



Accounting Committee

**NCREIF Virtual
Winter Conference 2021**

March 15 - 25

Committee Chairs:

Robert Fraher, KPMG – Chair

Hunt Holsomback, Alvarez & Marsal - Chair

Megan Hess, DWS – Co Vice-Chair

Heather Hopkins, Clarion – Co Vice-Chair



Accounting Committee Agenda

March 23

- Financial Technical Update – Lou DeFalco, PWC & Cindy Mai, PWC
- Hot Topics – Megan Hess, DWS
 - Leasing Literature (ASC 842) - Robert Fraher, KPMG
 - Derivatives (Debt Mark to Market) – Ian Sivak, Baker Tilly
 - Deferred Maintenance – Megan Hess, DWS
 - Escrow Deposits – Megan Hess, DWS
 - Capitalized Interests – Megan Hess, DWS
 - COVID Accounting – Mark Wojteczko, Deloitte
 - Reporting Model – Sabeen Alwy, USAA Real Estate Company
 - TGER – Benay Kirk, Alter Domus



Hot Topic: Leasing Literature (ASC 842)

Presented By: Robert Fraher, KPMG



ASC 842 – Initial Direct Leasing Costs

- The FASB determined that only **incremental costs** would qualify for capitalization.
- Costs would be incremental if they would not have been incurred absent the lease being obtained.

Incremental:

- Commissions paid upon execution of a lease (internal or external)
- Payments to existing tenant to incentivize them to terminate their lease

Not incremental:

- Leasing department salaries, bonuses, overhead, unsuccessful efforts
- Advertising, soliciting potential lessees, servicing existing leases
- Costs incurred before lease is obtained, such as legal or tax advice, negotiating the lease, due diligence on potential tenants

This will likely be a change in practice for many in our industry.



Polling Questions – Leasing Literature (ASC 842)

Question #1: Have you started implementing the leasing literature (ASC 842) for your funds/separate accounts?

A.	Yes
B.	No



Polling Questions – Leasing Literature (ASC 842)

Answers #1: Have you started implementing the leasing literature (ASC 842) for your funds/separate accounts?

(124 of 195 Attendees responded)

34 Responses 27.42%	Yes
90 Responses 72.58%	No



Polling Questions – Leasing Literature (ASC 842)

Question #2: Given ASC 842 requirements, do you expect a change in the treatment of certain initial direct leasing costs in 2022?

A.	Yes – We will follow GAAP and expense them
B.	No
C.	Do not know
D.	Not applicable



Polling Questions – Leasing Literature (ASC 842)

Answers #2: Given ASC 842 requirements, do you expect a change in the treatment of certain initial direct leasing costs in 2022?

(115 of 195 Attendees responded)

34 Responses 29.57%	Yes – We will follow GAAP and expense them
16 Responses 13.91%	No
47 Responses 40.87%	Do not know
18 Responses 15.65%	Not applicable



Polling Questions – Leasing Literature (ASC 842)

Question #3: Do you have ground leases within your fund/separate accounts?

A.	Yes
B.	No
C.	Do not know



Polling Questions – Leasing Literature (ASC 842)

Answers #3: Do you have ground leases within your fund/separate accounts?

(113 of 195 Attendees responded)

80 Responses 70.8%	Yes
30 Responses 26.55%	No
3 Responses 2.65%	Do not know



Polling Questions – Leasing Literature (ASC 842)

Question #4: Do you feel like you have adequate information to implement the lease literature for FMV?

A.	Yes – Fully knowledgeable
B.	Yes – But I would like more examples and policy outlines
C.	No
D.	Do not know
E.	Not applicable



Polling Questions – Leasing Literature (ASC 842)

Answers #4: Do you feel like you have adequate information to implement the lease literature for FMV?

