Sears Tower, Suite 5800
233 S. Wacker Dr.
Chicago, Illinois 60606
Tel: +1.312.876.7700 Fax: +1.312.993.9767
www.lw.com

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April 10, 2009

By Electronic and United States Mail

Robert E. Feldman
Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 17th Street, NW.
Washington, D.C. 20429

Re: Legacy Loans Program

Ladies and Gentlemen:

We appreciate the opportunity to comment on the Legacy Loans Program (the "LLP"), pursuant to which the Federal Deposit Insurance Corporation (the "FDIC") and the United States Department of the Treasury intend to partner with private investors to help banks remove distressed assets from their books. The comments expressed in this letter represent the views only of the attorneys who have prepared this letter and do not necessarily represent the views of other attorneys in our firm.[1] Further, these comments do not necessarily represent the views of, and may in fact conflict with, the views of our clients on these matters. We reserve the right to advocate for different or inconsistent positions on our clients' behalf. This letter should not be construed as expressing a legal opinion or providing legal advice to you or any other person, and may not be relied on as a legal opinion by any person.

We agree with the Federal Deposit Insurance Corporation (the "FDIC") that the LLP presents a significant opportunity to address many of the problems associated with the current lack of liquidity in the credit markets. As the FDIC, the Federal Reserve, the Department of the Treasury and others have recognized, the current economic crisis is multifaceted, complex and interconnected. Like a sliding puzzle, a solution to one problem may cause something else to shift out of place. We are closely following the Public Private Investment Program ("PPIP") of which the LLP is a part and other economic programs that have been established over the last

[1] Latham & Watkins operates as a limited liability partnership worldwide with affiliated limited liability partnerships conducting the practice in the United Kingdom, France and Italy and an affiliated partnership conducting the practice in Hong Kong. We have over 2100 attorneys in 13 countries, including more than 1500 attorneys in the United States.

year and a half, such as the Term Asset-Backed Securities Liquidity Facility ("TALF"). We are also closely following mortgage modification proposals, financial system oversight proposals, bankruptcy reform, stimulus legislation and other measures that have been designed to assist homeowners and restore confidence in our financial system. One of the great challenges, which we feel may not yet have been resolved within the legislative bodies and government agencies proposing them, is how to ensure that these varied programs will work together to restore economic stability given that some of their goals may be inherently contradictory.

One thing we have seen frequently in the press and public commentary, including the comments already made with respect to this program, is the belief that interventions within the financial sector constitute "handouts" to the wealthy at the expense of taxpayers and consumers. In our view, the opposite is true. For the average American to attain the American dream—a secure home, a stable job, retirement security—a strong, properly functioning financial system is necessary. And a strong, properly functioning financial system requires, in addition to appropriate financial reporting and sound risk management, investors who are willing to provide capital to banks and to purchase or lend against bank assets to support the banks' ability to make consumer and business loans. Those investors have retreated as they faced unexpected losses and uncertain asset valuation, contributing to the spiraling liquidity crisis. We see the PPIP and TALF as programs to encourage their return.

Banks cannot make mortgage loans using funds they do not have. They cannot make new mortgage loans if all their available funds are tied up in older loans that will take years to mature in accordance with their terms. Prior to the collapse of the securitization markets, securitization investors provided a significant portion of the funds that supported banks' ability to lend, usually at very low rates of return because of a perceived lack of risk. In 2006, for instance, new issuances of mortgage-backed securities were approximately $2.13 trillion, with non-agency MBS (the portion not issued through Fannie Mae, Freddie Mac, and Ginnie Mae) topping $917 billion. In 2008, total new issuance of mortgage-backed securities fell to $1.34 trillion, with a mere $40 billion of that coming from non-agency issuances.[2] To those who do not have a deep knowledge of this industry, that may seem like a loss to the financial sector that is not relevant to ordinary Americans—but it is extremely relevant. If a bank has only $100,000 to lend, and it makes a mortgage loan, it has no new ability to lend until more money comes in. Traditionally much of that has come from securitization: bank makes a $100,000 mortgage loan

