



Commercial Real Estate/Multifamily Finance Board of Governors (COMBOG)

**LOAN ORIGINATION COMMITTEE**

Maggie, Third Level  
Sunday, February 6, 2005  
11:30 a.m. – 12:30 p.m.

## Committee Meeting Notes

Chair: Deborah Schiavo, Bear, Stearns & Co. Inc.

Vice Chairs: Debra Hausser, Zurich North America  
Patrick Sargent, Esq., Andrews Kurth, LLP  
Nathan Stearns, LaSalle Bank N.A.  
Robert Vrchota, Fitch Ratings

MBA Staff Representative: Katie Schwarting  
(202) 557-2742 [kschwarting@mortgagebankers.org](mailto:kschwarting@mortgagebankers.org)

### I. Welcome and Introductions

### II. Complex and Large Loan Structures

- Attached is a list of issue the committee leadership would like feedback on and ideas for a possible white paper.

### III. MBA Inspection Form

- Here is a link to the current MBA created inspection form:  
<http://www.mortgagebankers.org/cref/docs/2005/Inspection%20Form.xls>
- MBA would like to bring together a group of industry representatives to review the current Inspection Form to ensure the form still meets the needs of the industry
  - Are there changes, additions or deletions to the current form?
- MBA will also work with Fannie Mae and Freddie Mac to try and achieve one standard inspection form across all industry products
- If you are interested in participating in the working group, please contact MBA staff representative, Katie Schwarting at [kschwarting@mortgagebankers.org](mailto:kschwarting@mortgagebankers.org)
- MBA anticipates starting the review project in March

### IV. E-Appraisal Effort

- CARS stands for Commercial Appraisal Report Standards.
- The CARS Review Team, led by Deb Schiavo and made up of MBA members on the Loan Origination Committee and the Technology Initiatives Committee, is working with the Appraisal Institute to develop fully electronic appraisals.
- The first step was to develop a data dictionary of fields used in commercial appraisal reports

- The Appraisal Institute, with input from the MBA CARS Review Team and other participants, have refined a key list of approximately 1000 data elements
- The CARS Review Team is working on the next steps in this effort. One of these is the development of an Executive Summary for appraisals that would be transmitted electronically
- The Working Group would like input from investors and the rating agencies on the Executive Summary information to ensure the information is useful to all the parties in the transaction

## V. MBA Updates

### a. Seismic Calculation

#### **Current Approach to Seismic Calculation**

- Probable Maximum Loss (“PML”) is the term historically used in commercial real estate to calculate and characterize building damageability in earthquakes, not including the damage to building contents, fixtures or equipment.
- The Loss estimates are expressed as a percentage of the building’s current replacement cost.
- American Society for Testing and Materials (“ASTM”) E2026-99 Standard Guide for Estimation of Damageability in Earthquakes (“ASTM Standard Guide”), offers options for how to calculate earthquake damage(s). However, the ASTM Standard Guide does not encourage the use of the term Probable Maximum Loss and has established new terminology, Scenario Loss (SL), Probable Loss (PL) and Scenario Expected Loss (SEL). This year, the ASTM Standard Guide is up for editorial modification and renewal.
- The different approaches have lead to much confusion and inconsistency in the industry. There are multiple definitions of PML in the market place and the ASTM Standard Guide complicates consistency, since it introduces new terminology for calculating losses.
- Some consultants, who complete the reports for lenders, utilize a PML calculation and then attest compliance with ASTM standard. Using PML calculation, which is not an ASTM standard, does not meet the ASTM Standard Guide requirements and therefore, can not be in compliance with ASTM guidelines.

#### **MBA Projects and Goals**

- Develop a Standard Practice for Seismic Due-Diligence as a work product of ASTM Task Group E26.25.82, Probable Maximum Loss. The MBA Seismic Working Group will work together with ASTM to develop an effective industry guide.
- Develop a Handbook for Seismic Due-Diligence Investigation that serves as a primer for understanding the impact of the calculation outcome, its technical background and offers suggestions on how to make decisions on retaining of evaluators, evaluation of reports, and selection of risk levels that are consistent with the fiduciary requirements of the user. The handbook will be written by the MBA Seismic Working Group.
- Goal - Establish a clear and consistent calculation method for establishing the maximum damage a building(s) would sustain as a result of a seismic event, as measured in percent of total damage. Create a handbook that gives the rationale for the standard and its technical background. Adoption and use in the commercial real estate community of the ASTM Standard Guide and MBA handbook, as the specific requirements for evaluation of the financial risk posed by a property, or portfolio of properties, to losses when earthquakes occur.