(102 of 195 Attendees responded)

3 Responses 2.94%	Yes – Fully knowledgeable
45 Responses 44.12%	Yes – But I would like more examples and policy outlines
31 Responses 30.39%	No
14 Responses 13.73%	Do not know
9 Responses 8.82%	Not applicable



Hot Topic: Derivatives (Debt Mark to Market Task Force)

Presented By: Ian Sivak, Baker Tilly

Debt Mark to Market Task Force Update

Task force update:

- Drafted recommendations for additions/changes to data submission fields and clarifications to guidance within Fair Value manual
- Received feedback on recommendations, significant feedback areas:
 - Some derivatives attached to debt in a way which prevents separation of derivatives and M2M adjustments from debt and debt appreciation
 - Should interest expense cash flows from derivative instruments be segregated for performance purposes?
 - How should derivative financing costs and M2M adjustments be classified for performance purposes?
 - Compliance with other reporting models
- Reaching out to individuals who provided feedback and revising recommendations with consideration for feedback
- Comments/feedback? E-mail Ian.Sivak@bakertilly.com



Polling Questions – Derivatives

Question #1: Are you recording deriv. val. adj in its own general ledger account?

A.	Yes – We have a separate GL account
B.	No – We book it with interest expense
C.	No – We book it with debt valuation unrealized
D.	Not applicable
E.	Do not know



Polling Questions – Derivatives

Answers #1: Are you recording deriv. val. adj in its own general ledger account?

(89 of 195 Attendees responded)

40 Responses 44.94%	Yes – We have a separate GL account
2 Responses 2.25%	No – We book it with interest expense
15 Responses 16.85%	No – We book it with debt valuation unrealized
25 Responses 28.09%	Not applicable
7 Responses 7.87%	Do not know



Polling Questions – Derivatives

Question #2: Are your deriv val. adj returns provided to NCREIF reported within the debt valuations or as a separate component?

A.	Submitted separately
B.	Submitted with interest expense
C.	Submitted combined with debt valuation
D.	Not applicable
E.	Do not know



Polling Questions – Derivatives

Answers #2: Are your deriv val. adj returns provided to NCREIF reported within the debt valuations or as a separate component?

(84 of 195 Attendees responded)

13 Responses 15.48%	Submitted separately
0 Responses	Submitted with interest expense
19 Responses 22.62%	Submitted combined with debt valuation
35 Responses 41.67%	Not applicable
17 Responses 20.23%	Do not know



Polling Questions – Derivatives

Question #3: Are your derivative adjustments impacting your income or appreciation returns?

A.	Income Returns
B.	Appreciation Returns
C.	Not applicable
D.	Do not know



Polling Questions – Derivatives

Answers #3: Are your derivative adjustments impacting your income or appreciation returns?

(98 of 195 Attendees responded)

6 Responses 6.12%	Income Returns
59 Responses 60.2%	Appreciation Returns
23 Responses 23.48%	Not applicable
10 Response 10.2%	Do not know



Hot Topic: Deferred Maintenance

Presented By: Megan Hess, DWS



Deferred Maintenance - Reimbursable Property Costs

Example:

You are the owner of a retail mall that undergoes a significant maintenance project (i.e. all parking lots are repaved within a one month period). Per the terms of the leasing arrangement with tenants, you are able to be reimbursed for this expense.

Business/Legal Treatment:

You bill back your tenants for the total cost of this project over the course of a 36 month period from a business operational perspective.

Accounting Treatment:

Capitalization vs. expense considerations



Polling Questions – Deferred Maintenance

Question #1: How are you accounting for deferred maintenance items as outlined in the prior slide?

A.	Exp./Cap. based on the nature of the item based on policy
B.	Capitalize in other assets and amortize over tenant repayment
C.	Capitalize in other assets and amortizing over 5 years
D.	Other Treatment
E.	Not applicable / Do not know



Polling Questions – Deferred Maintenance

Answers #1: How are you accounting for deferred maintenance items as outlined in the prior slide?

(95 of 195 Attendees responded)

38 Responses 40%	Exp./Cap. based on the nature of the item based on policy
14 Responses 14.74%	Capitalize in other assets and amortize over tenant repayment
3 Responses 3.16%	Capitalize in other assets and amortizing over 5 years
4 Responses 4.21%	Other Treatment
36 Responses 37.89%	Not applicable / Do not know



Polling Questions – Deferred Maintenance

Question #2: Tax Treatment – How do your deferred maintenance items get treated for tax purposes?

A.	Normal tax treatment for an Expense/Capitalizing items
B.	Cap. in other asset and amortize consistent with GAAP
C.	Cap. in other asset and amortize different than GAAP
D.	Other Treatment
E.	Not applicable / Do Not Know



Polling Questions – Deferred Maintenance

Answers #2: Tax Treatment – How do your deferred maintenance items get treated for tax purposes?

