



Real Estate Information Standards (REIS)

Via e-mail only
GIPS Executive Committee
standards@cfainstitute.org

November 25, 2010

RE: Invitation to Comment: Exposure Draft of the Guidance Statement on Real Estate

To the GIPS Executive Committee:

Thank you for the opportunity to comment on the Exposure Draft of the Guidance Statement on Real Estate ("Exposure Draft"). We applaud the efforts of GIPS Executive Committee and the Real Estate Working Group in the development of the revised guidance for real estate.

Responding Organization

The Real Estate Information Standards Board is the official governing body of the Real Estate Information Standards (REIS). The REIS Board is responsible for establishing information standards for private, institutional equity real estate in the United States, an industry estimated at \$750 billion. The REIS standards are interdisciplinary and include standards for performance measurement, valuation, fair value accounting and fund/account reporting. We think the use of a single set of interdisciplinary standards will facilitate capital formation and help provide investors with comparable financial information needed to support informed decision making.

The GIPS standards are the foundational standards upon which REIS depends for its performance standards, drawing upon the GIPS standards for basic ethical principles, such as full disclosure and fair representation of investment performance, and for other specific methodologies and disclosures.

The performance measurement elements of the REIS standards address performance calculation, measurement and presentation. Whereas the GIPS standards focus on reporting to prospective clients for all investable asset classes, the REIS standards focus on reporting private real estate investment information to existing clients.

We have, and continue to anticipate collaborating with your organization on matters of mutual interest and are very pleased that the REIS Guidance Statement for [Determining Investment Discretion for Real Estate Investment Accounts](#) ("REIS Guidance Statement") was considered and substantially adopted within the Exposure Draft.

Responses to Questions

1. *Do you agree with the proposed requirement to include new portfolios in a composite upon portfolio inception? Should this be a recommendation? Should this be an optional policy?*

REIS response:

We do not agree with the proposed requirement and we do not agree that this should be a recommendation. Rather, the firm's treatment of initial partial periods should be incorporated into its policies and procedures and consistently applied across all portfolios. Disclosure of the methodology used to account for partial period activity should be required within a GIPS compliant presentation in order to improve transparency and consistency in performance presentation.

It should be noted that including initial partial periods (which typically may have significant write-off of organization and other acquisition costs and include minimal investment income) may cause skewed return results, depending on how they are incorporated into the calculation particularly in the first year of returns for the composite or portfolio. .

The firm's policies and procedures should include a specific description pertaining to the firm's definition of a portfolio's inception date and this definition should be consistently applied across all portfolios. The "date of the portfolio's first external cash flow" could be interpreted in a variety of ways, including the date a property is purchased using cash, the date organizational costs are paid, or the date a line of credit is used for funding. Firms can also define portfolio inception dates as the date the first commitments are secured, the date the first cash commitment is received, the date of the first actual investment purchase, or the date the return is representative of the composite/portfolio strategy (or when minimum thresholds have been reached). Without more clarity on the inception date, performance comparability will be minimized.

2. *Do you believe this requirement should be limited to new portfolios in real estate closed –end fund composites?*

REIS Response

No, please see response to question #1 above.

3. *Do you believe there should be a corresponding disclosure requirement regarding partial period returns?*

REIS Response

GIPS should only require disclosure of the firm's treatment of initial partial periods within the GIPS compliant presentation. (See response #1 above.) We do not support a required or recommended treatment of initial partial periods.

4. *Alternatively, if a portfolio experiences an event that materially impacts performance prior to the portfolio's inclusion in a composite (the period from a portfolio's inception up to the beginning of the first full period), should this impact be brought forward and reflected in performance once the portfolio is included in the composite? If so, should this be required or recommended?*

REIS Response

Consistent with our answers above, the treatment of initial partial periods should be part of the firm's policies and procedures. The treatment of events materially impacting initial partial period performance should be a required disclosure only. This required disclosure should apply to any activity that took place either before or during the first partial period. The disclosure should reflect the impact within the performance presentation and be based on the firm's definition of materiality, and the firm should also disclose the methodology that was used to reflect these events in performance (e.g., Firms could include this impact in the opening net asset balance of the first full quarter, or in the income/appreciation components of the first full quarter, or amortize the impact of the events over several quarters).

5. *Should portfolios be required to remain in composites until the portfolio is terminated?*

REIS Response

The determination of when a portfolio terminates should be defined by the firm within its policies and procedures and consistently applied. The termination of a portfolio can often occur several years after the sale of the last asset in the portfolio (especially when environmental or post-sale litigation issues arise). Returns following the last asset sale may not be representative of composite strategy. For example costs associated with the dissolution of the portfolio are likely to occur after the last asset sale.

6. *Are there any composite construction or calculation issues that arise as a result of the proposed changes?*

REIS Response

Yes, the issues that can arise are addressed in the responses to the previous questions.

7. *Would the proposed changes create any issues in regards to benchmarks?*

REIS Response

Although the treatment of initial partial periods as proposed within the Exposure Draft may differ with the treatment of initial partial periods within benchmarks, these indexes are generally large enough that the entrance or exit of individual properties or funds are not material to the benchmark and would not likely compromise comparability to the composites in which they are used.

Additional Comments

As requested, we have included comments on each of the questions in the Exposure Draft. Except as noted herein, we are generally supportive of the Guidance Statement on Real Estate. We offer the following comments.

Investment Discretion

In the REIS Guidance Statement, we suggested that “the presence of a discretionary relationship may be inferred if a portion of the firm’s compensation is tied to performance”. We understand that firms consider this element to be one of their considerations that supports their conclusions that an account is discretionary. We would like to understand why this element was excluded in the Investment Discretion section of the GIPS Guidance Statement.

Fees and Expenses

The proposed guidance contains new information on the treatment of fees and expenses. We note the following: “Acquisition, disposition, financing and development costs on a particular transaction are considered “transaction expenses” and must be deducted from both gross-of-fees and net-of-fees returns regardless of whether the service is performed by the investment manager of a third party.”

Has the GIPS Executive Committee considered that an investment advisor may choose to structure its fees in a number of different ways depending on (i) the current market practice for the risk profile of a specific investment strategy (i.e., core, value-added, opportunistic) or ii) the fee preferences of a single-client account?

For example, the recurring investment management fee may be less on a lower risk core investment but an acquisition fee may be charged and perhaps a disposition fee. Alternatively, the investment management fee may be greater on a higher yielding, value-added strategy, with no acquisition or disposition fee charged.

Comparisons of returns and fee structures amongst advisors could therefore become very difficult.

Conclusion

Thank you for the opportunity to respond to this exposure draft. We appreciate the ongoing opportunity to collaborate with you on future initiatives. Should you have any questions or require clarification of our responses, please do not hesitate to contact John Baczewski, REIS Board Chair at 978-887-3750, or Marybeth Kronenwetter, REIS Administrator at 630-469-4088.

Yours truly,



John J. Baczewski, REIS Board Chair