Richard Keck
Partner
Duane Morris LLP
1540 Broadway
NY, NY 10036

212.692.1056

rkeck@duanemorris.com

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

Re: Comments of Flat Earth Capital LLC on Legacy Loan Program (LLP)

The undersigned serves as counsel for Flat Earth Capital LLC, which is actively considering participating as a private sector investor in the LLP. We hereby submits the following comments on Flat Earth's behalf:

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?**

   Flat Earth is primarily interested in residential mortgages, but would consider other relevant assets.

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?**

   As a general matter, the more strings that are attached to the investments, the less interest there will be in investing. Negative pledges and restrictions on alienability will be negatively received by the investment community.

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 government's increased equity participation in PPIFs is a positive to the extent it increases the leverage of private investors, but is a negative to the extent it precludes or limits the ability of private investors to direct servicing activities and other decisions impacting the value and performance of the loan portfolio. Flat Earth believes that one of the ways that the private sector can add value is by initiating steps to improve loan performance, such as contacting borrowers and voluntarily recalibrating their loan terms (including principal balance and/or interest rate) to a rate that optimizes the tradeoffs between enabling and encouraging borrowers to remain current on their loans while preserving the maximum percentage of the face value of cash loan.

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

Yes. Investors typically have expectations of privacy in their investment decisions. Requiring them to forfeit those privacy interests as a condition to investing in the PPIFs is likely to discourage some investors and make it more difficult and costly to raise the necessary private equity for PPIFs. As a co-investor, the government may have an interest in knowing the identity of the investors. However, absent a compelling public policy reason to disclose investor names publicly, they should be held in confidence by the government. The recent experience over bonus payments suggests that some groups or individuals may seek to intimidate private investors in PPIFs, particularly if the investments ultimately yield significant returns, and therefore maintaining their privacy is important in deterring this type of activity and in protecting investor safety.

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?**

Investors will be attracted by the opportunity to earn attractive returns on their investment. While the anticipated arbitrage on valuations and leverage both contribute to the potential attractiveness of an investment in a PPIF, perhaps the most important factor will be allowing the private investors sufficient latitude to direct the business decisions of the PPIF (see answer 3 above) so that they can actively influence the value of their investment.

It is unclear from the information published by the FDIC so far whether the private investments in the PPIFs are intended to be passive or active. To the extent they are meant to be passive, we believe this will depress investment demand and that the government will be passing up the opportunity to harness the creative and hardworking energies of the private sector to help turn around the values of the portfolio assets for the benefit of the taxpayer as well as the private investment community. Formulaic servicers running on autopilot do not have the same vested interest in performance as the investors.

Flat Earth therefore strongly recommends that the government design the LLP in such a way as to give private investors as much control over the PPIFs as possible consistent with protecting the interests of the government as an investor and lender. As a potential investor and not a potential seller, Flat Earth is not in a position to speak to how best to motivate the sellers.

Private investors should also be permitted to form the entities that will serve as the private equity investor/manager of each PPIF in which those investors participate and, subject to any parameters on governance and capitalization, be permitted to prepare the internal documentation for the PPIFs. Each such private investor bidding team, which must prequalify with the FDIC in order to be permitted to bid, would then only form individual PPIFs as and when they are successful in an individual bid. As needed, each PPIF would be formed and funded according to the agreed documentation following the auction and at or before the closing to the purchased This is a more typical process for any competitive bidding situation where private money will be invested.

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?

The question is framed in such a way as to suggest that private investors are only buying minority stakes in PPIFs alongside other private investors. No indication is given as to who among those would manage the PPIFs, and private investors will not want third-party institutional fund managers who will not be in a position to dynamically manage the underlying loans in the portfolio.

Flat Earth believes this approach would be suboptimal and significantly reduce both investor interest and bid amounts. Investors will not want to bid on something they cannot control, particularly given that part of the perceived latent value can only be unlocked by effective and proactive management of the portfolio assets. Instead, loan portfolios should be sold in lots that are sized to sell to a single purchaser (each of which will be set up as a separate "PPIF" backed by a single private investor or investor consortium). Having multiple investors in the same PPIF with no clear center of control makes pricing of bids difficult and will lower values.

