

Public-Private Investment Program (PPIP) – July Update

The Treasury Department (“Treasury”), the Federal Reserve (the “Fed”), and the FDIC first announced details regarding the Public-Private Investment Program (the “PPIP”) on March 23, 2009 (the “March 23 announcement”). The March 23 announcement described the PPIP as part of the Treasury’s ongoing effort to improve the stability and functioning of the financial system and to spur lending and the flow of credit.¹ The PPIP is targeted at “legacy assets,” predominantly comprised of residential and commercial mortgage loans held directly on the books of banks and securities backed by portfolios of residential and commercial mortgage loans (“Legacy Securities”).

Treasury, the Fed and the FDIC provided additional information on July 8, 2009 regarding the government’s recent progress toward implementation of the PPIP (the “July 8 announcement”). This issue of Dechert OnPoint discusses (i) the updates to the Legacy Securities Public-Private Investment Program (the “Legacy Securities Program”) and Legacy Loans Public-Private Investment Program (the “Legacy Loans Program”) contained in the July 8 announcement, (ii) the proposed Conflict of Interest Rules and Ethical Guidelines (the “Rules”), and (iii) the proposed terms and conditions of the to-be-formed public-private investment funds (“PPIFs”).

Legacy Securities Program Update

The July 8 announcement reviewed Treasury’s plans to invest up to \$30 billion of equity and debt in PPIFs established by private sector fund managers and private investors for the purpose of purchasing Legacy Securities. Through the Legacy Securities Program, the Treasury will partner with leading investment management firms in a manner that increases the flow of private capital into markets for legacy assets while maintaining equity “upside” for U.S. taxpayers. Each PPIF fund manager will receive an equal allocation of funds from Treasury.

Selection of Fund Managers

Treasury began a comprehensive two-month application evaluation process on May 15, 2009 to select the fund managers that will establish and manage the PPIFs. Treasury evaluated applications for fund managers according to established criteria, including: (i) demonstrated capacity to raise at least \$500 million of private capital; (ii) demonstrated experience investing in Legacy Securities, including through performance track records; (iii) a minimum of \$10 billion (market value) of Legacy Securities under management; (iv) demonstrated operational capacity to manage the Legacy Securities PPIP funds in a manner consistent with Treasury’s stated Investment Objective while also protecting taxpayers; and (iv) headquartered in the United States. In order to encourage participation by both small and large firms, these criteria were evaluated on a holistic basis and failure to meet any one criterion did not necessarily disqualify an application.

¹ For additional information on PPIP, see the issue of Dechert OnPoint related to PPIP, available at: http://www.dechert.com/library/Finance_and_Real_Estate_04-09_17_An_Analysis_of_the_Department_of_Treasury.pdf

Following a review of over 100 applications, Treasury pre-qualified the following firms to participate as fund managers:

- AllianceBernstein, LP and its sub-advisors Greenfield Partners, LLC and Rialto Capital Management, LLC;
- Angelo, Gordon & Co., L.P. and GE Capital Real Estate;
- BlackRock, Inc.;
- Invesco Ltd.;
- Marathon Asset Management, L.P.;
- Oaktree Capital Management, L.P.;
- RLJ Western Asset Management, L.P.;
- The TCW Group, Inc.; and
- Wellington Management Company, LLP.

Collectively, the nine pre-qualified fund managers have established 10 unique relationships with leading small-, veteran-, minority-, and women-owned financial services businesses to assist with asset management, capital raising, broker-dealer, investment sourcing, research, advisory, cash management and fund administration services. Set forth below is a list of the pre-qualified small-, veteran-, minority-, and women-owned businesses partnerships:

- Advent Capital Management, LLC;
- Altura Capital Group LLC;
- Arctic Slope Regional Corporation;
- Atlanta Life Financial Group, through its subsidiary Jackson Securities LLC;
- Blaylock Robert Van, L.L.C.;
- CastleOak Securities, LP;
- Muriel Siebert & Co., Inc.;
- Park Madison Partners LLC;
- The Williams Capital Group, L.P.; and
- Utendahl Capital Management.

Consistent with Treasury's previous announcements, small-, veteran-, minority-, and women-owned businesses will continue to have the opportunity to partner with the fund managers following pre-qualification.

During the two-month evaluation period, Treasury also conducted legal, compliance, and business due diligence on the fund managers and negotiated equity and debt term sheets² for each pre-qualified fund manager. Treasury will continue to negotiate final documentation with each pre-qualified fund manager with the expectation of announcing a first closing of a PPIF in early August.

