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April 10, 2009

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

Re: Comments on Legacy Loan Program

Dear Mr. Feldman:

I am pleased to submit the comments of Kirkland & Ellis LLP on the recently-announced Legacy Loans Program.

Kirkland & Ellis LLP ("**Kirkland**" or "**we**") is a full service law firm of over 1500 lawyers, with six U.S. and three international offices. We represent clients in transactions, litigation, restructuring and planning matters. In particular, we have one of the top practices, both globally and in the U.S., representing private funds, including private equity, debt and hedge funds. For example, in 2008 we were ranked No. 1 in global and U.S. private equity transactions by number of deals, and we have one of the top global and U.S. fund formation practices. We are also active in the securitization of financial assets. In 2008, we were ranked sixth among U.S. law firms as issuer's counsel in asset-backed securities.

We are well qualified to comment on the Legacy Loans Program (the "**LLP**"). In our representation of private fund and securitization clients, we are routinely engaged in the purchase, sale and financing of financial assets similar to legacy loans, frequently through auctions. A number of our private fund clients have expressed to us their interest in participating in the LLP. The views expressed in this letter are ours alone, but we have the additional perspective of having discussed the LLP with a number of clients who plan to participate.

Global Comments

We applaud the FDIC for its initiative in seeking public comment on the parameters of the LLP. This process should provide the FDIC with a great deal of informed commentary on the proposals that you have released. We recognize that the FDIC is seeking to move expeditiously to make the LLP operational.

Before we address the specific questions on which you have sought comment, we have several "global" comments, which either address significant considerations that we do not believe were considered in your specific questions or that transcend several of those questions.

A. Private Investment Funds as Investors. We appreciate the FDIC's response to our question on the April 9, 2009 conference call for investors that private funds, such as private equity and hedge funds, will be eligible to participate in the LLP. In order to avoid any ambiguity on this point, we suggest that such investors be specifically identified as eligible investors, subject only to the other, general eligibility criteria. Because private equity and hedge funds are a significant source of investment capital -- some market analysts estimate that, globally, private equity funds today hold uninvested capital commitments in excess of $1 trillion -- the eligibility criteria should be carefully constructed to encourage their participation in the LLP. In addition, private funds are particularly well suited to managing and investing in a PPIF, as they present an effective means to gather and deploy investment capital from a broad pool of investors who do not have the capacity or desire to manage or control a PPIF, such as individuals, endowments and pension funds.

B. Encouraging Private Participation in PPIFs. We believe that an important goal of the LLP is to encourage as much private participation as possible. The more private participants there are, the higher the auction prices are likely to be. As we note above, there is considerable interest among private investment funds in the LLP.

However, there are at least two ways in which we believe the LLP, as currently proposed, may have a chilling effect on participation by private investment funds. The first is the potential imposition of the executive compensation restrictions of the Emergency Economic Stabilization Act ("EESA"). In the LLP FAQs, the FDIC states that the executive compensation restrictions of EESA will not apply to "passive Private Investors." That phrasing suggests that the executive compensation restrictions will be applied to "active" private investors. If such is the case, then we can say almost categorically that private investment fund sponsors will not participate in the LLP.

The second deterrent in the LLP is the potential for excessive intrusion by governmental agencies, under the rubric of "oversight," in the business of private investors. The private market has established norms for reporting and inspection rights in favor of equity investors, debt investors and debt guarantors, and we think those standards would be appropriate here. The FDIC does not need to exercise substantial oversight in this program. The PPIFs are not banks, and a level of regulation or oversight equivalent to bank regulation will not be conducive to private investor participation in the LLP.

C. Price Maximization vs. Treasury Profit Sharing. We believe that one of the goals of the LLP is to obtain the highest price possible for each asset pool. The selling financial institution will then receive the greatest amount of proceeds possible, which will have the most beneficial effect on its financial condition and will reduce the likelihood of further governmental support to that institution.

Another goal of the LLP is to provide the government with the opportunity for a significant equity return through various means. The baseline means for the Treasury to earn profits is a 50% equity investment by the Treasury in each PPIF on the same terms by which the private investors have subscribed, including the fees and incentive arrangements for asset managers. The LLP proposal, however, contains several means by which the Treasury could increase its share of the profits of a PPIF, such as the issuance to the Treasury of warrants in the PPIF, the idea floated in question 12 of providing the government with increased participation in returns above a trigger level, or the idea that the Treasury would not be charged for some or all of the asset manager's fees or incentive arrangements.[1] These additional means would give the Treasury a share of the overall profits of a PPIF that are disproportionately larger (per dollar of invested equity) than the profits that would be available for the private investors.