For the reasons offered in earlier answers, Flat Earth believes both the government and the private investors would be better off if each purchasing entity (which we would take to be a distinct PPIF) were controlled by a separate private sector management team. The PPIF could prequalify and then participate in bidding based on its committed private equity and the matching government equity and loans based on the prequalification and program criteria. A successful bidder would then, within a short time after the auction, close on its funding and its acquisition of the portfolio to be purchased, perhaps simultaneously. PPIFs would not otherwise need to be funded unless or until they succeed in bidding for any portfolio. The same management team and/or investors could participate in multiple PPIFs that can bid in successive auctions.

Flat Earth recommends that the government consider conducting an absolute auction in multiple rounds of open bidding, either electronically or by other method. Ground rules for sellers should also be set, such as making it an absolute auction subject to any pre-specified reserve. Otherwise, sellers can back out after having caused investors and the government to have expended tremendous amounts of time, energy and money unnecessarily.

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

Flat Earth will be most interested in asset pools that offer opportunity for value remediation through management of servicing and potential liquidation in the future prior to maturity after the markets have stabilized and value has improved. Conforming residential mortgages would be first choice. Nonconforming residential first mortgages would be second choice. And other more esoteric asset pools would be third choice.

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

Optimal size might be on the order of $100 million to $300 million. Other optimal characteristics would include some homogeneity of attributes such as average loan size, maturity date, etc.

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?**

Flat Earth is not sure what is meant by the "note" in this question. Investors will want full, transparent and accurate disclosure of all information known and the opportunity to conduct their own due diligence on loan portfolios subject to auction. The terms of the guaranteed debt portion of the PPIF's funding must also be known at the time private investors price their participation and bid for the assets to be purchased.

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?**

    Private investors will not care who the lender is. They will primarily be looking for bankability (which the FDIC guarantee will go a long way in ensuring) and a reasonable, predictable cost of their financing. Private investors in the PPIF will also want to know whether the PPIF's debt structure creates any payment penalties or other additional operating costs or otherwise constrains the operation of the PPIF under investor and management control. Assuming seller financing can satisfy "true sale" and other accounting and regulatory requirements to achieve the agreed aims, having the selling institution take back a note from the PPIF may be the simplest, and therefore least expensive, approach from a due diligence standpoint as the selling institution already has credit risk on the relevant asset pool.

    Public issuance of debt to fund the purchase would increase transaction closing costs as well as operating costs for the PPIF and should be avoided if possible.

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?**

    First and foremost, the guarantee fee should be fixed and knowable prior to investor bidding on the loan portfolio so that its cost can be taken into account in the bidding. Subject to this caveat, Flat Earth has no particular view on how it should be calculated. Presumably the seller will as this will impact the bid amounts. The more the fee reflects the risk profile, the more in line the pricing is with reality and the fairer it is. However, there are diminishing returns for increasing granularity and this may also result in rate uncertainty, which will be viewed negatively by investors.

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?**

    This is a curious and counterintuitive suggestion. Assuming the private investors are given sufficient control over management of the portfolio, then one would think that any extraordinary returns would be generated by their skill and success in managing the value remediation of the portfolio. Flat Earth therefore would have thought that the percentage participation by the private investors would increase above a certain specified level. In other words, it would be like the government having preferred stock and the private investors having common stock. The preferred stock can be redeemed at a certain specified price and all additional value growth goes to the common shareholders. In addition, as the private sector entrepreneurs will not only be taking the risk, but also adding the value of managerial expertise, their reward should be greater if and to the extent base level expectations are exceeded.

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?**

Yes, provided that the bidding PPIFs would not have to be concerned with the allocation between the participating banks and would simply pay the winning bid amount for the entire pool of assets. To the extent the assets sold would be subject to any representations and warranties, such as title to the loans, pooled sales may raise some additional transactional complexities. Nevertheless, the approach may be preferable to the extent necessary to assemble optimally sized portfolios.

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?

One area of potential conflicts is in the auction process. Absent appropriate ground rules, there is the potential for seller's to back out, frustrating investors and causing them to lose interest in future auctions. There is also the matter of what assurances the seller will give the purchaser. Certainly title to the assets (i.e. the seller owns loan A with the right to sell it to purchaser free and clear) and possibly other matters (depending on the scope and depth of due diligence purchasers are permitted to conduct ahead of time) should be covered by some sort of representations and warranties that survive the sale.

