and benefits provided by them. Such financial assets as shares or bonds do not reflect national welfare and affects the national output capacity indirectly, meanwhile tangible property is a function of output capacity: it is land, buildings, machinery used for the creation of good (Zvie et al., 2005)

Table 1 (composed according to Geltner and Miller, 2000, VPK) presents a comparative characteristics of four investment instruments by risk, general average profitability, average growth, protection from inflation and liquidity.

A comparison of investment instruments enables making a deduction that according to the risk and profitability characteristics, real

*Table 1. **Characteristics of investment instruments***

	Instrument of monetary market	**Shares**	**Bonds**	**Real estate**
Risk	Low	Average or high	Low or average	Low or average
Profitability	Low	Average or high	Low or average	Average
Average Growth	None	Big	None	Small
Protection from inflation	None	Good	None	Good
Liquidity	High	Average or high when the company is in the Exchange Lists; low when shares are not included in the Exchange Lists	Depends on conditions in the market; however, the liquidity of the Government's securities is usually high	Low

estate is between the low risk and profitability level of deposits and cash and the high risk and profitability level of shares. In this respect, real estate is more similar to bonds; however, it distinguishes itself by small growth and a relatively good protection from inflation.

Real estate allocation in the diversification of real estate portfolio

Real estate, with its exceptional characteristics, plays a very important role among other investment instruments also because of the fact that the allocation of real estate as an alternative investment instrument into the investment portfolio increases diversification possibilities.

Acknowledging the benefit of real estate allocation into the investment portfolio, scientists raise a question of *what real estate allocation* should be in the modern investment portfolio. In different papers, the answer to this question varies from 0% to 67%. In 1986, D. Hartzell (1986) defined 3%-11%, to be the ideal limits, meanwhile P. Firstenberg, S. Ross and R. Zisler (1988), S. H Irwin and D. Landa (1987), R. B. Gold (1995) and H. R. Fogler (1984) all argued for 15% to 20% allocations. Nevertheless, later studies of such authors as B. J. Ziobrowski and A. J. Ziobrowski (1997) settle that real estate allocation in comparison with other property classes, should be even from 20% to 30%. More immoderate allocation, percentages were given by J. R. Webb and J. H. Runbens (1987) who argue for at least 43% of the whole investment portfolio. At the extreme, J. R. Webb. R. J. Curcio and J. H. Rubens (1988) have indicated that real estate gets two-thirds of all assets.

As a result, the answer to the question why empirical testing reveals such a variety of real estate allocations is related to the specificity

of the real estate itself (Seiler et al., 1999). Different authors distinguish different characteristics of investments into real estate that should be evaluated. Summarizing (Kencerevycius, 2004; Gitman, Joehnik, 1996; Geltner, Miller, 2000; Galiniene, 2004) a list of the most important ones may be provided:

1. *The specificity of real estate as a commodity* – the uniqueness of the market object (commodity): this feature may be divided into two parts: a) exceptional attention to the residential real estate, the characteristics of which are examined more often and more accurately in comparison with other commodities; b) the complexity and unrelatedness of a commodity – real estate requires exceptional rights.

2. *Risk* – in a log-term perspective the profitability of investments into real estate is unpredictable, however, in comparison to other investment instruments, it can be described as low or average (see Table 1).

3. *Liquidity* – in comparison to other commodities, the liquidity of real estate is low (see Table 1). There are two types of liquidation aspects: a) qualitative – it depends on demand in the market; b) quantitative – each market type has a different time of realization. It is related to other peculiarities of real estate – uniqueness and a need for capital.

4. *Investment time horizon* – two aspects of this feature may be distinguished: a) prices of real estate goes up and down sometimes slowly, sometimes fast; therefore, it is important to foresee for what time of period you invest – whether it is a short-term investment with a hope that prices will increase or a long-time investment taking into account regional perspectives, population increase and other factors that have an impact on the real estate market; b) real estate is intended for a long-term use, therefore, all physical changes in real estate appear because of the time factor.

5. *The investor's experience and management skills* – investments into real estate require specific knowledge: most decisions in the real estate market are made taking into account subjective criteria; usually, real estate agreements are closed, so the nature of real estate is "untransparent".

