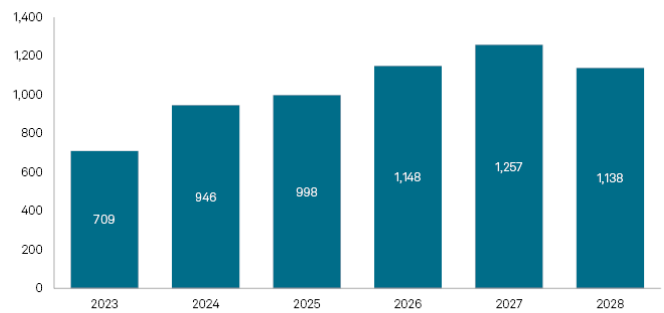
Addressing the Wave of Maturing CRE Debt and Pro-cyclical Regulatory Policy

Issue

Roughly $950B of US commercial real estate mortgages are estimated to mature in 2024 ($B)



Data compiled Aug. 19, 2024.

Data represents the aggregation of 3.6 million commercial real estate property mortgages, sourced from various tax filings from approximately 75% of US counties. While roughly 60% of the loans were originally missing a maturity date, analysis uses a random forest model to impute the missing values. Since the random forest model varies each time it is run, the values shown represent averages across five runs.

The raw data does not include roughly 25% of counties, so we created another model using gross county product and the number of properties in the county to estimate the total mortgage amounts in the missing counties. Ultimately, these were relatively minimal amounts compared to the overall market.

To help rebalance the wave of maturing loans, it is important to advance measures that will encourage additional capital formation and loan restructuring and avoid pro-cyclical regulatory actions such as the *Basel III Endgame*.

As urged by RER, a policy statement—*Policy Statement on Prudent Commercial Real Estate Loan Accommodations and Workouts*—issued by regulatory agencies encouraging financial institutions to work constructively with creditworthy borrowers on CRE loan workouts is helping to see loans through the current environment.

Many of these loans require additional equity, and borrowers still need time to restructure this debt. Capital formation is vital to help restructure maturing debt and fill the equity gap.

It is also important to bring more foreign capital into U.S. real estate by lifting legal barriers to investment, as well as repealing or reforming the archaic Foreign Investment in Real Property Tax Act (FIRPTA).

The original *Basel III Endgame* proposal would have increased capital requirements for the largest banks by as much as 20 percent. Based on the resounding opposition to the proposal from the industry participants, a revised proposal was announced in September by Michael Barr, the outgoing Fed Vice Chair for Supervision, that would increase Tier 1 capital requirements for global systemically important banks by roughly 9 percent—less than half of what would have been required in the original proposal. Nonetheless, concerns remain that any increase in capital requirements will have a pro-cyclical impact on credit capacity and carry a cost to commercial real estate and the overall economy, increasing the cost of credit and constraining capacity. Former Fed Vice Chair Randy Quarles warned it is a "mistake," saying, "It will restrict the ability of the financial system to provide support for the real economy."

Capital and Credit

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The proposed regulations come at a significant economic cost without clear benefits to economy.

In a January 12 letter, RER raised industry concerns about the negative impact of the *Basel III Endgame* proposal, including the increased cost of credit and diminished lending capacity, and requested that the proposal be withdrawn.

The revised proposal reduces risk weights for certain residential mortgages and retail exposures, extending this reduction to low-risk corporate debt. However, commercial real estate risk weights remain unclear. Yet, the Fed and other regulators remain deadlocked on advancing the revised proposal. With the appointment of Michelle Bowman to the post of Vice Chair for Supervision, there is speculation that the proposal could ultimately be withdrawn or end up being capital neutral.

The Roundtable's Position

- Providing banks with the flexibility to work constructively with their borrowers during times of economic stress has led to billions of dollars of loan restructurings and reduced undue stress in bank loan portfolios.
- While this policy statement is helpful, additional steps are called for to help restructure and transition the ownership and financing of commercial real estate from a period of low rates and robust markets to a time of higher rates. Additional capital is an essential element to this restructuring, and enacting policies that will encourage robust capital formation is imperative.
- In a January 12 comment letter, RER raised concerns about the proposed *Basel III Endgame* measure. The potential significant increase in capital requirements for large banks' capital market activities due to the proposal could materially reduce the depth of banks' products and services offerings to the real estate sector, which will in turn lead to an increase in hedging risk and the cost of raising capital in the industry.
- The largest U.S. banks' capital and liquidity levels have grown dramatically since the original *Basel III* standards were implemented in 2013 in response to the 2008 Global Financial Crisis. Since 2009, Tier 1 capital has increased by 56 percent and Common Equity Tier 1 capital has tripled. Today, as the Federal Reserve recently observed, the U.S. "banking system is sound and resilient, with strong capital and liquidity."[1]
- While well-intentioned, we are concerned that the proposals could increase the cost of credit, diminish lending capacity, and undermine the essential role banks play in lending and financial intermediation for real estate. With new supervisory leadership at the Fed, the *Endgame* proposal could be scrapped.
- Policymakers should consider additional measures to encourage constructive restructuring and new lending on solidly underwritten assets.

