COMMERCIAL MORTGAGE
SECURITIES ASSOCIATION

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April 10, 2009

Mr. Robert E. Feldman
Executive Secretary
Attn: Comments
Federal Deposit Insurance Corporation
550 17th Street, NW,
Washington DC 20429

LLP Comments@FDIC.gov

Re: Legacy Loans Program: Response to Request for Comment

Dear Mr. Feldman:

The Commercial Mortgage Securities Association (the "CMSA") submits this letter in response to the Federal Deposit Insurance Corporation ("FDIC") request for comment on the Legacy Loans Program (the "Program") published on the FDIC's website.

The CMSA is a global trade organization with its primary mission being to promote the ongoing strength, liquidity and viability of commercial real estate capital markets finance in the United States as well as worldwide. Based in New York, with a government relations office in Washington, DC, the CMSA is the collective voice for the entire market, with a diverse global membership of over 400 member firms represented by more than 5,000 individuals who actively engage in commercial real estate capital market finance activities. These members embody the full spectrum of the commercial mortgage-backed securities ("CMBS") market, including senior executives at the largest banks and investment banks, insurance companies, rating agencies, investors such as money managers and specialty finance companies, servicers and other service providers to the industry. The CMSA and its members are the leaders in setting standards and maintaining a favorable investing environment for the more than $900 billion in outstanding CMBS issuance in the U.S., and we submit these comments in an effort to further advance these dual objectives.

The CMSA applauds the announcement of the Program and supports the efforts of the FDIC and the U.S. Department of Treasury ("Treasury") to facilitate the sale by insured U.S. banks or savings associations ("Eligible Banks") of legacy loans in order to promote a resumption by these institutions of new lending activity. While we believe that the concept of the Program is well conceived, the success of the Program will rely on the details of its implementation, many of which are the subject of the FDIC's request for comment. We are therefore grateful for this opportunity to share our views with you on the Program from the commercial real estate finance perspective.

In submitting these comments, we are guided by certain goals and priorities that we believe the FDIC and Treasury have for the Program, and with which we concur. Specifically, we believe these priorities should be:

- to encourage the greatest participation possible by Eligible Banks;
- to achieve fair and equitable pricing for the legacy loans being sold by such Eligible Banks;
- to shape every aspect of the Program in a manner most likely to encourage new lending by participating Eligible Banks;
- to encourage broad participation by equity investors from different sectors of the economy; and
- to ensure that taxpayers share equitably in investment returns achieved by investors in the Program.

Which asset categories should be eligible for sale through the LLP?

From the perspective of the commercial real estate finance market, in order for the Program to achieve its objectives, all forms of commercial real estate debt instruments must be eligible for sale through the Program.

Secured Commercial Real Estate Loans. Commercial real estate loans that finance specific commercial real estate assets are generally either directly secured by a mortgage on the related real estate, or are secured by a pledge of the direct or indirect equity in a company that owns the real estate (commonly known as "mezzanine debt"). Loans falling into both broad categories currently occupy the balance sheets of Eligible Banks. It is therefore critical that both categories of commercial real estate loans be eligible for inclusion in the Program. In addition, it is important that the Program include loans on all types of commercial real estate. While loans backed by office buildings, retail properties, multi-family residential properties, hospitality properties and industrial properties have been mainstays of the commercial real estate finance markets, it is also critical that the Program include loans on other property types such as construction loans and loans on land that is slated for development. Including commercial real estate loans of all varieties that will give the Program the deepest possible impact on the balance sheets of Eligible Banks.

Fractional Loan Interests. Commercial real estate loans are commonly divided into multiple interests or tranches and syndicated among multiple lenders, particularly in the case of larger financings. Participating interests of varying sizes and priorities are held by each lender. In some cases, the senior interest in a commercial real estate loan may have been sold by an originating Eligible Bank into a CMBS securitization, while the junior interest may have been retained by the Eligible Bank. It is very important to the success of the Program that these partial interests in commercial real estate loans be eligible for inclusion in the Program.