Another area of potential conflicts is in the funding and governance of the PPIFs. As envisioned by Flat Earth, each PPIF would have a three buckets on the liabilities side of its balance sheet: (1) FDIC guaranteed debt; (2) government owned equity; and (3) private investor owned equity. The terms of the FDIC guarantee would need to be known in advance to minimize conflicts arising from this. The lender of the debt guaranteed, whether or not it is also the seller, will need to negotiate the loan documents with the PPIF. Probably represented by the private investors. The government euqity and private investor equity terms will need to be defined. One question is whether there will be standard documentation or whether the private investors can put different offers on the table for the government to consider. What are the parameters under which the government will get its money back.

Though couched as equity, the government investment may be treated by the government as more like debt in that it will be looking to get all its money back with some return, but generally no more and no less. Private investors, on the other hand, will recognize the nontrivial chance that they lose money and will be expecting to make an above normal return if things go well to compensate them for the risk that they would not. There is some possibility of public backlash against private investors who ultimately do well so the documentation will need to be clearly defined and give appropriate assurances of no claw-backs, excess profits taxes or other devices will be used to try to recover some of the earnings of the private investor.

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 would have thought that investors would arrive with their own designated asset managers and that would be part of the package. They can be prequalified by the government prior to bidding, and then any winning bidder would take control of the relevant PPIF subject to the creditor's rights of the lender and FDIC and the supermajority voting rights of the government as the passive equity partner. This approach is likely to make the best use of the private sector talents and get the best priced investment from the government's perspective.

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?

The PPIF should acquire the right to direct the servicing of the loan portfolio. To the extent the existing servicer has vested contractual rights, the purchasers will be able to evaluate the performance of the servicer and its contract rights and duties as part of due diligence on the portfolio. After the acquisition, the PPIF can take whatever steps it desires or needs to take with respect to the service, such as firing them, continuing to use them under the existing contract, or renegotiating the contract. To the extent any of these options will require payment of a breakup or other fee to the servicer, the purchaser can anticipate that fact and take it into account in valuing the portfolio in the auction.

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?

Flat Earth believes that more information will improve liquidity and result in auction prices that are closer to actual value. It is less concerned with a particular firm's opinion on value and more on access to the underlying portfolio information on which an opinion on value can be based.

18. Other questions and comments.

a. Flat Earth recommends that the government permit PPIFs to be established by the private investors rather than by the FDIC, the UST or other government department. Once scenario for how to do this was set forth above in answer 5. Flat Earth recommends that the PPIFs be allowed maximum flexibility as to type of entity and jurisdiction of formation.

b. Flat Earth recommends that there be no limit on the number of qualifying PPIFs. A particular group of investors and management team should be permitted to structure their investments into multiple PPIFs in order to optimize the size of each investment vehicle. There should also be a streamlined process for approval of subsequent PPIFs involving the same management team and investors.

c. There should be standardized corporate governance and other documentation for the PPIFs to protect the interests of the FDIC and UST, but this should not undermine the ability of the private investors to direct day to day decisions but rather should only constrain fundamental decisions to approval by the government stakeholders.

d. There should also be standardized capital structure terms and documentation for the PPIFs to reflect the rights and obligations of the equity holders, including the UST equity and warrants, rather than leaving this to be individually negotiated between the UST and each PPIF. This will increase transparency, level the playing field and improve transaction efficiency. The terms of documents should be developed by the government trough prior public consultation.

e. Qualification criteria for PPIFs (or the management investor groups that will serve as managers) should be objective and transparent rather than being evaluated subjectively by the UST and FDIC. The criteria should be published for public consultation prior to being made final.

f. Any qualification criteria imposed on the private investors in the PPIFs (other than those of general applicability under the federal and state securities laws) should be kept to a minimum. The selection criteria should primarily be imposed on the vehicles and management team. The potential of foreign investors to participate should be clarified.

g. Please publish the proposed timeline for answering these questions and getting the program underway.

Respectfully submitted,

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Richard Keck