[1] https://www.federalreserve.gov/publications/files/svb-review-20230428.pdf

Commercial Insurance Coverage in an Evolving Threat Environment

Issue

The proliferation of natural catastrophe threats has raised concerns about commercial insurance coverage for real estate. As economic losses caused by disasters increase, changing exposures around the world must be addressed in order to effectively manage natural catastrophe risk. These concerns have highlighted the lack of—and need for—insurance capacity and various lines of commercial insurance. Expanding coverage gaps and increased costs present challenges for businesses across many industries, including real estate. A lack of adequate coverage will lead to economic uncertainty, harm stakeholders and undermine the growth of communities.

- Real estate insurance rates have spiked, with consecutive quarterly increases in overall premiums.
- The nation has seen years of atypical weather patterns and historic losses from natural catastrophes attributed to climate change—economic damages have tripled in cost from just 10 years ago.
- High reinsurance costs and a lack of reinsurance capacity also contribute to higher premiums.
- The U.S. insurance industry is regulated at state-level, with no central federal regulation.

Risks from natural disasters like floods, hurricanes, wildfires, hail, tornadoes and drought cost the U.S. billions of dollars each year. Even if policyholders are able to find coverage for these various lines, prices are increasing dramatically, raising economic concerns.

Without adequate coverage, the vast majority of these natural catastrophe losses are likely to be absorbed by policyholders. These widening coverage gaps and price hikes raise serious economic concerns about protection gaps, coverage capacity and increased costs from natural catastrophes and business interruption losses.

The budget debate in Congress has raised concerns about the future of the National Flood Insurance Program (NFIP), which is subject to temporary funding extensions and now must be reauthorized by September 30, 2025.

It is important to find solutions—either market-based or with the partnership of the federal government—to fill these commercial insurance gaps across changing threat patterns, and provide the economy with the coverage it needs to address catastrophic events.

RER, along with its industry partners, continues to work constructively with policymakers and stakeholders to address this market failure and enact a long-term reauthorization of an **improved National Flood Insurance Program (NFIP)**.

A long-term reauthorization of the **National Flood Insurance Program (NFIP)** is essential for residential markets, overall natural catastrophe insurance market capacity and the broader economy. The NFIP's commercial property flood insurance limits are low—$500,000 per building and $500,000 for its contents—so it is important to exempt larger commercial loans from the mandatory NFIP purchase requirements.

Commercial Insurance Coverage in an Evolving Threat Environment

The **NFIP** is currently operating under a continuing resolution. Since 2017, Congress has extended the NFIP's authorization 33 times, though the program has lapsed briefly three times.

As policymakers continue to debate potential changes and improvements to the program, their challenge is to find a balance between improving the financial solvency of the program, reducing taxpayer exposure and addressing affordability concerns.

The Roundtable's Position

- Floods are the most common, costliest natural peril in the U.S. The NFIP was enacted in 1968 due to a lack of private insurance and increases in federal disaster aid.
- The Program is administered by the Federal Emergency Management Agency (FEMA) and is essential for homeowners, renters and small businesses in affected areas.
- The level of flood damage from recent storms makes it clear that FEMA needs a holistic plan to prepare the nation for managing the cost of catastrophic flooding under the NFIP.
- The NFIP is important for residential markets, overall natural catastrophe insurance market capacity and the broader economy. However, under the NFIP, commercial property flood insurance limits are low—$500,000 per building and $500,000 for its contents. NFIP has approximately 5 million total properties, only 6.7 percent are commercial. Nearly 70 percent of NFIP is devoted to single-family homes and 20 percent to condominiums. In the total program, 80 percent pay actuarial sound rates; however, in the commercial space, only 60 percent pay actuarial sound rates.
- Congressional hearings have illuminated numerous acute problems surrounding the NFIP, such as insolvency, increased risk of flooding across the country and insufficient and inaccurate flood mapping. The unintended negative outcomes generated by the NFIP continue to grow and are now spreading to GSEs (government-sponsored enterprises) Fannie Mae and Freddie Mac.
- Lenders typically require base NFIP coverage, and commercial owners must purchase Supplemental Excess Flood Insurance for coverage above the NFIP limits. The NFIP's low commercial limits make it problematic for most commercial owners. As a result, RER has been seeking a voluntary exemption for mandatory NFIP coverage if property owners have flood coverage from commercial insurers.
- RER supports increased private market participation. By permitting certain private issue insurance policies to satisfy the NFIP's "mandatory purchase requirement" for properties in flood plains financed by loans from federally guaranteed institutions, commercial property owners would have the ability to "opt out" of mandatory NFIP commercial coverage if they have adequate private coverage outside the NFIP to cover financed assets.
- RER and its partner associations support a long-term reauthorization of an improved NFIP that helps property owners and renters prepare for and recover from future flood losses. Given the low coverage amounts provided to commercial properties, it is important to permit larger commercial loans to be exempt from the mandatory NFIP purchase requirements.
- Going forward, it is important to protect American jobs and to ensure a sustainable and speedy economic recovery from future natural catastrophe events. If not remedied, these insurance gaps could hinder economic growth.

