

SEWARD & KISSEL TALF TASK FORCE: Federal Reserve Board Launches the Term Asset-Backed Securities Loan Facility

On March 3, 2009 the Federal Reserve Board (“FRB”) launched the Term Asset-Backed Securities Loan Facility (“TALF”), under which the Federal Reserve Bank of New York (“FRBNY”) will initially make up to \$200 billion of loans to eligible borrowers who pledge certain newly issued asset-backed securities (“ABS”) as collateral. The FRB first announced plans for the TALF on November 25, 2008, with the intent of increasing credit availability to households and small businesses by encouraging investors to purchase newly issued ABS backed by student loans, auto loans, credit card loans and small business loans guaranteed by the Small Business Administration (“SBA”). The ABS market has historically funded a substantial share of consumer credit and small business loans, and in recent months new ABS issuance has come to a near-complete halt, posing challenges to the availability of credit to consumers and small businesses and contributing to a further weakening of U.S. economic activity.

KEY TERMS AND CONDITIONS

- ***Timing***
 - o The initial TALF subscription date will be Tuesday, March 17 and the initial loan settlement date will be Wednesday, March 25. Going forward, monthly subscription dates will be the first Tuesday of every month, with related settlement dates to be announced. The facility will cease to make loans on December 31, 2009, unless the program is extended.
- ***Eligible Borrowers***
 - o Eligible borrowers under the TALF must be entities organized in the United States. Newly formed and existing U.S.-organized investment funds that are subsidiaries of offshore investment funds may borrow under the TALF so long as they are managed by an investment manager with a principal place of business in the United States.
- ***TALF Loans***
 - o TALF loans will have three year terms, and recourse for the payment of the loans will generally be limited to the “eligible collateral” (as more fully described below) pledged to secure such loans. Borrowers will be able to select either fixed or floating rate loans.
- ***Primary Dealers***
 - o Eligible borrowers must access the TALF through a primary dealer. Each primary dealer will be required to apply its internal customer identification program and due diligence procedures to prospective borrowers.
- ***Loan Agreement***
 - o A primary dealer will execute the TALF Master Loan and Security Agreement (the “Loan Agreement”) on behalf of each borrower. *Clients are advised to review Seward & Kissel’s observations on the Loan*

Agreement attached as Exhibit A, and are encouraged to contact their Seward & Kissel attorney with any questions or concerns.

- **Collateral Surrender Option**
 - o In lieu of repaying the outstanding principal or interest on a TALF loan, at any time a borrower may surrender the underlying collateral to the FRBNY in full satisfaction of its obligations with respect to such loan.

TALF TERMS AND CONDITIONS

TALF Loans

The FRB has launched the TALF with a facility size of \$200 billion, but the FRB has indicated that the facility may later be increased to \$1 trillion. Under the facility, each TALF loan will have a minimum loan size of \$10 million, a term of three years, and recourse for the payment of loans will generally be limited to the eligible collateral pledged to secure such loans. Borrowers will be able to elect for either fixed-rate or floating-rate loans, so long as the interest rate format corresponds to the interest rate format for the collateral that will be pledged. Various types of collateral may be pledged for each TALF loan, so long as the interest rate format for the entire pool of collateral is the same. Interest will be payable monthly (with all interest payments on the pledged collateral being directly applied to service interest on the corresponding TALF loan) and any remittance of principal on the pledged collateral must be used immediately to reduce the principal amount of the corresponding TALF loan. Prepayments in full and in part will be allowed, and upon prepayment the collateral securing the TALF loan will be released on a pro-rata basis, taking into considering minimum denomination restrictions. TALF loans will not be subject to mark-to-market or re-margining requirements, and substitution of collateral during the term of the loan will be allowed only in very limited circumstances if certain eligibility criteria with respect to the collateral are not satisfied. Borrowers may assign their TALF loans to other parties, but only with the prior consent of the FRBNY, and only until December 31, 2009. The FRBNY may withhold or delay its consent to assignments for any reason.