Each pre-qualified fund manager will have up to 12 weeks to raise at least \$500 million of capital from private investors for its PPIF. The equity capital raised from private investors will be matched by Treasury. Each fund manager will also be required to invest a minimum of \$20 million of firm capital into the PPIF. Upon raising this private capital, pre-qualified fund managers can begin purchasing Legacy Securities. Treasury will also provide debt financing up to 100% of the total equity of the PPIF. In addition, PPIFs will be able to obtain debt financing raised from private sources, and leverage through the Fed's and Treasury's Term Asset-Backed Securities Loan Facility ("TALF")³ for TALF-eligible assets, subject to total leverage limits and covenants.

Participation by Retail and Foreign Investors

Treasury clarified in the July 8 announcement that retail investors would be eligible to participate in the Legacy Securities Program. Treasury believes that appropriate retail participation (both indirectly through public pension fund investors and directly through individual investors) would enhance the Legacy Securities Program

² Sample Letter of Intent and Term Sheet available at: http://www.financialstability.gov/docs/S-PPIP_LOI_Term_Sheets.pdf

³ For additional information on TALF, see the issues of *Dechert OnPoint* related to TALF, available at: http://www.dechert.com/library/FS_Finance_and_Real_Estate_3-09_TALF.pdf, http://www.dechert.com/library/Finance_and_Real_Estate_05-09_19_Federal_Reserve_Bank_on_NY.pdf, and http://www.dechert.com/library/Finance_and_Real_Estate_05-09_20_New_York_Expands_TALF_to_Include_Legacy_CMB_S.pdf

primarily by increasing the amount of capital available to purchase Legacy Securities. Retail participation will also help to increase liquidity and functioning of markets for eligible Legacy Securities. Treasury has encouraged fund managers to propose structures that enable retail investors to participate and stated that any such participation must be structured to comply with applicable securities laws and requires approval by the Securities and Exchange Commission.

In addition, Treasury provided further guidance on the extent to which foreign investors would be eligible to participate in the Legacy Securities Program. Treasury seeks broad participation in the Legacy Securities Program from both U.S. and foreign institutions subject to certain eligibility requirements set forth below:

- **Sellers of Legacy Securities to a PPIF:** Legacy securities may be purchased solely from financial institutions from which the Secretary of the Treasury may purchase troubled assets pursuant to Section 101(a)(1) of the Emergency Economic Stabilization Act. Generally, sellers of Legacy Securities must be established and regulated in the U.S. (including territories or possessions of the U.S.) and have significant operations in the U.S. Any central bank of, or institution owned by a foreign government generally cannot be a seller of Legacy Securities. However if foreign government ownership of otherwise eligible Legacy Securities results from extending financing to financial institutions that then failed or defaulted on such financing or from other prudential action that results in government ownership of a financial institution, such assets remain eligible for sale to a PPIF.
- **Legacy Securities PPIF Fund Managers:** PPIF fund managers must be headquartered in the U.S., but its ultimate parent company need not be headquartered in the U.S. For purposes of this criteria, “headquartered” means the fund manager is established, licensed, and maintains a commercial presence in the U.S.
- **Passive Private PPIF Investors:** Treasury seeks broad investor participation from both U.S. and foreign investors in the Legacy Securities Program to maximize the program’s impact on the liquidity and functioning of markets for Legacy Securities. As such, there is no limitation on foreign investor participation. However, any private investor in a PPIF will be subject to a maximum investment of 9.9% of the PPIF.

Treasury’s Making Home Affordable Program

Treasury also used the July 8 announcement to clarify the manner in which the Legacy Securities Program will interface with Treasury’s recently announced Making Home Affordable Program (“MHAP”). Subject to the fund manager’s analysis and judgment and consistent with its fiduciary duties to the PPIF, fund managers of PPIFs that acquire interests in residential mortgage-backed securities (“RMBS”) have agreed: (i) to consent, on behalf of the PPIF, to reasonable requests from servicers or trustees for approval to participate in MHAP, or for approval to implement other reasonable loss mitigation measures (including, but not limited to, term extensions, rate reductions, principal write downs, or removal of caps on the percentage of loans that may be modified within the securitization structure) and (ii) where the PPIF acquires 100% of RMBS that are backed by a particular pool of residential mortgage loans, to instruct the servicer or trustee of such securities, if such servicer or trustee is participating in MHAP, to include such pool of residential mortgage loans in MHAP. PPIFs are eligible to receive their share of any standard investor subsidies payable to them under MHAP and Treasury’s Home Affordable Modification Program.

