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Subject: *National Real Estate Organizations' Joint Letter on Commercial/Multifamily Mortgage Finance Re:* Credit Risk Retention — *OCC* (Docket No. OCC-2011-0002, RIN 1557-AD40), *Federal Reserve System* (Docket No. R-1411, RIN 7100-AD-70), *FDIC* (RIN 3064-AD74), *FHFA* (RIN 2590-AA43), *SEC* (File No. S7-14-11, RIN 3235-AK96), *HUD* (Docket No. FR-5504-P-01, RIN 2501-AD53);

Ladies and Gentlemen:

The undersigned organizations welcome the opportunity to provide the collective insights of the real estate industry regarding the commercial and multifamily real estate elements of the proposed rule on credit risk retention ("Proposed Rule").[1] The Proposed Rule implements the credit risk retention requirements of section 15G of the Securities Exchange Act of 1934,[2] as added by section 941 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act" or "Act").[3] We recognize the extraordinary effort and

[1] 76 Fed. Reg. 24090 (April 29, 2011).
[2] 15 U.S.C. § 78o-11. Section 15G generally requires the securitizer of asset-backed securities to retain not less than five percent of the credit risk of the assets collateralizing the asset-backed securities. Section 15G includes a number of exemptions from these requirements, including an exemption for commercial mortgage-backed securities ("CMBS") that meet certain conditions.
[3] Public Law 111-203, 124 Stat. 1376-2223 (July 21, 2010). The proposed rule was jointly issued by the Office of the Comptroller of the Currency, Treasury ("OCC"), Board of Governors of the Federal Reserve

coordination that were required to develop and publish the Proposed Rule. We commend the Agencies for their thoughtful consideration of the numerous and complex aspects of the Dodd-Frank Act's risk retention provisions.

While each of the undersigned organizations may submit comment letters from their respective memberships' perspectives, we emphasize the importance of commercial and multifamily real estate as an asset class and collectively believe that certain policy principles should guide the risk retention rulemaking. We therefore recommend particular modifications to the Proposed Rule, as discussed below.

COMMERCIAL AND MULTIFAMILY REAL ESTATE

Commercial and multifamily real estate ("CRE") — including apartment buildings, office buildings, shopping centers, industrial facilities, health care and hotel properties — house virtually all of the nation's business and one-in-seven households.[4] A vibrant and sound CRE market is integral to our Nation's economy. The securitization market represents an important source of capital for CRE.

Concerns have been raised by the Financial Stability Oversight Council in a Dodd-Frank Act mandated report[5] regarding the potentially negative macroeconomic effects that the proposed risk retention rules could trigger, which warns that "overly restrictive, risk retention could constrain the formation of credit, which could adversely impact economic growth."[6] Given the fragile state of the U.S. economy, this broader economic view is of vital concern to CRE organizations — particularly for "smaller market participants."[7] We believe that the Agencies should take into strong consideration the results of a comprehensive cost benefit analysis of how the Proposed Rule will affect CRE and the overall national economy before the rules are finalized.

As the Agencies develop a risk retention framework for CMBS, it is important to be aware of the inherent and unique characteristics of CMBS that help mitigate the risks associated with securitization. More specifically, these characteristics relate not only to the type and sophistication of the borrowers, but to the structure of issued securities, the nature of the

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System ("Federal Reserve Board"), Federal Deposit Insurance Corporation ("FDIC"), U.S. Securities and Exchange Commission ("Commission"), Federal Housing Finance Agency ("FHFA"), and Department of Housing and Urban Development ("HUD") (collectively, the "Agencies").

[4] US Census Bureau, 2007 American Housing Survey.

[5] Financial Stability Oversight Council (FSOC), "Macroeconomic Effects of Risk Retention Requirements" (January 2011).

[6] FSOC Report at 3.

[7] Board of Governors of the Federal Reserve System, "Report to the Congress on Risk Retention" (October 2010) at 3.

underlying collateral, and the existing level of transparency in CMBS deals.

- *Commercial and Multifamily Borrowers.* Commercial and multifamily borrowers are sophisticated businesses with cash flows based on business operations and/or tenants under leases (*i.e.*, "income-producing" properties). Additionally, securitized commercial mortgages have different terms (generally 5 to 10 year "balloon" loans), and they are, in the vast majority of cases, "non-recourse" loans that rely on the credit of the underlying collateral, the ability of management, and the stability of tenants.

- *Structure of CMBS.* There are multiple levels of review and diligence concerning the collateral underlying CMBS, which help ensure that investors have a well-informed, thorough understanding of the risks involved with their investment. Specifically, in-depth property-level analysis and review are done by investors as part of their investment due diligence of CMBS bonds. Moreover, non-statistical, in-depth analysis is performed on CMBS that includes gathering detailed information about the nature of the income-producing properties and the integrity of their cash flows, the credit quality of tenants, and the experience and integrity of the borrower and its sponsors.

- *Third-Party Purchaser ("B-piece Buyer") Re-Underwrites Risk.* CMBS bond issuances typically include a first-loss, non-investment grade bond component. The third-party investors that purchase these subordinate securities (referred to as "B-piece" or "first-loss" buyers) conduct their own extensive due diligence (usually including, for example, site visits to every property that collateralizes a loan in the loan pool) and re-underwrite all of the loans in a proposed pool. Because of this, the B-piece buyers typically either negotiate the removal of any loans they consider to be unsatisfactory from a credit perspective or negotiate price adjustments if the loans are to remain in the pool. They specifically negotiate with bond sponsors or originators to purchase this non-investment-grade risk component of the bond offering.

