From: Ross Brown [mailto:rbrown@coastoakgroup.com]
Sent: Wednesday, April 08, 2009 7:01 PM
To: LLPComments
Subject: Legacy Loans Program

The following responses are submitted by an investment management and development firm with interest in participating in the PPIP/LLP. Our firm's expertise is focused on residential land development, but our principals have extensive experience as investors in all commercial real estate product types. During the 1990s our principals were affiliated with some of the largest real estate opportunity funds that acquired significant amounts of distressed debt in the US and Asia.

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?* In addition to real estate loans, many banks have commercial & industrial loan exposure that is also opaque and potentially subject to significant losses.

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?* Transfers of non-controlling equity interests (including profits interests) to asset management entities that are actively involved in maximizing performance of the assets should be permitted in order to provide incentive for management activities that maximize value. Admission of additional equity participants, or transfers or sales of equity interests, to obtain additional equity capital for asset improvements or value preservation / maximization (i.e. without any distributions to the investors) should also be permitted with FDIC approval of any change in control.

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?* In order to balance the goals of (a) stretching both public and private equity capital sufficiently so that available capital is sufficient for the volume of distressed assets, (b) providing a competitive process to enable fair prices for selling institutions and (c) providing an adequate dollar-profits incentive for private investors to expend resources to participate in the process, the auctions should allow for bids based on a range of Treasury participation from 20% to 50% of PPIF equity. The highest bid may come from an investor that requires larger dollar profits from each investment based on the investor's large availability of capital relative to limited human resources, so that such an investor would elect to forego bidding if Treasury's share were higher than 20%. Alternatively, the highest bid may come from an investor with capital constraints that would preclude participation if the Treasury were unwilling to provide 50% of the equity. Flexibility in the amount of Treasury equity becomes more critical as the transaction size becomes smaller, and this consideration relates to question

6 below. If the selling financial institution desires to participate in the PPIF equity, this option should be provided by reducing the Treasury's equity stake, maintaining the option for the private investor to accept between 20% and 50% co-investment equity from a combination of Treasury and the selling institution. The provisions regarding Treasury receiving warrants need to be implemented in a way whereby the warrants are an automatic part of the 20 to 50% participation.

4. *Is there any reason that investors' identities should not be made publicly available?* While full public transparency of investors' identities may seem fair and logical to enhance the public's trust and comfort with the PPIP process, public disclosure may discourage and in many cases prevent some potential investors (such as those with strict confidentiality requirements) from participating in the PPIP process. While full disclosure of each of the participants must be made to the Treasury to ensure compliance with various Federal regulations and OFAC compliance, investors should be able to participate without concerns of public disclosure.

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?* Broad participation from investors with either significant equity capital or operating expertise is critical to maximizing price. The most critical factor in obtaining investor participation is certainty that the assets will sell for the market clearing price, so any reserve price should be disclosed up front. An appropriate timeframe and process for due diligence and closing, dependent upon the nature of the collateral for the loans being auctioned, is critical to allowing maximum participation and closing success. For commercial real estate loans in particular, incremental risk created by a limited due diligence process and closing period will likely result in a lower price. Reliable closing and pricing based on multiple informed bids is the best motivation for sellers. If closing is expected shortly after bids are awarded, the program should feature a post-closing due diligence period for commercial real estate loans where assets are less granular and due diligence is very expensive. Strong representations should be provided in order to encourage participation and maximize price because the reps are a risk allocation mechanism and the selling institution, and therefore the FDIC, already holds the risks associated with the loans and assets. Because the selling institution may not be a creditworthy counterparty in the view of investors, the FDIC should consider guaranteeing the seller's obligations under representations and post-closing due diligence matters or else provide for a meaningful portion of the purchase price to be escrowed during the due diligence period.

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?* To maximize investor participation and closing certainty and to avoid inter-investor control issues, all of the investor equity in each PPIF should be awarded to one bidder, particularly for commercial real estate loans where assets

are less granular and decisions on loan resolution and collateral disposition are more individualized rather than programmatic. For larger portfolios, syndication of the equity in a process controlled by the winning bidder should be permitted prior to closing. Portfolios could be divided into a small number of logical sub-portfolios for which different PPIFs could be formed to allow separate bidding on these sub-portfolios as well as for the whole, but the number of sub-portfolios should be very small, generally no more than two or three, to maximize closing success and to avoid discouraging investor participation. For commercial real estate in particular, Dutch auctions would likely result in many investors electing to forego participation when the collateral varies so widely and in distressed situations where resolution strategies may have a significant impact on valuation and actual performance.

7. *What priorities (i.e., types of assets) should the FDIC consider in deciding which pools to set for the initial PPIF auctions?* Provided sufficient equity capital is made available to the selling institution, priority should be given to the loans that are most opaque and troublesome for investors considering the provision of capital to banks. These loans would include residential land / homebuilding commercial real estate loans.