Unsecured Loans to Real Estate Companies. For the reasons discussed above and elsewhere in this letter, the CMSA believes that secured commercial real estate loans are good assets for inclusion in the first legacy loan pools. Since the published proposal for the Program indicates that the range of included legacy assets may be expanded over time, the CMSA suggests strong consideration of including unsecured loans from real estate companies, such as REITS or other real estate developers. Although unsecured corporate debt may be more difficult to value and diligence than debt secured by specific real estate assets, there would be a tremendous benefit in creating liquidity for such debt from the perspective of freeing up banks' balance sheets to encourage new lending activity.

The CMSA supports the intended engagement by the FDIC of expert contractors to help evaluate legacy loans, as we believe that engaging experts will give the FDIC the ability to target the full spectrum of legacy commercial real estate loans currently owned by Eligible Banks in a manner that does not subject the FDIC or Treasury to undue risk. The CMSA believes that including the broadest variety of real estate loans, as well as fractional interests in these loans, in the Program will promote the greatest participation by Eligible Banks having these assets on their balance sheets. This in turn will promote a speedier resumption of new lending activity, especially in the commercial real estate sector.

Should the initial investors be permitted to pledge, sell or transfer their interests in the PPIF? If so, how should the FDIC ensure that subsequent investors meet the program's criteria for investors?

The CMSA believes that liquidity of investment will be an important factor in attracting equity capital from the private sector into Public Private Investment Funds ("PPIFs"). Therefore, we believe that restrictions on transfers or pledges of interests in PPIFs should only be imposed to accomplish compelling objectives.

We believe there are two compelling objectives related to the types of parties that should be permitted to participate in PPIFs: (i) ensuring that parties investing in a PPIF have the requisite sophistication to understand the nature of the investment and the financial stability to bear the economic risk of the investment; and (ii) ensuring that parties having management responsibilities for a PPIF have the requisite experience and ability to manage the fund in the best interest of all the investors, including Treasury.

Concerns about the sophistication and financial stability of investors are not unique to PPIFs. Similar concerns have always existed for other types of securities and are at the heart of what the Securities and Exchange Commission regulates under the Federal securities laws. The

CMSA does not see the need, from this perspective, to regulate the types of investors that may participate in PPIFs beyond the regulation already provided by the securities laws.

With respect to concerns about the experience and ability of parties managing assets for PPIFs, the CMSA believes that minimum standards of experience, staffing and operational capacity should be established for qualification to manage assets for PPIFs. Specific suggestions regarding the nature of such qualifications are discussed later in this letter. The organizational documents of PPIFs should impose these minimum standards contractually. We note that there are many different structures that might be adopted by private sector investors forming PPIFs, and we believe that flexibility in structuring PPIFs will promote robust participation in bidding by investors from different segments of the economy. We further note that asset management for a PPIF will comprise two distinct functions: (i) investment management functions involving decisions related to the ownership or possible disposition of legacy loans by the PPIF; and (ii) loan servicing functions related to the ongoing servicing of legacy loans. In some cases, these two functions may be performed by a single party and in some cases we anticipate that these functions may be split. Furthermore, we anticipate that sometimes an investor may serve in one or both of the foregoing capacities, and other times such functions will be delegated by the PPIF to third-party service providers. In any case, the CMSA believes that the best way to address these concerns is to impose minimum standards on the party performing such functions, whether or not such party is an investor in the PPIF, rather than by imposing transfer restrictions on PPIF investments. Although we are recommending minimum contractual standards for fund managers and servicers, we note that there may be entities well qualified to perform those functions that do not, for one reason or another, meet the minimum contractual standards. In order to promote broad participation in the Program by fund managers and to promote liquidity in the PPIF equity positions, we recommend that there be a procedure whereby Treasury or the FDIC would consider entities not meeting the strict contractual standards for approval to serve in those capacities based on a more holistic review of the entity's qualifications.

The CMSA believes that minimizing restrictions on transfers of investments in PPIFs will promote the greatest possible liquidity for these investments, which will in turn encourage the broadest possible participation from investors from all sectors of the economy. This in turn will help accomplish the goal of fair and equitable pricing for legacy loans.