Legacy Loans Program Update

In the July 8 announcement, the FDIC reaffirmed its commitment to building a successful Legacy Loan Program and will continue to work to increase the utilization of this program by open banks and investors. To this aim, the FDIC has incorporated the feedback it received following a public comment period into the design of the program. The FDIC plans to test a funding mechanism, which draws upon concepts successfully employed by the Resolution Trust Corporation in the 1990s, in a sale of receivership assets this summer. The FDIC expects to solicit bids for this sale of receivership assets in July.

Legacy Securities Program Conflict of Interest Rules

Along with the July 8 announcement, Treasury released new rules regulating conflicts of interest in the Legacy Securities Program. The Rules are the product of extensive interaction with the staff of the Special Inspector General for the Troubled Asset Relief Program (“SIGTARP”), as well as prospective fund managers and compliance professionals at the Fed.

Treasury's Process in Developing the Rules

Treasury conducted a rigorous process to develop the Rules. Below is a summary of the steps the Treasury followed:

- Fund manager applicants were required to identify all actual and potential conflicts of interest and propose measures to mitigate those conflicts.
- Treasury reviewed each potential fund manager's conflicts and identified any deficiencies with respect to governance and conflicts mitigation controls. Treasury conducted due diligence to obtain additional information regarding governance and conflicts of interest for all applicants selected as finalists, including information with respect to the proposed PPIF: (i) internal audit methodology, accounting policies and procedures and internal controls; (ii) mechanisms to identify, track, eliminate, mitigate, and monitor conflicts of interest; (iii) policies regarding affiliates, valuation, trade allocations, and handling of material non-public/sensitive information; and (iv) Chief Compliance Officer's responsibilities, authorities, and independence; and
- Treasury benchmarked these responses across several compliance and conflicts of interest metrics and prepared follow-up due diligence questions for each finalist;
- Finalists made in-person presentations to Treasury in order to provide additional opportunities for treasury to seek more information.

Summary of the Rules

Treasury developed the Rules based on the results of the above process. Below is a non-exhaustive summary of the Rules:

- **Conflicts regarding fund manager affiliates holding Legacy Securities:** PPIFs may not invest in, buy Legacy Securities from, or sell Legacy Securities to: (i) its affiliates (thus, a PPIF cannot sell assets from non-PPIF funds into the PPIF); (ii) any other PPIF managed by a different fund manager; or (iii) any investor that has invested 9.9% or more of the aggregate private capital raised by the PPIF or any of its affiliates. In addition, any transaction with a related party must be at arm's length, commercially reasonable, and on terms no less favorable to the PPIF than transactions with unrelated parties.

- **Alignment of fund manager and investor interests:** Treasury will require each fund manager to invest a minimum of \$20 million of firm capital in the PPIF they manage. Additionally, each PPIF it manages must allow co-investment by PPIF fund manager staff and employees in the PPIF it manages to better align incentives between the fund manager and the investors in the PPIF. Fund managers must demonstrate that their compensation systems align the economic interests of those that run the PPIF with interests of investors in the PPIF.

- **Key policies and procedures (allocation and valuation/pricing policy):** Fund managers must adopt policies and procedures that comply with the Investment Advisers Act of 1940 in all material respects. Each pre-qualified fund manager maintains strict internal policies regarding ethics and compliance. In addition, each pre-qualified fund manager is a registered investment adviser and maintains independent auditors and corporate governance processes.

- **Independent compliance department and oversight:** Fund managers will be required to maintain an independent compliance department that reports all positions in Legacy Securities (PPIF and non-PPIF funds) to Treasury on an on-going basis. This allows Treasury to monitor and audit all funds in the fund manager's family of funds that trade in eligible securities and allows Treasury to see the flow of Legacy Securities throughout the firm. Thus, Treasury will be able to evaluate if the fund manager is purposely disadvantaging the PPIF relative to other funds. In addition, Treasury and SIGTARP will have the right to conduct annual and ad hoc audits and compliance with all policies.

- **Personal conflicts of interest of fund manager employees:** Treasury will require that all PPIFs maintain stringent policies related to the handling of material non-public information, personal trading, outside business affiliations, and the giving and accepting of gifts and entertainment. In addition, all key individuals of the fund manager must comply with an approved code of ethics and associated personal trading policy.

