FDIC REQUESTS COMMENTS ON THE LEGACY LOAN PROGRAM April 2, 2009

E2M PARTNERS, LLC COMMENTS

Following up on the Treasury Department's March 23, 2009 announcement of the Public Private Investment Program ("PPIP"), the FDIC has issued a description of the Legacy Loan Program ("LLP") that is a part of the PPIP and has requested public comments on a list of questions relating to the LLP. See, *Legislative* Alert "Treasury Department New Public-Private Investment Program", March 23, 2009.

The following is a list of questions on which the FDIC is seeking public comments and the procedures for submitting comments, which are due by April 10, 2009:

1. Which asset categories should be eligible for sale through the LLP? Should the program initially focus only on legacy real estate assets or should any asset on bank balance sheets be eligible for sale? Are there specific portfolios where there would be more or less interest in selling through the LLP?

   The LLP should provide banks the flexibility to sell all categories of legacy assets in time. The program should initially focus only on real estate whole loans, due to the relative simplicity in valuing non-participated real estate loans and the need for immediate liquidity in the real estate silo of the banking industry. Legacy assets should be sold in pools, segregated by asset class, thereby creating a more efficient process. Furthermore, real estate asset pools should be segregated by underlying collateral product type (ie: multi-family, residential, land, industrial, etc.), which will increase the investor interest by bringing specialized firms into the fold.

2. Should the initial investors be permitted to pledge, sell or transfer their interests in a public-private investment fund ("PPIF")? If so, how should the FDIC ensure that subsequent investors meet the program's criteria for investors?

   Initial investors should be able to pledge, sell or transfer their interests, because any restrictions on these rights will result in reduced clearing prices paid to the banks. Potential buyers should be approved by the FDIC, based on pre-established investor criteria, prior to sale or transfer of PPIF interests, and any transferee, etc. should be subject to such qualification criteria.

3. 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? Should the amount of the government's investment depend on the type of portfolio?

   Integrity in pricing will be accomplished through increased competition for legacy assets. However, if the government equity percentage is too low the LLP could be subject to popular criticism, as the investors will be perceived to enjoy the majority of the upside potential. Conversely, if the government percentage is too high, investors may determine that the investment size does not warrant the requisite due diligence and deposit expenditures. A 25% to 50% government equity percentage would be appropriate. The scale of the government's investment should not be predicated on the type of portfolio.

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

   Yes, many investors do not want their names available in the public domain. Disclosure of participants will lead to fewer interested investors.

5. 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?

A wide range of asset pool sizes ($50 million in par value as a minimum), segregation of asset pools by asset type, transparency and quality of asset information, limited investor requirements and adequate due diligence time will lead to increased investor interest. The FDIC may increase participation by limiting investor downside or providing tax incentives for investors that experience capital losses. Additionally, reasonable certainty that winning bids will be accepted will further incent investors to engage in extensive due diligence.

Banks will be more motivated if the auction process allows for an undisclosed reserve price for the pool of assets, whereby winning bids that exceed the reserve price are automatically accepted. Winning bids below the stipulated reserve price may be accepted or rejected by the banks. Additional bank interest would come from the government taking the initial loss from the impairment of assets, in the event the winning bid is less than the current book value of the pool of assets. A significant percentage of balance sheet loans are valued on a hold-to-maturity basis, not a mark-to-market basis and many banks may be unable to remain solvent if required to write the assets down to reflect clearing prices. This result would be contrary to the overriding goal of the LLP, to restore financial stability to the banking industry.

6. 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? If the latter, would a Dutch auction process or some other structure provide the best mechanism for bridging the potential gap between what investors might bid and recoverable value? If multiple investors are allowed to bid through a Dutch auction, or similar process, how should asset management control be determined?

   An absolute auction would create the most investor interest. A reserve auction would create the most bank interest. Banks will be less interested in selling assets if no reserve price is stipulated. There is a potential for catastrophic industry wide write-downs if banks are not allowed to reject bids below a reserve price. Investors should be required to bid on the entire equity stake of a PPIF in order to facilitate the most efficient process and create clarity in pricing.