What is the appropriate percentage of government equity participation which will maximize returns for taxpayers while assuring integrity in the pricing by private investors? How would a higher investment percentage on the part of the government impact private investment in PPIFs?

The CMSA believes that the published proposal of up to 50% equity participation by Treasury appropriately balances the need for significant private sector participation in PPIFs to ensure meaningful price discovery on the one hand with the goal of ensuring that American taxpayers share in any investment returns realized from the Program on the other hand. Increasing the government's equity participation beyond 50% could have the effect of crowding out smaller private sector investors that may be interested in participating in PPIFs by eliminating the incentive for the larger and more active private sector investors to seek capital from smaller investors. The CMSA believes that Treasury should consider increasing its equity investment in PPIFs beyond 50% only in circumstances where available private sector equity capital is insufficient (which could happen in the early stages of the Program, before equity interests in PPIFs become well enough established to attract interest from smaller private sector investors).

In addition, we note that the use of government warrants in PPIF structures has the potential to chill private sector equity investment. If it is the view of Treasury and the FDIC that government warrants are required by the terms of the Emergency Economic Stabilization Act, then we urge that such warrants be structured in a way that does not suppress yields that may be obtained by private sector investors that dedicate capital to this important initiative. Artificially suppressing yields will undoubtedly hold down prices that potential investors may be willing to bid for interests in legacy loan PPIFs, which in turn may limit participation by Eligible Banks, both of which are inconsistent with the goals, and the ultimate success, of the Program. In any event, clarity as to the structure of government warrants to be included in the Program is a critical component of a successful launch. Gaining a full understanding of the impact of any included warrants at the earliest possible time will help facilitate the formation of capital for participation in bidding in the Program.

Is there any reason that investors' identities should not be made publicly available?

The principles of transparency that have been woven through the TARP and TALF programs are integral to earning public trust and confidence. Transparency promotes integrity and fair dealing. However, the CMSA also believes that there is merit in valuing the privacy of the investors that participate and profit from their investments in the Program. It would be self-defeating to promote transparency while at the same time chilling investor participation. In light of recent headlines relating to bonuses paid at financial institutions, disclosure of investor identities could cause investors to hesitate before participating in this Program. The CMSA supports the disclosure of the names of entities that win auctions to purchase legacy loan pools, along with the identities of fund managers or financial advisors that sponsor and manage such entities. However, we believe that disclosing the names of the passive investors in the entities that purchase legacy loan pools would discourage many investors from participating and would provide no significant public policy benefit.

How can the FDIC best encourage a broad and diverse range of investment participation? How can the FDIC best structure the valuation and bidding process to motivate sellers to bring assets to the PPIF?

The CMSA believes that the overall structure of the Program could provide a compelling incentive for liquidity to return to the market for legacy loans. While there are many details of the Program which are yet to be developed, we believe that there are several important issues related to the Program and to TARP generally which must be clarified before the process of formation of capital for investment in legacy loan pools can begin in earnest. The first of these is the nature of any increased government regulation of businesses participating in the Program, whether as investors, fund managers or selling banks. The second, which is the subject of a specific request for comment, is a detailed explanation of the terms of PPIF debt which the FDIC would be willing to guarantee, as such terms will have a direct impact on yields that can be expected to be achieved from investment in the Program. Lastly, the nature of any limitations on private sector returns, whether through the exercise of government held warrants or otherwise, must be fully understood before capital can be committed to the Program. Only when these features of the Program are understood, will a broad and diverse range of investors be in a position to fully evaluate their interest in investing in legacy loans. In addition, we have some specific thoughts concerning Program features that will attract investors and sellers to the Program.

