



April 19, 2006

Treasury's Office of Financial Institutions Policy
Attention: President's Working Group on Financial Markets Public Record Comments
Room 3160 Annex
Department of Treasury
1500 Pennsylvania Avenue, N.W.
Washington, DC 20220

RE: President's Working Group on Financial Markets: Terrorism Risk Insurance Analysis

Ladies and Gentlemen:

The Mortgage Bankers Association (MBA) applauds the President's Working Group on Financial Markets (PWG) for its efforts to develop a long-term terrorism insurance solution. We believe that a long-term terrorism insurance solution is not only essential to the efficient operation of the commercial real estate and finance sectors but is also a key component in the nation's preparedness against future terrorist attacks. Accordingly, MBA and its members stand ready to assist the PWG in its efforts to craft a long-term terrorism insurance solution.

On December 22, 2005 the President signed into law the Terrorism Risk Insurance Extension Act of 2005 (TRIEA). TRIEA extended, with amendments, the Terrorism Risk Insurance Act of 2002 (TRIA) until December 31, 2007. Recognizing that the war on terror is likely to extend well beyond TRIEA's expiration, a long-term terrorism insurance solution needs to be developed. TRIEA recognized this and charged the PWG with preparing a report on the long-term availability and affordability of terrorism insurance that also addresses group life coverage and coverage for chemical, nuclear, biological, and radiological events.

Published in the *Federal Register* on March 7, 2006, the Department of Treasury (Treasury), requested comments on 27 questions relating to the long-term availability and affordability of terrorism insurance. The questions focused on three topics:

1. Long-Term Availability and Affordability of Terrorism Risk Insurance;
2. Long-Term Availability and Affordability of Group Life Insurance Coverage; and,
3. Long-Term Availability and Affordability of Insurance Coverage for Chemical, Nuclear, Biological, and Radiological (CNBR) Events Caused by Terrorism

These insurance coverage related questions were geared toward insurance providers that possess the technical expertise and primary data sources to address the questions' high level of specificity. Given our members' concentration in real estate finance and mortgage loan servicing (servicers), not insurance, MBA will focus its comments on the features, or outcomes, of a long-term terrorism insurance solution rather than the specific formulaics of a long-term terrorism insurance solution. Given this focus, the balance of these comments will address the role MBA members play in commercial real estate finance; challenges facing commercial real estate finance lenders and loan servicers in meeting their fiduciary responsibilities regarding insurance coverage; results of MBA's terrorism survey demonstrating member concerns; the importance that terrorism insurance plays in the commercial real estate finance industry; and, finally the principles that we believe are necessary for a long-term solution for terrorism insurance.

MBA Members

MBA is the national association representing the real estate finance industry, an industry that employs more than 500,000 people in virtually every community in the country. Our membership of more than 3,000 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. MBA members provide over 70 percent of the nation's residential mortgages and the vast majority of its commercial mortgages. The MBA represents the single largest domestic debt sector in the country. Additionally, MBA is part of the 75-member Coalition to Insure Against Terrorism (CIAT). CIAT represents a wide range of businesses and organizations throughout the transportation, real estate, manufacturing, construction, entertainment and retail sectors.

Mortgage lenders typically place debt in an amount equivalent to 80 percent of the property's value while the owner's share is typically limited to a 20 percent equity position. As a result, the greatest risk for property and casualty events is effectively absorbed by the commercial real estate finance industry. Totalling more than \$2.5 trillion in investments, the commercial/multifamily side of the mortgage industry includes transactions made by commercial banks, life insurance companies, and individual and institutional investors through commercial mortgage-backed securities (CMBS). Over the past several years, CMBS and commercial mortgage loans have outperformed other asset classes, such as corporate bonds. These investments are a part of chief investment officers' permanent allocations and the retirement accounts and/or pensions of many people on fixed incomes.

A long-term solution for terrorism insurance coverage is therefore a crucial issue for MBA's members, especially servicers whose function includes receipt of insurance and mortgage payments, customer service, escrow administration, investor accounting, collections, and foreclosures, as well as ensuring that properties have necessary insurance coverage in place. MBA's members hold the single largest share of real estate debt outstanding in all markets and bear the lion's share of the financial risk associated with property damage or destruction.

Challenges Facing Commercial Real Estate Lenders and Servicers

Lenders and servicers bear the fiduciary responsibility, as described in transaction legal documents, of ensuring that required insurance coverage, including terrorism insurance coverage, is in place during the life of the loan. Unfortunately, prevailing insurance industry practices have greatly complicated the ability of lenders and servicers to meet their fiduciary responsibilities regarding insurance coverage, including terrorism insurance. Because the contract for property insurance is between the insurance company and property owner, not lenders or servicers, insurance companies are under no legal obligation to provide insurance coverage contracts or summaries to lenders and servicers. However, lenders and servicers are contractually required to verify that insurance coverage specified in the loan documents is in place on an annual basis. When insurance coverage information is not provided, lenders and servicers are required to expend additional resources to track down this information from insurance companies or property owners.

In the case of terrorism insurance coverage, there is significant risk for servicers not to be able to meet their fiduciary responsibility to verify that terrorism coverage is in place. For example, when commercial insurance carriers excluded terrorism insurance coverage prior to TRIA's enactment, the risk of a catastrophic terrorism loss shifted from the commercial insurance industry to the commercial real estate finance industry. For this reason, lenders and loan servicers who bear a fiduciary responsibility, as described in transaction legal documents, to investors and funding sources, have the greatest "standing" among all industries in assuring broad availability and affordability of terrorism insurance. Commercial real estate lenders and their servicing firms are likely to experience operational difficulties with regard to their existing portfolios if a long-term terrorism insurance solution is not created before TRIEA expires.