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

   The FDIC should prioritize the sale of asset pools based on marketability and diversity of pool sizes. Asset pools that are easiest to value (pools of assets with consolidated and transparent information already available) and most marketable are more likely to sell and should be brought to PPIF auctions first. Additionally, a wide range of asset pool sizes will foster increased investor participation.

8. What are the optimal size and characteristics of a pool for a PPIF?

   A broad range of asset pool sizes will increase bank participation as well as investor interest. Pools of assets should have a minimum face value of $50 million. Homogeny of asset type within a pool will streamline the auction process and increase investor participation. Additionally, the FDIC or the selling bank should provide transparent, accurate, and concise data for each asset within a pool.

9. 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?

   Investors will require an executable loan document prior to the auction process. The government should provide the investor community with standard loan documents to be used. Certainty of all loan terms will increase investors' willingness to perform due diligence and provide deposits. In the current lending environment, investors will be averse to refinance risk. A term of at least five years will adequately mitigate this risk for notes secured by legacy real estate loans.

10. 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?

It would be preferable for the selling bank to take a note in exchange for a pool of loans in order to increase process efficiency. To incent banks to take a note from the PPIF, the issuing bank should be allowed to sell the note. The advantage of issuing public debt would be to provide banks with up-front cash. However, the process for issuing public debt would significantly delay asset purchases and complicate the auction and closing processes. Issuing public debt is only practical for large transactions and therefore would not aid small PPIFs. The reporting and regulatory requirements, in addition to compliance with debt covenants associated with public debt, will deter potential investors from participating in the LLP. Issuance of public debt would significantly reduce the PPIF's flexibility.

11. 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?

Investors will require transparency regarding the guarantee pricing structure before submitting bids. The bids offered for bank assets will reflect the FDIC guaranty fee, regardless of the fee structure. Excessive government and third party fees will reduce pricing.

12. 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?

Private investors and the government will be partners in each of the PPIFs and should therefore share the profits and losses of the fund in proportion to their respective equity capital contributions. The program should not include these types of provisions, because inclusion could limit investor participation and reduce pricing. However, if the government requires a disproportionate share of the profits beyond specified return hurdles, the interested investors will price the bid accordingly, regardless of participation structure.

13. 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?

Investors will be indifferent to the pooling of assets from multiple banks, so long as participating banks agree on the assets available for sale and the seller financing prior to the formation of a PPIF. The FDIC should establish a broad range of PPIF sizes and/or allow asset pooling to encourage smaller banks to participate. Selling banks, which choose to pool assets with other banks, should be required to establish their relative asset contribution values, prior to the formation of the PPIF, to determine the allocation of proceeds.

14. What are the potential conflicts which could arise among LLP participants? What structural arrangements and safeguards should the FDIC put into place to address or mitigate those concerns?

An LLP conflict would occur if the PPIF investor were a related entity to the selling bank. To mitigate this risk the FDIC should require that each transaction include only unrelated buyers and sellers. The FDIC should impose stiff fines on institutions that execute related transactions. To further mitigate the related party risk the FDIC could limit PPIF participants to only one buyer and one seller.

15. 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?

The government should set minimum standards for an asset manager to qualify under the LLP. Assuming the minimum qualifications are met, the private sector should be responsible for determining the specific asset manager for each PPIF. The FDIC should stipulate a universal LLP asset management fee structure before the first PPIF is formed. The FDIC should require standard reporting requirements and approval rights on a limited number of major decisions, but otherwise allow the private sector to manage the assets. Delays in decision making, especially the ability to sell an individual asset, could significantly reduce profits realized by the PPIF.

16. 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 of the legacy loans is a known cost of the PPIF. The FDIC should stipulate a universal servicing fee structure for the LLP before the first PPIF is formed. Value should not be separately attributed to control of the servicing rights.

17. 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?

    Third party valuation analyses should be available only to the FDIC. Disclosure of the determined value will set benchmarks for the selling bank, potentially increasing the bid-ask spread. The selling bank and the investor should perform independent due diligence.