In order to encourage broad investor participation, the valuation and due diligence process should be designed so that it will be cost-effective for investors to conduct diligence on multiple pools of legacy loans. The CMSA believes that giving investors an opportunity to conduct meaningful due diligence will result in achieving fair and equitable pricing for selling institutions. However, a burdensome and expensive diligence process may discourage bidding, especially by bidders that may not have been successful in prior auctions. Conversely, limiting the opportunity for due diligence will suppress the prices that investors are willing to bid on legacy loan pools. The following are suggestions for the Program that will help achieve an efficient and streamlined due diligence process:

(i) utilize the FDIC's advisors to work with Eligible Banks to assemble a comprehensive diligence package that is available for review by all prospective investors;

(ii) have the Eligible Bank provide representations and warranties (with exceptions noted as necessary) addressing certain legacy loan characteristics that may be difficult to assess through diligence, with a prescribed remedy (such as cure or repurchase) in case of a breach; and

(iii) construct some legacy asset pools with simpler, more homogenous pools of legacy loans where the amount of diligence will be manageable for smaller investors.

We support the Program's published proposal that selling Eligible Banks should have the right to reject bids that they feel do not correctly reflect the value of the offered loans. Although some have expressed concern that this will deter investors from participating in the auction process, we feel that the risk of an Eligible Bank rejecting a bid is no different than an investor being out-bid by another bidder. The first step in a successful launch of the Program will be to encourage participation by Eligible Banks. Requiring Eligible Banks to sell legacy loans at the auction price is likely to discourage participation by Eligible Banks. We recommend that the FDIC re-assess this issue after the first few legacy loan pool auctions. If it appears that the ability of selling Eligible Banks to decline to sell legacy loans at the auction price has discouraged robust participation by investors in auctions, we believe a logical adjustment to the Program would be for the FDIC to work with Eligible Banks to establish a reserve price for each legacy loan pool. This would have the dual benefit of giving Eligible Banks some assurance that legacy loans will not be sold for unacceptably low prices while assuring bidders that the auction will result in a sale if a bid is received at or above a price that the FDIC (with the advice of its valuation consultant) believes is reasonable.

Another important issue for Eligible Banks considering the sale of Legacy Loans is the effect auction pricing will have on the valuation of their assets for regulatory and financial accounting purposes. More Eligible Banks would be willing to participate in the Program if it was clarified by applicable regulators that prices determined in the auction process will not be determinative of book value of assets (whether for legacy loans that were the subject of failed auctions or for similar assets on the balance sheets of Eligible Banks that have not been offered for sale in the Program).

<u>What type of auction process facilitates the broadest investor participation? Should we require investors to bid on the entire equity stake of a PPIF, or should we allow investors to bid on partial stakes in a PPIF?</u>

In order to facilitate broad investor participation, the Program should be simple yet flexible. Investors should have the option to bid on whole pools as well as interests in pools. However, the direct sale of partial interests in pools through the FDIC auction process would add a significant level of complexity. The CMSA believes that broad investor participation will be more effectively achieved by encouraging private sector managers to structure investment vehicles that facilitate indirect investment in legacy loan pools by smaller investors. Allowing private sector fund managers to structure collective investment vehicles will harness the structural expertise, as well as the pricing expertise, of the private sector for the benefit of the Program. This, in turn, will allow the FDIC auction procedure to run more smoothly by identifying only a single winning private sector bid for each auction.

We note that, while smaller investors may participate in legacy loan PPIFs by co-investing with larger investors, it may be difficult for small investors to bid directly on large pools. Smaller investors may lack the financial resources to commit to purchase larger pools and lack the man power necessary to conduct due diligence on such pools. However, many smaller investors have the resources and sophistication to evaluate and bid on smaller pools comprised of legacy secured by familiar collateral categories. As such, in order to attract greater direct participation from smaller investors, the FDIC should ensure that a sufficient number of small, relatively homogeneous (by property type and geographic region) pools are included among the pools offered in the Program. In this regard, we note that the investor survey posted on the FDIC's website indicates ranges of representative pool sizes, starting with $1 billion, which the CMSA believes may be too large to allow direct bidding by small investors both because of capital limitations as well as limitations on small investors' ability to diligence large pools.

