WINSTON & STRAWN LLP

BRIEFING

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Summary of Federal Reserve's Term Asset-Backed Securities Loan Facility and Program to Purchase Direct Obligations of Housing Related GSEs and MBS Guaranteed by GSEs

On November 25, 2008, the Federal Reserve Board of Governors (the "**Federal Reserve**") took direct aim at reinvigorating the consumer and small business lending markets by announcing the creation of the Term Asset-Backed Securities Loan Facility ("**TALF**").

Over the past two decades, the securitization markets have acted as one of the primary facilitators of growth for consumer spending and small business expansion. By providing a highly liquid, cost-effective method for banks and financial institutions to fund loans made to consumers and small businesses, the issuance of asset-backed securities ("**ABS**") collateralized by such loans have in turn increased the availability, and reduced the costs, of credit for consumers and small businesses. As a result of the recent turmoil in the credit markets triggered by the dramatic deterioration of the credit quality of mortgage-backed securities, new issuances and secondary sales of ABS collateralized by consumer and small business loans have grinded to a halt over the past few months.

Recognizing the critical role that the securitization markets have had in the overall financial stability of consumers and small businesses, the Federal Reserve has announced the preliminary details of a new program under which the Federal Reserve Bank of New York ("**FRBNY**") will make term loans available to investors of such ABS in an effort to stimulate liquidity and origination volume in such markets. This client briefing provides a summary of the scope and terms and conditions of the TALF as originally proposed by the Federal Reserve. We anticipate that such terms and conditions will continue to evolve over the coming weeks as the Federal Reserve digests the feedback that it has requested from industry participants. As a result, we intend to update this client briefing as such developments occur.

In addition to our summary of the TALF, we have provided a description at the end of this client briefing of the Federal Reserve's program to purchase direct obligations of housing-related, government-sponsored enterprises ("**GSEs**"), such as Fannie Mae, Freddie Mac and the Federal Home Loan Banks, and mortgage-backed securities ("**MBS**") guaranteed by Fannie Mae, Freddie Mac, and Ginnie Mae, which was also announced on November 25, 2008.

I. Term Asset-Backed Securities Loan Facility

A. Purpose of Facility

Unlike recently created government programs, such as the Treasury Troubled Asset Purchase Program (TARP), Federal Reserve Commercial Paper Funding Facility Program (CPFF) and the Treasury Capital Purchase Program (CPP), which have focused on strengthening the balance sheets of banks and dealers that have been damaged by troubled assets, the TALF focuses specifically on providing liquidity for investors that act as counterparties to the banks and dealers in the secondary markets for ABS. Over the past few months, the spreads for ABS collateralized by certain types of consumer and small business loans have widened to levels that appear excessive given the levels of default the industry expects for the assets underlying such ABS. The severity of such widening spreads has resulted in a significant reduction in the origination volumes for ABS collateralized by automobile loans, student loans, and credit card loans since the end of the second quarter of 2008, as shown in the following chart:

Category	Amount YTD 2008[1]	Amount 1H 2008[2]	Amount 2007[3]	Amount 2006[4]
Automobiles				
Industry Total	$32.7 billion	$32.0 billion	$78.8 billion	$85.0 billion
Credit Cards				
Industry Total	$63.8 billion	$55.0 billion	$94.1 billion	$67.1 billion
Student Loans				
Industry Total	$29.9 billion	$22.9 billion	$56.5 billion	$66.4 billion

Origination volumes for ABS collateralized by small business loans guaranteed by the U.S. Small Business Administration ("**SBA Loans**") have similarly decreased.

The Federal Reserve has determined that the inability of ABS investors to obtain term financing to buy ABS in the secondary markets from traditional funding sources, such as Structured Investment Vehicles ("**SIVs**") and commercial paper conduits ("**CP Conduits**"), has been at least partially responsible for the widening of ABS spreads. The Federal Reserve's expectations are that investors will be willing to accept smaller spreads to purchase ABS collateralized by consumer and SBA Loans from banks, dealers, and other counterparties in the secondary market, if the TALF is able to provide ABS investors with access to term financing on terms reasonably competitive with those previously provided by the SIVs and CP Conduits. The lowering of ABS spreads should in turn increase the availability, and reduce the costs, of lending provided by the banks and other financial institutions to consumers and small businesses.