6. *Physical characteristics* – when acquiring real estate it is always necessary to evaluate its quantitative as well as qualitative features because a physical object may have a lot of different modification possibilities.

7. *Geographical location* – the real estate market is bound to a certain place/location.

8. *High demand for equity*– investments into real estate require material, financial and human resources.

9. *Real estate may be a commodity at any stage of its life cycle* – it means that the commercial market may sell not only objects that are completed, but also those that are not. The utility of unfinished construction objects is equal to 0; however, in most cases this does not prevent real estate from being a commodity.

It should be noted that the greatest drawback of investments into real estate is its low liquidity which usually provides investors with flexibility considering capital flows as well as a capability to use new opportunities. Another very important aspect of traditional investments into real estate is the level of risk. Nevertheless, it should be mentioned that the real estate market is not indiscrete. The same as the riskiness of shares is different, the risk assumed in the real estate market and a possible profit (loss) may be highly different. For example, investments into residential real estate are often ascribed to a group of lower risk than investments into commercial real

estate. Usually (due to leasing or a hope for prices to go up), investments into real estate are considered to be a transition between investments into shares and bonds, meanwhile a significantly higher profitability is usually sought in cases of real estate development projects by taking a risk that is much higher.

Diversification inside the class of real estate

Since the Modern Portfolio Theory introduction, a lot of scientists have studied the strategies of the diversification of portfolio investments. The first work focused on potential benefit gained from the consolidation of different shares in one portfolio; however, researches expanded up to bonds, currencies, real estate, international shares and bonds. Recently, analysts have been also analysing the potential benefit of diversification inside the class of real estate (Sirmans, Worzala, 2003).

A mere comparison of real estate and shares that vary by size (capitalization) and industrial branch shows that real estate has such additional physical categories as size (square meter and value), type, geographical and economic characteristics, etc. As a result, the diversification inside real estate requires the allocation of different types of real estate. The main segmentation of the real estate market that has an impact on investment portfolio formation strategies is distinguished and discussed below in more detail.

The diversification of investment portfolio by type of asset. Even though some managers of real estate portfolio specialize in one or two fields of assets, most investors know the benefit brought by property diversification and manage several classes of real estate. As far back as 1984, J. R. Webb revealed that 61% of institutional investors diversified it by the property type (Webb, 1984), meanwhile in 1992 M. Louargand claimed that this method was used by 89% of investors (Louargand, 1992). Interclass diversification aims at recognizing as many subclasses as possible and maximizing homogeneity inside a group as well as enhancing heterogeneity among the groups. It reduces a correlation among the groups and thus increases the level of portfolio diversification. In this way, the nonsystematic risk falls down (Seiler, 1999).

As S. Devanly and S. Lee note, an increase of the portfolio is important for real estate investors as most real estate portfolios are rather small. Researches conducted in 1995–2004 by the abovementioned authors showed that an increase in portfolio size conditioned a more stable and less volatile return pattern over time (Devanly, Lee, 2005).

The impact of property size on return pattern. In the case of real estate, the diversification inside the class of real estate is related to a reduction of nonsystematic risk. Property size expressed in square meters or money terms (these sizes correlate with each other) is considered to be one of the conditions of profitability. A small number of investors participate in a market where big-sized real estate prevails. The existence of such a market predetermines an even lower liquidity of real estate; however, the issue mentioned is compensated by a better return pattern (Roulac, 1977). Bigger real estate also means more tenants; as a result, the loss of one tenant is not as painful in a big market as it could be in the case of small real estate (Hartzell et al., 1987).

Geographical and economic possibilities of diversification. The diversification inside the class of real estate is related not only to the type of real estate, but also to another method with a help of which the property of similar

nature could be grouped. In 1982, M. Miles and T. McCue were the first to discuss additional factors conditioning the impact of different classes of real estate on each other (Miles, McCue, 1982). They compared the diversification by geographical regions with the diversification by property type and made a conclusion that the latter method was more effective. J. Garreau explicated this field by drawing attention not only to geographical possibilities of diversification, but to economic regional conditions as well (Garreau, 1981). This opinion was shared also by T. Grissom, D. Hartzell and C. Liu. Their main idea was that the return pattern was influenced by different geographical regions which, in turn, differed by their economic development (Grissom et al., 1987).

