

Capital Markets Committee Call
September 26, 2006
11:00 – 12:00 p.m. ET

Introduction

MBA Staff Representative, Jennifer Williams, began the call and introduced herself to the members. She turned over the meeting to Joe Franzetti, Chair of the Capital Markets Committee. Joe Franzetti provided a brief overview of the topics that would be covered at the meeting by the respective MBA Staff Representatives, as follows:

I.	Catastrophic Insurance and TRIEA	George Green
II.	Insurance Availability	Katie Schwarting
III.	Basel II	George Green
IV.	Proposed Guidance on Banks' Concentrations of Commercial Loans	George Green
V.	Regulation AB	Jennifer Williams
VI.	Accounting Issues – FAS 140 and FAS 155	Jennifer Williams
VII.	Credit Rating Agency Legislation	Jennifer Williams

I. Catastrophic Insurance and TRIEA

During the call, George Green updated the group on MBA activities associated with natural disaster catastrophic insurance and the Terrorism Insurance Extension Act of 2005 (TRIEA). Joe Franzetti and other participants on the call highlighted the importance for the industry to find a resolution to terrorism insurance.

A. MBA Releases White Paper on Natural Disaster Catastrophic Insurance

On September 25th, MBA released its *White Paper on Natural Disaster Catastrophic Insurance – The Commercial Real Estate Finance Perspective*, which provides comprehensive information on all aspects of natural disaster insurance, including the effect of disasters on the insurance industry, the types and geographic occurrence of disasters, the current regulatory framework impacting insurance delivery, insurance availability and affordability and the impact on the CREF industry. The broad background provided in the White Paper is intended to serve as a primer for industry discussions about formulating solutions to the availability and affordability insurance crisis in some parts of the country.

B. Recent Government Studies

1. Government Accountability Office (GAO) Study

On September 28, 2006, the GAO released its report, *Terrorism Insurance: Measuring and Predicting Losses from Unconventional Weapons Is Difficult, but Some Industry Exposure Exists*. This report

indicated that, "Given the challenges faced by insurers in providing coverage for, and pricing, NBCR (nuclear, biological, chemical and radiological) risks, any purely market-driven expansion of coverage is highly unlikely in the foreseeable future."

2. President's Working Group Study

A provision of TRIEA calls for the President's Working Group on Financial Markets to complete a study that addresses the availability and affordability of terrorism risk insurance, including NBCR coverage and group life insurance coverage. *Terrorism Risk Insurance, The Report of the President's Working Group* was released on October 2, 2006. Although the report indicated that terrorism insurance coverage was widely available at prices that are declining, it failed to directly link the widespread availability of terrorism insurance to the federal reinsurance backstop offered by TRIEA and TRIEA's "make available" provision. The report indicates that TRIEA has negatively impacted the development of private sector terrorism insurance capacity. However, the report indicated that NBCR insurance from the private sector is generally not available.

As indicated in both the GAO and PWG studies, the lack of private sector capacity and appetite to provide NBCR insurance is a strong indicator that a long-term terrorism insurance solution will need to address NBCR events. The PWG report's conspicuous absence of policy recommendations leaves the administration's options open to negotiate with Congress a suitable long-term terrorism insurance solution.

3. Timing for Legislative Action

Legislative action on TRIEA is not expected to happen in 2006. However, the House is gearing up to address a long-term terrorism insurance solution early in its 2007 session. The Senate is expected to address this issue later in 2007 setting the stage for another possible House/Senate showdown over TRIEA in late 2007.

II. Insurance Availability

A. Evidence of Insurance Concerns with ACORD 28

During the call, Katie Schwarting explained the issues with the revised ACORD 28. The original ACORD 28 stated that the form was evidence that insurance was in force and conveyed all the rights and privileges afforded under the policy. Therefore, many lenders and their servicing agents accepted the ACORD 28 as Evidence of Insurance.

Effective July 29, 2006, ACORD has made changes to a standardized commercial property insurance form that adversely affects the commercial real estate finance (CREF) industry. For example, the ACORD 28 now states that the Evidence of Commercial Property Insurance is issued as a matter of information only and confers no rights upon the mortgagee or lender servicing agent. With regard to notification of a policy cancellation, the original ACORD 28 stated that the company would give the identified mortgagee and lender servicing agent written notice and would mail notification of any policy changes that would affect them. The form's changes have amended language to state that the issuing insurer will endeavor to provide written notice of cancellation, but that the failure to do so would not impose an obligation or liability upon the insurer, its agents or representatives.

Recently, MBA's Commercial/Multifamily staff met with National Association of Insurance Commissioners (NAIC) staff to relay concerns about the recent disclaimer changes in the ACORD 28 form (attached) and the broader Evidence of Insurance concerns facing the commercial real estate finance industry.