<u>What priorities (i.e., types of assets) should the FDIC consider in deciding which pools to set for the initial PPIF auctions?</u>

The initial auctions should include loans susceptible to straightforward evaluation, such as commercial mortgage loans. Since commercial mortgage loans are generally payable from cash flow generated by income-producing properties, and mortgage loan borrowers are required to provide periodic financial statements, prospective bidders can base their due diligence on finite, available data. In order to maximize the likelihood that the earlier auctions will be successful, the assets selected should be higher quality, lower leverage loans with good payment history. Pools with higher quality loans will require less intensive analysis and raise fewer due diligence concerns. For example, loans backed by properties with environmental issues, with declining income due to expiring leases, or requiring large infusions of capital, will need to be closely evaluated by prospective bidders so that the likelihood of defaults can be properly weighed and the value of the property can be assessed. This analysis could be expensive and time-consuming and may be better left to later auctions when the Program is better established.

<u>What are the optimal size and characteristics of a pool for a PPIF?</u>

We believe that there is no optimal pool. Rather, pools of varying size with varying characteristics will encourage greater participation by a broad range of investors. The greater the diversity of the types of pools made available, the greater the likelihood that particular potential investors will be able to find a pool suitable to meet their investment objectives. For example, investors with greater financial resources may want to own an entire pool rather than participate with other equity investors, resulting in the need for smaller sizes; others may be looking for a particular type of asset or property; some may be more interested in loans sold by a particular Eligible Bank; others may be more interested in a pool comprised of a lower number of loans with higher balances because of due diligence constraints; and still others may be more interested in a smaller, diverse group of loans. As discussed above, creating smaller more homogeneous pools may encourage greater participation from smaller investors. The advisors analyzing the individual loans for the FDIC can be helpful in creating pools that would appeal to a diverse group of investors ranging from smaller companies to large financial institutions.

<u>What parameters of the note and its rate structure would be essential for a potential private capital investor to know at the time of the equity auction to provide equity?</u>

In order for an investor to determine the value of an equity investment, it makes certain assumptions and analyzes the cash flow generated by the underlying assets, taking into account duration, timing and amount of the cash flow as well as loss estimates. One essential element for this analysis is the cost of financing the assets to be purchased. This cost will be measured not just by principal amount and interest rate of the debt, but also by term of the debt, principal repayment terms and availability of prepayment options. We understand that terms of the debt and the FDIC guarantee will be stipulated in the FDIC Guaranteed Secured Debt for PPIF Term Sheet, which has not yet been published. We hope the FDIC will provide an opportunity for comment on this important term sheet.

Clarity as to the economic terms of debt financing that the FDIC is willing to guarantee will be essential to allow fair and equitable pricing of legacy loans. As such, in addition to interest rate and principal amount of the debt, it will be important for an investor to know if the term of the debt will match the duration of the PPIF. Also, any other note term that could affect the timing or amount of the cash flow to the equity needs to be specified in advance. Specifically, investors will need to understand any Program requirements regarding how proceeds collected from the legacy loans included in a PPIF (including from disposition of such Loans) will be applied to repay the principal amount of the FDIC-guaranteed debt. To the extent available cash flow is directed in whole or in part to repay the note, the timing of such repayment will have a direct impact on the yield of the equity investor.

<u>Would it be preferable for the selling bank to take a note from the PPIF in exchange for the pool of loans and other assets that it sells? Alternatively, what would be the advantages and disadvantages of structuring the program so that the PPIF issues debt publicly in order to pay cash to the selling bank? Would a public issuance of debt by the PPIF limit its flexibility compared to the issuance of a note to a selling bank?</u>

The CMSA believes the Program should permit flexibility with respect to the structure of the FDIC guaranteed debt that may be issued by a PPIF. Providing flexibility with respect to the debt structure will enable the participants to utilize the least expensive means of financing. This will help the selling Eligible Banks to obtain the highest possible price for the assets being sold, the investors to achieve the highest possible yield on their investments and the FDIC to manage exposure under its guarantees of the debt.

Requiring the selling Eligible Bank to take back a note from the PPIF as partial compensation for a loan sale would have the advantage of simplicity and ease of execution of the transaction. However, the CMSA believes that these advantages are outweighed by certain disadvantages. A selling Eligible Bank that takes back a note from a PPIF does not receive cash directly from the sale of the legacy loans and may, therefore, be less likely to resume new lending activity. In addition, requiring PPIFs to issue guaranteed debt only to the selling Eligible Bank deprives the PPIF of the ability to market its debt to multiple lenders, which may result in a higher cost of financing, lower equity yields and therefore lower bids in the auction.