Two decades ago, the main and the most geographically developed financial market was the USA and financial instruments spent by related firms and institutions. However, today, at the global economic development phase, investors choose investment objects all around the world (AIG, 2002).

During the recent two decades, the number of analysts analysing investments in real estate has significantly increased. The academic community started discussing this question for the first time in the middle of 1960s, and during the last decade the amount of literature has significantly multiplied because of the availability of empirical data and increasing interest in institutional investors. It should be emphasized that today much more opportunities and alternatives have opened up for investors to invest their assets. New markets and new financial instruments have emerged, a lot of barriers among markets and countries have disappeared, technology facilitating investment has been developed.

In summary, it could be claimed that due to a different geographical location the diversification is related to the economic level of a region. Recently, an exceptional attention has been paid to the international diversification as it conditions a lower portfolio risk and a higher yield. However, in recent the years markets of advanced countries have started to correlate more, meanwhile investors have been looking for investment opportunities in emerging markets. International investments into real estate will gradually begin to increase their importance in Lithuania the market of which is emerging, but in the log-term perspective it will not be capable of satisfying all potential consumers of this field.

The market of real estate funds in the European Union

One of the possible forms of investment into real estate is real estate funds. According to Law on Collective Investment Undertaking (2005), "investment fund" shall mean a type of activity whereby the assets are managed by legal or natural persons by the right of common partial ownership under the trust right in accordance with the procedure and under the conditions established in Law and the rules of the investment fund. In other words, an investment fund is a specially constituted investment vehicle created with the sole purpose of gathering assets from investors and investing those assets in a diversified pool of assets. In this way, small investors may buy exposure to a professionally managed and diversified basket of financial or other assets. Overheads are spread over the pool of investors, reducing the average cost for the investor. Investors may be able to sell their shares back to the open when they want (open-ended funds) or their assets may be locked up for a fixed period (closed-ended funds) (White Paper, 2006). Assets of a

collective investment undertaking must be entrusted to a depository for safe-keeping.

Real estate funds are attributed to the investment instruments that look for investment opportunities in one concrete market branch. The investment fund industry has grown over the space of a decade to become a key actor in European capital markets. Investment funds mobilize household savings and channel them towards productive investments. The European fund industry currently manages over € 5 trillion of assets (Green Paper, 2005). The assets managed by the EU investment fund sector have increased four times over the last decade. The importance of investment funds will continue growing as most of European investors use them for the accumulation of pension funds. More and more often the market provides services on a pan-European basis (Europos Komisijos..., 2006). Investment funds account for 12.6% of the European household financial assets. The EU investment funds have experienced a five-fold growth in assets under management over the space of 12 years. Growth rates of around 10% per annum are expected in the period to 2010 – bringing total assets under management by funds to over € 8 trillion (White Paper, 2006)

Bond and share investment funds constitute the largest part of all investment funds. It should be noted that the part of real estate funds is relatively small, i.e. 4% (shares 30%, bonds 28%). Even though investment funds in comparison to other types of funds take the smallest share in the common Euro zone balance, from the first quarter of 2006 until the first quarter of 2007 it increased from € 214 to € 238 billion, i. e. by € 24.4 billion. Therefore, although real estate funds demonstrate the smallest growth and general allocation of the EU investment funds, the growth, even though a small one, is noticeable. The research of investment funds operating in the European Union, conducted at the request of the European Commission *PricewaterhouseCoopers*, revealed that in 2002–2006 all funds had a negative return at least for one year, except real estate funds which had a positive return during the whole period (European Commission..., 2008).