B. Scope of Facility

FRBNY has been given the authority under Section 13(3) of the Federal Reserve Act to make up to $200 billion of term loans to eligible borrowers that will be fully secured by Eligible ABS (as defined below) pledged by such borrowers.[5] The TALF loans will be non-recourse to the borrowers and will have a term of at least one year with interest payable monthly.[6] All cash proceeds of the Eligible ABS pledged under the TALF must be used by a borrower to pay interest due on, or reduce the principal amount of, the borrower's TALF loan.

1. Source: Asset Securitization Report Volume 8, Number 42 (November 3, 2008).

2. Source: Asset Securitization Report Volume 8, Number 27 (July 7, 2008).

3. Source: Asset Securitization Report Volume 8, Number 1 (January 7, 2008).

4. Source: Asset Securitization Report Volume 7, Number 1 (January 8, 2007).

5. The Eligible ABS pledged by a borrower will remain on the borrower's balance sheet unless and until such time as the borrower elects to put such Eligible ABS to FRBNY as further described below.

6. The Federal Reserve has indicated a willingness to consider extending the term of TALF loans beyond one year if it determines that longer maturities are necessary in order to stabilize the consumer and small business lending markets.

The TALF will be available to all U.S. persons that own Eligible ABS. Any natural person that is a U.S. citizen, a business entity that is organized under the laws of the United States or a political subdivision or territory thereof (including such an entity that has a non-U.S. parent company), or a U.S. branch or agency of a foreign bank will be considered a "U.S. person" for the purposes of qualifying for access to the TALF. As indicated above, the TALF is intended to provide term financing for investors of ABS, not issuers of ABS. However, an issuer of ABS will be permitted to participate in TALF in the event such issuer purchases Eligible ABS in the secondary market.

A borrower must pledge Eligible ABS to the FRBNY in order to receive a loan under TALF. In order to qualify as an "Eligible ABS", assets must satisfy the following conditions:[7]

1. Cash Assets. The collateral pledged by a borrower must be U.S. dollar-denominated cash ABS. Synthetic (or derivative) ABS will not qualify as collateral to be pledged under the TALF.

2. Rating Requirement. The ABS must have a long-term credit rating in the highest investment-grade rating category (*i.e.*, "AAA") from two or more major, nationally recognized statistical rating organizations (*e.g.*, Standard & Poor's Ratings Services, Moody's Investors Service, Inc., Fitch, Inc.) and cannot have a long-term credit rating of below the highest investment-grade rating category from any such rating agency. This rating requirement will, at least initially, limit the availability of the TALF to a small portion of the overall consumer and small business ABS markets. It remains to be seen whether the Federal Reserve will expand the scope of the TALF to finance lower tiered rated ABS if the initial rollout of the TALF proves to be successful.

3. Type of Underlying Assets. The ABS must represent a direct interest in an underlying pool of automobile loans, student loans, credit card loans, or SBA Loans. The ABS's underlying credit exposure must be a cash, not a synthetic (or derivative) exposure.

4. Domicile of Obligors. The obligors of the assets collateralizing the ABS must be U.S domiciled obligors. Although the Federal Reserve did not provide further details regarding the criteria that must be satisfied in order to qualify as a U.S. domiciled obligor, we believe that the definition of a "U.S. person" provided by the Federal Reserve in relation to the eligibility criteria for borrowers under the TALF should provide relevant guidance for this condition.

5. Time of Origination. In order to be eligible as collateral under the TALF, ABS must be newly or recently originated. The Federal Reserve has not yet provided details regarding the cutoff date for the origination of ABS that will be eligible for TALF funding.