[2] Statistics from www.SIFMA.org. We have seen similar trends in every class of asset-backed security as well: credit card issuance down from $90 billion in 2007 to $65 billion in 2008, with only $7 billion of new issuance so far in 2009 even with the support of the TALF program; auto loan issuance down from $66 billion in 2007 to $36 billion in 2008 and $7 billion in the first 3 months of 2009; and student loans—for which there were *no* new issuances during the period from September 2008 through January 2009—declining from $53 billion in 2007 to $28 billion in 2008, with a mere $2 billion in February and March 2009 combined. *See* Appendix 2 to the Federal Reserve's joint response, dated April 7, 2009, to the March 20, 2009 Congressional Oversight Committee inquiry into the TALF program.

so John Smith can buy his dream house, sells that loan into a securitization for $100,000, makes a similar loan to Annie Fernandez so she can buy her dream house, and so on. If the bank is waiting for John Smith to repay his loan before it has money to lend to Annie Fernandez, it may have a long wait. This is how securitization in the mortgage sector worked—it matched the outflow of cash to mortgage borrowers with an inflow of cash from securitization investors backed by the 30-year stream of payments on John Smith's loan and many others. When the mortgage crisis hit, that matching stopped and banks were left with long-term assets, many of questionable quality, and restricted ability to lend. Borrowers could no longer obtain mortgages, not only because standards had tightened but because of a sharp decline in funds in the system to lend. And with insufficient mortgage availability, housing prices fell. Repercussions have been felt well beyond the financial sector, as homeowners who have not lost their homes have nonetheless lost much of their equity in them; businesses have shuttered; unemployment levels have increased dramatically; and food banks are struggling to keep up with rapidly rising demand.

One of the reasons we decided to submit a comment letter is our hope that the parameters of the LLP will be established to complement TALF and similar programs and to encourage capital markets investors to again provide banks with the consistent financial support they need to restore normal lending capacity. Economic recovery depends on strong credit markets and available sources of liquidity. We urge the FDIC, the Treasury and the other agencies and governmental bodies involved in the LLP, TALF and other aspects of financial reform to consider the effects on traditional capital market investors of both substantive changes that may make their investments more risky[3] and the rhetoric that in many instances has vilified passive investors who took severe losses on investments that were funding the American dream.

I. Asset Categories

You have asked for comment on the types of assets to be included in the LLP. We would encourage the FDIC to take a broad view of asset classes for consideration for this program, so that banks can structure the portfolios of assets to be sold in ways that best support their particular needs. That being said, it is generally considered easier to diligence and value a pool of similar assets than a pool of dissimilar assets, so except in the circumstance where a single asset is being separately offered, combining assets by category (rather than merely by seller) may be the most efficient way to construct the program. Non-agency residential real estate assets are clearly contemplated by the program, and we think that in addition to mortgages, such assets should include real estate owned (REO) properties the purchase of which may be useful in stabilizing home prices. Commercial mortgages are also an important asset class for this program.

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[3] We fully appreciate the need to have consumer lending standards that protect consumers from predatory lending. At the same time, changing the terms on which consumer lending can be made or altering creditor remedies so that lending institutions cannot effectively protect themselves from loss may have the effect of severely curtailing the availability of consumer credit and further weakening our financial industry.

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In addition, we would strongly recommend including corporate loans generally within the program. With the collapse of the market for CLOs (structured securities backed by pools of corporate loans), banks' ability to make new corporate loans has been significantly curtailed, and obtaining new loans even when available has become prohibitively expensive. As a result we are seeing good companies struggling to refinance maturing debt or to obtain new debt for needed growth or capital improvements. The lack of funding, even when corporate fundamentals are sound, is forcing more companies into bankruptcy; and debtor-in-possession financing, which historically has been critical to help companies that are restructuring emerge from bankruptcy as going concerns, is much harder to obtain than historically. As a result, companies that would have been restructured in prior downturns are finding they have to liquidate, resulting in more unemployment and greater damage to the economy. Indeed, we see the scarcity of debtor-in-possession financing as a significant constraint on economic recovery. We think including corporate loans within the PPIP would help unlock the credit markets for both companies that are seeking liquidity for normal operations and companies that are in financial distress, and we view these loans as an important additional asset class for the program.

Although we see these as the areas of greatest need, we would not wish to see the program limited, especially where the needs of a particular bank fall outside of these areas. Accordingly, we suggest that the FDIC take as broad an approach to asset classes as possible.