The Council Directive 85/611/EEC on the coordination of laws, regulations and administ-

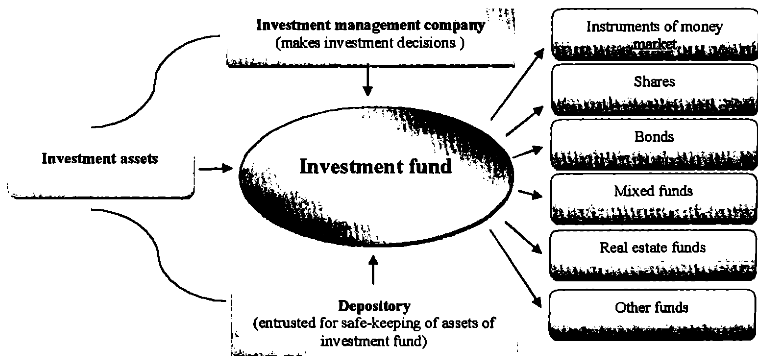

Figure 1. Scheme of the investment fund activities

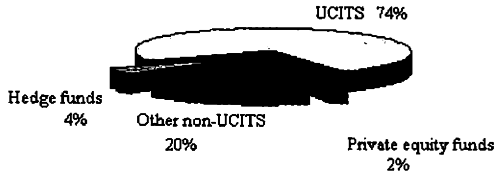

Figure 2. European investment fund industry

rative provisions relating to undertakings for collective investment in transferable securities (Council Directive, 1985) (hereinafter UCITS) serves as the cornerstone of the EU framework for investment funds. The UCITS Directive has provided the focal point for the growth of a vibrant European fund industry. This market is increasingly organized on a pan-European basis. The UCITS product passport is in widespread use. Cross-border fund sales represented some 66% of the total net industry inflows in 2005. The challenge for EU policymakers is to ensure that this regulatory framework remains effective in the face of changing market dynamics and investor needs. Profound structural changes in European financial markets are putting new strains on the UCITS regulatory system (White Paper, 2006). The above-mentioned White Paper claims that the UCITS Directive is no longer sufficient to support the European fund industry as it restructures to meet the new competitive challenges and the changing needs of European investors. As a result, the core elements of the Directive are not functioning effectively.

For the reasons provided above, today attention is focused on the categories of investment funds that are not UCITS compatible because of their investment policy or fund structuring. "Non UCITS" is a catch-all term referring to all non-harmonized funds whether or not subject to national regulation. This comprises a wide scope of investment styles and products ranging from retail-oriented products, such as open-ended real estate funds, to more volatile products such as commodity and private equity funds (White Paper, 2006).

White Paper, 2006 provides a percentage distribution of the European investment fund industry: non- UCITS funds make 26% of all funds (Figure 2).

Article 37 of the UCITS Directive defines the main difference between UCITS and non-UCITS as a requirement for UCITS funds to maintain liquidity to ensure that a subject would be able to re-purchase or redeem its units at the request of any unit-holder. Another exceptional requirement of UCITS funds is rules for the diversification in terms of counterparty's risk as well as a certain number of investment instruments and their maximum weight in the portfolio among other property classes. The aforementioned diversification requirements are applied not only to non-UCITS instruments; however, the practice proves them to be less strict than in the case of UCITS (European Commission..., 2008).

Despite the fact that real estate funds are

not regulated on the EU level, private investors can use the funds mentioned on the national level. However, the regulatory forms of their product or distribution are different. The research of the EU Member States, conducted at the request of the European Commission *PricewaterhouseCoopers*, has revealed that regulatory frameworks are different by liquidity requirement, limitations on borrowing and real estate evaluation on national level (European Commission..., 2008).

Legal requirements for the diversification are set for assets of real estate collective investment undertakings in Luxemburg, Germany, Ireland and Great Britain, and the fund portfolio is considered to be sufficiently diversified only when it is diversified inside the real estate portfolio. In Spain, the regulators require to diversify real estate in spite of the fact that the diversification rules are not legally set. Italy has provided conditions to build only close-ended real estate funds and determined certain diversification rules.

It should be stressed that, unlike diversification requirements, real estate investment companies or management companies managing assets of collective investment undertakings, borrowing requirements are significantly different among the Member States. In Luxemburg, a real estate management company may borrow up to 75% of the net asset value existing in the instruments of collective investment undertaking incorporation on the borrowing day. In Ireland, the borrowing possibilities are limited up to 25% of the net asset value. Great Britain determined borrowing requirements taking into account the rules of the UCITS framework; therefore, borrowing is very limited. Once a new law came into effect in Germany, it is allowed to borrow not more than 45% of the net asset value. Spain limited borrowing possibilities to 10% and Italy to 60% of the net asset value.

