From: Tom Sterken [mailto:tsterken@KellerRohrback.com]
Sent: Thursday, April 09, 2009 11:11 PM
To: LLPComments
Subject: Legacy Loans Program--Availability to Community Banks

Attention: Robert E. Feldman, Executive Secretary, Federal Deposit Insurance Corporation

Dear Mr. Feldman:

These comments are my personal opinion and do not necessarily represent or reflect the opinion of my firm or any other attorney, nor the opinion, circumstances or experience of any of our clients or their management.

The survival of many community banks is threatened by the current financial and credit crisis, and in some cases by the regulatory policies in response to these challenges.

We work with more than twenty community banks in the Pacific Northwest, several of whom are public companies traded on Nasdaq, and ranging in size from millions to billions of dollars in loans. Community banks have a significant presence in Oregon and Washington, with larger market shares in many communities than the large national or regional banks, and nationally, community banks represent a significant portion of the banking industry.

Like many community banks around the country, and especially so in this market where the local economy had remained relatively strong until recently, a number of our clients and other community banks have relied heavily on commercial and residential real estate lending, including construction and development lending, over the past decade to grow. Until recently, this growth strategy worked very well, and while their real estate lending concentrations were among the highest in the country, most community banks enjoyed high management, capital and other ratings from their primary regulators, in safety and soundness exams, as well as in compliance.

Eventually though, the unprecedented national credit and financial crisis primarily caused by the largest financial institutions and investment firms, dragged down our local housing market and economy, and in the past 6 months I understand that a number of community banks here have been, or are in the process of being examined and downgraded 1 or 2 levels by their primary regulators, and that cease and desist orders are being issued or considered following their safety and soundness exam.

Depending in many cases on the timing of their exams and therefore, their downgrades, I understand that some community banks here were were not allowed to participate in the Capital Purchase Program last Fall, or the more recent Capital Assistance Program, and are being shut out of most other programs to help banks raise capital to cover increasing loan loss reserves to cover declining real estate values, and be able to make loans to borrowers in their communities. Those that were fortunate enough to be able to get additional TARP capital, were given a significant competitive advantage, that has only increased as real estate values fall further and more banks are downgraded and required to sign regulatory orders that typically contain operating and financial covenants (e.g., no broker deposits, no loan restructures, higher than normal liquidity, capital and NPA ratios) that are unrealistic and virtually guarantee their eventual non-compliance and potential closure at considerable cost to the FDIC fund and the nation's taxpayers--particularly if financial conditions do not stabilize or improve.

I understand that some banks that have been asked to agree to covenants that they would be in violation of upon signing. For example, even after increasing their loan reserves and charge-offs to respond to examiners' findings and address the decline in housing and real estate values, a number of banks are being asked to agree to maintain a liquidity ratio of 15% (when ratios of 10% or so have been more common for well-run banks) and a risk-based capital ratio of 13% (without being able to renew or use any new broker deposits or other wholesale funding sources typically used by banks in percentages ranging to as much as 20% or more), and NPA ratios and prohibitions on loan restructures that do not take into acccount the practicalities of the loan workout and collection process.

I suspect that most, if not all of the TARP recipients in the Pacific Northwest, including some of our clients, would be in the same regulatory, liquidity and capital predicament today as the other community banks who were excluded from TARP now find themselves.

In any event, properly structured, the new Legacy Loan Sale Program announced by the Treasury and FDIC last month could provide a vehicle to save and strengthen many community banks, by allowing them to sell their loans at a significantly better price than what the FDIC can obtain today by liquidating the banks and selling their loans through existing Internet-based auction vendors, with possibly some seller financing being provided by the banks. With all the rumors of bank failures, merger and acquisition activity has dried up, and the prices FDIC is able to realize from an acquiror for deposits and other bank assets declining. Upon purging their balance sheets, these new "good banks" would then be able to raise capital from private investors or through the securities markets, thus saving the federal government and the FDIC fund from the costs of closing, liquidating and selling numerous banks and their assets. With their current regulatory problems and capital constraints and the adverse conditions in the capital markets, these banks cannot raise any significant capital nor can they sell their banks and realize any going concern, good will or franchise value.

However, while the Summary of Terms for the Program indicates that all domestic banks are eligible to participate as sellers, it is my understanding from recent conversations with FDIC representatives, that some think that like TARP the Legacy Loan Program should not be available to 4 and 5 rated banks.

I submit that excluding banks from participating based solely on their current regulatory rating status would unnecessarily threaten the availability of credit to borrowers in many communities, destroy the wealth of community banks' founders and other shareholders, and cost the federal government and the FDIC's insurance fund geometrically more, than allowing as Treasury apparently intended, all domestic banks to potentially participate in the program. Excluding many community banks from the program would also significantly reduce its potential impact in strengthening the banking system, freeing up the credit markets and stimulating the economy throughout the nation. Rather than excluding many banks from participating, all banks large and small should be allowed to participate, at least with appropriate safeguards, such as management review and where necessary, replacement, restrictions on executive compensation, commitments for private capital upon completion of their loan sales, and risk-based guaranty fees, similar to those used for the Temporary Liquidity Guarantee Program.

Also, even if all such banks will be eligible for the program, there is the question of how soon such a program structure and buyers will be available for community banks (they will likely need to be able to sell in multi-bank pools or conduits) and the commercial and residential, subdivision, construction and land development loans that predominate in their loan portfolios.

A significant portion of the banks' nonperforming loans here are residential construction for homes and condos, and subdivision development loans for lots. These are also the types of loans with some of the steepest discounts in the current auction market, and therefore, could offer the greatest opportunity for value enhancement under the Legacy Loan Program. Some of the additional capital resources could, for example, might be used by the banks to provide low cost loans to buyers of partially completed homes in troubled subdivisions financed by the banks, to complete their homes, increasing the banks' collateral position and assets. It is critical then, for the program to promptly address and provide a market for the sale of these types of loans, which should not be as difficult to value as many securitization products, and should over time generate attractive returns to the investors. It's my understanding that a number of investors have expressed interest in this kind of product for this market.

The organization and development of prospective buyers for these types of loans will probably require a different strategy and appeal to different, more local or regional buyers, as these loans are local and regional products. In order to accelerate the process, developing these buyers should proceed on a parallel track with the securitization-type products, and possibly involve local and regional banking associations, investment bankers and other service providers.

Thank you for your consideration.

Best regards,

Tom Sterken
Keller Rohrback, L.L.P.
1201 Third Avenue, Suite 3200
Seattle, WA 98101
206.224.7585--direct