II. Investor Qualifications, Liquidity Concerns and Related Issues

You have a raised of number of separate questions regarding how to encourage investment participation, whether to permit transfers and pledges of investors' equity interests, and whether the identity of participating investors should be made public. In our view, these are all interrelated.

The program materials that have been released so far with respect to the LLP indicate that investors will have to be "pre-qualified" to participate in the auction process, but do not indicate what the required qualifications will be. In our view, "qualification" should be limited to (1) demonstrable ability to purchase the assets; (2) to the extent Treasury is relying on investor valuations to set the price of the assets and the size of equity investments in those assets, sufficient expertise to value the assets (which expertise should be able to consist solely of hiring a qualified advisor); and (3) the customary type of clearance expected for establishing US bank accounts, such as customer identification procedures and comparison to OFAC lists. Global participation should be encouraged, including from sovereign wealth funds and offshore feeder funds, to provide the largest possible experienced investor base and source of capital. Notwithstanding some of the reactions we have seen so far, in our view, this program—while it involves government funding—does not involve government subsidy, but merely uses the leverage provided by the FDIC-guaranteed funding to allow investors to earn a return commensurate with risk without having to build the risk premium fully into a depressed purchase price for the assets.[4] Moreover, the Treasury co-investment does not subsidize the private investment but expands its reach so that a larger group of assets can be purchased. Private investors—side-by-side with Treasury—are still taking the first loss position.

You have asked whether there is any reason the identities of the investors should not be disclosed. We believe that not disclosing investors' identities would maximize investment, particularly in a political climate in which such investors, if disclosed, could expect criticism for "taking advantage" of distressed circumstances instead of recognition for making what is, fundamentally, simply a necessary investment in assets that had to be sold for the health of the selling bank and the financial system. If the auction process is fair, there should be no risk of the sort of favoritism that would make an investor list an important part of the oversight process. We do think making public aggregate data about the characteristics of the investors would be valuable. We note, further, that disclosure of investor identities is not an all-or-nothing proposition, and while we would favor no such disclosure, an alternative approach could include making public information, for example, only about investors who received funds under the Capital Purchase Program established under the Troubled Asset Relief Program ("TARP"). Any such disclosure, of course, may discourage participation by those investors.

Investments in the PPIP will be more attractive to investors if they are transferable, and lawyers who are active in fund structuring are very experienced in establishing transfer restrictions that permit transfers subject to fundamental qualifications (such as qualified institutional buyer status) or to more specific criteria. Transfer restrictions that include screening under an anti-money laundering program could be established. Although we see no potential issues in permitting the transfer of passive investments in LLP funds, the FDIC and Treasury may wish to consider the consequences of permitting transfers of controlling equity interests by an equity investor that is also in charge of the management of the fund. An additional complicating factor may arise with respect to transfers to or from employee benefit plan or ERISA investors, as investments by these funds in more than 25% of the equity may cause the entire fund to be treated as plan assets and change many of the management fundamentals. Given the importance of employee benefit plan and ERISA investors to the success of this program, we would encourage you to work with structuring experts to maximize the ability of these investors to participate.

Although we feel that broad investor participation will support a more robust auction process, more accurate price discovery, and increased investment in these types of assets generally, we caution that allowing participation by individual investors poses its own issues. The private investment in these vehicles, as you know, is the first loss position in a highly leveraged, complex vehicle that is investing in distressed, illiquid assets. While there is significant opportunity to invest wisely and earn a meaningful rate of return on this program, the risk continues to be substantial. Said another way, the FDIC-guaranteed debt is at the top of the

[4] To the extent FDIC guarantee fees are not charged commensurate with risk, the leverage provided could be viewed as a government subsidy. It is not clear to us whether fees will be structured on that basis.

capital structure. The investors are at the bottom, and protect the FDIC against first losses, rather than the other way around. As you know, most vehicles structured in the private sector involving pooled assets would customarily limit those investments, at a minimum, to accredited investors who were also qualified purchasers for purposes of the Investment Company Act (or in some instances to key employees who were directly involved in managing the assets and structuring the pool). Although the Investment Company Act and other securities law issues that are resolved through that approach could be eliminated by structuring an SEC-registered fund that included individual investors, the suitability issue remains—even with robust disclosure, can investments be structured so that retail investors can participate without taking on excessive risk? We can easily envision the current outcry demanding retail participation transformed into a commensurate outcry over outsized retail losses if investments sour. [5]