Beneficial Ownership & Corporate Transparency Act

Issue

Under the Corporate Transparency Act (CTA), many U.S. businesses are required to disclose information on their "beneficial owners" under regulations issued (and to be issued) by the Treasury Department's Financial Crimes Enforcement Network (FinCEN).

The stated goal of the CTA is to prevent and combat money laundering, terrorist financing, corruption, tax fraud and other illicit activity by requiring companies to disclose beneficial ownership information, or BOI, to FinCEN, a bureau of the U.S. Department of the Treasury.

The Rule imposes heavier compliance burdens on real estate businesses with numerous legal entities that own and operate real property across all asset classes. While the CTA and its implementing regulations are not specifically targeted to real estate businesses, it will have a direct impact on the industry. As discussed below, certain types of entities will be exempt from the reporting requirements; however, these exemptions will not apply to many typical real estate limited liability companies and partnerships formed to own and operate commercial properties.

The CTA requires reporting companies to supply three categories of information: information about the entity, BOI and information about the company applicant. Each reporting company will have to provide information on its "beneficial owners" as well as the "company applicants" involved in forming the entity. A beneficial owner refers to an individual who owns at least 25 percent of an entity or indirectly exercises "substantial control" over it.

While this disclosure obligation began on January 1, 2024, the U.S. Court of Appeals for the Fifth Circuit on December 26, 2024, vacated the stay and reinstated the nationwide preliminary injunction enjoining enforcement of the Corporate Transparency Act (CTA) and the Reporting Rule, including the impending reporting deadlines. The appellate court said it was taking such action in order to preserve the constitutional status quo while that court considers the parties' weighty substantive arguments in an expedited appeal.

On March 2, 2025, the Treasury Department announced it would suspend enforcement of the Corporate Transparency Act (CTA) against U.S. citizens and domestic reporting companies, including beneficial ownership information reporting requirements, citing a move to reduce regulatory burden and focus on foreign entities. The Treasury Department will further be issuing a proposed rulemaking that will narrow the scope of the rule to foreign reporting companies only.

RER continues to track this important issue and plans to comment on the proposed rulemaking after it is released.

The Roundtable's Position

- RER has repeatedly raised concerns, along with its coalition partners, about the regulatory burden posed by the CTA and has supported the court challenges to the law.
- There is significant concern about the CTA's far-reaching scope and its impact on many commercial and residential real estate businesses that use the LLC structure for conducting business.

Beneficial Ownership & Corporate Transparency Act

- The CTA amended the Bank Secrecy Act to require corporations, limited liability companies and similar entities to report certain information about "beneficial owners" who own at least 25 percent of an entity or indirectly exercise "substantial control" over it. The CTA authorizes FinCEN to collect and disclose beneficial ownership information to authorized government authorities and financial institutions, subject to effective safeguards and controls. The statute requires the submission of regular reports to the federal government that include a litany of sensitive personal identifiers of the owners, senior employees and/or advisors of covered entities.
- Although the measure is intended to provide support for law enforcement investigations into shell companies engaged in money laundering, tax evasion and terrorism financing, it places many costs and legal burdens on small businesses, especially those in the real estate industry. In 2021, RER and its coalition partners submitted detailed comments to FinCEN regarding the development, disclosure and maintenance of a new federal registry that will contain beneficial ownership information.
- The real estate coalition's extensive comments emphasize the "scope of the CTA is far-reaching and will impact many commercial residential real estate businesses who are frequent users of the LLC structure for conducting business. If not implemented with a clear set of rules and regulations, the CTA could result in an outcome of confusion, missteps and ultimately fines on law-abiding businesses."
- In 2022, RER and its coalition partners submitted comments to the U.S. Department of the Treasury (DOT) and FinCEN that support efforts to thwart illegal money laundering in real estate, while encouraging policymakers to find a balanced approach that does not unfairly burden law-abiding businesses.
- RER continues to work with industry partners to address the implications of FinCEN's proposed rules and the impact they could have on capital formation and the commercial real estate industry.