- **Conflicts with fund manager placement agents and broker-dealer relationships:** Fund managers may not have "pay-to-play" arrangements with placement agents, underwriters, and other service providers in which money or other forms of direct or indirect compensation are exchanged for services for the privilege to engage in such activities. In addition, PPIFs may not

execute trades through any broker-dealer affiliated with the fund manager.

Material Terms and Documentation

In connection with the Legacy Securities Program, Treasury has entered into a standard non-binding Letter of Intent (the “Letter of Intent”) with each of the selected fund managers. Separate term sheets, an equity term sheet (the “Equity Term Sheet”) and a debt term sheet (the “Debt Term Sheet”), have been attached to each Letter of Intent setting forth the terms of Treasury’s equity and debt investments in the PPIFs. Under each Letter of Intent, Treasury has agreed to negotiate in good faith to execute mutually acceptable definitive and binding written agreements with respect to (i) its investment in the applicable PPIF, which will be formed as a limited partnership by each of the fund managers (the “Equity Investment”) and (ii) a senior secured credit facility to be provided by Treasury to each of the PPIFs (the “Debt Investment”).

Equity Term Sheet

Under the standard terms in the Equity Term Sheet, each fund manager will form one or more private vehicles (the “Private Vehicles”) to invest alongside Treasury and the Private Vehicles will each become limited partners (“Limited Partners”) of the applicable PPIF. Each fund manager will form or select an affiliate entity that will act as the general partner of the PPIF (each, a “General Partner”) and such General Partner will be permitted to form feeder vehicles to facilitate the participation of investors in the Private Vehicles. The General Partners and each of the Limited Partners (together, the “Partners”) will subscribe for interests in the applicable PPIF (“Interests”). The investment objective of each of the PPIFs will be to generate attractive returns for the Partners through long-term investments in Legacy Securities eligible for investment under the PPIP (“Eligible Assets”).⁴ The offering materials and governing documents of the Private Vehicles and any side letters entered into with investors will be subject to the review and approval of Treasury.

⁴ For additional information on Eligible Assets, see the issue of DechertOnPoint related to the PPIP, available at http://www.dechert.com/library/Finance_and_Real_Estate_04-09_17_An_Analysis_of_the_Department_of_Treasury.pdf.

Each General Partner must make a direct or indirect capital commitment to the PPIF (a “Capital Commitment”), through the Private Vehicles or another affiliate, of at least \$20 million. Furthermore, no investor (together with its affiliates) may make an indirect Capital Commitment through any Private Vehicle that would exceed 9.9% of the aggregate Capital Commitments to the applicable PPIF. Treasury’s Capital Commitment in each case will equal the aggregate Capital Commitments of the Private Vehicles and the General Partner, up to a certain maximum dollar amount negotiated and determined separately between Treasury and each of the respective fund managers. Pending investment or distribution by each PPIF, funds held by each PPIF may be invested in (i) cash, (ii) Treasury securities, or (iii) money market mutual funds that invest only in direct obligations of the United States or obligations guaranteed by the United States (“Temporary Investments”).

Diversification and Investment Limitations

The PPIFs will be subject to certain diversification and investment limitations. Without the written consent of Treasury, PPIFs are not permitted to acquire a residual interest in a Real Estate Mortgage Investment Conduit, invest in any securities other than Eligible Assets or Temporary Investments, enter into derivative contracts that are not solely intended to hedge the applicable PPIF’s interest rate exposure with respect to any debt obligation, hedge any credit risks arising from investments made by the applicable PPIF, lend any Eligible Asset or economic interest therein, or violate any additional covenants set forth in a schedule to the Equity Term Sheet of the applicable PPIF, which includes PPIF-specific information.

Investment Period

The obligation of the PPIFs to fund Capital Commitments and make new investments will expire on the third anniversary of the initial closing (the “Investment Period”), at which time all Partners will be released from further obligations with respect to undrawn Capital Commitments, except to the extent necessary to cover certain partnership expenses, indebtedness and obligations of the PPIF to complete investments. The Investment Period may be terminated earlier, in the discretion of Treasury, at any time after the one-year anniversary of the initial closing. During the Investment Period, proceeds distributable to the Partners may be retained and re-invested by the General Partner, however proceeds actually distributed to Treasury may not be recalled.