III. The Auction Process

To encourage maximum participation, the auction process needs to be fair and transparent. Investors should be permitted the opportunity to conduct reasonable due diligence. We would suggest that the FDIC consider the extent to which such due diligence should include not only the traditional data provided to investors in these types of assets, but also, in the case of residential mortgages and related assets, to the extent reasonably available from the selling institution or servicers, the types of expanded disclosure reflected in the American Securitization Forum's ("ASF") "Project RESTART" program for residential mortgage-backed securities. In the period since the economic crisis began, there has been a focused industry effort, including involvement by both issuers and investors, to redefine and standardize the information relevant to an investment in pooled mortgages. We would encourage the FDIC to consider the ASF's work in this area in formulating an appropriate approach to diligence.

We would expect confidentiality provisions to be put in place to protect the selling bank with respect to the auction process. This is industry standard, and should not discourage investment. Further, we would expect that the diligence process would be structured to protect consumer information as required by law and consistent with the FDIC's current practices.

In an auction of pooled assets, it is inevitable that bidders will disagree as to the value of specific assets in the pool even if their views of the value of the pool as a whole are quite similar. Although for residential mortgage loans, valuations may well be determined across the aggregate pool, for larger or more unique assets—e.g., commercial loans—valuation will likely be

[5] One possible approach to balance the political issues of excluding individual investors against the political issues of allowing individual investors to take first loss risk positions in leveraged pools of distressed assets, would be to allow retail investors to participate on different terms than institutional investors, with somewhat lower yield but also lower risk. There are a number of possible structures that, while adding complexity to the program, might strike an appropriate balance between allowing retail participation in attractive investment opportunities and permitting or encouraging those investors to take substantial risks they may not fully understand.

determined on an asset by asset basis even if that detail is not reflected in the aggregate bid. We appreciate that it may be faster to sell large pools of assets than to disaggregate them, but we would encourage you to consider with your advisors, for each selling bank, whether there are assets that would be best auctioned individually or in smaller groups. As noted above, we believe that the best price discovery will be achieved, at a minimum, if unlike assets (e.g., residential mortgages and commercial mortgages) are not pooled together even if offered by a single institution. We would also note that, to the extent possible, obtaining disaggregated bid prices even on pooled assets may provide meaningful information to both the FDIC and the selling institution.[6] On the other hand, bidders may be discouraged from participating if they have to share this disaggregated data—which they may view as proprietary—and that should also be considered in structuring the bidding process.

You have asked whether investors should be required to bid on the entire equity stake in a vehicle or whether partial bids should be allowed. We believe allowing partial bids would add complexity to the bidding process and subsequent fund management. Some of the same goals may be achieved by offering smaller pools of assets where it appears unlikely that a single comprehensive bid will maximize value.

There has been much commentary as to whether banks should be able to refuse the highest offered price after going through the auction process, or whether they should be allowed to set a reserve price. Although we appreciate that the PPIP is designed to eliminate the effects of the current market disruption on asset pricing, whether it will do so in practice remains to be seen. We would not want to see banks have to choose between retaining assets on their books that they would prefer to sell, or entering the process and risking a forced sale at a price significantly below their valuations. At the same time, we have great sympathy for the position that investors will not want to devote the resources to a diligence and auction process where the winning bid may ultimately be rejected.

Our suggestion would be to allow banks to determine at the beginning of the process for an asset pool whether they wish to retain the right to reject a winning bid or to set a reserve price, or whether they are willing to sell to the highest auction bidder regardless of the ultimate size of the bid. That information could then be made available to potential bidders before they begin their diligence process (including the dollar amount of the reserve price, if established) and could be considered by them in determining whether to devote their resources to bidding on that particular pool. If a selling bank received too few indications of interest for a pool that it reserved the right not to sell or for which it set a high reserve, it could reconsider whether to change the conditions under which it was participating in the auction or to withdraw the pool from the auction process. As selling banks observe the results of auctions by industry peers, and develop confidence in the process as able to set a fair price, we would expect that fewer of them would reserve the right to reject a winning bid.