Overcollateralization

The principal amount of each TALF loan will be the lesser of the par or market value of the pledged collateral less a collateral haircut established by the FRBNY for each item of collateral based on the asset class and expected average life. Initial collateral haircuts, which may change for later subscription dates, are as follows:

SECTOR	SUBSECTOR	ABS EXPECTED LIFE (YEARS)						
		0-1	>1-2	>2-3	>3-4	>4-5	>5-6	>6-7
Auto	Prime retail lease	10%	11%	12%	13%	14%		
Auto	Prime retail loan	6%	7%	8%	9%	10%		
Auto	Subprime retail loan	9%	10%	11%	12%	13%		
Auto	Floorplan	12%	13%	14%	15%	16%		

Auto	<i>RV/motorcycle</i>	7%	8%	9%	10%	11%		
Credit Card	<i>Prime</i>	5%	5%	6%	7%	8%		
Credit Card	<i>Subprime</i>	6%	7%	8%	9%	10%		
Student Loan	<i>Private</i>	8%	9%	10%	11%	12%	13%	14%
Student Loan	<i>Gov't guaranteed</i>	5%	5%	5%	5%	5%	6%	6%
Small Business	<i>SBA loans</i>	5%	5%	5%	5%	5%	6%	6%

If pledged collateral is priced at a premium to par (subject to a cap of 110% of par value), borrowers will need to make periodic principal prepayments to adjust for the expected reversion of market value toward par value as the collateral matures.

Pricing

Interest rates will be set on each subscription date. Initial interest rates are as follows:

SECTOR	SUBSECTOR	FIXED	FLOATING
Auto		3-year LIBOR swap rate + 100 bps	1-month LIBOR + 100 bps
Bank/Retail Card		3-year LIBOR swap rate + 100 bps	1-month LIBOR + 100 bps
Student Loan	<i>Private</i>	N/A	1-month LIBOR + 100 bps
Student Loan	<i>Gov't guaranteed</i>	N/A	1-month LIBOR + 50 bps
Small Business	<i>SBA loans 7(a)</i>	N/A	Fed Funds Target + 75 bps
Small Business	<i>SBA loans 504</i>	3-year LIBOR swap rate + 50 bps	N/A

For each TALF loan, the FRBNY will assess a non-recourse administrative fee equal to 5 basis points, which must be paid by the borrower on the loan settlement date.

Primary Dealers

Eligible borrowers must have client relationships with primary dealers, who will act as agents for the borrowers in accessing TALF loans. Primary dealers will execute the Loan Agreement on behalf of each borrower and will collect, aggregate, and submit loan requests on behalf of the borrowers.

Timeline

Prior to each subscription date, each primary dealer will collect the following information from prospective borrowers: (i) the requested loan amount, (ii) the requested interest rate format, (iii) the CUSIP numbers of the ABS to be pledged, and (iv) copies of the applicable offering documents (either final or preliminary, if the issuance has not yet closed) for the ABS to be pledged.

On each subscription date, a primary dealer will submit individual client loan requests to the FRBNY's custodian (The Bank of New York Mellon) for review. The primary dealer

will also submit to the FRBNY the aggregate loan request amount for all of its customers by rate type and asset class.

No fewer than two business days before the loan settlement date, the custodian will send a confirmation to the primary dealer listing each borrower's loan amount and the ABS expected to be delivered on the loan settlement date. The confirmation will also include the administrative fee and margin (the dollar amount of the haircut), if applicable, to be collected by the primary dealer and paid on the loan settlement date.

On the loan settlement date, the borrower or its agent will deliver, against payment of the TALF loan, the ABS collateral, the administrative fee and applicable margin to the FRBNY's settlement account at the custodian.

Loan Agreement

Under the Loan Agreement, recourse for the payment of the TALF loans is generally limited to the eligible collateral pledged to secure such loans. However, there are exceptions for breaches of representations, warranties and covenants, and for situations where pledged collateral or the borrower does not meet the eligibility requirements.

Clients are advised to review Seward & Kissel's observations on the Loan Agreement attached as Exhibit A, and are encouraged to contact their Seward & Kissel attorney with any questions or concerns.

Prohibitions on Hedging

Issuers and sponsors of ABS issuances will be prohibited from entering into transactions designed to hedge against a borrower's loss on ABS issued by such issuer or sponsor and purchased by the borrower with TALF financing. The same prohibition against hedging will also apply to transactions between primary dealers and borrowers that relate to losses of a borrower specifically related to ABS collateral purchased with TALF financing, but will not apply to hedging transactions on a borrower's broader portfolio, which may include securities purchased with TALF financing.