The two goals described above conflict with each other. If the government is entitled to take more of the profits of a PPIF for each dollar of invested equity than the private investors are entitled to receive, the result will be that the private investor will bid a lower amount. That, in turn, will reduce the overall purchase price for the pool, to the detriment of the selling financial institution -- and, indirectly perhaps, to the detriment of the government in its capacity as a provider of capital to financial institutions.

The foregoing analysis is based on the assumption that the Treasury is investing in 50% of the common equity of the PPIF. Alternatives exist for the deployment of the Treasury equity capital would, we think, result in even higher prices being bid at auctions.

For example, the Treasury could invest its funds in preferred equity issued by each PPIF, rather than in common equity. The preferred equity would have a dividend yield payable to the Treasury and a preference in the cash flow allocations of the PPIF. In consideration for its purchase of the preferred equity, the Treasury could receive a right to participate in some proportion (say, 10%) of the common equity cash flows, which would be the equivalent of a warrant. This deployment of Treasury capital would mirror the manner in which the Treasury has

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1 We also note that the LLP materials released to date recognize that PPIFs will have asset managers, but they do not make any mention of management fees or incentive arrangements being paid by a PPIF. These concepts should be addressed. We think that appropriate arrangements must be made for allocation of cash flow to managers and that those arrangements should be equally applicable to all equity investors in a PPIF -- Treasury and each private investor.

invested much of its funds in the Capital Purchase Program. It would also satisfy the EESA requirement for the issuance of warrants in a manner that is much more in keeping with its intent than issuing warrants to Treasury in addition to a 50% equity stake.

The use of Treasury funds to purchase PPIF preferred equity would provide greater protection to to the Treasury, and therefore taxpayers, than would the purchase of riskier common equity. The inclusion of the warrants would also provide taxpayers with a meaningful participation in the profits of the PPIF. Finally, we believe it would result in higher bid prices for auction pools, because it would provide enhanced leverage for the private investors.

D. The Auction Process and Deposits. It appears to us that the FDIC is contemplating that each auction of a pool of legacy loans would be a single round process in which bidders would have one opportunity to submit bids and the FDIC would select the highest bidder to purchase that property.

The use of a single round auction would be a mistake if there are a large number of bidders. It would result in lower prices and, therefore, in fewer successful auctions, assuming as we do that sellers have the right to reject auction prices that they deem inadequate. A multiple-round auction approach would be preferable to both bidders and sellers. The reason is that it is expensive to enter a bid. A bidder would, in all likelihood, want to perform significant due diligence on a pool of legacy loans prior to submitting a final, binding bid. The cost of performing the requisite level of due diligence could be significant. Bidders would not want to incur the full extent of those costs unless the number of competing bidders was sufficiently low that the bidder believed it had some reasonable chance of winning. The costs of performing due diligence on asset pools for which the bidder is unsuccessful might be labeled "dry hole costs."

A bidder who is bidding against too many other bidders would not be likely to invest much time or money in constructing that bid, for fear of incurring significant dry hole costs. Moreover, that bidder is going to assume that there are undiscovered problems in the asset pool for which it is bidding, and it is therefore very likely to bid a lower amount than it would in a situation in which it had more comfort about the quality of the asset pool. The end result, we believe, is that a single round auction process in which bidders are, in effect, assuming the worst about an asset pool will result in a lower top bid than would a multi-round auction process. In turn, that lower top bid would be less attractive to the selling institution, which might just choose to reject the bid and keep the asset pool.

We recognize that the multi-round auction process is more involved and that it takes a longer time. It may require the FDIC to retain investment bankers or other intermediaries to conduct the auctions, presumably at additional expense. But it seems to us that a multi-round process would in the end result in better informed buyers willing to pay higher purchase prices.

The requirement to make a Deposit equal to five percent of the "bid value"[2] will also deter bidders, particularly if there are a large number of bidders and a correspondingly low probability of winning. The FDIC should eliminate the Deposit requirement and instead use its bidder pre-qualification process as the basis for making a determination that bidders have the wherewithal to fund their bids. Otherwise, bidders will face the prospect of incurring significant costs, particularly if -- as we expect to be the case -- bidders are seeking to buy multiple pools at the same time.[3] Once again, the effect of this requirement, if not revised, will be to reduce the willingness of private investors to bid on asset pools.

E. Purchase and Sale Documentation; Rights of Purchasers. The materials released to date by the FDIC do not contain any information about the terms of the documentation by which asset pools will be purchased and sold. We are assuming that seller and buyer would sign some type of asset purchase agreement, and we recommend that the agreement include terms and conditions customarily found in documentation for purchases and sales of similar types of assets between private parties. We think adopting a widely accepted approach to documentation should facilitate private sector participation. In particular, the inclusion of customary seller representations and warranties regarding the asset pool being sold and any related information provided by the seller, coupled with recourse to the seller for breaches of its representations and warranties, including the ability to return non-conforming assets, should encourage investor diligence on the asset pool and result in potentially higher bids.

