



# CHECKLIST FOR EFFECTIVE USE OF PRIVATE REAL ESTATE IN DC PLANS

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SECOND QUARTER 2016/DCREC BEST PRACTICES COMMITTEE

## **TOPICAL AREAS**

Product Structure & Investor Eligibility

Daily Valuation

Investment Strategy

Liquidity Management

Purchases and Redemptions

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## **PURPOSE OF CHECKLIST**

This “Checklist” is designed to assist Plan Sponsors and Plan Advisors/Consultants within the DC marketplace who are evaluating direct real estate funds for use in their DC Plans, as part of a multi-asset risk/age-based fund or in some cases as a stand alone option.

DCREC assumes that these questions will be IN ADDITION to the standard fund evaluation questions, such as the fee and expense breakdown at both the FOF and acquired fund level, management experience, investment philosophy, process and performance.

## Suggested Questions: Structure and Eligibility

- What is the legal structure of the Fund? CIT, 40 Act, Separate Account?
- Is the Fund a Fund-of-Funds investment vehicle or a Fund that invests directly into real properties?
- Is the Fund's Investment Manager a fiduciary?
- If a Fund-of-Funds, who are the Investment Managers of the underlying real estate funds?
- What is the Fund's current investor composition? Is it designed only for qualified employee benefit plans?
  - % of DC Investors:
  - % of DB Investors:
  - % of Retail/HNW:
  - % of Other (define):
- Is the Fund available as a direct investment by plan participants (stand-alone on the plan menu), or only as a "sleeve" of a target-date, target-risk fund or other multi-asset investment portfolio?

**Suggested Questions:  
Fund-of-Funds Valuation**

- Does the Investment Manager have documented, transparent, and consistent valuation procedures for the Fund-of-Funds, as well as the underlying real estate funds?
- Does the Manager provide daily NAV history? If so, what is the reporting period (monthly or quarterly)?
- How does the Fund arrive at the daily NAV per share or unit?
- What is the current aggregate and per share NAV of the fund?
- When is the closing NAV for the current day published and available to investors?
- Do the underlying funds require a valuation reconciliation or “true-up” monthly or quarterly? If so, what is the process and has the differential improved over time?
- Are there peer group performance measurements available for daily valued real estate? Please describe.

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**Suggested Questions:  
Underlying Real Estate Investments Valuation**

- In the past, real estate funds have typically been valued quarterly. What is the process for bridging the gap between quarterly and daily valuation of the underlying real estate and related debt?
- Does the real estate fund manager retain an independent, third-party firm to value the real estate? If so, what is the firm's specific role?
- Who engages and selects the independent third-party appraisers of the properties in the underlying funds? Are the appraisals on a pre-determined, periodic schedule?
- Once a real estate investment is made, at what point will it be valued at fair market value vs. capitalized acquisition cost? How soon after a property acquisition is made is an independent appraisal done?
- On what basis are properties carried and reported in the underlying fund(s)? GAAP, market value or both?
- Are there periodic adjustments to the real estate investments which could cause material adjustments in the Fund NAV during certain times of the year, e.g. month end, quarter end?

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**Suggested Questions:  
Strategy and Allocations**

- What is the investment strategy of the Fund and of the major underlying Funds that invest in real estate?
- What is the investment process and the asset management philosophy for the underlying real estate portfolio managers?
- How many other funds/accounts within your firm (or the underlying real estate manager) have a similar investment strategy and the ability to buy the same types of properties as the Fund? How do you manage potential conflicts and/or allocate investments?
- Does the Fund invest in listed REITs or REIT funds for liquidity and diversification? If so, what types of REITs and what strategies?
- Describe how and why the allocation strategy may change, particularly during periods of economic stress. Provide historical examples, if possible.

**Suggested Questions:  
Investment Attributes**

<b>Investment Attributes</b>	<b>Policy Limits</b>	<b>Actual (Current)</b>	<b>Average Allocation Prior Three Year Period</b>
<b>Asset Allocation</b>			
<b>Cash</b>			
<b>Liquid Securities</b>			
<b>Real Estate</b>			
<b>Core</b>			
<b>Non-Core</b>			
<b>Number of Investments</b>			
<b>Diversification by Geography and Asset Type</b>			
<b>Consolidated Leverage Ratio (FOF level)</b>			

### Suggested Questions

- What is the liquidity mechanism for the Fund? Liquidity sleeve, line of credit, other?
- Are there defined targets with minimum and maximum asset allocations to liquid investments, including cash?
- Does the Fund utilize listed REITs as a liquidity mechanism?
- If the Fund is a Fund of Funds, do the underlying funds also have mechanisms to provide liquidity? Please describe.
- How quickly is new capital invested, and how is this inflow and deployment timing managed?
- How often does the Fund rebalance for liquidity requirements?
- Has the Fund denied a redemption out of the Fund or an inflow into the Fund during the last ten years? If yes, please provide detail of the circumstances.
- Does the Fund provide a quarterly distribution? If so, are these automatically reinvested, paid out, or does the investor have an option to choose?
- What were the highest and lowest amounts of liquid investments (listed REITs, other instruments and cash) held over the past three years, dollars and percentages? Since inception?

### Suggested Questions: Purchases

- Can purchases be made on any trading day and is pricing based on the prior day's or current day's NAV?
- Does the Fund have any capacity limits on the size of a particular investor's allocation, at the FOF level or at the underlying funds?
- Does the Fund have limits on investment inflows into the Fund (or an underlying Fund)? How are these limits set?
- Does this Fund have priority for investment into underlying funds if there is an entry queue for the underlying funds? Does the queuing process differ for new investors versus existing investors?
- Have the Fund's purchase procedures integrated smoothly with Record Keeper systems? If there have been issues, please explain.
- Which Record Keeper platforms is the Fund on?

### Suggested Questions: Redemptions

- What is the Fund's redemption policy?
- Does the Fund have any redemption penalties, lock-ups or other redemption restrictions?
- Could redemption limits at underlying real estate funds affect the manager's ability to rebalance? If so, how is this mitigated?
- Are redemptions made pro-rata or based on timing of receipt of notification?
- Does the Fund have any restrictions on the size of redemptions? If so, are these restrictions subject to notification requirements and/or are they at the Manager's discretion?
- Can redemptions be made with in-kind distributions?

## **Resources & Important Reference Info**

### **DCREC Study: A Path to Better Retirement Outcomes: Allocating Real Estate Assets to Retirement Portfolios**

The academic study was conducted by Michael E. Drew, PhD, a Professor of Finance at the Griffith Business School at Griffith University, Adam N. Walk, PhD, also from the Griffith Business School, and Jason M. West from Bond University. <http://www.dcrec.org/Resource>

### **The NCREIF PREA Reporting Standards**

An industry initiative co-sponsored by the National Council of Real Estate Investment Fiduciaries (NCREIF) and the Pension Real Estate Association (PREA) with a mission to establish and implement information standards for the real estate industry which will facilitate transparency, consistency and informed decision-making. <http://www.reportingstandards.info/>

### **ASC 820, Fair Value Measurements and Disclosures (Financial Accounting Standards Board)**

<https://asc.fasb.org/>

### **Uniform Standards of Professional Appraisal (The Appraisal Foundation)**

<http://www.appraisalfoundation.org/>

### **NCREIF Fund Index - Daily Price Returns**

<https://www.ncreif.org/fund-index-daily-price.aspx>

## **Defined Contribution Real Estate Council (DCREC)**

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