6. Origination of Underlying Loans. The loans that collateralize the ABS must be originated by a third party that is unrelated to the borrower. ABS that are backed by loans originated by a borrower that desires to borrow under the TALF or an affiliate of such borrower will not be eligible to receive TALF financing.

7. Compliance with Executive Compensation Requirements of EESA. All originators of the loans underlying the Eligible ABS (or in the case of SBA Loans, the ABS sponsor) must have agreed (or already be subject to) the executive compensation requirements in Section 111(b) of the Emergency Economic Stabilization Act of 2008.[8]

A borrower will not be permitted to substitute collateral during the term of its TALF loan and will not be subject to re-margining or mark-to-market requirements that would require a borrower to pledge additional collateral following the date FRBNY makes such a loan to the borrower. This feature of the TALF should alleviate some of the pressures of margin calls that ABS investors have recently been facing.

7. In addition to the specific eligibility criteria set forth by the Federal Reserve, the Federal Reserve has confirmed that both fixed and floating rate ABS will be eligible for funding under the TALF and such ABS do not need to be supported by DTC (*i.e.*, physical certificated ABS will be eligible for TALF).

8. The executive compensation requirements of the Emergency Economic Stabilization Act of 2008 are beyond the scope of this client briefing. If you desire further details regarding such requirements, please contact your relationship partner at Winston & Strawn LLP and he or she will direct you to an attorney in our employee benefits group to respond to your request.

The Federal Reserve has indicated that it may expand the scope of ABS that are eligible for financing under the TALF to include commercial mortgage-backed securities, non-GSE residential mortgage-backed securities, and other asset classes if the initial implementation of the TALF has a positive impact on the liquidity and pricing of the consumer and small business loan securitization markets.

C. Pricing and Allocation of TALF Loans

FRBNY will offer and price TALF loans pursuant to a monthly competitive auction process. Borrowers that desire TALF loans must submit a sealed bid indicating the amount of credit and pricing (based on a spread over the one-year overnight index swap (OIS)) desired by such borrower. Any bid submitted by a borrower will be subject to a minimum interest rate spread established by FRBNY for each auction. Based on such bids, FRBNY will select borrowers that are eligible to receive financing from the TALF and will establish a fixed interest rate for such TALF loans. FRBNY has absolute discretion to reject any bid made by a potential borrower and intends to develop procedures to further scrutinize whether loans should be secured by ABS that has been identified as having a high risk of loss.

In the event that a borrower is selected to receive a loan from the TALF, the borrower must use a primary dealer as its agent to access the TALF and must deliver eligible collateral to a clearing bank. Any such primary dealer will simply be acting on behalf of a borrower in an agency capacity and will not have any liability with respect to TALF Loans.[9]

D. Allocation of TALF Losses

Any credit losses related to Eligible ABS that have been financed by loans made under the TALF will be absorbed by participating borrowers and the Federal Reserve in accordance with the following predetermined set of loss allocation rules:

1. First Loss: The first loss related to any such Eligible ABS that have always be incurred by a participating borrower in an amount up to but not exceeding the discount (or "haircut") applied by the FRBNY to the class of assets that collateralizes such Eligible ABS. Although FRBNY has not yet established the discount for each class of assets underlying ABS that is eligible for the TALF funding, they have indicated that they are weighing the benefits of increasing the length of the term of the TALF financing against the burdens of imposing higher discounts (or lower advance rates) on participating borrowers. The Federal Reserve has also indicated that it expects to establish different discounts for different classes of eligible assets. Because the TALF loans will be structured as non-recourse loans to the borrowers, a borrower's risk of loss on any ABS pledged as collateral for a TALF loan will be limited to the discount applied by FRBNY to the asset class collateralizing such ABS (*i.e.*, a borrower will not retain any tail risk beyond such discount).

