June 21, 2010

The Honorable Barney Frank
Chairman, Committee on Financial Services
2129 Rayburn House Office Building
Washington, D.C. 20515

The Honorable Spencer Bachus
Ranking Member, Committee on Financial Services
2129 Rayburn House Office Building
Washington, D.C. 20515

The Honorable Christopher Dodd
Chairman, Committee on Banking,
Housing, and Urban Development
534 Dirksen Senate Office Building
Washington, D.C. 20510

The Honorable Richard Shelby
Ranking Member, Committee on Banking,
Housing, and Urban Development
534 Senate Office Building
Washington, D.C. 20510

Dear Chairmen, Ranking Members and Members of the Conference Committee,

As representatives of the commercial and multifamily real estate industry, an economic sector that was and continues to be heavily impacted by the market downturn starting in 2008, the undersigned organizations appreciate your work to promote transparency and stability in the financial markets through comprehensive financial regulatory reform. However, we have concerns about the potential impact on owners, operators and developers of commercial and multifamily real estate that utilize derivatives to manage risk.

As you may know, many commercial and multifamily real estate companies rely on interest rate and currency derivatives to manage financial risks associated with their building, development and operations activities. These activities include interest rate swaps and hedging for variable-rate private-activity bonds used to finance mixed-income and affordable workforce housing developments. Without access to the low-rate variable-rate bonds, many affordable multifamily housing projects are not feasible. While real estate companies are often able to access these derivatives on an unsecured basis, they are generally able to post their physical assets as collateral when necessary. These transactions allow commercial and multifamily real estate companies to better match their financial obligations to their cash flows and are often a central component of a comprehensive risk management strategy.

Throughout the debate on financial regulatory reform, we have supported efforts to provide transparency for 100% of derivative transactions and to require clearing and margin requirements for all trades that occur between dealers and other systemically significant institutions. However, additional certainty is needed to ensure that commercial and multifamily real estate companies are appropriately treated as derivatives end users and are protected from costly cash margin requirements that would further constrain liquidity and credit in our industry and hamper efforts to de-leverage, re-equitize, and otherwise create jobs in, and bring stability to, real estate markets.

Our organizations prefer the House-passed approach to derivatives reform, which would create transparency for all derivative transactions and focus clearing and margin requirements on those entities whose derivatives transactions could pose risk to the broader financial system. At the same time, the House-passed bill would protect non-systemic end users that rely on derivatives to hedge risk – including balance sheet risk, such as debt – regardless of their primary business activity.

On the other hand, the derivatives proposals in the Senate amendments and in the Conference Base Text raise a number of issues for our organizations and our members. First, by defining the beneficiaries of a "commercial end user" exemption by a list of approved primary business activities, the Base Text could be interpreted to exclude by omission owners, operators and developers of physical assets, such as real estate. Second, the Base Text's specific denial of end user protections to all "financial entities" and to "certain affiliates" may be interpreted to deny protections commercial and multifamily real estate entities that own property through partnerships, or based on their ownership. Third, the Base Text does not make clear allowances for the hedging of balance sheet risk, such as debt, when determining which entities are Major Swap Participants.

In the attached pages, we propose possible legislative remedies to address the issues identified above and to ensure that the industry sector that many view as "the next shoe to drop" is not subjected to requirements that would further constrain liquidity and credit at a time when both are needed more than ever.

Finally, we must underscore the importance of maintaining legal certainty for current contracts. The House bill would provide legal certainty for existing derivatives contracts that they will not be retroactively subjected to new requirements – including clearing or margin requirements. The Base Text does not specifically proscribe against retroactive enforcement. We strongly encourage you to adopt the House approach to make clear that current contracts will not be re-opened or subjected to new legal requirements that did not exist at the time they were originally negotiated, and which would fundamentally change the economics of the transaction.

Thank you for this opportunity to provide comments on this important component of financial regulatory reform. Please do not hesitate to contact us if you need additional information.