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[6] We understand that the FDIC's current practice includes offering pooled assets, but accepting bids on an asset-by-asset basis. If this is intended to be an aspect of the program, we would recommend clarifying it in the program materials.

We would also suggest that the engagement of experienced auction managers—who might be selected by the selling bank or by the FDIC for the program as a whole—be considered to oversee and advise on the process and to conduct the auction. There are many financial industry participants who could add significant value to the price discovery process and also assist with technical issues, settlement processes, and general coordination.

One further note: we appreciate that the PPIP will be run in conjunction with various initiatives to protect consumers through mortgage modification programs. We would suggest that, to the extent you intend to require modification of residential mortgages and have not done so prior to the asset sale, the specifics of what will be required be explicitly provided to investors before they bid.

IV. Small Bank Participation

To most completely address the issues in the banking sector, PPIP participation should be available to all banks regardless of their size or the number or value of legacy assets they wish to include. In some instances, pooling their assets with those of other banks to create a sufficiently large pool may be most efficient (perhaps via a bankers' bank or a similar structure); but in other cases, they may be best served by being allowed to participate using a very small pool. Some comment letters have already suggested that, for assets of community banks, the best value may be obtained through a sale within the community—and of course there may be further long-term benefits to the community to keeping investments local. We would like to see the program operated in a manner that facilitates that.

There are, as you've noted, a number of complexities associated with pooled asset portfolios, including how to resolve differing views as to whether to accept a bid and how to allocate the bid price among multiple sellers. While it would be possible to require bidders to itemize their bids, what would then happen if the winning bid for the pool places a lower value on assets of one bank than the unsuccessful bids would have placed? One possible way of dealing with this would be to allocate the winning bid among selling institutions by using the average itemized bids for assets in the pool, although this would still be, at best, an approximation of relative value. Because of these complexities, it seems to us that pooling assets of smaller banks should only be considered if it is clearly not feasible to sell them separately.

V. Terms of FDIC-Guaranteed Debt

All of the economics surrounding the FDIC-guaranteed debt—which we understand will consist of a loan by the selling institution to the purchasing fund, with the fund's obligations guaranteed by the FDIC—should be made available to potential investors at the beginning of the auction process. This should include the term of the loan; the face amount; the applicable interest rate or the method by which it will be determined (e.g., for a fixed rate loan, swaps + 100bp); the amount or percentage of any upfront or continuing fees; whether it is renewable, and if so how the terms at renewal will be determined; the nature and consequences of any events of default; to what extent distributions to equity investors in the fund will be permitted prior to the full repayment of the FDIC-guaranteed loan; the nature and extent of any restrictions on additional debt by the fund; the circumstances, if any, under which assets can be resold by the fund; and in what priority collections of assets and proceeds of asset sales will be applied. Consistent with current lending criteria, we would expect the FDIC-guaranteed debt, at a minimum, to constitute eligible collateral for pledging at the Federal Reserve's discount window.

You have asked about whether the funds should instead issue public FDIC-guaranteed debt to support its asset purchase. There are a few aspects of such an approach that would need to be considered: How would the debt be raised before the auction process occurred, especially given that the total amount of debt needed would be tied to the price paid for the assets? Would there be debt raising processes occurring for a number of funds concurrently, with only one closing in connection with the asset sale? And would the public debt issuance negate any Investment Company Act exemption on which the fund would otherwise rely?

In addition, you have asked whether the guarantee fee with respect to the FDIC debt should adjust based on the risk characteristics of the pool. Certainly that is an option. We question, though, whether it is necessary given the intention to adjust the leverage of the pool based on those same characteristics. In a pool with 1:1 leverage, for instance, the FDIC guarantee will be protected by an equity investment equal to 50% of the value of the assets (as established in the auction), whereas it would only be protected by a 20% equity cushion if leverage were 4:1. Adjusting the guarantee fee as well as the leverage may well be viewed as double-counting, and may discourage private investment in the assets that banks most critically need to sell.