ELIGIBLE COLLATERAL

TALF loans must be secured by "eligible collateral", which are subject to the following requirements:

- The collateral must be U.S. dollar-denominated cash (not synthetic) ABS that are cleared through the Depository Trust Company. Eligible ABS must have a short-term and/or long-term investment-grade rating from each major nationally recognized statistical rating organization ("NRSRO") that rates it, and must be rated by at least two NRSROs. Eligible collateral will not include ABS with credit ratings based on the benefit of a third-party guarantee. Further, any ABS that has been placed on review or watch for downgrade by any major NRSRO

- will also be ineligible. For the purposes of determining TALF-eligible collateral, the major NRSROs are currently Fitch Ratings, Moody's Investors Service and Standard & Poor's.
- Except for SBA Pool Certificates or Development Company Participation Certificates, eligible ABS must be issued on or after January 1, 2009. SBA Pool Certificates and Development Company Participation Certificates must have been issued on or after January 1, 2008.
 - All or substantially all (meaning at least 95 percent of the dollar amount) of the credit exposures underlying eligible ABS must be exposures to U.S.-domiciled obligors, and all or substantially all (meaning at least 85 percent of the dollar amount) of the underlying credit exposures must have been issued after certain specified dates, depending on the nature of such credit exposures, as indicated below.
 - The credit exposures of eligible ABS must be auto loans, student loans, credit card loans or small business loans guaranteed as to principal and interest by the SBA. The underlying credit exposures must not include exposures that are themselves cash or synthetic ABS (i.e. eligible collateral cannot be CDOs or re-securitizations). The FRB has indicated that eligible collateral under the TALF may be later expanded to include ABS backed by commercial mortgage loans, non-agency residential mortgage loans and/or other asset classes.
 - o All or substantially all of the underlying auto loans (except for auto dealer floorplan loans) must have been originated on or after October 1, 2007.
 - For TALF purposes, auto loans include retail loans and leases relating to cars, light trucks, recreational vehicles or motorcycles, and will include auto dealer floorplan loans.
 - o All or substantially all of the underlying SBA-guaranteed loans must have been originated on or after January 1, 2008. There are no date restrictions with respect to the credit exposures underlying SBA Pool Certificates or Development Company Participation Certificates.
 - o All or substantially all of the underlying student loans must have had a first disbursement date on or after May 1, 2007.
 - For TALF purposes, student loans include federally guaranteed student loans, including consolidation loans, and private student loans.
 - o Eligible collateral that is credit card ABS and auto dealer floorplan ABS must be issued to refinance existing credit card or auto dealer floorplan ABS, respectively, maturing in 2009 and must be issued in amounts no greater than the amount of the maturing ABS.
 - The collateral for a borrower under the TALF cannot be backed by loans originated or securitized by the borrower or by an affiliate of the borrower.

Sponsors of ABS issuances will be required to retain an accounting firm to provide a certification indicating that the ABS to be issued is TALF eligible. Such a certification will also be included in the prospectus or other offering document for the issuance.

Borrowers may also pledge eligible ABS they have previously acquired, so long as it meets the issuance date requirements set forth above.

ELIGIBLE BORROWERS

All U.S. companies that own eligible collateral not originated by themselves or an affiliate may participate in the TALF, provided they maintain an account relationship with a primary dealer. Under the program guidelines, a “U.S. company” is:

- A business entity or institution that is organized under the laws of the United States or a political subdivision or territory thereof (regardless of whether such an entity has a parent that is a non-U.S. company), including any U.S.-organized subsidiary of such an entity, and conducts significant operations or activities in the United States;
- A U.S. branch or agency of a foreign bank (other than a foreign central bank); or
- An investment fund (defined under the program terms as any type of pooled investment vehicle, including hedge funds, private equity funds and mutual funds, and including but not limited to vehicles that primarily or exclusively invest in eligible collateral and borrow from the TALF) that is U.S.-organized and managed by a investment manager that has its principal place of business in the United States, including U.S.-organized investment fund subsidiaries of foreign investment funds.

In any case, no entity that is directly or indirectly controlled by a foreign government may borrow from the TALF.

TALF SPECIAL PURPOSE ENTITY

The FRBNY will create a special purpose entity (“SPE”) to purchase and manage eligible collateral received by the FRBNY in connection with any TALF loans. The SPE, pursuant to a forward purchase contract with the FRBNY, will commit to purchase any eligible collateral securing a TALF loan received by the FRBNY at a price equal to the amount of the TALF loan plus accrued but unpaid interest.

The U.S. Treasury Department, under the Troubled Asset Relief Program, will provide credit protection to the FRBNY by purchasing subordinated debt issued by the SPE to finance the first \$20 billion of eligible collateral purchases made by the SPE. Eligible collateral purchases made by the SPE in excess of \$20 billion will be financed by the FRBNY, and such loans will be senior to the debt purchased by the U.S. Treasury Department.

SEWARD & KISSEL TALF TASK FORCE

Seward & Kissel LLP has created a multidisciplinary TALF Task Force to advise clients on all aspects of the TALF program. For more information, please contact one of the members of the Seward & Kissel TALF Task Force.

