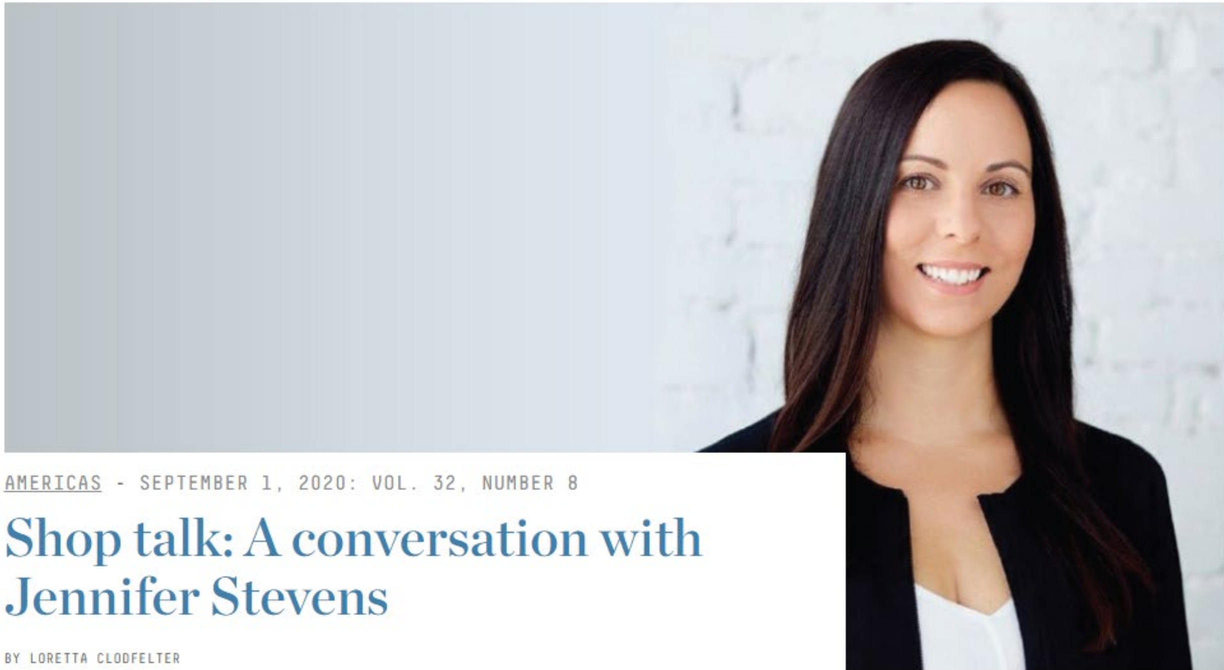

Jennifer Stevens has long focused on empowering the institutional investment community to elevate best practices. She has 16 years of experience with institutional portfolio management and consulting, strategic and investment planning, real asset investment underwriting, and a specialization in areas including environmental, social and governance (ESG) and industry best practices. Prior to launching Alliance Global Advisors, a firm focused on GP advisory solutions, Stevens held several positions within The Townsend Group, advising clients with cumulative total plan assets of more than $300 billion and approximately $20 billion in real estate allocations. Stevens recently tackled issues of governance in a conversation with Loretta Clodfelter, senior editor of Institutional Real Estate Americas.

In your experience, what do limited partners think about governance factors in the real estate investment industry?

In my experience, governance is reflective of elements that relate to organizational structure, oversight, culture, transparency and alignment of interest. Being a good fiduciary is a reflection of good governance.

When it comes to ESG, do you think governance gets more or less attention than the environmental and social factors?

If you believe the definition of governance provided, you may rightfully assume that limited partners — and their consultants — have always considered "governance" a critical part of their manager assessment and investment due diligence. Real estate investors have been evaluating the organizational structure, negotiating terms and conditions, requesting a voting seat on advisory committees, and encouraging better alignment of interest for decades. To the contrary, the environmental and social aspects of ESG didn't gain traction until the last few years. Investors were never skeptical of the G component, just the E and S components of ESG. Following the global financial crisis, there was emphasis on transparency in this previously private sector.

What are best practices for transparency and reporting when it comes to real estate investments?

Communication is critical. Despite the size and scale of the global real estate investment industry, this is a very small industry. Without exception, investment managers should be the first to alert their investors to challenges in the investment portfolio they manage — whether they are related to organizational changes, complications with a lender, overall performance or other headline risk. The first time investment officers and consultants hear about an issue should not be when a board member reads a headline and asks about it.

Disclose your concerns, especially post-COVID. Nobody is immune — yet. Always adhere to industry standards. Send notice of significant events in writing, and consider picking up the phone to discuss successes and challenges with your investors. For reports, include an executive summary with "need-to-know" information and statistics for those who may be short on time. Always have senior management read and sign off on quarterly and annual performance reporting — both the report itself and data provided to the LP/consultant's database. If you make a mistake, correct it.

Are there any new governance trends of which limited and general partners should be aware?

Diversity and inclusion [D&I] is considered part of governance, and one might say it is "trending." From a governance lens, it is essential to have leaders in the organization involved in setting the right tone for D&I initiatives and a governance structure that fosters an inclusive and aware work environment. If you don't have a D&I policy in place, it is time to institute one. Prominent LPs have incorporated D&I in their investment policy statements and DDQs.

In recent years, there has also been increased attention on fee disclosure, especially in California as a result of AB-2833. The rule relates to disclosure of all fees paid to private equity investment managers, but we also saw an extension to the alternatives asset classes.

In June 2020, ILPA [Institutional Limited Partners Association] released new guidance for enhancing the transparency of subscription lines of credit. Building and sustaining culture in a work-from-home environment can also relate to governance. Reporting on ESG efforts in itself is a matter of good governance.

Looking specifically at commingled funds, co-investments and joint ventures, what do limited partners want to see for terms and structure? Does it vary among investment types?

Key terms and conditions preferences vary based on investor opinion; risk classification — core versus noncore; vehicle type — separate accounts, open-end, closed-end, and special situations vehicles, such as co-investments and secondaries.

Limited partners seek to reward managers for consistent relative outperformance. This doesn't mean that the highest return wins. Risk must be considered and adequately addressed when establishing an investment vehicle. Despite the low interest-rate environment, investors seek to cap unnecessarily high leverage, recourse and cross-collateralization due to past experiences. Investor rights are carefully negotiated with the goal of limiting affiliate transactions, key-person risk and strategy drift. Manager co-investment is expected, and it is preferred that key persons contribute to the co-investment. In an open-end fund, other policies such as lock-out, redemption come into play.

Finally, investors seek to understand the components of fees and in what order the fees are paid. The market expects to pay a market-rate — or below market-rate — management fee and, in noncore, an incentive fee with a preferred return more closely aligned with the target return of the fund.

Do you have any advice for new and emerging managers when it comes to establishing governance best practices?

Our firm is centered around elevating best practices in the real asset investment industry. A new manager should improve transparency through reporting and communication. Integrate ESG across the organization early — many managers are playing catch-up right now. Create awareness of risk across the organization and assign a leader whose primary job responsibility is to help mitigate it. Align your interests with the LPs through investment-vehicle structuring, understanding the expectations of LPs and setting fair compensation structures. Establish a fair process for exclusivity, allocation and rotation. Refer to ILPA guidance and resources available through organizations such as IREI, NAREIM, NCREIF and PREA.