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**February 13, 2017**

**Item Name:** Repeal of the Legacy Real Estate Policies – First Reading

**Program:** Real Assets

**Item Type:** Information

**Executive Summary**

This item proposes the repeal of two legacy Real Estate policies specifically:

1. Appraisal of CalPERS Real Estate Interests (Real Estate Appraisal Policy); and
2. Real Estate – Accounting (Real Estate Accounting Policy)

Business procedures for accounting and reporting of valuations for CalPERS' real assets have been developed through a multi-year, collaborative process by the CalPERS Investment and Financial offices. With the establishment of the new procedures, which reflect improved business processes and clarity, staff recommends the repeal of the legacy policies.

Additionally, maintaining business procedures such as these at the staff level, instead of at the board-policy level, are expected to increase the consistency and focus of the CalPERS investment policy framework, and facilitate the ongoing maintenance of up-to-date procedure documentation.

Versions of the legacy policies marked for repeal are provided as Attachments 1 and 2 respectively. A consultant opinion letter from Pension Consulting Alliance is provided as Attachment 3.

**Strategic Plan**

This item supports the CalPERS Strategic Plan goal to cultivate a high-performing, risk intelligent and innovative organization. By removing procedural language from statements of investment policy, the policy framework can be maintained at a consistent, strategic level of detail and materiality.

**Background**

The legacy policies were initially created following the adoption of the Equity Real Estate Investment Strategy in 1996, and a subsequent review of all policies related to Real Estate. In the course of the review a new policy was developed for real estate accounting, and the Equity Appraisal Policy was modified for real estate.

In 2009, as part of a policy review and consolidation project initiated in 2007, the Real Estate Appraisal and Real Estate Accounting policies were updated to reflect a revised template and other adjustments to increase consistency across policies.

In addition, non-material changes were made to the legacy policies in 2014. The changes reflected revisions to the CalPERS Policy Glossary of Terms and the addition of general references to the CalPERS Investment Beliefs in the introductory statements.

The Investment Office's most recent Policy Revision Project, initiated in 2014, further enhanced the CalPERS investment policy framework by:

- Removing content more appropriately addressed at the staff level through procedure documentation
- Deleting ambiguous, editorial, or duplicative language that did not add value or clarity to policies
- Applying a new template with key investment responsibilities, constraints, and parameters consolidated and consistently presented in designated appendices

In recognition that development of updated procedure documentation for the real assets valuation and accounting processes was underway, and to make the highest use of staff and Committee time, the Real Estate Accounting and Real Estate Appraisal policies were not subjected to the revisions of the most recent Policy Revision Project.

### **Analysis**

In the nearly twenty years since the Real Estate Accounting and Real Estate Appraisal policies were developed, CalPERS has made several governance and process improvements that make the ongoing maintenance of the Real Estate Accounting and Real Estate Appraisal policies obsolete:

1. CalPERS hired a Chief Financial Officer in 2012, strengthening CalPERS' efforts to increase transparency, improve risk management, and strengthen internal controls of our financial operations.
2. The Investment Office expanded its internal deliberative and governance group structure, including increased participation by key enterprise partners, including members of the Financial and Legal Office teams.
3. The Investment Office has enhanced our technological infrastructure and reporting capabilities.
4. The Total Fund Policy and Real Assets Program Policy have been revised and refocused through the most recent Policy Revision Project, and will be subject to regular compliance testing and review by staff.

As previously stated, the business procedures currently in place governing the real assets valuation and accounting processes were developed through a collaborative workgroup. Staff from the Investment and Financial Offices will continue to work collaboratively to ensure that the procedures are maintained and reflect best practices and CalPERS business processes as they continue to evolve.

## **Budget and Fiscal Impacts**

Not Applicable

## **Benefits and Risks**

Benefits associated with the repeal of the Real Estate Accounting and Real Estate Appraisal policies include:

- Continued enhancement of CalPERS' investment policy framework - Strengthens consistency and focus of policy documents at a strategic level.
- More effective use of staff and Committee time in maintaining the procedures going forward – By its very nature, operational and procedural documentation changes over time due to a variety of causes (changes in organization, technology, processes, business trends, etc.). Maintaining this type of guidance at the staff level will facilitate the ongoing review and revision process, helping to ensure the documents remain current.

The current Real Assets Program Policy requires, in Appendix 2, Investment Office Staff Responsibilities, item one, that all aspects of portfolio management be consistent with all applicable policies and procedures. Considering the robust procedures already in place related to the functions outlined in the legacy policies, staff does not anticipate any risks will be posed to the System should the Committee accept staff's recommendation to repeal the legacy policies.

## **Attachments**

Attachment 1 – Appraisal of CalPERS Real Estate Interests – Marked for Repeal

Attachment 2 – Real Estate Accounting Policy – Marked for Repeal

Attachment 3 – Board Investment Consultant Opinion Letter – Pension Consulting Alliance

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