**For more information, please contact one of the members of the Seward & Kissel
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EXHIBIT A

TALF MASTER LOAN AND SECURITY AGREEMENT: SEWARD & KISSEL OBSERVATIONS

With respect to the Master Loan and Security Agreement (the “Loan Agreement”) recently released in connection with the Term Asset Backed Securities Loan Facility (“TALF”) of the Federal Reserve Bank of New York (the “Lender”), the following are certain issues and observations that we thought our clients should be made aware of before committing to participate in the program.

Although there has been no indication that the Lender is accepting comments on the form of Loan Agreement, it is our hope that if the comments of potential Borrowers are passed along to the Lender through their Primary Dealers, certain changes can be effected. Capitalized terms which are used but not otherwise defined herein shall have the meanings assigned to such terms in the Loan Agreement.

IMPORTANT BUSINESS ISSUES

1. SECTION 2.1 Definitions – Collateral Enforcement Event.

Upon the occurrence of a Collateral Enforcement Event the Lender can, among other things, declare all Loans to be immediately due and payable and liquidate the Collateral (*see* Section 14.1).

Clause (v) of the definition of Collateral Enforcement Event provides in effect that if any lien to secure a Loan ceases to be enforceable or to be a first priority security interest, a Collateral Enforcement Event shall occur, and clause (vi) of such definition provides in effect that if any Collateral securing a Loan becomes subject to an encumbrance, a Collateral Enforcement Event shall occur. A Collateral Enforcement Event could occur under such clauses even if only a single Item of Collateral securing the Loan is affected. We believe that it is appropriate that the same five business day cure period to prepay in part the Loan or to deliver Substitute Collateral that applies to Deficient Collateral (Collateral that fails to conform to the Eligibility Criteria) should apply in these instances as well (*see* clause (iii) of Collateral Enforcement Event and Section 11.2(g)).

In addition, clause (ii) of the definition of Collateral Enforcement Event should contain customary materiality standards and grace periods.

2. SECTION 3.8 Settlement of Loans.

Notwithstanding the Lender’s receipt of an Initial Loan Request or a Loan Request, or the Custodian’s delivery of a Confirmation, the Lender is under no obligation to make any Loan or to accept as Collateral any assets that have appeared on an Eligible Collateral Schedule or that are Expected ABS Collateral. The Lender’s approval of any Loan is only be evidenced by such Loan’s settlement.

This in effect means that a Borrower's Loan Request may be rejected by the Lender at any time before the Lender actually disburses the proceeds of such Loan, even if the Custodian has already delivered a Confirmation to the Borrower's Primary Dealer indicating that a Loan would be made on the Loan Closing Date. It would seem that such a rejection could occur after a Borrower has already committed to acquiring Eligible Collateral in reliance on the anticipated settlement of the Loan.

3. SECTION 4.0 Interest Payments on the Collateral.

Regardless of when Interest Receipts on the Collateral are received, they will only be applied to the applicable Loan on the next Payment Date (i.e. three business days after the 15th day of a calendar month), with any positive interest spread being remitted back to the Borrower. The Lender has the right to invest such Interest Receipts during this interim period at its discretion, with any investment earnings on such Interest Receipts being for the Lender's own account. This provision is unusual as we believe that Interest Receipts should be invested in certain specified eligible investments (i.e. short-term cash equivalents) and that the Borrower should have the right to receive the investment earnings on such Interest Receipts. At the very least, since the Lender is receiving the upside of such investments, and since there are no specifications or guidelines as to what would be considered eligible investments, the Loan Agreement should make it clear that the Lender carries the risk of any investment losses and that any such losses will not be deducted from the Interest Receipts that are applied on each Payment Date.

In addition, it should be noted that all monthly interest shortfalls (i.e. the difference between interest on the Loan and Interest Receipts received during a Loan Accrual Period) will be capitalized, even if such shortfalls are due to timing differences (*see* Section 4.5).

4. SECTION 5.0 Principal Repayments on the Collateral.

On each day that Principal Receipts on the Collateral are received, the Lender will reduce the outstanding principal balance on the applicable Loan in an amount equal to the Principal Receipt minus a deduction for the applicable Collateral Haircut Percentage. However, although the Loan's principal balance is reduced on such date, the Principal Receipts will not technically be applied to the Loan until the next Payment Date. The Lender has the right to invest such Principal Receipts during this interim period. Because there are no specifications or guidelines as to what would be considered eligible investments, we would also like to see a clarification in this context that the Lender carries the risk of any investment losses and that any such losses will not be deducted from the Principal Receipts that are applied on each Payment Date.