Real Estate Capital Formation

Issue

On February 15, 2023, the Securities and Exchange Commission (SEC) proposed changes to require SEC-registered investment advisers to put all their clients' assets, including all digital assets like Bitcoin, with "qualified custodians".

- *Safeguarding Advisory Client Assets*—would significantly expand requirements of Custody Rule to maintain client assets with a qualified custodian for certain physical assets such as real estate.

The proposal would also require a written agreement between custodians and advisers, expand the "surprise examination" requirements, and enhance recordkeeping rules. These rules were originally designed for digital assets. "Reasonable" safeguarding requirements is ambiguous as applied to real estate. The SEC's release indicates that deeds evidencing ownership of real estate can be held at a qualified custodian—this is not accurate. Deeds are recorded with a government authority. Land and buildings cannot be physically absconded. Lenders and other interested parties have an interest in ensuring no misappropriation of real estate.

The Roundtable's Position

- RER sees no policy reason to impose the proposed rule on real estate—real estate cannot readily be stolen. Lenders and others have an interest in ensuring no misappropriation of real estate. Title insurance protects real estate investors against covered title defects, such as a previous owner's debt, liens and other claims of ownership. It's an insurance policy that protects against past problems, whereas other insurances usually deal with future risks. Titles are recorded in the name of the acquiring entity by a government entity.
- Different jurisdictions present even more challenges. Different laws for titles exist between not only states but also countries. The rule applies to registered investment advisors regardless of where the asset is located.
- For these reasons, we believe that the SEC's policy reasons for imposing the rule on real estate seem irrelevant. RER has submitted a comment letter to SEC and met with senior staff from the investment management division, requesting an exception for real estate.
- In addition to the proposed Custody Rule, the SEC has a number of proposed rulemaking measures that could have a chilling effect on real estate capital markets, further impair liquidity and be a "death by a thousand cuts" for commercial real estate. Capital formation is vital when credit markets tighten to restructure maturing debt.
- Fortunately, on June 5, 2024, the U.S. Fifth Circuit Court of Appeals issued an opinion that vacated the SEC Private Fund Adviser Rules, holding that the SEC exceeded its statutory authority in adopting the Rule. Specifically, the court held that the "promulgation of the [Rule] was unauthorized … no part of it can stand."
- With the change of administrations, SEC Chair Gary Gensler will be replaced by SEC veteran Paul Atkins, subject to Senate confirmation. Under Atkin's leadership, it is likely that the Commission may either withdraw the proposed rule altogether or grant an exception for real estate.

Expanding on the EB-5 Visa with the "Gold Card" Concept

Issue

The U.S. faces a strategic imperative to modernize its immigration system in a way that strengthens the domestic labor force and unleashes private capital for economic growth. The push for immigration reforms has prompted renewed interest in investor programs like the EB-5 Visa and the proposed "Gold Card" concept. Both programs can attract high net-worth individuals who can contribute to America's economy.

- The Gold Card ideas sketched by the Trump administration would help reduce the national deficit. Individuals would pay $5 million to receive legal residency status with a path to citizenship.
- The EB-5 Visa is a job creation program that has existed for decades. It attracts overseas investors to provide capital for economic development projects in the U.S.
- The EB-5 program has delivered $350 billion in economic impact and created over 1.5 million American jobs—at no cost to taxpayers.
- EB-5 investment can help finance housing, grid modernization and manufacturing plants to further recent executive orders and national priorities.
- Combined, both EB-5 and the Gold Card offer mechanisms to attract global capital and top-tier talent.

In 2022, Congress modernized the investor visa through the EB-5 Reform and Integrity Act. These reforms have helped improve the program's transparency and accountability and spur investments particulalrly in infrastructure, rural areas and high unemployment census tracts.

The Roundtable's Position

- The Gold Card program, along with an improved EB-5 visa program, can leverage private investment to stimulate job creation, reduce the national deficit, finance infrastructure, increase housing supplies and support energy grid expansion—at no cost to U.S. taxpayers.
- Reforms enacted in 2022 to the EB-5 Visa introduced new integrity measures and expanded rural access, making the program more transparent, secure and effective.
- Further agency guidance should clarify that EB-5 investments should be "sustained" as tied to a visa applicant's period of conditional residency, so capital is at work in the marketplace for a sufficient period to finance larger, complex projects that create the most jobs.

Additional Resources

- RER letter to Commerce Secretary Lutnick, regarding dual EB-5/Gold Card regime (March 11, 2025)

Expanding on the EB-5 Visa with the "Gold Card" Concept

- Roundtable Weekly, "Lawmakers Navigate Action-Packed Week on Capitol Hill" (March 17, 2025)
- RER letter to Congress, regarding EB-5 "sustainment" period (February 28, 2024)
- RER fact sheet, "EB-5 Reform and Integrity Act of 2022" (April 11, 2022)