(92 of 195 Attendees responded)

22 Responses 23.91%	Normal tax treatment for an Expense/Capitalizing items
4 Responses 4.35%	Cap. in other asset and amortize consistent with GAAP
1 Responses 1.09%	Cap. in other asset and amortize different than GAAP
0 Responses	Other Treatment
65 Responses 70.65%	Not applicable / Do Not Know



Hot Topic: Escrow Deposits

Presented By: Megan Hess, DWS



Polling Questions – Escrow Deposits

Question #1: How do you account for a deposit paid to the title company that is made by a third party buyer when selling a RE investment?

A.	DR Cash/CR Deposit- deposit is received by title
B.	DR Cash/CR Deposit-NON REFUNDABLE deposit by title
C.	Recorded when deal dies w/non-refundable deposit
D.	Other Treatment
E.	Not applicable / Do not know



Polling Questions – Escrow Deposits

Answers #1: How do you account for a deposit paid to the title company that is made by a third party buyer when selling a RE investment?

(89 of 195 Attendees responded)

20 Responses 22.47%	DR Cash/CR Deposit- deposit is received by title
12 Responses 13.48	DR Cash/CR Deposit-NON REFUNDABLE deposit by title
31 Responses 34.83%	Recorded when deal dies w/non-refundable deposit
4 Responses 4.50%	Other Treatment
22 Responses 24.72%	Not applicable / Do not know



Hot Topic: Capitalized Interest

Presented By: Megan Hess, DWS



Polling Questions – Capitalized Interest

Question #1: Prop Level Cap Int–How does prop. Level cap int impact a property UNLEVERAGED return?

A.	Cap Int in the basis of the RE and reduced int. exp. in NOI
B.	Remove cap int from RE basis & exclude exp Offset from NOI
C.	Other Treatment
D.	Not applicable
E.	Do not know



Polling Questions – Capitalized Interest

Answers #1: Prop Level Cap Int–How does prop. Level cap int impact a property UNLEVERAGED return?

(97 of 195 Attendees responded)

32 Responses 32.99%	Cap Int in the basis of the RE and reduced int. exp. in NOI
8 Responses 8.25%	Remove cap int from RE basis & exclude exp Offset from NOI
3 Responses 3.09%	Other Treatment
22 Responses 22.68%	Not applicable
32 Responses 32.99%	Do not know



Polling Questions – Capitalized Interest

Question #2: Fund Level Cap. Int.–Where do you book additional fund level capitalized interest due to fund level leverage?

A.	Prop. Level Submissions – Inc basis and reduced NOI
B.	Prop. Level Submissions – Inc basis BUT Fund level reduced NOI
C.	Fund Level – Inc basis and reduced NOI
D.	Other Treatment
E.	Not applicable / Do not know



Polling Questions – Capitalized Interest

Answers #2: Fund Level Cap. Int.–Where do you book additional fund level capitalized interest due to fund level leverage?

(97 of 195 Attendees responded)

8 Responses 8.25%	Prop. Level Submissions – Inc basis and reduced NOI
4 Responses 4.12%	Prop. Level Submissions – Inc basis BUT Fund level reduced NOI
13 Responses 13.4%	Fund Level – Inc basis and reduced NOI
3 Responses 3.09%	Other Treatment
69 Responses 71.14%	Not applicable / Do not know



Hot Topic: **COVID Accounting**

Presented By: Mark Wojteczko, Deloitte



Polling Questions – COVID Accounting

Question #1: How have you accounted for deferrals under rec. approach with renegotiated extended repayment terms?

A.	Reversed/reserve the income if > rec. approach time frame
B.	No changes – Cash will just come in later
C.	Not applicable – Used Variable Lease Approach and didn't take income
D.	Do not know



Polling Questions – COVID Accounting

Answers #1: How have you accounted for deferrals under rec. approach with renegotiated extended repayment terms?

