Legacy Loans Program – Program Description and Request for Comments

The Treasury and the FDIC recently announced that they will establish the Legacy Loans Program (LLP) to remove troubled loans and other assets from banks. This program is necessary because uncertainty about the value of these assets makes it difficult for banks to raise capital and secure stable funding to support lending to households and businesses. All FDIC-insured depository institutions will be eligible to participate in the program.

While the idea of having the government purchase loans and other assets from banks has been proposed before, the problem of determining a fair price for the assets has prevented the idea from moving forward. The concern has been that a price set by the government might result in overpaying for the assets.

To address this concern, the Treasury will join with private investors to purchase these assets. This combination uses the expertise of the private sector and discipline from the financial markets to determine a market-based price for loans and other assets that have been hard to value.

The vehicle for purchasing assets from a bank will be Public-Private Investment Funds (PPIFs). Private investors will bid for the opportunity to contribute up to 50 percent of the equity for the PPIF. The winning bid for this equity share will set the implied value of the equity share held by the Treasury. With proposed financing guaranteed by the FDIC, this will define the overall price offered to the selling bank.

Because the government will be in partnership with private investors, the government will share in any profits. If private parties profit from their investment, as they expect to, the Treasury will also. At the same time, the Treasury will only suffer losses if the private investors do.

Credit markets have not functioned well recently because of a lack of financing for certain assets. To address this, a PPIF will be able to issue FDIC-guaranteed debt. For providing the guarantee, the FDIC will be paid a fee, a portion of which will be allocated to the Deposit Insurance Fund. The FDIC will be protected against losses by the equity in the pool, the newly established value of the pool's assets, and the fees collected.

This program will be coordinated with the other components of the financial recovery package to clean up bank balance sheets so that banks can once again provide the lending to further the recovery of the U.S. economy.

II. Request for Comment

The FDIC is requesting comment from interested parties on all aspects of the proposed LLP. In particular it has formulated the following questions for interested parties to consider:

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?

Initial focus on legacy real estate 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?

Yes! To pre-qualified investors… same 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?

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

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?

Offer tranches of properties in various sizes… from 20 properties to 50 properties per bundle. Keep the size reasonable so that individuals and smaller businesses can participate!

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?

Once again, this is dependent on the size of the PPIF… offer scaled options on bundles from smaller to larger numbers of properties. Asset management must be in designated skilled hands, this is not a good business for unqualified amateurs.

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

By definition these assets are in default… Bundles can be made of 20 to 50 residential properties, or 10-20 commercial properties where properties have mixed potentials for possible re-finance, short sales, and defaults.

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

20 to 50 residential properties per 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?

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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?

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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?

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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?

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?

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?

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?

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?

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?

Comments on the LPP may be submitted until April 10, 2009.You may submit comments by any of the following methods:E-mail: LLPComments@FDIC.gov. Include "Legacy Loans Program" in the subject line of the message.

- Mail: Robert E. Feldman, Executive Secretary, Attention: Comments, Federal Deposit Insurance Corporation, 550 17th Street, NW., Washington, DC 20429.
- Hand Delivery/Courier: Guard station at the rear of the 550 17th Street Building (located on F Street) on business days between 7 a.m. and 5 p.m. (EDT).

Public Inspection: Please note that all comments will be posted generally without change (including any personal information) to the FDIC's website http://www.fdic.gov/llp/index.html). Paper copies of public comments may be ordered from the Public Information Center by telephone at (877) 275-3342 or (703) 562-2200.