

and the returns from the capital invested in our funds. We do not recognize carried interests until the end of any determination or “clawback” period, which typically occurs at or near the end of a fund term, however we do provide supplemental information on the estimated amount of unrealized carried interests that have accumulated to date based on fund performance up to the date of the financial statements.

Fee Related Earnings

We generated the following fee related earnings during the year:

FOR THE YEARS ENDED DECEMBER 31
(MILLIONS)

| | 2013 | 2012 |
|------------------------------------|---------------|---------------|
| Fee revenues | | |
| Base management fees..... | \$ 502 | \$ 352 |
| Incentive distributions..... | 32 | 15 |
| Performance fees..... | 30 | 17 |
| Transaction and advisory fees..... | 53 | 53 |
| | <u>617</u> | <u>437</u> |
| Direct costs..... | (317) | (257) |
| Fee related earnings..... | <u>\$ 300</u> | <u>\$ 180</u> |

Fee related earnings increased by 67% to \$300 million for the year, as a result of substantial increases in fee bearing capital and associated revenues as well as operating margins.

Base management fees increased 43% to \$502 million compared to \$352 million in the prior year. Our private funds contributed \$68 million to the increase mainly resulting from new commitments to our infrastructure and real estate flagship funds, including \$15 million of catch-up fees that had been deferred until the final close of a large real estate fund during 2013. Some of our private funds earn fees only on invested capital or earn higher fees once capital is invested. We estimate that private fund base management fees will increase by approximately \$18 million upon calling the \$9.0 billion of third-party capital that has not been invested to date. Increases in the capitalization of our listed issuers through unit price appreciation and issuance of new capital added a further \$57 million of base fees. We earned \$36 million of fees from Brookfield Property Partners, which was launched in April 2013 and pays a minimum base fee to us of \$50 million per year. Base fees from our public securities activities increased by \$25 million due to net inflows and market value appreciation of the securities under management. Base management fees include \$172 million (2012 – \$119 million) earned in respect of Brookfield capital.

We received \$32 million of incentive distributions from Brookfield Infrastructure Partners during 2013, representing an increase of \$17 million from 2012. The increase was the result of a 15% growth in BIP’s limited partnership unit distributions from \$1.50 per unit during 2012 to \$1.72 per unit in 2013.

We earned \$30 million of performance fees for managing public securities portfolios, based on exceeding performance thresholds in a number of our strategies, in particular our real estate hedge funds and structured products funds.

Transaction and advisory fees totalled \$53 million in 2013, consistent with the prior year. We have expanded our investment banking activities into the U.S., UK and India and we continue to advise on a number of mandates in Canada and Brazil. Our primary focus is on real estate and infrastructure transactions.

Direct costs consist primarily of employee expenses and professional fees, as well as business related technology costs and other shared services. Operating margins, which are calculated as fee related earnings divided by fee revenues, increased to 49% for the year, compared to 41% in 2012. We had expanded our operating capabilities considerably in prior years, which enabled us to expand our asset management revenues without a commensurate increase in operating costs. Gross margins also benefitted from the receipt of catch-up base management fees and increased performance fees during 2013. Direct costs increased by \$60 million year-over-year in particular due to geographic expansion in our infrastructure, public securities and advisory businesses, as well as \$25 million of costs reallocated from our corporate activities segment to our asset management segment following the launch of Brookfield Property Partners and \$9 million of additional costs incurred that directly relate to employee compensation income based on the in-year performance fees.

Carried Interests

We concluded the initial phase of our investment in GGP with the reorganization of the consortium that we established to acquire our initial investment. This reorganization enabled our clients to convert this investment into cash, units of Brookfield Property Partners, or to continue to hold their GGP shares with us as manager. This investment had a 38% gross IRR and 2.6x gross multiple of equity invested and we received \$558 million of accumulated carried interest in accordance with the terms of our consortium agreements.