



Commercial Mortgage Securities Association™ (CMSA)

Position Paper

Subject: Natural Catastrophe Insurance

Background: In recent years, the availability and affordability of 'commercial' insurance coverage for natural catastrophes has been dwindling, which threatens the health of the commercial real estate sector and the overall U.S. economy. The damage caused by of natural disasters in recent years (well over \$60 Billion in the last two years), coupled with the fear of future catastrophes, has placed a tremendous strain in many insurance markets. The lack of affordable insurance coverage impacts the commercial mortgage-backed securities (CMBS) whose underlying loans require "all risk" insurance.

As of June 2006, \$44 billion of properties underlying outstanding CMBS were in wind prone areas, including more than \$36.5 billion in loans spread over 5,428 projects in Florida. During 2006, CMBS servicers also reported sharp increases in windstorm insurance premiums ranging from 25% to 400%. Further, there appears to be a growing capacity shortage as many borrowers have found that they are unable to secure coverage equal to the replacement cost of their buildings as required to satisfy their loan commitments. This situation jeopardizes future economic growth and exposes both current policyholders and taxpayers who are bear the cost through post-disaster, ad hoc funding that is costly and inefficient.

As such, CMSA has been engaged in addressing the problem in advance of natural disaster by facilitating the private market in a way that serves policyholders and protects taxpayers. To that end, CMSA has been actively involved in the creation and organization of a coalition of commercial insurance policyholders who have joined to address this issue, the "Natural Catastrophe Policyholders Coalition (NCPC)." The coalition's mission is to promote policies that encourage the availability and affordability of catastrophe insurance for businesses. As a founding member of NCPC, CMSA is working with its industry counterparts to provide feedback on the legislation to policymakers and to attempt to explicitly include language to address 'commercial' coverage in order to protect the commercial real estate marketplace.

Commercial properties, like homes, are essential elements of local communities. From grocery stores, dry cleaners, convenience stores and pharmacies to shopping malls and manufacturing plants, local communities rely on the services of local businesses. In this regard, available and affordable 'commercial' coverage is crucial to a strong local economy that provides jobs and income. Without jobs, there will be nothing to attract – and retain – residents to the areas that the underlying legislation attempts to help. Put simply, rebuilding a home is obviously an essential need, but so is restoring the ability to work and provide for one's family.

A recent RAND study highlights the issues in the commercial market and the importance of providing this coverage. In fact, the report found that the 'commercial' property insurance market has experienced significant disruption in the last several years, which has had significant, negative affects on business, the economy and taxpayers. The RAND study also details the significant increases in the price of 'commercial' coverage, accompanied by decreases in availability for such coverage. These findings provide strong evidence that businesses should be eligible for the same coverage as homes.

The importance of 'commercial' coverage to our national economy cannot be overstated. In fact, similar to residential coverage, property insurance for commercial entities – from the largest manufacturing plant to the corner mom-and-pop markets – is not a luxury; it is a lender requirement for insurance to be in place for the duration of the mortgage in order to protect the asset. Failure to maintain property insurance can lead to mortgage defaults and property foreclosures that would have a significant on the CMBS market and investors. This situation could be very disruption to our financial markets and our overall economy, potentially at a time when communities are trying to recover from devastating disasters.

To date, there have been several bills introduced in Congress that focus on 'homeowners' insurance, and CMSA has been very involved in the legislative process to address the availability and affordability of 'commercial' insurance. Specifically, CMSA is working to extend 'commercial' insurance coverage in several vehicles, including H.R. 3355, the "Homeowners Defense Act of 2007," introduced by Reps. Ron Klein (D-FL) and Tim Mahoney (D-FL). H.R. 3355 aims to address the availability and affordability of homeowners insurance by creating a federal/state "Consortium" that would provide a voluntary backstop for state and regional catastrophe programs, securitize and sell catastrophe bonds, and collect and store catastrophe risk and coverage information. The bill also authorizes the Secretary of the Treasury to make liquidity loans and catastrophic loans to state and regional reinsurance programs to ensure the solvency of such programs.

H.R. 3355 passed the U.S. House of Representatives by a vote of 258 to 155, but not before policymakers agreed to consider natural disaster legislation that would better protect local businesses and address availability and affordability issues in the 'commercial' insurance market. The agreement came during consideration of a CMSA supported amendment offered by Rep. John Campbell that would extend the provisions of the legislation to 'commercial' insurance coverage. In a significant victory for CMSA and the commercial real estate sector, the amendment was offered and withdrawn after the bill sponsors and House Financial Services Committee Chairman Barney Frank (D-MA) agreed to consider the inclusion of 'commercial' coverage in H.R. 3355 or as a separate bill that would address 'commercial' coverage in the upcoming months.

CMSA Position: CMSA supports efforts to address the need for catastrophe insurance, specifically urging the development of legislative solutions to ensure the availability of adequate and affordable catastrophe insurance in all regions of the United States. CMSA believes that any solution should address 'commercial' insurance coverage for natural disasters in order to protect the local economy and businesses that provide jobs and serve the community.

Status: In the U.S. House of Representatives, CMSA will continue to work with Rep. John Campbell (R-CA) on legislation aimed at addressing the commercial insurance coverage for natural disasters. In the upcoming months, we anticipate one hearing on commercial insurance coverage in the House Financial Services Committee, in addition to the introduction and potential consideration of legislation.

In the U.S. Senate, it is unclear whether the Senate Banking Committee will consider H.R. 3355, or companion legislation (S. 2310) introduced by Sens. Hilary Clinton (D-NY) and Ben Nelson (FL). Earlier this year, Senate Banking Committee Chairman Christopher Dodd (D-CT) introduced and passed out of committee S. 2286, the "Commission on Natural Catastrophe Risk Management and Insurance Act of 2007," which establishes a nonpartisan commission to examine these issues and report to Congress. Consideration of this legislation is uncertain at this time.

Further, Congress has begun consideration of legislation to extend the National Flood Insurance Program (NFIP), which does include some very limited coverage for commercial entities. The House-passed version of the legislation also includes a controversial proposal to include limited "wind coverage" for both homeowners and commercial entities as part of the program. The timeline for Senate consideration is uncertain at this time program, but the program expires in September of 2008.