B. Insurance Availability Conference Calls

Katie Schwarting conducts periodic conference calls for both lenders and servicers who are dealing with insurance issues including proof of coverage, affordability, coverage amounts, and limitations. The email announcing the next scheduled conference call is directed to Asset Administration, Capital Markets, Mortgage Banking, Loan Origination, Portfolio Investors, and Multifamily Housing Committees. The call is part of a continuing series held to address critical and emerging issues surrounding property and casualty insurance.

III. Basel II

George Green provided a regulatory update on Basel II. The banking agencies issued earlier in September a revised Basel II proposal. MBA will be reviewing the proposal and will prepare comments by the deadline of March 26, 2007.

IV. Proposed Guidance on Banks' Concentrations of Commercial Loans

In April 2006, the MBA responded to the banking regulatory agencies proposed guidance to require enhanced risk management measures or risk-based capital for banks that meet certain threshold tests for commercial real estate (CRE) banking concentrations. In a comment letter, the MBA indicated that meeting the CRE threshold tests did not represent de facto evidence that enhanced risk management practices or increased risk-based capital was required; CRE portfolio diversification should be taken into account; and bank examiners should not be overly prescriptive when evaluating a bank's risk management practices. In a recent House Financial Services Committee hearing there were strong differences among banking regulatory agencies regarding the implementation of the guidance. Concerns were raised that the guidance was too prescriptive and those banks that met the threshold tests would be required to have increased risk-based capital or increased risk management measures. Given the lack of consensus among the banking regulatory agencies on this issue, the proposed guidance is not anticipated to be released in 2006.

V. Regulation AB

Jennifer Williams provided an update on the educational opportunities that MBA sponsors for member questions regarding Regulation AB. For example, MBA's Commercial/Multifamily Reg AB Working Group held a conference call on September 15th to specifically address the following Regulation AB reporting requirements:

1. Deadlines for reports required under the Exchange Act
2. The respective parties required to file such reports;
3. The scope of the respective reports to be filed; and,
4. The penalties for noncompliance with the Regulation AB reporting requirements.

Please contact Jennifer Williams if you would like to join MBA's Regulation AB Working Group.

VI. Accounting Issues – FAS 140 and FAS 155

A. FAS 140 and the Servicer Discretion Project

FASB is still on track for providing additional guidance on servicer discretion in Qualified Special Purpose Entities (QSPEs). On September 20, 2006, FASB staff met with the FASB Board during a FASB Education Session to discuss two approaches that the staff drafted to clarify permitted activities in a QSPE, including understanding the types of activities that a servicer can provide for mortgage loans. During the FASB Educational Session, some of the board members provided feedback on the two approaches and requested the staff to review the practical aspects of the two approaches. The approaches have not been made available to the public.

MBA continues to work with the Capital Consortium to follow progress from FASB on the servicer discretion project. The Capital Consortium, which includes MBA, CMSA, ASF/TBMA, RER and NAR, plans to wait until the approaches are finalized in a proposal at a future FASB Board meeting before continuing further advocacy options. Currently, the issue of permitted activities in a QSPE is coupled with many other FAS 140 amendment issues, including legal isolation. Currently, the FASB timetable on the FAS 140 project calls for an exposure draft for public comment in the second quarter of 2007, with a final statement in the fourth quarter of 2007. At the most recent FASB Board Meeting, which discussed the legal isolation issue, some FASB board members remarked that FASB may decide to separate certain FAS 140 issues from the overall FAS 140 project, such as legal isolation, depending on the progress FASB makes on the various FAS 140 issues.

B. FAS 155 – Accounting for Certain Hybrid Financial Instruments

Issuers, investors and others voiced their concerns to MBA regarding a recent interpretive view shared by some accounting firms that all prepayment options embedded in mortgage loans included in mortgage backed securities would be deemed embedded derivatives according to derivative interpretive guidance under FAS 133, Accounting for Derivatives and Hedging Activities, issued by FASB and revised upon the issuance of FAS 155. MBA hosted an educational call on September 20th regarding FAS 155 and the current interpretive guidance. MBA also plans to seek clarification from FASB on accounting for embedded prepayment options under the current accounting guidance.

VII. Credit Rating Agency Legislation

MBA has been following legislation introduced in both the House Committee on Financial Services and the Senate Banking Committee earlier this summer entitled The Credit Rating Agency Duopoly Relief Act of 2006. The legislation intends to bring more competition to the credit-rating industry, which Congress notes, is essentially controlled by two firms -- Moody's Investors Service and Standard and Poor's Rating Service. The Senate approved the legislation on September 22nd and the House passed the Senate's version of the bill this week. The Senate bill, sponsored by **Banking Chairman Shelby**, would allow firms that have issued ratings for at least three years to be certified as nationally recognized. Those firms also would have to obtain written endorsements from institutional investors who have used their ratings for the past three years. The Senate Banking Committee approved the measure in early August.

The new legislation directs the Securities and Exchange Commission (SEC) to propose new regulations over credit rating agencies by June 2007. MBA plans to provide industry comments once the SEC proposed the new regulations over credit rating agencies.