

RREEF Direct Real Estate's response to GIPS Executive Committee's (EC) invitation to comment on proposed GIPS 2010 Exposure Draft:

June 17, 2009

CFA Institute
Centre for Financial Market Integrity
Reference: Global Investment Performance Standards
P.O. Box 3668
Charlottesville, Virginia 22903

Global Investment Performance Standards 2010

Dear GIPS Executive Committee:

Our responses to the summary of proposed revisions to the Global Investment Performance Standards are as follows:

0.A.7 - GIPS Compliance Statement – Do you agree with including disclosure of the firm's verification status in the claim of compliance?

Yes, we agree with including disclosure of the firm's verification status in the claim of compliance. However, we believe this should be expanded to also recommend the inclusion of the status of a performance examination, stating whether the firm has had a performance examination as a part of the verification. We believe the performance examination is equally as important as the verification, and since a performance examination is essentially an audit of the composite and performance calculations it provides a higher level of assurance to investors with regard to the data being presented in a fully compliant presentation.

0.A.7 - Do you agree with the classification of a current verification being within the last 24 months?

No, we do not agree with the period of current being within 24 months of the end date but rather *within 12 months of the end date*. Two years seems to be a stretch to use the label of current. Since compliant presentations show annual performance, we believe the current label could follow that same annual (or 12 months) rule. Financial audits are completed annually and considered current within the last 12 months and we would recommend performance and verification follow this same classification.

1.A.2 Fair Value – Do you agree with the change from Market Value to Fair Value?

Yes

Appendix D & 6.A.2 - Do you agree with the requirements and recommendations in the GIPS Valuation Principles? Do you agree that real estate investments must be valued by an independent external appraiser every 12 months beginning 1 January 2012?

No, we do not agree that real estate assets should be required to have an external appraisal completed every 12 months. Currently it is an accepted industry-wide practice on separately managed accounts to externally value real estate every 36 months. This change would require investment advisors to modify agreements with separate account investors and require either the investor or the advisor to incur the additional cost of the external appraisals. This change could potentially also cause a firm to be unable to claim compliance with the standards after a long history of making a claim which could alarm investors.

There are several questions and issues that should be considered:

With respect to separately managed accounts, the U.S. industry standard is to perform an external valuation every 36 months. This requirement is included in the existing investment management agreements of separately managed accounts. If the annual external valuation becomes a requirement, who pays for the annual external valuations? If a separate account does not want the annual external appraisal performed and the investment manager incurs the cost in order to continue to claim compliance then the cost of verification could triple.

There could also be a potential conflict of interest if a separate account client does not elect to have an external valuation completed annually causing the investment manager to be involved in all phases of the external appraisal process. The independence of an external appraisal whereby the investment manager is selecting the appraiser, providing them with the data to perform the appraisal as well as incurring its cost may not be any better than an appraisal conducted internally. An internal appraisal also has the potential to be more reliable given it would not have the disparity in approach that often exists among external appraisers.

We feel external appraisals every 12 months should not be a requirement and remain as a recommendation.

3.A.1 - Non-Fee-Paying Portfolios – Do you agree with requiring the inclusion of non-fee paying portfolios in composites?

Yes, we believe all portfolios should be included in at least one composite regardless of whether they earn a fee and as long as the portfolio is managed to the strategy. This requirement will allow for a more complete picture regarding the firm's track record of that particular strategy.

However, we feel the percent of the composite that is comprised of non-fee paying portfolios should be disclosed in the presentation.

3.A.9 Do you agree with changing 3.A.9 from a recommendation to a requirement?

Yes, we agree with this change as we do not see value in marketing to unqualified prospects.

4.A Disclosures – Should firms be allowed to remove certain disclosures after a defined period of time? If so, which disclosures would be eligible for removal and what period of time?

We recommend including disclosures for the appropriate periods presented instead of removing them. For example, if the composite name changed effective January 1, 2004 and the presentation shows 10 years of history as of December 31, 2008, the presentation should be entitled with the new name but the disclosures should reference the years (1999 – 2003) with the old name.

4.A.16 When presenting NET-OF-FEES RETURNS, FIRMS MUST disclose:

- b) If model or actual INVESTMENT MANAGEMENT FEES are used.
- c) If returns are net of PERFORMANCE BASED FEES.

We agree with the disclosure of actual investment management fees and performance based fees in a net-of-fees return. This disclosure will provide a better comparability between investment manager compliant presentations.

4.A.20 Do you agree with requiring the disclosure of key characteristics and risks in the composite description?

Yes

5.A.1 The following items MUST be included in each COMPLIANT PRESENTATION:

- b) Annual returns for all years. For COMPOSITES with a COMPOSITE INCEPTION DATE beginning on or after 1 January 2011, when the initial period is less than a full year, FIRMS MUST present returns from the COMPOSITE inception through the initial year-end.

Yes, we agree with this requirement. We feel the initial period of a composite is meaningful and as long as it is disclosed with the period of the year presented it is useful in overall performance results of the composite.

5.A.8 Do you agree with the requirement to present the percentage of the composite assets composed of proprietary assets?