- *Transparency.* CMBS market participants have access to a wealth of information through initial offering documents that provide significant details on the loans, the properties that secure the loans, the borrowers, and the deal structure. In addition, the CRE Finance Council-developed Investor Reporting Package™ provides access to loan-, property-, and bond-level information while securities are outstanding, including updated loan and bond balances, ongoing property performance, the amount of interest and principal received, and updated bond ratings.

Section 941 of the Dodd-Frank Act expressly contemplates differentiation among securitization of various asset classes. The legislative history of the Act, as well as the Federal Reserve Board's report to Congress on risk retention, underscores the importance of asset classspecific regulation.[8] We urge the Agencies to take into account the character of CRE in implementing the risk retention rules and refrain from a one-size-fits-all approach.

PUBLIC POLICY PRINCIPLES

We are committed to facilitating the establishment of a fully-functioning, transparent, liquid and responsible securitization market for commercial and multifamily real estate mortgages. Because the CMBS market involves a complex set of interactions among numerous stakeholders, we believe that the Proposed Rule should advance the following public policy objectives:

- Advance an alignment of interests among investors, issuers, originators, servicers and borrowers;
- Support credible, safe and sound lending practices that reflect the needs and sophistication of issuers, investors, and the owners of commercial and multifamily real estate properties;
- Support the efficient flow of mortgage capital from investors to borrowers;
- Help restore investor confidence and the ability of investors to accurately assess the risks in the collateral and the securitization structure;
- Ensure risks are properly assessed, mitigated and/or priced by those who assume or control them; and
- Increase transparency across all aspects of the market, assuring adequate information for investors while protecting individual privacy and proprietary business models.

RECOMMENDATIONS

Consistent with these principles, we urge the Agencies to adopt the following recommendations:

Risk Retention Structures that Consider Market Dynamism. Because markets are dynamic, flexibility — including the availability of a broad range of risk retention structures — is critical to a well-functioning CMBS market. We support the optional menu approach for risk retention structures in the Proposed Rule because it generally would accommodate a broad range of market participants. We also recommend that the Agencies permit additional, optional structures, so long as the base five percent risk retention requirement is satisfied.

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[8] "The Committee believes that implementation of risk retention obligations should recognize the differences in securitization practices for various asset classes." S. Rep. No. 111-176 at 130 (2010).

Eliminate the Proposed Premium Capture Cash Reserve Account. We are concerned that a particular element of the Proposed Rule, the Premium Capture Cash Reserve Account (PCCRA), as proposed, will fundamentally alter the economics of the CMBS business model and effectively eliminate the incentives for securitization. By requiring financial returns from CMBS issuance to be placed in an account that is in a first-loss position, the ability of issuers to earn a return will be severely curtailed or eliminated. We therefore urge the elimination of the PCCRA.

Risk Retention Hold Period. The CMBS market provides extensive and robust transparency with regard to the performance of underlying loans, which allows investors the opportunity to determine loan performance and identify loans or securitizations that are not performing as expected. Accordingly, the required risk retention hold period need not be for the life of the securities for holders of risk retention, whether issuers, originators or first-loss third-party purchasers.

Third-Party Risk Retention. The Dodd-Frank Act, through the "Crapo Amendment" provisions, takes into account the critical role served by third-party purchasers of the first-loss, B-piece CMBS position. We support the role of the B-piece buyer serving the risk retention function and emphasize the importance of the economic viability of this structure, consistent with the statutory Dodd-Frank language. We recommend that the risk retention requirements be crafted in a manner that provides sufficient incentives for third-party purchasers to serve as holders of risk retention, while recognizing and supporting the interests of all other investors in the CMBS.

Underwriting Standards for Zero Risk Retention. The Proposed Rule sets forth underwriting requirements in which zero risk retention would be required, as permitted by the Dodd-Frank Act. Under the statutory directive, the risk retention requirements should set forth a meaningful exemption that more closely aligns with the character of "low-risk" CRE loans. The proposed underwriting standards should be both carefully reviewed to eliminate those requirements that are clearly out of conformity with CRE lending practicing, and enhanced to create a workable exemption for high-quality CRE loans. The use of effective, industry-developed representations and warranties should also be considered.

Qualified Loan Exemption. Section 941 of the Dodd-Frank Act exempts certain types of securitizations from risk retention requirements and authorizes the Agencies to exempt or establish a lower risk retention requirement for other types of securitizations. We are concerned about the manner in which the Agencies would define a CRE loan — specifically, the Proposed Rule's categorical exclusion of any loan to a real estate investment trust (REIT). This would inappropriately penalize a REIT seeking to finance its property by unnecessarily increasing its borrowing costs compared to other non-REIT property owners. As the final credit risk retention rule is developed, we strongly urge the Agencies not to exclude loans to REITs from potentially meeting the definition of qualifying CRE loans.

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This letter represents the broad strokes of the industry's position on the Proposed Rule; the individual responses by the undersigned organizations will provide a more detailed examination of the issues raised in the Proposed Rule.

We appreciate the Agencies' objectives. We are concerned, however, about the impact the Proposed Rule, as currently written, would have on the new issue CMBS market. We believe that the Agencies should appropriately craft the Proposed Rule to ensure a liquid, credible, safe and sound CMBS market. This involves, among other things, taking into consideration the potential economic impact of the regulatory regime.

Thank you for the opportunity to submit comments on this critically-important rulemaking.

Sincerely,

American Land Title Association
American Securitization Forum
Building Owners and Managers Association International
CCIM Institute
Commercial Real Estate (CRE) Finance Council
Financial Services Roundtable
Institute of Real Estate Management
International Council of Shopping Centers
Mortgage Bankers Association
NAIOP, Commercial Real Estate Development Association
National Apartment Association
National Association of Home Builders
National Association of Real Estate Investment Trusts
National Association of Realtors
National Multi Housing Council
Society of Industrial and Office Realtors
The Real Estate Roundtable