The Member States share similar evaluation practice: in Luxemburg, Germany and Great Britain, real estate funds are evaluated by independent evaluators having experience in a certain field of evaluation. The evaluation should be conducted before buying a new real estate object and while conducting a constant assessment of assets constituting a portfolio. The annual evaluation is set in Luxemburg, Germany and Great Britain, meanwhile in Ireland it must be conducted twice a year. Unlike other countries, France has not determined the frequency of evaluation, however, it requires the evaluation to be conducted by two evaluators not dependent on each other and who must provide one report on the assets evaluated.

Despite the fact that real estate funds still face dramatic differences among Member States and a need deep further evaluation, the absence of a "European passport" is a source of frustration for real estate funds, for example, long-established retail products such as open-ended real estate funds (€ 150 billion in assets under management in the EU) which see a potential benefit in serving the pan-European investor base. It should be mentioned that there is a broadening investor exposure, subject to varying conditions or restrictions and via different distribution methods, to non-harmonized funds (White Paper, 2006).

Therefore, since 2006 the European Commission has been considering how to modernize the EU investment fund system in order to solve the new tasks set by competition, and today a real estate fund is one of the catego-

ries of investment funds that attract a lot of attention. In future, the European Commission will look over the situation and consider a possibility to distribute fund units in EU Member States other than by following a simplified procedure.

The regulation of real estate funds in Lithuania

Investment funds have been operating in most of the EU Member States for a long time; however, until 2007 Lithuanian laws did not provide a possibility for such kind of funds to operate in the country. The operation of the abovementioned funds was forbidden by the Law on Collective Investment Undertakings (2003) (hereinafter CIU) then in force in the Republic of Lithuania. A possibility for investment funds to operate in Lithuania, i. e. in the form of collective investment funds, appeared only in 2003, when the Law on CIU was adopted. After the adoption of the aforementioned law in 2003 a pension fund scheme began to be created, the key actors of the investment market formed. Regulations of the law valid until 2007 implemented most of the main EU legislations and additionally provided only a possibility to set up national collective investment undertakings of limited distribution, meaning that the regulated and supervised alternative investment schemes that could be used by investors could not be established in Lithuania. A necessary edition of the Law on CIU was adopted on 15 November 2007, and the possibility for specialized funds to appear was provided from 1 March 2008 when the amendments adopted by the Seimas came into force.

The following key peculiarities of the amendments of the Law on CIU may be distinguished: the structure of collective investment undertakings is broadened; new investment fields emerge: real estate funds, private equity funds, funds of funds, alterative investment funds, hedge funds; a more liberal regulation of professional and institutional investors and limitations on their activity.

A collective investment undertaking has the following legal forms, types and kinds: 1) *a harmonized collective investment undertaking*, i.e. a collective investment undertaking that meets requirements of the EU legislation its assets are invested into securities and/or other liquid assets set by the law, and its securities (investment units or shares) confer their holder's right to redeem them at any time; 2) *a specialized collective investment undertaking* – a CIU that does not meet the requirements of the EU legislation. This category includes real estate funds.

The law provides for a certain specificity of real estate funds. The major features of the regulation of real estate investment funds are identified below:

(1) it is allowed to invest directly into a land, building, premises, real estate under construction, securities of real estate companies, investment units or shares of other real estate funds as well as movable property necessary for the exploitation of a real estate object;

(2) the law provides for a prohibition to buy real estate with a limited ownership right to it;

(3) upon the expiration of a 2-year-term, the investment portfolio must be completely diversified;