Yes, we agree with this inclusion. The investment manager may own a small percentage of many portfolios that belong in their composites. We feel that disclosing the amount of the composite the investment manager invests in is useful information for a potential investor.

5.B.6 FIRMS SHOULD update COMPLIANT PRESENTATIONS quarterly.

We strongly agree with this recommendation. Keeping compliant presentations updated on a quarterly basis requires firms to review the standards as well as their own firm

policies and procedures and composite contents more frequently, likely leading to earlier discovery of any potential errors and/or issues.

6.A.4 INCOME and CAPITAL RETURNS (components returns) MUST be calculated separately using geometrically LINKED TIME-WEIGHTED RATES OF RETURN

We strongly agree with this new requirement. Real estate investment managers have accounting systems with the data by category (income and capital) to calculate the separate component returns. We believe this method is correct and that the components should never be added together.

However, we feel the requirement that “The income and capital appreciation component returns MUST be presented in addition to TOTAL RETURN” is not necessary for GIPS compliance presentations. If a portfolio is a mix of real estate and other investments that are not real estate would you only show component returns for the real estate portion? Real estate presentation should be consistent with other asset classes and present total return only.

We understand clients may still require component returns to be reported to them in the manager’s quarterly reporting. Managers will continue to calculate this information and the component returns could be provided as supplemental information to a compliant presentation if they feel the information is useful to a potential investor.

6.A.6 Do you agree with the additional requirements and recommendations for closed-end real estate funds as defined?

Yes. One potential issue that may arise involves firms that have separately managed accounts blended with closed end funds in a current composite by strategy. The new closed-end provisions may cause firms to redefine some composites by removing the closed-end funds from existing composites and establishing new composites by strategy and vintage year. We do not believe this exercise would be burdensome or cause a firm to no longer claim compliance.

6.A.8.c For periods beginning on or after 1 January 2012, FIRMS must explain and disclose the impact of material differences between:

i. The valuation used in performance reporting and the valuation used in financial reporting.

ii. The EXTERNAL VALUATION and the valuation used in performance reporting.

We suggest additional language in item i. regarding the background of this requirement. If the goal is that performance should follow audited financial statements we suggest additional language describing this point.

We agree with both requirements in 6.A.8.c.

6.A.9.b Do you agree that component returns must be disclosed, and that the method prescribed in provision 6.A.9.b.will no longer be acceptable for periods beginning after 1 January 2011?

No, we do not agree component returns must be disclosed. We feel only total return must be disclosed (see 6.A.4 comments.) However, if they are required to be disclosed, components that are calculated and compounded separately using geometric linking may not sum to the total and should not be forced or adjusted to sum to the total.

Appendix E – GIPS Glossary Do you agree with the definition of prospective client? If not, how should it be defined?

Yes

Should specific verification procedures be included for GIPS provisions 0.A.16 and 0.A.17?

Yes. Delineating specific verification procedures as well as incorporating a statement as to whether a firm has had a performance examination as part of their verification (our recommendation for section 0.A.7) would give a potential investor complete information surrounding what is actually behind every firm's verification status.

Other Comments

General provisions of the standards #6. Real Estate, 0.A.3; There is confusion across real estate managers and verification firms with respect to this item. Specifically, do total Firm Assets (or Firm Assets under Management) presented in a compliant presentation include both discretionary and non-discretionary assets at Fair Value? The question is whether non-discretionary real estate assets require quarterly valuations. We feel the standards should specifically state that non-discretionary assets are not required to be valued quarterly. The quarterly valuation requirement is included in the standards within the Input Data – Requirements. This section only applies to data (or portfolios) included in a composite. Since non-discretionary portfolios are not included in a composite we do not feel the quarterly valuation requirement applies.

A second comment regarding section 0.A.3 relates to the calculation of Firm Assets. Are Firm Assets equal to Total Assets (real estate plus cash and other receivables) or Net Asset Value? We feel this should be clearly defined so all real estate managers are consistent in the presentation. Based on the required disclosure in section 6.A.3.f., we feel the Firm Assets should be Net Asset Value. In 6.A.3.f., the requirement states to disclose the "Percent of total Market Value of Composite assets to total Real Estate assets valued by an External Valuation for each period." Since Composite assets are Net Asset Value we feel the Firm Assets should also be Net Asset Value so the percentage calculated represents the same measure in the numerator and denominator.

Within Appendix D - Fair Value, we would like to see additional guidance on the fair value of debt for real estate. Within a firm's NAV of a real estate portfolio where the debt is valued quarterly as well as the asset, should debt follow the same guidance as an asset fair value in that it is valued quarterly, and should the effects of the debt valuation be included in the composite?

The current standards are silent regarding this point. We feel additional guidance for Appendix D is necessary.

We appreciate the opportunity to comment on the exposure draft and would like to thank the CFA Institute and the various working groups that participated in developing the proposed changes to the standards. We look forward to the new version of the standards. If you have any questions regarding the content of this letter please contact Michelle Clements at (312) 278-6574 or Michele Couey at (415) 262-2052.

Regards,

RREEF Direct Real Estate