b. Legislative Update

**TRIA**

- Currently, the Terrorism Risk Insurance Act (TRIA) sunsets on December 31, 2005.
- MBA and a coalition of other industry members (CIAT – Coalition to Insure against Terrorism) are working together to try and get TRIA reauthorized for 2 more years, through December 31, 2007.
- Congress would like to hold hearing on the issue this year to determine whether it is necessary for TRIA to continue.
- Congress is also waiting to see the results from the Treasury Department study—which is not due until June 30. The study assesses the effectiveness of the TRIA program and the likely availability and affordability of terrorism insurance after its termination.
- On In January 5, 2005, the Congressional Budget Office (CBO) released a report called “Federal Terrorism Insurance: An Update,” assessing changes in the market since TRIA was enacted. The report, while recognizing the potential market disruptions associated a failure to renew TRIA, recommended that Congress consider a range of alternative policy initiatives, including revision of commercial/multifamily location patterns to less-dense areas and retrofitting to reduce property damages resulting from terrorist attacks. MBA and other industry observers are concerned that the CBO report ignores that terrorism risk cannot be modeled, and that retrofitting will not prevent catastrophic damages.
- MBA invited Congressional staff participated in the Legislative Committee meeting, they indicated the importance of the free market’s ability to provide terrorism insurance coverage without a federally supported program (TRIA)
- MBA members will have a chance to come to Washington, DC in April and meet with their specific legislators to explain the importance of renewing TRIA, as part of the MBA National Policy Conference, April 19-20.

**REMIC**

- The tax vehicles used to issue mortgage-backed securities are primarily real estate mortgage investment conduits (REMICs), created by Congress in 1986, and grantor trusts. Congress believed that the REMIC vehicle should be flexible enough to accommodate most legitimate business concerns.
- During 2004, MBA and its REMIC Task Force spearheaded a real estate industry coalition to develop a REMIC modernization proposal that would make REMICs more useful to borrowers.
- Examples of recommended changes include releases, additions and substitutions of collateral; the alteration of guarantees, reserves, or other credit enhancements; demolition of part of the property incidental to renovation or expansion; or prepayment of the loan and recasting of principal payments. None of these changes involve new loan origination activity and are, thus, consistent with the pass-through nature of a REMIC or grantor trust. Materially extending a final maturity date for a non-defaulted loan or increasing the principal balance of a loan would generally not be allowed.
- The industry’s proposal does not change the way in which REMICs or grantor trusts are taxed.
- The industry proposal led to the 2004 introduction of federal legislation, S. 2422, introduced by Senators Gordon Smith and Kent Conrad, and H.R. 4113, introduced

by Congressmen Mark Foley and Earl Pomeroy, to modernize the REMIC rules. While the legislation did not pass Congress in 2004, it attracted bipartisan support and was praised as “sound public policy” by Chairman Bill Thomas of the House Ways and Means Committee. The legislation will be reintroduced in early 2005.

- MBA and its industry partners will continue to work with the 109<sup>th</sup> Congress to advocate modernization of the REMIC laws.
- The first step is looking for the right tax bill to attach the REMIC language.
- One possibility is Bush’s push to make changes to the U.S. Tax Code – Friday, January 7 President Bush appointed a 9 member panel to look at reforms to the tax code. The panel is to report to Treasury by July 31.
- MBA and its partners will also work with the Treasury Department to advocate regulatory reforms that would make REMICs more useful to borrowers.

c. Mold Update

- **Draft Mold White Paper**
  - Open for public comment until **Wednesday, March 23** at 5:00 p.m., Eastern
- Link to draft Mold White Paper:  
<http://www.mortgagebankers.org/cref/docs/2005/Consolidated%20Paper%20-%20FINAL%20DRAFT.pdf>
- The paper includes:
  - Executive Summary
  - Paper on the issues
    - History of mold and commercial real estate
    - Effects of mold and dampness on the marketplace
    - Managing mold and the risks
    - Looking Ahead – future
  - Helpful Appendixes – Resource Guides
- QUESTION: Was Legionnaire’s disease covered in the National Academy of Science study on damp indoor spaces and health?
  - ANSWER: Yes and Legionnaire disease is also touched on in the MBA White Paper
- **ASTM Mold Assessment Committee**
  - MBA continues to work with ASTM to develop an inspection standard for visible signs of mold and water damage on commercial properties
  - Next ASTM meeting is schedule for Wednesday, April 20 in Reno, NV
  - The ASTM Mold Task Force anticipates completing the standard by Fall 2005
- **Conyers Bill – revisions in 2005**
- Congressman John Conyers Jr. (D – MI) introduced a mold bill in 2003, called United States Toxic Mold Safety and Protection Act of 2003 (H.R. 1268), also known as the Melina Bill. The Bill ultimately did not get enough signatures and died in December 2004
  - Conyers is intending to reintroduce a bill on mold – that the new bill is his “top priority for 2005.”
  - MBA contacted the Conyers’ staff member primarily responsible for drafting the mold legislation, Mr. Joel Segal. Mr. Segal is interested in sitting down

with real estate representatives to discuss the proposed draft legislation he is writing. He expressed how important bi-partisan participation on the legislation is for passing the bill.