VI. Conflicts

There are a number of conflicts inherent in a highly leveraged structure between the equity provider and the debt provider. Equity investors may be reluctant to sell assets even when otherwise appropriate if the consequence is that the vehicle will be delevered. Similarly, equity investors may be reluctant to recognize losses on investments in a timely manner if recognition would trigger remedies with respect to the debt. If assets perform worse than anticipated, such that the equity cushion erodes, the manager may no longer have "skin in the game" that would cause it to manage effectively on behalf of the FDIC. Traditional forms of self-dealing, such as selling assets out of the fund to affiliated entities, would also be a concern.

All of these conflicts can be managed with appropriately drafted documentation and management procedures. We would encourage the FDIC to establish a set of overarching principles with respect to these types of conflicts, subject to modification on a deal-by-deal basis to address issues specific to a single participant.

VII. Fund Management and Servicing

To maximize value for these assets, it seems to us to be essential that they be sold servicing released. New investors will want to be able to control the process of realizing on these assets, and leaving the servicing in the hands of the seller will not give them that control.

If servicing remains with the selling institution on a temporary basis during a transition period, the parameters of that servicing authority—including servicing fees, standard of care, and scope of authority to deal with payment issues—should be clearly documented at the time of sale.

Although provisions related to fund management remain unclear, we believe the expectation is that private investors will also manage the funds. While we would consider it important that private investors have control over the *selection* of a fund manager—subject to appropriate experience and qualifications—we believe broader participation will be achieved if investors have the ability to appoint a third-party manager rather than filling that role themselves.

Two additional notes: you have indicated that executive compensation rules will not apply to "passive" Private Investors. In our view, they also should not apply to more active investors, servicers and fund managers—at least not by virtue of their participation in the PPIP. We encourage you to provide guidance with respect to these matters. Further, you have indicated that fund management will be subject to waste, fraud and abuse rules. We would urge you to clarify the specifics of these rules and how they will apply and assist the management of the program as quickly as possible.

VIII. Fund Structure and Investor, Seller and Treasury Economics

You have asked about the appropriate percentage of Treasury investment in these asset pools. Because the Treasury investment is side-by-side with the private investment, rather than subsidizing it, the questions are different than those related to the leverage determination with respect to the FDIC-guaranteed debt. We would suggest that there are three major considerations: the extent to which the investors would need additional equity to be able to complete the acquisition of the entire pool of offered assets; the extent to which the Treasury wishes to assume the risk of an equity investment in the assets; and the need to maximize the use of the remaining funds available for this purpose under TARP. In formulating a bid, it will be important to investors to know the maximum amount of equity the Treasury is willing to co-invest, both as a dollar amount and as a percentage of total equity. To the extent private investors do not need to utilize that maximum amount of Treasury co-investment, it may well be consistent with the success of the overall program to have a smaller Treasury investment. Although we do not have views on an appropriate percentage, we would suggest that, beyond the determination of how much equity would be needed to facilitate the sale, the other factors involve balancing the potential risk to the Treasury funds against the desire to share the potential upside from a co-investment with taxpayers. For larger pools, a smaller percentage investment may be more appropriate than for smaller pools.

It will be important that the fund operating principles be established at the outset of the program and honored. As mentioned elsewhere in relation to the terms of the FDIC-guaranteed debt, the priority for application of proceeds among the FDIC, the Treasury and the private investors (sometimes referred to as the "cash flows" or "waterfall") should be established prior to the completion of the auction. Although we do not support having a maximum rate of return for private investors, if there is an intention to impose a maximum rate of return that should be clear from the outset. Although we appreciate that this would not be within the FDIC's control, punitive changes in the tax laws with respect to private investors who are perceived as having received too much profit on these investments should be resisted, not only to maintain fairness with respect to the assistance the government is requesting under this program, but also to preserve the ability to access private capital to support future government programs.

We have seen references to a requirement for issuance of warrants by these funds to comply with the terms of the TARP program. We fail to see how, other than as a technical matter, the issuance of warrants is meaningful given the nature of these funds and the Treasury co-investment in them from the outset. Again, the economics of any warrants and how those will affect private investors should be made clear prior to the auction.