Distributions

Investment proceeds of the PPIFs are to be distributed within 30 days of the end of each fiscal quarter in which such proceeds are received by the applicable PPIF. Investment proceeds will be distributed first to each of the Partners (in proportion to their respective percentage interests) until such Partners have received distributions equal to the amount of their capital contributions. Remaining investment proceeds will also be distributed to each Partner in proportion to their respective percentage interests except that Treasury will receive an additional distribution amount of funds payable, calculated on the basis of the applicable Warrant Percentage. The Warrant Percentage used to calculate such additional distributions in favor of Treasury will be (a) 2.5% for PPIFs that have elected Treasury leverage of up to 100% of Capital Commitments or (b) 1.5% for PPIFs that have elected Treasury leverage of up to 50% of Capital Commitments, and will be calculated on the basis of Capital Commitments made by the Private Vehicles and the applicable General Partner up to the amount of Treasury's Capital Commitment.

Treasury Management Fee

In consideration for management services provided to the PPIFs, Treasury will pay each General Partner an annual fee, quarterly in arrears (the "UST Management Fee"). During the Investment Period, the UST Management Fee will be equal to 0.20% per annum of Treasury's Capital Commitment and after the Investment Period will be equal to the lesser of 0.20% per annum of Treasury's Capital Commitment and the fair market value of Treasury's interest in the applicable PPIF. The UST Management Fee may be paid out of investment proceeds otherwise distributable to Treasury but not from drawdowns of Treasury's Capital Commitment. Private investors will bear no responsibility for any portion of the UST Management Fee and will pay management fees at the Private Vehicle level as determined by each PPIF.

Restrictions on Fund Investment Activities

Certain general restrictions are placed on the investment activities of each General Partner and its affiliates while involved in the operations of the PPIF. Prior to (i) each of the PPIFs investing 85% of Capital Commitments or (ii) one year from the date of initial closing of the PPIF, whichever is earlier, General Partners and their affiliates may not form or accept commitments to other pooled investment funds that have the primary

objective of investing in Eligible Assets (other than any feeder vehicles or private REITs formed to invest in the PPIFs, any publicly offered vehicle, or any pooled investment fund formed to invest in Eligible Assets pursuant to another program sponsored by the U.S. Federal Government or the Fed). General Partners and their affiliates may continue to manage existing pooled investment funds or separate accounts having a primary investment objective similar to the PPIFs that are in existence as of the initial closing of the applicable PPIF if such funds were disclosed in writing to Treasury prior thereto.

PPIFs are also not permitted to invest in, acquire investments from, or sell investments to affiliates, significant investors, and other PPIFs as discussed above under "Summary of the Rules" with respect to fund manager conflicts.

Furthermore, without the written consent of Treasury, none of the General Partners nor any of their affiliates may engage in any transaction with their related PPIFs that is not expressly contemplated by the partnership agreement governing the terms of the applicable PPIF (in each case, the "Partnership Agreement").

General Partner Removal

The Equity Term Sheet sets forth various scenarios in which General Partners may be removed. General Partners may be removed at any time on a no-fault basis upon the election of Treasury if Treasury has the written consent of at least a majority in interest of investors in the related Private Vehicles.

Furthermore, General Partners may be removed upon the election of Treasury in the following circumstances:

- There is an occurrence of an event of "cause" (such as a breach by the General Partner of its obligations or an act of bad faith by its executives).
- There is an occurrence of a "Key Person Event" that has not been cured by the General Partner within 30 days, so long as Treasury has the written consent of at least one third in interest of investors in the Private Vehicles. An event constituting a "Key Person Event" will differ with respect to each PPIF, but in each case will involve the removal or resignation of certain key officers or employees of the fund manager who are significant in the operations and management of the PPIF (each, a "Key Person").

- There is a removal of the General Partner or an affiliate thereof, as the general partner of any Private Vehicle.

Dissolution

Each PPIF will dissolve eight years from its initial closing and may be extended with the written consent of Treasury for up to two consecutive one-year periods. PPIFs may be dissolved earlier (i) after the expiration or termination of the Investment Period, upon the liquidation of all investments; (ii) upon the bankruptcy, dissolution, or similar event of withdrawal of the relevant General Partner; or (iii) if there is a change in any law or regulation that would materially adversely impact either the relevant General Partner, a majority in interest of investors in the Private Vehicles or their respective affiliates as a result of their participation in the PPIF.