Allowing PPIFs to structure debt to be issued publicly will have the advantages of injecting cash into selling Eligible Banks as compensation for legacy loans, and allowing PPIFs to achieve more cost-effective financing through the issuance of more liquid debt instruments. In addition, public debt would provide for broader market participation in PPIFs through investments in PPIF debt. However, structuring debt to be issued publicly will add a layer complexity not applicable where the selling Eligible Bank takes back the note. Specifically, the debt will need to be structured and marketed, which may increase the amount of time necessary to complete the sale transaction or may necessitate interim financing pending public distribution of the notes.

<u>In return for its guarantee of the debt of the PPIF, the FDIC will be paid an annual fee based on the amount of debt outstanding. Should the guarantee fee be adjusted based on the risk characteristics of the underlying pool or other criteria?</u>

Based on the published proposal for the Program, the CMSA understands that the FDIC will risk adjust its guarantee exposure by determining what level of guaranteed leverage a specific PPIF may incur. Presumably, as the risk profile of an asset pool increases, the maximum leverage that the FDIC would be willing to guarantee would decrease. However, the FDIC could consider allowing the maximum 6-to-1 leverage on any asset pool, subject to requiring a higher guarantee fee as the risk profile increases. For each asset pool, the FDIC could provide a matrix of permitted leverage and corresponding guarantee fee rate options that investors can select from when making their bids. Providing such flexibility, while adding complexity to the Program, may result in higher prices bid by investors.

<u>Should the program include provisions under which the government would increase its participation in any investment returns that exceed a specified trigger level? If so, what would be the appropriate level and how should that participation be structured?</u>

The CMSA does not believe that the Program should be structured to provide for an increase in the government's participation in investment returns that exceed a specified trigger level. Based on the published proposal for the Program, Treasury and the investors in a PPIF will benefit from all of the investment returns *pro rata*, based on their respective equity investments. To the extent the investors' profit potential is capped, the bids submitted by investors will necessarily reflect this limitation and likely result in lower prices to the selling Eligible Banks, or perhaps discourage some potential bidders from participating. In addition, capping the investors' returns could reduce the incentives of investors to manage the PPIF in a manner that seeks the highest possible returns for the duration of the PPIF, which could ultimately result in the overall returns to Treasury on its equity investment being less than if the investors' returns were not capped. Finally, if it is the view of Treasury and the FDIC that government warrants are required by the terms of the Emergency Economic Stabilization Act, then we urge that such warrants be structured in a way that does not result in the increase of the government's participation in investment returns that exceed a specified trigger level.

Should the program permit multiple selling banks to pool assets for sale? If so, what constraints should be applied to such pooling arrangements? How can the PPIF structure equitably accommodate participation by smaller institutions? Under what process would proceeds be allocated to selling banks if they pool assets?

Pooling together legacy loans from multiple sellers will involve greater structural complexity, but may also permit broader participation by smaller banks. While the CMSA suggests that the Program begin with single-seller auctions for simplicity and ease of execution, it may be possible to expand the Program in subsequent auctions. To increase the ability of smaller Eligible Banks to participate, the FDIC might consider running bi-weekly or monthly open pools where smaller Eligible Banks could agree to participate in these open pools that would be sent out to bid on regular or semi-regular basis. Allowing Eligible Banks the flexibility to pool loans will increase diversity in the pools (if diversity would increase the price) or create specialized pools that might appeal to investors with particular property type expertise or geographic interest. For example, several banks could join together to create a pool of hotel loans or other particular loan type. As discussed above, pools of different sizes and characteristics will encourage greater participation by a broad range of investors. Allocation of proceeds among the multiple selling Eligible Banks could be determined in the same manner that the FDIC evaluates the pools for leverage. To the extent the FDIC obtains valuations for the loan pools of each selling Eligible Bank separately from independent valuation consultants, those relative valuations among the loans contributed by each selling Eligible Bank could be used to set "contributory levels" and allocate proceeds among the selling Eligible Bank based on such relative valuations. These valuations should be completed prior to the aggregate pool going out to bid so that each selling Eligible Bank would know the allocation, and therefore be able to better understand their potential proceeds. Additionally, it might be beneficial to have the group of Eligible Banks establish an overall pool reserve price based on the contributory levels prior to the bidding process and require each Eligible Bank to sell their loans if the highest bid at least equals the reserve price. Otherwise, if one or more Eligible Banks refused to sell to the winning bidder, the pool composition could change and potentially compromise the sale.