- MBA will continue to provide further updates in the upcoming months on the progress of this bill.

d. SEC ABS Rule – FINAL

- On January 7, the SEC offered the final rule in the Federal Registrar
- Rule is effective 60 days after filing (March 8, 2005), however, the SEC built in an escalating transition period of requirements
  - Full compliance required by January 1, 2006
  - First annual attestation and servicer compliance statement will be March 2007
- Highlights:
  - “Servicer” definition: includes anyone responsible for management or collection of pooled assets AND anyone responsible for allocation or distribution to holders of the securities. This definition will include most CMBS trustees within the SEC definition of servicer.
  - Disclosure: SEC raised the disclosure information threshold for unaffiliated servicers – 2 separate requirements:
    - 10% or higher of the pooled assets threshold - identify the servicer
    - 20% or higher of the pooled assets threshold – full disclosure required
  - Disclosure of Static Pool data
    - 20 SEC approved the use of a company’s website for display of static pool data, the historical performance data for past deals
    - Specifically on website information disclosure of static pool data, the SEC will require a direct link to the relevant information and will not accept information generally available on company websites.
  - Disclosure of Points and Fees
    - SEC removed any specific language requiring a lender to disclose the amount of points and fees charged to a borrower
  - Annual Reporting – Responsible Party concept and Filing 10-K Reports
    - SEC eliminated their proposed “responsible party concept,” which would require one party (the depositor or servicer) to attest to the compliance of all other parties in the transaction
    - Instead, one party (the depositor or servicer) will gather the external audit report and compliance statements from each party and offer them as part of the 10-K Report. The one party who files the 10-K will also assert that all parties required to offer the audit report and compliance have been received and are included with the 10-K Report.
    - New 10-D report for distribution and pool performance information for the distribution period and also certain non-financial disclosures
  - Annual Reporting – External Audit
    - The new annual report replaces the current USAP standard.
    - SEC requires that each servicer in the transaction, servicing 5% or more of the pooled assets must complete an independent third party annual audit of their business, to ensure servicer compliance with the servicing standards.
    - The third party auditor will prepare a report based on “servicing criteria” and looking on a “platform” basis at all transactions

- Annual Reporting – Servicer Compliance
    - The servicer will provide a statement that on a transaction level basis, that the servicer is in compliance and has fulfilled all of its obligations with respect to all transaction documents
  - Sarbanes-Oxley Reporting
    - SEC added language the SOX certificate, which codifies the ability of the certifying party (the signor) to reasonably rely on information provided by unaffiliated third parties
  - A link to a copy of the MBA Issue Paper is included. The Issue Paper contrasts the issues MBA raised in their letter submitted during the proposed rule comment period and the final outcome of the rule.
    - Link to MBA Issue Paper:  
<http://www.mortgagebankers.org/documents/NewsLink/Letters/022405issuepaper.pdf>
  - A link to the actual SEC ABS Rule is available on the MBA website and provided here:
    - Link to SEC ABS Rule: <http://www.sec.gov/rules/final/33-8518fr.pdf>
  - MBA is currently hosting a conference call for MBA members to listen to the SEC staff discuss the final rule. The call will be held on Tuesday, March 1.
- e. Quarterly Informational Conference Calls
- What should the topic be for our next informational conference call?
  - Suggestions:
    - Tenants in Common Structures
      - Tenant changes without lender consent
      - Management issues
      - Administrative issues
      - Patriot Act
      - How to make them less risky?
      - 1031-Exchanges
    - Earnouts – ex: \$58 million loan with a \$10 million earnout
      - How to account for the \$10 million?
      - How to disclose the \$10 million?
      - Effect on Loan to Value (LTV)?
      - Effect on Debt Service Coverage (DSCR)?
      - Letter of Credit (LOC) for the \$10 million as insurance, but investors don't want a \$10 million dollar pay down of the loan
    - Green Buildings
      - Construction
      - Environmentally safe?
    - Broker Compensation
  - Request – MBA send out a short description of the issue prior to the conference call

VI. Emerging Issues and Concerns  
None reported

VII. Other Business  
None reported