

Because of Dodd-Frank, a variety of regulatory standards must be met before a bank can sell a cap to a borrower. This has lengthened the typical closing process from just a few hours to more typically several days.

Much of this will be dependent upon the responsiveness of the borrower and lender.

Here is a quick overview of the cap process. The cap arranger helps quarterback this entire process as part of their services. As you'll see, the first three steps are generally done simultaneously.

Step 1 – Obtain a Legal Entity Identifier (LEI)

Lead time - preferably at least four days before closing

Borrower responsibilities - minimal

This is time sensitive because much of it is dependent upon the GMEI website.

- Cap arranger will register the entity with the CFTC; however, borrower needs to provide basic entity information such as legal name, tax ID, address, contact person, etc.
- Registration costs \$120 per entity.
- Once filed, the CFTC typically creates an LEI by the next business day.

Step 2 – Know Your Customer (KYC)

Lead Time - preferably at least four days before closing

Borrower responsibilities - moderate, may need to provide a variety of information

- Each potential bidding bank has a different set of KYC requirements; however, each bank usually requires a tax ID, formation documents, organization structure, and general financial information.
- Depending on structure and cost, the borrower may exclude some banks based on their intensive pre-trade documentation requirements.
- Some banks will circulate pre-trade emails with mandatory disclosures.

Step 3 – Create bid package and coordinate approval with lender’s counsel

Lead time - no minimum amount of time needed, but try to allow for at least four business days.

- this step usually begins simultaneously with Step 1.
- this step usually takes the longest because lenders are frequently juggling multiple closings

Borrower responsibilities - minimal

- Each transaction is unique and will require coordination with lender’s counsel to ensure terms are met and the loan can close smoothly.
 - These frequently include rating requirements, downgrade triggers, critical terms, etc.
- This process usually takes several days as terms change, certain language is modified, bidding cap providers make comments, etc.
- Additional documentation will be required by the lender, such as a Collateral Assignment and Opinion. These will be circulated, negotiated, and approved by lender’s counsel and each bank that wants to bid on the cap.

Step 4 – Register through Markit.com or complete Bilateral Agreements with each bank

Lead time - at least two days prior to closing

Borrower responsibilities - Borrower *is required* to be the one to complete this documentation

- Must have the LEI from Step 1 to complete this step.
- Once this step is complete, it can take up to 24 hours for the CFTC website to list the entity as DF compliant.
- Bidding banks will need to confirm this compliance before trading.
- Cap arranger will help the borrower decide if they should use Markit or by executing bilateral agreements.

Step 5 – Cap Auction

Lead time - day of closing or day before closing at borrower’s discretion

Borrower responsibilities - must be available by phone to execute with winning bank

- Because all documentation has been approved at this point, the auction is usually a smooth process.
- Borrower executes with winning bank or with preferred bank.
 - Some clients give lender right to match the lowest quote in order to reward the relationship.
 - Some clients even elect to allow their lender to win the auction as long as the lender is within a certain range of the lowest quote.

Step 6 – Documentation required for closing

- Lender's counsel will require a Cap Confirmation; however, this can take the winning bank more than a few hours to generate.
 - o In lieu of a formal Confirmation, lenders will allow for an email from the winning cap provider stating the cap has been purchased along with the critical terms.
- Within 24 hours of closing, the Confirmation and Collateral Assignment will need to be signed by the borrower and cap provider. The cap arranger coordinates this process.
- An Opinion from the cap provider usually takes 5 - 10 business days to generate after the Confirmation is signed by the borrower.

Step 7 – Paying for the Cap

- Borrower has two business days to pay for the cap, which is why some borrowers buy the cap ahead of closing. This allows extra time to circulate the documentation before the loan closes.
- Most borrowers elect to pay for the cap out of closing, so wiring instructions for the cap provider will be provided to escrow agent.

The cap process is relatively straightforward as long as you understand the timeline and requirements.

While caps are an integral part of many real estate transactions, they are one of the easiest aspects of the closing.

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