What should the relative role of the government and private sector be in the selection and oversight of asset managers? How can the FDIC most effectively oversee asset management to protect the government's investment, while providing flexibility for working assets in a way which promotes profitability for both public and private investors?

While the government should put certain minimum standards in place for asset managers and servicers, investors must have the flexibility to choose their own asset manager and servicer, if different, and make decisions regarding the servicing of the pool. Because the interests of the government and the private investors will be aligned, as they will share in returns on a *pari passu* basis based on their equity percentage as investors in each pool, we concur with the structure outlined in the published proposal, which outlines the government's asset management role as primarily a passive one. Minimum standards should be developed for asset managers and servicers based on experience with assets comparable to the assets in the pool. Some useful criteria may be the size of the current assets being managed or serviced by the entity, its financial strength rating and other criteria commonly used in the capital markets to determine if an asset manager or servicer of loans is "qualified". In order to avoid conflicts of interest, the CMSA recommends that no borrower or affiliate of a borrower under a loan included in a PPIF should be allowed to be the asset manager of that PPIF. Additionally, in order to ensure ongoing compliance with the minimum standards, servicer and asset manager events of default should be included in the servicing contracts to allow servicers and managers to be terminated in cases where they fail to maintain the minimum standards or otherwise default in their duties.

In order to oversee the performance of the pools and asset managers/servicers, the CMSA recommends that a standard reporting package be utilized. To the extent the loans are commercial real estate loans, an example would be the CMSA's Investor Reporting Package, which has been developed with the input of many participants in the commercial real estate finance industry, including servicers and investors, and is used primarily with respect to commercial mortgage loans that have been securitized.[1] However, as many of the loans that will be considered for sale under the Program were not originated to be securitized, the related loan documents may not require the borrowers to deliver all of the information called for in the Investor Reporting Package. Accordingly, the information required in the Investor Reporting Package may need to be pared back to accommodate the more limited nature of information that the underlying borrowers are required to deliver under the loan documents. Such standardized reporting will allow the government to monitor the performance of the pools on a monthly basis. Also, the government may consider reserving the right to inspect the books and records of the PPIF.

Finally, it was discussed on yesterday's FDIC conference call for investors that the document package required to be entered into for each asset pool may contain certain covenants and other restrictions that asset managers must comply with in connection with the management and disposition of the assets. The CMSA notes that in the context of commercial real estate loans, removing discretion from asset managers by mandating or restricting certain actions in connection with the management and disposition of assets may chill investor participation in the Program. We believe that any such covenants and restrictions should be avoided and, if implemented to serve a compelling purpose, should be crafted as narrowly as possible.

In addition, the government may consider requiring annual compliance certifications be delivered by the servicers/asset managers of the pools. Guidelines for these types of annual

[1] CMSA's Investor Reporting Package is available at http://www.cmsaglobal.org/IndustryStandards.aspx?id=10078.

compliance statements are set forth in the Uniform Single Attestation Program ("USAP"), developed by the Mortgage Bankers Association of America. The USAP annual reporting method is commonly used in the loan servicing industry and servicers already generally comply with this type of annual compliance requirements. Adopting such an approach would simplify reporting and compliance to use standards already in place rather than new standards to be developed specifically for the Program.

How should on-going servicing requirements of underlying assets be sold to a PPIF and paid for? Should value be separately attributed to control of the servicing rights?