2. Second Loss: The second loss incurred by any such Eligible ABS will be allocated to the U.S. Treasury under the TARP in an amount not to exceed $20 billion. In the event that any Eligible ABS that have been financed by the TALF incurs losses that exceed the "first loss" position retained by the participating borrower (as described above), the borrower will be permitted (and will have the economic incentive) to put the Eligible ABS to FRBNY in full satisfaction of the borrower's obligations to pay principal and interest on TALF loans to FRBNY. FRBNY in turn will sell any such Eligible ABS pursuant to a forward purchase agreement to a special purpose vehicle (the "TALF SPV") that FRBNY will create for the sole purpose of buying, selling, and managing any Eligible ABS acquired under the TALF. The TALF SPV will utilize the proceeds from subordinated debt issued by the TALF SPV to the U.S. Treasury under the TARP ("TARP Subordinated Loans") to purchase such Eligible ABS. The amount of any such TARP Subordinated Loans will not exceed $20 billion over the term of the TALF. Any losses incurred by Eligible ABS that exceed the discount applied to the underlying assets of such Eligible ABS will be allocated as a credit-related loss to the outstanding principal balance of the TARP Subordinated Loan made by the U.S. Treasury to the TALF SPV. As a result, the U.S. Treasury's aggregate "second loss" for all Eligible ABS financed under the TALF will not exceed $20 billion.

3. Third Loss: The third (and final) loss related to any Eligible ABS that have been financed under the TALF will be allocated to the Federal Reserve. In the event the TALF SPV is required to purchase in excess of $20 billion of Eligible ABS that investors have put to FRBNY, FRBNY has agreed to lend additional funds to the TALF SPV to finance any such

9. Note that a primary dealer can itself be eligible as a borrower under the TALF.

purchases (the "TALF Senior Loans"). Any such loans made by FRBNY to the TALF SPV will be senior to the TARP Subordinated Loans, will be fully secured by all Eligible ABS purchased by the TALF SPV, and will have full recourse to the TALF SPV (including first priority to all cash flows generated by the Eligible ABS purchased by the TALF SPV).

In the event that any residual amounts remain in the TALF SPV following the repayment of any outstanding TARP Subordinated Loans and TALF Senior Loans, such amounts will be shared equally between the FRBNY and the U.S. Treasury.

E. Timing for Implementation of TALF

The Federal Reserve has expressed an awareness that there will be numerous complexities that will have to be resolved before the TALF can be officially launched. Although the Federal Reserve has not explicitly provided a deadline for implementing the TALF, it has requested industry participants to provide feedback to their initial proposed terms of the TALF, and they would like to be in a position to implement the TALF on or prior to February 2009.

F. Term of TALF

FRBNY may make new loans under the TALF in an amount not exceeding the maximum program size up until December 31, 2009, unless the term of the TALF is extended by the Federal Reserve. Any loans made under the TALF prior to the termination date will remain within the TALF until the maturity date applicable to each such loan.

II. Program to Purchase Direct Obligations of GSES and Mortgage-Backed Securities Guaranteed by GSES

The Federal Reserve also announced today that it will create a program to purchase the direct obligations of GSEs and MBS backed by guaranties provided by Fannie Mae, Freddie Mac, and Ginnie Mae. Similar to consumer and small business loan ABS, spreads on GSE obligations and MBS guaranteed by GSEs have widened to historically high levels, which has resulted in a higher cost, and reduced availability, of residential mortgages. Under the new program, the Federal Reserve will purchase up to $100 billion of GSE direct obligations through a series of competitive auctions that will begin next week. The Federal Reserve will also purchase up to $500 billion of MBS guaranteed by GSEs through the use of asset managers that are selected through a competitive process. The Federal Reserve intends to begin purchasing such MBS before the end of 2008. The new program is intended to reduce the costs, and increase the availability, of mortgages, which will hopefully provide long-term stability for housing prices across the nation.

The Global Financial Markets Spotlight Group of Winston & Strawn advises financial organizations and investors in banks on financing and funding issues and has been advising clients on matters under the Emergency Economic Stabilization Act of 2008 and all programs that have been established to restore market stability. Please contact one of the following attorneys below or on the following page for more information:

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