MBA Terrorism Insurance Survey

Seeking a long-term solution to terrorism insurance is underscored by the role that both TRIA and TRIEA have played in ensuring that terrorism insurance is both available and affordable. A study performed by the MBA in the Spring of 2004 demonstrated that terrorism insurance coverage was both widely required and, thanks to TRIA, widely available. MBA surveyed loan administrators who serviced over \$656 billion of the then approximately \$2 trillion in commercial real estate debt outstanding. The survey showed that 94 percent of that \$656 billion required terrorism insurance. It also found that 84 percent had terrorism insurance in place. The 10 percent of commercial/multifamily debt for which terrorism insurance was required, but was not in place, included properties for which the servicer and borrower were working to place coverage, properties for which the requirements have been waived and some properties that may have "all-risk" coverage that have been deemed to include terrorism coverage, but for which an explicit statement of terrorism coverage did not exist.

Also within that study, servicers estimated that if insurance companies were not mandated to provide terrorism insurance, approximately 80 percent of that \$656 billion in debt would not have terrorism coverage. The average loan size in the survey was just over \$5 million and there did not appear to be any relationship between the average loan size of the servicer and the percentage of that servicer's portfolio with terrorism insurance coverage. This counters the popular belief that terrorism coverage is only necessary for "trophy properties". Thus, the lack of availability of terrorism insurance in a post-TRIEA environment would catch a wide range of borrowers, servicers, rating agencies and others between obligations to have terrorism insurance in place and a lack of affordable coverage.

Post September 11, 2001 Terrorism Insurance Market Challenges

Following the terrorist attacks of September 11, 2001, insurance coverage for potential losses from terrorism was largely unavailable and, when available, extremely expensive and often inadequate. MBA stood with the Congress and President Bush to pass TRIA in November 2002 and its extension, TRIEA, in 2005. The need for TRIA and TRIEA was compelling then and continues to be now. Terrorism insurance is a necessary component in today's society evidenced by the fact that a majority of our members require legal documents to provide for coverage when closing commercial mortgage transactions. This required coverage assures marketplace stability, information transparency, and continuity for the commercial real estate finance industry. MBA agrees with the assertion contained in the Treasury Department's June 30, 2005 Report on TRIA (Treasury Report) that the Program has been effective. We also agree that if TRIEA is allowed to sunset without a long-term terrorism insurance solution in place, terrorism risk insurance coverage will become less available and increasingly more costly.

Another key development post September 11 was the implementation of ACORD Standard 28-Evidence of Commercial Property Insurance (ACORD 28). This form was introduced October 31, 2003 and endorsed by the National Association of Insurance Commissioners (NAIC), the Council of Insurance Agents and Brokers (CIAB), major lenders and servicers, Freddie Mac, Fannie Mae, and MBA. ACORD 28 is a stand alone document to be used by the commercial real estate finance industry as a way to track property insurance coverage--such as terrorism, business interruption or mold coverage. However, it is imperative that the insurance industry use this form to prevent wasted resources tracking whether terrorism insurance is in place and to avoid market disruptions due to the lack of clarity.

ACORD 28 is intended to boost investor confidence, increase information transparency, lower operating expenses and ultimately enhance liquidity in the marketplace. ACORD 28 is important because it serves as a proof of coverage until the lender or servicer is able to obtain a copy of the insurance policy.

MBA recommends that the use of ACORD 28 be included in any long-term solution as a vehicle for communicating terrorism insurance coverage to lenders and servicers.

Principles for a Long-Term Terrorism Insurance Solution

The MBA will be evaluating specific long-term terrorism solution proposals based on a set of principles that will ensure adequate insurance for terrorism, as required by commercial real estate finance lenders and servicers. MBA will examine each long-term terrorism insurance proposal based on it meeting the following principles:

- Widely Available - Terrorism insurance needs to be widely available, which would require the existing "make available" provision in TRIEA be included in a long-term terrorism insurance solution.
- No Interruptions - The long-term terrorism insurance solution should be crafted in a manner that eliminates short-term interruptions in terrorism insurance availability or price shocks when it is implemented.
- Affordable - Terrorism insurance needs to be priced in an affordable manner.
- All-Peril Coverage – Terrorism insurance will cover all-perils including nuclear, biological, chemical, and radiological threats.
- All Terrorism Sources – Terrorism insurance should cover both foreign and domestic source terrorist events.
- Lender/Servicer Notifications - lenders/servicers are listed as mortgagee, loss payee and additional insured depending on the loan documentation and as such they are entitled to specific notifications of coverage lapses, gaps, and renewals. Any long-term solution needs to preserve and implement the required notification. MBA has suggested that the NAIC issue a Model Bulletin recommending every state require the use of ACORD 28 in order to promote the widespread use and communication of coverage between the insurance industry and lenders and servicers.

The intent of TRIA was to provide a short-term federal terrorism reinsurance program that would provide a window of opportunity for a thoughtfully considered long-term solution to emerge. As indicated by the Treasury Report, challenges remain in predicting terrorism risk. This uncertainty has stymied concerted industry efforts to develop an exclusive private sector terrorism insurance solution. The charge of the PWG to develop a long-term solution for terrorism insurance provides the opportunity to reinvigorate this discussion by exploring the full spectrum of potential solutions.

As the nation's largest representative of commercial real estate mortgage lenders and servicers, MBA stands ready to provide any assistance that the PWG may require to ensure any long-term terrorism solution will protect the largest property stakeholders. We look forward to the opportunity of partnering with the PWG and the insurance industry to help develop a long-term solution for terrorism insurance that makes coverage inclusive, available and affordable. Should you have any questions or need clarification about this submittal, please contact George Green at (202) 557-2840 or by e-mail at ggreen@mortgagebankers.org.

Most sincerely,



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