Withdrawals and Transfers

Partners generally may not withdraw from the PPIFs. Investors in the Private Vehicles may only withdraw for legal reasons and, upon such withdrawal would only receive a note payable with distributions to the Private Vehicles. Furthermore, neither the General Partners nor the Private Vehicles may transfer their Interests without the prior written consent of Treasury. Under the Equity Term Sheet, investors in the Private Vehicles are permitted to transfer their interests in the Private Vehicles provided that the relevant General Partner ensures that transferees are in compliance with the applicable screening requirements and securities laws.

Reports and Financial Information

General Partners are required to deliver customary periodic reports and financial information to SIGTARP. General Partners must also provide additional reports to Treasury or SIGTARP, as requested, provided that if such reports are not customarily provided by investment fund managers or are not required by law, Treasury will bear the reasonable expenses in connection with their preparation.

General Partners must provide Treasury, SIGTARP, and the Government Accountability Office access to the books and records and Key Persons of the PPIFs and the Private Vehicles, including any information in the possession of the applicable General Partner and its affiliates regarding the beneficial owners of interests in the Private Vehicles and material events. General Partners are also required to provide Treasury,

SIGTARP, and the Government Accountability Office with certain information relating to Eligible Assets held by other pooled investment funds of the applicable fund manager. General Partners are not required to identify by name the investors in such pooled investment funds or the clients with respect to such separate accounts.

Most Favored Nations

Treasury has the right to elect the benefit of any provision of the governing documents of the Private Vehicles and any side letter of the Private Vehicle that has the effect of benefiting any investor in the Private Vehicles (other than the General Partners and their affiliates and their respective officers, directors or employees) in a manner more favorable than the benefits established in favor of Treasury by the relevant Partnership Agreement.

Debt Term Sheet

Under the PPIF, during the Investment Period, Treasury will also provide secured non-recourse loans to each of the PPIFs on the terms set forth in the Debt Term Sheet (the "Loans") to be used to acquire Eligible Assets. Depending on the election of each PPIF, the Loans will be in the aggregate amount of up to either 50% of total drawn Capital Commitments (a "Half Turn Election") or 100% of total drawn Capital Commitments (a "Full Turn Election"), not to exceed a maximum amount determined individually for each of the PPIFs. Recourse under the Loans is limited to the PPIF and its assets and does not extend to the Limited Partners, the General Partners, or any of the fund managers. Further to the discussion of "*Distributions*" above, the Warrant Percentage applicable to PPIFs that make a Full Turn Election will equal 2.5% and the Warrant Percentage applicable to PPIFs who make a Half Turn Election will equal 1.5%.

PPIFs making the Full Turn Election will be permitted to subsequently make a Half Turn Election if they are in compliance with the agreements governing the Loans (the "Loan Documents") on a *pro forma* basis and if the applicable PPIF reduces its outstanding Loans to at least an amount permitted to be borrowed under the Half Turn Election. The applicable Warrant Percentage however, will not be adjusted. The Full Turn Election will not be subsequently available to PPIFs who initially make a Half Turn Election.

Financial Conditions

Treasury's obligation to make each Loan is conditional upon the continuing satisfaction of certain financial tests set forth in the Debt Term Sheet. In order to draw down on the Loans, PPIFs must be in compliance with an asset coverage test requiring the asset coverage ratio of the PPIF to be at least 225% if a Half Turn Election is in effect, and 150% in other cases (the "Asset Coverage Test"). Furthermore, if a Half Turn Election is in effect, each PPIF must also meet a leverage ratio test (the "Leverage Ratio Test"), such that the ratio of the PPIF's indebtedness to the net asset value of its assets, does not exceed 5.00 to 1.00 if Loans are outstanding or, the maximum leverage allowed pursuant to the TALF if Loans are not outstanding. Furthermore, a PPIF will not be permitted to make additional investments if the Asset Coverage Test is not met.

Third Party Debt

PPIFs making a Half Turn Election may also finance Eligible Assets using the TALF program or, with the written consent of Treasury, additional debt offered by third party lenders, subject to the satisfaction of the Asset Coverage Test and the Leverage Ratio Test.

Eligible Assets financed with such third party debt must be financed and held through a wholly owned financing subsidiary of the PPIF (a "Financing Subsidiary"), which subsidiaries may be capitalized with proceeds of Capital Commitments and the Loans. Such third party debt will be recourse solely to the applicable Financing Subsidiary and not to the PPIF. PPIFs making a Full Turn Election are not permitted to incur any additional third party debt including debt as a result of the TALF program.

