

**CAPITAL MARKETS COMMITTEE MEETING
MORTGAGE BANKERS ASSOCIATION
Sunday, February 6, 2005
1:00- 2:00 PM PT
SAN DIEGO, CALIFORNIA**

Chair:

**John Scheurer
Managing Director
Allied Capital**

Vice Chairs:

**Bret Ersoff
Managing Director
Lehman Brothers**

**Joseph P. Forte, Esq.
Partner
Dechert**

**Peter Horos
Senior Portfolio Manager
Allstate Investments**

**Guy K. Johnson
President
Johnson Capital**

**Gale Scott
Managing Director
Standard & Poor's**

Featured Speaker:

**Joseph Hu, Ph. D., Managing Director
Structured Finance Ratings, Standard & Poor's**

MBA Staff Representative:

**Leanne Tobias
Director, Commercial Real Estate Finance**

The Capital Markets Committee of the Mortgage Bankers Association met at 1:00 pm on February 6, 2005 at the Manchester Grand Hyatt in San Diego. The meeting was convened by Committee Chair John Scheurer, Managing Director of Allied Capital, who welcomed participants and attendees. Also representing the Committee were Vice Chairs Joseph Forte, Peter Horos, and Guy Johnson. Kim Diamond of Standard and Poor's represented Vice Chair Gale Scott, and John Herman of Lehman Brothers represented Vice Chair Bret Ersoff.

Dr. Joseph Hu, Managing Director of Standard and Poor's, provided an in-depth presentation of recent trends in the commercial mortgage-backed securities (CMBS) industry.

Key trends highlighted by Dr. Hu include the following:

--Record CMBS volumes in 2003 and 2004, due to interest rate declines and favorable credit performance.

--Core property groups represented in CMBS (office, industrial, multifamily and retail) have posted long-term default rates in the 3% range, while longitudinal loss severity rates for core property groups have been held to 30%. Default rates and loss severities for lodging and health care properties have been higher than for core property groups.

--CMBS spreads to Treasuries have tightened, and are at their lowest levels since 1998.

--The average size for CMBS issues increased to \$1.1 billion in 2004. Fusion structures (the combination of small "conduit" loans and large loans in one issue) have increased in popularity, accounting for 70% of 2004 issues.

--Super senior CMBS structures were introduced during 2004 and have proved popular with conservative investors and investors new to the CMBS asset class. Super senior CMBS structures offer two tranches of AAA-rated debt. The senior AAA tranche has higher subordination levels than typically encountered in most CMBS structures.

--Real estate fundamentals are expected to improve in 2005, and should contribute to continuing stability in CMBS performance, and continuing demand for CMBS. This assessment, however, is dependent on the strength of the economy. January 2005 economic data, including disappointing job growth figures, indicate lingering economic fragility. Increasing interest rates may also temper CMBS volumes in 2005.

Mr. Scheurer next introduced Brendon Weiss, legislative director for Congressman Vito Fossella (R- New York) and Jon Skarin, legislative director for Congressman Michael Capuano (D- Massachusetts). Messrs. Skarin and Weiss briefed the Committee on the outlook for real estate mortgage investment conduit (REMIC) modernization legislation and for extension of the Terrorism Risk Insurance Act (TRIA).

REMICs are the legal vehicles used to issue CMBS. Under federal law, unamended since 1986, common collateral modifications—including those approved by

lenders—are impermissible for properties financed through REMICs. Impermissible modifications include incidental demolitions necessary to reconfigure space for incoming tenants, building additions, the drawing down of reserve funds, the sale of pad parcels, outparcels and excess land, and the addition of loan collateral to facilitate property transfers. MBA and others in the real estate industry have proposed REMIC modernization legislation to modernize the REMIC laws and make CMBS financing more useful to borrowers.

Messrs. Skarin and Weiss observed that REMIC modernization was greeted with bipartisan support in the 108th Congress, and that several tax bills were expected to be introduced in the 109th Congress. They believe that the REMIC modernization proposal supported by MBA has an excellent chance of passage in the 109th Congress, but advised MBA members to advocate adoption of REMIC reform legislation to their Congressmen and Senators.

TRIA was enacted in response to the real estate market slowdown caused by inadequate terrorism insurance after September 11, 2001. TRIA requires that insurance carriers continue to offer terrorism insurance coverage on the same terms as other perils, and provides for federal reimbursement of insurers for most losses incurred in federally-certified foreign terrorism attacks which produce aggregate damages of \$5 million or more. MBA championed the enactment of TRIA to ensure the continued health of the commercial and multifamily real estate markets. Unless extended by Congress, TRIA will sunset on December 31, 2005. Insurers are already beginning to exclude from coverage terrorism losses that take place after December 31, 2005, should TRIA not be renewed. MBA strongly supports the extension of TRIA.

Messrs. Weiss and Skarin discussed the likelihood of TRIA extension beyond December 31, 2005. They noted that Congress would strongly prefer private market solutions to the provision of terrorism insurance, and that reductions of federal involvement are favored. Messrs. Weiss and Skarin also predicted that, at best, Congress might support a one-time extension of TRIA of no longer than two years, through December 31, 2007, and that extension is more likely to occur if private market solutions have been proposed by industry.

Mr. Forte noted that it would be helpful for the insurance industry to meet with members of Congress to discuss potential solutions that would allow the offering of continued terrorism insurance coverage for commercial and multifamily real estate.

Mr. Scheurer noted that TRIA extension and REMIC modernization were priorities for MBA's Capital Markets membership and that the Committee would be working with MBA to advocate favorable Congressional action on these fronts. Mr. Scheurer also urged MBA members to contact their Senators and Representatives to show support for the extension of TRIA and the modernization of the REMIC laws.

Mr. Scheurer thanked all participants and adjourned the meeting at 2:00 pm.