(107 of 195 Attendees responded)

28 Responses 26.17%	Reversed/reserve the income if > rec. approach time frame
33 Responses 30.84%	No changes – Cash will just come in later
11 Responses 10.28%	Not applicable – Used Variable Lease Approach and didn't take income
35 Responses 32.71%	Do not know



Polling Questions – COVID Accounting

Question #2: W/Receivable Approach, did you book reserves on extended/renegotiated repayment terms on previously executed deferrals?

A.	Booked a reserve on the deferral of 50%
B.	Booked a reserve on the deferral of 100%
C.	No reserve as agreed to extended repayment terms
D.	N/A – Used Var. Lease Approach w/No income
E.	Do not know



Polling Questions – COVID Accounting

Answers #2: W/Receivable Approach, did you book reserves on extended/renegotiated repayment terms on previously executed deferrals?

(84 of 195 Attendees responded)

13 Responses 15.48%	Booked a reserve on the deferral of 50%
8 Responses 9.52%	Booked a reserve on the deferral of 100%
28 Responses 33.33%	No reserve as agreed to extended repayment terms
9 Responses 10.71%	N/A – Used Var. Lease Approach w/No income
26 Responses 30.96%	Do not know



Polling Questions – COVID Accounting

Question #3: How long do you intend to include the COVID disclosures in your report?

A.	Will continue through 12/2021
B.	Not including in 2021
C.	Will stop before year end
D.	Still evaluating
E.	Do not know



Polling Questions – COVID Accounting

Answers #3: How long do you intend to include the COVID disclosures in your report?

(109 of 195 Attendees responded)

25 Responses 22.94%	Will continue through 12/2021
7 Responses 6.42%	Not including in 2021
3 Responses 2.75%	Will stop before year end
53 Responses 48.62%	Still evaluating
21 Responses 19.27%	Do not know



Hot Topic: Reporting Model - Operating vs. Non-Operating

Presented By: Sabeen Alwy, USAA Real Estate Company



Reporting Model

- **Overview**

- The financial reporting presentation model impacts the fund level time-weighted return (TWR) calculations for appreciation and income (the total return calculation remains the same across all financial reporting presentation models) and could lead to performance comparability issues
- Accounting Committee formed a cross discipline Task force in December 2020
- Presented the comparability issue at RS Council Meeting in February
- Educational session held on March 17th at NCREIF Winter conference
 - Create awareness
 - Shared examples of the reporting models and impacts to returns
 - Polled NCREIF Members in attendance

- **Next Steps:**

- Review presentation and more detailed example (excel model) and solicit feedback from key stakeholders
- Assessing responses to survey questions
- Additional outreach with all stakeholders
- Finalize prospectus for RS Council
- Consider future applicability of Operating Model (Net) in Accounting Manual



Hot Topic: TGER

Presented By: Benay Kirk, Alter Domus



TGER follow up questions

- **How does TGER impact Gross IRR calculations? Older convention, which seems best to add management fees and carry back to net cash flows and calculate Gross fund IRR (i.e. to assess Gross to Net spread). Fund level costs and expenses (the difference between Gross Deal IRR and Gross Fund IRR) are generally stated, allowable, sometimes auditable and irrelevant to GP performance.**
- **Components of TGER:**
 - Ongoing Management Fees
 - Performance Fees/Compensation
 - Transaction Fees
 - Vehicle Costs



TGER follow up questions

- Fund Level IRR Reporting Hierarchy:
 - Level 1 – Gross IRR before ALL investment management fees and vehicle costs
 - Level 2 – Gross IRR before all investment management fees and after deduction for vehicle costs
 - Level 3 – Net IRR after deduction ongoing management fees, transaction fees and before performance fees/compensation
 - Level 4 – Net IRR after all investment management fees



TGER follow up questions

CORRECTION to Q&A yesterday

Question: If a fund does not fair value the debt and the debt arrangement fees are amortized over the life of the loan, what amount would be included in TGER?

~~**Answer:** The amortized amount per the income statement would be included in TGER.~~

Answer: The amount is to represent the full amount paid regardless of whether the fund has adopted the fair value of debt option.



**Hot Topic:
Other Questions or Topics?**



Upcoming:

***Summer Conference: July 19 - 22, 2021
Chicago, IL***

Thank You!

rfraher@KPMG.com

hholsoeback@alvarezandmarsal.com

megan.hess@dws.com

heather.hopkins@clarionpartners.com