Interest and Repayment

Loans repaid or prepaid may not be re-borrowed. The Loans will be due on the tenth anniversary of the initial closing of the applicable PPIF unless the PPIF is terminated or dissolved earlier in which case the Loans will be due at such time. Loans may be prepaid at any time by the PPIFs without premium or penalty.

The Loans will bear interest at a rate per annum equal to LIBOR plus an applicable margin for each accrual period. If the LIBOR interest rate cannot be determined, the Loans will bear interest equal to the prime lending rate published by the Wall Street Journal. The applicable margin will be (i) initially, (a) in the case of Loans bearing interest at the prime lending rate, if a Half Turn

Election is in effect, 1.00%, and if a Full Turn Election is in effect, 0.0%; and (b) in the case of Loans bearing interest at the LIBOR interest rate, if a Half Turn Election is in effect, 2.00%, and if a Full Turn Election is in effect, 1.00% and (ii) after the date any third party debt is incurred, the greater of (x) 2.00% and (y) 100 basis points higher than the weighted average applicable margin applicable to all third party debt outstanding.

If an event of default occurs and is continuing, the interest rate margin will increase by 2.00% and a PPIF will not be permitted to distribute funds to holders of Interests until all of the Loans are paid off.

Allocation of Investment Proceeds

Investment proceeds of each PPIF will be allocated in accordance with a priority of payments waterfall more particularly set forth in the Debt Term Sheet, to pay expenses, interest on the Loans and, subject to compliance with the Asset Coverage Test, to acquire additional Eligible Assets or to make distributions to the Partners and repay Loans.

During the Investment Period, General Partners may only use funds made available by the Loans to make investments in additional Eligible Assets if after giving effect thereto, the Asset Coverage Test would be satisfied. Furthermore, in the event that the Asset Coverage Test is not satisfied, payments must be made to pay down the principal amount on the Loans until the Asset Coverage Test is satisfied, before distributions can be made to Partners. After the Investment Period, investment proceeds not required to pay interest and specified expenses will be allocated to repay Loans and to make distributions to Partners. Investment proceeds from investments held by Financing Subsidiaries must be used to repay third party debts and any surplus proceeds must be distributed to the PPIF to be allocated in accordance with the priority of payments waterfall.

Collateral

The Loans will be secured by (a) a first priority security interest in all of the investments of the PPIF, (b) a pledge of the equity interests of all Financing Subsidiaries, (c) the PPIF's rights under certain permitted interest rate hedges, (d) all other existing and future assets and property of the PPIF, and (e) all proceeds of the foregoing (collectively, the "Collateral"). Investments held by Financing Subsidiaries used to incur permitted

third party debt will not constitute Collateral and may be used to secure such third party debt.

All Eligible Assets, Temporary Investments, and proceeds thereof are required to be maintained in a custodial account. PPIFs must also maintain an interest reserve account containing an amount reasonably determined to accrue on the Loans in three accrual periods.

PPIF Covenants

The Loan Documents will contain affirmative and negative covenants customary for borrowers in financings of this type. The affirmative covenants to be included in the Loan Documents include covenants relating to the delivery of financial statements, notices of events of default or other material events, compliance with laws, policies and contractual obligations, the implementation of conflict of interest standards and rules of ethics approved by Treasury, payment of taxes and other obligations, maintenance of business and property, inspection rights of Treasury, SIGTARP and the Government Accountability Office, maintenance of security interests in the Collateral, and the distribution of investment proceeds by Financing Subsidiaries to the PPIFs.

The negative covenants in the Loan Documents will include limitations on the incurrence of unpermitted additional debt, liens, and other adverse claims on the Collateral, mergers or other reorganizations of the PPIF, transactions with affiliates, capitalization of subsidiar-

ies, investments other than investments in Eligible Assets or Temporary Investments, interest rate hedges, and engaging in other business.

Events of default under the Loan Documents will also be customary and will include the non-payment of amounts due, violations of the Loan Documents, bankruptcy events of PPIFs and their Financing Subsidiaries, certain events of “cause” and Key Person Events as discussed under “*General Partner Removal*” above, the withdrawal, commencement of liquidation proceedings, insolvency, or dissolution of the relevant General Partner, a vote by Treasury and the requisite number of investors to remove the General Partner, or a change of control.

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