5. SECTION 11.1 Borrower's Information.

The Borrower must covenant that it will provide the Lender with any reports or statements reasonably requested and that it must permit the Lender and its representatives to inspect the Borrower's financial records on site, to make and remove copies of such financial records, and to discuss the affairs, finances and condition of the Borrower internally and with independent accountants. This is extremely broad and there are no exceptions for information held by a Borrower which is subject to preexisting confidentiality agreements to which the Borrower is bound.

The problem with the scope of Section 11.1 is further exacerbated by the fact that the Lender is obligated to use its reasonable best efforts to hold the Borrower's non-public information in confidence only to the extent that it applies to information "concerning any Loan" (*see* Section 18.16).

6. SECTION 15.0 Indemnification.

The Borrower will have to provide a very broad indemnification to the Lender, the Custodian, the Administrator and their related parties. We note that while the Loan Agreement's limited recourse provision with respect to the Loans is generally limited to principal and interest received on the Collateral (with the exception of carve-outs for certain breaches by the Borrower, as discussed below) (*see* Section 17.0), the indemnification obligations of the Borrower have no such limit.

7. SECTION 19.0 Assignments.

A Borrower may only assign its rights and obligations under a Loan with the prior consent of the Lender. The Loan Agreement further states that the Lender may delay or withhold its consent for any reason and for any time period. In addition, with the exception of "unusual and exigent circumstances" in the financial markets, the Lender will not consent to any loan assignments after December 31, 2009.

CLARIFICATIONS WITH RESPECT TO RECOURSE PROVISIONS

1. SECTION 17.0 Limited Recourse.

While the Limited Recourse provision in the Loan Agreement is generally limited to principal and interest received on the Collateral, such limited recourse is inapplicable to (i) any Deficient Collateral for which the Borrower does not prepay in part the applicable Loan or deliver Substitute Collateral within the cure period, (ii) Obligations of a Borrower who, at any time, is not an Eligible Borrower, and (iii) Obligations of a Borrower that arise as a result of the inaccuracy of certain representations and warranties made by such Borrower.

With respect to the carve-out for Deficient Collateral, we would like to see clarification that the proviso applies only to the pro rata portion of the Loan attributable to the Deficient Collateral that is not cured, and not to the entire Loan. Our concern is

that the language could be read to imply that a failure to cure one Item of Deficient Collateral could give the Lender full recourse against the entire Loan amount.

2. SECTION 4.9 Interest on Deficient Collateral.

Should the Borrower fail to cure Deficient Collateral within the five business day period, additional interest in the amount of 2% will accrue on “the outstanding principal amount of such Loan and any accrued and unpaid interest thereon.” We would like to see clarification that this additional interest amount will only accrue on the pro rata portion of the Loan that is attributable to such Deficient Collateral, and not the entire Loan amount.

ADDITIONAL NOTABLE PROVISIONS

1. SECTION 7.3 Borrower’s Acknowledgements With Respect to Collateral.

The Borrower must make several acknowledgements with respect to the Collateral, including authorizing the Lender and the Custodian to at any time take any and all actions that may be necessary or, in their sole discretion, desirable to obtain, preserve, perfect or enforce the Lender’s security interest in the Collateral. We believe that the language in this provision is too broad and should be narrowed by imposing customary reasonableness standards.

2. SECTION 10.0 Representations and Warranties Made by Borrower.

The Borrower must make a number of representations and warranties with respect to, among others, its power and authority to enter into all agreements constituting the Lending Agreement and the enforceability of such agreements, its rights in the Collateral, the security interests granted in the Collateral, and the eligibility of the Borrower and the Collateral. We believe that it would be appropriate to apply customary materiality standards with respect to the representations and warranties the Borrower must make.

In addition, the Borrower must make the representation that the Collateral is free of any security interests with the exception of those granted by the Loan Agreement (*see* Section 10.1(e)(iii)). For purposes of clarification, this exception should be expanded to include any security interests granted by the Custody Agreement for the benefit of the Custodian.

3. SECTION 11.2 Covenants Made by Borrower.

The Borrower must covenant in clause (e) of Section 11.2 that it will not perform any act that may impair the Lender’s rights or interests in any of the Collateral, and that it will perform any act that would reasonably be expected to prevent such an impairment. Further, the Borrower must covenant in clause (f) of such section that it will execute any agreement or document and take any other actions that the Lender deems

necessary or desirable, including but not limited to actions relating to the perfection of the Lender's security interests in the Collateral. We believe that these covenants are unnecessarily broad and should be narrowed by applying customary reasonableness standards.