Sincerely,

American Resort Development Association
American Seniors Housing Association
Building Owners and Managers Association International
International Council of Shopping Centers
NAIOP, Commercial Real Estate Development Association
National Apartment Association
National Association of Real Estate Investment Managers
National Association of Real Estate Investment Trusts
National Multi Housing Council
The Real Estate Roundtable

CC: Members of the Conference Committee on H.R. 4173

Attachment - Legislative Certainty for Commercial Real Estate End Users

As representatives of the commercial real estate industry, we propose the following modifications to the Conference Base Text of H.R. 4173. These changes would provide greater certainty that owners, operators and developers of commercial real estate engaged in derivatives transactions for the purpose of managing risk will appropriately be treated as end users.

On page 676, we propose the end user clearing exemption be amended as follows:

(10) END USER CLEARING EXEMPTION.—

(A) DEFINITION OF COMMERCIAL END USER.—

(i) IN GENERAL.—In this paragraph, the term 'commercial end user' means any person other than a financial entity described in clause (ii) who, as its primary business activity, owns, operates, uses, produces, processes, manufactures, develops, distributes, merchandises, or markets goods, services, physical assets (which shall include but not be limited to commercial real estate), or commodities (which shall include but not be limited to coal, natural gas, electricity, ethanol, crude oil, gasoline, propane, distillates, and other hydrocarbons) either individually or in a fiduciary capacity.

(ii) FINANCIAL ENTITY.—The term 'financial entity' means—

(I) a swap dealer, major swap participant, security-based swap dealer, or major security-based swap participant;

(II) a person predominantly engaged in activities that are in the business of banking or financial in nature, as defined in Section 4(k) of the Bank Holding Company Act of 1956, that is not primarily invested in physical assets (which shall include but not be limited to commercial real estate), directly or through interests in its affiliates that own such physical assets;

(III) a person predominantly engaged in activities that are financial in nature that is not primarily invested in physical assets (which shall include but not be limited to commercial real estate), directly or through interests in its affiliates that own such physical assets;

(IV) a commodity pool or a private fund as defined in section 202(a) of the Investment Advisers Act of 1940 (15 U.S.C. 80b–2(a)) that is not primarily invested in physical assets (which shall include but not be limited to commercial real estate), directly or through interests in its affiliates that own such physical assets; or

(V) a person that is registered or required to be registered with the Commission.

On page 678 we propose similar changes to clarify the prohibitions relating to certain affiliates. The proposed changes would provide greater certainty for commercial real estate entities that invest in physical assets through partnerships, or which are part of a larger corporate entity:

> (ii) PROHIBITION RELATING TO CERTAIN AFFILIATES.-An affiliate of a commercial end user shall not use the exemption under subparagraph (B) if the affiliate is-
>
> > (I) a swap dealer;
> >
> > (II) a security-based swap dealer;
> >
> > (III) a major swap participant;
> >
> > (IV) a major security-based swap participant;
> >
> > (V) an issuer that would be an investment company, as defined in section 3 of the Investment Company Act of 1940 (15 U.S.C. 80a-3), but for paragraph (1) or (7) of subsection (c) of that Act (15 U.S.C. 80a-3(c)), <u>that is not primarily invested in physical assets (which shall include but not be limited to commercial real estate), directly or through interests in its affiliates that own such physical assets</u>;
> >
> > (VI) a commodity pool;
> >
> > (VII) a bank holding company with over $50,000,000,000 in consolidated assets; or
> >
> > (VIII) an affiliate of any entity described in subclauses (I) through (VII) <u>unless such affiliate is the corporate parent or holding company of such commercial end user</u>.

On page 636, we encourage you to specifically include “balance sheet risk” as a form of "commercial risk" when designating which entities are major swap participants. Given that variable rate debt risk is carried on the balance sheet, this additional clarity is critically important for commercial real estate owners, operators and developers.

(33) MAJOR SWAP PARTICIPANT.—

> (A) IN GENERAL.—The term ‘major swap participant’ means any person who is not a swap dealer, and
>
> > (i) maintains a substantial position in swaps for any of the major swap categories as determined by the Commission, excluding—
> >
> > > (I) positions held for hedging or mitigating commercial risk, <u>including operating and balance sheet risk</u>; and…