KOHLBERG KRAVIS ROBERTS & CO.

Mr. Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington DC 20429

Dear Mr. Feldman,

We would like to thank the Chairman and the FDIC for the opportunity to comment on the proposed Statement of Policy on Qualifications for Failed Bank Acquisitions and for reaching out to the investment community at a critical juncture in the recapitalization of our banking system. As we all recognize, a healthy banking system is fundamental to sustaining our economic recovery.

As we indicated at our meeting with the Chairman on July 6th, the fear and collapse of confidence in our leading banks that gripped our nation last year has abated. The reputation and standing of the FDIC as an independent and professional agency dedicated to the protection of depositors and taxpayers has only been enhanced by its performance during this difficult time.

And yet, I cannot help feeling that we remain a crossroads as we search for a way forward on the reform of our financial regulatory system, the development of systemic safeguards, the creation of new capital and other standards and the protection of consumers. Finding the right balance between public and private stakeholders lies at the core of the debate.

We therefore welcome the Chairman's clear endorsement of the role private capital can play in the rehabilitation of failed banks, both in minimizing losses to taxpayers and in providing expertise in support of bank management as they work to improve the core operations of the bank. There are a variety of sources of private capital, each with its own character and appetite for risk. Some will seek to partner with well capitalized banks in conducting acquisitions, others will focus on purchasing and managing large portfolios of troubled assets and others will form consortia to acquire resolved banks.

There should be little public controversy in private equity firms partnering with well capitalized banks to acquire failed banks. For example, KKR played a constructive role in the early 1990s in providing capital to Fleet Financial Group to acquire the Bank of

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New England. As the next year or two unfolds, there are likely to be more such opportunities, entirely beneficial to the health of the banking system. A clear statement by the FDIC that any new rules on consortia bids for failed banks do not apply to these types of transactions would, we believe, be in the best interests of our banking system. Established regulatory policies on private investment in banks would of course continue to be applied.

Similarly, we hope that having mutual funds, private equity firms and other private sources of capital compete at auction for troubled loan portfolios is not controversial. Simply stockpiling these assets at the taxpayer's risk is unappealing. We welcome the direction in which the FDIC is moving to conduct separate processes where appropriate for disposing of troubled assets and the core banking franchise itself. This should result in a better overall economic outcome for the public by better matching the risk profile of the asset to the source of capital.

Which brings us to the heart of the matter at hand. Should public policy seek to actively engage private equity consortia in acquiring failed banks? Or should such consortia be subject to uniquely high and restrictive conditions that will discourage their participation?

The case for engagement is that over the course of this economic cycle, hundreds of banks may fail and the ultimate cost to the FDIC and the public could run into the tens of billions. Reducing that burden with private sector capital makes a good deal of sense. There is also every reason to believe that the leading private equity firms would take a long term view of banks' prospects and act in a rational and responsible manner, fully observant of all regulatory and other requirements. KKR for example has invested in 165 companies over the last thirty three years, through all kinds of economic vicissitudes. The average holding period for our investments is more than six years, and value was created through a dedication to improving operating fundamentals, focusing on the long term, backing great management teams, and constructively engaging with multiple stakeholders, including regulators, community groups and others. We are familiar with the responsibilities of investing in highly regulated industries, and over the years have invested in twelve financial institutions, including banks, insurance companies, asset management firms and payment systems.

What then is the concern? That we fail, or that we succeed?

The initial response to the fear of potential failure seems to have been to raise capital standards to prohibitive levels. But how likely is a failure of a resolved bank that is capitalized with 6% Tier 1 common equity to risk weighted assets? With 50% more equity than the Supervisory Capital Assessment Program, and a risk mitigated balance sheet, we would say the chances are low. Investors will do everything they can to avoid losses, including raising additional capital. And if the environment is such that a failure is unavoidable, what are the economic consequences? In such cases private capital mitigates public losses; it does not add to them. To raise the cost of insuring against any possible failure through discriminatory capital standards simply means there is less private capital available, thus maximizing losses to the public.

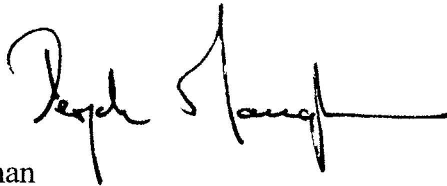
If we succeed, there is an understandable public concern that we may make too much money too quickly. There is no easy way around this concern. As we all understand, risk and return are inextricably linked. One cannot transfer risk in an uncertain world without also creating the possibility of a profit. One protection is the auction process itself and the requirement that any winning bid provides a lower cost to the taxpayer than continued public ownership of the asset. Another would be that the FDIC retains an economic interest in the resolved bank so that it participates in any value recovery. In such cases, the FDIC would need to limit its governance rights and accept that the bank will be run as a commercial enterprise. The timing of any exit is, of course, a question of judgment, but the ability to access public capital markets should not be restricted since this is a desirable policy outcome.

Thank you for your consideration of these observations. Our detailed comments on the proposed Statement are incorporated in a separate communication from the Private Equity Council.

We are confident that the FDIC will continue to show leadership at this time of national need.

We are, of course, available at any time to clarify our views and provide any further information the agency may require.

Sincerely,



Deryck Maughan