8. *What are the optimal size and characteristics of a pool for a PPIF?* This response is focused exclusively on commercial real estate ("CRE") loans, which have very different characteristics and require a different process versus residential mortgages. The amount of distressed CRE assets needing to be cleansed through this process requires participation by very large investors in order for a sufficient impact to be generated by the program. Assuming the Legacy Loans Program is intended to utilize half of Treasury's $75 to $100 billion, 25% of this equity is intended to solve legacy CRE loans, and the average FDIC-guaranteed leverage for these CRE positions is 3:1, the goal of the program is to transact $75 to $100 billion of aggregate purchase price in CRE assets. Assuming a purchase price of 30% to 50% of principal balance and a two-year period for loan sales, the principal-balance volume of loan sales needs to meet or exceed $6 to $14 billion PER MONTH. Administering this volume absolutely requires consolidation into very large pools, generally with a principal balance of $5 billion or more. Success of the program requires $10 to $12.5 billion of private equity capital over a relatively short period for large CRE transactions (in addition to 3X this amount for residential mortgages) in an environment where large fund sponsors consider uninvested capital to be a precious resource and where other future investment opportunities are expected to be plentiful. Therefore, the program should be designed to encourage the private investors in CRE transactions to quickly re-sell a portion of the pools and monetize a small profit in order to redeploy capital into subsequent LLP opportunities. Smaller investors would have the opportunity to participate indirectly by purchasing from the PPIFs after the initial transaction closes, and the private investors will be motivated and incentivized to quickly trade smaller components in order to efficiently manage the larger elements and recycle capital. Allowing the FDIC guarantee on CRE positions to be transferable with FDIC approval of the subsequent purchaser would greatly facilitate this process. Optimal characteristics involve a consistent collateral type to maximize

interest from investors with varying degrees of appetite for different products. For example, separating a pool composed of loans secured by retail centers and loans secured by residential land developments into two separate pools would allow investors that desire both to bid on both, but allow investors that wish to avoid one or the other to bid on only one.

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?* Assuming this question refers to the FDIC-guaranteed leverage, the following terms need to be disclosed to all bidders at the inception of the process: (a) leverage ratio, expressed as a percentage of the total price or as a multiple of total equity; (b) interest rate, fixed or floating; (c) principal repayment / amortization terms and requirements; (d) interest reserve requirements; (e) guaranty fee; (f) maturity and extension options; (g) covenants.

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?* The note should be issued to the selling institution, which could then sell or hypothecate with the FDIC guarantee in place. Public debt issuance carries significant costs that would ultimately be borne by the selling institution in the form of lower prices for the loan pool, so the selling institution should control the process if they desire additional cash. In addition, requiring the PPIF to issue debt publicly would result in a longer required period between selecting the winning bidder and closing the transaction.

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?* If the public policy goal is to provide assistance in dispositions of toxic assets with reduced losses versus a non-subsidized process, thereby encouraging sellers to participate and avoiding additional bank failures, the guarantee fee should be relatively low. Adjustments for varying risk characteristics merely serve to decrease the price and discourage participation for the most toxic positions.

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?* If the goal is to maximize participation of selling institutions by providing a moderate subsidy to increase auction prices, providing enhanced returns to the Treasury's equity above a threshold is absolutely not appropriate. In fact, for commercial real estate loans and REO in particular, private investors would generally seek a structure whereby the controlling investor or manager achieves enhanced returns above a target level (not the other way around) in order to incentivize performance on distressed assets where management execution is critical. If Treasury elects to demand a disproportionate return above certain targets, private investors would underwrite and bid a lower price. Some investors would find this

alternative very appealing because the lower price would decrease their downside risk and they would still be able to generate a satisfactory return, albeit with less upside. However, this outcome would increase the losses that selling institutions are required to sustain in order to sell assets and thereby discourage participation in the program.

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?* The program should permit multiple selling banks to pool assets that are collateralized by similar product types in similar locations to provide for greater efficiency. In such circumstances, the bidders could be required to provide asset-by-asset allocations of their bids, and the allocation from the winning bidder would be used to allocate the proceeds. However, institutions should not be able to pull assets in order to reverse cherry pick because the potential for that activity would significantly discourage investor participation and pricing, undermining the basic goals of the program. Selling institutions could be subject to group voting rights as to whether to accept or reject the bid in total, or minimum bids for individual institutions' positions should be disclosed to investors prior to the auction.

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?* If auctions are managed in a way whereby investors could be asked to participate in arranged marriages with other investors, the potential for failures and conflict with respect to control and asset strategy is likely fatal. If one winner is declared for each PPIF and that investor is permitted to syndicate equity with FDIC approval, then conflicts can be managed.

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?* Investors will have significantly less interest in the program without full control of asset management selection and decision-making. The FDIC should have basic approval of the qualifications of the asset management service providers selected by the investor but not over ongoing decisions. The government's interest as an equity investor is protected by the alignment of interest with the private investor and the FDIC's selection of the appropriate amount of leverage. For commercial real estate in particular, the interest alignment would be enhanced if the private investor or manager were allocated an increased share of profits above target returns, which would provide additional incentive for performance on distressed assets where execution is critical.

16. *How should on-going servicing requirements of underlying assets be sold to a PPIF and paid for? Should value be separately attributed to control of the servicing rights?* Servicing should follow the loans and the PPIF could then separately sell servicing rights if the investor deems this appropriate. This process ensures that servicing rights with value are bid for along with the loans and that any severing

of these rights from control of the loan does not discourage investor participation 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?* More information on these types of distressed assets will result in higher bids. All available information should be shared with potential bidders. This information should also be made available to selling institutions in order to avoid situations where auctions fail to achieve minimum prices.