(4) assets must be evaluated by at least two independent licensed real estate evaluators authorised to engage in the activity of real estate valuation, with the exception of the property valuator assistants who would produce

individual reports. The real estate objects comprising the investment portfolio of a real estate CIU whose participants, in accordance with its instruments of incorporation, may be only professional investors, or the objects of real estate intended to be acquired may be valued by a single independent real estate valuator authorised to engage in the activity of valuation of real estate. It also stipulates that the same real estate evaluator is able to evaluate the same collective investment undertaking not more than three years in a row; before every evaluation of a real estate object, the depository of the real estate collective investment undertaking must ensure that real estate evaluator(s) meet(s) the selection, independency, qualification criteria set in the instruments of incorporation of the collective investment undertaking;

(5) a real estate investment company or management company managing the assets of a collective investment undertaking may borrow up to 75% of the net asset value existing in the instruments of collective investment undertaking incorporation on the borrowing day for a period determined in advance;

(6) the investment portfolio of the real estate collective investment undertaking established may not comply with the diversification requirements set in this article for four years as of the day when its instruments of incorporation and prospects are approved by the Securities Commission.

It should be noted that even though the UCITS Directive foresees investments only into the activity of CIU (investment funds, investment companies) investing into transferable securities and is not applied to specialized, including real estate, funds, it should be emphasized that, with certain exceptions, the regulation of real estate of CIU provided by the law is constructed following the scheme and logic of the UCITS Directive and is based on the examples of other Member States having experience in the operation of real estate funds.

Currently, real estate funds have been characterized by a special maturity. They have been demonstrating an attractive risk/reward ratio in countries with the regulated existence of these funds. The development of the abovementioned funds in Lithuania is primarily connected to the principal changes in the legal base as the new edition of the Law on CIU provides the foundation for the development of the real estate fund system.

The regulation of real estate funds, their establishment and possibility to enter the Lithuanian market are essential as most EU Member States have created conditions for the formation of analogical national investment products. The regulation will allow developing alternative markets of investment instruments in Lithuania. In this way, potential incorporators of real estate funds will not have to use the legal bases of foreign countries and introduce them in countries with a regulated operation of real estate funds.

In summary, it is likely that due to the stabilization of the real estate market, the development of the financial system and new alternative investment instruments, real estate funds will soon become an attractive investment instrument: defects of the operation of the funds identified in the practice will be removed, new management skills will appear, the education of potential investors will be enhanced and the investors' base will develop.

Conclusions

1. Real estate is a competitive investment instrument. The allocation of real estate into investment portfolio increases diversification possibilities. It is important to diversify not only among different property classes, but also inside each class. The main aim is to increase homogeneity inside a group in order to increase heterogeneity among the groups. The groups overviewed included the type of real estate, geographical and economic regions and the size of real estate. Nowadays, much more opportunities and alternatives have opened up for investors to invest their assets. New markets and new financial instruments have emerged, a lot of barriers among markets and countries have disappeared, the technology facilitating investment has been developed. The geographical aspect provides a possibility to diversify the portfolio's risk better and achieve higher profits. International investments into real estate will gradually begin to increase their importance in Lithuania whose market, even though just emerging, in a long-term perspective will not be capable of satisfying all potential consumers of this field.

2. What concerns the EU practice of the regulation of real estate funds, there is no common practice. These funds are regulated on the national level, and Council Directive of 85/611/EEC of 20 December 1985 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities is not applied to them. The Directive provides a possibility to distribute fund units in EU Member States other than by following a simplified procedure.

3. Despite the fact that real estate funds are not regulated on the EU level, private investors can use these funds on the national level. The regulatory forms of their product or distribution are different. At the moment, the European Commission is looking for the ways to modernize the EU investment fund system in order to solve the new tasks set by competition. There is a broadening investor exposure, subject to varying conditions or restrictions and via different distribution methods, to non-harmonized funds. Today, a real estate fund is one of the categories of investment funds that attract a lot of attention. The European Commission will look over the situation and consider a possibility to distribute real estate fund units in EU Member States other than by following a simplified procedure.

4. In Lithuania, a new edition of the Law on Collective Investment Undertakings laid a foundation for the development of the real estate fund system. It is likely that at the beginning this investment instrument will be accepted as a new and relatively risky alternative, its operation will be imperfect in comparison with the practice settled in more advanced countries. It is probable, though, that due to the stabilization of the real estate market and the development of a financial system, real estate funds will become an attractive investment instrument.

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