F. Terms of the FDIC-Guaranteed Debt. Another major feature of the LLP about which little has been said to date is the debt to be issued by each PPIF. The Legacy Loan Program Summary of Terms (the "LLP Term Sheet"), in the section headed "Non-Recourse Debt," contains a few terms.

In addition, the last bullet point in the "Non-Recourse Debt" section references a Debt Service Coverage Account and the concept of "working capital" at the PPIF. That sort of terminology is typical of a debt obligation of an ongoing operating business, where the ability of

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2 The term "bid value" is undefined. We assume this means the amount of private investor equity that the bidder would propose to inject into the PPIF, rather than meaning the total auction price of the asset pool.

3 The LLP Term Sheet states that Deposits will be returned to unsuccessful bidders "subject to their adherence to material terms of the auction procedures." We do not understand what this phrase means, and we believe that -- without clarification -- it will cause significant concern to bidders. The possibility of forfeiture of deposits for non-compliance with auction procedures, when those auction procedures are presently unknown and could ultimately be quite intricate or cumbersome, is cause for concern. The FDIC should drop this concept or to narrow it substantially to apply only to breaches involving egregious conduct.

the issuer to repay the debt is analyzed using balance sheet and income statement precepts. We believe that a better model to use in this circumstance is an amortizing securitization or a cash flow collateralized loan obligation, in which the expected cash flow from a liquidating pool of assets is analyzed to determine the ability to repay the debt.

We understand from comments made on the April 9, 2009 conference call for investors that the FDIC understands it must provide greater clarity on the terms of the debt prior to the time that bids are submitted in auctions. It is essential that the FDIC take this step. However, the FDIC should not dictate precisely the terms of the debt to be issued by a PPIF; doing so is likely to result in suboptimal structuring and in lower auction prices.

We suggest that the FDIC specify the particular parameters under which the FDIC will guarantee the debt of a PPIF. The bidder would then be permitted to structure a debt instrument that best suits the bidder's evaluation of the pool, so long as it meets the FDIC's specifications. As an adjunct to the specification of such parameters, in any auction the FDIC, the seller and the financial intermediary representing the seller could design a "stapled" debt instrument that the financial intermediary would stand ready to underwrite for the winning bidder. Each bidder would then have the choice of either accepting the stapled debt security or designing its own debt security within the FDIC's standing parameters.

True Sales. We think it will be important to buyers to know that the sale of each asset pool by a selling bank is a true sale that would not be recharacterized in the event of a subsequent insolvency of the selling bank. At this stage, we do not have enough information to conclude definitively whether or not it would be possible for law firms to give true sale opinions in these transactions. As a means of saving participants from incurring the expense of a true sale opinion in each transaction, the FDIC should consider some type of program term or other regulatory action that would definitively establish that the sales would be considered true sales.

Responses to FDIC Questions

In addition to the global concerns that we express above, we have responses to a number of the questions posed by the FDIC in its request for comments. These are set forth below following each of the FDIC's questions.

2. *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?*

Initially, it is important to identify the meaning of the term "investor" in answering this question. We think that each PPIF will have just one private investor, which will be the winning bidder.[4] If that winning bidder is a private investment fund, then it will have a number of passive investors such as pension funds, endowments, insurance companies and individuals as its limited partners. Those passive investors in the private fund would not be direct investors in the PPIF.

The ownership of the PPIF should be transferable by the private investor. The FDIC should publish non-discretionary criteria for investor eligibility that would enable investors to determine on their own whether they are eligible. If, however, the FDIC intends to retain discretion over which investors are permitted to participate, then the FDIC should institute a process under which investors are "pre-qualified" for participation in the LLP across the board -- not just for the initial purchase of interests in a particular PPIF. In that case, the selling investor would be able to transfer its interest in a PPIF to any other qualified investor.

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?*

The FDIC has proposed that Treasury will purchase "up to" 50% of the equity of a PPIF, and, in accordance with EESA, receive warrants, the terms and conditions of which are not spelled out. If the goal is to maximize the efficiency of the auction process, bidders will need to know in advance the entire capital structure -- including equity -- of the PPIF, to enable them to model their expected returns. Therefore, it is essential that the terms and conditions of Treasury equity securities and warrants, if any, be clearly established in advance of any auction.