Servicing rights for commercial mortgage loans can have value and are commonly priced and sold separately from the loans. Currently and historically, the market for selling servicing rights to commercial mortgage loans is limited to performing loans that are sold to bankruptcy-remote entities, such as CMBS issuances or loans sold and/or securitized by Fannie Mae, Freddie Mac and Ginnie Mae. In addition, servicers that purchase servicing rights require that the servicing agreement does not permit the termination of the servicer without cause. To the extent servicers do not ascribe value to servicing rights, they will not bid to purchase the servicing rights, but will only bid to service the loans on a fee basis instead.

If the servicing rights have value, both the selling Eligible Banks and the investors should be able to price the value of the servicing rights based on basic data that is typically supplied in connection with a sale of loans. In certain cases, the selling Eligible Bank may want to keep this right, however, investors are likely to want to be able to choose their own servicer to the extent they are in a position to do so. The CMSA recommends that bids be solicited on a "servicing retained" and "servicing released" basis depending on the preference of the selling Eligible Bank. Selling Eligible Banks may also want to solicit bids on both a released basis and a retained basis for particular pools. This will encourage flexibility, permit Eligible Banks who are active servicers to potentially keep the servicing rights and permit investors to determine if they would rather have the right to sell the servicing rights and choose their own servicer or keep current servicing arrangements in place. In certain cases, servicing rights for commercial mortgage loans may already have been irrevocably sold by an Eligible Bank. Providing flexibility as to servicing rights will allow these loans to be included in the Program.

Should data used by the independent valuation consultant, as well as results of such consultant's analysis, be made available to potential bidders? Should it be made available to potential sellers prior to their decision to submit assets to bid?

As mentioned above, the CMSA believes that providing potential investors an opportunity to do meaningful diligence on legacy loan pools prior to bidding will result in more informed bids and therefore more fair and equitable pricing of legacy loans. As a result, the CMSA would support providing to potential investors the data used by the FDIC's valuation consultants so that the investors can use that information in formulating their bids. However, the CMSA does not believe that providing the results of the consultant's analysis is appropriate. The consultant's view as to valuation of a pool of assets may be unduly influential in the bidding process, which would detract from true price discovery for legacy loans. Indeed, the consultant's evaluation may well act as a cap on investor bids, which would not be healthy for the auction process and could discourage participation by Eligible Banks.

<u>An Observation Concerning the Structure of Equity Investments in PPIFs</u>

PPIFs will need to have a source of additional capital to fund periodic expenses related to owning legacy loans. The owners of loans secured (directly or indirectly) by commercial real estate may sometimes find it necessary or advisable to advance funds in connection with the servicing of such loans, in instances where borrowers fail to fund the cost of certain basic property maintenance measures (e.g., payment of property taxes, payment of property insurance premiums). In addition, certain types of loans require the lenders to fund additional advances to the borrower under the loan for development of the related property or for some other pre-agreed purpose and generally subject to the borrower meeting conditions to receipt of the additional funds. Finally, when commercial real estate loans default, lenders must incur costs in working out and/or pursuing remedies under the loan in order to protect their positions. In cases such as those described above, a PPIF will need to have a source of funding for such expenses. Many fund structures would provide for equity holders to contribute capital to cover expenses of the fund. Since Treasury is expected to be a 50% partner in each PPIF, it will be necessary for Treasury to be prepared to fund such episodic expenses on a *pro rata* basis with private sector equity holders. Contributions from both the government and private sector equity investors will maintain the balance between public and private sector participation which, as discussed above, is a hallmark of the Program which, in the CMSA's estimation, will be critical to its success.

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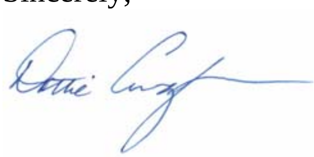
The CMSA appreciates the opportunity to comment on the Program. We have kept our responses brief, but would welcome the opportunity to elaborate on any of the ideas reflected in this letter. Please do not hesitate to contact us with any questions or comments or if the CMSA can assist with the Program in any way.

Sincerely,



Dottie Cunningham
Chief Executive Officer
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