We would anticipate that any fund used in this program would be established so as not have entity-level taxation. Structuring so that the tax attributes of investments and their returns pass through directly to investors, without intermediate entity level taxation at the fund, is a critical part of making the economics work for any pooled investment vehicle. We appreciate that there may be political sensitivity related to efforts to structure these vehicles to minimize the tax impact, but we fear that double taxation would limit investor participation and reduce the efficacy of the LLP. As an example, if an investor buys a note for $100 in one year and receives $108 in principal and interest the following year, that investor will have taxable income with respect to the $8 received above the purchase price. If the same investor is allocated $108 from a $100 investment by a fund that is taxed as a partnership, he will likewise have taxable income with respect to that $8. On the other hand, if the investor invests $100 in a corporation that buys a $100 note and receives $108 with respect to that note, the corporation will be taxed on $8 of income, leaving only about $105 for distribution to the investor. And the investor will be taxed again with respect to the $5 in income it receives. As a result of this double taxation, on an after-tax basis the investor will receive several dollars less from an investment in a corporation than from a direct investment in the related asset. Structuring a fund—which, unlike most corporations, has no real purpose other than to serve as a pass-through vehicle—that does not have entity-level taxation allows investors to participate in pooled investment vehicles and receive after-tax returns that are comparable to those that would have been achieved through a direct investment in the related assets.

We would also expect that most funds would be structured so as not to require registration under the Investment Company Act. Again, this reflects practicalities—the rules for registered investment companies are often inconsistent with the goals of the investors and managers in pooled investment vehicles that have limited purposes. The two most frequently used exemptions for private fund formation are Sections 3(c)(1) (funds with fewer than 100 holders) and 3(c)(7) (funds selling only to qualified purchasers) of the Investment Company Act, though there are several other exemptions that might also apply, including Sections 3(c)(5)(C) and Rule 3a-7. Consideration should also be given to whether the Congress's proposed changes to the Investment Company Act, which would eliminate some of these exemptions and impose, at a minimum, registration and reporting obligations on the funds, may have a negative effect on the efficacy of the LLP.

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IX. Use of Valuation Report Data

Given the primary goal of this program—to strengthen bank's balance sheets—it seems highly desirable that valuation data should be shared with the selling bank. Although the opportunity to find "bargains" might encourage investment, there is no intention, we believe, of causing banks to sell assets at values significantly below those that an independent expert would assign to them. Similarly, if an independent valuation suggests that the selling bank is expecting an unreasonable return from the assets, that would be important information for the bank to consider both with respect to offering the assets in the PPIP and with respect to setting a reserve price or accepting or declining a bid. This may also affect whether banks will feel it necessary to mark down their assets or will continue to treat them as held to maturity.

With respect to sharing the valuation data with potential investors, the issue seems less clear. If all investors have access to this information, it may act as a limit on the likely bids and set a price for them that is lower than an investor using different methodology would have concluded to be appropriate. It may also draw in investors who will do less of their own diligence in reliance on the valuation, and while that may be advantageous for the speed and cost of the program, it will make the price discovery process less robust. Disclosure of valuations to all parties may also make it more difficult to bring valuation experts into the program, and will likely amplify their concerns about liability.

X. Documentation

We appreciate the desire to have standardized documentation, and with respect to smaller asset pools this may be critical to being able to achieve a speedy and efficient sale. However, we would encourage the FDIC to consider permitting documentation for larger asset pools and complicated assets that is tailored to pool characteristics, investor characteristics, management structure and long-term fund strategy (for instance, whether the fund is intended to be buy-and-hold or whether it is expected to pursue strategic dispositions). Fund formation is a complex discipline involving tax considerations, ERISA issues, Investment Company Act and Securities Act issues and margin regulations, in addition to more basic corporate concerns. A one-size-fits-all approach rarely fits everyone, and may decrease investor interest and depress fund economics. Purchases of distressed assets can be complex in other ways, and risks that go beyond creditworthiness, such as a pending lawsuit involving an asset, may need to be addressed in the sale documentation. Accordingly, we would encourage a flexible approach with respect to fund documentation consistent with traditional private sector approaches.. If standardized documentation is prescribed, we would encourage flexibility for investors and funds to obtain variances from the standard terms.

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We thank you for the opportunity to comment on this exciting new initiative to support our nation's financial system. Should you wish to discuss any of these matters further, please feel free to contact me at (312) 876-7700 or at ellen.marks@lw.com.

Very truly yours

Ellen L. Marks
of LATHAM & WATKINS LLP

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Ellen L. Marks, Chair
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Kevin Fingeret
Marc Hanrahan
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