In addition, it is not clear that the EESA -- specifically Section 113(d) -- actually requires Treasury to receive warrants in connection with its investment in a PPIF. Section 113(d) was enacted to provide for "reasonable participation" by Treasury, on behalf of U.S. taxpayers, in any equity appreciation of a troubled asset, and to protect against losses that may arise out of the sale of a troubled asset. We presume that Treasury's "up to" 50% equity interest in the PPIF would

4 As you will see in our answer to question 6, we do not believe that it is a good idea to permit potential investors to bid for minority ownership positions in PPIFs.

include a right to participate in the common "upside", making an additional warrant superfluous. Furthermore, there are better ways to mitigate the risk that Treasury will lose its equity investment in a PPIF -- for example, by giving Treasury a preferred interest -- than diluting the common equity interest of its private partners. As we note in our global comment C, we think the structure that would produce the highest auction prices would be for the Treasury to purchase a preferred equity interest in each PPIF and receive the equivalent of a warrant entitling it to a percentage of the common equity returns.

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

We believe that publication of the identity of the entity that wins the bidding to invest in a PPIF is acceptable. We note, though, that many of those entities are likely to be limited partnerships or other investment vehicles in which there is a managing partner and a number of passive investors. The passive investors will be the type of investors that frequently participate in private investment funds, such as government and private pension funds, endowments, high net worth individuals and offshore investors. We do not believe there is any reason to require publication of the identities of these passive investors. However, we believe that identification of the managing partner of the winning bidder would be expected and acceptable.

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?*

We have described in this letter many ways in which we believe the participation of private investment funds in the LLP can be enhanced. By adopting our suggestions, the FDIC would be likely to see substantial participation by private investment funds.

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 auction process that auctions both minority interests and controlling interests to bidders at the same time is unlikely to facilitate participation. First, virtually all minority investors would want to know the identity of the controlling party before bidding. Second, most controlling parties would want to know the identity of the minority investors before bidding. In the absence of this information, the amounts of their respective bids might well be reduced.

Finally, it is unlikely that potential minority investors would want to expend the resources necessary to investigate asset pools and participate in auctions.

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?*

As we indicate in our global comment F, the parameters under which the FDIC will guarantee the debt instruments need to be well-defined prior to the commencement of an auction. The bidder will then be able to specify the precise terms of the debt that best suit the particular asset pool for which it is bidding.

Following are a list of the debt features that we think the FDIC should specify:

- the guarantee fee and the schedule for payment of that fee
- the minimum requirements, if any, that the FDIC will impose for principal repayment
- the final maturity of the debt
- the restrictive covenants that the FDIC would require
- the level of servicing fees permitted

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?*

We believe that a risk-based fee would be acceptable to private investors, if the FDIC can establish an appropriate methodology for quantifying risk.

We think there are two key issues for private investment funds. The first is that the investor will want to know, in advance of bidding, exactly what fee the FDIC proposes to charge for its guarantee of the debt related to the particular asset pool. We note, consistent with earlier comments in this letter, that there is a tradeoff between the level of the fee and the level of the bids that private investors will submit. If the fee is high, then less cash flow will ultimately be available to be returned to the private investors; in that case, the amount that the investor will bid will be lower. Conversely, a lower FDIC fee will result in higher bid amounts.

The second issue is that private investors will need to have a strong level of assurance that the fee will not change over the life of the transaction. If investors perceive a risk that the fee could increase in later years, then they will again be likely to bid lower amounts to protect against that risk.

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?*

We see no justification for the government to increase its participation in investment returns that exceed a specified trigger level. If the government invests in 50% of the common equity, it should receive the same returns that accrue to the private investor that puts in the other 50%. Further participation would simply be confiscatory. Indeed, the mere possibility that such an action might occur will have a chilling effect on the willingness of private investment funds to participate.

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?*

We believe that the selection of asset managers for the LLP should be based on objective published criteria that allow asset managers to gather commitments from a variety of investors and be prepared to bid on appropriate PPIF interests. A pre-qualification process may be advisable to provide managers with certainty that they will be treated as a qualified bidder in the auctions. Asset managers should not be limited to entities that are registered investment advisers or other regulated entities, in order to encourage a greater number of bidders that meet appropriate objective qualifications.

As we note in global comment B above, we believe that existing private-market informational and reporting rights will adequately protect the interests of the FDIC and the Treasury in a PPIF, including its lenders and private investors. While some FDIC oversight is appropriate, many asset managers will find being regulated like a bank unattractive and will not participate.

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?*

Any bidder who wishes to acquire an asset pool will want to control the servicing rights of that pool. We see no benefit to an approach that would involve a separate award by the FDIC or the seller of the servicing rights. Such an approach will simply be a disincentive to private investor participation. Each bid should indicate a single amount that reflects ownership of the assets and control of the servicing; the relative values of the components should not be separately included.

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We very much appreciate the opportunity to comment on the FDIC's proposals. Please do not hesitate to contact the undersigned if you would like to discuss any aspect of these comments.

Sincerely,

Kenneth P. Morrison by [illegible]

Kenneth P. Morrison, P.C.

KPM